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Comments on Proposal Concerning
Test for Determining whether
Affiliated Party Sales Were
Made in the Ordinary Course of
Trade

Public Document

BY HAND

Honorable Faryar Shirzad
Assistant Secretary for Import Administration
United States Department of Commerce
Central Records Unit, Room 1870
Pennsylvania Ave & 14th St., N.W.
Washington, DC 20230

Re: Affiliated Party Sales

Dear Assistant Secretary Shirzad:

We are writing, on behalf of the Arcelor Group, to comment on the Department's recent proposal to modify its practice for determining whether sales to affiliated customers in the comparison market should be included in the calculation of normal value.

We believe that a review of the Department's practice on this issue is long overdue. The Department's previous practice established improperly narrow standards for using sales to affiliates at prices that were lower than the average prices for sales to unaffiliated customers — while at the same time including all sales to affiliates at higher-than-average

prices. We believe that the modified methodology proposed by the Department represents a significant improvement. However, a few problems remain.

In particular, we are concerned that, the proposed methodology may prove impermissibly narrow in circumstances in which the sales to affiliated customers are “comparable” to sales made to unaffiliated customers. Moreover, there is a risk that the proposed methodology may create impossible burdens for respondents that have established extensive distribution networks in their home markets. As a result, it may become prohibitively expensive for such companies to respond to the Department’s questionnaires, even if they are confident that there has been nothing “unfair” about their pricing.

In order to avoid such an outcome, we would urge the Department to refine its methodology for determining whether sales to affiliates are in the “ordinary course of trade” in the following manner:

- ? The Department should include sales to affiliated customers in the comparison market in the calculation of normal value whenever it is demonstrated that the terms of those sales are equivalent to the terms of sales to unaffiliated customers.
- ? The existence of sales in commercial quantities to an unaffiliated customer at the same time and on the same terms as the sale to the affiliated customer should (in the absence of evidence that the sale to the unaffiliated customer was “fictitious”) constitute conclusive evidence that the sales to the affiliated customer were in the ordinary course of trade.
- ? Because of the inherent difficulties in attempting sale-specific comparisons (where sales may vary in terms, timing and market conditions), an overall approach may be necessary. In this regard, a “cushion” methodology better reflects the statutory requirements — because it ensures that the sales to affiliates are included in the analysis if, on average, their prices are within the range of prices for a reasonable proportion of the sales to unaffiliated customers. The Department’s proposed methodology — which simply compares the average

prices for sales to affiliated and unaffiliated customers — is less consistent with the statutory requirements, because it may result in the exclusion of sales to affiliates whose prices are equivalent to many (but not all) sales to affiliated customers.

- ? Even if the Department adopts an overall approach as a part of its analysis, it should not be then end of the analysis. For example, the Department might establish a *rebuttable* presumption that sales to affiliates that “fail” the overall test were not made in the ordinary course of trade. In order to comply with the statutory requirements, however, respondents should be given an opportunity to rebut that presumption, with appropriate evidence or analysis.
- ? The Department should establish reasonable reporting requirements for downstream sales by affiliated resellers, where the initial sale to the affiliated reseller is found to have been outside the ordinary course of trade. In particular, the Department must in each case consider whether the benefits of requiring that information (in terms of the accuracy of the results) outweigh the burdens of requiring that such sales be reported. If the Department concludes that the complete exclusion of the sales to affiliated resellers would lead to an inaccurate result, it should allow the respondent the option of not reporting downstream sales in any situations in which the prices for sales to affiliated resellers are higher than the prices for sales to unaffiliated customers.

In our view, without such modifications, the Department’s proposed methodology may fail to properly implement the statutory requirements, while imposing unnecessary and unrealistic burdens on the parties responding to its questionnaires.

1. The Department’s Methodology Should Result in the Inclusion of All Sales that Are Within the “Ordinary Course of Trade” under the Statute

As the Department is aware, the antidumping statute specifically provides that sales to affiliated U.S. customers may not be used in the calculation of export price and constructed export price.¹ The statute does not, however, contain any such prohibition on the use of sales to affiliated customers in the comparison market in the calculation of normal value.

¹ See Tariff Act of 1930, as amended, § 772(a) and (b); 19 U.S.C. § 1677a(a) and (b).

Instead, the statute provides only that normal value should, in the first instance, be based on the price at which the merchandise is “sold (or, in the absence of a sale, offered for sale)” in the comparison market “in the usual commercial quantities and in the ordinary course of trade.”² Under the statute, then, the sales to affiliated customers are not to be treated differently from sales to any other customers. If those sales are “in the usual commercial quantities and in the ordinary course of trade,” they should be included in the Department’s analysis.

Under the statute, a sale to an *unaffiliated* customer in the normal course of business is in the “ordinary course of trade” (unless, of course, it is excluded under the statutory provisions governing below-cost sales).³ It follows, then, that a sale to an *affiliated*

² See Tariff Act of 1930, as amended, § 773(a)(1); 19 U.S.C. § 1677b(a)(1). The relevant provision also indicates that the home-market sales used to establish normal value should also be, “to the extent practicable, at the same level of trade as the export price or constructed export price.”

³ Section 771(15) of the Tariff Act defines the term “ordinary course of trade” as follows:

Ordinary course of trade. The term "ordinary course of trade" means the conditions and practices which, for a reasonable time prior to the exportation of the subject merchandise, have been normal in the trade under consideration with respect to merchandise of the same class or kind. The administering authority shall consider the following sales and transactions, among others, to be outside the ordinary course of trade:

- (A) Sales disregarded under section 773(b)(1).
- (B) Transactions disregarded under section 773(f)(2).

See 19 U.S.C. §1677(15).

customer at the same time and on the same terms must also be in the “ordinary course of trade.” In other words, it is not necessary that the average prices of the sale to the affiliated customer be identical to (or within a narrow range of) the average price of all sales to unaffiliated customers. Rather, it is only necessary that the prices for the sales to the affiliates be equivalent to an arm’s-length transaction at roughly the same time.

This interpretation of the statute is reflected in the Department’s regulations. The regulations do not require a comparison of *average* prices for sales to affiliated and unaffiliated customers. Rather, the regulations provide that the Department will include a sale to an affiliated customer in its analysis only if the price for “that sale” is “comparable” to the price at which the producer sold the foreign like product to “a person who is not affiliated with the seller.”⁴ Significantly, the regulations refer to the comparability of a single transaction with an affiliate (“that sale”) to a single price (“the price”) at which the merchandise is sold to a single unaffiliated customer (“a person who is not affiliated with the seller”). Under the regulations, then, it is not necessary that the *average* prices for sales to affiliated and unaffiliated customers fall within a narrow range. Instead, a sale to

⁴ Thus, Section 351.403(c) of the regulations provides that:

If an exporter or producer sold the foreign like product to an affiliated party, the Secretary may calculate normal value based on that sale only if satisfied that the price is comparable to the price at which the exporter or producer sold the foreign like product to a person who is not affiliated with the seller.

an affiliated customer may be used whenever the price for that individual transaction is “comparable” to the price for a single arm’s-length sale to an unaffiliated customer.

The Department has followed precisely such an approach in determining whether “transfer prices” with affiliates (for production inputs, transportation services or commissions) can be used in its analysis, under the “special rule” of Section 773(f)(2) of the Tariff Act. The same analysis is applicable to the determination whether sales to an affiliate are in the “ordinary course of trade.” In fact, the statutory definition of “ordinary course” of trade specifically incorporates the “special rule” of Section 773(f)(2) of the Tariff Act.⁵ Consequently, the Department should apply a consistent standard, and consider a sale to an affiliate to be within the ordinary course of trade as long as the price is equivalent to the price for a comparable sale to an unaffiliated customer.

Of course, in most cases, there are likely to be variations in the prices of a particular product for sales to unaffiliated customers. In such circumstances, the prices for *some* of the sales to unaffiliated customers will necessarily differ from the overall average price. .

⁵ The “special rule” of Section 773(f)(2) of the Tariff Act provides that:

A transaction directly or indirectly between affiliated persons *may* be disregarded if, in the case of any element of value required to be considered, the amount representing that element does not fairly reflect the amount usually reflected in sales of merchandise under consideration in the market under consideration....

See 19 U.S.C. § 1677b(f)(3). By its terms, of course, that “special rule” applies only “for calculation of cost of production and for calculation constructed value.” However, this provision is also explicitly incorporated into the statutory definition of “ordinary course of trade.” *See* Tariff Act of 1930, as amended, § 771(15), 19 U.S.C. § 1677(15).

However, none of the sales to unaffiliated customers will be considered outside the ordinary course of trade. It follows, then, that sales to affiliated customers that are equivalent to any of the sales to unaffiliated customers must also be considered within the ordinary course of trade — because such sales to affiliates are necessarily comparable to sales to unaffiliated customers that are within the ordinary course of trade. It would be illogical to deem a sale to an affiliate to be outside the ordinary course of trade, when a sale to an unaffiliated customer on the same terms is deemed within the ordinary course of trade.

Under the relevant provisions of the statute and regulations, then, it is not necessary that the average prices for sales to affiliates fall within a narrow band around the average price for sales to unaffiliated customers. Instead, it is necessary only that the prices of the sales to affiliates fall within the range of normal transactions.

2. A “Cushion” Methodology Better Reflects the Statutory Requirements than the Average-Price Comparison Proposed by the Department

In the real world, of course, there may be numerous variations in the terms, timing and market conditions for the relevant transactions that make it difficult to obtain direct comparisons of the prices for individual sales to affiliated and unaffiliated customers. Moreover, given the strict statutory deadlines under which the Department operates, it may not be feasible to find an appropriate arm’s-length comparison for each individual sale to an affiliated customer. In these circumstances, it is understandable that the Department would seek some type of overall analysis to make a determination whether the sales to affiliates have been made at arm’s-length prices.

The analysis adopted by the Department should, however, conform as closely as possible to the requirements of the statute. And, as discussed above, the relevant provisions require only that the sales to affiliates fall within the range of normal transactions. Any overall approach adopted by the Department should, therefore, focus on whether the sales to affiliates fall within the normal range of transactions.

In this regard, the methodology proposed by the Department does not properly implement the statutory requirements. Because that methodology focuses on a comparison of the *average* prices for sales to affiliated and unaffiliated customers, it does not provide any indication whether the sales to affiliates fell within the normal range. For example, suppose that 90 percent of the sales to unaffiliated customers and 100 percent of sales to affiliated customers were all made at a price of 200. If 10 percent of the sales to unaffiliated customers were made at a price of 300, the average price for sales to unaffiliated customers would be 210. The average price for the sales to affiliated customers (200) would then differ from the average price for sales to unaffiliated customers by 5 percent — even though the prices for the sales to affiliates were identical to the prices for 90 percent of the sales to unaffiliated customers.

By contrast, the “cushion” approach described (and preliminarily rejected) in the Department’s August 15 notice better implements the statutory requirements. Under such an approach, sales to affiliates would be considered in the “ordinary course of trade” as long as there is a sufficient quantity of sales to unaffiliated customers at prices above and

below the average price for sales to affiliates. In other words, this methodology allows the sales to affiliates to be used only if they fall within the normal range of transactions.⁶

The Department preliminarily rejected this test out of concern over its complexity, implementation, and uncertainty as to the appropriate size of the “cushion.”⁷ However, once a reasonable “cushion” size is identified, the calculations required to implement the test are no more complex or difficult to implement than the proposed methodology.⁸ The

⁶ A slight modification in the proposed methodology may be required to address situations in which the sales to affiliates are at the same price as many of the sales to unaffiliated customers, but there are no sales to unaffiliated customers at higher (or, alternatively, lower prices. For example, in the hypothetical situation described above (90 percent of the sales to unaffiliated customers and 100 percent of sales to affiliated customers at a price of 200, and 10 percent of the sales to unaffiliated customers at a price of 300), there would be no sales to unaffiliated customers at prices below the average price of sales to affiliated customers.

⁷ The Department also expressed concern that the “quantity cushion” test defined the “normal” price range of sales too narrowly. This concern is, however, misplaced. The “quantity cushion” does not define any price range. It simply ensures that the sales to affiliates fall within the actual normal range of prices.

⁸ Assume, for example, a cushion size of 20 percent — *i.e.* if the weighted average price of sales to an affiliate is greater than or equal to at least 20 percent of sales (by quantity) to unaffiliated customers, and lower than or equal to at least 20 percent of sales (by quantity) to unaffiliated customers — the affiliated sales would fall within the “cushion” and, therefore, would be in the ordinary course of trade. To determine whether sales to an affiliate fell within the 20 percent cushion, the Department would continue to calculate an affiliate-specific weighted-average price for each product purchased as it has in the past. Then, for each product, the Department would then calculate, as percent of total unaffiliated sales of the product, the “cushion” of sales below each affiliate’s average price and the “cushion” of sales above each affiliate’s average price. The calculated “cushions” for each affiliate can then be weight-averaged according to the quantity of each product purchased by the affiliates to calculate the affiliates upper and lower “cushion.” If both cushions are greater than 20 percent, then the sales to the affiliate would be considered as ordinary course of trade sales.

appropriate cushion size is, in turn, a function of the purpose of the analysis. Since the analysis is intended to determine whether the sales fall within the range of normal transactions, the cushions should be set to exclude only the sales that are outside that range.

4. Although an Overall Analysis May Be Useful, It Should Not Establish an Irrebuttable Presumption

Of course, any methodology that relies on an overall analysis of aggregate data is susceptible to some distortions. Suppose, for example, that the prices for sales to affiliated and unaffiliated customers are exactly the same at any point in time, but that the prices vary over time. If sales to affiliated customers fall disproportionately in one part of the period, an aggregate analysis may find that the aggregate prices for the sales to affiliates differ significantly from the aggregate prices for sales to unaffiliated customers — simply because most of the sales to unaffiliated customers were made at a different time when prices were different. There may also be other factors that affect the price comparability that result in distortion in the overall data.

In order to prevent such distortions in its analysis, the Department should use its aggregate analysis only to establish a presumption as to whether the sales to affiliates are within the ordinary course of trade. Where the aggregate analysis is distorted by variations in timing or other terms, the parties should be given an opportunity to provide alternative evidence and analysis to overcome this presumption. If the evidence demonstrates that the sales to affiliates fell within the normal range of transactions, the Department should include them in its analysis — regardless of the results of its aggregate analysis.

5. The Department Should Establish Reasonable Reporting Requirements for Downstream Sales by Affiliated Resellers

As the Department is aware, many companies sell their products through affiliated resellers. Even when the number of affiliated resellers is small, the burdens of providing information on the resales may be immense — where, for example, the resellers operate separate computer systems and are under distinct management. When the number of affiliated resellers is large, the burdens are multiplied.⁹ Moreover, there may be cases in which the affiliated resellers themselves sell to other affiliated resellers, who resell, in turn, to their customers. Even in less complicated situations, when the exporter owns only a minority interest in the reseller, it may not be able to insist that the reseller undertake the enormous effort required to respond to the Department’s questionnaires.

In these circumstances, it often is impractical, if not impossible, for a company to provide complete information on re-sales by its affiliated resellers. A decision by the Department to require complete reporting of sales by resellers may, therefore, force the responding company to drop out of the case altogether — even if there has been nothing “unfair” about its pricing. In such circumstances, the reseller reporting requirement may, by itself, create an impenetrable procedural barrier to trade.

Under the Department’s current methodology, it is not necessary for respondents to report sales by affiliated resellers where the sales to the resellers are made at arm’s-length

⁹ For example, in the recent investigation of cold-rolled carbon steel products from France, the Department found that the Usinor group sold cold-rolled steel products through more than two dozen affiliated resellers.

prices. We are concerned, however, that the proposed modifications in the arm's-length test may substantially increase the number of cases in which the Department will require reporting of resales by affiliated resellers. We would urge the Department to explore alternatives that would minimize the burdens such requirements would impose.

One obvious approach would be to clarify that sales by affiliated resellers do not have to be reported (even if the sales to the resellers do not meet the arm's-length test) for resellers that constitute a small percentage of total sales. For example, the Department could specify that affiliated resellers whose purchases represent less than one percent of total home-market sales do not have to report their resales (even if the total sales to affiliated companies are, in aggregate, greater than five percent).¹⁰ In addition, the Department could excuse affiliated resellers from any reporting where the resales are made in smaller quantities or at a different level of trade than the other home-market and U.S. sales. In such circumstances, the information on the resales is unlikely to have any meaningful effect on the Department's analysis (in view of the small volume of resales or

¹⁰ The Department's regulations currently provide that sales to affiliated resellers will not be used in the calculation of normal value if the sales to the affiliates represent less than five percent of total sales in the comparison market:

Sales through an affiliated party. If an exporter or producer sold the foreign like product through an affiliated party, the Secretary may calculate normal value based on the sale by such affiliated party. However, the Secretary normally will not calculate normal value based on the sale by an affiliated party if sales of the foreign like product by an exporter or producer to affiliated parties account for less than five percent of the total value (or quantity) of the exporter's or producer's sales of the foreign like product in the market in question ...

their unsuitability for comparison). And, the limitations on reporting requirements would be consistent with the requirements of Section 782(c) of the statute — which requires the Department to “avoid imposing an unreasonable burden” on responding parties.¹¹

In addition, the Department should also allow respondents to forego any reporting of resales by affiliated resellers where the prices for sales to the affiliated resellers are found to be *higher* than the prices for sales to unaffiliated customers — provided that the respondents agree to the inclusion of the higher-priced sales to affiliated resellers in the normal value calculation. Of course, the use of the higher-priced sales to the affiliated resellers would increase the normal value and hence the dumping margins. Nevertheless, respondents might be willing to accept that result in order to reduce the burden of preparing a complete response for the affiliated resellers.¹²

As a more general matter, the Department should ensure that its procedures provide for the maximum amount of flexibility to minimize reporting requirements where requiring complete reporting of resales by affiliated resellers will not make any meaningful difference in the accuracy of its calculations. The Department should ensure that its initial

¹¹ See 19 U.S.C. § 1677m(c).

¹² Such an approach would not require any change from the Department’s current practice, and should not raise any issues under the WTO Antidumping Agreement. The Department would not have to create an unbalanced rule that would treat higher-than-average prices as within the ordinary course of trade. Instead, as a procedural matter, the respondents would be given the opportunity to admit that the higher-priced sales were within the ordinary course of trade. If the respondents did not make such an admission, they would be required to provide information on the resales by the affiliated resellers. If the respondents did make such an admission, the higher-priced sales to the affiliated resellers would be included in the analysis.

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questionnaires obtain sufficient information to allow it to make informed decisions on what the reporting requirements should be. And, once it has sufficient information, it should inform respondents of the reporting requirements as promptly and as clearly as possible.

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Please do not hesitate to contact us if you have any questions.

Respectfully submitted,

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