Offset Policy under the New Countervailing Duty Law

Craig A. MacDonnell

Follow this and additional works at: http://scholarship.law.cornell.edu/cilj

Part of the Law Commons

Recommended Citation

Available at: http://scholarship.law.cornell.edu/cilj/vol15/iss2/5

This Note is brought to you for free and open access by Scholarship@Cornell Law: A Digital Repository. It has been accepted for inclusion in Cornell International Law Journal by an authorized administrator of Scholarship@Cornell Law: A Digital Repository. For more information, please contact jmp8@cornell.edu.
The Trade Agreements Act of 19791 (TAA) enacted United States obligations incurred at the Tokyo Round multilateral trade negotiations. The TAA and the Tokyo Round are principally trade liberalizing measures.2 Nevertheless, at least one TAA section exhibits protectionist characteristics. TAA Section 771(6)3 restricts

---

2. See infra notes 32-44 and accompanying text.

NET SUBSIDY.—For the purpose of determining the net subsidy, the administering authority may subtract from the gross subsidy the amount of—

(A) any application fee, deposit or similar payment paid in order to qualify for, or to receive, the benefit of the subsidy,
the number of offsets allowed in calculating countervailing duties. A countervailing duty is a tariff levied to raise the price of an import benefitting from an exporting nation’s subsidy. An offset reduces the countervailing duty to calculate accurately the actual, or net, benefit received by the exporter when accepting a subsidy from its government.

Prior to the TAA, the Tariff Act of 1930 allowed the Treasury Department wide discretion in administering countervailing duties. The Treasury Department permitted countervailing duty offsets for both indirect taxes paid by and dislocation costs incurred by foreign exporters. An exporter incurs dislocation costs by relocating a plant site in response to government subsidies. A producer incurs indirect taxes at each transaction along the path of production. The restrictive enumeration of offsets in TAA section 771(6) rejects prior practice. It curtails the discretion of the new countervailing duty administering authority, the International Trade Administration, and refuses to allow dislocation costs or indirect taxes paid, but not rebated, as countervailing duty offsets.

(B) any loss in the value of the subsidy resulting from its deferred receipt, if the deferral is mandated by Government order, and
(C) export taxes, duties or other charges levied on the export of merchandise to the United States specifically intended to offset the subsidy received.

Id.

4. Id.
5. See infra notes 19, 23-24 and accompanying text.
6. Id.
7. Id.
9. The Tariff Act of 1930 provided:
   (5) The Secretary shall from time to time ascertain and determine, or estimate, the net amount of each such bounty or grant, and shall declare the net amount so determined or estimated.
   (6) The Secretary shall make all regulations he deems necessary for the identification of articles and merchandise subject to duties under this section and for the assessment and collection of such duties.

10. See infra notes 72-73 and 147-50 and accompanying text.
11. See infra notes 69-71 and accompanying text.
12. These taxes are either value added taxes (VAT) or prior stage cumulative taxes (PSC). See infra notes 93-99 and accompanying text.
The TAA prohibits the offsetting of all dislocation costs. This Note demonstrates that the TAA's prohibition of dislocation costs as offsets is unfair to foreign exporters, and does not comport with the theory of comparative advantage. The Note concludes that section 771(6) should be re-drafted to allow dislocation cost offsets if such costs are shown by clear evidence.

Legislative history indicates that Congress was not aware of all policies relevant to indirect taxes when it promulgated TAA section 771(6). Coincidentally, however, the provision exhibits correct results in its treatment of indirect taxes. This Note argues that TAA section 771(6)'s blanket prohibition against allowing indirect taxes as offsets accords with administrative necessity. Finally, this Note seeks to demonstrate an inconsistency between section 771(6) and section 771(5), which further highlights that Congress was unaware of certain economic theories relevant to the offset of indirect taxes.

I

OFFSETS IN THE CONTEXT OF INTERNATIONAL TRADE

A. DEFINITIONS

The concepts of "gross subsidy," "net subsidy," and "actual export benefit" are crucial to a discussion of countervailing duty and offset policy. "Gross subsidy" refers to the total benefit a government confers to the exporting producer regardless of factors which may reduce its value. "Net subsidy" is the actual benefit conferred by the foreign sovereign, after deducting from the gross subsidy factors which reduce its real value. "Actual export benefit" refers to the net subsidy received by the exporting producer.

The following example, the receiver's fee, illustrates these concepts. The receiver's fee is an offset recognized under Treasury practice and the TAA. It is a mandatory payment by the exporter to


15. See infra notes 81-92 and accompanying text.
16. Id.
17. See infra notes 172-88 and accompanying text.
18. See infra notes 192-93 and accompanying text.
20. Oleoresins From India, 44 Fed. Reg. 21,009, 21,010 (1979) ("application" fee) [hereinafter cited as Oleoresins].
21. Id.
the government without which the government will not release the subsidy benefits.\textsuperscript{22} For example, suppose nation $X$ wants to subsidize producer $A$ one dollar per item exported. For producer $A$ to receive this subsidy, it must pay Nation $X$ a twenty-five cent receiver's fee. The dollar paid to producer $A$ is the gross subsidy. The net subsidy is the seventy-five cent difference between the one dollar gross subsidy and the twenty-five cent receiver's fee. Seventy-five cents also represents the actual export benefit. This seventy-five cent net subsidy represents the competitive advantage the product has in the United States.

The United States imposes countervailing duties to counteract export subsidies proscribed by the TAA.\textsuperscript{23} Ideally, the countervailing duty imposed by the United States counteracts the actual export benefit received by the imported product. As explained above, the actual export benefit is not always the total subsidy received by the exporter. The administering authority therefore must reduce, or "offset," the countervailing duty to allow for factors which reduce the gross subsidy to the net subsidy that the foreign exporter actually receives. The imposition of a countervailing duty equal to the gross subsidy paid by the foreign government oversimplifies the calculation of a countervailing duty. Discounting factors, such as the receiver's fee, reduce the benefit received by an exporter, and thus should not be included in the countervailing duty. The TAA has provisions specifying both allowable countervailing duties and allowable offsets.\textsuperscript{24}

B. THE GATT AND SUBSIDIES

The General Agreement on Tariffs and Trade\textsuperscript{25} (GATT) is a

\begin{itemize}
  \item \textsuperscript{22} \textit{Oleoresins}, supra note 20, at 21,010.
  \item \textsuperscript{23} The TAA applies countervailing duties against the "net subsidy" received by the import. Trade Agreements Act of 1979, § 701(a), 19 U.S.C. § 1671(a) (Supp. IV 1980). The administering authority determines the net subsidy by aggregating the impermissible subsidies under TAA section 771(5) and subtracting the offsets allowed under TAA section 771(6). Id. § 771(6).
  \item \textsuperscript{24} TAA section 771(5) specifies foreign subsidies which will prompt the United States to impose countervailing duties. Trade Agreements Act of 1979, § 771(5), 19 U.S.C. § 1677(5) (Supp. IV 1980). TAA section 771(6) specifies the allowable offsets. Id., § 771(6).

Some consider GATT overly complex. \textit{See Trade Agreements Extension Act of 1951: Hearings Before the Senate Committee on Finance on H.R. 1612, 82d Cong., 1st Sess. 92 (1951) ("Anyone who reads GATT is likely to have his sanity impaired.") (statement of Senator Milliken).}
multilateral trade agreement developed during the post-war era.26 In addition, the acronym GATT connotes the organization which implements the provisions of the Agreement and conducts negotiations for further accords.27 Early GATT activities focused on the reduction of protectionist tariffs.28 The GATT achieved significant tariff reductions during six multilateral tariff conferences, or Rounds, held between 1947 and 1967.29 The national leaders who negotiated these limitations on international trade barriers believed that reducing tariffs ultimately benefitted all nations by encouraging international free trade and discouraging retaliatory measures.30

The economic theory of comparative advantage justifies international free trade.31 Comparative advantage posits that unnatural market factors, such as tariffs and subsidies, distort the market and misallocate resources.32 For example, protectionist tariffs may force the market price of a foreign producer’s good to a level that is unnaturally above his production costs,33 thereby allowing a less effi-


29. Id.

30. J. JACKSON, supra note 26 at 9-10, 36-39. Professor Jackson notes that the initial efforts at liberalizing world trade rested on three premises:

(1) International [world] trade is beneficial (which in turn is at least partly based on premises such as the value of economies of scale, the utility of market exchange, and ideas stemming from the theory of comparative advantage);

(2) Self-interest economic policies on the international scene contribute to misunderstanding, instability, and war in international relations generally, and

(3) International agreement on policy is necessary, or at least useful, because independent national actions to promote trade and stability will usually be frustrated by the actions of other states.

Id. at 9-10.

31. Id.

32. For a basic discussion of the theory or law of comparative advantage see S. ROBOCK and K. SIMMONDS, INTERNATIONAL BUSINESS AND MULTINATIONAL ENTERPRISES 17, 99 (1973). See also G. BRYAN, TAXING UNFAIR INTERNATIONAL TRADE PRACTICES, 273-74 (1980).

33. For the purposes of this Note the term “production costs” shall refer to all costs incurred by the producer in manufacturing, distributing, marketing, securing, and transporting his goods to the marketplace. As such, the selling price represents production costs plus profit. The theory of comparative advantage is couched in terms of market share, as accorded by efficiency. Yet market share is affected by factors other than efficiency, such as production capacity, elasticity of supply and demand, and the availability of raw materials. This discussion assumes all other variables are constant. In addition, the comparative advantage theory dictates only that producers should be allocated a
cient domestic producer to secure an "undue" portion of the market.\textsuperscript{34}

During the period in which GATT trade rounds reduced tariffs, nontariff barriers, including subsidies, became more prevalent.\textsuperscript{35} Although the GATT signatories were concerned over the growth of subsidy-related trade distortions,\textsuperscript{36} the initial GATT regulations were weak and ineffective.\textsuperscript{37} Before the Tokyo Round Agreements, the GATT made only interim, non-comprehensive efforts at international subsidy control.\textsuperscript{38} Largely unabated by GATT regulation, subsidies distorted international trade in a manner comparable to

\footnotesize{share of the market comparable to their efficiency; it does not assume that market share allocation is dependent solely on production efficiency.}

\footnotesize{34. In this example, if there had been no protectionist tariff, the imported good would have enjoyed a lower selling price. Demand for the lower-priced good would have been greater. With the tariff computed into the selling price, however, the imported good necessarily yields a portion of the market it would have captured if there had been no tariff. Because tariffs are unnatural market factors that misallocate resources, this portion is considered "undue."}

\footnotesize{35. J. JACKSON, supra note 26 at 368. See GATT, BISD (10th Supp.), at 201, 203, 204-10 (1962). See also GATT, BISD (9th Supp.), at 185-94 (1961).}

\footnotesize{36. J. JACKSON, supra note 26 at 367. GATT had already become sensitive to the effects of subsidies; but the early rounds of negotiation could not achieve consensus with regard to subsidies. Id. This difficulty rested on many factors:}

\footnotesize{From its inception GATT has been concerned with subsidies, but there has been great difficulty in obtaining a consensus for any common approach to the problem of international regulation of subsidies. This is due in part to the complexity of the subject and the difficulty of drawing the line between justifiable government policies, on the one hand, and policies that constitute a dangerous and improper attempt to export one's own problems at the expense of foreign nations, on the other hand. The difficulty in reaching a consensus on subsidies also reflects a view that they are a preferable means of protection, as compared with tariffs or quotas. The subsidy can promote and expand international trade rather than restrict it because, so the theory goes, if subsidies lower the price of the product, it will increase consumption. The economist will readily detect the premise of price elasticity of demand that lies behind this theory, a premise that does not always accord with reality. A subsidy may have a "trade diverting" effect rather than a "trade creating" effect, i.e., may shift sales away from another exporting country rather than increase the overall amount of sales.}

\footnotesize{Id. at 367-68.}

\footnotesize{37. The original GATT subsidy article merely required that signatories notify GATT of the "extent . . . nature . . . estimated effect and . . . circumstances" of the subsidy and consult with other signatories as to possible injurious effects. GATT, supra note 25, art. XVI \S 1.}

\footnotesize{38. The only significant measure of regulation that GATT reached in the intervening years between the original accord (1947) and the Tokyo Round were "standstill" agreements (first agreed upon in 1955 and subsequently extended) which "froze" subsidies at existing levels. J. JACKSON, supra note 26 at 371-76. These "standstill" agreements were promulgated in the hope that an agreement abolishing distortive subsidies eventually would be negotiated. Id. at 373 n.12. The Subsidies and Countervailing Duties Code, negotiated in the Tokyo Round, represents the manifestation of that hope. The Agreement on Interpretation and Application of Articles VI, XVI, and XXIII of the General Agreement on Tariffs and Trade, GATT Doc. MTN/NTM/W/236 reprinted in BISD (26th Supp.), at 56-83 (1980) [hereinafter cited as Subsidies Code]. Although not all subsidies are abolished under the Code, the most distortive types are. Id., Annex A and Interpretive Notes, BISD (26th Supp.), at 80-83.}
The Tokyo Round produced several agreements regulating nontariff trade barriers. Many consider the Subsidies and Countervailing Duties Code (Subsidies Code), however, to be the “keystone” of the six year trade conference. The Subsidies Code is crucial because of the widespread use of subsidies and the differing subsidy approaches prevailing among the major trading nations.

The tension between the United States and the European nations provided the focus of the Subsidies Code negotiations. The European nations traditionally have relied on government subsidization of private industry. Consequently, European negotiators were reluctant to suffer penalties for such subsidization. The United States, on the other hand, traditionally has opposed government intervention into private industry and unilaterally has penalized subsidized imports as a method of protecting domestic industry. Prior to the Tokyo Round, there were no legal limitations on the ability of the United States to impose countervailing duties.

The GATT, however, restricted the ability of other signatory nations to impose countervailing duties. According to GATT Article VI:6(a), a signatory nation could impose a countervailing duty only if the foreign subsidy caused “material injury” to a domestic industry. Prior to the Tokyo Round, the United States was exempt from the “material injury” requirement because its countervailing duty

39. Just as tariffs allow less efficient domestic producers to capture domestic markets that more efficient foreign exporters normally would dominate, subsidies permit less efficient foreign exporters to capture other markets by being able to sell at a price which does not accurately reflect production costs. As such, subsidies disrupt the comparative advantage the most efficient producer should enjoy. See generally S. ROBOCK and K. SIMMONDS, supra note 32 and G. BRYAN, supra note 32 at 273.

40. Among the agreements reached during the Tokyo Round were the following: (1) further reciprocal tariff reductions; (2) a new antidumping agreement; (3) an agreement on government procurements; (4) a technical trade barrier (standards) agreement; (5) an accord on customs valuation; (6) an attempt to regulate import licensing systems; (7) a reform of dispute settlement procedures; (8) an agreement concerning special trade treatment of developing countries; and (9) various sectoral agreements on agriculture, dairy products, aircraft, steel, and meat. Graham, Results of the Tokyo Round, 9 GA. J. INT’L & COMP. L. 153, 160-73 (1979).

41. Subsidies Code, supra note 38.


44. Id. at 1448-49.

45. Id. at 1453.

46. Id. at 1448-49.

47. Id.

48. GATT, supra note 25, Art. VI: 6(a), 4 BISD at 11.
legislation, the Tariff Act of 1930, pre-dated the ratification of GATT Article VI: 6(a). The Tariff Act of 1930 allowed countervailing duties at the discretion of the Treasury Secretary, regardless of any injury suffered by United States industry. The Tokyo Round subsidy negotiations initially centered around restrictions on the unilateral ability of the United States to impose countervailing duties.

The acceptance of the “material injury” requirement by the United States triggered movement in the stalled negotiations. The United States government agreed that before it could impose countervailing duties, it had to determine that the subsidized imports caused “material injury” to a domestic industry. In return for this concession, the United States secured, inter alia, a prohibition of industrial export subsidies and an extensive annex to the agreement illustrating impermissible export subsidies. Although United States negotiators believed that it was defensible for the United States to accept an injury requirement without corresponding concessions, they also realized that mutual compromise was necessary to secure domestic approval of the trade package. United States negotiators were concerned that Congress would never ratify a liberal trade accord which ignored the concerns of domestic industry.

49. The GATT applies to contracting parties through a Protocol of Provisional Application which was signed on October 30, 1947. The Protocol exempts legislation already “existing” at the time the agreement was signed. Protocol of Provisional Application of the General Agreement on Tariffs and Trade, art. 1, para. (b), 61 Stat. A 2051, T.I.A.S. No. 1700, 55 U.N.T.S. 308, reprinted in 4 BISD at 77.

50. See supra notes 8-9 and accompanying text.

51. Rivers and Greenwald, supra note 43 at 1449.

52. After over five years of negotiations there had been alarmingly little progress. In the words of one commentator, “[t]he negotiations went nowhere (and did so slowly).” Id.

53. Id. at 1475-76. Subsidies Code, supra note 38, Art. 9, BISD (26th Supp.) at 68.


55. Rivers and Greenwald note:

The United States, like its trading partners, had both a political and an economic interest in including an injury test in the law. If the British, French or Brazilians have a serious problem with U.S. policies, it is by definition a U.S. problem as well. The Administration, in its deliberations, was just as concerned about a rash of countervailing duty actions against hams from Denmark, steel from the United Kingdom and manufactured products from Brazil as the Danes, the British, and the Brazilians. In addition to difficult political problems created by such actions, the national economic interest was hardly served by a law that erected higher import barriers where the imports in question caused no injury to any domestic industry.

Rivers and Greenwald, supra note 43, at 1454.

56. Proper characterization appears to have been an important lobbying technique. Writing on the efforts of the administration to get the TAA through Congress, one commentator noted: “Mr. Strauss has been taking the aggressive line he knows Congress wants to hear; he sometimes sounds as though he were supporting a piece of protectionist
The drafters of the TAA also wondered whether a trade bill which was not in the best interest of the domestic economy would be politically troublesome for legislators representing districts producing goods in competition with subsidized imports. Accordingly, the TAA contained several provisions with protectionist elements.


57. This became especially important after the release of a Congressional Budget Office Study on the impact of the TAA, which predicted a loss of jobs in the urban manufacturing centers of the Northeast. Farnsworth, Harm to Northeast Seen in Trade Pact, N.Y. Times, Mar. 11, 1979, § 1, at 23, col. 1.

58. The list of impermissible subsidies did not include dislocation costs. It did, however, consider the following tax practices to be impermissible subsidies:

(g) The exemption or remission in respect of the production and distribution of exported products, of indirect taxes\(^1\) in excess of those levied in respect of the production and distribution of like products when sold for domestic consumption.

(h) The exemption, remission or deferral of prior stage cumulative indirect taxes\(^1\) on goods or services used in the production of exported products in excess of the exemption, remission or deferral of like prior stage cumulative indirect taxes on goods or services used in the production of like products when sold for domestic consumption; provided, however, that prior stage cumulative indirect taxes may be exempted, remitted or deferred on exported products even when not exempted, remitted or deferred on like products when sold for domestic consumption, if the prior stage cumulative indirect taxes are levied on goods that are physically incorporated (making normal allowance for waste) in the exported product.\(^3\)

NOTES

1 For the purpose of this Agreement:
The term “direct taxes” shall mean taxes on wages, profits, interest, rents, royalties, and all other forms of income, and taxes on the ownership of real property.
The term “import charges” shall mean tariffs, duties, and other fiscal charges not elsewhere enumerated in this note that are levied on imports.
The term “indirect taxes” shall mean sales, excise, turnover, value added, franchise, stamp, transfer, inventory and equipment taxes, border taxes and all taxes other than direct taxes and import charges.
"Prior stage" indirect taxes are those levied on goods or services used directly or indirectly in making the product.
"Cumulative" indirect taxes are multi-staged taxes levied where there is no mechanism for subsequent crediting of the tax if the goods or services subject to tax at one stage of production are used in a succeeding stage of production.
"Remission" of taxes includes the refund or rebate of taxes. . . .

3 Paragraph (h) does not apply to value-added tax systems, and border tax adjustment in lieu thereof and the problem of the excessive remission of value-added taxes is exclusively covered by paragraph (g) . . . .

Subsidies Code, supra note 38, Annex I, Illustrative List of Export Subsidies, BISD (26th Supp.), at 81, 82.
TAA, and the provisions quantifying subsidies in section 771(6) of the TAA.

C. THE TAA: CONGRESSIONAL ENACTMENT OF THE SUBSIDIES CODE

Enacting legislation to implement the terms of an international trade accord that was negotiated by the executive branch is significantly different from the normal legislative process. The executive branch commits the United States government to certain agreements, and Congress does not have complete freedom to mold and shape the implementing legislation. Unwritten rules of intra-government comity and political common sense dictate that Congress must include the major provisions and the basic policies of executive negotiated agreements in the implementing legislation. Beyond the essential provisions and policies, however, some room exists for the give-and-take of domestic political compromise. It was within these bounds that Congress formulated many aspects of the TAA.

Congress enacted and modified the Subsidies Code enumeration of impermissible export subsidies in TAA section 771(5). This provision identifies the gross subsidies. TAA section 771(5)(A) incorporates Subsidies Code Annex A by reference. In TAA section 771(5)(B), Congress added four domestic subsidies to the GATT listing. Congress thus modified the Subsidies Code enumeration of countervailable subsidies by adding additional domestic subsidies which would trigger United States countervailing duties. In so doing, Congress promoted protectionist goals.

TAA section 771(6) provides specific guidelines for calculating offsets:

---

59. TAA section 771(5) includes the following as impermissible export subsidies:
(A) Any export subsidy described in Annex A to the Agreement (relating to illustrative list of export subsidies).
(B) The following domestic subsidies, if provided or required by government action to a specific enterprise or industry; or group of enterprises or industries, whether publicly or privately owned, and whether paid or bestowed directly or indirectly on the manufacture, production, or export of any class or kind of merchandise:
   (i) The provision of capital, loans, or loan guarantees on terms inconsistent with commercial considerations.
   (ii) The provision of goods or services at preferential rates.
   (iii) The grant of funds or forgiveness of debt to cover operating losses sustained by a specific industry.
   (iv) The assumption of any costs or expenses of manufacture, production, or export of any class or kind of merchandise.


60. Id.

61. Id.
OFFSET POLICY

(6) Net Subsidy.—For the purpose of determining the net subsidy, the administering authority may subtract from the gross subsidy the amount of—

(A) any application fee, deposit, or similar payment paid in order to qualify for, or to receive, the benefit of the subsidy,

(B) any loss in the value of the subsidy resulting from its deferred receipt, if the deferral is mandated by Government order, and

(C) export taxes, duties, or other charges levied on the export of merchandise to the United States specifically intended to offset the subsidy received. 62

The administering authority deducts the offsets from the gross subsidy to determine the net subsidy. The countervailing duty counteracts the net subsidy. This provision differs considerably from prior practice. Previous legislation, the Tariff Act of 1930, authorized Treasury discretion in determining offsets. 63 Section 771(6) limits the administering authority to the offsets specified. 64 Legislative history shows that Congress intended section 771(6) to limit discretion in administering net subsidy calculations and desired to eliminate both dislocation costs 65 and unrebated taxes from offset consideration. 66 Decisions of the International Trade Administration, the new administering authority, reflect this congressional intent. 67

Congress exercised its limited ability to alter the Subsidies Code when it enacted TAA sections 771(5) and 771(6). Both provisions promote protectionist goals and counteract the free trade ideal of the Subsidies Code. TAA section 771(5) adds to the Subsidies Code listing of impermissible subsidies, making it more likely that subsidies will be found and countervailing duties imposed. In drafting section

63. See supra notes 8-9, 48-50 and accompanying text.
64. The Senate Report notes:
The bill defines the “net subsidy” to place clear limits on offsets from a gross subsidy. The gross subsidy is the value of the subsidy provided, or made available, and used . . . . For purposes of determining the net subsidy, there is subtracted from the gross subsidy only the items specified in section 771(6). The list is narrowly drawn and is all inclusive. For example, offsets under present law which are permitted for indirect taxes paid but not actually rebated, or for increased costs as a result of locating in an underdeveloped area, are not now permitted as offsets. In determining the amount of offsets which are permitted, it is expected that the administering authority will offset amounts which are definitely established by reliable, verified evidence . . . .
65. Id.
66. Id.
771(6), Congress limited the administering authority's discretion in reducing the net subsidy by injecting into a liberally oriented trade package a provision which restricted the administration's ability to find offsets. In effect, this provision results in higher countervailing duties and protection for domestic industry.68

II

DISLOCATION COSTS

A. PRACTICE PRIOR TO THE TAA

Many countries attempt to foster national economic and social goals by promoting the industrial development of depressed domestic regions.69 These governments grant various relocation subsidies to induce producers to move to such areas. Without the subsidies, the producer would not relocate. Dislocation costs are expenses solely incurred by a producer when relocating to an economically disadvantaged region. Such costs may be operational, such as increased utility costs in a remote area70 or increased labor cost

68. This analysis is supported by free trade advocates. Washington Lobbyist Robert L. McNeil believes § 771(6) will "certainly have a protectionist effect" and that it represents "a reassertion of congressional will" to protect domestic industry from foreign imports. Telephone interview with Robert L. McNeil, Executive Vice Chairman of the Emergency Committee for American Trade (January 15, 1982). In general terms, dissatisfaction with Treasury's handling of the CVD cases was the primary reason for § 771(6). Those that support limiting the discretion of the Treasury Department can be divided into two groups: those who saw Treasury's approach as potentially harming domestic industry, and those who thought that Treasury's discretion was being manipulated by other forces in the government. Specifically, some legislators felt that CVD cases were being decided to facilitate or secure international political goals and agreements. Telephone interview with William Reinsch, Chief Legislative Assistant for Senator Heinz (January 18, 1982), and telephone interview with Jeffrey Lang, General Counsel for the Senate Finance Committee (minority) (January 18, 1982).

69. MANUAL FOR THE PREPARATION OF INDUSTRIAL FEASIBILITY STUDIES (United Nations) 88 (1978) (noting that both lesser developed countries and industrially advanced nations grant subsidies to industries if they locate in particular regions). The literature on economic development with respect to lesser developed countries and regions is vast. See, e.g., I. LITTLE, T. SCITOVSKY, AND M. SCOTT, INDUSTRY AND TRADE IN SOME DEVELOPING COUNTRIES, 230-70 (1970) (general discussion of export incentives); G. CUKOR, STRATEGIES FOR INDUSTRIALIZATION IN DEVELOPING COUNTRIES (1971) (discussing the proper role of government); R. PANDY AND H. SHOUE, EXPORT INCENTIVES IN DEVELOPED AND DEVELOPING ECONOMIES (1967) (survey of incentive mechanisms); B. BALASSA, ECONOMIC DEVELOPMENT AND INTEGRATION 65-84 (1967) (discussing generally the role of exports in the process of economic growth); P. ALPERT, ECONOMIC DEVELOPMENT 128 (1963) ("The promotion of village industries as a means of providing additional sources of income and employment to rural populations is an essential aspect of community development plans"); R. MEIER, DEVELOPMENTAL PLANNING, 174-80 (1965) (discussing techniques for stimulating local industry); Selwyn, MARKETS AND THE LOCATION OF INDUSTRY—THE REGIONAL PLANNING OF INDUSTRY, in INDUSTRIALIZATION IN DEVELOPING COUNTRIES 101-02 (R. Robinson ed. 1965) (tax concessions used to encourage location of industry in depressed areas).

70. Bromine and Brominated Compounds from Israel, 43 Fed. Reg. 56,746 (1978) [hereinafter cited as Bromine].
resulting from the added commuting time that workers must spend to reach a new remote location. Such costs also may be capital expenditures incurred in the relocation itself, such as the cost of transporting heavy equipment. Increased operational costs are a recurring expense. Capital relocation costs are a distinct non-recurring expense. Nevertheless, both forms of dislocation costs increase a producer's overall costs and result directly from the relocation. Both forms of dislocation costs reduce the actual export benefit received by the subsidized producer. Thus, offsetting dislocation costs, either operational or capital, does not confer an unjust competitive benefit on the importer, rather it accurately calculates the importer's actual export benefit.

Under the discretion provided by the Trade Act of 1930, the Treasury Department allowed certain dislocation costs to offset foreign subsidies. Generally, Treasury deducted only increased operational expenses. The Treasury Department did not offset the cost of the act of relocation.

Treasury decisions from the period just prior to the TAA did not accept all dislocation cost claims blindly. Working without congressional guidelines, the Secretary recognized the potential for abuse if offsets were granted in a summary fashion. Consequently, Treasury required the producer to identify and verify the dislocation costs to the satisfaction of the Secretary. In addition, the producer had to prove that the costs were incurred after the government had authorized relocation assistance. Treasury decisions held that a producer's relocation prior to the grant of government subsidies demonstrated that the relocation presented a favorable cost benefit relationship, and that dislocation cost rebates constituted a post-hoc subsidy. Even with these limitations, however, Treasury was reluctant to rely solely on the claim of the producer. When the possibility of long term relocation savings appeared, the Secretary disallowed offsets for established costs, reasoning that the move was made for

72. In Bromine, supra note 70, Treasury found that increased labor and electricity costs at the new site exceeded the development assistance supplied by the Israeli government. There was no net benefit accruing to the producer from the development assistance and therefore Treasury imposed no countervailing duty.
73. Id.
74. E.g., Non-Rubber Footwear and Handbags From Uruguay, 43 Fed. Reg. 3904, 3905 (1978) [hereinafter cited as Leather Handbags]; see Notice of Revised Method of Calculation of Bounty or Grant with Regard to Certain Indirect Taxes, 44 Fed. Reg. 3478, 3479 (1979) [hereinafter cited as Revised Method]; Bromine, supra note 71; Diuron, supra note 73; Oleoresins, supra note 20.
75. See supra note 74. See also infra notes 77-78 and accompanying text.
76. Oleoresins, supra note 20.
commercial reasons independent of government inducement.\textsuperscript{77} Until the enactment of the TAA, Treasury proceeded on an \textit{ad hoc}\ basis, having established neither a comprehensive definition of dislocation costs nor an efficient means of calculation.

\section*{B. TAA CHANGES AND CONGRESSIONAL JUSTIFICATIONS}

The TAA removes the Treasury Department's discretion in allowing dislocation costs as offsets to countervailing duties. TAA section 771(6) contains an inclusive enumeration of allowable offsets.\textsuperscript{78} Dislocation costs, either operational or capital, are not included in the enumeration.\textsuperscript{79} Furthermore, the legislative history demonstrates that Congress desired to remove dislocation costs from the list of permissible offsets.\textsuperscript{80} Thus, the TAA drastically alters Treasury practice.

The legislative history of the TAA reveals three major justifications for the change with regard to dislocation costs.\textsuperscript{81} Congress believed that allowing dislocation costs as offsets would disrupt comparative advantage, present calculation difficulties, and mask possible cost savings.\textsuperscript{82}

Congress apparently believed that allowing dislocation costs as offsets would disrupt the comparative advantage enjoyed by the most efficient producer.\textsuperscript{83} If that was the prevailing opinion, Con-

\begin{itemize}
  \item \textsuperscript{77} \textit{Diuron}, supra note 72.
  \item \textsuperscript{78} See supra notes 64-67 and accompanying text.
  \item \textsuperscript{79} Id.
  \item \textsuperscript{80} Id.
  \item \textsuperscript{81} The only legislative history that provides evidence of the reasons that led Congress to eliminate dislocation costs from net subsidy calculation is the Senate floor debate, wherein Senator Heinz articulated three substantive reasons for the change:

  \begin{enumerate}
    \item The committee voted to exclude regional aids. Clearly, a payment for locating a plant in a particular region of a country is a subsidy. However, it has been Treasury's practice to offset such a subsidy with its estimate of any additional costs of locating in that region, inevitably a calculation of great inaccuracy.
    \item The theory is that if the company has a choice of locating in either region A or B of a country and would normally choose A because the cost to locate in B is greater, a subsidy to offset the cost of locating in B has no effect on exports from the territory of the subsidy-granting country. That is, the price of the product produced in B will be the cost less the subsidy that is equal to the additional location cost plus profit which is the same as the price (cost plus profit) of a product produced in A.
    \item The difficulty with this theory is that this type of subsidy is functionally no different than any subsidy that has the purpose of eliminating a comparative disadvantage. [2] It is also impossible to calculate with any precision the additional location costs with the result that the true effect of the subsidy can be masked. [3] Finally an offset of this nature would not take into account savings achieved by location decisions, such as labor rate differentials, raw material availability, and so forth . . . .
  \end{enumerate}

\textsuperscript{125} CONG. REC. 20,167-68 (1979) (remarks of Sen. Heinz).
\item \textsuperscript{82} Id.
\item \textsuperscript{83} Id.
gress was incorrect. Unless the exporter receives an actual export benefit, comparative advantage is not disrupted. Dislocation costs reduce the export benefit received, so allowing them as offsets accords with the comparative advantage theory.\(^8^4\) On a theoretical level, section 771(6) is unjustified insofar as it disallows dislocation costs as offsets.

TAA proponents believed that a precise calculation of dislocation costs was impossible.\(^8^5\) They feared that foreign nations would inflate dislocation cost claims to mask subsidy benefits.\(^8^6\) In addition, the prevailing United States political sentiment desired a provision that would protect domestic industry.\(^8^7\) In fairness, however, the United States should allow dislocation costs which are conclusively documented.\(^8^8\) Allowing verified dislocation costs to act as offsets is fairer than prohibiting all dislocation costs even if documented.

The legislative history of the TAA indicates that all offsets permitted under section 771(6) should be "definitively established by reliable, verified evidence."\(^8^9\) This standard could apply to dislocation costs as well as to those offsets that are included within section 771(6). In addition, the historic cost, against which increased relocation costs will be compared, should be subject to a "definitively established by reliable, verified evidence" standard. For example, if the relocating firm previously has produced the product which will be manufactured at the new location, the ITA should use as a reference the "definitively established" cost of goods and services at the firm's original location. Thus, the ITA could exercise caution and still allow dislocation costs as offsets by permitting dislocation costs only when the producer conclusively documents both the original

\(^8^4\) An analogy to the receiver's fee example is helpful in understanding why dislocation costs do not disrupt the comparative advantage of the most efficient producer. See supra notes 20-22 and accompanying text. Both dislocation costs and receiver's fees are expenses necessarily incurred as a precondition to the receipt of subsidy benefits. As such, both should be allowed to offset the amount of the net subsidy. Dislocation costs are a unique production expense; offsetting the gross subsidy in their amount facilitates relocation within the foreign country without decreasing the price of goods abroad. Because United States CVD law will adjust the price upward in the amount of the net subsidy, United States industries need not be alarmed at the prospect of legitimate dislocation costs acting as offsets.

\(^8^5\) See supra note 81.

\(^8^6\) Id.

\(^8^7\) See supra notes 56-57 and accompanying text.

\(^8^8\) The administering authority could further the goals of fairness and accuracy by incorporating into dislocation cost analysis the limiting factors that evolved under Treasury practice. Like Treasury, the ITA could allow dislocation costs only if the firm otherwise would not have relocated. Diuron, supra note 72. Similarly, the ITA could look to the timing of government benefits and attempt to ensure that remissions of dislocation costs were not post hoc subsidies. Oleoresins, supra note 75.

\(^8^9\) S. Rep. No. 249, supra note 64.
cost level and the increased cost level. This approach would force
the foreign producer to substantiate actual costs, assist the ITA in
ascertaining the amount of actual export benefit, and protect domes-
tic industry.

The third justification given by Congress concerned cost savings
resulting from relocation.90 Congress decided that dislocation offsets
would not account for "savings achieved by location decisions, such
as labor rate differentials, raw material availability, and so forth."91
Consequently, Congress feared that manufacturers would reap an
unjust comparative advantage. The original precondition for per-
mitting government subsidized regional development to offset coun-
tervailing duties was that government subsidies provided the
relocation inducement.92 Relocation cost savings alone were insuffi-
cient to prompt private relocation. Treasury permitted offsets
equivalent to relocation costs only if the relocation assistance was
necessary to induce the manufacturer to relocate. Yet, if cost savings
exist that reduce the actual dislocation cost, they also affect the bene-
fit received and should be considered. Thus, congressional concern
with relocation cost savings is justified.

To prevent abuse of a dislocation cost offset provision, the
administering authority must require strict adherence to a strict stan-
dard. Potential cost savings of relocation present a problem of abuse
if not exhaustively investigated. Savings may result from the
decreased cost of labor, raw materials, or other services at the new
location. To require the United States administering authority, how-
ever, to be responsible for such investigation would be an over-
whelming and expensive burden. Thus, to effectively administer
dislocation costs as offsets, much of the burden must be borne by the
exporter or his government. The only alternative that avoids placing
an intolerable burden on the administering authority, and gives the
exporter an incentive to calculate potential cost savings, is to create a
presumption of intolerable cost savings, absent conclusively verified
documentation to the contrary. Granted, this saddles the exporter
with a burden it may not wish to discharge, yet in the event that cost
savings are minimal as compared to dislocation costs, the exporter
has an incentive to verify savings.

This proposal provides incentives for exporters to prove reloca-
tion cost savings. Nevertheless, the review of cost savings is contin-
gent upon adequate verification. Either of two verification standards
could make this proposal effective. First, the administering author-

90. See supra note 81.
91. Id.
92. See supra note 69.
ity must be vested with complete discretion to evaluate the veracity of cost savings documentation and to disallow completely dislocation cost offsets if the data are unsatisfactory. Second, cost savings documentation should be verified by the exporter's government in some formal fashion. Although both the exporter and its government have an incentive to secure favorable trade treatment for their products, they are less likely to falsify documentation if United States regulations require formal verification.

III
INDIRECT TAXES

Unlike the United States, which relies on a direct income tax, many countries primarily employ indirect taxes. An income tax is direct because the government seeks to tax directly the income earned by a producer. An indirect tax, however, is assessed upon the goods produced rather than on the producer. Thus, the producer is taxed only indirectly. All European nations and the United States adopted direct income taxes before 1914. During World War I, the European nations developed indirect tax systems. Presently, indirect taxes are the principal form of European Economic Community taxation. Turnover taxes, paid at each transaction during the manufacture of a product, are a common form of indirect tax. The complex operation of turnover tax systems, requiring tax payments, withholding allowances, and government remissions, provide opportunities for foreign governments to subsidize producers. Accordingly, they create problems for United States trade officials attempting to locate and quantify foreign subsidy practices.

93. The European nations and the European Economic Community (EEC) rely heavily on indirect taxes. The EEC countries on the average get more than half of their total tax revenue from indirect taxes. M. von Steinaecker, Domestic Taxation and Foreign Trade: The United States-European Border Tax Dispute 4 (1973).

94. Id. at 3 n.*. The Subsidies Code defines “direct taxes” to include “taxes on wages, profits, interest rents, royalties and all other forms of income, and taxes on the ownership of real property.” Subsidies Code, Annex I, supra note 38.

95. M. von Steinaecker, supra note 93, at 3 n.*. The Subsidies Code defines “indirect taxes” to include, “sales, excise, turnover, value added, franchise, stamp, transfer, inventory and equipment taxes, border taxes and all taxes other than direct taxes and import charges.” Subsidies Code, Annex I, supra note 38.

96. M. von Steinaecker, supra note 93, at 4.

97. Id. at 5-6.

98. The EEC collects revenue throughout Europe using a value added tax which applies a rate not exceeding one percent, to an assessment basis which is determined in a uniform manner for Member States according to Community rules. A. Easson, Tax Law and Policy in the EEC 124 (1980).

99. A turnover tax is levied on businessmen and computed as a percentage of their turnover. M. von Steinaecker, supra note 93, at 5.

100. See infra text accompanying notes 103-17 for an explanation of indirect tax system mechanics.
After a background section, explaining the two principal indirect tax systems, and an economic assessment of indirect taxes, this Note will analyze present United States offset practice. In particular, the Note will highlight the change in offset practice prescribed by the TAA with regard to the payment of indirect taxes that are not rebated, and will discuss the inconsistency between TAA section 771(5), which allows tax remissions without countervailing duties, and TAA section 771(6), which fails to allow an offset for the payment of indirect taxes without rebate.

A. BACKGROUND

I. Turnover Tax Systems

There are two major types of turnover tax systems: prior-stage cumulative taxes (PSC) and value-added taxes (VAT). Both systems assess taxes at each transaction during the production of a product. Withholding practices, however, distinguish the systems and provide significant differences in United States countervailing duty treatment.

A foreign government imposes PSC taxes at every exchange in a production process based upon a percentage of the full value of the product at the time of each sale. Because the tax is assessed upon the full value of the product, it incorporates the cumulative value added by all previous producers. The effect is cumulative because at each transaction the levy is paid on a base increased by all previous increases in the value of the product. This "snowball" effect,
where the purchaser pays a tax on previous increments in value, is graphically referred to as a "cascade" tax. In addition, the amount of tax paid on a finished product varies depending upon the number of transactions during the production process. Thus, the PSC system presents an accounting problem because the amount of tax depends upon the integration of the production process, not the value of the final good. Identical goods may be subject to different amounts of tax because of differing production integration.

Under a VAT system, a business pays a tax only on the value it adds to the product. As with PSC taxes, the government assesses a tax at each transaction on the full value of the product at the time of each sale; however, the government permits the seller collecting the tax to withhold the amount he paid in taxes to a prior producer. Thus, while the seller collects a tax on all accumulated

The escalation in the taxes charged at each stage of production results from the calculation of the tax upon the total value of the product at that stage of production, including the value added by previous producers and taxed in a previous transaction. Thus, the tax collected on the transaction between B and C (2 dollars) reimposed a tax on the value added by A, even though the government previously had collected a tax on that value in the transaction between A and B.

105. K. DAM, supra note 28, at 123.
106. Id. Returning to the example given supra at note 104, this concept may be demonstrated if we postulate a merger between B and C. The merged firm now adds a value of $20 to the widget. All other factors remain the same. Producer A has no costs, but adds a value of $10 to the widget. The government assesses its one dollar tax (10% \times 10 = 1) on the transfer of the uncompleted widget to B/C. Producer B/C then processes the widget adding $20 in value, raising the widget's value to $30. The government assesses a 3 dollar tax (30 \times 10\% = 3) on the transfer of the completed widget to D. D then sells the widget at retail without adding any value to the widget. The taxes paid on the finished product total four dollars. The following graph illustrates the example:

<table>
<thead>
<tr>
<th>Producer</th>
<th>Cost</th>
<th>Value Added</th>
<th>Tax</th>
</tr>
</thead>
<tbody>
<tr>
<td>A</td>
<td>0</td>
<td>10</td>
<td>1</td>
</tr>
<tr>
<td>B/C</td>
<td>10</td>
<td>20</td>
<td>3</td>
</tr>
<tr>
<td>D</td>
<td>30</td>
<td>0</td>
<td>0</td>
</tr>
<tr>
<td>Total</td>
<td>30</td>
<td>30</td>
<td>4</td>
</tr>
</tbody>
</table>

As in the note 104 example, the manufacturers created a finished widget with a 30 dollar value. The widget in this example, however, was taxed four dollars, and the widget in the previous example was taxed six dollars. The merger of producers B and C created the different levels of taxation because it eliminated a transaction, and the taxation of the widget between B and C. Thus, the amount of tax assessed on a good in a PSC system is dependent upon the number of transactions in its production, not the value of the finished good.

107. M. VON STEINAUECKER, supra note 93, at 5 n.5.
108. Id.
109. Id. The lack of cascade effect in the VAT system is best illustrated using an example based upon the hypothetical presented supra at note 104. As in note 104, manufacturers A, B and C combine to produce widgets. Each producer adds a value of $10 to the product. They market the widgets through a retailer, D. The government taxes each transaction at 10% and there are no costs assumed by the first producer, A. Producer A has no costs, but adds a value of $10 to the widget. The government assesses its one dollar tax (10\% \times 10 = 1) on the transfer of the uncompleted widget to B. B then processes the widget adding $10 in value raising the widget's value to $20. The govern-
value, he does not remit the entire amount to the government. The seller withholds an amount equal to the taxes paid to a previous producer, thereby readjusting the taxes paid so that the seller’s net taxes only account for the value it adds to the product. The VAT does not incorporate the cumulative value added by all previous producers at each transaction. The tax does not “cascade.” Because there is no cascading, the total amount of tax paid on a finished product does not vary with the number of transactions incurred during production.\textsuperscript{110} The VAT withholding practice encourages producers to maintain accurate tax and production records. Thus, a VAT system, unlike a PSC system, is very accountable.\textsuperscript{111} In addition, VAT sys-

\begin{table}[h]
\centering
\begin{tabular}{|c|c|c|c|c|c|}
\hline
Producer & Cost & Value Added & Tax Assessed & Tax Withheld & Net Tax \\
\hline
A & 0 & 10 & 1 & 0 & 1 \\
B & 10 & 10 & 2 & 1 & 1 \\
C & 20 & 10 & 3 & 2 & 1 \\
D & 30 & 0 & 0 & 0 & 0 \\
\hline
Total & 30 & 6 & 3 & 3 & \\
\hline
\end{tabular}
\caption{Example of VAT System}
\end{table}

In comparing the VAT system to the PSC system example supra at note 104, it is important to note that the government assesses an equal amount of taxes under each system, six dollars. Nevertheless, the VAT’s withholding system adjusts the taxes collected to three dollars ($6 - 3 = 3$) which corresponds to the total value added.

\textsuperscript{110} The illustration developed supra at notes 104; 106 and 109, shows the irrelevance of mergers to the total tax levied under a VAT system. Assume the same firms as in supra note 106. Firm A adds $10 in value, and merged firm B/C adds $20 in value. Producer A has no costs, but adds a value of $10 to the widget. The government assesses its one dollar tax ($10 \times 10\% = 1$) on the transfer of the uncompleted widget to B/C. Producer B/C processes the widget adding $20 in value, raising the widget’s value to $30. The government assesses a 3 dollar tax ($30 \times 10\% = 3$) on the transfer of the uncompleted widget to D. B/C, however, does not remit the entire three dollars to the government. It withholds the one dollar tax paid to A, and remits two dollars corresponding to its value added. D does not process the widget and sells it at retail. The example is summarized as follows:

\begin{table}[h]
\centering
\begin{tabular}{|c|c|c|c|c|c|}
\hline
Producer & Cost & Value Added & Tax Assessed & Tax Withheld & Net Tax \\
\hline
A & 0 & 10 & 1 & 0 & 1 \\
B/C & 10 & 20 & 3 & 1 & 2 \\
D & 30 & 0 & 0 & 0 & 0 \\
\hline
Total & 30 & 4 & 1 & 3 & \\
\hline
\end{tabular}
\caption{Example of VAT System with Mergers}
\end{table}

The net tax in the present example corresponds directly with the total value added, as it did when B and C were separate entities in the example given supra at note 109. PSC systems, however, assess and collect different amounts of tax on a product depending upon the number of transactions in the production process. When B and C were separate entities, PSC collected six dollars. When B and C merged, PSC collected four dollars.

\textsuperscript{111} K. DAM, supra note 28, at 140.
tems rebate taxes paid on exports. These so called "border tax adjustments" ensure that exported goods bear no domestic tax burden and put into effect the "destination principle," i.e., internationally traded goods are subject to only the indirect taxes of the country of destination.

The PSC system is less sophisticated than the VAT system. It is easier to administer because there are no regular rebate or withholding practices and no complex record keeping requirements. The governmental taxing authority monitors the transactions necessary in production and assesses the required taxes. PSC taxes are used in less sophisticated economies. VATs, on the other hand, require sophisticated withholding procedures, rebate practices, and record keeping. VAT systems predominate in more sophisticated economies, particularly in Western Europe.

The distinction between VAT and PSC taxes is straightforward. Both systems tax the product directly and the producer indirectly. In addition, both systems tax the production process at points of exchange. VAT withholding practices readjust the tax to account solely for the value added by the immediate producer. PSC systems have no established withholding practice and "cascade." In addition, VAT systems rebate taxes on exported goods. Recently, countries using PSC tax systems have begun to rebate taxes. The PSC rebates typically promote exports. They also blur the distinction between the two tax systems and have caused fairness problems in United States countervailing duty treatment.

112. M. von Steinäecker, supra note 93, at 8. In terms of the example supra at note 109, D receives a rebate of three dollars, constituting the value added tax paid on the product. Id. at 24.

113. Id. at 8.


115. K. DAM, supra note 28, at 140. See supra note 94.

116. E.g., India (see Certain Footwear From India, 44 Fed. Reg. 61,588 (1979)); Pakistan (see Certain Textiles and Textile Products From Pakistan, 44 Fed. Reg. 40,884 (1979)); Colombia (see Leather Handbags From Colombia, 44 Fed. Reg. 18,660 (1978)).

117. Indirect taxes are not generally rebated upon domestic consumption. G. Bryan, supra note 32, at 295. Unlike the VAT system, typically only exporters receive rebates in nations utilizing a PSC system. Id. at 296.
2. Tax Shifting

In 1947, the GATT determined that indirect tax rebates did not constitute a subsidy to the producer, so long as the rebates were not excessive. The GATT did not accord the same subsidy exemption to direct tax rebates. Two justifications support the distinction between GATT treatment of direct and indirect taxes. First, the GATT recognized that countries relying on indirect taxes traditionally have refunded those taxes to make exports price-competitive. The practice is long established and firmly entrenched. Second, the GATT based the distinction on the economic theory of full tax shifting. The theory holds that market prices always reflect the net amount of indirect taxes assessed on the product sold, but that market prices do not reflect the net amount of direct taxes assessed on the manufacturer's profits. This distinction between the tax systems remains in the present GATT. Subsequent academic literature, however, contests the theory of full tax shifting, and threatens the justification for the subsidy exemption granted to indirect tax rebates.

The theory of full tax shifting holds that market prices of goods reflect the taxes assessed on the goods. The assumption underlying the theory is that the price of a good is a function of its cost. An indirect tax is levied directly on the product at each transaction in its production process. When an indirect tax raises the price of a product, the producer forwards, or shifts, the increase to the consumer in the form of a higher price. Similarly, when an indirect tax rebate reduces the costs associated with a product, the producer forwards, or shifts, the decrease to the consumer in the form of a lower price.

118. BRYAN, supra note 32, at 293. GATT Article XVI contains the provisions applicable to export subsidies. A supplemental provision to Article XVI states, The 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. GATT, supra note 25, Annex I, Ad Article XVI, 4 BISD at 68. According to this provision, indirect taxes, which are borne by the product, may be rebated on exports, so long as the rebate does not exceed the tax levied on like domestic consumption. Id. See generally, J. JACKSON, supra note 26 at 392-95.

119. K. DAM, supra note 28, at 139. In the words of the GATT interpretive note, the distinction between direct and indirect taxes is founded upon the choice of the phrase "duties or taxes borne by the like product" and thus describes the duties and taxes which may be refunded. Id. Indirect taxes are borne by the product, while direct taxes are borne by a producer. See supra notes 95-96 and accompanying text.

120. K. DAM, supra note 28, at 139.

121. Id. at 139-40, 214.

122. Id.

123. Id. at 214-15; M. von Steinaecker, supra note 94, at 23; G. BRYAN, supra note 32, at 290, 293.

A tax rebate lowers the price of the finished product which enables consumers to purchase more and increase their level of satisfaction.\(^{125}\) The GATT determined that the benefit was fully shifted to consumers, increasing their welfare, and that the tax rebate did not benefit the producer and was not a subsidy.

As a corollary to the tax shifting acceptance of rebates, tax shifting also allows offsets for indirect taxes paid but not rebated. If a product benefits from a countervailable subsidy (i.e. a subsidy against which the United States may levy a countervailing duty) and is also subject to PSC taxes which are not rebated, the United States should reduce the countervailing duty by the amount of the tax paid. As with rebates, consumers benefit from the offset of indirect taxes paid but not rebated. The offset reduces the countervailing duty and, according to the theory of full tax shifting, the producer will shift the benefit to the consumer in the form of a price lower than would have occurred had the entire countervailing duty been levied.\(^{126}\)

Recent economic literature questions the veracity of full tax shifting.\(^{127}\) Economists believe that price changes are not determined solely by costs, but by a combination of cost and the producer's perception of the market reaction to a price change.\(^{128}\) A

---

125. G. Bryan, supra note 32, at 274.
126. The United States Treasury Department adopted this approach in allowing offsets for taxes paid but not rebated. See infra notes 147-50 and accompanying text.
127. See supra note 123.
128. Economists argue that the degree to which indirect taxes are shifted depends on the elasticity of demand. Only in the case where demand is perfectly inelastic (a vertical line) is the indirect tax fully shifted forward to the buyer.
producer, seeking to maximize profits, will raise prices in response to a tax assessment only if the decrease in the number of products demanded is small enough so that profits after the change are at least as large as they were before the price increase. Similarly, a producer will only reduce prices in response to a tax rebate if the increase in the amount demanded is large enough so that profits after the change are at least as large as they were before the price increase. Thus, the producer must take account of the market reaction to a price change before raising or lowering prices in reaction to tax payments or rebates. Economists call the market reaction to price changes “price elasticity.” When a market is highly elastic, a price change causes a large shift in the quantity demanded. When a market exhibits low elasticity, a price change causes a small shift in the quantity demanded.

The recognition of demand elasticity as a factor in the producer's decision to raise or lower prices alters the subsidy analysis of indirect taxation and rebates. Originally, the GATT assumed that indirect taxes and rebates were fully shifted to the consumer: tax assessments automatically resulted in higher consumer prices, and tax rebates automatically resulted in lower consumer prices. Present theory, however, does not agree with this simple view. Economists now believe that consumer prices respond to tax assessments or rebates only so long as the producer believes that the quantity demanded by the market responds in a manner which maintains or increases profits. The problem is demonstrated most clearly in the context of indirect tax rebates. According to the new theory of tax shifting, if a producer does not believe that market demand will increase sufficiently in response to a price decrease, it will not shift the entire tax rebate to the consumer and only the producer will benefit immediately from the rebate.

Despite contemporary modification of the theory of tax shifting, the Tokyo Round did not alter GATT treatment of indirect tax rebates. The Subsidies Code maintains prior practice, stating that rebated indirect taxes are not export subsidies. Given the doubt

is being shifted. K. DAM, supra note 28, at 214-16; G. BRYAN, supra note 32, at 290, 293. If indirect taxes are not fully shifted forward to the purchaser, then a rebate of those taxes unduly benefits the manufacturer; that is, the manufacturer is subsidized by the amount of the difference between the total tax incidence and the amount actually shifted. Id. The producer receives an actual export benefit. Id.

130. Id.
131. Id.
132. See supra note 118.
133. M. VON STEINAECCKER, supra note 93, at 24.
134. See Annex A and Interpretive Notes, supra note 38.
that has been cast upon the full tax shifting theory justifying GATT treatment of indirect tax rebates, only the tradition argument\textsuperscript{135} remains to justify the subsidy exemption.

B. TREASURY PRACTICE PRIOR TO THE TAA

Pre-TAA United States countervailing duty practice adhered strictly to the theory of full tax shifting. Under the discretion allowed by both the Trade Act of 1930 and the GATT, the Treasury did not impose countervailing duties on rebated indirect taxes,\textsuperscript{136} and allowed offsets for indirect taxes paid but not rebated.\textsuperscript{137} Identifying the abuses caused by the excessive rebate or offset of indirect taxes constituted the principal issue in pre-TAA practice.

The complex operation of indirect taxes presented opportunities for nations to mask export subsidies.\textsuperscript{138} Rebating indirect taxes in excess of taxes actually paid conferred a benefit upon the exported product. Declaring the payments as tax rebates removed them from consideration as subsidies. Thus, the declaration of a payment to an exporter as an indirect tax rebate could mask an otherwise impermissible subsidy which ordinarily would provoke a countervailing duty. If the foreign determinations were accepted blindly and offset by the United States countervailing duty administering authority, the United States could excessively reduce its countervailing duty. Thus, the United States developed standards to determine when a rebate claim or a tax payment claim was excessive.

The Treasury Department faced conflicting considerations in establishing a standard for excessive rebates. Fairness considerations required equal treatment of VAT and PSC rebates;\textsuperscript{139} the difficulty in calculating PSC rebates accurately, however, made

\textsuperscript{135} See supra note 120 and accompanying text.
\textsuperscript{138} For an explanation of indirect tax system mechanics, see supra text accompanying notes 103-13.
\textsuperscript{139} Revised Method, supra note 74.
treatment equal with VAT rebates difficult. According to the theory of full tax shifting, producers shift both VAT and PSC tax rebates to consumers. Thus, in fairness to exporters laboring under each system, Treasury allowed a subsidy exemption for both rebates.

The inability of Treasury to calculate the amount of a non-excessive rebate, however, resulted in different tests for each indirect tax system. VAT systems provide an accurate measure of excessive indirect rebates. PSC systems do not. VAT systems require extensive record keeping and provide an accurate measure of taxes assessed on each product.

A comparison of rebates allowed on exported goods and taxes assessed on similar domestic goods provided a simple test for whether an exported good received an undue benefit by virtue of an excessive indirect tax rebate. The Treasury Department declared that VAT rebates on exports were not excessive if identical to or less than taxes assessed on similar goods consumed domestically. PSC taxes provided no comparison similar to the VAT test. PSC systems did not have extensive record keeping requirements. While fairness considerations required that Treasury treat VAT rebates and PSC rebates equally, the inability to calculate whether a PSC rebate was excessive provided a stumbling block to the allowance of PSC rebates without a countervailing duty.

Treasury solved the dilemma by adopting the "physical incorporation" test. The Treasury Department did not assess a countervailing duty against a rebate corresponding to goods physically incorporated into an exported product. Stated in another way, PSC rebates on goods physically incorporated into an export were not countervailable subsidies. This test compromised the fairness and calculation considerations. The test allowed countervailing duty exemptions for both VAT and PSC taxes, yet it provided a principled method to accurately limit PSC rebate claims.

The theory of full tax shifting justifies the offset of indirect taxes paid but not rebated. VAT systems generally have a rebate mechanism. Thus, the offset issue arises only in cases involving exports from nations utilizing a PSC tax system. As with rebates, however,

---

140. Id.
142. See supra notes 107-13 and accompanying text.
143. Revised Method, supra note 74.
144. Id.
145. See supra notes 103-06 and accompanying text.
146. Revised Method, supra note 74.
147. Id.
148. Id.
PSC tax systems provide no accurate method of calculating whether taxes paid were excessive.\textsuperscript{149} Treasury applied the physical incorporation test to regulate the offset of PSC taxes paid but not rebated.\textsuperscript{150} Treasury considered only unrebated taxes on goods physically incorporated into the final export as a permissible offset to existing subsidies.

Utilizing the physical incorporation test, the Treasury Department exempted indirect tax rebates from countervailing duties, and allowed offsets to PSC taxes paid but not rebated. In doing so, the Treasury satisfied both the theory of full tax shifting and the need to treat VAT and PSC taxes equally. Finally, Treasury used the physical incorporation test to overcome calculation difficulties inherent in PSC taxes.

C. Post-TAA Practice

1. TAA Indirect Tax Provisions

The TAA enacted subsidy provisions regulating United States countervailing duty treatment of tax rebates\textsuperscript{151} and United States offset treatment of unrebated taxes.\textsuperscript{152} The rebate provision, TAA section 771(5), expressly adopts the Subsidies Code and is consistent with the theory of full tax shifting.\textsuperscript{153} The offset provision, TAA section 771(6), rejects prior Treasury Department practice and does not allow offsets for indirect taxes paid but not rebated.\textsuperscript{154} Thus, under TAA section 771(5) the new countervailing duty administering authority, the International Trade Administration (ITA), will exempt both VAT rebates and PSC rebates satisfying the physical incorporation test from countervailing duties. Nevertheless, under TAA section 771(6) the ITA will not offset a countervailing duty to account for PSC taxes paid but not rebated.

The Tokyo Round Subsidies Code re-enacted rebate provisions consistent with the theory of full tax shifting. The Subsidies Code prohibits export subsidies on non-primary products\textsuperscript{155} and allows the use of countervailing duties to combat them.\textsuperscript{156} In addition, the Subsidies Code provides an illustrative list of prohibited export subsidies\textsuperscript{157} which includes provisions consistent with United States

\begin{footnotes}
\item[149] See supra notes 103-06 and accompanying text.
\item[150] See supra note 137.
\item[153] See infra notes 156-62 and accompanying text.
\item[154] See infra notes 164-67 and accompanying text.
\item[155] Subsidies Code, supra note 38, Art. 9, BISD (26th Supp.), at 68.
\item[156] Subsidies Code, supra note 38, Art. 4, BISD (26th Supp.), at 61.
\item[157] Annex I and Illustrative Notes, supra note 38.
\end{footnotes}
Treasury Department treatment of indirect tax rebates. The prohibited subsidies include:

(g) 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.

(h) The exemption, remission or deferral of prior stage cumulative indirect taxes on goods or services used in the production of exported products in excess of the exemption, remission or deferral of like prior stage cumulative indirect taxes on goods or services used in the production of like products when sold for domestic consumption; provided, however, that prior stage cumulative indirect taxes may be exempted, remitted or deferred on exported products even when not exempted, remitted or deferred on like products when sold for domestic consumption, if the prior stage cumulative indirect taxes are levied on goods that are physically incorporated (making normal allowance for waste) in the exported product.

Thus, the Subsidies Code precludes the assessment of countervailing duties on PSC and VAT rebates, so long as the rebates do not exceed indirect taxes levied on goods consumed domestically. In addition, it precludes the assessment of countervailing duties on PSC taxes rebated on goods physically incorporated into the export.

This provision is consistent with both prior Treasury rebate practice and the theory of full tax shifting. TAA section 771(5) defines subsidies against which the United States will levy countervailing duties. It expressly adopts the Subsidies Code Illustrative List of Export Subsidies.

The Subsidies Code contains no provision regarding offset treatment of indirect taxes paid but not rebated. TAA section 771(6), on the other hand, contains an inclusive listing of permissible offsets. Indirect taxes paid but not rebated do not appear in section 771(6). Thus, section 771(6) radically alters United States offset treatment of indirect taxes. Under discretionary Treasury practice, "physically incorporated" PSC taxes that were paid but not rebated

---

158. See supra notes 139-50 and accompanying text.
159. Annex I and Illustrative Notes, supra note 38, (g), (h) [footnotes omitted].
160. Id.
161. Id.
162. Prior to the TAA, the Treasury Department did not impose countervailing duties on VAT rebates so long as they did not exceed domestic VAT taxes assessed. Treasury did not impose countervailing duties on PSC rebates which satisfied the physical incorporation test. See supra notes 139-50 and accompanying text.
165. The legislative history of TAA section 771(6) states that the enumeration therein is all inclusive. See supra note 64.
offset any countervailing duty assessed against an import. The ITA, restricted by TAA section 771(6), may no longer offset countervailing duties by an amount corresponding to indirect taxes paid but not rebated.

TAA section 771(5) and TAA section 771(6) are inconsistent both in their treatment of PSC taxes and in their approach to tax shifting. TAA section 771(5) permits the rebate of VAT and PSC taxes without a countervailing duty penalty. TAA section 771(6) eliminates the unrebated payment of PSC taxes from the list of permissible offsets, even when conditions which would legitimate a rebate of the same taxes are satisfied. The TAA, by sanctioning the rebate of PSC taxes, yet disallowing their offset, prompts foreign governments to institute rebate practices and capitalize on the countervailing duty benefits that the United States accords to indirect tax rebates. Nevertheless, the institution of rebate practices by foreign governments presents no significant economic change in indirect tax policy.

TAA section 771(5) and TAA section 771(6) are also inconsistent on tax shifting grounds. The theory of full tax shifting justifies both the exclusion of non-excessive rebated taxes from countervailing duties and the offset of non-excessive taxes paid but not rebated. TAA section 771(5) is consistent with prior United States and GATT practice, which was based upon the theory of full tax shifting. Thus, the inconsistency between TAA section 771(5) and TAA section 771(6) is a product of the radical change in offset policy that Congress created when it enacted TAA section 771(6). Despite prior reliance on the full tax shifting theory, Congress did not examine tax shifting considerations when adopting the TAA.

2. TAA Section 771(6): Congressional Justifications for the New Offset Treatment of Indirect Taxes

Congress advanced several arguments to justify the change in offset practice created by TAA section 771(6). First, Congress asserted that calculating indirect taxes would be "no more than a guess." Second, Congress feared that allowing indirect taxes as
offsets would confer an "undue amount of benefit" on the producer.\textsuperscript{174} Third, Congress believed that the United States should not base its countervailing duty policy on the varying tax methodologies of different nations.\textsuperscript{175}

Most nations utilizing a PSC system cannot account for the number of transactions occurring during the manufacture of a product. Thus, it is difficult to calculate the exact amount of the tax levied.\textsuperscript{176} Some nations attempt to estimate the amount of taxes levied and rebate the estimated tax incidence.\textsuperscript{177} Consequently, United States countervailing duty offsets based upon foreign estimates of PSC rebates would be arbitrary. Congressional concern with the arbitrary nature of PSC rebates is justified.

Congress has indicated that an undue benefit accrues to exporters under a PSC system because PSC taxes are not "cascaded."\textsuperscript{178} This argument seizes on the difference between VAT and PSC taxes, and ignores the cumulative nature of PSC taxes.\textsuperscript{179} Because PSC taxes are cumulative they are, in fact, a "cascade" type tax.\textsuperscript{180} While PSC taxes may benefit exporters unduly, Congress is incorrect in claiming that it is the lack of PSC cascade effect that causes this result.

The undue benefit issue is related closely to the calculation issue. Congress feared that exporters under a PSC system would receive an undue benefit from "excessive" PSC tax rebates or "excessive" claims of PSC tax payments.\textsuperscript{181} "Excessive" tax rebates, only partially disclosed to United States authorities, would escape countervailing duties normally levied against such subsidies. Similarly, "excessive" claims of PSC tax payments would provide an undue benefit in the form of an enlarged United States countervailing duty offset.

Prior to the passage of the TAA, the Treasury Department addressed this problem when it adopted the physical incorporation test for PSC rebates and offsets.\textsuperscript{182} The physical incorporation test limited possible undue benefits which otherwise might occur if PSC taxes were rebated perfunctorily. Treasury efforts to adopt similar

\begin{itemize}
  \item \textsuperscript{174} Id.
  \item \textsuperscript{175} Id.
  \item \textsuperscript{176} On the varying quantity of PSC taxes assessed on similar goods see supra notes 103-06 and accompanying text.
  \item \textsuperscript{177} See supra note 137.
  \item \textsuperscript{178} 125 CONG. REC. 20,168 (1979) (statement of Sen. Heinz).
  \item \textsuperscript{179} For an explanation of the distinction between VAT and PSC taxes see supra notes 101-13 and accompanying text.
  \item \textsuperscript{180} See supra note 104-06 and accompanying text.
  \item \textsuperscript{181} 125 CONG. REC. 20,168 (1979) (statement of Sen. Heinz).
  \item \textsuperscript{182} See supra note 146 and accompanying text.
\end{itemize}
guidelines with respect to unrebated taxes that deserved offsets also represented a good faith attempt to prevent undue benefits.\textsuperscript{183} In addition, the administering authority may further guard against undue benefits by adopting evidentiary requirements that are as strict as those proposed for dislocation costs.\textsuperscript{184} Thus, the exporter would have to show that the physical incorporation test was "definitely established by reliable, verified evidence."\textsuperscript{185} The drafters of the TAA and the negotiators of the Subsidies Code apparently accepted the compromise struck between fairness principles and accuracy goals when they adopted the physical incorporation test for rebate analysis.\textsuperscript{186} For Congress to allow the physical incorporation test in its section 771(5) treatment of indirect tax rebates, yet not allow the same test to regulate the offset treatment of similar taxes, is anomalous.

Congress evinced concern that the administering authority "should not base countervailing duty policy on the tax methodologies selected by varying countries."\textsuperscript{187} Nevertheless, the TAA recognizes the significant differences between VAT and PSC tax systems. TAA section 771(5), which determines the proper method of rebate calculation, distinguishes between the type of tax system employed in the exporting country.\textsuperscript{188} It is inconsistent to criticize offset practice on the grounds of tax methodology differentiation, when the underlying controversy grows out of a system which expressly distinguishes tax systems for the purpose of ascertaining permissible rebate levels.

D. ALTERNATIVE JUSTIFICATIONS AND A PROPOSAL FOR SECTION 771(6)

The congressional arguments for disallowing indirect tax offsets under TAA section 771(6) are not completely satisfactory. Congressional objections to foreign tax distinctions in offset policy are inconsistent with the distinction drawn between PSC and VAT rebates in TAA section 771(5). Congressional fears of calculation difficulties and undue benefit accruing to exporters are alleviated largely by the

\begin{itemize}
  \item \textsuperscript{183} See supra notes 147-50 and accompanying text.
  \item \textsuperscript{184} See supra note 137 and accompanying text.
  \item \textsuperscript{185} Id.
  \item \textsuperscript{187} 125 CONG. REC. 20,168 (1979) (statement of Sen. Heinz).
  \item \textsuperscript{188} TAA section 771(5)(A) incorporates the Subsidies Code Illustrative List of Export Subsidies, which, in turn, recognizes the distinction between VAT and PSC taxes. Trade Agreements Act of 1979, § 771(5)(A), 19 U.S.C. § 1677(5)(A) (Supp. IV 1980).
\end{itemize}
physical incorporation test and the strict burden of proof placed on
the exporter. 189

Unlike the arguments of Congress, current tax shifting theories
provide adequate justification for section 771(6). 190 The theory of
full tax shifting justified indirect tax offsets on the grounds that the
consumer, and not the producer, benefitted from the offset. 191 Economists
now widely recognize that indirect taxes are partially, not
fully, shifted forward. 192 The amount of tax shifted forward fluctu-
ates with the producer's perception of demand price elasticity. 193
Because taxes are not fully shifted, offsets equal to total taxes are not
economically justified. 194 Similarly, complete prohibitions of indi-
rect taxes as offsets, such as that enacted by section 771(6), are not
economically justified. Allowing complete offsets subsidizes the pro-
ducer in the amount of taxes shifted to the consumer. Similarly,
prohibiting the offsets penalizes the producer in the amount of taxes
not actually shifted.

The administrative cost accompanying a case-by-case approach
would be prohibitive. Such an approach would require an examina-
tion of the demand price elasticity for each product under scrutiny.
While the notion of demand price elasticity is a useful theoretical
tool, its actual calculation is extremely difficult. 195

Assuming that a case-by-case approach is infeasible, which rule,
complete offset recognition or offset prohibition, comports with
United States countervailing duty policy? In large part, caution
characterizes United States policy. 196 Congress traditionally has dis-
couraged practices which benefit foreign producers. Prohibiting
unrebated taxes from offset consideration does not benefit foreign
producers. Allowing unrebated taxes as offsets will benefit foreign

---

189. See supra text accompanying notes 187-88.
190. See supra text accompanying notes 178-86.
191. See supra text accompanying note 125.
192. See supra note 127.
193. See supra notes 127-31 and accompanying text.
194. One commentator states that "[o]ne conclusion to be drawn from the economic
literature is that full refund of an indirect tax constitutes in fact a subsidy to exports and
therefore has the same distorting effect on international trade that any other export sub-
sidy would have." K. DAM, supra note 28, at 215.
195. Elasticity of demand is much too difficult to measure on a case-by-case basis, for
it to be the determining factor in CVD calculations. Professors Posner and Easterbrook
write: "It is, to put it mildly, hard to measure elasticities, and a finding [with respect to
elasticity] is bound to be ambiguous." R. POSNER & F. EASTERBROOK, ANTITRUST
CASES, ECONOMIC NOTES AND OTHER MATERIALS 336 (2d ed. 1981). "Unfortunately,
while there are econometric techniques for estimating . . . elasticity of demand . . .
because of data problems they rarely yield very reliable results." Id. at 350 (emphasis
added).
196. In fact the alteration of the Trade Agreements Act demonstrates congressional
cautions. See supra text accompanying notes 59-68.
producers. Thus, the rule accepted in TAA section 771(6) complies with traditional congressional intent. The policy most likely will have two results: (1) in the short run, the producer will be penalized to the extent that taxes are shifted; and (2) in the long run, the country of origin may revise its tax system to provide for indirect tax rebates.

Contemporary theories of tax shifting shed new light on the actual effects of offsets and rebates. Historically, United States tolerance of rebates has rested on the acceptance of traditional foreign tax practices; that tolerance likely will continue despite their distortive characteristics. The allowance of offsets by the United States did not rest on foreign traditions. The United States Treasury Department allowed offsets in an attempt to treat rebates and unrebated taxes fairly, and to the extent that indirect taxes were believed to be shifted. Because permitting a full offset in the entire amount of taxes paid effectively subsidizes the producer, a flat prohibition of unrebated taxes as offsets, though necessarily inexact, must be the preferred rule. Thus, due to the current belief that indirect taxes are not fully shifted, rather than the reasons articulated in the legislative history, TAA section 771(6) reaches a justifiable result. Any modification of TAA section 771(6) to allow dislocation costs should not alter the effect of TAA section 771(6) in terms of unrebated taxes.

IV
CONCLUSION

Each nation must make commitments to effectuate the goals of a multilateral agreement. Many nations will benefit from free trade, and the Tokyo Round Subsidies Code seeks to promote that goal. Thus, it is in the interest of each nation to interpret the Subsidies Code in accordance with both its express provisions and its spirit. The TAA, United States legislation adopting the Subsidies Code, generally complies with the intended free trade goals. In several instances, however, the TAA deviates from free trade ideals. In particular, TAA section 771(6) does not allow dislocation costs or unrebated indirect taxes as offsets.

The prohibition of dislocation costs as offsets is technically within the letter of the Subsidies Code. Nevertheless, the prohibition violates the spirit of the Code because it prevents a reduction in the gross subsidy by costs which necessarily reduce the actual export

197. See supra note 120 and accompanying text. The argument that this tradition should be accorded considerable weight is discussed in J. Michael Finger What the "Zenith Case" Might Have Meant, 13 J. WORLD TRADE L. 48-49 (1979).
198. See supra notes 147-50 and accompanying text.
benefit received by the producer. Potential abuse of administrative discretion should not be an obstacle. If properly circumscribed by clearly articulated and strict evidentiary standards, the exercise of administrative discretion need not be arbitrary. Allowing dislocation costs is within the spirit of United States countervailing duty policy, and in fact furthers the goals of that policy. Congress should not disallow these offsets because they contain potential discretionary abuses and present preliminary calculation problems.

The prohibition of indirect taxes as offsets presents a more difficult question. The Subsidies Code, relying on the theory of full tax shifting, allows non-excessive tax rebates to escape countervailing duties. The Code does not contain an offset provision. The TAA adopted the Subsidies Code countervailing duty exemption for indirect tax rebates. Nevertheless, inconsistent with the theory of full tax shifting, the TAA prohibits indirect tax offsets. Congress attempted to justify this inconsistency using calculation, undue benefit, and variable tax methodology arguments. None of these offers a completely satisfactory explanation for the inconsistent treatment accorded to rebates and offsets. New theories of partial tax shifting, however, provide a satisfactory justification for section 771(6). The administrative burden that would be required to determine the variable amount of tax actually shifted provides a satisfactory rationale for the prohibition of indirect tax offsets. Nevertheless, the United States rebate policy is inconsistent with the offset provision and is unlikely to accord with the offset provision due to the continued recognition by the United States of longstanding European tax practice contained in TAA section 771(5).

Craig A. MacDonnell

---

199. See supra note 137 and accompanying text; Notice of Revised Method of Calculation, supra Note 141.