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**APPELLATE BODY REPORT ON EU-
BIODIESEL: FURTHER THOUGHTS ON THE
ISSUE OF “PARTICULAR MARKET
SITUATION”**

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Appellate Body Report on *EU-Biodiesel*: Further Thoughts on the Issue of “Particular Market Situation”

Weihuan Zhou*

1 INTRODUCTION

In *Debunking the Myth of ‘Particular Market Situation’ in WTO*, an article published by the *Journal of International Economic Law* (JIEL) in December 2016, the author analysed the issue of Particular Market Situation (PMS) in depth in the context of the WTO Agreement on Antidumping (AD Agreement) and proposed a standard approach to the interpretation and application of PMS. (JIEL Article)¹ The main arguments of that article and the relevant provisions of the AD Agreement are set out briefly in this section.

First, the author argued that an interpretation of the AD Agreement, based on the relevant text, context and the object and purpose of the agreement, does not provide sufficient guidance as to what the term PMS exactly means and covers. The main provisions of the AD Agreement include:

Article 2.1

For the purpose of this Agreement, a product is to be considered as being dumped, i.e. introduced into the commerce of another country at less than its normal value, if the export price of the product exported from one country to another is less than the comparable price, in the ordinary course of trade, for the like product when destined for consumption in the exporting country.

Article 2.2

When there are no sales of the like product in the ordinary course of trade in the domestic market of the exporting country or when, because of the particular market situation or the low volume of the sales in the domestic market of the exporting country, such sales do not permit a proper comparison, the margin of dumping shall be determined by comparison with a comparable price of the like product when exported to an appropriate third country, provided that this price is representative, or with the cost of production in the country of origin plus a reasonable amount for administrative, selling and general costs and for profits.

Article 2.4

A fair comparison shall be made between the export price and the normal value. This comparison shall be made at the same level of trade, normally at the ex-factory level, and in respect of sales made at as nearly as possible the same time. Due allowance shall be made in each case, on its merits, for differences which affect price comparability, including differences in conditions and terms of sale, taxation, levels of trade, quantities, physical characteristics, and any other differences which are also demonstrated to affect price comparability.

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¹ Weihuan Zhou and Andrew Percival, “Debunking the Myth of ‘Particular Market Situation’ in WTO Antidumping Law” (2016)19(4) *Journal of International Economic Law* 863-892.

Article 2.7

This Article is without prejudice to the second Supplementary Provision to paragraph 1 of Article VI in Annex I to GATT 1994.

The second Supplementary Provision to paragraph 1 of Article VI of the GATT 1994 provides:

2. It is recognized that, in the case of imports from a country which has a complete or substantially complete monopoly of its trade and where all domestic prices are fixed by the State, special difficulties may exist in determining price comparability for the purposes of paragraph 1, and in such cases importing contracting parties may find it necessary to take into account the possibility that a strict comparison with domestic prices in such a country may not always be appropriate.

At best, two observations can be drawn from the above provisions, including that:

1. a PMS does not include the other two circumstances envisaged in Article 2.2 of the AD Agreement in relation to 'no domestic sales in the ordinary course of trade' and 'low volume of domestic sales', and the extreme market conditions arising from complete or substantially complete state monopolies as contemplated separately in Article 2.7 of the AD Agreement; and
2. the interpretation of PMS requires an assessment of the comparability of normal value *vis-à-vis* export price, although it remains uncertain whether this assessment should be undertaken under Article 2.2 or Article 2.4 of the AD Agreement.

Second, by resorting to the drafting records of the AD Agreement and the preceding Antidumping Codes negotiated during the GATT era, the author found no further clarifications due to the lack of such records on the issue of PMS. However, the discussions of the issue of "input dumping" during the Uruguay Round suggests that

1. in circumstances where the price of raw materials used for the production of final goods is distorted or artificially lowered, a determination of whether the final goods are sold at dumped prices must still be based on whether the domestic price of the goods is comparable to their export price.²

Third, based on the analysis of the AD Agreement, the negotiating records, and relevant GATT/WTO jurisprudence on antidumping, the author proposed that the term PMS should be interpreted and applied as follows:

1. unlike the use of the non-market-economy (NME) methodology which was permitted under China's WTO Accession Protocol but has arguably expired, the burden of proving that a PMS exists is on investigating authorities and not on the exporters or producers or governments of exporting countries involved in antidumping investigations;
2. a PMS would arise only if the situation in concern precludes a "proper comparison" between export price and normal value. Accordingly, and given the burden of proof, investigating authorities must establish that the situation at issue has actually affected the comparability of the two prices; and

² Ibid., at 876-878.

3. the comparability of normal value and export price is affected if the market situation has caused a distortion in the normal value but not in the export price. However, the price comparability should not be treated as being affected if the situation has caused a distortion in both the normal value and the export price in an even-handed manner. Accordingly, neither the existence of a situation in the market nor a finding of distortion in the domestic price of the subject goods, by itself or collectively, constitute sufficient evidence for a finding that a PMS exists. A situation in the exporting market under investigation should not be treated as being “particular” unless it affects the price comparability.

This standard approach was illustrated by the typical antidumping practice in Australia. To date, Australia has been the most frequent user of the PMS approach as Australia committed not to use the NME methodology as a precondition for the negotiations of the China-Australia Free Trade Agreement (ChAFTA) in 2005. In determining that a PMS exists, Australian antidumping authorities have consistently relied on (arguably insufficient) evidence showing that prices of main raw materials used for the production of final goods under investigation are artificially lowered due to government intervention or influence in the raw materials markets. Based on such evidence, the authorities have assumed that the domestic prices of the final goods are also distorted and hence not comparable with their export prices. This antidumping practice is arguably inconsistent with Article 2.2 of the AD Agreement for the lack of evidence to show that a proper comparison between the allegedly distorted normal value and the export price has been affected. The assumption is not only unfounded but also unreasonable because a distortion in the price of raw materials is likely to affect or flow through to both the domestic price and the export price of the subject goods in an equal manner. Therefore, the assumption would result in a comparison between an undistorted Constructed Normal Value (CNV) and a distorted export price, and ultimately an inflation of dumping margins. If this occurs, the Australian approach to PMS may also be found in violation of Article 9.3 of the AD Agreement which states:

Article 9.3

The amount of the anti-dumping duty shall not exceed the margin of dumping as established under Article 2.

A final major point raised in the JIEL Article concerns how to avoid unjustified inflation of dumping margins if the term PMS is abused as above. It was argued that if antidumping authorities decide not to assess whether input price distortions have precluded a proper comparison between normal value and export price of final goods in finding that a PMS exists, they must make necessary adjustments for the difference resulting from the use of undistorted input costs for the calculation of CNV and distorted costs for the determination of export price, so as to ensure “fair comparison” between the two prices under Article 2.4 of the AD Agreement. Before the Appellate Body’s rulings in *EU – Biodiesel*, the issue whether such an adjustment is required to be made under Article 2.4 was unsettled. This Appellate Body Report

was not discussed in the JIEL Article as it was released after the revisions of that article have been completed.

This paper is organized as follows. Section 2 offers a detailed analysis of the Appellate Body's report on *EU – Biodiesel*, focusing on three issues: (1) on what basis antidumping authorities may replace the actual input costs incurred by exporters with a benchmark/surrogate input cost in determining CNV (i.e. Article 2.2.1.1 of the AD Agreement); (2) if a benchmark input cost is employed, whether the authorities are required to make adjustments to ensure the cost reflects the market conditions prevailing in the country of origin, and if so, how (i.e. Article 2.2 of the AD Agreement); and (3) what role Article 2.4 may play in the above context.³ Section 3 discusses the most recent development of the use of PMS in antidumping practices in Australia, the United States (US) and the European Union (EU) in the light of *EU – Biodiesel*. Section 4 concludes with a summary of the major arguments advanced in the paper.

2 Appellate Body Report on *EU – Biodiesel*

The *EU – Biodiesel* dispute concerns the EU's imposition of antidumping duties on biodiesel exported from Argentina and Indonesia.⁴ In the preliminary determinations, the EU authorities found that domestic sales of biodiesel in Argentina were not made in the ordinary course of trade due to state intervention in the domestic biodiesel market. In calculating a CNV, the authorities employed the production costs recorded by the Argentinean producers under investigation but decided to further consider the impacts of the Differential Export Tax (DET) system under which Argentina imposed taxes on the exports of soybeans and soybean oil – the main raw materials used in the production of biodiesel. The provisional dumping margins were found to be between 6.8% and 10.6%. In the final determinations, the EU authorities found that the DET system had created a PMS in the domestic raw materials market by artificially lowering the prices of soybeans and soybean oil which were lower than the international prices essentially by the amount of the export taxes. Therefore, the records of the Argentinean producers were found to be not reasonably reflecting the raw materials costs and were replaced with the average reference prices of the raw materials published by the Argentine Ministry of Agriculture for the calculation of the CNV. The use of the surrogate input costs resulted in an increase of the provisional dumping margins to a range from 41.9% to 49.2%.

³ In discussing these issues, the paper also builds on Weihuan Zhou and Andrew Percival, "Panel Report on *EU – Biodiesel*: A Glass Half Full? – Implications for the Rising Issue of 'Particular Market Situation'" (2016)2(2) *Chinese Journal of Global Governance* 142-163.

⁴ Panel Report, *European Union—Anti-Dumping Measures on Biodiesel from Argentina*, WT/DS473/R, adopted 26 Oct 2016 (as modified by the Appellate Body Report) paras. 2.2-2.3, 7.179-7.184; Appellate Body Report, *Union—Anti-Dumping Measures on Biodiesel from Argentina*, WT/DS473/AB/R, adopted 26 Oct 2016, paras. 5.1-5.10. The EU authorities' final decisions which imposed the antidumping measures challenged by Argentina can be found at: trade.ec.europa.eu/tdi/case_history.cfm?id=1893&init=1893

Before the panel, Argentina challenged the EU Regulation “as such” and “as applied” in violation of a number of provisions of the AD Agreement.

2.1 “As such” claim

The “as such” claim concerned Article 2(5) of the Basic Regulation which states:

5. Costs shall normally be calculated on the basis of records kept by the party under investigation, provided that such records are in accordance with the generally accepted accounting principles of the country concerned and that it is shown that the records reasonably reflect the costs associated with the production and sale of the product under consideration.

If costs associated with the production and sale of the product under investigation are not reasonably reflected in the records of the party concerned, they shall be adjusted or established on the basis of the costs of other producers or exporters in the same country or, where such information is not available or cannot be used, on any other reasonable basis, including information from other representative markets.

Argentina argued that the second paragraph of Article 2(5) is inconsistent “as such” with Articles 2.2 and 2.2.1.1 of the AD Agreement. Article 2.2.1.1 sets out, in the relevant part, how production costs should be determined for the construction of normal value:

Article 2.2.1.1

For the purpose of paragraph 2, costs shall normally be calculated on the basis of records kept by the exporter or producer under investigation, provided that such records are in accordance with the generally accepted accounting principles of the exporting country and reasonably reflect the costs associated with the production and sale of the product under consideration.

Argentina argued that the second paragraph of Article 2(5) of the EU Regulation mandates the EU authorities to reject production costs recorded by exporters if the costs have been found to be distorted or artificially low and hence not reasonably reflecting prices (i.e. a violation of Article 2.2.1.1), and subsequently to use costs other than those prevailing in the country of origin to construct normal value (i.e. a breach of Article 2.2). Both arguments were rejected by the panel and the Appellate Body.

On the alleged breach of Article 2.2.1.1, both the panel and the Appellate Body held that the second paragraph of Article 2(5) comes into play only after determinations have been made on whether production costs are “reasonably reflected” in the producer’s records under the first paragraph of that article.⁵ In other words, it is the first paragraph of Article 2(5) that should be subject to Argentina’s claim of violation of Article 2.2.1.1; hence, Argentina’s “as such” claim was misplaced. Understandably, Argentina did not target the first paragraph which reproduces Article 2.2.1.1 of the AD Agreement.

As far as the alleged violation of Article 2.2 is concerned, the panel found that the second paragraph of Article 2(5) does not *require* the EU authorities to replace

⁵ Panel Report, *EU – Biodiesel*, para. 7.153; Appellate Body Report, *EU – Biodiesel*, paras. 6.198, 6.237.

producers' costs with costs in another country, but merely permits the authorities to "establish or adjust the costs reported in the producers' records on the basis of information from other representative markets".⁶ In upholding the panel's finding, the Appellate Body observed that out-of-country *information* can be used to establish production costs as long as necessary adjustments are made to ensure the costs reflect the cost of production in the country of origin.⁷ While the second paragraph of Article 2(5) may be read to permit the EU authorities to "use 'information from other representative markets', as the basis for arriving at the costs of production, without adapting it to reflect the costs of production in the country of origin", this is not mandatory.⁸

The panel and Appellate Body's rulings seem to be consistent with the existing WTO jurisprudence on the "mandatory/discretionary distinction", that is, whether a member's measure mandates WTO inconsistent acts (so that the measure is in violation "as such") or merely provides authorities the discretion to do so (so that only the practical application of the measure may be found in breach of WTO rules).⁹ In the present dispute, the EU authorities were vested with the discretion in determining production costs in a way that is not inconsistent with the AD Agreement. That is, the discretion for the authorities to make adjustments to out-of-country information determines that an "as such" violation of Article 2.2 cannot be established. Therefore, even though it is possible for the authorities to act inconsistently with the AD Agreement as they did in a series of cases¹⁰, a breach of the agreement is not "mandatory" and must be established on a case-by-case basis.

The ruling that out-of-country information may be used for the establishment of production costs in the country of exportation is sound as it takes into account the possibility of the lack of domestic costs information. However, the Appellate Body did not elaborate on what adjustments should be made to ensure out-of-country information reflects the market condition prevailing in the exporting country. This issue will be further discussed below.

2.2 "As applied" claim

The panel ruled in favour of Argentina on all "as applied" claims under Articles 2.2.1.1 and 2.2 of the AD Agreement. All of the panel's rulings were subsequently endorsed by the Appellate Body.

(1). Article 2.2.1.1

⁶ Panel Report, *EU – Biodiesel*, para. 7.169.

⁷ Appellate Body Report, *EU – Biodiesel*, para. 6.242.

⁸ Appellate Body Report, *EU – Biodiesel*, para. 6.243.

⁹ Appellate Body Report, *United States—Anti-Dumping Act of 1916*, WT/DS136/AB/R, WT/DS162/AB/R, adopted on 26 September 2000, paras. 88–89.

¹⁰ Panel Report, *EU – Biodiesel*, para. 7.147.

With respect to the condition that producers' records must "reasonably reflect the costs associated with the production and sale of the product under consideration" under Article 2.2.1.1 (Reasonableness Test), the Appellate Body found that this test

... requires a comparison between the costs in the producer's or exporter's records and the costs incurred by such producer or exporter... "the object of the comparison is to establish whether the records reasonably reflect the costs actually incurred, and not whether they reasonably reflect some hypothetical costs that might have been incurred under a different set of conditions or circumstances and which the investigating authority considers more 'reasonable' than the costs actually incurred.¹¹

[and]

... relates to whether the records kept by the exporter or producer under investigation suitably and sufficiently correspond to or reproduce those costs incurred by the investigated exporter or producer that have a genuine relationship with the production and sale of the specific product under consideration.¹²

Accordingly, the Appellate Body upheld the panel's finding that

... the EU authorities' determination that domestic prices of soybeans in Argentina were lower than international prices due to the Argentine export tax system was not, in itself, a sufficient basis under Article 2.2.1.1 for concluding that the producers' records do not reasonably reflect the costs of soybeans associated with the production and sale of biodiesel, or for disregarding those costs when constructing the normal value of biodiesel.¹³

In essence, the rulings above establish that investigating authorities must use the production costs actually incurred by producers or exporters for the calculation of a CNV even though the costs are considered to be "distorted" or "artificially lowered" due to state intervention. This is because the Reasonableness Test is confined to an assessment of whether the records suitably and sufficiently reflect the actual costs incurred and does not allow for consideration of the reasonableness of the costs themselves. On what the requirements of "suitably", "sufficiently", and "having a genuine relationship with the production and sale of the specific product under consideration" may entail, the Appellate Body provided further clarification based on the remainder of Article 2.2.1.1 which essentially concerns the allocations and adjustments of costs in a way that reflects the costs actually incurred in the production of the subject goods by each exporter or producer under investigation.¹⁴

In the present case, the EU authorities' decision to use surrogate costs was based on a finding of PMS in the raw materials market which, in turn, was based on the finding that the prices of soybeans and soybean oil were lower than the international prices due to the DET system. In rejecting the EU authorities' findings in the context of the Reasonableness Test, the Appellate Body clarified that as long as the recorded production costs suitably and sufficiently reflect the actual costs incurred, the

¹¹ Appellate Body Report, *EU – Biodiesel*, para. 6.41.

¹² Appellate Body Report, *EU – Biodiesel*, para. 6.56.

¹³ Panel Report, *EU – Biodiesel*, para. 7.248; Appellate Body Report, *EU – Biodiesel*, para. 6.55.

¹⁴ Appellate Body Report, *EU – Biodiesel*, para. 6.22.

existence of a PMS due to price distortions and state intervention by itself does not justify a deviation from an exporter's actual costs.

To be clear, the WTO tribunals in *EU – Biodiesel* did not examine what may constitute a PMS; nor did they exclude the possibility that the existence of a PMS may render production costs not being reasonably reflected in producers' records. However, in the latter situation, evidence in addition to state intervention and price distortion must be adduced to determine whether recorded production costs reflect the actual costs incurred in the production of the subject goods. While the rulings concerned export taxes, they suggest that price distortions caused by other trade or domestic instruments, such as export restrictions, domestic subsidies, or price controls, standing alone, would also fail the Reasonableness Test.

In the author's view, the tribunals' rulings come very close to the proposition that state intervention causing price distortions, and a finding of PMS on that basis, is irrelevant to the determination of whether surrogate costs should be employed. In this connection, the Appellate Body rejected the EU's submission that production costs used for the calculation of a CNV must be one "in normal circumstances, i.e. in the absence of the alleged distortion caused by Argentina's export tax system".¹⁵ This suggests that *distorted* production costs in a PMS should still be used for the construction of normal value as long as they reflect the prevailing conditions in the market.

The Appellate Body's rulings are sound. Government regulations exist in all markets; and such regulations, combined with various types of industrial financial assistance and other governmental measures, undoubtedly affect prices, either directly or indirectly. Thus, it is impossible to determine what price is "reasonable" and whether chosen surrogate costs are completely free of government regulation or distortion. Furthermore, each country has its own market which determines that production costs vary from country to country. The use of surrogate costs for the construction of normal value ignores the differences in the market conditions in different countries. Given the differences, one country can always treat the other as having a "particular" market situation as it applies its own standards in determining what costs are reasonable. In rejecting state intervention and price distortion as being sufficient to satisfy the Reasonableness Test, the Appellate Body has adroitly avoided *tit-for-tat* abuse of surrogate costs through findings of PMS. Finally, if an exporter's actual costs of production are found to be distorted, it is reasonable to assume that such a distortion has affected or 'flowed through' to both of the export price and the domestic selling prices of the goods to the same extent,¹⁶ so that a proper comparison between the export price and the normal value would not be precluded. This offers an additional explanation why the Reasonableness Test should not concern price

¹⁵ Appellate Body Report, *EU – Biodiesel*, para. 6.30.

¹⁶ Thomas Prusa and Edwin Vermulst, "United States – Definitive Anti-Dumping and Countervailing Duties on Certain Products from China: Passing the Buck on Pass-Through", (2013)12(2) *World Trade Review* 197–234 at 217–19.

distortions. In the context of determining whether a PMS exists, this imposes an obligation on investigating authorities to establish that input price distortions have impacted on normal value and export price asymmetrically to justify the construction of normal value.¹⁷

Finally, one must note that the Appellate Body contemplated several scenarios which may satisfy the Reasonableness Test, including:

if certain costs relate to the production both of the product under consideration and of other products, or where the exporter or producer under investigation is part of a group of companies in which the costs of certain inputs associated with the production and sale of the product under consideration are spread across different companies' records, or where transactions involving such inputs are not at arm's length.¹⁸

Except for the last scenario, the others concern whether production costs are reasonably *allocated* rather than whether the costs themselves are reasonable. The last example deals with situations where raw materials are purchased not at arm's length prices, i.e. between related parties. While this example may be treated as involving a consideration of the reasonableness of the purchase price of inputs, it leaves no room for consideration of price distortions associated with state intervention.¹⁹ As the Appellate Body has clarified in other disputes, what this scenario concerns is whether the terms and conditions for the sale of the inputs at issue are compatible with normal commercial practice for such sales in the market in question.²⁰ Therefore, it deals with *business activities* which cause the transaction prices of inputs lower or higher than arm's length prices²¹, not state influence on or regulation of input prices.

In light of the above, the Appellate Body's decisions under Article 2.2.1.1, particularly on the Reasonableness Test, have ruled out the possibility that state intervention and price distortions alone would justify the use of surrogate costs for the construction of normal value. Hopefully, this could dissuade WTO members from abusing PMS or state intervention to effectively extend the NME methodology.

(2). Article 2.2

¹⁷ This observation can be drawn from the Appellate Body's interpretation of the 'pass through' issue in the context of assessing the application of countervailing duties to tackling "input subsidies" under the Agreement on Subsidies and Countervailing Measures. See generally Appellate Body Report, *United States—Final Countervailing Duty Determination with Respect to Certain Softwood Lumber from Canada*, WT/DS257/AB/R, adopted 17 February 2004. Also see Sherzod Shadikhodjaev, 'How to Pass a Pass-Through Test: the Case of Input Subsidies' (2012)15(2) *Journal of International Economic Law* 621–46 at 635–36.

¹⁸ Appellate Body Report, *EU – Biodiesel*, para. 6.33.

¹⁹ See generally Stéphanie Noël and Weihuan Zhou, "Replacing the Non-Market Economy Methodology: Is the European Union's Alternative Approach Justified Under the World Trade Organization Anti-Dumping Agreement?" (2016)11(11/12) *Global Trade and Customs Journal* 559-567 at 563-65.

²⁰ Appellate Body Report, *United States – Anti-Dumping Measures on Certain Hot-Rolled Steel Products from Japan*, WT/DS184/AB/R, adopted 23 August 2001, para. 140.

²¹ *Ibid.*, para. 143.

Under Article 2.2 of the AD Agreement, the tribunals made a significant distinction between the *cost* of production and the *information* used for the establishment of the cost. In the words of the Appellate Body,

... In circumstances where the obligation in the first sentence of Article 2.2.1.1 to calculate the costs on the basis of the records kept by the exporter or producer under investigation does not apply, or where relevant information from the exporter or producer under investigation is not available, an investigating authority may have recourse to alternative bases to calculate some or all such costs. Yet, Article 2.2 does not specify precisely to what evidence an authority may resort. This suggests that, in such circumstances, the authority is not prohibited from relying on information other than that contained in the records kept by the exporter or producer, including in-country and out-of-country evidence. This, however, does not mean that an investigating authority may simply substitute the costs from outside the country of origin for the "cost of production in the country of origin". Indeed, Article 2.2 of the Anti-Dumping Agreement and Article VI:1(b)(ii) of the GATT 1994 make clear that the determination is of the "cost of production [...] in the country of origin". Thus, whatever the information that it uses, an investigating authority has to ensure that such information is used to arrive at the "cost of production in the country of origin". Compliance with this obligation may require the investigating authority to adapt the information that it collects.²²

The Appellate Body considered two specific circumstances (in footnotes) where out-of-country information or evidence may need to be used. One circumstance would be "where the producer under investigation purchases inputs from outside the country of origin to produce the product under consideration".²³ In this circumstance, the Appellate Body, however, seems to be concerned about the accuracy of the out-of-country information and not about whether the information reflects the market condition of the country of origin.²⁴ The other circumstance pertains to "where the producer under investigation refuses access to and does not provide information concerning costs, and the investigating authority relies on "best information available" under Article 6.8 and Annex II to the Anti-Dumping Agreement".²⁵ The Appellate Body did not consider what adjustments may be required in these circumstances.

Accordingly, investigating authorities are allowed to use information or evidence in a different market/country to determine the cost of production in the exporting country under investigation. There appears to be no limitation on what information or evidence may be employed. However, out-of-country information can be used only when the conditions under Article 2.2.1.1 are satisfied, or in-country information is unavailable or is otherwise not provided. Furthermore, if out-of-country information is used, such information must be adjusted to reflect the cost of production in the country of origin.

²² Appellate Body Report, *EU – Biodiesel*, para. 6.73.

²³ Appellate Body Report, *EU – Biodiesel*, FN 228.

²⁴ *Ibid.*

²⁵ Appellate Body Report, *EU – Biodiesel*, FN 230.

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On the use of the reference prices by the EU authorities, the Appellate Body, in upholding the panel's findings, held that the authorities had failed to make adjustments on the following ground:

... Other than pointing to the deduction of fobbing costs, the European Union has not asserted, either before the Panel or before us, that the EU authorities adapted, or even considered adapting, the information used in their calculation in order to ensure that it represented the cost of production in Argentina. On the contrary, the EU authorities specifically selected the surrogate price for soybeans to remove the perceived distortion in the cost of soybeans in Argentina. As the Panel stated, the EU authorities selected and used this particular information precisely because it did not represent the cost of soybeans in Argentina. Thus, we agree with the Panel that the surrogate price for soybeans used by the EU authorities did not represent the cost of soybeans in Argentina for producers or exporters of biodiesel.²⁶ (emphasis added)

This ruling shows that an adjustment must be made to the benchmark costs to ensure the costs used for the construction of normal value reflect the price distortions associated with the DET system and hence the market conditions in Argentina. This suggests that no matter what cost information or evidence is employed to determine the production cost of a producer or exporter in the country under investigation, the practice of using surrogate costs must not be conducted to disregard the policy and regulatory environment of the country which may have directly or indirectly affected input prices. For example, if surrogate costs are used based on a finding of PMS, adjustments must be made to reinstitute any price distortions associated with the PMS into the surrogate costs. Accordingly, while the Appellate Body did not provide full clarity on all types of adjustments, it challenged head-on the rampant antidumping practice of using benchmark input costs in the construction of normal value in order to inflate dumping margins. The rulings on adjustments reinforce the rulings on the Reasonableness Test and impose an additional disincentive for antidumping authorities to abuse benchmark prices.

In addition, one should note the jurisprudence on Article 14(d) of the Agreement on Subsidies and Countervailing Measures (SCM Agreement), which provides

(d) the provision of goods or services or purchase of goods by a government shall not be considered as conferring a benefit unless the provision is made for less than adequate remuneration, or the purchase is made for more than adequate remuneration. The adequacy of remuneration shall be determined in relation to prevailing market conditions for the good or service in question in the country of provision or purchase (including price, quality, availability, marketability, transportation and other conditions of purchase or sale). (emphasis added)

In *US – Softwood Lumber IV*, the US authority found that the Canadian prices of stumpage did not reflect competitive market prices and hence applied benchmark prices based on stumpage prices in the US to determine adequacy of remuneration.²⁷ The Appellate Body observed that

²⁶ Appellate Body Report, *EU – Biodiesel*, para. 6.81.

²⁷ Appellate Body Report, *United States – Final Countervailing Duty Determination with respect to Certain Softwood Lumber from Canada*, WT/DS257/AB/R, adopted 17 February 2004, para. 77.

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... investigating authorities may use a benchmark other than private prices in the country of provision under Article 14(d), if it is first established that private prices in that country are distorted because of the government's predominant role in providing those goods.²⁸

However, unlike Article 2.2 of the AD Agreement and *EU – Biodiesel*, the reason why price distortions caused by state intervention constitute a basis for the use of benchmark prices under Article 14(d) of the SCM Agreement is that government influence on private prices would preclude the measurement of benefit conferred by subsidies.²⁹ Therefore, this ruling is specific to the purpose of Article 14(d) and does not affect the Appellate Body's decisions in *EU – Biodiesel* and my discussions above.

The Appellate Body went on to rule that

... where an investigating authority proceeds in this manner, it is under an obligation to ensure that the resulting benchmark relates or refers to, or is connected with, prevailing market conditions in the country of provision, and must reflect price, quality, availability, marketability, transportation and other conditions of purchase or sale, as required by Article 14(d).³⁰

However, the Appellate Body had insufficient evidence to determine whether the US had made proper adjustments but merely recognized that it may be difficult for investigating authorities to make all adjustments to replicate market conditions prevailing in the country under investigation.³¹ Towards this end, the Appellate Body offered an enlightening remark:

It is clear, in the abstract, that different factors can result in one country having a comparative advantage over another with respect to the production of certain goods. In any event, any comparative advantage would be reflected in the market conditions prevailing in the country of provision and, therefore, would have to be taken into account and reflected in the adjustments made to any method used for the determination of adequacy of remuneration, if it is to relate or refer to, or be connected with, prevailing market conditions in the market of provision. This is because countervailing measures may be used only for the purpose of offsetting a subsidy bestowed upon a product, provided that it causes injury to the domestic industry producing the like product. They must not be used to offset differences in comparative advantages between countries.³²

This remark suggests that if benchmark prices are employed, adjustments must be made to fully reflect the comparative advantage that the country of origin gains from its factor endowments. This raises an issue with the Appellate Body's decisions in *EU – Biodiesel* that adjustments of benchmark prices must be made to reflect price distortions caused by state intervention in the country under investigation. That is, whether adjustments of benchmark prices should be required if a comparative advantage is created by state intervention. Given the Appellate Body's decisions in *EU – Biodiesel*, it is submitted that government-caused price distortions are not intended to be dealt with under the AD Agreement unless otherwise specified in the

²⁸ Ibid., para. 90.

²⁹ Ibid., paras. 93, 100-1.

³⁰ Ibid., para. 106.

³¹ Ibid., para. 108.

³² Ibid., para. 109.

agreement (e.g. Article 2.7 of the agreement). Thus, Articles 2.2 and 2.2.1.1 of the AD Agreement do not concern state interference but should focus on business practices of companies that amount to price differentiation between different markets. Rather, state intervention should be dealt with under the other WTO agreements such as the SCM Agreement and the GATT 1994.

In *US – Carbon Steel (India)*, the Appellate Body observed that the term “prevailing market conditions” in the context of Article 14(d) of the SCM Agreement, consist of generally accepted characteristics of an area of economic activity in which the forces of supply and demand interact to determine market prices.³³ By referring to *US – Softwood Lumber IV*, the Appellate Body confirmed that to allow for an assessment of adequacy of remuneration, “any benchmark for conducting such an assessment must consist of market-determined prices for the same or similar goods that relate or refer to, or are connected with, the prevailing market conditions for the good in question in the country of provision.”³⁴ As discussed above, this ruling does not affect the Appellate Body’s decisions in *EU – Biodiesel*; rather, it lends support to the view that price distortions associated with state intervention should not be dealt with under the AD Agreement.

On adjustment of benchmark prices, the Appellate Body found that “the illustrative list of “prevailing market conditions” parenthetically identified in the second sentence of Article 14(d) – “price, quality, availability, marketability, transportation and other conditions of purchase or sale” – are all factors that may affect the comparability of a benchmark price with the financial contribution at issue.”³⁵ The Appellate Body considered that when ex-factory benchmark prices are used, an adjustment must be made to include the transportation costs generally applicable in the country of origin.³⁶ This adjustment, however, suggests that the adjustments required to be made under Article 14(d) of the SCM Agreement are similar to those contemplated under Article 2.4 of the AD Agreement. To the extent that the adjustments under Article 14(d) do not require consideration of government-caused price distortions, the adjustments required under Article 2.2 of the AD Agreement are fundamentally different as they may well become predominantly focused on price distortions associated with government intervention given the existing antidumping practices of WTO members.

In *US – Countervailing Measures (China)*, the Appellate Body further clarified that price distortions resulting from state influence are the key to determine whether benchmark prices should be used under Article 14(d) of the SCM Agreement.³⁷ While the Appellate Body did not touch upon adjustments of benchmark prices, its rulings,

³³ Appellate Body Report, *United States – Countervailing Measures on Certain Hot-Rolled Carbon Steel Flat Products from India*, WT/DS436/AB/R, adopted 19 December 2014, para. 4.150.

³⁴ *Ibid.*, para. 4.151.

³⁵ *Ibid.*, para. 4.211.

³⁶ *Ibid.*, paras. 4.246-249.

³⁷ Appellate Body Report, *United States – Countervailing Duty Measures on Certain Products from China*, WT/DS437/AB/R, adopted 16 January 2015, paras. 4.39-4.107.

read together with its decisions in *EU – Biodiesel*, confirmed that state intervention and resultant price distortions are matters to be considered under the SCM Agreement, whereas the central issue under the AD agreement should be business practices, particularly pricing behaviours of producers or exporters, that result in price differentiation between domestic and foreign markets.

(3). Article 2.4

A final major issue in *EU – Biodiesel* concerned Argentina's contention that the EU authorities had failed to make due allowance for the difference between the CNV and the export price in accordance with Article 2.4 of the AD Agreement. Fair comparison between the two prices cannot be achieved unless an adjustment was made to the difference arising from the use of different cost bases in the determination of the CNV (based on the benchmark price) and the export price (based on the actual production cost).

The panel rejected the contention on the grounds that (1) Article 2.4 concerns “*differences in characteristics of the compared transactions* that have an impact, or are likely to have an impact, on the prices involved in the transaction”, and does not require adjustment of differences resulted from the *methodology* employed in the calculation of export price and normal value;³⁸ and (2) the alleged difference arose exclusively from the methodology used by the EU authorities to construct a normal value based on surrogate prices and hence did not affect the price comparability of the two prices.³⁹

The Appellate Body overruled the panel's finding that there is a “*general proposition* that differences arising from the methodology applied for establishing the normal value cannot, in principle, be challenged under Article 2.4 as ‘differences affecting price comparability’”, and held that

... The Appellate Body report in *EC – Fasteners (China) (Article 21.5 – China)* does not contain any such “general proposition”. The reasoning in that report is tailored to the circumstances of that dispute, in which the analogue country methodology was used. The Appellate Body explained that Article 2.4 of the Anti-Dumping Agreement had to be read in the context of the second *Ad Note* to Article VI:1 of the GATT 1994 and Section 15(a) of China's Accession Protocol. Neither of those provisions is relevant for purposes of this dispute. Moreover, we would have serious reservations regarding what the Panel referred to as the “general proposition”. The text of Article 2.4 itself makes clear that “[d]ue allowance shall be made *in each case, on its merits*”. This indicates that the need to make due allowance must be assessed in light of the specific circumstances of each case.⁴⁰

However, given the Appellate Body's findings under Articles 2.2.1.1 and 2.2, it found it unnecessary to determine “whether the EU authorities also failed to conduct a “fair comparison” in comparing the constructed normal value to the export price.”⁴¹

³⁸ Panel Report, *EU – Biodiesel*, paras. 7.294-296.

³⁹ Panel Report, *EU – Biodiesel*, paras. 7.299-302.

⁴⁰ Appellate Body Report, *EU – Biodiesel*, para. 6.87.

⁴¹ Appellate Body Report, *EU – Biodiesel*, para. 6.89.

The author has argued elsewhere that the panel's distinction between 'methodology-resulted' differences and 'transaction-resulted' differences is unjustified as Article 2.4 concerns *whether* the comparability of export price and normal value has been affected by an alleged difference, not how or in what circumstances the difference arises.⁴² The difference at issue, which was equivalent to the export tax, did affect the comparability between the CNV and the export price and hence should be adjusted to ensure fair comparison. An adjustment of the difference is required to avoid the inflations of dumping margins that eventuated in *EU – Biodiesel*.

The panel also misinterpreted the Appellate Body's rulings in *EC – Fasteners (China)* (Article 21.5 – China) which concerned the EU's application of the NME methodology against China and use of surrogate costs in calculating a CNV. On the issue whether the EU was required to make due allowances for cost differences alleged by China, the Appellate Body ruled in that case:

Article 2.4 of the Anti-Dumping Agreement has to be read in the context of the second Ad Note to Article VI:1 of the GATT 1994 and Section 15(a) of China's Accession Protocol. We recall that the rationale for determining normal value on the basis of [the surrogate prices] was that the Chinese producers had not clearly shown that market economy conditions prevail in the fasteners industry in China. [footnote omitted] Costs and prices in the Chinese fasteners industry thus cannot, in this case, serve as reliable benchmarks to determine normal value. In our view, the investigating authority is not required to adjust for differences in costs between the NME producers under investigation and the analogue country producer where this would lead the investigating authority to adjust back to the costs in the Chinese industry that were found to be distorted.⁴³ (emphasis added)

In *EU – Biodiesel*, the Appellate Body clarified that the previous ruling applies only to the circumstances where the AD Agreement or other WTO instruments such as Accession Protocols explicitly allow the replacement of distorted costs with benchmark prices for the construction of normal value on the sole basis of state intervention and price distortion. In such circumstances, investigating authorities are not required to make adjustments to the cost differences arising from the distortion, because such an adjustment would result in reintroducing the distortion into the CNV.⁴⁴ However, in other circumstances where price distortions caused by government intervention are not explicitly regulated (e.g. Articles 2.2 and 2.2.1.1 of the AD Agreement), price differences arising from the use of undistorted surrogate costs would still be subject to adjustments under Article 2.4.

The Appellate Body did not explain, however, how the adjustments under Article 2.4 should operate with the adjustments required under Article 2.2 to ensure benchmark costs reflect the market conditions prevailing in the country of origin. Apparently,

⁴² Weihuan Zhou and Andrew Percival, "Panel Report on *EU – Biodiesel*: A Glass Half Full? – Implications for the Rising Issue of 'Particular Market Situation' " (2016)2(2) *Chinese Journal of Global Governance* 142-163 at 154-155.

⁴³ Appellate Body Report, *European Communities—Definitive Anti-Dumping Measures on Certain Iron or Steel Fasteners from China (Recourse to Article 21.5 of the DSU by China)*, WT/DS397/AB/RW, adopted on 12 February 2016, para. 5.207.

⁴⁴ Appellate Body Report, *EU – Biodiesel*, FN 270.

when a price difference is related to a price distortion caused by government, the adjustment required under Articles 2.2 and 2.4 would deal with the same difference. In *EU – Biodiesel*, the difference is essentially the export tax which was factored into the export price but not the CNV. The Appellate Body seems to have deliberately exercised judicial economy on whether the EU authorities failed to make adjustments under Article 2.4 to allow some time for it to consider this overlapping issue. However, the Appellate Body observed that

“[t]he manner in which the normal value is calculated pursuant to Article 2.2 of the Anti-Dumping Agreement may inform the types of adjustments required under Article 2.4. This, however, does not mean that any adjustment envisaged under Article 2.4 – in particular adjustments for taxation – may instead be taken into account in determining the normal value pursuant to Article 2.2.”⁴⁵

This observation, reading together with the Appellate Body's rulings under Article 2.2, suggests that if a distortion-caused difference is adjusted under Article 2.2, the same adjustment will not be required under Article 2.4. However, allowing such adjustment to be made under Article 2.2 would not render Article 2.4 superfluous as price difference arising from other factors will still be adjusted under Article 2.4. Despite the uncertainty over the overlapping issue, the Appellate Body's rulings under Article 2.4 are consistent with its rulings under Articles 2.2 and 2.2.1.1, seeking to use adjustments to prevent abuse of benchmark production costs and to offset inflations of dumping margins.

3 Recent Developments in Australia, the US, and the EU

3.1 Australia

The author has discussed Australia's approach to the use of PMS and surrogate production costs in previous publications.⁴⁶ To avoid unnecessary repetition, it would suffice to note that Australia has consistently treated China as having a PMS in antidumping investigations based on evidence such as China's industrial development policies, provision of subsidies to industries, and trade measures, and consequently resorted to CNVs for the calculation of dumping margins. In this regard, section 269TAC(2)(a)(ii) of the *Customs Act 1901* – the principal Australian antidumping legislation – allows the use of CNV when “the situation in the market of the country of export is such that sales in that market are not *suitable* for use in determining [normal value].” (emphasis added) This “suitability” test differs from the test contemplated in Article 2.2 of the AD Agreement which concerns whether a market situation would preclude a proper comparison between export price and normal value. On its face, it may not constitute an “as such” violation as it provides Australian authorities the discretion to apply the test under Article 2.2 of the AD

⁴⁵ Appellate Body Report, *EU – Biodiesel*, para. 6.48.

⁴⁶ See, e.g. Weihuan Zhou, “Australia's Anti-Dumping and Countervailing Law and Practice: An Analysis of Current Issues Incompatible with Free Trade with China” (2015)49(6) *Journal of World Trade* 975-1010.

Agreement. However, the “suitability” test has been consistently applied to condemn price distortions caused by state intervention. This consistent practice, which is recognised in Australia’s Antidumping Commission (ADC)’s Dumping and Subsidy Manual⁴⁷, strongly suggests that the Australian law and practice in determining whether a PMS exists and a CNV should be used may be in breach of Article 2.2 of the AD Agreement. Unfortunately, whether such claims would succeed remains dependent upon the WTO tribunals’ interpretation of the term PMS and the relevant context, which is currently lacking.

For the calculation of a CNV, Regulation 43 of the *Customs (International Obligations) Regulations 2015* allows Australian authorities to disregard exporters’ cost records which do not ... “reasonably reflect *competitive market costs* associated with the production or manufacture of like goods”. (emphasis added) Thus, the regulation adds a qualification to the Reasonableness Test by requiring the costs recorded by exporters to be “competitive market” prices. This qualification evidently amounts to a departure from Article 2.2.1.1 of the AD Agreement which, according to the WTO rulings in *EU—Biodiesel*, require the use of actual costs of production for the calculation of CNV and does not allow for consideration of whether such costs are competitive market prices as long as they are sufficiently and suitably recorded. In practice, Australian authorities have routinely resorted to surrogate prices to offset alleged Chinese government’s influence on the prices of raw materials and consequently to arrive at an inflated CNV. According to *EU—Biodiesel*, both the regulation and the practice are in violation of Articles 2.2.1.1 and 2.2 of the AD Agreement.

The most recent Australian antidumping investigation involving the issue of PMS and surrogate costs concerned A4 Copy Paper exported from Brazil, China, Indonesia and Thailand.⁴⁸ The applicant, Paper Australia Pty Ltd, argued that both China and Indonesia had a PMS as the domestic prices of A4 copy paper were artificially lowered by the governments.⁴⁹ Consequently, the applicant proposed CNVs for China and Indonesia using benchmark production costs.⁵⁰

In its final report, the ADC found that a PMS existed in Indonesia, and in constructing a normal value, that “the actual cost of pulp recorded by exporters in their records does not reasonably reflect a competitive market cost.”⁵¹ The ADC observed that

⁴⁷ Anti-Dumping Commission, Dumping and Subsidy Manual (November 2015), at 35, available at: www.adcommission.gov.au/accessadsystem/Documents/Dumping%20and%20Subsidy%20Manual%20-%20November%202015_20%20Nov%202015%20-%20final%20on%20website.pdf

⁴⁸ The public record of the investigation is available at: www.adcommission.gov.au/cases/Pages/CurrentCases/EPR-341.aspx

⁴⁹ The application is available at: www.adcommission.gov.au/cases/EPR%20301%20%20350/EPR%20341/001%20-%20APPLICATION%20A4%20Copy%20Paper%20-%20Public%20File.pdf, at 44-49.

⁵⁰ *Ibid.*, at 52-54.

⁵¹ The final report (REP341) is available at:

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... a market situation is primarily concerned with the effect on prices in the domestic market from government influence. On that basis the primary and most relevant comparison in assessing a market situation is a comparison of domestic prices with government influence and domestic prices without government influence.⁵²

The ADC identified a series of Indonesian government's policies and programs in the pulp and paper sector, and observed that while these measures served economic, social and environmental objectives, they provided "ongoing support for the Indonesian pulp industry".⁵³ Moreover, the ADC found that the export ban on Indonesian logs artificially lowered the cost of producing pulp.⁵⁴ The ADC compared Indonesian log and pulp prices with the prices in the Asian region and found that the former were lower than the benchmark prices.⁵⁵ Accordingly, the ADC concluded that the actual cost of pulp recorded by Indonesian exporters "does not reasonably reflect a competitive market cost".⁵⁶ In constructing a normal value, the ADC replaced the actual pulp cost with a benchmark "consisting of quarterly import pulp prices into China and Korea based on an average CIF price for bleached eucalyptus kraft wood originating from Brazil and South America."⁵⁷

The above represent the ADC's standard approach to PMS and the use of surrogate costs. This approach runs counter to the *EU – Biodiesel* decisions. In essence, the Australian approach relies on alleged government intervention and price distortions and a comparison between allegedly distorted prices and selected benchmark prices which are assumed to be undistorted. The WTO tribunals in *EU – Biodiesel* have explicitly disapproved of this approach to using benchmark costs for the construction of normal value. In A4 Copy Paper, the ADC received submissions on how its approach contradicted the panel and the Appellate Body reports on *EU – Biodiesel*.⁵⁸ In response to the submissions, the ADC completely ignored Australia's obligations to comply with WTO rules and insisted that its approach is supported by Australian laws and jurisprudence.⁵⁹

In relation to China, the ADC found, for the first time in recent years, that there was no PMS despite the Chinese government's influence in the pulp industry distorting the domestic pulp price.⁶⁰ Central to this finding were the facts that the Chinese paper industry predominantly relied on imported pulp and that the Chinese pulp price was typically higher than regional benchmarks. The latter is arguably the determinative factor; if the Chinese pulp price were lower than the benchmarks, then

www.adcommission.gov.au/cases/EPR%20301%20%20350/EPR%20341/221%20-%20Report%20-%20Final%20Report%20-%20REP%20341.pdf, at 50-51.

⁵² Ibid., at 167.

⁵³ Ibid., at 168.

⁵⁴ Ibid., at 170-172.

⁵⁵ Ibid., at 173-174.

⁵⁶ Ibid., at 230.

⁵⁷ Ibid., at 230.

⁵⁸ For example, see submissions by Sinar Mas Group available at:

www.adcommission.gov.au/cases/EPR%20301%20%20350/EPR%20341/146%20-%20Submission%20-%20Exporter%20-%20Sinar%20Mas%20Group.pdf

⁵⁹ The final report (REP341), at 60-61.

⁶⁰ The final report (REP341), at 153.

given the ADC's findings on Indonesia, it is conceivable that the ADC will make the same findings and adopt the same approach to the construction of normal value. This confirms that the Australian authorities rely heavily on benchmarks in determining whether a PMS exists and surrogate prices should be employed.

The Australian approach creates many WTO-consistency issues, including:

1. a lack of positive evidence and objective assessment on whether any alleged government influence in upstream markets (e.g. the raw materials markets) has actually affected or flowed through to the domestic price of final goods under investigation (Article 2.2);
2. a lack of positive evidence and objective assessment on whether the above government influence has precluded a proper comparison between export price and normal value due to any asymmetric impact on the two prices (Article 2.2);
3. the use of surrogate costs on the sole basis that producers' costs are lower than selected benchmark prices and do not represent competitive market prices (Article 2.2.1.1);
4. no adjustments to benchmark prices to ensure surrogate costs reflect the prevailing market conditions in the country of exportation (Article 2.2); and
5. because of issue 4 above, no adjustment to CNV to ensure a fair comparison between export price determined based on distorted production cost and CNV calculated based on benchmark costs (Article 2.4).

3.2 The US

The US Department of Commerce (USDOC) has primarily relied on the NME methodology permitted under China's WTO Accession Protocol to resort to CNV and surrogate prices. In dealing with exports from other countries, the primary basis for the use of CNV has been "outside the ordinary course of trade".⁶¹ As a result, the term PMS has been rarely invoked. In anticipation of the expiry of the NME methodology in December 2016, the US amended its antidumping laws, through the *Trade Preferences Extension Act of 2015*, by (1) expanding the scope of "outside the ordinary course of trade" to cover "situations in which the administrative authority determines that the particular market situation prevents a proper comparison with the export price or constructed export price", and (2) expanding the application of PMS to the use of surrogate costs when "the cost of materials and fabrication or other processing of any kind does not accurately reflect the cost of production in the ordinary course of trade."⁶² While the first change appears to be consistent with the wording in Article 2.2 of the AD Agreement, the second change creates the flexibility for consideration of price distortions associated with state intervention in

⁶¹ See Matthew R. Nicely and Brian Gatta, "U.S. Trade Preferences Extension Act (TPEA) of 2015 Could Lead to Increased Use of "Particular Market Situation" in Calculating Normal Value in Anti-Dumping Cases" (2016)11(5) *Global Trade and Customs Journal* 238-243.

⁶² *Ibid.*, at 243.

determining whether surrogate costs should be used and hence the possibility of violating Article 2.2.1.1 of the AD Agreement.

The term PMS was recently applied in the USDOC's Administrative Review of Certain Oil Country Tubular Goods (OCTG) from South Korea.⁶³ In its final determinations released on 17 April 2017, the USDOC was satisfied that "record evidence supports a finding that a particular market situation exists in Korea which distorts the OCTG costs of production."⁶⁴ This finding was based on consideration of four factors collectively, including:⁶⁵

1. Korean imports of hot rolled coil (HRC) – a major raw material for the production of OCTG – from China. Due to the overcapacity in Chinese steel production, the significant imports of Chinese HRC at artificially lowered prices, combined with the Korean subsidisation of steel products, distorted the HRC prices in Korea;
2. Strategic alliances between certain Korean HRC producers and Korean OCTG producers which *may* have impacted "HRC pricing in a distortive manner";
3. Korean HRC subsidies; and
4. Electricity market distortions. The USDOC observed that a PMS "may exist where there is government control over prices to such an extent that home market prices cannot be considered to be competitively set."

The USDOC concluded that "[t]hese intertwined market conditions signify that the production costs of OCTG, especially the acquisition prices of HRC, are distorted, and, thus, demonstrates that the costs of HRC to Korean OCTG producers are not in the ordinary course of trade."⁶⁶ Based on these findings, the USDOC imposed an uplift on the HRC costs recorded by the Korean exporters by the amount of the subsidies received by HRC producers and suppliers.⁶⁷

The USDOC's approach to PMS above is slightly different from that of the ADC as it did not explicitly resort to a benchmark. In effect, however, both the USDOC and the ADC treated government intervention as being sufficient to create a PMS and the resultant price distortions as being sufficient to employ surrogate costs. Both the US and Australian authorities are comfortable of making the (unjustified) assumptions that input price distortions would lead to price distortions of final goods and hence preclude a proper comparison between export price and normal value.⁶⁸ Using state intervention and price distortions as the basis to employ surrogate production costs,

⁶³ A summary of the final determinations is available at: www.gpo.gov/fdsys/pkg/FR-2017-04-17/pdf/2017-07684.pdf; Detailed issues and decision memorandum for the decision can be found at: enforcement.trade.gov/frn/summary/korea-south/2017-07684-1.pdf

⁶⁴ Ibid., Issues and Decision Memorandum, at 40.

⁶⁵ Ibid., Issues and Decision Memorandum, at 40-41.

⁶⁶ Ibid., Issues and Decision Memorandum, at 41.

⁶⁷ Ibid., Issues and Decision Memorandum, at 42.

⁶⁸ Ibid., Issues and Decision Memorandum, at 43. The USDOC observed that "where a particular market situation affects the cost of production for the foreign like product, such as through distortions in the cost of inputs, for example, it is reasonable to conclude that such a situation may prevent a proper comparison with the export price or constructed value."

both authorities have acted inconsistently with Article 2.2.1.1 of the AD Agreement. Neither of the authorities considered it necessary to make adjustments to the surrogate costs to ensure the costs reflect the market conditions prevailing in the country of origin, amounting to a breach of Article 2.2 of the AD Agreement. While the Australian approach has been consistently applied for almost a decade, it remains to be seen how the US approach will develop in future investigations.

3.3 The EU

Like the USDOC, the EU authorities have primarily relied on the NME methodology and “no sales in the ordinary course of trade” in deciding to employ the constructed method and surrogate costs.⁶⁹ However, the EU authorities also had experience of replacing actual producers' costs with surrogate costs based on findings of PMS, as seen in *EU – Biodiesel*. While the relevant EU regulation was found to be not WTO-unlawful “as such”, the application of the regulation in practice has been squarely condemned by the WTO tribunals in *EU – Biodiesel*. Like the US, the EU has also been revising its antidumping laws, seeking to create an approach that mirrors the NME methodology. It has been proposed that under the new approach, the NME list will be replaced by a country-neutral methodology which is primarily aimed at addressing market distortions caused by state intervention.⁷⁰ The main section of the proposal is set out below:

There are circumstances however in which the domestic prices and costs would not provide a reasonable basis to determine the normal value. This could be the case, for instance, when prices or costs are not the result of free market forces because they are affected by government intervention. Relevant considerations in this respect include, for instance, the fact that the market in question is to a significant extent served by enterprises which operate under the ownership, control or policy supervision or guidance of the authorities of the exporting country; the state presence in firms allowing the state to interfere with respect to prices or costs; the existence of public policies or measures discriminating in favour of domestic suppliers or otherwise influencing free market forces; and the access to finance granted by institutions implementing public policy objectives.

In such circumstances, it would be inappropriate to use domestic prices and costs to determine the value at which the like product should be normally sold (“the normal value”) and a new provision (Article 2(6)a) stipulates that the normal value would instead be constructed on the basis of costs of production and sale reflecting undistorted prices or benchmarks. For this purpose, the sources that may be used would include undistorted international prices, costs, or benchmarks, or corresponding costs of production and sale in an appropriate representative country with a similar level of economic development as the exporting country.

⁶⁹ Stéphanie Noël and Weihuan Zhou, “Replacing the Non-Market Economy Methodology: Is the European Union’s Alternative Approach Justified Under the World Trade Organization Anti-Dumping Agreement?” (2016)11(11/12) *Global Trade and Customs Journal* 559-567 at 563.

⁷⁰ European Commission, “Commission Proposes Changes to the EU’s Anti-Dumping and Anti-Subsidy Legislation”, Press Release (9 November 2016), available at: europa.eu/rapid/press-release_IP-16-3604_en.htm

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This methodology would allow the Commission to establish and measure the actual magnitude of dumping being practised in normal market conditions absent distortions.⁷¹

In the latest press release of the European Council, it was confirmed that “[w]hen a significant distortion is recognised in an exporting country”, the new methodology would allow the Commission to “set a price for the product by referring either to the costs of production and sale prices in a country with similar levels of economic development or to appropriate undistorted international costs and prices”.⁷² It is intended that the new methodology would lead to the same level of anti-dumping duties as the EU had been able to impose through the NME methodology.⁷³

The EU's new antidumping methodology is still under negotiations with the European Parliament; hence it remains unclear what its final form would be and how it will be implemented in practice. In its current form, it is hard to imagine how the new methodology could be reconciled with the Appellate Body's rulings in *EU – Biodiesel*. Arguably, the wording of the new methodology and the outcomes that it is intended to achieve demonstrate a more overt breach of the WTO rules than the US and Australian laws. That is, the new methodology allows the use of surrogate costs on the sole basis of state intervention and price distortions for the purpose of offsetting the distortions, thereby amounting to the use of production costs which do not reflect the market conditions prevailing in the country of exportation for the construction of normal value. An application of the new methodology by EU authorities in antidumping investigations would constitute an “as applied” violation of Articles 2.2.1.1 and 2.2 of the AD Agreement. Whether an “as such” breach could be established will depend on the exact wording of the EU law which incorporates the new methodology.

4 Conclusion

This paper has analyzed the Appellate Body's rulings in *EU – Biodiesel* in detail and the latest development of antidumping laws and practice in Australia, the US, and the EU. The paper has argued that the *EU – Biodiesel* rulings have the following implications:

1. state intervention and resultant price distortions do not constitute sufficient ground for the use of surrogate/benchmark production cost for the construction

⁷¹ European Commission, “Proposal for a Regulation of the European Parliament and of the Council amending Regulation (EU) 2016/1036 on protection against dumped imports from countries not members of the European Union and Regulation (EU) 2016/1037 on protection against subsidised imports from countries not members of the European Union”, 9 November 2016, available at: eur-lex.europa.eu/procedure/EN/2016_351

⁷² See European Council, “Anti-Dumping Methodology: Council Agrees Negotiating Position”, Press Release (3 May 2017), available at: www.consilium.europa.eu/en/press/press-releases/2017/05/03-anti-dumping/

⁷³ See European Commission, “Joint Press Conference by Jyrki Katainen, Vice-President of the EC, and Cecilia Malmström, Member of the EC, on the Treatment of China in Anti-Dumping Investigations”, 20 July 2016, available at: ec.europa.eu/avservices/video/player.cfm?ref=I124960

of normal value. The Reasonableness Test under Article 2.2.1.1 of the AD Agreement concerns whether the cost records of producers or exporters suitably and sufficiently reflect the actual costs incurred by the producers or exporters in the production of the subject goods, and does not allow for consideration of whether the costs reflect competitive market prices;

2. the terms “suitably” and “sufficiently” leave no room for consideration of price distortions caused by state intervention. They concern business activities including whether production costs are reasonably and accurately allocated to the subject goods or whether the terms and conditions for the sale of the inputs at issue are compatible with normal commercial practice for such sales in the market in question;
3. the production costs used for the construction of normal value must reflect the market conditions prevailing in the country of exportation. Such market conditions include government policies and regulations that directly or indirectly affect prices. Therefore, if benchmark prices are employed to counteract price distortions, adjustments to the benchmarks must be made to reintroduce the distortions into the production costs; and
4. if the adjustments contemplated under point 3 are not made, then adjustments of the difference between the CNV and the export price which are established using different cost bases (i.e. undistorted vs. distorted) must be made under Article 2.4 to ensure fair comparison between the two prices.

Reading together with the WTO jurisprudence under Article 14(d) of the SCM Agreement, it has also been argued that state intervention and price distortions would better be dealt with under the SCM Agreement and the GATT 1994, leaving the AD Agreement to focus on business practices, particularly pricing behaviours of producers or exporters, that result in price differentiation between domestic and foreign markets.

While the *EU – Biodiesel* rulings do not offer further clarifications on the meaning and application of the term PMS, they apply to the use of PMS on the basis of state intervention and price distortions as a pathway to the use of surrogate costs and ultimately to inflating dumping margins. This pathway is unequivocally closed by the Appellate Body in *EU – Biodiesel*. Furthermore, in light of the *EU – Biodiesel* rulings, the antidumping laws and practice in Australia, the US and the EU (i.e. the new methodology) may well contravene Articles 2.2.1.1 and 2.2 of the AD Agreement.

The paper is still a work-in-progress and has not discussed the more general issues in relation to why state intervention should not be dealt with under the AD Agreement and how state intervention should be dealt with under the other WTO agreements.