September 9, 2002

Honorable Faryar Shirzad
Assistant Secretary for Import Administration
U.S. Department of Commerce
Central Records Unit, Room 1870
Pennsylvania Avenue and 14th Street, N.W.
Washington, D.C. 20230

Attention: Affiliated Party Sales

Re: Proposed Modification of the Department's Practice Concerning the Determination of Whether Sales to Affiliated Parties are in the Ordinary Course of Trade; Rebuttal Comments

Dear Assistant Secretary Shirzad:

We are writing on behalf of Koyo Seiko Co., Ltd. and Koyo Corporation of U.S.A. (collectively "Koyo"), to rebut certain of the comments filed in response to the Department's notice, published in the Federal Register on August 15, 2002, regarding the above-captioned topic. See Antidumping Proceedings: Affiliated Party Sales in the Ordinary Course of Trade, 67 Fed. Reg. 53339 (Aug. 15, 2002) ("the Notice"). These comments are being filed on September 9, 2002, pursuant to the Department's extension of the deadline published in the Notice.

1. Appropriateness of the Department's Proposal to Change its Methodology

One of the commenters, Stewart and Stewart ("Stewart") argues it is improper for the Department, as it proposes, to apply a new arm's length methodology in all reviews initiated on the basis of requests received on or after the first of the month following the date of publication

of the final notice of the new methodology. Stewart argues that under section 129(c) of the Uruguay Round Agreements Act, 19 U.S.C. 3538(c), the Department may not apply its new methodology to entries made before the date of implementation of the Appellate Body report in the Japan – Hot-Rolled dispute.[1] As Stewart notes, however, the United States has taken the position in other dispute settlement proceedings that section 129(c) does not require any particular action with respect to entries that are not subject to the particular decision in dispute.[2] Thus, section 129(c) addresses only the manner in which the Department may address entries subject to the Japan hot-rolled steel investigation, and does not affect the Department's ability to develop and implement policies in other ongoing antidumping proceedings.

As Stewart notes, section 123(g) of the URAA, 19 U.S.C. 3533(g), governs the Department's broader implementation obligations in cases in which a Department practice is found to be inconsistent with the United States' WTO obligations. While acknowledging that section 123(g) is silent on the entries that may be covered by that implementation, Stewart argues that the prospective limitation on implementation contained in section 129(c) should also be read into section 123(g), and, indeed, considered as a general principle for the implementation of WTO decisions. Koyo notes that there is nothing in the legislative history of the URAA to support this position. Moreover, the United States, in its submissions to the panel in the dispute settlement proceedings involving section 129(c) has already taken the position that it enjoys discretion under other provisions of the antidumping laws to implement WTO decisions with

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1 Stewart Comments at 1-8.

2 *See*, *e.g.*, *United States – Section 129(c)(1) of the Uruguay Round Agreements Act*, WT/DS221/R (circulated 15 July 2002), paras. 3.64 – 3.84 (describing United States' position).

respect to unliquidated entries – both in the case that is the subject of the dispute and in its antidumping procedures generally.[3]

Stewart also claims that implementing the Appellate Body ruling with respect to entries made before the date of implementation in the Japan – Hot-Rolled case would lead to inconsistent implementation obligations for WTO Members, with the United States implementing earlier because of its retrospective antidumping system. The better view, of course, is that applying the new policy to entries in pending reviews would prevent the assessment of antidumping duties calculated in a WTO-inconsistent manner, an implementation problem that is far less complicated for Members that use a prospective method of assessment.

Moreover, as Stewart is well aware, the Department enjoys considerable discretion to modify its policies from review to review, and to apply new policies to previous entries in the course of its retrospective annual administrative reviews. Stewart has not provided any compelling reason why the Department should not avail of that discretion in this instance.

Finally, Stewart fails to note that the longer the Department continues to apply its old, admittedly WTO-inconsistent arm's length test, the more it compels WTO Members to pursue domestic litigation or dispute settlement proceedings challenging that application. A proliferation of such litigation, whose outcome would hardly be in doubt, does not serve the interests of either the Department, petitioners, or respondents in ongoing proceedings before the Department.

2. The Proposed "98/102" Band Should Not Be Narrowed Further

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3 *Id.*

In its comments, Koyo argued that the Department's proposed "98/102 percent" test of whether sales to affiliated parties should be deemed to be outside the ordinary course of trade was too narrow and should be expanded to a 95/105 percent test. Koyo also argued that while the Department's proposed test addressed the lack of "even-handedness" found by the WTO Appellate Body in the Department's former 99.5 percent test, the proposed approach was also too narrow in that it left no room to examine the commercial realities of particular cases that may affect whether affiliated party sales are outside the ordinary course of trade. Accordingly, Koyo urged the Department to broaden its proposed standard and to consider commercial reasonableness in determining whether sales are outside the ordinary course of trade.

Other commenters have also found fault with the 98/102 percent approach, but some of their proposals are far-fetched in the extreme. Dewey Ballantine, for example, proposes that the Department should retain its current 99.5 percent test for determining whether low-price sales to affiliates are outside the ordinary course of trade, and adopt a 120 percent test for determining whether high-price sales are outside the ordinary course of trade.[4] According to Dewey Ballantine, the WTO Appellate Body decision does not compel the Department to use symmetrical tests to examine both low- and high-price sales to affiliates. Dewey Ballantine quotes the Appellate Body as noting that "we do not suggest that the methods for verifying whether high and low-priced sales to affiliates are 'in the ordinary course of trade' must necessarily be identical."[5] It is, however, a huge leap from a statement that the tests need not

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[4] Dewey Ballantine Comments at 3-7.

[5] *Id*. at 3-4, *quoting United States – Anti-Dumping Meaures on Certain Hot-Rolled Steel Products from Japan*, WT/DS184/AB/R (24 July 2001) at n.113.

necessarily be identical to the conclusion that a 99.5/120 percent test would come close to satisfying the Appellate Body's requirement of even-handedness or the Department's obligation to ensure a fair comparison in determining dumping margins. None of the justifications put forth by Dewey Ballantine for such a wildly asymmetrical test withstand scrutiny. For example, Dewey Ballantine argues that the Department's current practice recognizes the need for an asymmetrical test. However, it is precisely the lack of even-handedness in the current test that was found to be flawed by the Appellate Body. This lack of even-handedness is hardly corrected by adopting a bright-line test that continues an asymmetrical bias towards the inclusion of high-price sales to affiliates.

Dewey Ballantine also argues that the 120 percent threshold for high-price sales is necessary to ensure that profitable sales are retained for analysis. Again, this does not follow. The Department's task in revising the arm's length test is to derive an even-handed test, not to skew the process to increase the likelihood of a particular outcome. To the extent that the issue of profitability is relevant, Koyo notes that it is quite possible that affiliated party sales that are made at, for example, 80 percent of the average price of non-affiliated sales might well be above cost and therefore profitable. Dewey Ballantine does not, however, appear concerned that the Department's proposed test would exclude those sales as outside the ordinary course of trade. Dewey Ballantine nevertheless assumes that affiliated party sales made at 120 percent of the average are both within the ordinary course of trade and "non-aberrational." Put simply, Dewey Ballantine's proposal is based on self-serving favorable assumptions, rather than on an attempt to provide an even-handed, broadly-applicable definition of the circumstances in which affiliated party sales – both low- and high-price – may be said to be "outside the ordinary course of trade."

Other commenters, including Stewart and Wiley Rein & Fielding ("Wiley"), argue that the proposed 98/102 band should be narrowed to a 99.5/100.5 percent test, because the proposed 98/102 percent band creates an incentive to manipulate affiliated party sales.[6] Koyo submits that the concern over manipulation of margins through sales to affiliated parties is grossly exaggerated for several reasons. First, the definition of "affiliation" includes within its scope parties that are related through nothing more than a mere five percent ownership share.[7] In the real commercial world, it is rare that a respondent would find a company with which it has such an attenuated affiliation willing to serve as an accomplice to develop complex pricing schemes to "game" the dumping margin calculation process. Far more likely is that sales to such "affiliates" are treated as normal commercial transactions – i.e., arm's length sales. It is illuminating that none of the commenters are able to point to specific, concrete examples of manipulation or "gaming" the calculation of dumping margins, and instead rely entirely on complex hypotheticals. It would be inappropriate to establish an arm's length methodology that ignores commercial reality for the purpose of counteracting manipulation that has not been shown to exist.

Second, in certain industries, such as antifriction bearings, the number of products and prices ranges into the thousands. In such conditions, it would be extremely difficult for a respondent to develop schemes to sell such a broad array of products in the comparison market at prices that are intended to influence the antidumping margins on merchandise sold in the United

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6 Stewart Comments at 12; Wiley Comments at 10-13.

7 19 U.S.C. 1675(33)(E).

States. And to set prices with the necessary precision – especially after considering the numerous adjustments required to calculate the net selling prices that are used in the arm's length test – such that they fall within the narrow 98/102 percent band (not to mention the 99.5/100.5 percent band) in a manner that would "game" the process, defies reality.

Moreover, in simple commercial terms, there is no basis for an assumption that prices that vary by more than one half of one percent from an average price are outside the ordinary course of trade. Rather than removing a supposed incentive to manipulate, Stewart's and Wiley's proposed narrower band would defy commercial reality, which is the basis for the "outside the ordinary course of trade" determination that is supposedly implemented through the arm's length test.

Similarly, Koyo also disagrees with the proposal of Skadden, Arps, Slate, Meagher & Flom LLP ("Skadden") that, even if the Department were to adopt the 98/102 percent test in investigations, it should use a 99.5/100.5 percent test in administrative reviews.[8] The mere fact that the Department uses a different standard for *de minimis* dumping margins in reviews than investigations, however, does not mean that selling prices that differ by more than one half of one percent from an average price must necessarily be considered to be outside the ordinary course of trade.

Stewart also argues that the Department should counteract what it predicts will be "dramatically fewer price comparisons" as a result of the introduction of an even-handed approach to high price sales to affiliates by modifying its practice regarding the reporting of downstream sales. Stewart (and other commenters, such as Dewey Ballantine and Wiley)

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8 Skadden Comments at 7-10.

propose that the Department should eliminate the consideration of affiliated party sales entirely and instead require respondents to report the downstream sales by their affiliates (i.e., abolish the 5 percent threshold for the reporting of downstream sales).[9] The net effect of this proposal would be that, rather than treating high- and low-price sales to affiliated parties in an even-handed manner, the Department's implementation of the Appellate Body decision would result in a fundamental change in its approach to affiliated party sales, going well beyond the Appellate Body's recommendation. Moreover, requiring the reporting of downstream sales presumes the *ability* of a respondent to do so – i.e., to obtain the necessary information from the affiliates involved. However, in light of the expansive definition of affiliation to include parties that have only a five percent ownership share, it is frequently the case that a respondent simply cannot obtain a so-called affiliate's downstream sales data. In this circumstance, the Department will either be tempted to apply "facts available" because of the reporting failure or,
at best, to use constructed value because of a lack of matching comparison market sales (contrary to the assertion of certain commenters). Koyo submits that it would be inappropriate to establish a methodology that increases the likelihood of such outcomes.

Finally, several commenters suggest that the Department's proposal would lead to various types of gaming of the system by respondents, including sales of non-matching and matching models at different prices to affiliates and even the purchase of stock in order to create affiliations that could be used to exclude certain sales from the Department's analysis. It is noteworthy that none of these commenters can point to any instances in which the Department

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9 Stewart Comments at 12-13; Dewey Ballantine Comments at 7-8; Wiley Comments at 7-10.

has found any such gaming in practice, and it is difficult to avoid the conclusion that these concerns simply represent the theoretical musings of Washington counsel rather than bear a relationship with any commercial realities. Moreover, as Koyo noted in its initial comments, the Department already possesses statutory authority to address any such attempts to manipulate prices, if they are in fact found to exist in specific cases.

Pursuant to the instructions in the Department's notice, we are filing an original and six copies of these rebuttal comments. In addition, we are filing a copy on a DOS-formatted 3.5" diskette, in WordPerfect format.

Koyo very much appreciates the opportunity to address this important issue. If you have any questions regarding the contents of this letter, please feel free to contact the undersigned.

Sincerely,

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Niall P. Meagher
Neil C. Pratt

Counsel to Koyo Seiko Co., Ltd. and
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