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Constructive Methods and Abuse of Antidumping Laws: A Legal Analysis of State Practice within the WTO Framework

P. R. Thulasidhass

*PhD student, Centre for International Legal Studies, Jawaharlal Nehru University,
New Delhi*

This article outlines the problems of *constructive antidumping methods* utilised by some WTO member countries when imposing dumping duties on products from other countries, as well as their negative impacts on free trade. It highlights five such methods – the arm's length test, the practice of *zeroing*, the constructed cost method, the use of downstream sales, and the captive production method – based on the analogy drawn from case laws decided by the WTO Appellate Body. The central theme of this article is that although the developed countries preach the concept of free trade, they do not follow the same in practice, and they are the frequent innovators of these constructive methods, the primary aim of which is to protect their domestic producers against the global competitiveness of developing countries. If such practices are not checked, it may lead to exploitation of the vulnerable economic position of developing countries.

Keywords: Antidumping Agreement, developing country, free trade, zeroing

Editorial Office: 410 22nd St. E., Suite 820, Saskatoon, SK, Canada, S7K 5T6.

Phone (306) 244-4800; Fax (306) 244-7839; email: kerr.w@esteycentre.com

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1. Introduction

The establishment of the international trade regime, through adoption of the GATT in 1947 and followed by its successor the World Trade Organisation in 1994, has liberalised restrictive trade barriers and thereby required states to rely on their comparative advantage to deliver economic welfare and sustainable growth. As a result, countries and corporations have engaged in aggressive global competition that could be referred to as trade wars in the post–Second World War world. “This global competition has not only opened new markets,” as Barfield (2005) observed, “it has challenged both nations and corporations to work harder than ever before to survive.” Against this backdrop, and considering the possibility of a sudden surge in international trade and its possible negative impact on domestic industries, the trade regime itself has introduced three major remedial measures, namely, countervailing duties, safeguards, and antidumping measures, to protect vulnerable industries in case of emergency. Among these, antidumping actions are the most widely used trade restrictions under the WTO regime since its inception. The reason may be twofold: first, antidumping actions are easier to use than any other protective remedies and their use allows wide discretion to member states; second, the agreement is not unambiguous and it contains provisions that are often subject to interpretation. The precise scope of the rules contained in WTO agreements is not always evident from a mere reading of the legal texts. In most cases, the answer can be found only after interpreting the legal terms contained in the provisions at issue (WTO, 2004). As a result of these circumstances member states have latitude to take antidumping actions based on fictitious grounds and in constructed circumstances. Consequently, the emergency measure becomes a hindrance for ‘free trade’, which the regime came into force in order to foster.

This article is structured as follows: section 2 deals with the definition and determination of dumping, dumping margins, and material injury. Section 3 analyses five different types of constructive antidumping actions that are often used by member states in their trade relations. Finally, section 4 ends with concluding remarks.

2. Definition and Determination of Dumping

In accordance with Article VI of the GATT, a product is said to be dumped when “products of one country are introduced into the commerce of another country at less than the normal value.” Introduction of a product under such conditions is

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condemned if it causes or threatens to cause material injury to an established industry or materially retards the establishment of a domestic industry. In order to offset or to prevent dumping, the country where the product has been introduced may levy an antidumping duty not greater in amount than the margin of dumping. The antidumping provision requires three conditions to be fulfilled in order for a product to be considered liable on the grounds of dumping and a duty imposed: first, the product is exported at less than the normal value; second, it has caused or threatened material injury or has materially retarded a domestic industry; and finally, the duty imposed shall not be more than the dumping margin. These are the substantial elements of antidumping measures. However, procedural issues related to determining the normal value of the product and the dumping margin, evaluating injury to domestic industries, defining 'domestic industries' in operational terms, etc. are dealt with in a separate agreement called the Agreement on Implementation of Article VI of the General Agreement on Tariffs and Trade 1994 (the Antidumping Agreement). Any investigation into antidumping measures is initiated and conducted only in accordance with the provisions of this agreement.

Article 2 of the Antidumping Agreement defines 'dumping' as occurring "if the export price of the product is less than the comparable price, in the ordinary course of trade, for the like product when destined for consumption in the exporting country." The provision also implies the meaning of 'dumping margin' is the difference between the export price and the domestic price. When there are no sales in the domestic market of the exporting country, then "the margin of dumping shall be determined by comparison with a comparable price of the like product when exported to an appropriate third country" or by comparison "with the cost of production in the country of origin plus a reasonable amount for administrative, selling and general costs and for profits." As per the provision, there are three methods to determine the dumping margin, namely, i) based on the price difference between the export price and the domestic price; ii) based on the price difference between the export price and the price of the product exported to a third country; and iii) based on the price difference between the export price and the cost of production plus other costs and profit. However, the provision does not provide any guidance as to when each of these methods shall be engaged, how to determine an appropriate third country, or what is meant by 'in the ordinary course of trade'. In all such cases it is left to the discretion of the member states to adopt their own methods for determining the dumping margin; this degree of latitude often leads to problems associated with antidumping duties arrived at based on constructed circumstances. Section 3 will examine these state

practices, including the arm's length test, the use of the constructed cost method, and the practice of considering downstream sales.

Article VI (2) of the GATT defines 'dumping margin' as the "price difference" between the export price and the normal value. This price difference of the exported product may be either less than the normal value or more than the normal value. On this account, a logical conclusion is that there is a possibility to establish either a positive dumping margin or a negative dumping margin when considering different categories of 'like product' for antidumping measures. However, the Antidumping Agreement does not provide any guidelines as to how to deal with positive and negative dumping margins when establishing an overall dumping margin. This ambiguity often allows member states to adopt constructed antidumping measures, for example, the practice of *zeroing*, which will also be looked at in section 3.

Similarly, constructive antidumping measures are also, at times, imposed by adopting different methods for injury determination under Article 4 of the agreement. The captive production method is one such method. Although the provision under Article 4 requires member states to take into account the "domestic producers as a whole" while determining injury to "domestic industry", some countries consider only a particular segment of the domestic producers. This limited inclusion leads to the determination that there is injury to the domestic industry, where there would have been no injury if the domestic producers as a whole had been considered. Even in cases where injury is likely to occur, considering only a particular segment of domestic producers may increase the dumping margin artificially – when using the 'proportionality test' provided under Article 11 of the agreement. Article 11 provides that "an anti-dumping duty shall remain in force only as long as and to the extent necessary to counteract dumping which is causing injury." Therefore, adopting constructive methods in injury determination can have a serious impact on the level of dumping duty to be imposed. The captive production method of the United States is one such method that will be explained in detail in section 3.

3. Constructive Antidumping Actions: A Legal Analysis

The expression 'constructive antidumping action' is used to indicate a situation where the export *per se* is not liable to antidumping actions in the strict sense of the relevant provisions, but is subsequently liable to antidumping actions due to the inventive and innovative methods adopted by the authorities in determining the injury and the dumping margin. However, the word 'constructive' does not mean to say, and is distinct from, 'constructed normal value' under Article 2 and 'constructive

remedies' under Article 15 of the Antidumping Agreement. Some of the significant constructive antidumping practices are as follows.

3.1 Arm's Length Test

The practice of using the arm's length test, or 99.5 percent test, is a method followed by the United States in accordance with its Tariff Act 1930 in order to avoid incorporating certain sales at a lower price in determining the 'normal value', if the lower price is due to the affiliation between the seller and the customer. Article 2.1 of the Antidumping Agreement defines 'normal value' as "the comparable value, in the ordinary course of trade, for the like product when destined for consumption in the exporting country." However, the agreement does not define 'in the ordinary course of trade'. The United States uses the arm's length test to determine whether a particular sale is in the ordinary course of trade, or not. The test authorises the investigating authorities to classify export market customers as affiliated and unaffiliated; thereby, the authorities first determine the weighted average normal value of the unaffiliated customers, and in the second step the authorities will compare this weighted average with each of the affiliated customers' sales. If such sales were made at least at the price of 99.5 percent of the weighted average, then such sales will be considered as sales made in the ordinary course of trade. Otherwise, they will be considered as not made in the ordinary course of trade. Consequently, by excluding certain sales made at lower prices in determining the normal value, the test facilitates an artificial increase of the weighted average normal value, to the detriment of the interest of exporters.

The arm's length test used by the United States was questioned by Japan in the *U.S. – Hot-Rolled Steel Products* case, on the grounds that the test is inconsistent with Article 2.1 of the Antidumping Agreement.¹ In this case, the United States imposed definitive antidumping duties on hot-rolled steel products from Japan by using the arm's length test, whereby it excluded some of the sales made to affiliated customers at a lower price, the inclusion of which would have reduced the weighted average normal value and consequently the dumping margin. Japan questioned this practice, arguing that a 0.5 percent difference in sales is common in fluctuating markets, and any rejection of such sales as not being made in the ordinary course of trade is inconsistent with Article 2.1. Further, Article 2.4 requires a "fair comparison", and it does not permit any arbitrary rule, such as the arm's length test, that rejects low-priced sales from the calculation of normal value, thereby artificially inflating the dumping margin (Raju, 2004). The dispute settlement panel for the case found that the arm's length test excludes certain home-market sales and, therefore, "skews the normal value upward"; hence, it is not consistent with Article 2.1 of the agreement.

The United States filed an appeal and argued before the Appellate Body that the purpose of the arm's length test is to determine whether the affiliation between the seller and the customer has, in general, affected the pricing of the goods sold to the affiliated customer. Such a sale cannot be considered a sale made in the ordinary course of trade. Article 2.1 requires that a determination of dumping must be based on transactions made in the ordinary course of trade but without providing any guidance as to what is meant by 'in the ordinary course of trade'. On that account it is left to the discretion of the member countries to adopt any method to determine whether particular sales are made in the ordinary course of trade or not. Further, the United States contended that the method, by automatically excluding affiliated sales at a price lower than the 99.5 percent threshold, prevents distortion of normal value. Accordingly, the practice is consistent with Article 2.1 of the agreement.

The Appellate Body accepted the argument regarding the discretion of the member states to adopt any methods, but it held that adoption of any such methods shall be exercised in an *even-handed* way that is fair to all. Further, it observed that not only low-priced sales but also high-priced sales shall be considered as not made in the ordinary course of trade. The inclusion of low-priced sales leads to a lower dumping margin, to the disadvantage of the importer. Similarly, the inclusion of high-priced sales leads to a higher dumping margin, to the disadvantage of the exporter. Hence, there must be a balance between the two. In this regard, the Appellate Body considered another test, called the *aberrationally high test*, followed by the United States to exclude high-priced sales. Under this test, unlike the arm's length test, the exclusion is not automatic but is made only upon request of the exporter; the burden of proving that a sale is aberrationally high is upon the exporter.

When considering both tests together, the Appellate Body held that the tests are not even-handed. The combined application of the two operates systematically to raise the normal value through the automatic exclusion of marginally low-priced sales coupled with the automatic inclusion of all high-priced sales except those proved, upon request, to be aberrationally high priced. The Appellate Body declared that the application of the two tests is disadvantageous to exporters and inconsistent with Article 2.1 of the agreement.

This case illustrates one example of the significant ambiguities that exist in the Antidumping Agreement. For the issue under consideration, the concept of 'in the ordinary course of trade' is central to determining the dumping margin and imposing dumping duties, but in the absence of any proper definition, member states are left free to use their own methods to determine what is in the ordinary course of trade.

Using such ambiguities, some countries may engage in constructive antidumping actions where in fact practices do not amount to dumping in the real sense.

3.2 The Practice of Zeroing

Zeroing is the practice of considering negative dumping margins as zero while establishing an overall dumping margin that often artificially escalates the margin in a way that is detrimental to the interest of the exporter. In detail, a 'dumping margin' is the price difference between the export price and the normal price. In determining the price difference, there is a possibility that the calculation may show either a *positive dumping margin* or a *negative dumping margin*. Positive dumping margins are those where the export price is lower than the normal value; negative dumping margins are those where the export price is higher than the normal value. In accordance with Article VI of the GATT and Article 2 of the Antidumping Agreement, imposition of dumping duties is permissible only when there exists a *positive dumping margin* and not otherwise.

When the exporter has more than one like product in the export market, the price difference is determined in accordance with Article 2.4.2 of the Antidumping Agreement, which provides that the dumping margin "shall normally be established on the basis of a comparison of a weighted average normal value with a weighted average of prices of all comparable export transactions." However, in practice, many developed countries follow two different stages in establishing the dumping margin in such circumstances. First, they establish the dumping margin for each individual type of product or for the products from each individual exporter or producer from a particular country, irrespective of whether the dumping margins are positive or negative. In the second stage, those dumping margins are combined to find an overall dumping margin. When combining these margins some countries follow the practice of considering negative dumping margins as zero, thereby artificially increasing the value of the overall dumping margin, to the detriment of the exporter. This is popularly known as the practice of *zeroing*, a practice that was questioned by India for the first time in the *EC – Bed Linen* case.²

In the *Bed Linen* case, the European Communities identified the products under investigation as cotton-type bed linen from India and classified these products as different models and types, i.e., pillow covers, bed sheets, etc. The EC then calculated for each of the models the weighted average normal value and the weighted average export price. For some models the normal price was higher than the export price, which established a positive dumping margin, and for other models the normal price was lower than the export price, which established a negative dumping margin. When calculating the overall dumping margin, the EC treated the negative dumping margins

as zero and added those zeroes with the positive dumping margins. Consequently, the EC established a definitive antidumping duty against India. The panel in the case found that the practice of *zeroing* was inconsistent with Article 2.4.2 of the Antidumping Agreement.

The European Communities filed an appeal and argued before the Appellate Body that the panel had failed to consider the word ‘comparable’ in Article 2.4.2. Since the different models of bed linen are not comparable, the investigating authorities first established dumping margins for each of the noncomparable types or models and then in the second stage combined those margins to establish an overall dumping margin. Further, the EC contended regarding this second stage that Article 2.4.2 provides no guidance, and hence it is left to the discretion of each member country to establish its own method. Thus, the EC argued, its method of *zeroing* is not inconsistent with Article 2.4.2.

The Appellate Body rejected the EC’s argument regarding the two stages of dumping-margin calculation, holding that it did not find any such different stages of calculation within the meaning of Article 2.4.2. In the Appellate Body’s opinion, the provision itself provides clear guidance as to the determination of dumping margins through the following wording:

... on the basis of a comparison of a weighted average normal value with a weighted average of prices of all comparable export transactions
(Article 2.4.2)

Here, the words ‘all comparable export transactions’ negate the validity of the practice of *zeroing* – since the practice considers negative dumping margins as zero and thereby does not take fully into account the entirety of the prices of some export transactions. Thus, the Appellate Body held that the practice of *zeroing* does not permit a “fair comparison” between export price and normal value, as required by Article 2.4 and by Article 2.4.2.

In reply to the EC’s concern with respect to *targeted dumping*, where the European Communities argued that countries may dump their products by increasing export prices for some transactions in order to avoid a positive dumping margin on other transactions, and consequently avoid the imposition of antidumping duties, the Appellate Body quoted the second sentence of Article 2.4.2:

A normal value established on a weighted average basis may be compared to prices of individual export transactions if the authorities find *a pattern of export prices which differ significantly among different purchasers, regions or time periods*, and if an explanation is provided as to why such differences cannot be taken into account appropriately by the use of a

weighted average-to-weighted average or transaction-to-transaction comparison. (emphasis added by the Appellate Body)

The Appellate Body held that this provision allows member states, in structuring their antidumping investigations, to address three kinds of targeted dumping, namely, dumping that is targeted to certain purchases, targeted to certain regions, or targeted to certain time periods. The practice of zeroing is neither warranted nor permissible in any of these cases. Consequently, it declared that the practice of zeroing was inconsistent with Article 2.4.2 of the Antidumping Agreement.

Though the Appellate Body declared the practice of zeroing to be inconsistent with the provisions of the Antidumping Agreement, the practice continues to be a hindrance to free trade. Since the *EC – Bed Linen* case in 2000 there have been 15 other cases related to the practice of zeroing alone filed before the WTO Dispute Settlement Body (DSB) thus far. The reason is that the reports of the panels and the Appellate Body do not become precedence for subsequent disputes even if the issues involved are the same. On the other hand, a maximum remedy against any violation will be only to require the violating member to discontinue the practice. And no question of reparation arises. In either case, the WTO agreements provide leeway for member countries to adopt any methods and practices, even on fictitious grounds, without concern for the consequences. Practical solutions could be to adopt authoritative interpretations or to amend the relevant provisions at once, expressly prohibiting the practice of zeroing and other such constructive methods, rather than require complainants to approach the WTO DSB every time to declare a practice inconsistent with the provisions of the agreement.³ This would enable the member states, especially the developing member countries, to escape from unreasonable financial burdens and trade restrictions.

3.3 Constructed Cost Dumping Method

Hoekman and Leidy (1989) are of opinion that there are two kinds of dumping, namely, price dumping and cost dumping. Price dumpings are those which occur due to price discrimination between the export price and domestic price. As defined by the Antidumping Agreement, price dumping may occur when the export price is “less than the comparable price, in the ordinary course of trade, for the like product when destined for consumption in the exporting country.”⁴ On the other hand, cost dumping, as defined by the Antidumping Agreement, may occur when the export price is compared with “the cost of production in the country of origin plus a reasonable amount for administrative, selling and general costs and for profits.”⁵ Generally, the investigating authorities prefer the cost-dumping method for determining a dumping margin on the ground that it allows a certain degree of flexibility for the investigating

authorities when fixing reasonable amounts for cost of production, selling, general and administrative costs (SG&A), and a reasonable amount for profit. Thus the method brings determination of 'normal value' within the purview of the discretion of the investigating authorities.

There is tremendous variation in costs of different factors of production in different countries, whether the cost of material inputs or the cost of labour, which are often cheaper in developing countries (Lee, 2006). All these factors exert considerable influence on the price of a product in a given market (Barefield, 2005). In such a case, the investigating authorities from developed countries may not consider the comparative advantages of a developing country, like cheap labour costs or cheaply available local inputs. However, the decision to use either the price-dumping or cost-dumping method is not left solely to the discretion of the member states. Article 2.2 provides certain guidelines as to when and how the constructed normal value method may be used as a mechanism to determine a dumping margin. The provision requires the investigating authorities to adopt constructed normal value only in the following three circumstances:

1. when there are no sales in the exporting market of the like product in the ordinary course of trade,
2. when the sales in the export market do not permit the proper comparison due to a particular market situation, or
3. when the sales in the export market do not permit the proper comparison due to the low volume of sales.

Further, Article 2.2.2 requires that the determination of SG&A and profit shall be based on "actual data pertaining to the production and sales in the ordinary course of trade of the like product by the exporter or producer under investigation." When comparing the provisions of Article 2.2.2 with those of 2.2 the following question may arise: If the investigating authority rejects particular actual data on the grounds of market situation or low-volume sales in accordance with Article 2.2 and subsequently decides to use the same data for determining SG&A and profit in accordance with Article 2.2.2, is such use permissible under the Antidumping Agreement?

Such a question was raised by Brazil in the *EC – Tube or Pipe Fitting* case.⁶ In this case, the European Commission imposed a definitive antidumping duty upon certain iron tubes and pipe fittings from Brazil on the basis of constructed normal value under Article 2.2 of the Antidumping Agreement. The issues involved in the case were the same as those discussed above. In the antidumping investigation, the European Commission rejected the price-dumping method on the grounds that certain products sold in the domestic market were of low quantity, and hence the actual data

were not reliable. The European Commission therefore resorted to a constructed normal value (i.e., the cost-dumping method) in accordance with Article 2.2. To calculate the constructed normal value the European Commission used actual SG&A and profit data from the Brazilian exporters, which were based on production and sales made ‘in the ordinary course of trade’. The data relied on by the European Commission included those data that were previously rejected as not reliable for the price-dumping method.

Brazil, however, argued before the panel that relying on those data, which were rejected as not reliable for proper comparison of prices under Article 2.2, for determining SG&A and profit was inconsistent with Article 2.2.2 of the Antidumping Agreement. Relying on the chapeau of Article 2.2.2, which reads,

For the purpose of paragraph 2, the amounts for administrative, selling and general costs and for profits shall be based on actual data pertaining to production and sales in the ordinary course of trade of the like product by the exporter or producer under investigation,

the panel found in favour of the European Communities and held that the provision allows the investigating authorities to exclude only data from production and sales that were not made in the ordinary course of trade; and the low-volume sales were not outside the ordinary course of trade.

Brazil appealed before the Appellate Body and argued that when the actual data are not reliable then the SG&A and profit shall be determined based on sub-clause (ii) of Article 2.2.2 of the agreement, which includes the phrasing, “the weighted average of the actual amounts incurred and realized by other exporters or producers subject to investigation in respect of production and sales of the like product in the domestic market of the country of origin”. On the other hand, the European Communities argued that the wording “in the ordinary course of trade” appears in both Article 2.2 and Article 2.2.2, whereas the wording “low volume of sales” appears only in Article 2.2 and not in Article 2.2.2. Hence, the low volume of sales cannot be considered to be not in the ordinary course of trade. Consequently, the exclusion of data of low-volume sales under Article 2.2 and the use of the same data under Article 2.2.2 is not inconsistent with either provision of the Antidumping Agreement.

The Appellate Body observed that Article 2.2.2 explicitly excludes data outside the ordinary course of trade by mentioning the words ‘in the ordinary course of trade’. Similarly, the omission of the words ‘low-volume sales’ in Article 2.2.2 confirmed their view that low-volume sales were not to be excluded from the chapeau of Article 2.2.2 for the calculation of SG&A and profits. Hence, the practice of the European Communities was deemed not inconsistent with Article 2.2.2.

The findings in this dispute clearly indicate how loosely the provisions of the Antidumping Agreement are framed. For instance, the provision under consideration allows the investigating authorities to reject particular data as not reliable for the price-dumping method on grounds such as ‘particular market situation’ or ‘low-volume sales’ and subsequently to use the same data for the cost-dumping method.

3.4 The Practice of Downstream Sales

The practice of using downstream sales is a method whereby first-hand, low-priced sales are replaced by downstream sales, i.e., second-hand sales, in calculating and determining normal value in the domestic market of the exporting country. The method is used to prevent the practice of disguising high-priced domestic sales by passing them through affiliates. But often this would result in an artificial increase in the normal value and consequently a higher dumping margin – based on a logical view that the value of downstream sales will always be more than the normal value of the first-hand sale, since the downstream sales shall include all the transportation charges, storage expenses, any profit of the first-hand buyer, etc., and these are commonly known factors in the domestic market.

Regarding the use of downstream sales, two provisions, namely, Article 2.2 and Article 2.3 shall be considered for a proper understanding. Article 2.2 deals with the determination of constructed normal value when no normal value in the domestic market of the exporting country exists or when the existing normal value is unreliable, and Article 2.3 deals with the determination of constructed export price when the export price is unreliable. In relation to the use of downstream sales, Article 2.3 provides that “where there is no export price or where ... export price is unreliable because of association or a compensatory arrangement between the exporter and the importer or a third party, the export price may be constructed on the basis of the price at which the imported products are first resold to an independent buyer.” In this case Article 2.3 expressly authorizes the use of downstream sales, whereas under Article 2.2, no such expressed authorization for the use of downstream sales in determining constructed normal value is made. In such a case, the question may arise as to whether the investigating authorities may use downstream sales in determining the constructed normal value under Article 2.2. In the *EC – Bed Linen* case, the Appellate Body answered the question negatively and held that:

The duty of the treaty interpreter is to examine the words of the treaty to determine the intentions of the parties. This should be done in accordance with the principles of treaty interpretation set out in Article 31 of the *Vienna Convention*. But *these principles of interpretation neither require nor condone the imputation into a treaty of words that are not there or the*

importation into a treaty of concepts that were not intended. (emphasis added)

Given this background, we may now consider the practice of using downstream sales that was questioned by Japan in the *U.S. – Hot-Rolled Steel Products* case.⁷ In this case, the U.S. investigating authorities replaced low-priced affiliated sales with the downstream sales value and determined a definitive antidumping duty against certain hot-rolled steel products from Japan. Japan challenged the practice as inconsistent with Article 2.1 of the Antidumping Agreement. The dispute settlement panel found in favour of Japan and held that the use of downstream sales to determine the normal value is not relevant because they are not sales of the exporter or producer for whom the dumping margin was being calculated. Further, when articles 2.2 and 2.3 are considered, the latter expressly allows the use of downstream sales where the export price is unreliable because of association, whereas Article 2.2 is silent as to the use of downstream sales in determining the ‘normal value’. Consequently, the practice of using downstream sales is inconsistent with Article 2.1.

The United States appealed the matter to the Appellate Body and argued that Article 2.1 does not impose any limitation on who must make the sales, and the rejection of the use of downstream sales in determining normal value would allow exporters to shield their high-priced domestic sales from scrutiny simply by passing them through affiliates. When considering the panel report and the argument of the United States, the Appellate Body observed that, according to Article 2.1 of the Antidumping Agreement, the normal value is “... the comparable price, in the ordinary course of trade, for the like product when destined for consumption in the exporting country.” The Appellate Body came out with a conclusion that the text expressly imposes four conditions on sales transactions in order that they may be used to calculate the normal value, namely, i) in the ordinary course of trade, ii) like product, iii) destined for consumption in the exporting country, and iv) the price must be comparable. The Appellate Body held that all the above explicit conditions are satisfied in the present case. The identity of the seller of the like product is not grounds for precluding the use of downstream sales while calculating the normal value under Article 2.1.

The only condition the Appellate Body imposed upon the investigating authorities was that “the price must be comparable”, and such a comparison shall be a “fair comparison” in accordance with Article 2.4 of the agreement. To make a fair comparison, Article 2.4 requires that the comparison shall be made at the same level of trade, and if it is otherwise, then due allowance shall be made for such differences. Japan raised the issue that the U.S. investigating authorities failed to make proper

allowance for its use of downstream sales in determining the normal value; hence the comparison was not a fair comparison under Article 2.4. The same issue was also raised in the original submission of Japan before the panel, but the panel rejected the issue as unnecessary, since the issue of downstream sales was found in favour of Japan. Regarding this, the Appellate Body observed that, though Article 2.4 requires fair comparison and the burden of proving fair comparison lies on the investigating authorities, the Appellate Body may not be able to entertain the issue due to lack of factual records. In the words of Appellate Body,

examination of this issue must be based on the factual findings of the Panel.... As the Panel did not examine this issue, ... we find that *there is not an adequate factual record* for us to complete the analysis by examining Japan's claim under Article 2.4 of the *Anti-Dumping Agreement*. (emphasis added)

The real tragedy of the issue is the existence of Article 17.6 of the WTO Dispute Settlement Understanding (DSU), which provides that “[a]n appeal shall be limited to issues of law covered in the Panel report and legal interpretations developed by the Panel.” Hence, the Appellate Body was reluctant to declare a particular practice as inconsistent, even though the practice in reality is inconsistent with the existing provisions of the covering agreement. There may be some alternative approach to Article 17.6 of the DSU whereby the Appellate Body could be allowed to consider the facts, at least to the extent where they have been raised by the parties but not considered by the Panel, or the Appellate Body may refer the issue to the same Panel for reconsideration. Otherwise, the ends of justice will not be served.

3.5 Captive Production Method

The captive production method is followed by the United States in accordance with its Tariff Act 1930. Section 771 of the act authorises the investigating authorities to “focus primarily” on a particular segment of domestic producers while determining ‘injury’ to the domestic industry, whereas the Antidumping Agreement requires that the injury determination shall be based on injury to the domestic producers as a whole and not to a particular segment of domestic producers. For instance, the agreement defines ‘injury’ as “material injury to a domestic industry, threat of material injury to a domestic industry or material retardation of the establishment of such an industry”,⁸ and Article 4 provides that the term ‘domestic industry’ means “domestic producers as a whole of the like product” or “whose collective output of the products constitutes a major proportion of the total domestic production of those products”. The captive production method was, therefore, questioned by Japan in the *U.S. – Hot-Rolled Steel*

Products case on the ground that it is inconsistent with articles 3 and 4 of the Antidumping Agreement.⁹

To provide a brief background for the case, in the United States there are two kinds of domestic producers of a like product, namely, those who sell products for the ‘merchant market’ and those who sell products for a ‘captive market’. The merchant market is the open market, including that for imported products; hence, there is a possibility of direct competition between exporters and domestic producers in the merchant market. In contrast, the captive market is a closed one, covering only the internal transfer of locally produced like products, the majority of which are used for manufacturing a downstream product. The provision of the U.S. Tariffs Act mentioned above requires the investigating authorities to “focus primarily” on the merchant market. However, Japan argued that this different treatment of captive production shields a significant portion of domestic producers (i.e., those engaged in captive production) from import competition; hence, the provision is not consistent with articles 3 and 4 of the agreement. The panel found in favour of the United States and held that specific circumstances might well call for specific attention to be given to various aspects of the industry’s performance. Further, the provision in question simply requires an authority to “focus primarily” but “not exclusively” on the merchant market. Hence, the captive production provision is not inconsistent with Article 3 or Article 4 of the agreement.

Japan appealed the matter before the Appellate Body and argued that having a primary focus on particular segment of the domestic producers does not amount to an ‘objective examination’ of the facts within the meaning of Article 3.1 of the agreement. The Appellate Body observed that Article 3.1 requires that an injury determination shall be based on “positive evidence” and “objective examination” of both the volume of dumped imports and the consequent impact of those products on domestic producers. Further, Article 3.4 elaborates Article 3.1 by expressly mentioning some of the relevant factors, such as decline in sales, profits, output, market share, productivity, etc., and finally declares that the list is not exhaustive. Hence, the use of “any other factors” like the “economic performance of a particular segment of the domestic industry” is not inconsistent with the provisions of the Antidumping Agreement.

However, the Appellate Body further held that, in the application of the captive production provision, an ‘objective examination’ under Article 3.1 means that “the investigating authorities cannot examine parts of a domestic industry on a selective basis”. Rather, if the authorities “examine one part of a domestic industry, they must examine, in like manner, all the other parts of the industry” or “provide a satisfactory

explanation as to why it is not necessary". The United States failed in both these aspects and thus acted inconsistently with articles 3.1 and 3.4 of the agreement when applying the captive production provision. Although Japan won the case, as scholars often say, it lost the argument.

4. Conclusion

Imposition of emergency measures under constructed circumstances is not limited to the purview of the Antidumping Agreement alone. It may also fit well into the framework of other agreements, for example the Agreement on Safeguards or the Agreement on Subsidies and Countervailing Measures. The reason is that the substantial requirements for justifying the imposition of emergency measures in all three cases are the same, i.e., a sudden surge in imported products and material injury to domestic producers. Although recourse to emergency measures is one of the welcome features of the trade regime, such measures are difficult to defend when imposed using constructed circumstances. If such use is allowed then it becomes a predatory mechanism in interstate trade relations. On the one hand, it facilitates the imposition of protective remedies even when protection is not essential and thereby offers unreasonable advantage to domestic producers. On the other hand, it negates the legally available advantage to producers from other countries. For instance, Article 5.8 of the Antidumping Agreement requires that member states not impose antidumping measures when the margin of dumping is *de minimis* or when the volume of dumped imports is negligible.

The margin of dumping is said to be *de minimis* when it is less than 2 percent of the export price. Similarly, the volume of dumped imports is said to be negligible when it is less than 3 percent of imports of the like product in the importing country. However, the adoption of constructed methods such as the arm's length test or the practice of zeroing artificially increases the margin and increases the imposition of antidumping measures. Consequently, it negates the legally available advantage and condemns the member states to approaching the WTO dispute settlement system each and every time to have the practice declared inconsistent with the provisions of the agreement. These circumstances lead to trade restrictions and serious economic consequences for vulnerable economies. They may hamper the attainment of the objectives promised under the WTO regime. It is time to remind ourselves that the Preamble to the *Agreement Establishing the World Trade Organisation* acknowledges that "there is a need for positive efforts designed to ensure that developing countries, and especially the least developed among them, secure a share in the growth in international trade commensurate with the needs of their economic development."

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Endnotes

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2. European Communities – Anti-Dumping Duties on Imports of Cotton-type Bed Linen from India, Appellate Body Report (WT/DS141/AB/R) of 1 March 2001.
3. Articles IX and X of the Marrakesh Agreement Establishing the World Trade Organisation.
4. Article 2.1 of the Antidumping Agreement 1994.
5. Article 2.2 of the Antidumping Agreement 1994.
6. European Communities – Anti-Dumping Duties on Malleable Cast Iron Tube or Pipe Fittings from Brazil, Appellate Body Report (WT/DS219/AB/R) of 22 July 2003.
7. *Supra* note 1.
8. Footnote 9 (Article 3) to the Antidumping Agreement 1994.
9. *Supra* note 1.