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PROPOSALS ON THE PROHIBITION OF ZEROING

Communication from Japan

The following communication, dated 20 April 2006, is being circulated at the request of the Delegation of Japan.

The submitting delegation has requested that this paper, which was submitted to the Rules Negotiating Group as an informal document (JOB(06)/109), also be circulated as a formal document.

This paper aims to clarify the prohibition on zeroing, taking into account the useful discussions at the Rules Group meetings.[1] Part I of this paper provides further explanations on the principles underlying the prohibition of zeroing. Part II provides revised legal drafts relating to this issue,[2] based on earlier proposals submitted by Members.[3]

I. EXPLANATION

Below, we explain several important points regarding the prohibition of zeroing. §These points relate to the draft legal text in Part II.

1. Prohibition of Zeroing as a generally-established principle

The WTO Appellate Body ("AB") has confirmed repeatedly that "dumping is defined in relation to a product as a whole" and that, "while an investigating authority may choose to undertake multiple comparisons or multiple averaging at an intermediate stage to establish margins of dumping, it is only on the basis of aggregating *all* these 'intermediate values' that an investigating authority can establish margins of dumping for the product under investigation as a whole."[4]

Article 2.1 of the AD Agreement, which sets forth the definition of dumping, applies throughout the AD Agreement[5]. The basic principle of the prohibition of zeroing therefore applies to all determinations of dumping and margins of dumping. This is true both in original investigations

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[1] This proposal does not prejudge the position of Japan in any dispute settlement proceedings.

[2] We reserve the right to propose additional legal draft proposals relating to other aspects of the application of the prohibition of zeroing in the context of the AD Agreement.

[3] TN/RL/GEN/8 and TN/RL/GEN/44.

[4] United States – Laws, Regulations and Methodologies for calculating Dumping ("US-Zeroing") W/T DS 294 AB/R (18 April 2006), para. 126.

[5] *US-Zeroing*, para. 125.

and in subsequent proceedings, and regardless of the methodology used in calculating the margins of dumping.

2. "Fair Comparison" between normal value and export prices with regard to all comparable export transactions

As stated above, an anti-dumping investigation shall determine whether a product from a given exporter/producer under investigation as a whole has been dumped in the importing market, not whether individual sales of that product or models of that product have been sold below normal value. Also, a fair comparison must be made between normal value and export prices. However, by "zeroing" negative results of multiple comparisons, authorities fail to take fully into account the entirety of the prices of some export transactions. That inflates the margin of dumping. In addition, as the AB found in *US – CRS Sunset Review*, zeroing could, in some instances, turn a negative margin of dumping into a positive margin of dumping. There is therefore an inherent bias in the zeroing methodology.[6] Although the basic principle (prohibition of zeroing) is already embodied in the current AD Agreement, there seem to be Members which have different views on this principle. Thus, we believe it is useful to clarify the basic principle in Article 2.4.

3. T-T comparisons must be subject to the same disciplines as W-W comparisons.

The current text of the AD Agreement clearly prohibits zeroing in the calculation of the dumping margin in W-W comparisons in original investigations. The AB has confirmed this in the following significant cases: *EC – Bed Linen, US – CRS Sunset Review, US –Softwood Lumber, and US – Zeroing*[7].

As discussed above, zeroing is prohibited as a general principle, regardless of the type of comparison methodology. For the purpose of establishing the existence of the margin of dumping, W-W and T-T comparisons have no functional difference. Indeed, if an authority "zeroes" in W-W or T-T comparisons, it fails to take fully into account the entirety of the prices of some export transactions, namely, those export transactions with negative comparison results. This practice inflates the margin of dumping. Since zeroing could even turn a negative margin of dumping into a positive margin of dumping, it is an inherently biased practice. If zeroing were prohibited in a W-W comparison but not in a T-T comparison, the two methodologies could produce substantially different results under otherwise identical conditions. This would be an absurd result, since a choice of a different methodology could easily turn a negative dumping margin into a positive one.

Since it is clear from the above that the current AD Agreement prohibits zeroing in T-T comparisons as well as in W-W comparisons, we believe no textual clarification is needed on this issue, and we do not propose any changes to the current text of the AD Agreement to that effect.

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[6] *US – CRS Sunset Review, para. 135*

[7] The Appellate Body Report, *European Communities – Anti-dumping Duties on Imports of Cotton-Type Bed Linen from India*, WT/DS141/AB/R (1 March 2001), The Appellate Body Report, *United States – Sunset Review of Anti-dumping Duties on Corrosion Resistant Steel Flat Products from Japan* (*US – CRS Sunset Review)*, WT/DS244/AB/R (15 December 2003), *United States – Final Dumping Determination on Softwood Lumber from Canada*, WT/DS264/AB/R (11 August 2004); *US – Zeroing*, W/T DS 294 AB/R (18 April 2006).

4. Prohibition of Zeroing in subsequent proceedings

(1) Article 9.3 Reviews

Article 9.3 review proceedings involve a calculation of the margin of dumping. Therefore, the same substantive disciplines on the dumping margin calculation as in original investigations should apply in these reviews. As discussed above, the prohibition of zeroing is a general principle for the calculation of the margin of dumping. We see no reason why this general principle should apply to the calculation of the margin of dumping in original investigations, but not in subsequent proceedings.

Article 9.3.1 reviews have two functions: determining the definitive level of duties, and establishing the cash deposit rates for the subsequent period.

- The cash deposit rate calculated in an Article 9.3.1 review and the dumping margin calculated in an original investigation under the retrospective system have the same function. Both of them establish the amount of security applicable to imports in the subsequent period.

- The determination of definitive level of duties in an Article 9.3.1 review and the dumping margin calculation in an original investigation in a prospective *ad valorem* system have the same function. Both establish the upper limit of liability for anti-dumping duties specific to each exporter or foreign producer.[8]

Since Article 9.3.1 reviews and original investigations share these two functions, we see no logical reason why zeroing is allowed in the former proceeding while prohibited in the latter.

If zeroing is prohibited only in original investigations but not in subsequent proceedings, the result would be fundamentally unfair, particularly in a retrospective duty assessment system, where the original investigation determines only the deposit rate, and the upper limits to the definitive duties are determined in Article 9.3.1 proceedings. Specifically, while a margin of dumping, which is calculated in the original investigation based on prices and volumes of export transactions during the period of investigation without zeroing, only serves as the rate of deposits for future entries, the margin of dumping calculated in the duty assessment phase under Article 9.3.1 for such entries could substantially increase, as a result of zeroing, even if the prices and volumes of such entries and the normal value were exactly the same as those in the original investigation. Since, unlike in a prospective *ad valorem* system where the calculated dumping margin without zeroing sets the upper limit of an importer's final liability of anti-dumping duties, a retrospective duty assessment system can charge a higher duty rate than the deposit rate, those entries could easily face a higher duty rate only because of zeroing. This would be an absurd result; the exporters and importers face substantial uncertainty, and this would undermine the prohibition of zeroing in the original investigation.

As the AB confirmed in *US – Zeroing*, the margin of dumping established for an exporter or foreign producer operates as a *ceiling* for the total amount of anti-dumping duties that can be levied on the entries of the subject product (from that exporter) covered by the duty assessment proceeding.[9] If zeroing is permitted in Article 9.3 reviews, the authorities systematically disregard part of the transactions. That would be contrary to the very function that the antidumping duty is supposed to

[8] If the lesser duty rule is applied, the upper limit of an importer's final liability will be the lesser of the dumping margin and the injury margin (TN/RL/GEN/99). For the sake of simplicity, this paper puts this issue aside for the moment.

[9] US –Zeroing, *para. 130-133*.

serve: to be imposed "to the extent necessary to counteract dumping" that can be only determined for the product as a whole.[10]

The rationale to support the prohibition of zeroing in Article 9.3.1 proceedings applies with equal force to the dumping margin calculation in the refund proceedings under Article 9.3.2. Article 9.3.2 proceedings establish the entitlement of an importer to a refund of any excess duties paid. Here again, the function of the calculation and determination of the margin of dumping in the refund proceeding is the same as that in an original investigation: to establish the upper limit of an importer's liability for anti-dumping duties. Thus, the same substantive disciplines on the dumping margin calculation applicable to original investigations (e.g. prohibition of zeroing) must apply to the refund proceedings as well.

(2) Article 9.5 Reviews

In addition, there is no reason why the substantive rules for determining the margin of dumping in an original investigation do not apply to new shipper reviews under Article 9.5. Such reviews are merely substitutes for an original investigation for producers and exporters that had not exported during the period of the original investigation. Thus, the prohibition of zeroing should apply in Article 9.5 reviews.

(3) Article 11 Reviews

Finally, where the authorities conduct reviews under Article 11 and when they make a determination of the margin of dumping during the period of review, there is no reason why such reviews are not governed by disciplines of dumping margin calculation under Article 2, because the definition of "dumping" as contained in Article 2.1 applies to the entire AD Agreement. Thus, the prohibition of zeroing should also apply in reviews under Article 11.

(4) Conclusion

In sum, we believe that the logic is compelling that zeroing be prohibited in the calculation of the dumping margin in both original investigations and in subsequent proceedings. However, there seem to be some Members which have different views, due to different ways of reading the current

[10] Some Members have contended that the term "margin of dumping" in duty assessment proceedings can be interpreted as applying on a transaction-specific basis and that the determination of the margin of dumping under Article 9.3 proceedings would have to be made on an importer-specific basis because the duty must be levied on the importers. The Appellate Body rejected this contention. This contention confuses the practical aspects of levying the antidumping duty with the basic rules for determining dumping and margins of dumping. These two issues are related but distinct issues.

The margins of dumping under Article 9.3 must also be determined on an exporter/producer-specific basis. Article 6.10 clarifies that margins of dumping must be determined on an individual exporter/producer basis. This basic rule informs Article 2, which therefore requires that dumping and the margins of dumping must be determined on an exporter/producer specific basis, and this rule applies both to original investigations and to reviews. As the Appellate Body has confirmed, "[e]stablishing margins of dumping for exporters or foreign producers is consistent with the notion of dumping, which is designed to counteract the foreign producer's or exporter's pricing behavior" and "it is the exporter, not the importer, that engages in practices that result in situations of dumping (US –Zeroing, *para. 129).*

Although the AD Agreement is clear on how authorities must calculate dumping margins, the Agreement is silent on how the authorities should levy the amount of these margins of dumping on the imports. So long as the margin of dumping is calculated for the product as a whole for a given exporter/ producer on a basis of entire prices of all export transactions of the product in question and the total amount of anti-dumping duties that are levied does not exceed the exporters' or foreign producers' margins of dumping, it is up to the authority to decide how to *assess* the final duty liability among the parties that imported from the exporter.

language of Article 2.4.2. Hence, we believe that it is useful to clarify this point in the text of Article 2.4.2, without prejudice to the overarching definition of "dumping" under Article 2.1.

5. The same margin calculation methodology shall normally be consistently used in original investigations and in Article 9.3 reviews

The authorities should apply the same methodology, in principle, consistently in determining the margin of dumping in original investigations and Article 9.3 proceedings.[11] If the authority can arbitrarily change its dumping margin calculation methodology between an original investigation and subsequent Article 9.3 reviews, exporters would have little predictability.

This rule would not impose a rigid discipline on authorities, nor would it be a total prohibition on changing methodologies after the investigation. Rather, the authorities would be able to change their methodologies whenever a change in the factual situation justifies a change. For example, even when W-W comparisons were used in the original investigation, T-T comparisons can be chosen by the authorities in subsequent Article 9 reviews, on the ground that there are very few sales during the period of review.

We note that this principle applies to the choice of all calculation methodologies in Article 2.4.2, including the weighted average to transaction ("W-T") methodology in the second sentence of Article 2.4.2.

6. Single margin of dumping for the entire period of investigation or review

Authorities could circumvent the prohibition of zeroing if they were allowed to subdivide the period of investigation or review, and calculate separate margins for each of the subdivisions (e.g. month, quarter, semi-annual). This should not be allowed. Indeed, the Appellate Body confirmed that the period of investigation "form[s] the basis for an objective and unbiased determination by the investigating authority."[12] If an authority calculates separate margins for subdivided periods within the period of review/investigation, and does not offset positive margins from one subdivision with negative margins from other subdivisions, this would have the same effect as zeroing. Authorities may not make an affirmative dumping determination regarding an exporter or producer that has no margin of dumping for the period of review/investigation as a whole, regardless of whether the export price during a portion of the period was less than the normal value.

We believe that the period of investigation or review must normally be one year. This is because a shorter period of investigation cannot normally reflect adequately the exporter's overall business, and may "be subject to market fluctuations or other vagaries that may distort a proper evaluation."[13]

7. There must be clear and adequate disciplines on W-T comparisons

As stated above, there is a clear principle that authorities must calculate a single margin of dumping without zeroing for the product as whole for the entire period of investigation or period of review. However, we acknowledge the arguments of some Members that, in certain circumstances, the ordinary margin calculation methodology might not properly reflect the exporter's business practices and the consequent injurious effect of the exporter's sales below normal value.

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[11] Please see TN/RL/GEN/44, proposal 1.

[12] The Appellate Body Report, *European Communities – Anti-Dumping Duties on Malleable Cast Iron Tube or Pipe Fittings from Brazil* (WT/DS219/AB/R) adopted 18 August 2003, para. 80.

[13] Ibid.

The second sentence of Article 2.4.2 sets forth the circumstances where authorities may use W-T comparisons. Authorities may do so if they "find a pattern of export prices which differ significantly among different purchasers, regions or time periods, and if an explanation is provided as to why such differences cannot be taken into account appropriately by the use of a weighted average-to-weighted average or transaction-to-transaction comparison."

We are open to discuss further how the margin of dumping may be calculated in such a comparison.

II. PROPOSALS

2.4 (first sentence) A fair comparison shall be made between the export price and the normal value on the basis of differences between the export price and the normal value with regard to all comparable export transactions during a period of time which shall normally be one year.

2.4.2 (first sentence) Subject to the provisions governing fair comparison in paragraph 4, the existence of margins of dumping ~~during the investigation phase~~ shall normally be established on the basis of a comparison of a weighted average normal value with a weighted average of prices of all comparable export transactions or by a comparison of normal value and export prices on a transaction-to-transaction basis.

(No textual proposals regarding the second sentence of Article 2.4.2 at this juncture.)

9.x The provisions of Article 2 shall apply to all determinations pursuant to paragraphs 3 and 5 of this Article. The authorities shall normally use the same methodologies consistently in determining a margin of dumping in an investigation initiated pursuant to Article 5, and in subsequent determinations pursuant to paragraph 3. If the authorities use a different methodology in subsequent determinations pursuant to paragraph 3, the parties concerned shall be provided with an opportunity to make comments, and a full explanation shall be given why such different methodology was used.

11.x If the authorities calculate the margin of dumping in any review under this Article, such margin of dumping shall be calculated in accordance with the provisions of Article 2.

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