

Problems with Dumping and Injury Margin Calculations in Ten User Countries

Edwin Vermulst and Gary Horlick¹

I. Introduction

The World Trade Organization (WTO) anti-dumping rules, as laid down in the WTO Anti-Dumping Agreement (ADA), conceptually distinguish between two forms of dumping:

- *Price* dumping, i.e. selling at a lower price abroad than in the home market;
- *Cost* dumping, i.e. selling below cost in an export market.

In addition, *de facto* a third form of dumping exists: *Non-market economy* dumping. Where a non-market economy is under investigation, dumping may be established in a special manner.

In all three cases, the establishment of dumping nominally² is a technical mathematical exercise, which focuses on facts, notably the prices and costs of merchandise in two separate markets. If dumping and resulting injury are found, anti-dumping duties may be imposed to offset or prevent injurious dumping in the importing country market. Anti-dumping duties therefore are defensive (and not punitive) in nature.

Systematic price dumping assumes separation of markets and existence of a closed home market, through governmental or market activity. These conditions should make parallel imports impossible. It is perceived to be “unfair” not to allow competition in one’s home market, yet to benefit from the openness of other markets to sell at low prices there. This perception of unfairness can be said to form the current basis for most anti-dumping legislation, although the ADA itself does not label dumping as “unfair” and the WTO carefully avoids that assertion.

However, price differentiation as a pricing policy (as often used within domestic economies) is a widely used instrument to introduce products to new markets

(however, the effect of such a policy is often balanced by parallel imports). Similarly, temporary sales below fixed costs (but above variable costs) are common in many industries during downturns in the business or product cycle. Therefore, it is important that key **substantive** concepts of the ADA are applied appropriately. Furthermore, some ADA rules may need to be revised to better reflect business realities in a globalized economy.

In the areas of *price* and *cost* dumping, current WTO rules leave too much leeway for dumping to be found and anti-dumping measures to be applied in circumstances where *systematic* dumping does not take place (and, indeed, where domestic competition laws would not find objectionable conduct). We characterize such dumping as *incidental* dumping.

A finding of incidental dumping, as opposed to systematic dumping, may result from various factors, including, but not limited to:

- differences in economic or business cycles in two markets;
- price differentiation to initially enter a market without established purchaser knowledge of the new item;
- exchange rate fluctuations;
- technicalities of dumping margin calculation methods, such as asymmetrical comparisons between domestic and export prices, restrictive interpretations of allowances, systematic exclusion of sales below cost and use of remaining sales above cost as the basis for normal value, use of constructed normal values with unrealistically high profit margins, etc.

In the case of *non-market economy* dumping, the use of the surrogate country concept if coupled to a one country-one duty rule make dumping proceedings

Notes

- 1 Edwin Vermulst is a partner at Vermulst, Verhaeghe & Graafsma, Brussels, Belgium. Gary Horlick is a partner at WilmerHale, Washington, D.C. The views expressed here are the authors’, and not necessarily those of their firms or clients.
- 2 As we will see below, in reality importing country authorities have much discretion in deciding on the calculation details. Furthermore, use of the *best information or facts available* rule could lead to findings of dumping where none would be found otherwise.

involving such countries more akin to country-specific safeguard actions.

One could argue that the application of the lesser duty rule provides a counter-weight for incidental dumping findings. However, the two are not necessarily linked. Furthermore, the calculation of injury margins suffers from problems of its own, caused largely by the absence of any regulation in the ADA.

This project, in which we analyse the problems with dumping and injury margin calculations³ in the ten user countries: Australia, Brazil, China, the EC, India, Indonesia, Korea, Mexico, South Africa and the United States, is a follow-up to a similar study which we undertook during 2004.⁴ As we did at that time, we again requested the authors of the country studies, all experienced local practitioners, to succinctly describe the ten major problems with such calculations in less than ten pages.

In the following sections, we focus on what appear to be *systemic* problems, i.e., problems that were identified in more than one jurisdiction. Furthermore, while acknowledging its arbitrariness, we have grouped together very specific problems under broader conceptual categories.

We wish to thank Daniel Moulis, Ana Caetano, Xiaochen Wu, Lakshmi Kumaran, Erry Bundjamin, Wahyu Indra Gunawan, Keon Ho Lee, Luz Elena Reyes de la Torre, Gustav Brink as well as our co-authors John Greenwald and Folkert Graafsma for their time and efforts in contributing to this analysis and for their comments on previous drafts.

A. Dumping Margins: Sales Below Cost/Constructed Normal Values

Various aspects of sales below cost and/or constructed normal value calculations were identified 13 times as problematic.

Six contributors⁵ identified problems with the calculation of a reasonable profit in the establishment of constructed normal values.

Four contributors⁶ considered the 20 per cent sales below cost threshold as arbitrary.

One contributor⁷ considered the refusal of the authorities to take into account FOREX gains, while treating FOREX losses as a cost in CNVs as inconsistent.

Two other contributions⁸ note that the increased recourse to very detailed PCNs⁹ increases the likelihood of recourse to CNVs for one or more PCNs.

B. Dumping Margins: Related Parties

Related party issues may arise in several contexts. Foreign producers may source inputs from related suppliers. They may sell the product for export through related parties located in the exporting country or in the importing country. Last, they may sell their products through related parties in their domestic market.

In all these cases, a first issue will be to determine whether parties are in fact related, a second issue ought to be whether their relationship has any influence on the prices charged between them and the third issue is how the authorities should proceed if they determine that the relationship has in fact influenced the prices charged. Although interrelated, the three steps can theoretically be distinguished.

The ADA does not contain a definition of 'related parties' for any of these contexts, although the very vague definition in footnote 11 to Article 4.1(i) ADA¹⁰ supposedly can be applied by analogy. Two contributors¹¹ have suggested that a definition of related parties should be provided in the ADA.

The second issue has proved more controversial. Seven contributors have reported as problematic that the authorities do not check whether transactions between related parties are actually conducted at arm's-length basis¹² or that the basis for the determination is not clear.¹³

Notes

- 3 We initially intended to cover only dumping margin calculation issues. However, following a suggestion by Ana Caetano to also cover injury margins, we expanded the scope of the project to cover both. This turned out to be a good decision because, as we will see, many of the contributors identified problems with injury margin calculations in their jurisdiction.
- 4 The results of this study "TEN I" were published in G. Horlick and E. Vermulst, *The 10 Major Problems with the Anti-Dumping Instrument: An Attempt at Synthesis*, 39 *Journal of World Trade* 1 (February 2005), pp. 67–74. The underlying country studies were published in 39 *Journal of World Trade* 1 (February 2005), pp. 75–180.
- 5 Australia, China, the EC, Korea, South Africa, the United States.
- 6 Australia, China, the EC, Korea.
- 7 The United States.
- 8 The EC, Korea.
- 9 See also section D. below.
- 10 Article 4.1(i) ADA provides that when producers are related to the exporters or importers, the term 'domestic industry' may be interpreted as referring to the rest of the producers.
- 11 China and Korea.
- 12 India with respect to purchases from related suppliers; Australia and the EC with respect to export sales to related parties in the exporting country; EC and Korea with respect to the constructed export price; Korea and South Africa with respect to domestic sales to related parties.
- 13 China in the case of domestic sales to related parties.

Similarly, many contributors have identified problems with the calculations made by the authorities in the case of related party sales,¹⁴ notably the deduction of excessive costs and/or profit on the export side.

C. Dumping Margins: Non-market Economies

Six contributors¹⁵ consider that the establishment of normal value in the case of non-market economies could be improved. Most note the arbitrary character of the surrogate country approach. The automaticity with which the USDOC uses information from Indian import statistics to calculate factors of production in dumping cases involving China is also criticized. In the case of the EC, the ad hoc grant of MET and/or IT is also criticized.

D. Dumping and Injury Margins: PCNs

It has increasingly become the practice of countries using the anti-dumping instrument to sub-divide the product under investigation into distinct models or types, often on the basis of product control numbers (PCNs), as an intermediate step in the calculation of dumping and injury margins. While there is no explicit provision in the ADA authorizing this practice, it is presumably based on the requirement to make a fair comparison between normal value and export price. If, for example,¹⁶ a producer sells mainly prime grade on the domestic market, but exports mostly off grade, a comparison of the weighted average domestic price with the weighted average export price, without distinguishing between the grades, will lead to an unjustifiable finding of dumping which does not make sense.

The contributions from Australia and Brazil point out that if the investigation reveals that certain models or types are not injuriously dumped, then such models or types ought to be excluded from the scope of the measures, although this is not always done in those countries (or in most others).

Other contributors¹⁷ note inconsistencies in the use of PCNs throughout the calculations. Thus, the Brazilian, Indian and Indonesian contributions provide examples of the authorities comparing a normal value, encompassing all domestically sold PCNs, with export transactions which consist only of certain PCNs.

Clearly, such an inconsistent approach distorts the comparison.

E. Dumping Margins: Duty Drawback

Article 2.4 ADA provides in relevant part that due allowance shall be made for differences in taxation. This is the legal basis for duty drawback claims made in many cases where the exporting country operates a duty drawback scheme. The exporters may then benefit from a refund of or an exemption from customs duties paid or payable on importation of raw materials on the condition that the raw materials are used in the production of exported products. If such import duties are included in the domestic sales, a difference in taxation will occur. Many users of the anti-dumping instrument apply the more detailed rules that can be found in the WTO Agreement on Subsidies and Countervailing Measures by analogy in the anti-dumping context.

Four contributors¹⁸ note that their jurisdictions tend to apply excessive evidentiary requirements to duty drawback claims.

F. Dumping Margins: Level of Trade and Quantity Differences

Where exporters sell to different levels of the distribution chain in their domestic and export markets, level of trade claims may be made. If, for example, an exporter sells to distributors abroad, but to retailers on his domestic market, one can expect the export price to be relatively lower than the domestic price because the distributors on the export market need to cover their costs and make a profit (the distributors' margin) on their resale price to the retailers.

Similarly, if exporters sell larger quantities for export and smaller quantities domestically, the export price for the larger quantities on a per unit basis would normally be lower than the unit price of the domestic sales. (Often, the two situations will overlap as distributors normally would buy higher quantities than retailers.)

Article 2.4 ADA provides that due allowance shall be made for differences in levels of trade and quantities. However, four contributors report that claims for level of trade and/or quantity differences are often rejected in their jurisdictions.¹⁹

Notes

14 Australia, China and the EC in the case of export sales to related parties in the exporting country; Australia, the EC, Korea and the United States in the case of the construction of the export price; Korea in the case of domestic sales to related parties.

15 Brazil, the EC, India, Korea, South Africa, the United States.

16 See the contribution on the Indian system by Lakshmi Kumaran.

17 Brazil, India, Indonesia, Korea, Mexico.

18 Australia, Brazil, China, the EC.

19 Brazil, China, the EC, Korea.

G. Injury Margins

The subject that has come in for most criticism in the country studies is the calculation of injury margins on the basis of the lesser duty rule in Article 9.1 of the ADA.²⁰ On the positive side, while the application of the lesser duty rule is not mandatory under the ADA, it would appear that most of the jurisdictions covered by this project – the major exception being the United States – in fact do apply a lesser duty rule. On the negative side and presumably because of the absence of any regulation in the ADA, practices vary widely both between countries and within countries.²¹ Some of the problematic aspects signalled by the authors of the country studies include:

- the calculation of only one injury margin for all exporters from all countries;²²
- unjustified and non-transparent calculation of target prices;²³
- unpredictable calculation of reasonable profit in target prices;²⁴
- on the exporters' side, Brazil relies on import statistics, rather than exporters' actual data;
- zeroing of non-injurious export transactions;²⁵
- weighing on the basis of exporters' sales and disregard of domestic models for which no comparable export models exist in the calculations;²⁶

H. Dumping and Injury Margins: All Others Rate

Another area where the ADA leaves authorities ample discretion pertains to the establishment of what is often called the "all others rate". This is the anti-dumping duty that the authorities will apply to exporters that did not or insufficiently cooperate in the proceeding. It must be distinguished from the rate that will be applied to cooperating, non-sampled exporters in cases where the authorities resort to sampling; this would appear to be adequately covered by Article 9.4 ADA.

While four contributors²⁷ have pointed out that the all others rate will typically be higher than the highest duty imposed with respect to any cooperating producer, a practice which is also followed by many other users on the ground that non-cooperation must not be rewarded, the general concern seems to be that the all others rate is often set at a prohibitively high level. By way of exception, Gustav Brink has pointed to South African cases where the methodology led to relatively low duty levels, possibly because the exporters 'gamed' the rules.

I. Dumping and Injury Margins: Transparency

Several contributors²⁸ observe that their systems lack transparency as a result of which dumping and/or injury margin calculations made by the authorities are difficult to check. Indeed, the data used to calculate injury margins normally ought²⁹ to come from the questionnaire responses of the foreign and the domestic producers, as a result of which neither side has access to opposing parties' data.³⁰

As far as dumping margin calculations are concerned, Gustav Brink correctly notes that it will normally be virtually impossible for the domestic industry to check the underlying calculations because all figures used in the calculation come from the questionnaire responses of the foreign producers, to which the domestic industry does not have access.

J. Dumping and Injury Margins: Reviews

The contributors for Brazil and Mexico note problems with the calculations in the case of reviews. In Mexico, it appears possible for exporters to request a review only if they have a 'representative' volume of exports to Mexico.

In Brazilian sunset reviews, both dumping and injury margins are calculated very arbitrarily in cases where there are no imports.

Notes

20 Article 9.1 ADA provides in relevant part that "[i]t is desirable that ... the duty be less than the [dumping] margin if such lesser duty would be adequate to remove the injury to the domestic industry."

21 Keon Ho Lee, for example, notes that in Korea the calculation of injury margins is subject to 'vast discretion'. Daniel Moulis points out that insufficient guidance in Australia facilitates abuse.

22 India, Korea, Mexico.

23 Brazil, India, Indonesia, Mexico, South Africa.

24 Brazil, Indonesia.

25 The EC.

26 Both in the EC.

27 China, India, Mexico, South Africa.

28 Brazil, the EC, Indonesia, South Africa.

29 Although they sometimes appear to be taken from import statistics, as Ana Caetano points out in the case of Brazil.

30 With the exception of the United States, none of the users investigated use a system of disclosure of confidential information under administrative protective order.

II. Conclusions

Most of the problems identified in the country studies appear directly linked to areas that are insufficiently regulated in the ADA. This is the case notably for the calculation of injury margins, related party issues, the establishment of a reasonable profit in constructed normal values, the adjustments for duty drawback, level of trade and quantity differences, the all others rate and PCN problems.

The problems signalled in review investigations in Mexico and Brazil could probably be tackled through access to the WTO dispute settlement process.

The transparency problem noted in several contributions appears unique in that it seems essentially a domestic issue that can be solved domestically if the will exists. Indeed, countries such as the United States and Canada have positive experience with systems of disclosure of confidential information under administrative order that could serve as a model for other jurisdictions.

The other problems identified, i.e., the 20 per cent rule and the treatment of NMEs, seem sufficiently regulated in the ADA but reflect the belief that the ADA rules themselves are not appropriate for the present state of the world's economies.