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Affiliated Party Sales
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VIA MESSENGER

Mr. 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, DC 20230

Re: Comments on Affiliated Party Sales

Dear Mr. Shirzad:

On behalf of the Government of the Republic of Korea (“Korea”), we submit the following comments in response to the Department’s request concerning a proposed modification in determining whether sales to affiliated parties are in the ordinary course of trade, and thus may be used in the calculation of normal value. See, 67 Fed. Reg. 53339 (Aug. 15, 2002). These comments are timely submitted within the deadlines specified in that Federal Register notice.¹

¹ As the U.S. Government is aware, Korea submitted third party comments to the dispute settlement body on this issue. See Submission of Korea as a Third party, WT/DS184 (31 July 2000).

Introduction

The Department currently calculates a weighted-average ratio for each affiliated customer which is an accumulation of comparisons of weighted-average selling prices for each product to the affiliated customer, compared to the weighted-average prices to all unaffiliated customers for the same product. In those instances where the Department does not have an identical product sold to both affiliated and unaffiliated customers, the Department assumes that sales of the specific product are not at arm's length and assigns a zero ratio to sales of that product when calculating the weighted-average ratio.² The Department will include sales to an affiliated party in the calculation of normal value only if the weighted-average ratio for the specific affiliated customer is greater than 99.5 percent. Where the Department has rejected sales to an affiliated party because it has determined through the application of the 99.5 percent test that these sales are not in the ordinary course of trade, the Department may require the respondent to report the sales by the affiliate to its downstream customers.

The WTO Appellate Body has rejected the Department's current methodology because its approach is not applied in an "even-handed" manner. 67 Fed. Reg. 53340. The Department's ratio rejects all 'low priced?' sales to affiliated parties but will eliminate very high priced sales only if the respondent demonstrates that the sales are so unusual that they are clearly not in the ordinary course of trade. In practice, the Department has rarely eliminated such high-priced sales. Accordingly, to comply with the WTO ruling, the Department has proposed to modify the test, but in only one respect. Specifically, the Department proposes to modify its reliance on a single bright line, the 99.5 ratio, and replace it with a band of 98 to 102 percent. All other aspects of the Department's calculation would remain unchanged. 67 Fed. Reg. 53340. That is to say, if the weighted-average ratio for an affiliated customer is less than or equal to 98 or

² Alternatively, the Department assumes all sales to the affiliated customer are not at arm's length.

alternatively, greater than or equal to 102, the Department would eliminate all sales to the affiliated customer, and the Department would instead require the respondent to report the affiliated party's resales which would be used in the normal value calculation.

Discussion

The Department's proposal does not fully address the concerns raised in the World Trade Organization's ("WTO") decision, because many of the distortions inherent in the Department's original methodology remain unaddressed and therefore unresolved in the proposed revision. As Korea stated in its submissions to the WTO, we do not object to the application of a test for affiliated parties, per se, but object to a test that is arbitrary and does not fairly compare certain sales. We urge the Department to revise the arm's length test to eliminate these lingering concerns, and provide some suggestions of how the Department can address them.

The Department's reliance on a single fixed ratio fails to recognize the variability in the underlying data and thus fails to reflect commercial reality. There are many reasons that prices of the same products to affiliated customers could vary from prices to unaffiliated customers, where the affiliation has played absolutely no role in setting the price. For example, a producer could sell to an affiliated and an unaffiliated customer at exactly the same price. However, over time, its prices could decline, reflecting for example, reduced material costs. Over the course of a year, the affiliated customer might purchase the bulk of its products during the latter part of the year (during a lower price period), while the unaffiliated customer might purchase the bulk of its products during the early (and higher priced) portion of the year. Simply due to changes in prices over time, and the periods in which the customer purchased the products, the weighted-average price to an affiliated customer in this scenario would appear to be less than the price to the unaffiliated customer, although at any point in time the prices to the two customers were identical. The ratios to determine if sales to affiliated parties are outside the ordinary course of trade are calculated in a vacuum with no regard for other key factors that play a key role in determining the price such as volume, time of purchase, or type of contract.

In modifying the arm's length test to use a range of ratios, rather than a single ratio, to

determine whether to use sales to affiliated parties in the calculation of normal value, the Department's current proposal makes no attempt to correct the underlying deficiencies in relying on the ratio to make the determination whether sales to affiliated parties are in the ordinary course of trade. Moreover, as the Department has recognized, the test would potentially result in the exclusion of an even larger number of direct sales to affiliated parties from the calculation of normal value, causing additional distortion in the Department's calculation.

We would propose two possible changes or modifications to the Department's proposal. First, the Department should consider broadening the band to, perhaps, to 95% to 105%. This appears to be one of the approaches that the Department examined in reaching its proposal. As noted above, and as the Department itself concedes in its Federal Register notice, the Department's new, proposed test might actually result in using sales to affiliates less frequently. Not only does this undermine the intention of the WTO decision, it also runs contrary to the Department's stated concern "that the band not be overly narrow." The Government of Korea believes that a broader band is capable of being administered by the Department, presents no more potential for manipulation than the proposed band, and is a more just and commercially realistic test.

Second, the Department new methodology should establish some means of conducting a more systematic examination of sales to affiliated parties to determine whether such sales are in the ordinary course of trade. Such an examination must include all components of the transaction, including product mix, timing of the sales, and examination of the specific products at issue. The examination should at a minimum compare prices at similar points in time. Alternatively, although the Department would not correct the inherent deficiencies in relying on the ratio it now calculates, it could minimize the distortions in its analysis by eliminating the calculation of a weighted-average ratio for determining whether to include all sales to affiliated

parties, and instead make the determination on a product-specific basis. Under this methodology, the Department would continue to use sales of specific products to affiliated parties that are within the 98-102 ratio (or the 95-105 ratio that Korea proposes), even if the weighted-average ratio were beyond these parameters.

Respectfully Submitted,

Haeng-Kyeom Oh
Minister for Economic Affairs
Embassy of the Republic of Korea