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**PANEL REPORT ON EU—BIODIESEL: A
GLASS HALF FULL?—IMPLICATIONS FOR
THE RISING ISSUE OF “PARTICULAR MARKET
SITUATION”**

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Panel Report on *EU—Biodiesel*: A Glass Half Full?—Implications for the Rising Issue of “Particular Market Situation”

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Abstract

This article provides a detailed analysis of the World Trade Organisation (“WTO”) panel report on the *EU—Biodiesel* dispute which represents the latest development of the WTO jurisprudence on anti-dumping. The panel’s decision has significant implications for the rising use of Particular Market Situation (“PMS”) by traditional users of anti-dumping (such as Australia) against economies like China in anti-dumping investigations. The panel correctly established that a finding of PMS does not provide a sufficient ground for the use of surrogate costs in the determination of constructed normal value (“CNV”) and that the use of that methodology would result in the imposition of anti-dumping duties in excess of dumping margins that should have been established consistently with the WTO Anti-Dumping Agreement, that is, by using actual costs recorded by exporters under investigation. It is argued that both Australia’s anti-dumping laws which essentially authorise the use of surrogate costs in the construction of normal value solely based on a finding of PMS and Australia’s use of that methodology in practice are contrary to WTO rules. The panel’s decision, therefore, is a positive step toward the resolution of the issues related to PMS by imposing constraints on the use of a protectionist methodology in determining CNV so as to prevent unjustified inflation of dumping margins and anti-dumping duties.

Keywords

WTO – anti-dumping – Particular Market Situation – surrogate prices/costs – China – Australia

1 Introduction

On 29 March 2016, the WTO panel on the *European Union—Anti-Dumping Measures on Biodiesel from Argentina* (“EU—Biodiesel”) dispute issued its report.¹ The report addressed some of the most controversial and persisting issues under the laws of the World Trade Organisation (“WTO”) on anti-dumping and in global anti-dumping practice, and by doing so, has developed the WTO jurisprudence on anti-dumping in significant ways. These issues include: when the anti-dumping investigating authority of an importing country decides to determine the normal value (“NV”) of the exported goods under investigation on the basis of a constructed method,

- (1) whether the authority is allowed to replace the actual input costs incurred by exporters with a benchmark/representative input cost in the calculation of the constructed normal value (“CNV”), on the ground that the actual input costs are distorted or artificially lowered;
- (2) if a benchmark/representative input cost is employed, whether the authority is required to make due allowance for the difference, resulting from the use of the benchmark/representative cost, between the export price (“EP”) and the CNV, so as to ensure ‘fair comparison’ between the two prices;
- (3) whether the use of a benchmark/representative input cost in the calculation of a CNV would result in the imposition of anti-dumping duties in excess of the dumping margins that should have been established in accordance with the WTO Agreement on Anti-Dumping (“AD Agreement”)?

Anti-dumping is one of the few protectionist measures permitted under WTO rules for member states to counteract the injurious effects of dumping, typically through the imposition of customs duties on subject imports. For a

¹ Panel Report, *European Union—Anti-Dumping Measures on Biodiesel from Argentina*, WT/DS473/R, circulated on 29 March 2016. (hereinafter “EU—Biodiesel”). The panel’s decision has been appealed and is currently being considered by the Appellate Body.

finding of dumping, an investigating authority must be satisfied that the EP of the subject goods is lower than the NV of the goods. Accordingly, the calculation of NV is essential to the determination of whether dumping has occurred, and if it has, the magnitude of dumping margin and ultimately the anti-dumping duties to be imposed.

The WTO judicial responses to the questions above in *EU—Biodiesel* are a positive step toward the resolution of the long-standing disputes between traditional users of anti-dumping measures (such as the US, the EU, Australia) and leading targets of these measures (particularly China) over the use of surrogate prices in determining NV by treating China or economies like China as a non-market economy (“NME”). Upon its accession to the WTO, China agreed that by 11 December 2016 members of the WTO may treat it as a NME in anti-dumping investigations (known as “NME Assumption”) and hence use surrogate prices or costs for the Chinese industry concerned to determine NV unless the Chinese firms can establish that they operate in a competitive market.² As the NME Assumption is to expire at the end of 2016,³ frequent users of the assumption are likely to resort to alternative means to calculate NV using surrogate costs that have the effect of continuing to treat China or economies like China as a NME. One of such means is to rely on a finding of Particular Market Situation (“PMS”) by virtue of Article 2.2 of the AD Agreement which provides:

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

2 See *Protocol on the Accession of the People's Republic of China*, WT/L/432 (23 November 2001), para. 15. For a good summary of the issues relating to the treatment of China as a NME in antidumping investigations, see Laura Puccio, “Granting Market Economy Status to China: An Analysis of WTO Law and of Selected WTO Members’ Policy”, European Parliamentary Research Service, November 2015.

3 It however remains controversial as to whether an importing member is to be prohibited from using surrogate prices in determining normal value of Chinese exports after the expiration of the NME Assumption. See, for example, Miranda, J., “Interpreting Paragraph 15 of China’s Protocol of Accession” (2014)9(3) *Global Trade and Customs Journal* 94–103; Stewart, T.P., Fennell, W.A, Bell, S.M. and Birch, N.J., “The Special Case of China: Why the Use of a Special Methodology Remains Applicable to China after 2016” (2014)9(6) *Global Trade and Customs Journal* 272–279; Weijia Rao, “China’s Market Economy Status under WTO Antidumping Law after 2016” (2013)5(2) *Tsinghua China Law Review* 151–168.

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. (emphasis added)

Under the AD Agreement, a NV generally should be established by reference to the actual selling price of subject goods in the market of exporting countries. However, a finding that a PMS exists allows investigating authorities to disregard the domestic selling prices of subject goods and determine a NV based on the selling price of 'like' goods in a third country (i.e. a surrogate price) or on a constructed method by adding up the cost of production, other costs associated with the sale of the goods in the domestic market, and the profit on the domestic sale (i.e. a CNV). In practice, Australia has been the most frequent user of this alternative means to treat China as a NME and has consistently used surrogate/benchmark prices for inputs to manufacture in calculating a CNV. The result of this approach has been an inflation of the input costs, thereby inflating the CNV, the dumping margin and ultimately the anti-dumping duties that are imposed.⁴ However, it must be noted that unlike the NME Assumption, PMS may be invoked by all WTO members. Accordingly, the abuse of PMS by one country may ignite *tit-for-tat* anti-dumping actions based on findings of PMS and the use of surrogate prices by other countries.

In *EU—Biodiesel*, the panel ruled that the use of surrogate input costs, on the ground that the costs actually incurred by exporters are distorted or artificially lowered, in the calculation of a CNV is unlawful under the AD Agreement. Rather, a CNV must be determined based on the cost associated with the production and sale of the subject goods in the exporting country in accordance with Article 2.2.1.1 of the AD Agreement which provides in the relevant part:

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.

The panel further found that the construction of NV based on surrogate input costs would likely lead to inflation of dumping margins and hence the

4 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 at 980–991.

application of anti-dumping duties in excess of dumping margins that should have been established consistently with the AD Agreement based on the actual input cost of target exporters. However, the panel rejected the proposition that investigating authorities are required to make due allowance for the difference between EP and CNV resulted from the use of surrogate costs under Article 2.4 of the AD Agreement which reads:

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.* (emphasis added)

This article offers a detailed analysis of the panel's rulings above in *EU—Biodiesel* and their implications. Section 2 provides an overview of the panel's findings and discusses the strengths and weaknesses of the rulings. It argues that the panel has erred in finding that (1) the EU regulation authorising the use of surrogate costs based on a finding of PMS is not "as such" in violation of the AD Agreement, and (2) an adjustment of the difference between EP and CNV resulted from the use of surrogate costs is not required to ensure 'fair comparison'. Section 3 analyses the implications of the panel's rulings for the rising issue of PMS in general and for Australia's use of PMS against China in particular. It argues the relevant Australian laws and Australia's applications of the laws in anti-dumping investigations have violated the AD Agreement. Section 4 concludes.

2 Panel's Rulings: A Glass Half Full?

The *EU—Biodiesel* dispute arose out of the European Union's ("EU") anti-dumping investigation into biodiesel exported from Argentina and Indonesia.⁵ While the EU authorities found dumping margins between 6.8% and 10.6% in provisional determinations against Argentina's exports of the subject goods,

5 The description of the facts is based on above n. 1, Panel Report, *EU—Biodiesel*, paras. 2.2–2.3, 7.179–7.184.

their final findings increased the margins to a range from 41.9% to 49.2%. The significant increase in the dumping margins was a result of the use of surrogate costs of soybeans and soybean oil, the main raw materials used in the production of biodiesel, in the calculation of a CNV. A CNV was employed because the EU authorities found domestic sales of biodiesel in Argentina were not made in the ordinary course of trade due to government intervention. In calculating a CNV, the authorities relied on the production costs recorded by the Argentinean producers under investigation in the provisional determinations, whereas in the final determinations they found that the domestic prices of soybeans and soybean oil were artificially lowered due to Argentina's imposition of export taxes on the raw materials. This resulted in the domestic prices lower than international prices. Consequently, the domestic input prices were found to have not been reasonably reflected in the records kept by the Argentinean producers and were replaced with the average reference prices of the raw materials published by the Argentine Ministry of Agriculture. According to the EU authorities, the Argentine export tax system created a PMS in the raw materials market so that the actual costs incurred by the Argentinean producers were distorted and artificially low and, therefore must be disregarded in the calculation of CNV. Before the panel, Argentina claimed that both the EU regulations authorising the use of surrogate input costs (i.e. "as such" claims) and the EU's application of the regulations in this investigation (i.e. "as applied" claims) were in breach of the AD Agreement.

2.1 *"As such" Claims*

With respect to the "as such" claims, the EU regulation at issue allows the investigating authorities to find the existence of a PMS "when prices are artificially low" (amongst the other defined circumstances), and then to establish NV by a constructed method. Article 2(5) of the regulation sets out how costs should be determined in the construction of NV as follows:

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.⁶

As the first paragraph of Article 2(5) is essentially the same as Article 2.2.1.1 of the AD Agreement, Argentina's challenge targeted the second paragraph only. It contended that this paragraph allows the EU authorities to use costs from markets other than the exporting country "when the prices of the raw materials included in the records of the exporters are considered as being abnormally or artificially low because the market is regulated or because of some alleged distortion".⁷ In making the contention, Argentina relied on evidence relating to "the text of this provision, its legislative history, its consistent application by the EU authorities, and judgments of the General Court of the European Union".⁸

The panel rejected Argentina's "as such" claims essentially on the grounds that the second paragraph of Article 2(5) does not *require* the EU authorities to (1) use costs in representative markets but merely provides the authorities several options for determining production costs, or (2) "conclude that the records do not "reasonably reflect" costs where prices are artificially low, but merely . . . enables them to do so".⁹ As far as the EU's practice is concerned, while the panel accepted, based on Argentina's evidence, that there have been a series of investigations where the authorities disregarded costs in the exporting markets as they were artificially low, the panel was not convinced that the authorities are *mandated* to do so in every case.¹⁰ In addition, in holding that the second paragraph of Article 2(5) was not contrary to the AD Agreement, the panel relied heavily on the observation that determinations as to whether production costs are "reasonably reflected" in the producer's records are made under the first paragraph of Article 2(5) not the second paragraph which comes into play only after the determinations under the first paragraph have been made.¹¹ That is, the second paragraph does not require the EU authorities "to determine that a producer's records do not reasonably reflect the costs associated with the production and sale of the product under consideration when these records reflect prices that are considered to be artificially

6 See above n. 1, Panel Report, *EU—Biodiesel*, paras. 7.72–7.73.

7 See above n. 1, Panel Report, *EU—Biodiesel*, para. 7.74.

8 See above n. 1, Panel Report, *EU—Biodiesel*, paras. 7.76–7.80.

9 See above n. 1, Panel Report, *EU—Biodiesel*, paras. 7.128–7.144.

10 See above n. 1, Panel Report, *EU—Biodiesel*, para. 7.147.

11 See above n. 1, Panel Report, *EU—Biodiesel*, paras. 7.132, 7.144, 7.148, 7.150, 7.152.

or abnormally low as a result of a distortion.”¹² Nor does this paragraph require the authorities to use costs in another country as it merely offers a number of options for the determination of production costs.¹³ Thus, Argentina failed to establish that the second paragraph will necessarily lead to violations of the relevant WTO rules as it can be applied in a WTO-consistent manner.¹⁴

The panel’s rulings above in favour of the EU had much to do with the ‘mandatory/discretionary distinction’ under the WTO jurisprudence. In essence, the distinction concerns whether a member’s measure mandates WTO-inconsistent acts (so that the measure is “as such” in breach) 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).¹⁵ In determining whether a measure is mandatory or discretionary, WTO panels must examine evidence at hand as a whole including whether the measure has been consistently applied in a manner contrary to WTO rules.¹⁶ Thus, the *EU—Biodiesel* panel adopted the correct approach in determining whether the EU regulation had set forth a mandatory rule on the use of surrogate costs in the construction of NV.

However, the panel’s reasoning is questionable. While it is true that the second paragraph of Article 2(5) of the EU regulation provides the authorities with the discretion to choose a way to determine production costs, it explicitly allows the establishment of such costs in a way inconsistent with the AD Agreement. The relevant provisions of the regulation, reading together, clearly authorises the authorities to disregard producers’ costs in the exporting country if the costs are found to be distorted due to the existence of a PMS and then to use surrogate costs including “information from other representative markets”. This is supported by Argentina’s evidence showing that the EU authorities had consistently resorted to such an approach to establish production costs in many cases. However, it must be noted that while Article 2.2 of the AD Agreement allows authorities to calculate a CNV in the presence of a PMS, it does not, nor does Article 2.2.1.1 of the agreement, allow the use of surrogate costs based on a finding of PMS. As the panel correctly

12 See above n. 1, Panel Report, *EU—Biodiesel*, para. 7.153.

13 See above n. 1, Panel Report, *EU—Biodiesel*, para. 7.169.

14 See above n. 1, Panel Report, *EU—Biodiesel*, paras. 7.173–174.

15 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.

16 Appellate Body Report, *United States—Sunset Review of Anti-Dumping Duties on Corrosion-Resistant Carbon Steel Flat Products from Japan*, WT/DS244/AB/R, adopted on 9 January 2004, paras. 97, 99.

found, Article 2.2.1.1 requires the use of actual costs incurred by producers under investigation as long as (1) the records are consistent with the generally accepted accounting principles (“GAAP”) of the exporting member (“GAAP Condition”) and (2) reasonably reflect the costs of production of the subject goods (“Reasonableness Condition”).¹⁷ Accordingly, PMS is not a valid ground for authorities to replace an exporter’s actual costs with surrogate costs. In this regard, as will be discussed below, the panel correctly rejected the proposition that the Reasonableness Condition provides room for consideration of whether the costs properly recorded by producers are reasonable; thus, a finding of distortion in the costs of production by itself does not justify a deviation from an exporter’s actual costs.¹⁸

In short, it is submitted that the panel has placed too much emphasis on the effect of each of the relevant provisions of the EU regulation and has overlooked their collective effect. Based on Argentina’s evidence, there is little doubt that the EU regulation allowed the use of surrogate costs based on a finding of PMS and that this approach to the determination of a CNV has become a general practice. To that extent, the EU regulation necessarily provides for a WTO violation and is “as such” WTO-inconsistent.¹⁹ The panel emphasized that the requirement of Article 2.2 of the AD Agreement is that a CNV must reflect “conditions prevailing in the country of origin”, and not that “sources of information other than producers’ costs in the country of origin” can never be used for the construction of NV.²⁰ While this is probably a sound observation as it gives consideration to the possibility of lack of domestic costs information, the “as such” violation in the EU regulation lies in the element which authorises the use of surrogate costs in the construction of NV as long as a PMS is found to exist. The panel’s failure to condemn this violation is likely to impact badly on the judicial efficiency of the WTO dispute settlement mechanism by inviting endless individual disputes on the same issue.

2.2 “As applied” Claims

On whether the EU’s use of surrogate costs for soybeans and soybean oil in constructing NV in the present investigation was in breach of Articles 2.2.1.1 and 2.2 of the AD Agreement, the panel sided with Argentina. The panel

17 See above n. 1, Panel Report, *EU—Biodiesel*, para. 7.131.

18 See above n. 1, Panel Report, *EU—Biodiesel*, para. 7.248.

19 See Nicolas Lockhart and Elizabeth Sheargold, “In search of Relevant Discretion: The Role of the Mandatory/Discretionary Distinction in WTO Law” (2010)13(2) *Journal of International Economic Law* 379–421 at 398–99.

20 See above n. 1, Panel Report, *EU—Biodiesel*, para. 7.171.

found that “Article 2.2.1.1 is concerned with the “reasonable reflect[ion]” of the costs that producers *actually* incur in the production of the product in question”.²¹ (original emphasis) It concluded as follows:

the ordinary meaning of the phrase “provided such records . . . reasonably reflect the costs associated with the production and sale of the product under consideration”, in its context, . . . concern[s] whether the costs set out in a producer/exporter’s records reflect all the actual costs incurred by the producer/exporter under investigation in—within acceptable limits—an accurate and reliable manner. This . . . calls for a comparison between . . . the costs as they are reported in the producer/exporter’s records and . . . the costs actually incurred by that producer. [footnote omitted] We emphasize, however, that 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. [footnote omitted]²² (original emphasis)

Thus, the EU’s finding that the raw materials prices were lower than international prices due to the distortion created by the Argentine export tax system “does not constitute a legally sufficient basis under Article 2.2.1.1 for concluding that the producers’ records do not reasonably reflect the costs associated with the production and sale of biodiesel”.²³ In addition, the EU’s use of the surrogate costs was found to be in breach of the requirement that a CNV be established by reference to “the cost of production in the country of origin” under Article 2.2 as the surrogate costs “were not those actually prevailing in Argentina, but rather, were those that would have prevailed in the absence of the alleged distortion.”²⁴

The panel’s rulings confirmed that the cost base for the construction of NV, as required under the AD Agreement, is the actual costs incurred by the exporters under investigation. The Reasonableness Condition is confined to an assessment of whether the records accurately and faithfully reflect the actual costs incurred and does not allow for consideration of the reasonableness of

21 See above n. 1, Panel Report, *EU—Biodiesel*, para. 7.232.

22 See above n. 1, Panel Report, *EU—Biodiesel*, para. 7.242.

23 See above n. 1, Panel Report, *EU—Biodiesel*, para. 7.248.

24 See above n. 1, Panel Report, *EU—Biodiesel*, paras. 7.258–60.

the costs themselves.²⁵ Besides the panel's sound reasoning, the rulings are justifiable for at least two other reasons.

First, it is next to impossible to determine what price is 'reasonable'. It seems to be a shared view that a price determined by market forces should be regarded as 'reasonable'. However, if price reasonableness relies on an undistorted and un-regulated market, one wonders whether such a market actually exists. 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. As Watson observed on the US treatment of China as a NME, "[m]any of the nonmarket aspects of China's economic policies that [the US Department of] Commerce points to are, in fact, common in other countries comfortably recognized as market economies."²⁶ Thus, those who insist that the Reasonableness Condition must involve an assessment of whether input costs are undistorted market-based prices must be prepared to explain why the surrogate costs employed are unaffected by any government influence. It would be insufficient to merely consider whether the alleged distortion affecting input costs of subject goods has affected the surrogate costs as the latter may well have been distorted by other types of government measures. In *EU—Biodiesel*, the only distortion identified by the EU authorities was Argentina's imposition of export tax on the raw materials. However, if the existence of such a single policy instrument can justify a finding of PMS and the use of surrogate prices, all WTO members may conveniently take the same approach in anti-dumping investigations. Further, in using the reference price published by the Argentine Ministry of Agriculture as the surrogate price, the EU did not seem to have considered whether the price was undistorted by other government measures or policies.²⁷ In the absence of such consideration, the authorities had assumed, arguably unjustifiably, that the reference price, which was determined by the Argentinean government, was undistorted. The mere fact that the reference price reflected the level of international price of the raw materials is not sufficient to prove that the price was unregulated or unaffected by government

25 See above n. 1, Panel Report, *EU—Biodiesel*, FN 400.

26 See William Watson, "Will Nonmarket Economy Methodology Go Quietly into the Night?: US Antidumping Policy toward China after 2016", Cato Institute Policy Analysis Number 763 (28 October 2014) at 8, available at: <http://object.cato.org/sites/cato.org/files/pubs/pdf/pa763.pdf>.

27 See Council Implementing Regulation (EU) No. 1194/2013 of 19 November 2013, imposing a definitive anti-dumping duty and collecting definitively the provisional duty imposed on imports of biodiesel originating in Argentina and Indonesia, OJ 2013 L 315, 26.11.2013, p. 5.

influence. By the same token, a domestic price of a good cannot be regarded as being distorted on the sole basis that it is lower or higher than the price of the good in the international market.

Second, an investigation of dumping is essentially a comparison of two prices, namely, the EP and the NV of the subject goods. 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 EP and the domestic selling prices of the goods to the same extent.²⁸ It follows that unless investigating authorities can establish that the distortion has only affected the domestic selling prices and not the EP, replacement of actual production costs with surrogate costs, which are typically higher, in the construction of a NV, while leaving the EP to be based on the distorted production costs, would serve only to inflate dumping margins and anti-dumping duties. To avoid such unjustified inflation, investigating authorities should not be allowed to inquire into the reasonableness of the actual costs of production so long as the costs are accurately recorded. Even though a distortion may be identified, a distortion affecting both the EP and domestic selling prices even-handedly would not affect the calculation of dumping margins and the amount of any anti-dumping duties that are subsequently imposed.

2.3 "Fair comparison" Claims

The difference between an EP (determined by reference to the allegedly distorted production costs) and a CNV (determined by reference to surrogate costs without the distortion), as contemplated above, became the ground for a separate claim by Argentina. As the EU authorities' determination of dumping margins was based on a comparison between the two prices calculated on the basis of different production costs, Argentina contended that the authorities had failed to make due allowance for the difference and to ensure 'fair comparison' in accordance with Article 2.4 of the AD Agreement.²⁹

28 The 'passing through' issue has been considered by the WTO tribunals in the context of assessing the application of countervailing duties to tackling "input subsidy" 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. For discussions of this issue, see, for example, 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; Sherzod Shadikhodjaev, "How to Pass a Pass-Through Test: the Case of Input Subsidies" (2012)₁₅(2) *Journal of International Economic Law* 621–646.

29 See above n. 1, Panel Report, *EU—Biodiesel*, paras. 7.277, 7.282.

The panel dismissed Argentina's claims on the ground that 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 EP and NV.³⁰ (emphasis added) In the present investigation, the alleged difference arose exclusively from the methodology used by the EU authorities to construct a NV based on surrogate prices and hence did not affect the price comparability of the two prices.³¹

The panel's rulings are fundamentally incorrect both in law and on the facts. The text of Article 2.4 contains no explicit limitations on what kinds of differences between EP and NV should be adjusted. While it does set out a non-exhaustive list of factors that may affect price comparison, it states explicitly that "any other differences which . . . affect price comparability" must be adjusted to ensure 'fair comparison'. This has been confirmed by the Appellate Body in *US—Hot-Rolled Steel* where it was held that "[t]here are . . . no differences 'affect[ing] price comparability' which are precluded, as such, from being the object of an 'allowance'".³² Thus, the text and the Appellate Body's ruling both suggest that Article 2.4 concerns *whether* the comparability of EP and NV has been affected by an alleged difference, not how or in what circumstances the difference arises. In this regard, the panel's finding that the price comparability of the EP and the CNV of biodiesel was not affected by the difference resulted from the use of different production costs was not supported by any evidence. Rather, the panel appears to have assumed that any difference arising exclusively from the 'methodology' used cannot affect price comparability within the meaning of Article 2.4. However, the facts of the investigation suggest that the price comparability must have been affected given the difference between the surrogate price and actual prices which, as found by the panel, roughly equalled the export tax imposed by Argentina.³³ Further, Article 2.4 makes explicit reference to 'taxation' as a cause of differences that may affect price comparability. In the present investigation, the export tax clearly falls within the category of taxation; and as the tax did give rise to a difference between the EP and the CNV, it must be adjusted to ensure 'fair comparison'. The panel's distinction between 'methodology-resulted' differences and 'transaction-resulted' differences is not only unjustifiable but may

30 See above n. 1, Panel Report, *EU—Biodiesel*, paras. 7.294–7.296.

31 See above n. 1, Panel Report, *EU—Biodiesel*, paras. 7.299–7.302.

32 Appellate Body Report, *United States—Anti-Dumping Measures on Certain Hot-Rolled Steel Products from Japan*, WT/DS184/AB/R, adopted on 23 August 2001, para. 177.

33 See above n. 1, Panel Report, *EU—Biodiesel*, para. 7.299.

also have unwanted ramifications. For the sake of argument, assume the actual costs of the raw materials were not distorted, but at the time of exportation, biodiesel was subject to an export tax at the same level of the export tax on the raw materials while there was no equivalent tax applicable to domestic sales of biodiesel. Following the panel's reasoning, the export tax would be a required adjustment to the NV as it causes a difference between the EP and the domestic selling price which arises from exporting and domestic transactions and affects price comparability. If this is correct, then one wonders why the same difference caused by the same level of taxation should not be adjusted to achieve the same objective (i.e. 'fair comparison') merely because the difference arises in different circumstances. The panel's approach would end up promoting the use of protectionist methodologies in the calculation of EP and NV with the ostensible objective of inflating dumping margins.

The panel cited two Appellate Body reports to support its findings. First, the panel relied heavily on the Appellate Body report on *US—Zeroing (EC)* where the Appellate Body did make the same rulings as the panel's.³⁴ For the reasons advanced above, the authors do not believe the Appellate Body's rulings in *US—Zeroing (EC)* have established good law; the focus of Article 2.4 should be on whether an alleged difference has precluded 'fair comparison' between EP and NV rather than on how or in what circumstances the difference arises. This observation finds support from a later report of the Appellate Body on *US—Final Lumber AD Determination (Article 21.5)* in which the Appellate Body ruled:

... the use of zeroing under the transaction-to-transaction comparison methodology artificially inflates the magnitude of dumping, resulting in higher margins of dumping and making a positive determination of dumping more likely. This way of calculating cannot be described as impartial, even-handed, or unbiased. For this reason, we do not consider that the calculation of "margins of dumping", on the basis of a transaction-to-transaction comparison that uses zeroing, satisfies the "fair comparison" requirement within the meaning of Article 2.4 ...³⁵

34 Appellate Body Report, *United States—Laws, Regulations and Methodology for Calculating Dumping Margins ("Zeroing")*, WT/DS294/AB/R, adopted on 9 May 2006, para. 157.

35 Appellate Body Report, *United States—Final Dumping Determination on Softwood Lumber from Canada (Recourse to Article 21.5 of the DSU by Canada)*, WT/DS264/AB/RW, adopted on 1 September 2006, para. 142.

The fact that the Appellate Body in the latter case did not apply its own ruling in the earlier case suggests that it may have realised that the earlier ruling had inappropriately restricted the scope of differences that may need to be adjusted. It is evident from the latter ruling that the core obligation of investigating authorities under Article 2.4 is to ensure ‘fair comparison’ and that differences which arise from the use of a particular ‘methodology’ in the calculation of dumping margin fall within the required adjustments. Second, the panel referred to a recent report of the Appellate Body on *EC—Fasteners (Article 21.5)* which concerned the EU’s use of surrogate costs in the construction of NV based on the NME Assumption against China.³⁶ On the issue whether the EU was required to make due allowances for cost differences alleged by China, the Appellate Body ruled:

*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.*³⁷ (emphasis added)

The panel considered this finding of the Appellate Body and concluded that it supported its ‘methodology’ and ‘transaction’ distinction and hence its findings that ‘methodology-resulted’ differences are not required to be adjusted. This constitutes a misinterpretation of the Appellate Body’s rulings. A better understanding of the Appellate Body’s rulings would be that (1) the obligation of making adjustments under Article 2.4 may be qualified by specific provisions of the AD Agreement or other WTO instruments such as Accession Protocols which explicitly allow the replacement of distorted costs with surrogate costs in the construction of NV, and (2) in those circumstances,

36 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.

37 *Ibid.*, para. 5.207.

investigating authorities are not required to make adjustment of the cost differences between EP and CNV if such an adjustment would result in reintroducing the distorted costs into the CNV. In this regard, the Appellate Body further held that adjustments must still be made to cost differences unrelated to the distorted costs.³⁸ Thus, the Appellate Body was not concerned about whether a difference resulted from the ‘methodology’ used or from the ‘transaction’ and, consequently, its finding above do not seem to support the panel’s ‘methodology’ and ‘transaction’ distinction. Rather, the Appellate Body’s concern seemed to be that adjustments of distorted and replaced costs may contradict the specific circumstances where the use of surrogate costs is explicitly authorised under the WTO. The Appellate Body’s reference to the second *Ad Note* to Article VI:1 of the GATT and Section 15(a) of China’s *Accession Protocol* suggests that such circumstances are rare—the former concerns the existence of “a complete or substantially complete monopoly” in the exporting countries under investigation while the latter relates to the NME Assumption, both specific rules with limited scope of applications.³⁹ In any event, as argued above, a finding of PMS is not a valid ground for the use of surrogate costs under the AD Agreement; and therefore any cost differences resulted from the use of that unjustified methodology must be adjusted to achieve ‘fair comparison’.

2.4 “Excessive dumping margin” Claims

Argentina’s final claim in relation to ‘dumping’ relied on Article 9.3 of the AD Agreement, contending that the EU had imposed “anti-dumping duties in excess of the margin of dumping that should have been established in accordance with Article 2” of the agreement.⁴⁰ The relevant part of Article 9.3 provides that “the amount of the anti-dumping duty shall not exceed the margin of dumping as established under Article 2.”

The panel found in favour of Argentina on the grounds that (1) the reference to dumping margin in Article 9.3 does not encompass a margin “established in a manner that is *not* consistent with the disciplines of Article 2”, (2) the EU authorities’ calculation of the dumping margins in the present investigation did not comply with the requirements of Articles 2.2.1.1 and 2.2, and

38 Ibid., paras. 5.213–5.234.

39 See above n. 2, Puccio, “Granting Market Economy Status to China: An Analysis of WTO Law and of Selected WTO Members’ Policy”, at 4–5. For a background of the introduction of the second *Ad Note* to GATT Article VI:1, see GATT Analytical Index, Article VI Anti-Dumping and Countervailing Duties, at 228, available at: https://www.wto.org/english/res_e/booksp_e/gatt_ai_e/art6_e.pdf.

40 See above n. 1, Panel Report, *EU—Biodiesel*, para. 7.352.

(3) the anti-dumping duties imposed ranging from 22% to 25.7% went beyond the margins from 6.8% to 10.6% as calculated in accordance with Article 2 in the provisional determinations.⁴¹ In essence, the panel believed that “the maximum level at which anti-dumping duties may be levied” under Article 9.3 must not exceed the dumping margins calculated consistently with Article 2.⁴²

The panel was correct to rule out the possibility of application of inflated anti-dumping duties by using WTO-inconsistent methodology in determining dumping margins. However, this issue of unjustified inflation could have been, and would better be, resolved under Article 2.4 by requiring investigating authorities to make adjustments of differences that affect ‘fair comparison’. As the use of surrogate production costs based solely on a finding of PMS is not authorized under the AD Agreement, due allowances must be made to any differences between EP and CNV caused by the use of that methodology. Article 2.4 would also provide a better approach to this issue as it directs authorities to calculate correct dumping margins rather than leave the issue to be solved by WTO tribunals. In the present investigation, the panel’s findings under Article 9.3 benefited from the EU authorities’ provisional determinations in which the actual producers’ costs were used in determining CNV. However, where authorities have relied on surrogate costs throughout an investigation and hence have not considered dumping margins that should have been established in a WTO-lawful manner, then WTO panels would need to determine the correct dumping margins first before making any findings under Article 9.3. This would impose undue burdens on WTO panels and may suffer from problems such as lack of sufficient information or evidence. Alternatively, WTO panels may simply rule against the use of surrogate costs and mandate investigating authorities to reassess dumping margins using correct costs information. Such a reinvestigation is not desirable because it would create continuing uncertainties to exporters and may not lead to WTO-consistent outcomes. In short, Article 2.4 should be employed to deal with the issue of unjustified inflation of dumping margins while Article 9.3 provides an additional safeguard against the imposition of excessive anti-dumping duties.

41 See above n. 1, Panel Report, *EU—Biodiesel*, paras. 7.359–7.365. The anti-dumping duties applied were lower than the dumping margins calculated in the final determinations due to the EU authorities’ application of the “lesser duty rule”.

42 See above n. 1, Panel Report, *EU—Biodiesel*, para. 7.363.

3 Implications for the Issue of PMS

The panel's rulings in *EU—Biodiesel* represent a significant development of the WTO anti-dumping jurisprudence and have significant implications for WTO members' anti-dumping practice. To the authors' knowledge, this is the first time that the WTO tribunals have unequivocally ruled that the Reasonableness Condition under Article 2.2.1.1 of the AD Agreement does not allow for consideration of the reasonableness of an exporter's actual costs so long as the costs are properly recorded in accordance with local GAAP. Accordingly, the panel's ruling firmly recognises as a general principle that CNV must be based on the exporter's costs and imposes a considerable restraint on the use of surrogate costs. The ruling is of particular importance to the rising use of PMS as a basis for disregarding actual producers' prices for determining NV and actual producers' costs for calculating CNV. With the expiration of the NME Assumption against China, the element of PMS under Article 2.2 of the AD Agreement offers a convenient alternative for the users of the assumption to continue to treat China or economies like China as a NME in anti-dumping investigations. This element has actually been employed by members like Australia and the EU. The WTO tribunals have not had a chance to consider the issue of PMS until recently in the ongoing *EU—Cost Adjustment Methodologies (Russia)* dispute.⁴³ While the disciplines on PMS have yet to be developed,⁴⁴ the panel's rulings in *EU—Biodiesel* have resolved one of the key issues in this connection, that is, to disqualify PMS from being a valid ground for the use of surrogate costs in constructing NV. Accordingly, cost distortions due to government interventions, standing alone, cannot render an exporter's actual costs as being unreasonable within the meaning of Article 2.2.1.1 of the AD Agreement, and hence cannot justify the replacement of the actual costs with surrogate costs. The panel's approach, therefore, has the effect of restraining artificial inflation of CNV and dumping margins through the use of surrogate costs in constructing NV.

43 See *European Union—Cost Adjustment Methodologies and Certain Anti-Dumping Measures on Imports from Russia*, Request for Consultations by the Russian Federation, WT/DS474/1 (9 January 2014); and *European Union—Cost Adjustment Methodologies and Certain Anti-Dumping Measures on Imports from Russia (second complaint)*, Request for Consultations by the Russian Federation, WT/DS494/1 (19 May 2015).

44 The authors are analysing the issue of PMS and the desirable WTO disciplines in a separate article.

3.1 *Has Australia Violated the WTO Rules in Treating China as Having a PMS?*

As a precondition for negotiations of the China—Australia Free Trade Agreement, Australia recognised China as a full market economy in 2005 and committed not to apply the NME Assumption against China in anti-dumping investigations.⁴⁵ However, given the protectionist needs of Australian import-competing industries, the Australian government has come under considerable pressure to impose higher anti-dumping duties against Chinese imports.⁴⁶ As an alternative to the NME Assumption, Australia has consistently treated China as having a PMS due to government interventions in the relevant markets in recent anti-dumping investigations.⁴⁷ The findings of PMS, by the Anti-Dumping Commission (“AD Commission”) and formerly Australian Customs and Border Protection Service (“Australian Customs”), have generally been based on the following evidence: (1) China’s macroeconomic policies which provide a policy directive to foster the development of the relevant industries;⁴⁸

45 See *Memorandum of Understanding between the Department of Foreign Affairs and Trade of Australia and the Ministry of Commerce of the People’s Republic of China on the Recognition of China’s Full Market Economy Status and the Commencement of Negotiation of A Free Trade Agreement between Australia and the People’s Republic of China*, 18 April 2005, available at: http://dfat.gov.au/trade/agreements/chafta/Documents/mou_aust-china_fta.pdf.

46 See, for example, Australian Manufacturing Workers’ Union, Submission to the Department of Foreign Affairs and Trade Concerning A Possible China-Australia Free Trade Agreement (AMWU Submission), June 2005, available at: http://dfat.gov.au/trade/agreements/chafta/Documents/4NMA_07_AMWU.pdf.

47 See, for example, Australian Customs and Border Protection Service, Certain Hollow Structural Sections Exported from the People’s Republic of China, the Public of Korea, Malaysia, Taiwan and the Kingdom of Thailand, Report to the Minister No. 177 (7 Jun. 2012) (REP 177); Australian Customs and Border Protection Service, Aluminium Road Wheels Exported from the People’s Republic of China, Report to the Minister No. 181 (12 Jun. 2012) (REP 181); Australian Customs and Border Protection Service, Dumping of Zinc Coated (Galvanised) Steel and Aluminium Zinc Coated Steel Exported from the People’s Republic of China, the Republic of Korea, and Taiwan, Report to the Minister No. 190 (30 Apr. 2013) (REP 190); Anti-Dumping Commission, Dumping of Hot Rolled Plate Steel, Exported from the People’s Republic of China, Republic of Indonesia, Japan, the Republic of Korea and Taiwan, and Subsidisation of Hot Rolled Plate Steel Exported from the People’s Republic of China, Report Number 198 (16 Sep. 2013) (REP 198); Anti-Dumping Commission, Alleged Dumping and Subsidisation of Silicon Metal Exported from the People’s Republic of China, Report No. 237 (3 Jun. 2015) (REP 237); Anti-Dumping Commission, Alleged Dumping of Certain Crystalline Silicon Photovoltaic Modules or Panels Exported from the People’s Republic of China, Report No. 239 (6 Oct. 2015) (REP 239).

48 See, for example, above n. 47, REP 177, at 118–148; REP 239, at 88–89.

(2) the provision of financial assistance or subsidies to the relevant industries;⁴⁹ and (3) import and export measures such as tariffs and quotas.⁵⁰ Over time, Australian investigating authorities have focused on China's raw materials markets such as the steel and iron industry, the aluminium industry, the silicon industry, and the solar photovoltaic industry, finding that the prices of the raw materials were artificially lowered by interventions of the Chinese government and hence the existence of a PMS in these markets. Following the findings of PMS, the authorities have consistently replaced the actual production costs incurred by the Chinese exporters under investigation with benchmark prices such as costs in third countries,⁵¹ and reference prices provided by trading centres such as London Metal Exchange⁵² and by independent consultancy companies like MEPS (International) Ltd.⁵³ The use of the surrogate prices for raw materials results in increased costs in the form of uplifted costs of inputs to manufacture and consequently inflated NV and dumping margins.

Accordingly, Australia's anti-dumping practice against China would seem to be a disguised use of the NME Assumption. However, while surrogate costs are allowed to be employed under the NME Assumption, the use of such costs is not justified by findings of PMS. Based on the panel's rulings in *EU—Biodiesel*, there is a strong argument that Australia's anti-dumping practice has breached Articles 2.2.1.1, 2.2 and 9.3 of the AD Agreement. Put aside the issues relating to the Australian authorities' findings of PMS and choice of surrogate costs (which one of the authors has discussed elsewhere),⁵⁴ a finding of PMS does not provide a sufficient ground for the use of surrogate costs in constructing NV. In the absence of an assessment of whether an exporter's actual costs have been recorded accurately, the authorities must determine NV on the basis of the actual costs. The application of uplift to actual costs as a result of the use of surrogate costs has resulted in an unjustified inflation of dumping margins and hence an imposition of anti-dumping duties in excess of dumping

49 See, for example, above n. 47, REP 177, at 153–154; REP 181, at 36–37; REP 239, at 94–95.

50 See, for example, above n. 47, REP 177, at 148–151; REP 239, at 26–32.

51 See, for example, above n. 47, REP 177, at 43–62, 257–274 (the surrogate costs were based on a basket benchmark consisting of costs of hot-rolled coil (“HRC”) incurred by exporters in other countries subject to the investigation); REP 190, at 60–63 (the surrogate costs were based on benchmark HRC prices in Korea and Taiwan).

52 See, for example, above n. 47, REP 181, at 36–44 (the actual aluminium and alloy costs were replaced).

53 See, for example, above n. 47, REP 238, at 41–43 (the surrogate costs were MEPS-based average price for 304 stainless steel cold-rolled coil using the monthly reported MEPS North American and European prices alone (excluding the Asian price)).

54 See above n. 4, Zhou, “Australia's Anti-Dumping and Countervailing Law and Practice: An Analysis of Current Issues Incompatible with Free Trade with China”.

margins which should have been calculated by using the actual costs in determining CNV. In addition, while the *EU—Biodiesel* panel would disagree, the authors believe that Australia's anti-dumping practice, which has compared EP (determined based on an exporter's actual costs) and CNV (determined based on uplifted surrogate costs) in determining dumping margins, is contrary to the principle of 'fair comparison' under Article 2.4 of the AD Agreement.

The final question is whether the relevant Australian laws are "as such" in violation of the AD Agreement. While section 269TAC(1) of the *Customs Act 1901* requires NV to be established generally by reference to the actual selling price of subject goods in the market of exporting countries, sections 269TAC(2)(a)(ii) and 269TAC(2)(c) authorise the Minister to construct NV based on a finding of PMS. In calculating a CNV, the production costs are determined pursuant to Regulation 43 of the *Customs (International Obligations) Regulations 2015* which allows investigating authorities to disregard exporters' cost records which do not (i) satisfy the GAAP Condition or (ii) "reasonably reflect *competitive market* costs associated with the production or manufacture of like goods". Thus, Australian regulations add a qualification to the Reasonableness Condition by requiring the costs recorded by exporters to be "competitive market" prices. This qualification evidently amounts to a departure from Articles 2.2.1.1 and 2.2 of the AD Agreement which according to the panels' 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 reasonable market prices as long as they are accurately recorded. As shown above, in practice the "competitive market" condition has been translated into an assessment of whether a PMS exists due to governments' influence in the relevant markets. Accordingly, Australian regulations necessarily provide a violation of the AD Agreement by mandating investigating authorities to consider whether exporters' actual costs are "competitive market" prices and to disregard the actual costs in determining CNV. Such an approach to the construction of NV, which has consistently inflated dumping margins, has become a general practice in Australia's anti-dumping investigations against China.

4 Conclusion

It has become a common but notoriously controversial practice of traditional users of anti-dumping measures to treat countries like China as a NME in anti-dumping investigations. The NME methodology is used simply for the purpose of facilitating findings of dumping and of higher dumping margins so that more and heavier anti-dumping duties can be imposed to afford protection

to domestic import-competing industries. Based on the NME Assumption, investigating authorities are allowed to replace the actual prices or costs of exporters with surrogate prices or costs which are typically higher in the calculation of NV, leading to inflated dumping margins and anti-dumping duties ultimately imposed. After the expiration of the NME Assumption, these traditional users are most likely to rely on a finding of PMS to continue to treat China and similar economies as a NME. This anticipated rising use of PMS has been seen in the practice of some WTO members such as Australia and the EU which have employed surrogate costs in the determination of CNV solely based on a finding that a PMS exists in the market under consideration. The significance of the panel's decision in *EU—Biodiesel* lies in its unequivocal rejection of a finding of PMS as a valid basis for the use of surrogate production costs in determining a CNV. Thus, even if a PMS is found to exist, authorities must still use exporters' actual costs in the construction of NV provided that they are properly recorded in records that comply with local GAAP. Thus, it is submitted that Australia's practice mentioned above is contrary to WTO rules. However, the panel's decision has two major weaknesses: (1) it fails to impose an obligation on authorities to make allowance for the difference between the EP and the CNV that necessarily results from the use of surrogate costs, hence the failure to promote 'fair comparison'; and (2) in finding that the EU regulation is not 'as such' in breach of WTO rules, it fails to prohibit WTO members from authorising authorities to employ surrogate costs in the construction of NV solely based on a finding of PMS. Accordingly, the panel's decision is undesirably limited to condemning the practice of using surrogate costs while it should have required that national legislation of WTO members must not authorise such practice merely because a PMS is found to exist.