WHO'S WINNER OF US TAX BILL?

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The most sweeping overhaul of US corporate tax law in nearly two decades may have been seen as vital legislation to solve the US-EU trade rift, but Chinese exporters are also being advised to stay on the alert for its divergent messages.

Experts interviewed by China Business Weekly agree that the impact of the new tax bill on China will be minimal, but it is also likely that the tax law rewrite will have expansionary effects on China's foreign trade given the tight trade correlations between the two countries.

In a bid to end a tough trade friction with Europe, the election-year bill, signed by US President George W. Bush late last month, repealed a US$5-billion annual subsidy for US exporters that had been ruled illegal by the World Trade Organization.

Now, with the repeal of such trade subsidies, goods exported from the United States may become a little more expensive, thereby giving Chinese exporters of similar goods some added advantage, according to Jinshu Zhang, attorney with US law firm Greenberg Traurig, LLP.

As far as the EU is concerned, he said, Chinese exporters may be competing with their US counterparts in honey, sugar, suits, trousers, bed linen, and so on.

"It is interesting to note that the new bill has reduced tariffs on ceiling fans, which are largely imported from China. So the Chinese ceiling fan industry is a clear winner under this new bill,?he told China Business Weekly.

However, the repealing of the trade subsidy is "gradual and the adverse impact on US exporters may largely be offset by the new tax cuts to US manufacturers and other domestic producers, at a total cost of US$76.5 billion in 10 years.?

Therefore, any trade advantage the Chinese manufacturers enjoy may be insignificant, not to mention that the Chinese exporters face their own share of trade sanctions from the EU.

Since this new bill gives new tax cuts, from a top rate of 35 per cent down to 32 per cent, to US manufacturers and other domestic producers, including traditional manufacturing, engineering, energy production, computer software, films and videotapes and food processing, Chinese exporters in relevant industries will suffer a new disadvantage.

According to Kenneth Louie, associate professor of economics with the Sam and Irene Black School of Business at the Pennsylvania State University, Erie, the new tax cut will apply to many more US companies than the old export subsidy did.

On top of the tax breaks that replace the subsidy, the law also provides other stimulating measures, such as a year's reduction in the tax on repatriated profits and the simplification of foreign tax credit regulations, he said.

Experts said it is still hard to understand the fall-out of these stimulations at the moment.

"On the one hand, this incentive seems to encourage companies to expand their operations globally,?Zhang said, "On the other hand, any funds expatriated back into the United States to take advantage of the tax break would be money that could otherwise be reinvested overseas in places like China.?

Zhang pointed out that even without the new tax breaks for US manufacturers, Chinese exporters are already facing challenges such as increased costs of labour, raw materials and transport.

With the new 3-per-cent tax cut given to US domestic manufacturers, Chinese exporters of low-margin goods may completely lose their competitive edge.

Zhang said there may also be a lesson to be learned by the Chinese Government.

"Since direct export subsidies are easy targets for trade sanctions, especially after China's accession to the WTO, why not expand the incentives to all manufacturing sectors, just as the new US tax bill does, since the bulk of products are destined for export anyway??

In considering the tax breaks, **George Haley**, US-based professor of international business with the University of New Haven, told China Business Weekly: "We must keep in mind the legislation is hammered out under pressure of elections.?

The original purpose of the legislation was to put an end to the subsidies which amounted to US$49.2 billion.

To avoid the furor that would be caused by merely removing the subsidies, the US Congress replaced the subsidies with a 3-per-cent reduction in the corporate tax rate.

"However with elections coming, Congress was unable to resist granting favours to any industry that came to it with hat in hand.?Haley said. "The definition of manufacturing was expanded to include such things as the production of Hollywood films and music, construction, engineering and architectural firms... So, though the legislation began as a trade-oriented piece of legislation, what it became was a legislation aimed at rewarding special interests and a last-minute effort by members of US Congress to buy votes for their own re-election.?

Timing of new bill

Without any fanfare, Bush signed on October 22 the most sweeping rewrite of corporate tax law since 1986 as he flew to a campaign appearance in Pennsylvania.

In this politically charged season leading to one of most contentious presidential elections in history, anything can be seen as politically motivated, Zhang said.

"The repeal of the subsidies was inevitable since the EU has threatened to impose huge sanctions on US imports based on the WTO ruling. Therefore, it should not cost the Bush administration any 'political capital.'"

Louie said Bush has been severely criticized for his handling of the economy and has been blamed for the substantial loss of US manufacturing jobs during his administration. If he is to win re-election, it is especially important for him to try to show that he is doing something constructive to stem the tide of job losses and that the goal of the new bill is to create jobs in America.

Zhang said the new tax incentives were viewed as gifts to small businesses and big corporations alike and therefore should win some new support from this traditionally pro-Republican base. Giving tax cuts to the domestic manufacturing sector is also touted as a measure against a further shift of jobs overseas.

"However, the Democrats may complain that this bill gives too many goodies to special business interests. Apparently uncertain of the publicity value of this new bill, the Bush campaign has not made a big fanfare out of its passage and execution into law,?Zhang said.

Whoever wins the election this week, Sino-US trade ties will continue to be fostered, experts agreed.

Yi Xiaoxiong with Marietta College told China Business Weekly that for the first time since the Ronald Reagon era, the China issue is not being touted during the presidential election.

People are paying more attention to US domestic issues and the war in Iraq.

Also, given the size and importance of China's economy, neither party is likely to act to harm trade relations between the two countries, according to Oded Shenkar, professor of global business management at the Ohio State University's Fisher College of Business.

While the candidates differ in their approach to trade agreements, these different approaches will end up with similar policies, according to experts.

"Senator John Kerry says he will review all trade agreements ... however, it is doubtful that he would act strongly to curtail or otherwise harm trade with China,?said Robert Ross, professor with Clark University.

Roger Chen, professor at the University of San Francisco's School of Business, said the Taiwan question will be a major challenge for the new US Government, whoever wins.

"It is apparently the biggest issue ahead in terms of Sino-US foreign policy, which will have a long-term impact on the economic relations of the two countries,?Yi agreed.

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