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PUBLIC DOCUMENT

The Honorable Carlos M. Gutierrez
Secretary of Commerce
Attn: Import Administration, APO/Dockets Unit
Room 1870
U.S. Department of Commerce
14th Street & Constitution Ave., NW
Washington, DC 20230

Re: Antidumping Methodologies for Proceedings that Involve Significant Cost Changes Throughout the Period of Investigation (POI)/Period of Review (POR) that May Require Using Shorter Cost Averaging Periods; Request for Comment

Dear Secretary Gutierrez:

The following comments are submitted on behalf of Hogan & Hartson LLP in response to the Department of Commerce's ("Department") Request for Comment on Antidumping Methodologies for Proceedings that Involve Significant Cost Changes Throughout the Period of Investigation (POI)/Period of Review (POR) that May Require Using Shorter Cost Averaging Periods, 73 Fed. Reg. 26,364 (Dep't Commerce)(May 8, 2008)("Request for Comment").

For the Department's convenience, we have organized our comments to provide some general contextual observations followed by answers to the specific questions posed by the Department in its Federal Register notice.

I. GENERAL COMMENTS

A. Statutory Background

Under the antidumping statute, "normal value" is calculated on the basis of prices at which the foreign like product is first sold "in the usual commercial quantities" and "in the ordinary course of trade." 1/ Home market sales are deemed to have not been made in "the ordinary course of trade" where, inter alia, such sales are disregarded pursuant to the below costs test established under Section 773(b)(1). These provisions parallel the provisions of articles 2.1 and 2.2.1 of the WTO Antidumping Agreement that likewise require home market prices to be made in the "ordinary course of trade" and permit the investigating authorities to treat sales that fail the below cost test as "outside the ordinary course of trade." 2/

As set forth in Section 773(b)(1), the below cost test involves three tests: (1) are the sales below cost at the time of sale; (2) have such below cost sales been made "within an extended period of time" and "in substantial quantities"; and (3) are the sales at prices which "permit the recovery of all costs within a reasonable period of time." 3/ The statute further

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1/ 19 U.S.C. § 1677b(a)(1)(A).

2/ Agreement on Implementation of Article VI of the General Agreement on Tariffs and Trade 1994, arts. 2.1, 2.2.1.

3/ 19 U.S.C. § 1677b(b)(1). A WTO panel examining the parallel provisions of the WTO Antidumping Agreement concluded that the Article 2.2.1 requires essentially the same analysis. See Panel Report, European Communities – Anti-Dumping Measure on Farmed Salmon from Norway, SWT/DS337/R, paras. 7.232, 7.233 (16 November, 2007)(adopted 15 January, 2008) ("EC – Salmon") ("On its face, the methodology set out in the first sentence of Article 2.21 involves two steps: First, the below-cost sales that may potentially be treated as not being made in the ordinary course of trade by reason of price must be ascertained. This initial step requires investigating authorities to identify sales made at prices below 'per unit (fixed and variable) costs of production plus administrative, selling and general costs.' Article 2.2.1 does not prescribe any particular time period for the purpose of measuring the per unit costs that must be used in this assessment, suggesting that investigating authorities have a degree of discretion to calculate such costs over different periods of time, which might be, for example, the day of sale or the period of investigation . . . . Secondly, the investigating authority must 'determine' whether 'such' below-cost sales display three specific characteristics, *i.e.*, whether the below cost sales identified under the first step are made; (i) 'within an extended period time'; (ii) 'in substantial quantities';

clarifies that an "extended period time" means "normally 1 year, but not less than 6 months" and "substantial quantities" means either: (a) the volume of such sales represents 20 percent or more of the volume of sales under consideration for the determination of normal value; or (b) the weighted average per unit price of the sales under consideration for the determination of normal value is less than the weighted average per unit cost of production for such sales. 4/ Lastly, with respect to cost recovery, the statute specifies that "[i]f prices which are below the per unit cost of production at the time of sale are above the weighted-average per unit cost of production for the period of investigation or review, such prices shall be considered to provide for recovery of costs within a reasonable period of time." 5/ These provisions, too, are paralleled in Article 2.2 of the WTO Antidumping Agreement.

B. The Issue Presented – Appropriately Measuring Cost of Production

As described above, it is not the purpose of the "below cost test" to mechanically exclude any and all transactions that are made below the cost of production, but instead to identify and exclude from the normal value calculation only those transactions that are made at prices that are not within the "ordinary course of trade." Thus, under the statutory tests, even where transaction prices fall below cost such transactions are required to be accepted and used in determining normal value where they are not made in substantial quantities over an extended period of time or where they are made at prices that permit recovery of costs within a reasonable period of time.

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and (iii) 'at prices which do not provide for the recovery of all costs within a reasonable period of time.' It is only below-cost sales that are found to exhibit all three of these characteristics that may be treated as not being made in the ordinary course of trade by reason of price.").

4/ 19 U.S.C. § 1677b(1)(2)(B),(C).

5/ 19 U.S.C. § 1677b(1)(2)(D).

The principal focus of the Department's current proposal is with respect to the initial determination of whether transaction prices are "below the per unit cost of production at the time of sale." In this regard, neither the statute, nor the WTO clearly specifies the time period over which costs should be calculated for this purpose. Section 773(b)(3) states that the cost of production includes the cost of materials and of fabrication "during a period which would ordinarily permit the production of that foreign like product in the ordinary course of business." Examining the parallel provisions of the WTO Antidumping Agreement (the first sentence of Article 2.2.1), a WTO dispute settlement panel recently concluded that "investigating authorities have a degree of discretion to calculate such costs over different periods of time, which might be, for example, the day of sale or the period of investigation." 6/ Likewise, as discussed in the Request for Comment, while the Department intends to retain a general preference for averaging costs over the entire period of investigation ("POI") or review ("POR"), the Department's prior practice has recognized the agency's authority to calculate costs over periods shorter than the period of investigation or review (e.g., quarterly or monthly), where circumstances warrant.

As further outlined in the Request for Comment, the Department's preference for calculating cost of manufacture over the entire POI or POR is premised on the assumption that averaging costs over this longer period tends to result in a "normalized" weighted-average cost that can reasonably be compared to sales prices covering the same extended period of time. 7/ As stated in Carbon and Certain Alloy Steel Wire Rod from Canada, the Department uses annual average costs "in order to even out swings in production costs experienced by respondents over

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6/ EC – Salmon, para. 7.232.

7/ Request for Comments, 73 Fed. Reg. at 26,364.

short periods of time. This way, we smooth out the effect of fluctuating raw material costs." 8/ In the Request for Comment, the Department also cites to factors such as "erratic production levels, the extent to which and how accurately monthly accruals are made, periodic maintenance, inventory methods, etc." as also affecting the timing and accuracy of per unit costing over shorter periods of time. 9/ The Department has also cited predictability and consistency as further factors supporting the presumption in favor of period-wide averages. 10/ We endorse this general preference for use of period-wide averages where prices actually fluctuate on a short-term basis during the POI or POR for the reasons articulated by the Department. However, as more fully discussed herein, this presumption must be rebuttable and must not be applied where prices exhibit significant longer-term trends during the POI or POR.

It bears emphasizing at the outset that the methodologies under consideration here are exceptional, and the circumstances calling for their application are likely to arise only infrequently in practice. As further discussed below, it is our position that the monthly or quarterly cost averaging periods will normally be justified only in situations where there are sustained changes in costs that exceed at least 25% per annum. Such dramatic cost increases are rare. Therefore, the use of shorter cost periods advocated herein is likely to be infrequent.

8/ 71 Fed. Reg. 3822 (Dep't Commerce)(Jan. 24, 2006)(final results of administrative review)(Issues and Decision Memorandum: Comment 5).

9/ Request for Comments, 73 Fed. Reg. at 26,265 (citing Color Television Receivers from the Republic of Korea, 55 Fed. Reg. 26,225, 26,228 (Dep't Commerce)(Jun 27, 1990)(final results of administrative review)(where the Department stated that the use of quarterly data would cause aberrations due to short-term cost fluctuations); Grey Portland Cement and Cement Clinker from Mexico, 58 Fed. Reg. 47,253, 47,257 (Dep't Commerce)(Sep. 8, 1993)(where the Department explained that the annual period used for calculating costs accounts for any seasonal fluctuation which may occur as it accounts for a full operation cycle.).

10/ Request for Comments, 73 Fed. Reg. at 26,364.

C. Standards That Have Been Adopted by the Department in Other Cases

Commerce has recognized its authority to use shorter costing periods where circumstances warrant. The limited cases in which the Department has exercised this authority fall into different categories. First, the Department has exercised this authority with respect to high technology products – in particular, semiconductors - that experienced "significant and consistent cost and price changes over a short period of time." 11/ In such cases, the significant and consistent cost and price changes were the result of technological advancements and changes in production processes. 12/

A second, similar, category of cases is represented by the Department's determination in Brass Sheet and Strip from the Netherlands, 65 Fed. Reg. 742 (Dep't Commerce)(Jan. 6, 2000)(final results of administrative review), in which the Department was able to make a "contemporaneous comparison of metal values and sales prices" which the Department describes as having "resulted in a more accurate calculation of the dumping margin in that instance because the respondent treated the cost of the input metals as a pass-through to its customers in its normal books and records." 13/ In that case, the cost of metals was shown to represent a "significant percentage of the total cost of producing brass sheet and strip, the cost of the metal inputs dropped consistently and significantly throughout the POR, and prices and costs

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11/ Request for Comments, 73 Fed. Reg. 26,365 (citing Static Random Access Memory Semiconductors from Taiwan, 63 Fed. Reg. 8909m 8926 (Dep't Commerce)(Feb. 23, 1998)(where the Department determined that quarterly, rather than annual, averages resulted in a more accurate comparison of pricing behavior during the period of investigation given the significant decrease in price and cost of static random access memory semiconductors throughout the POI); Erasable Programmable Read Only Memories form Japan, 51 Fed. Reg. 39,680, 39,685 (Dep't Commerce)(Oct. 30, 1986)(where the Department found that significant changes in the COP during a short period of time due to technological advancements and changes in the production process justified the use of quarterly weighted-average costs).

12/ Id.

13/ Request for Comments, 73 Fed. Reg. at 26,366.

for the shorter periods could be accurately matched." 14/ The Department concluded that monthly cost reporting was appropriate in response to the declining costs of these metal inputs in that case:

> In applying these criteria to this case, we have reviewed the information on the record and note that both OBV's sales prices for the subject merchandise and the cost of metal used in the manufacture of this merchandise correspondingly and consistently declined during the POR. Specifically, our analysis of data from the LME identifies a significant drop in metal values. In this case, we have determined that computing a single POR weighted-average cost would distort the results of the cost test because: (1) the cost of copper and zinc are treated as pass-through items when brass is sold to customers; (2) these metal costs represent a significant percentage of the total cost of producing brass sheet and strip; and (3) the cost of the metal dropped consistently and significantly throughout the POR. To avoid this distortion, we have relied upon monthly weighted-average costs rather than calculating quarterly or a single weighted-average POR cost for metal. 15/

As the Department explained, the problem with using the standard annual POR average costs in such circumstances is that it will create fictitious results:

> As a result of using the normal POR average cost methodology, the decline in metal prices would tend to create below-cost sales when the LME metal price falls below the weighted-average LME POR price . . . . Hence, in this review, the method of calculating metal costs does have an impact on the comparison used in the margin calculations. For example, and as noted by the petitioner, the normal cost methodology could create fictitious profits (or losses) on home market sales. 16/

For example, assume the respondent priced its products at a healthy margin above its monthly cost in each month of the POR by fully passing monthly increases in raw material

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14/ Id.

15/ Brass Sheet and Strip from the Netherlands, 65 Fed. Reg. at 747 (comment 2).

16/ Id.

costs to its customers. The Department would presumably agree that the sales in question were profitable when sold. The rationale applied in Brass Sheet and Strip from the Netherlands recognizes that arbitrarily comparing monthly prices to a POR average costs under these circumstances will artificially create losses in months of the POR in which monthly costs are low, and will artificially create profits in months of the POR in which monthly costs are high, thus entirely distorting the cost-price comparison.

It bears emphasizing that this type of distortion does not arise (or does not arise to a significant enough degree) in "normal" market circumstances in which raw material costs are relatively stable and/or experience only minor or random fluctuations over the period of review. 17/ Under normal circumstances, as noted above, the smoothing out of cost fluctuations by the use of POR averages does not substantially distort the price/cost comparison. However, this rationale breaks down completely in circumstances, such as those identified in Brass Sheet and Strip from the Netherlands and similar cases, where there has been a sharp and consistent change in costs and those costs are being passed on to customers. In these such cases, as the Department has found, comparing monthly prices to annual costs leads to serious distortions and inaccuracies.

The Department's decision in Certain Pasta from Italy 18/ is instructive here. In that case, the respondents contended that the fluctuating price of semolina warranted the use of cost reporting on a monthly basis because semolina comprised a substantial portion of the total

17/ We note that the Court of International Trade ("CIT") upheld the Department's rejection of monthly cost reporting in Fujitsu Gen. Ltd. v. United States, 19 C.I.T. 359 (CIT 1995). However, it is notable, and consistent with the argument presented herein, that the CIT based its decision on the fact that Fujitsu had "produced no persuasive evidence to substantiate its claims that its COPs were declining at a significant rate." Fujitsu, 19 C.I.T. at 367.

18/ 65 Fed. Reg. 77,852 (Dep't Commerce)(Dec. 13, 2000)(final results of administrative review).

cost of manufacturing and therefore was a "single-primary input product." 19/ The Department ultimately rejected the use of monthly raw material prices, finding unpersuasive the respondents' contention that the price fluctuations were steady or significant. The Department summarized its practice with respect to raw material cost reporting by stating,

> [p]reviously, the Department has used monthly or quarterly costs in instances of non-inflation only when there is a single-primary input product and that input experiences a significant and consistent decline or rise in its cost throughout the reporting period . . . Conversely, when there are inconsistent fluctuations in both directions we use a single weighted-average cost for the entire POR. 20/

In reference to the specific facts of the case, the Department noted, "the consistency of the variation in costs is questionable since the price decline only existed for six months and then reversed direction." Further, in support of its reasoning that an annual average cost is appropriate where there are fluctuations in both directions, the Department cited Fujitsu General Ltd. v. United States, 88 F.3d 1034, 1038-39 (Fed. Cir. 1996) ("where the court noted no significant rise from the beginning to the end of the POR and approved costs constructed on an annual basis"). 21/ In Fujitsu, the Federal Circuit upheld the Court of International Trade's decision to uphold the Department's use of annual costs 22/ because "no persuasive analysis, if any, was provided to show that any such declines, viewed over the full review period, had any statistical significance, particularly in light of the October increases in COP." 23/

19/ Id.

20/ Id.

21/ Id.

22/ See infra at note 6.

23/ 88 F.3d at 1039.

In other cases where the Department has denied requests for shorter cost averaging periods, the Department has principally focused on two factors: (1) whether the cost changes throughout the POI/POR were significant; and (2) whether sales during the shorter averaging periods could be accurately linked with the COP/CV during the same shorter averaging periods. 24/ In those more recent investigations, the Department analyzed the significance of the cost changes throughout the POI/POR by "conducting a comparative COM analysis between the annual average cost method and the suggested shorter period average cost method (e.g., quarterly cost averaging period). In comparing costs under the two methods, the Department examined the five most frequently sold models of the foreign like product (control numbers) in the comparison market. For each of the five models, the Department compared the difference between the annual average COM (entire COM, not for a particular input) and the shorter period average COMs. 25/ The Department in those cases also looked at how closely the shorter cost averaging period was linked with the COP of the shorter period, taking into consideration case-specific factors such as the raw material inventory turnover period, the inventory valuation method used, the extent to which raw materials are purchased pursuant to long-term contracts, erratic production levels during the year, sales made pursuant to long-term contracts, the extent to which monthly accruals are made, and year-end adjustments. 26/ In the Request for Comment the Department has stated that "we believe it is necessary for a respondent

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24/ Id. (citing Steel Concrete Reinforcing Bars from Turkey, 70 Fed. Reg. 67,665 (Dep't Commerce)(Nov. 8, 2005)(final results of administrative review); Carbon and Certain Alloy Steel Wire Rod from Canada, 71 Fed. Reg. 3822 (Dep't Commerce)(Jan. 24, 2006)(final results of administrative review); Stainless Steel Sheet and Strip in Coils from France, 71 Fed. Reg. 6269 (Dep't Commerce)(Feb. 7, 2006)(final results of administrative review).

25/ Request for Comments, 73 Fed. Reg. at 26,366.

26/ Id.

to provide evidence on the administrative record of a direct linkage between resulting costs and sales prices before we consider" using shorter cost averaging periods. 27/ The Department also noted the methodology to determine the existence of the linkage that applied in the remand determination involving Turkish rebar, in which the Department calculated and analyzed the consistency of profit percentages for each shorter averaging period. 28/

D. General Position

Having examined the statute and regulations, court cases addressing the issue, WTO case law, and the Department's recent practice, we have arrived at the following general conclusions for the Department's consideration:

Identifying Significant Changes in Cost

- The Department should retain a general presumption in favor of period-wide averages. We endorse the normal preference for use of period-wide averages where costs and prices may fluctuate on a short-term basis during the POI/POR. This default methodology is appropriate in such circumstances for the reasons articulated by the Department; doing so smoothes out the effect of fluctuating raw material costs and erratic production levels, appropriately takes into account monthly accruals, periodic maintenance, inventory methods, and provides predictability and consistency.

- The Department should not require perfect consistency in trends where monthly averaging periods are at issue. As at least one NAFTA panel has previously found, it is not reasonable for the Department to require absolute lock-step consistency where month-to-month averaging periods are at issue. See In the Matter of Carbon and Certain Alloy Steel Wire Rod from Canada, USA-CDA-2006-1904-04 (Nov. 28, 2007) at 51-52. If there is a clear cost trend during the period, minor variations should be disregarded. Given the more limited number of averaging periods, consistent trends may be more appropriate where quarterly periods are at

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27/ Id.

28/ Id. (referencing Redetermination Pursuant to Court Remand, Habas Sinai ve Tibbi Gazlar Istihsal ve Endustrisi A.S. v. United States, Court NO. 05-00613, Slip Op. 07-167 (CIT Nov. 15, 2007)(March 3, 2008).

issue, unless there is evidence of a change in trends during the period (see below).

- The Department should recognize the marketplace reality that sustained changes in cost may not coincide perfectly with the Department's period of investigation/review. Cases may arise where the period of review/investigation spans more than one trend. Further, a trend may extend forwards or backwards in time relative to the administrative investigation or extended review period. The existence of multiple sustained trends during an investigation or an extended review period should not be mistaken as evidence of "fluctuations." Six months would be a reasonable minimum period of time over which to establish the existence of a sustained trend.

- The Department should presume changes are significant if they exceed 25 percent on an annualized basis. Although no standard should be applied without exception, we believe that any changes in costs exceeding 25 percent on an annualized basis should rebuttably be presumed to be "significant." The 25 percent threshold has been an established benchmark for the Department's application of "high inflation" calculation methodologies 29/ where similar considerations of possible distortions in the cost/price comparisons are at issue.

Linkage Between Costs and Prices

- The Department should presume the existence of linkages. As a matter of basic economics and of commercial reality, prices usually follow costs in competitive markets. Accordingly, the Department should reasonably presume that significant cost changes are linked to changes in pricing provided that the direction and magnitude of the changes are the same. ~~Establishing overly difficult evidentiary burdens on respondents to~~ establish such linkage will lead to excessive rejection of meritorious claims for shorter cost averaging periods and should be avoided. The Department's analysis of linkage should accordingly focus on factors that may suggest that such a linkage does not exist in a specific case – as for example, where there are observable contradictory trends in costs and prices, or where prices and costs are impacted differently by changes due to long-term contracts, hedging, or other mechanisms that interfere with the normal economic interplay between costs and prices.

29/ See, e.g. Import Administration: Antidumping Procedures Manual, Ch. 8 at 77-78 (Jan. 22, 2007), available at http://ia.ita.doc.gov/admanual/index.html (noting that the "25% rate has been used as a general guide for assessing the impact of inflation on AD investigations and reviews.").

- The Department should take into account any standard pricing mechanisms in the industry such as "surcharge" mechanisms. Certain industries, such as the flat-rolled stainless steel industry in North America, have established standard metals surcharges that are automatically and uniformly applied to sales prices and are updated on a regular basis to reflect changes in raw material and energy costs. In such cases, the Department should accept such evidence as prima facie establishing the required linkage between costs and prices.

II. RESPONSES TO THE DEPARTMENT'S QUESTIONS

Responses to the specific questions posed by the Department in its Federal Register notice are as follows:

(i) Are there other factors relevant to the consideration of whether and when to rely on shorter cost averaging periods besides significant cost changes and the linking of sales and costs during the same shorter period? If so, identify the factor(s) and explain in detail why such factor(s) should be considered.

Response: We agree that, in general, the principal factors relevant to the consideration of whether and when to rely on shorter cost averaging periods are: (1) significant cost changes; and (2) the linking of sales and costs during the same shorter period. However, we also note that because there is great variation among industries and market conditions may change over time, the Department should make its determinations regarding cost reporting periods on a flexible, case-by-case basis. The Department must consider the specific facts of the respondent and the industry in which the respondent operates, rather than limiting itself strictly to these two factors. In addition, as discussed elsewhere herein, the Department should exercise flexibility in the application of these two criteria.

(ii) How should the significant cost changes factor be analyzed and what numeric threshold should we rely upon as a basis for resorting to shorter cost averaging periods? Provide the basis for your suggested threshold number. Should the nature of the industry (e.g., steel, consumer electronics, perishable products, etc.) affect the analysis? If so, explain in detail how the analysis would be affected.

Response: As a preliminary matter, the Department should not require perfect consistency in trends where monthly averaging periods are at issue. In at least one recent case a

NAFTA panel found that it was "not persuaded" and that it was "unreasonable" for the Department to require that changes in cost have to be in the same direction in each and very month of the period. 30/ We do not believe it is realistic for the Department to require absolute consistency where month-to-month averaging periods are at issue. If there is a clear cost trend during the period, minor variations in one or a few months, should be disregarded. We suggest that the Department may employ standard statistical techniques (e.g., performing linear regression and establishing a trend line) to confirm the general consistency of the cost trend during the period. The Department could also consider whether cost values alternate above and below the average cost value, or tend to be above or below the average cost based on whether they are at the beginning or the end of the observed cost trend. The former would be more indicative of normal fluctuations while the later would be more indicative of a trend. Given the more limited number of averaging periods, consistent trends may be more appropriate where quarterly periods are at issue, unless there is evidence of multiple trends during the period.

Second, given the arbitrary nature of investigation and administrative review periods, cases may arise where the period in question spans more than one trend. Upward trends, downward trends, and/or stable trends may be evident within an investigation period or extended review period. While an investigation period for a market economy proceeding will be 12 months in length, an extended review period might last from 17 months to as many as 24 months for a first review. Further, a trend may extend forwards or backwards in time before or after the investigation or extended review period. The existence of multiple sustained trends during an investigation or an extended review period should not be mistaken as evidence of "fluctuations."

30/ See In the Matter of Carbon and Certain Alloy Steel Wire Rod from Canada, USA-CDA-2006-1904-04 (Nov. 28, 2007) at 51-52.

Third, six months would be a reasonable minimum period of time over which to establish the existence of a sustained trend. A recession is commonly defined as two consecutive quarters (i.e., six months) of negative growth in gross domestic product (GDP). 31/ We note that six months is also the length of time over which the Department considers contemporaneous model matches in an administrative review.

Lastly, in answer to the Department's specific question, in determining how to analyze the significant cost changes factor and what numeric threshold should be relied upon, the Department should look to its prior analysis in the context of economies experiencing high and hyperinflation in which the Department established numerical thresholds for determining the existence of high inflationary economies at 25% per annum, respectively. 32/ Given the similarity of concerns – the potential distortion of price and cost comparisons due to changes in prices, we suggest that the Department may reasonably rely on the same numerical thresholds as a rebuttable basis for resorting to shorter cost averaging periods. We also note, however, that any numerical threshold the Department decides to use should be flexible and responsive to case-specific facts. In certain situations, a lower numeric threshold might be sufficient to trigger the need for shorter cost reporting periods.

In addition, we agree that the nature of the industry should affect the analysis, as has been recognized by the Department's prior practice in the context of highly dynamic industries such as semiconductors, perishable products, and certain metal products. Such determinations to deviate from the normal 25% standard would need to be made on a case-by-case basis

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31/ See http://www.econterms.com/glossary.cgi?query=recession (last accessed June 22, 2008)

32/ See, e.g. Import Administration: Antidumping Procedures Manual, Ch. 8 at 77-78 (Jan. 22, 2007), available at http://ia.ita.doc.gov/admanual/index.html (noting that the "25% rate has been used as a general guide for assessing the impact of inflation on AD investigations and reviews.").

considering evidence presented by the parties to the proceeding regarding cost patterns and pricing practices in the industry in question.

(iii) How should the correlation between prices and shorter cost averaging periods be analyzed to reasonably assess that the prices and shorter period average costs are accurately linked?

Response: As a matter of basic economics and of commercial reality, prices tend to follow costs in competitive markets. Accordingly, the Department should reasonably presume, on a rebuttable basis, that significant cost changes are also linked to changes in pricing. 33/ Establishing overly difficult evidentiary burdens on respondents to establish such linkages (which may be difficult to prove in practice) will inevitably lead to excessive rejection of otherwise meritorious claims for shorter cost averaging periods and should be avoided. The Department's analysis of cost/price linkages should accordingly focus on the negative – i.e., on factors that may evidence that such a normal linkage between costs and prices does not exist in a specific case – as for example, where prices or costs may in fact be impacted differently by consistent changes in the period due to the existence of long-term contracts, hedging arrangements, or other mechanisms that interfere with the normal economic interplay between costs and prices.

In evaluating the linkage between costs and prices, the Department should also take into account any standard pricing mechanisms in the industry or market such as a standard "surcharge" mechanism that links costs and prices. Certain industries, such as the flat-rolled stainless steel industry in North America, have established standard metals surcharges that are automatically and uniformly applied to sales prices and are updated on a regular basis to reflect

33/ On a case-by-case basis, the Department may determine on the basis of the evidence presented that an appropriate lagging of price and costs should be accounted for.

changes in raw material and energy costs. 34/ In such cases, the Department should accept such evidence as prima facie establishing the required linkage between costs and prices. 35/

We also agree that the Department should consider any other relevant evidence identified by the Department as potentially bearing on the precise relationship between cost changes and price including the raw material inventory period, the inventory valuation method used, the extent to which raw materials or sales prices are established by long-term contracts, and erratic production levels throughout the year. Such factors, though relevant, are not susceptible to a single rule applicable in all cases and must be considered in the context of the particular respondent, market, and industry. In some cases, evidence such as that pertaining to inventory valuation systems and periods may not be directly relevant to establishing linkage itself but rather may be important in determining the timing of the linkage and possible necessity for a particular lag in matching costs and prices.

The existence of monthly accruals and adjustments need to be considered as well. Consistency must be maintained in the time period to which these items relate and the time period to which these items are applied. For example, an annual adjustment should continue to be absorbed on the costs throughout the full period of investigation or review, and not just the

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34/ See, e.g., Stainless Steel Sheet and Strip from Mexico, Stainless Steel Sheet and Strip from Mexico, 70 Fed. Reg. 3677 (Dep't Commerce)(Jan. 26, 2005)(final results of 2002-2003 administrative review)(Issues and Decisions Memorandum: Comment 8).

35/ While the Department correctly determined to use monthly costs in Brass Sheet and Strip from the Netherlands, 65 Fed. Reg. 742, 747 (Dep't Commerce)(Jan. 6, 2000)(final result so administrative review(comment 2)("Brass Sheet and Strip from the Netherlands"), the unique circumstances at issue in that case make it an inappropriate benchmark for future cases. In that case, there was a direct contractually-based pass-through of the metals cost to the customer, essentially reducing the manufacturing cost to the cost of fabrication. While such an extreme example meets the standard for "linkage," it is unrealistic, and unnecessary, to require such a level of linkage in other cases where it is otherwise demonstrated that there is a general or indirect linkage between rising (or declining) costs and rising (or declining) prices in the period.

costs for a shorter period of time such as the specific month or quarter in which that item is recorded.

Lastly, we believe that an analysis comparing profit levels from period to period, as was apparently conducted in the Rebar from Turkey remand decisions, may be appropriate. However, in doing so, the Department must not rigidly seek perfect consistency in profit rates from month to month. Some fluctuation in profit levels is to be expected in any marketplace and industry. In conducting this type of profit analysis, the Department should therefore make case-by-case determinations (perhaps informed by market analysis conducted by the International Trade Commission in its original injury investigation and/or in subsequent sunset reviews) with regard to a reasonable range of normal profit levels.

(iv) Should it matter whether costs are trending consistently up, consistently down, or up and down throughout the POI/POR in the decision to use shorter cost averaging periods? Explain in detail why or why not.

Response: We agree with the Department that when there are not observable cost trends in either direction, there is no justification for using shorter cost averaging periods. The Department should not, however, require a perfect, complete month-to-month trend in the same direction. The Department should look for a clear, observable trend, but a slight deviation in a small number of months should not prevent the use of shorter cost averaging periods. As noted above, in at least one recent case a NAFTA panel found that it was "unreasonable" for the Department to require that changes in cost have to be in the same direction in each and very month of the period. It is not realistic for the Department to require absolute consistency where month-to-month averaging periods are at issue. If there is a clear cost trend during the period, minor variations should be disregarded.

Likewise, given the arbitrary nature of investigation and administrative review periods, cases will arise where more than one sustained cost trend might exist during the period in question. For example, a period might span two trends – one upward, and one downward. In such cases, it may be appropriate for the Department to use monthly or quarterly costs for the period of investigation/review. Such circumstances should not be mistaken as evidence of "fluctuations." See our response to item (ii) above for additional discussion on this point.

(v) ***If shorter cost averaging periods are used based on the argument that it is distortive to rely on a single average cost when costs have changed significantly throughout the year, should the recovery of cost test be modified in any way? That is, should sales that are below the shorter cost averaging period still be considered to provide for the recovery of costs within a reasonable period time if they are above the annual average cost? See section 773(b)(2)(D) of the Act.***

Response: The recovery of cost test may not lawfully be modified in any way. As noted above, the statute, 19 U.S.C.§ 1677b(b)(2)(D), states that:

> If prices which are below the per unit cost of production at the time of sale are above the weighted average per unit cost of production for the period of investigation or review, such prices shall be considered to provide for recovery of costs within a reasonable period of time.

(emphasis added). This language is mandatory, requiring the comparison to be made to the entire period of investigation review. This provision reflects the requirements of the second sentence of Article 2.2.1 of the WTO Antidumping Agreement, which likewise states that "[i]f prices which are below per unit costs at the time of sale are above weighted average per unit costs for the period of investigation, such prices shall be considered to provide for recovery of costs within a reasonable period of time." In a recently-adopted report, a WTO dispute settlement panel held that while the investigating authorities have discretion to utilize shorter averaging periods to determine if transaction prices are below cost at the time of sale (the first step in the analysis), the investigating authorities may accept that prices that are above per unit costs on a period-wide average basis allow for recovery of costs within a reasonable period of time, irrespective of the use of shorter time periods for the initial determination of whether the sales are below cost. 36/

Given these circumstances, we see no plausible legal basis for the Department to determine that sales that are at prices that are above period-average costs do not allow for recovery of costs within a reasonable period of time. That having been said, there is nothing in the U.S. statute or the WTO Antidumping Agreement that would preclude the Department from additionally making affirmative determinations that cost recovery is met on the basis of other factors or time periods. In particular, we note that under certain circumstances growing periods or product development periods, additions of new equipment, and other factors affecting period costs may suggest that cost recovery is being met even where the standard year-long period average cost recovery test is not met. Such determinations should be made on a case-by-case basis on the basis of evidence and argument presented by the parties.

(vi) To what extent should the costs from the window periods in reviews affect the overall analysis?

Response: We assume that by "overall analysis" the Department is referring to the evaluation of whether or not there is a need to move to shorter cost periods. In the context of administrative reviews, the Department has historically focused primarily on cost trends during the relevant POR.

The Department's cost test in administrative reviews evaluates sales throughout the extended period of review against cost of production. The extended POR includes an additional five months of sales during two wing periods, thus increasing the extended review period from 17 months (in a standard review) to as many as 24 months (in a first review). Thus, the wing periods can account for 20 to 29 percent of the full extended review period. If an increase or

36/ EU – Salmon, paras. 7.232, 7.233.

decrease in costs spans one or both of the wing periods, the potential distortion to the cost test results and the overall margin are the same as if the trend exists during the POR. Therefore, the Department should consider costs from the window periods in its overall analysis.

(vii) If we were to gather information at the outset of every segment of a proceeding in order to determine early on whether a respondent needed to provide cost information for shorter cost averaging periods, what information should we request? Provide specific questions that could be incorporated into the section A questionnaire.

Response: The Department should collect certain data at the outset of every segment of a proceeding (i.e., in the initial questionnaire response) in order for the Department, and other interested parties, to determine early in the investigation or review whether a respondent needs to provide cost information for shorter cost averaging periods. In doing so, the Department should retain the flexibility to ask additional questions to consider the evidence on a case-by-case basis. We also recommend that the Department consider a multi-step approach – first, as a threshold matter, to ascertain whether the circumstances support further inquiry into the possible use of shorter reporting periods, and second, to obtain more detailed information, including monthly and quarterly cost data where such circumstances exist.

Possible standard questions to be included in Section A of the questionnaire that would provide the Department with the information necessary to make the threshold determination concerning further inquiry might include the following:

- *If you experienced a sustained increase/decrease in cost of manufacturing or a significant component of costs during the period of investigation/review of more than 50% on an annual basis, document and quantify the increase/decrease in costs and contact the official in charge. In your Section D response, please provide the cost of production data on a POI/POR-average basis, a quarterly basis, and a monthly basis. Include in your narrative response an explanation of how the monthly/quarterly costs were calculated.*

- *Did you experience a sustained increase/decrease in cost of manufacturing of between 25% and 50% on an annual basis, or a sustained increase/decrease in a significant component of costs during the period of investigation/review of* *between 25% and 50% on an annual basis? If so, document and quantify the increase/decrease in costs and contact the official in charge.*

- *If the cost of manufacture or a significant component of costs did not increase/decrease by at least 25% on an annual basis during a sustained portion of the period of investigation/review but you believe a shorter cost averaging period is nevertheless appropriate, please explain the basis for your claim in full, document and quantify the increase/decrease in costs, and contact the official in charge. Provide the cost of production data submitted with your Section D response on a POI/POR-average basis, a quarterly basis, and a monthly basis. Include in your narrative response an explanation of how the monthly/quarterly costs were calculated.*

If the respondent reports sustained increases/decreases of costs exceeding 25% during the POR (or the respondent or another party otherwise proposes reporting costs on the basis of a shorter averaging period), the Department should require answers to the following additional questions in the context of the respondent's Section D response:

- *With respect to the items that increased/decreased significantly in cost during the POI/POR please provide the following information:*
  - *the identity of the input;*
  - *the sources of the input;*
  - *the average percentage of COM the input represents;*
  - *whether the input was purchased pursuant to long-term contracts;*
  - *a monthly index showing the purchase price of the input over the POI/POR;*
  - *any public data (e.g., published price indices) for the input;*
  - *any narrative explanation (with supporting documentation, if available) describing the circumstances;*
- *Please explain whether price changes in the home market are linked to changes in cost of production (e.g., through use of price surcharges for changes in input prices). Provide supporting documentation, if available.*
- *Please identify the inventory valuation system (e.g., LIFO or FIFO) used for raw materials.*

- *Please provide any additional information that you believe is relevant for the Department to evaluate the increase/decrease in costs experienced during the POI/POR.*

(viii) Should shortening the cost averaging period affect price comparisons? For sales comparison purposes, should prices be compared across cost-averaging periods?

Response: We do not believe that shortening the cost averaging period should affect the manner in which price comparisons are selected. As noted above, the below-cost test is focused on determining whether home market sales were made in the ordinary course of trade and can be used to determine normal value. That question has no bearing on how price comparisons are made across markets. In the case of original investigations, the Department is normally obliged to compare weighted-average prices in both markets. Therefore, there is a built-in symmetry in the comparisons, and the problem of comparing across cost-averaging periods does not arise.

The question is seemingly more complicated in the case of administrative reviews where individual export transactions are compared to monthly normal values and it is therefore possible that the application of the Department's normal matching hierarchy may result in some comparisons across cost averaging groups. However, in reality this problem, to the extent it occurs, is not significantly different from the normal complications that arise in any case in which, by application of the Department's six-month contemporaneity rule, the Department compares export prices in one month to a monthly weighted-average normal value in a different month within the window. We note that price comparisons are statutorily preferred over normal value based on constructed value. 37/

37/ Ball Bearings and Parts Thereof from France, Germany, Italy, Japan, and the United Kingdom, 71 Fed. Reg. 40,064 (Dep't Commerce)(July 14, 2006)(final results of administrative review)(Issues and Decision Memorandum: Comment 15)(noting that "[t]he statute has a clear preference for price-to-price comparisons").

(ix) *Are there other points you deem relevant to the issue at hand?*

Response: We also submit for the Department's consideration that the determination to utilize monthly or quarterly cost averaging periods may be justified for certain clearly identified categories of subject product. For example, where a particular series or grade of product within the broader class or kind of merchandise subject to investigation/review experienced significant cost changes during the period, it may be appropriate to restrict the use of shorter cost averaging periods to the particularly affected category. A possible example of such a circumstance is with respect to stainless steel products where "austenitic" grades of stainless steel (i.e., AISI 300 series grade material) that incorporates a substantial amount of nickel is particularly vulnerable to changes in the underlying global price of nickel, whereas "ferritic" and "martensitic" grades of stainless steel (i.e., AISI 400 series grade material) does not contain significant nickel and would be unaffected by such changes. In such a situation, if changes in nickel prices are associated with significant changes in the cost of raw materials used to produce 300 series stainless steel, the Department would be justified in using the shorter averaging periods solely for the 300 series product.

* *

Please do not hesitate to contact the undersigned if there are any questions concerning this matter.

Respectfully submitted,

HOGAN & HARTSON L.L.P.

By: ____________________
Craig A. Lewis