UNITED STATES - TAX TREATMENT FOR
"FOREIGN SALES CORPORATIONS" -
RECOURSE BY THE UNITED STATES TO ARTICLE 22.6
OF THE DSU AND ARTICLE 4.11 OF THE SCM AGREEMENT

WT/DS108

ANSWERS OF THE UNITED STATES

TO QUESTIONS FROM THE EUROPEAN COMMUNITIES

March 20, 2002

1. Does the United States have access to data on the use of the FSC/ETI scheme for a more recent year than 1996?

1. No. See the answer of the United States to Question 23 from the Arbitrator.

2. Is it not correct that in US countervailing duty practice the US Departement [sic] of Commerce assumes a 100 % pass through for tax subsidies?

2. No. See the answer of the United States to Question 33 from the Arbitrator.

3. Does the United States consider that the FSC/ETI scheme increases US exports by an amount less than the amount of the subsidy?

3. In the view of the United States, it is impossible to know whether the FSC/ETI subsidy increases U.S. exports by more or less than the amount of the subsidy. As indicated in the *US Second Submission*, paras. 117-128, the United States reran the EC/Treasury model and ran an Armington trade model to estimate the effects of the FSC/ETI subsidy. Although each of these runs assumed full pass-through, the results showed that trade effects less than the amount of the subsidy fell within the reasonable range of estimates.

4. Moreover, these runs exaggerated the effect of the subsidy, because they assumed full pass-through. The EC's own expert has found this assumption to be "implausible", and the 1997 Treasury study on which the EC relies stated that the assumption of full pass-through overstates the effect of the subsidy. In Exhibit US-17, the United States reports on the results obtained by relaxing the assumption of full pass-through. These results show even more clearly that trade effects less than the amount of the subsidy fall within the reasonable range of estimates.

5. What the United States can say with confidence is that the trade impact of the FSC/ETI measure on the EC is less than the $4.043 billion figure claimed by the EC.

4. In its November 1997 report to Congress (Exhibit EC-1) the US Treasury Department made some assumptions concerning elasticities of supply and demand for estimating the effect of the FSC scheme on US exports. Can the United States explain the reasons for using those assumptions and why other available data on supply and demand elasticities were not used?

6. Although it did not say so explicitly in its report, Treasury consistently made assumptions that tended to err on the side of overstating the effect of the FSC measure on the value of U.S. exports. For example, when explaining the equation used to calculate these effects, the report states as follows:[1]

> The equation is based on the assumption that firms are as sensitive to taxes as they are to any other cost of doing business. Thus, the equation will overstate the effect on exports if the firm does not consider taxes in making its production

[1] Exhibit EC-1, page 12.

decisions.

7. Similarly, when explaining the decision to use perfectly elastic export supply curves the report, after noting that estimates of supply elasticities are subject to wide margins of error, the report states as follows:[2]

> Consequently, in constructing the estimates in this report the export supply elasticities are presumed to be infinite, except for agriculture and natural resources, for which a value of 3 is chosen. These assumed values tend to overstate the export supply elasticities, which means that the estimates tend to overstate the loss in exports that would accompany removal of FSC benefits.

8. Consistent with this approach, and as has already been documented in the U.S. submissions in this proceeding, Treasury also chose an older source for the elasticities of the foreign demand for U.S. exports that tended to provide estimates that were on the high end of those available in the literature. In any event, it is the true elasticities of U.S. export supply and foreign demand for U.S. exports, rather than Treasury's assumptions, that are important in this proceeding. In its submissions, the United States has presented a balanced review of the available evidence on these elasticities.

5. What amount of suspension of concessions does the United States consider will induce compliance?

9. The United States intends to comply with the recommendations and rulings of the DSB. Therefore, no amount of suspension of concessions is necessary to induce compliance.

[2] *Id.*, page 14.