

WORLD TRADE ORGANIZATION

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Negotiating Group on Rules

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PROPOSAL ON ISSUES RELATED TO AFFILIATED PARTIES

Paper from Brazil; Colombia; Costa Rica; Hong Kong, China;
Japan; Korea; Norway; Singapore; Switzerland; the Separate
Customs Territory of Taiwan, Penghu, Kinmen and Matsu; and Thailand

This proposal concerns the issues related to affiliated parties. These issues have been identified in document TN/RL/W/10. Other Members have also referred to this issue in documents TN/RL/W/66, TN/RL/W/81, TN/RL/W/86 and TN/RL/W/130.

This proposal indicates one way to overcome and resolve the problems resulting from the lack of clear definitions of affiliated parties and the problems resulting from the absence of rules in the treatment of affiliated transactions. The discussions in the Negotiating Group may assist in improving this proposal. Consequently, we reserve our right to modify or complement the proposal as appropriate.

In preparing and/or analyzing specific provisions, it is clear that amendment of the existing text may have an impact on other Articles of the AD Agreement, which have so far not been explicitly addressed. These links cannot be fully addressed until we have seen a comprehensive overview of proposed amendments. Consequently, we also reserve the right to make proposals on provisions which may not have been explicitly addressed so far for clarification or improvement.

Issues: Definition of “Affiliated Party” Transactions and Their Relevance in Determining Normal Value and Constructed Export Price; “Collapsing” of Multiple Entities.

Relevant Provisions: Articles 2.2 and 2.3.

Description of the Problems

The issue of “affiliation” arises in various places in the Anti-Dumping Agreement (“AD Agreement”), i.e., the calculation of normal value and the use of constructed export price (CEP), and plays a crucial role in the determination of dumping margins.¹ Yet the AD Agreement does not provide a clear and concrete set of criteria for determining when parties should be considered “affiliated” and does not adequately address those situations in which the existence of possibly affiliated parties affects the calculation of dumping margins. Given the importance of these issues, it is important to rethink the issue of affiliation and ensure that the AD Agreement clearly and appropriately defines these various issues.

¹ The issue of affiliation in relation to the definition of domestic industry is not within the scope of this proposal.

1. Problems Resulting from the Lack of Clear Definitions of Affiliated Parties

Authorities often conduct substantial investigations on transactions between a responding party and what are variously termed “related”, “associated” or “affiliated” parties in determining margins of dumping. For example,

- Authorities often request that a responding party submit all data related to sales in the exporting country by both the responding party and its associated purchasers, alleging that sales by the responding party to its associated purchasers might not be at arm’s length, or not “in the ordinary course of trade” within the meaning of Article 2.
- In other cases, the authorities allege that purchases of raw materials or services from affiliated suppliers do not “reasonably reflect the costs associated with the production and sales of the product under consideration”. The authorities request affiliated suppliers’ costs of production or services, in addition to prices of the responding party’s individual purchases from both affiliated and unaffiliated suppliers.
- In other cases, the authorities request the responding party to submit resale and cost data of a purchaser in the importing country to use CEP only on the grounds that the responding party has some equity stakes in the purchaser in the importing country.
- The authorities sometimes demand that the responding party combine or “collapse” the data of production and sales by “affiliated” parties with those by the responding party in order to establish a single margin of dumping for these entities.

In many of these cases, the authorities expand these inquiries far beyond what they need to determine the margin of dumping for the responding party. The authorities often request information on an “affiliated” party, over which the responding party has, in fact, no control at all. In other cases, the authorities request unnecessarily extensive data maintained by such “affiliated” parties in a prescribed format. These inquiries put excessive and unnecessary burdens on the responding party. In many cases, the responding party is simply unable to respond to all these inquiries, resulting in application of “adverse” facts available.

2. Problems Resulting from the Absence of Rules in the Treatment of Affiliated Party Transactions

Some authorities have applied special rules increasing or lowering the sales prices and costs recorded in a responding party’s normal financial and cost accounting system because of alleged affiliation between parties. For example,

- Upon finding a relation of affiliation between a responding party and a purchaser, the responding party is requested to submit resale data by the purchaser to independent parties, indifferent to whether the price of the responding party’s sales is reliable or not. Such practice of negating the reliability of actual data has no rationale but just creates opportunities for the authorities to resort to facts available and calculate artificially high dumping margins.
- Sales expenses for transportation services provided by an affiliated party, which are to be deducted from invoice prices in calculating normal value at ex-factory level, are rejected even if that affiliated service provider is providing similar services at the same price to independent parties. Such rejection also results in increase of the normal value and creation and increase of the dumping margin.

- Similarly, the responding party's cost of production is increased to the highest of the costs of the affiliated supplier, the purchase price from its unaffiliated suppliers, or the actual purchase price from the affiliated supplier. Such methodology has no rationale other than to increase the responding party's costs of production to the highest possible level that one can imagine, resulting in creation and increase of the dumping margin.
- In other cases, the authorities disregard export prices when such prices are higher than the export prices to independent importers, but take them when such prices to an associated importer are lower than the export prices to an independent buyer. Such practice is just a misuse or abuse of the discretion pertaining to the use of CEP.

The combination of an overly expansive definition of associated, affiliated or related parties (some authorities deem respondents to be affiliated with suppliers or purchasers based on an ownership interest of as little as 5%) and the absence of rules on the treatment of transactions between such parties, has led to excessive burdens and distorted results. The definition of affiliated parties should be applied consistently in all situations, and specific rules should be applied both in determining affiliation and in the proper treatment of affiliated party transactions.

Elements of the Solution

1. Definition of "Affiliated Party"

Proposal:

Add a provision (or separate annex) defining "affiliated parties" to be applied in all determinations of dumping where parties are related, associated or affiliated, and where the prices in transactions between such parties could be unreliable. The proposed definition is as follows:

An "affiliated party" shall be any party, which is considered to, directly or indirectly, control or be controlled by another party or which is under the common control of a third party. For the purposes of this definition, control is the power to govern the financial and operating policies of an enterprise by having:

- (a) more than one half of the voting power of an enterprise;
- (b) power over more than one half of the voting rights by virtue of an agreement with other investors;
- (c) such power under a statute or an agreement;
- (d) power to appoint or remove the majority of the members of the board of directors or equivalent governing body; or
- (e) power to cast the majority of votes at meetings of the board of directors or equivalent governing body.

The term "association" in Article 2.3 should be replaced by "affiliated parties" and should follow the single unified definition.

Explanation:

Article 2.2 of the AD Agreement provides no specific reference to association or relationship between parties in connection with the determination of normal value. Article 2.3 of the AD Agreement establishes that when there is no export price or where it appears to the authorities concerned that the export price is unreliable because of an association or compensatory arrangement between the exporter and the importer or a third party, the export price may be constructed, but provides no clear guidance on what kinds of affiliation require this use of constructed export price (“CEP”).

The concern in relation to affiliated parties is that one party may make transactions with another party on other than commercial terms. In market economies, one assumes that one party does not confer a gift on another party in the form of non-commercially priced sales. Indeed, the assumption must be that unless there is a substantial identity of economic interests between the entities involved, the price of the transaction will be an arm’s length price. This, in turn, implies that the identity of economic interests is dependent on the degree of common ownership and the ability of the owners of one party to control the actions of the other party.

The issue of the extent of the relationship necessary to constitute an identity of economic interests and confer control has been extensively analyzed in the context of corporate accounting practices and incorporated into International Accounting Standard 27 (IAS 27), “Consolidated Financial Statements and Accounting for Investments Subsidiaries”. We believe that the criteria in IAS 27, which we hereby adopted into this proposal, are well established and accepted, and thus, provide the most reliable basis to address the issue of affiliation between two entities. In addition, adopting these criteria into the AD Agreement has the benefit of enhancing the transparency and predictability of the AD regime and ensuring consistency among Members in applying antidumping rules. Practically, this proposal defines affiliated parties to be similar to those that are consolidated into a consolidated financial statement, into which a responding party also would be consolidated, in accordance with the accounting standards in many countries.

It should be noted that the ability of one party to *influence* the prices of another is not an appropriate standard for determining the “affiliated party.” For example, a buyer with a long-term commercial relationship or which buys in large quantities may use its buying power to influence the seller to provide a better price. Such influence is the very essence of the ordinary course of business, and is not evidence of “control” over the other party.

2. Calculation of Dumping Margins where Affiliated Parties are Involved**(1) Sales to Affiliated Parties for Determining Normal Value****Proposal:**

- Amend Article 2.2 to clarify that the authorities shall exclude all sales by the responding party to its affiliated parties from the sales in the exporting country (or to the third country) for determining the normal value, only if the weighted average price of sales by the responding party to the affiliated party varies by more than W percent² from the weighted average price of sales to all the unaffiliated parties (average-to-average comparison) and the weighted average price of sales by the responding party to the affiliated party is more than the highest of the weighted average price of sales to each unaffiliated party or less than the lowest of the weighted average price of sales to each unaffiliated party based on a company-by-company comparison.

² The appropriate level of the percentage figures in this document (“W”, “Y”, “T” and “V”) will be discussed at a later stage in the negotiation.

- Furthermore, clarify that such comparison shall be done for the same products sold at the same level of trade, taking into account differences in product mix.
- Furthermore, clarify that when the authorities exclude such sales under the condition mentioned above, the excluded data shall not be replaced with any data.
- Furthermore, clarify that in case there are no or too few unaffiliated parties with respect to sales by the responding party to make the above-mentioned comparisons, the sales prices to its affiliated parties shall be replaced by the weighted average price of sales of the same product by other responding parties which are regarded as reliable. In case there are no other responding parties, the authorities shall use all the sales prices into the calculation of the normal value.
- Amend Article 2.2 to clarify that in no event shall the authorities request that a responding party submit information in connection with sales by the affiliated parties to third parties.
- Furthermore, clarify that the authorities do not have any discretion whether or not to follow the above-mentioned procedures on a case-by-case basis.

Explanation:

This proposal is intended to clarify and simplify the rules on the treatment of sales by a responding party to its affiliated parties for determining normal value. Article 2.2 of the AD Agreement provides no specific reference to the treatment of sales between association or affiliated parties in connection with the determination of normal value. In such absence of explicit rules in the AD Agreement, Members have developed various tests to examine whether sales to affiliated parties were reliable or not. Members also have developed rules on the treatments of sales to affiliated parties, where these sales were found not to be at arm's length. As the AD regime has developed, these tests and rules also have become so complicated that they have made the results unpredictable and at the same time, have created excessive burdens on responding parties. To solve such problems, clarifying the basic concept that affiliation by itself is not a sufficient condition to deem unreliable the price of such transactions, our proposal is intended to streamline the rules so that they can be implemented by all Members without any difficulties, to reduce the burden on both the authorities and responding parties, and to increase the predictability of the AD regime for all international business participants. For example, certain authorities request a responding party to submit detailed data pertaining to the resale by the purchaser, but such practice should be explicitly prohibited because it is too burdensome for both the authorities and respondents and is considerably unfortunate for both to resort to facts available.

(2) Sales Expenses by Affiliated Service Providers**Proposal:**

Add provisions to clarify that a responding party's sales expenses (i.e., sales expenses that are the subject of due allowance made in the comparison between the export price and the normal value at the same level of trade) for services that are provided by affiliated parties shall be based on the actual price charged to the responding party by the affiliated supplier, unless the sales expense is a major expense and the evidence on the record shows that charges by the affiliated supplier for the service significantly differ from the comparable charges by unaffiliated service providers for the same service or from the comparable charges by the affiliated supplier for the same service to unaffiliated parties, and that the difference materially affects the price comparison. Even in case there exist no comparable charges, the sales expense by affiliated suppliers shall be based on the actual price charged to the responding party by the affiliated supplier, unless the major expense is below the cost

incurred at the affiliated supplier for providing that service. More specifically:

- The actual price charged by the affiliated supplier shall be used, unless the sales expense is a major expense;
- In case the sales expenses is a major expense and:
 - (i) when the responding party is sourcing the same service from both an affiliated supplier and an unaffiliated supplier, the authorities shall substitute the comparable price charged by the unaffiliated supplier for the actual sales expense charged by the affiliated supplier, only if the actual sales expense by the affiliated supplier varies by more than Y percent from the comparable price charged by the unaffiliated supplier for providing the same service; otherwise, the actual price charged by the affiliated supplier shall be used.
 - (ii) when the responding party is NOT sourcing the same service from an unaffiliated supplier, the authorities shall request that the responding party submit the cost data incurred at the affiliated supplier for providing that service.
 - (a) In this case, the responding party may submit a comparable price charged by the affiliated supplier for the same service to unaffiliated parties. In such case, the authorities shall substitute the comparable price charged by the affiliated supplier to unaffiliated parties for the actual sales expense by the affiliated supplier, only if the actual sales expense by the affiliated supplier varies by more than Y percent from the comparable price charged by the affiliated supplier for the same service to unaffiliated parties; otherwise, the actual price charged by the affiliated supplier shall be used.
 - (b) If the responding party does not submit the comparable price mentioned above, the authorities shall substitute the cost incurred at the affiliated supplier for the actual sales expense by the affiliated supplier, only if the actual sales expense by the affiliated supplier is below the cost incurred at the affiliated supplier for providing that service; otherwise, the actual price charged by the affiliated supplier shall be used.
- All of such examinations shall be conducted at a level of cost classification maintained in the respondent's accounting system and shall not be done cumulatively, provided that such accounting system is in accordance with the generally accepted accounting principles of the exporting country.

Further add a provision to clarify that the rules that we are proposing in connection with the costs data shall apply to sales expense data of affiliated suppliers of the major expense.

Furthermore, clarify that the authorities do not have any discretion whether or not to follow the above-mentioned procedures on a case-by-case basis.

Explanation:

This proposal intends to avoid overly burdensome calculations of sales expenses (i.e., sales expenses that are the subject of due allowance made in the comparison between the export price and the normal value at the same level of trade, normally at the ex-factory level). Sales expenses, such as transportation expenses, charged by an affiliated party are sometimes put under an extensive scrutiny

by the authorities but more often than not, they end up with relatively minor adjustment to the prices in a respondent's accounting record. This proposal clarifies that the authorities should not impose unnecessary burdens on a respondent when the detailed examination of such expenses is likely to result only in a minor adjustment and therefore does not materially affect the margin of dumping for the respondent, regardless of whether the sales expenses is for the due allowance to the normal value or export prices. Furthermore, the authorities should respect the prices actually charged by an affiliated party and recorded in a respondent's accounting statement, unless the sales expenses significantly differ from the comparable ones enough to be deemed unreliable. This proposal also clarifies that the authorities should not force a respondent to submit additional data pertaining to the affiliated party as long as there is a comparable expense to examine the reliability of the recorded expenses.

(3) Costs by Affiliated Suppliers

Proposal:

With respect to costs (costs of production, and administrative, selling, and general costs as provided in Article 2.2.1), amend Article 2.2.1.1 to clarify that a responding party's costs for inputs provided by affiliated suppliers shall be based on the actual prices charged to the responding party by the affiliated suppliers, unless the input is a "major input" and the evidence on the record shows that the price of the major input significantly differs from the comparable price charged by unaffiliated suppliers for the same input or from the comparable price charged by the affiliated supplier for the same input to unaffiliated parties, and that the difference materially affects the costs calculation. Even in case there exist no comparable prices, the price charged by affiliated suppliers shall be based on the actual price charged to the responding party by the affiliated suppliers, unless the major input is sold to the responding party at a price below the cost incurred at the affiliated supplier for providing that input. More specifically:

- The actual price charged by the affiliated supplier shall be used, unless the cost item at issue is a major input;
- In case the cost item at issue is a major input and:
 - (i) when the responding party is sourcing the same input from both an affiliated supplier and an unaffiliated supplier, the authorities shall substitute the comparable price charged by the unaffiliated supplier for the actual price charged by the affiliated supplier, only if the actual price charged by the affiliated supplier varies by more than T percent from the comparable price charged by the unaffiliated supplier for providing the same input; otherwise, the actual price charged by the affiliated supplier shall be used.
 - (ii) when the responding party is NOT sourcing the same input from an unaffiliated supplier, the authorities shall request that the responding party submit the cost data incurred at the affiliated supplier for providing that input.
 - (a) In this case, the responding party may submit a comparable price charged by the affiliated supplier for the same input to unaffiliated parties. In such case, the authorities shall substitute the comparable price charged by the affiliated supplier to unaffiliated parties for the actual price charged by the affiliated supplier, only if the actual price charged by the affiliated supplier varies by more than T percent from the comparable price charged by the affiliated supplier for the same

input to unaffiliated parties; otherwise, the actual price charged by the affiliated supplier shall be used.

- (b) If the responding party does not submit the comparable price mentioned above, the authorities shall substitute the cost incurred at the affiliated supplier for the actual price charged by the affiliated supplier, only if the actual price charged by the affiliated supplier is below the cost incurred at the affiliated supplier for providing that input; otherwise, the actual price charged by the affiliated supplier shall be used.
- All of such examinations shall be conducted at a level of cost classification maintained in the respondent's accounting system and shall not be done cumulatively, provided that such accounting system is in accordance with the generally accepted accounting principles of the exporting country.

Further amend Article 2.2.1.1 to clarify that the rules that we are proposing in connection with the costs data shall apply to cost data of affiliated suppliers of the major inputs.

Furthermore, clarify that the authorities do not have any discretion whether or not to follow the above-mentioned procedures on a case-by-case basis.

Explanation:

Responding parties have borne heavy burdens to respond to the authorities' unnecessarily extensive questions on their affiliated suppliers. The burden on a responding party must be balanced with the need of the authorities for additional information. In the same way as sales expenses, in order to balance the burden on a responding party with the authorities' need for additional information, we are proposing that the AD Agreement shall clarify the conditions for the authorities to request additional cost data; the major input accounts for at least a specified percentage of the total costs under consideration and the price charged for the major input significantly differs from a comparable price charged by unaffiliated parties. Such examination should not be done by the authorities arbitrarily categorizing the cost items, but should be done in accordance with the cost accounting system adopted by the responding party, which is supposed to be in accordance with the GAAP. This proposal also provides the responding party with the alternative of using another cost data which the affiliated party charges to unaffiliated parties for the same supply, should the responding party choose not to submit the relevant cost information. The goal should be to find a reliable but easier way to obtain an alternative, and not to maximize the burdens on respondents.

(4) Export to Affiliated Parties (CEP)³

Proposal:

- Amend Article 2.3 to further clarify that the authorities shall disregard the export price as unreliable and use CEP, only if the weighted average price of export sales by the responding party to the affiliated importers varies by more than V percent from the weighted average price of export sales to all the unaffiliated importers (average-to-average comparison) and the weighted average price of export sales by the responding party to the affiliated importer is

³ The existence of a "compensatory arrangement" between two parties is unrelated to whether such parties are "affiliated". The issue of the calculation of the normal value and the export price in a case where there is a compensatory arrangement or other contractual arrangements, which could affect the reliability of the price, whether between affiliated or unaffiliated parties, is not within the scope of this proposal and will be discussed in a separate paper.

more than the highest of the weighted average price of export sales to each unaffiliated importer or less than the lowest of the weighted average price of export sales to each unaffiliated party based on a company-by-company comparison.

- Furthermore, clarify that such comparison shall be done for the same products sold at the same level of trade, taking into account differences in product mix.
- Furthermore, clarify that in case there are no or too few unaffiliated parties with respect to export sales by the responding party to make the above-mentioned comparisons, the export sales prices to its affiliated parties shall be replaced by the weighted average price of export sales of the same product by other responding parties which are regarded as reliable. In case there are no other responding parties, the authorities shall use all the export prices for a fair comparison with the normal value.
- Furthermore, clarify that the authorities do not have any discretion whether or not to follow the above-mentioned procedures on a case-by-case basis.

Explanation:

Under the current practice, the excessive use of CEP has led to greater burdens on respondents and more frequent abuses by authorities in making asymmetrical comparisons. In order to clarify conditions where CEP should be used, this proposal is intended to specify what examination should be conducted with respect to the export sales to an affiliated party. The main idea of this proposal is similar to that for the home market sales to an affiliated party, and thus, export sales to an affiliated party should be under the examination that we propose for the purpose of analyzing the reliability of the prices of affiliated party transactions, because the affiliation by itself is not a sufficient condition to deem unreliable the prices of such transactions. Since the export sales are the very subject of anti-dumping investigation, however, they should not be excluded from the calculation of dumping margins, although they should be in the case of home market sales. The export sales, instead, should be constructed based on the basis of the price at which the imported products are first resold to an independent buyer, as is set forth in Article 2.3. Thus, this proposal clarifies the condition where CEP should be used, and is intended to avoid the excessive use of CEP.

(5) Treatment of Two Affiliated Parties into a Single Responding Party (So-Called “Collapsing”)

Proposal:

Add a provision to prohibit the establishment of a single margin of dumping for two or more affiliated parties by treating such parties as if they were a single responding party.

Explanation:

There are circumstances in which affiliated companies produce the same product to export to the importing Member. In such a case, certain authorities treat these affiliated entities as if they were a single responding party. In other words, the authorities “collapse” them to establish a single margin of dumping for these entities. In many cases, however, the two entities have independent operations with independent decision-making with respect to production, pricing and exporting. The entities sometimes actually compete with each other. In such cases, there is no reason to investigate these entities collectively and establish a single margin of dumping for them. As such, collapsing is not appropriate and shall be prohibited.
