CONGRESS OF THE UNITED STATES
CONGRESSIONAL BUDGET OFFICE

A
CBO
STUDY

SEPTEMBER 1994

How the GATT Affects U.S. Antidumping and Countervailing-Duty Policy

HOW THE GATT AFFECTS
U.S. ANTIDUMPING AND
COUNTERVAILING-DUTY POLICY

The Congress of the United States
Congressional Budget Office

NOTES

GATT refers to the General Agreement on Tariffs and Trade.

Unless stated otherwise, all years referred to in the text are calendar years.

Numbers in the text and tables may not add up to totals because of rounding.

Cover photo shows cargo being unloaded at the port of Newark, New Jersey, in 1971. (*U.S. News & World Report* Collection, Prints and Photographs Division, Library of Congress.)

Preface

The Congressional Budget Office (CBO) studied U.S. antidumping and countervailing-duty laws and policy at the request of the Ranking Minority Member of the Subcommittee on Trade of the Committee on Ways and Means. In May 1994, CBO published a paper, "A Review of U.S. Antidumping and Countervailing-Duty Law and Policy," in order to assist the Congress as it developed legislation to carry out the agreement reached during the Uruguay Round of the General Agreement on Tariffs and Trade. This report, which was prepared by Bruce Arnold of CBO's Natural Resources and Commerce Division, under the supervision of Elliot Schwartz and Jan Paul Acton, contains a more detailed discussion of the topic.

The study concludes that U.S. laws treat the pricing of imports in the U.S. market differently than they treat the pricing of domestically produced goods. Over time, the antidumping and countervailing-duty laws have become a general source of protection for U.S. firms from foreign competition. In keeping with CBO's mandate to provide nonpartisan analysis, the study makes no recommendations.

The earlier drafts of this study were reviewed by a number of individuals representing a variety of viewpoints on trade law and policy. Their comments and questions led to a clarification and strengthening of the analysis, although they do not necessarily agree with the conclusions. The author particularly wishes to thank Joseph E. Stiglitz, Council of Economic Advisors; Susan G. Esserman, Department of Commerce; Nancy E. Schwartz, Office of Management and Budget; Alfred E. Eckes, Ohio University; Emil Friberg, General Accounting Office; Leonard M. Shambon, law firm of Wilmer, Cutler & Pickering; and Thomas R. Howell and Alan William Wolff, law firm of Dewey Ballentine. Within CBO, Mark Booth, Robert A. Dennis, Daniel Gadra, Nicola O. Goren, and Christopher Williams provided many useful suggestions on earlier drafts.

Paul L. Houts edited the manuscript and Christian Spoor provided editorial assistance. Donna Wood typed the many drafts. With the assistance of Martina Wojak-Piotrow, Kathryn Quattrone prepared the study for publication.

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Director

September 1994

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Summary

The antidumping and countervailing-duty laws provide protection to domestic firms from import competition. Because U.S. law and procedures have changed substantially over the last century, U.S. antidumping law is now a tangled and confusing subject. It was once a reasonably close approximation of a prohibition on predatory pricing of imports, and served as a complement to antitrust law, which prohibited predatory pricing by domestic firms. Over the years, however, antidumping law and antitrust law have evolved in different directions, so that now the United States treats similar pricing practices differently depending on whether the product being sold is domestically produced or imported.

Predatory pricing, as the term is currently used, refers to the practice of intentionally selling a product at a loss in order to drive competitors out of business, thereby establishing increased market power that allows the seller to raise prices above competitive market levels and increase profits. Predatory pricing is one of a number of unfair competitive practices that the Sherman Act has been interpreted to prohibit. An early Supreme Court decision, however, ruled that acts committed in other countries were beyond the jurisdiction of the Sherman Act. Among other things, that interpretation effectively ruled out most prosecutions of predatory pricing of imports under the Sherman Act.

The Antidumping Act of 1916 specifically applied to the practice of pricing imports substantially below their normal market value with the intent of destroying, injuring, or preventing the establishment of an industry in the United States. Over time, however, antidumping law and policy have evolved along a path of ever-increasing protection for U.S. firms from imports and decreasing concern for consumers and the economy as a whole. In contrast, antitrust law relating to predatory pricing, at least in recent decades, has taken a path of increasing concern for consumers and the economy as a whole and decreasing concern for firms suffering intense competition.

Antidumping law no longer acts primarily against predatory pricing. It acts against international price discrimination (sales at a lower price in the United States than in the home country of the exporter) and sales below cost, regardless of whether the sales are predatory or not. Yet the relevant provisions of the antitrust laws prohibit only predatory pricing; they do not prohibit below-cost selling or price discrimination, as prohibited by the antidumping laws, except in cases where it is predatory. That difference is important.

Predatory pricing impairs economic welfare because it leads to monopolies, which cause economic inefficiency and raise concerns about social equity. It seldom occurs, however, because it is rarely a profitable strategy. Moreover, it is usually not possible to establish a monopoly. By contrast, nonpredatory price discrimination and sales below cost generally provide net benefits to the country receiving the lower price, and both are relatively common. Moreover, seldom do cases of price discrimination or selling below cost have anything to do with predatory pricing.

Countervailing-duty laws provide for added duties on imports that have been subsidized by the government of the exporting country. They date from before the turn of the century. Unlike the antidumping laws,

these laws have not changed in character over time, though they have become more inclusive. The first such U.S. law covered only imports of sugar. A later law covered all dutiable imports, and a later revision expanded coverage to include both dutiable and non-dutiable imports.

Over the years since World War II, U.S. tariffs have steadily declined in accord with agreements reached in successive rounds of negotiations to liberalize the General Agreement on Tariffs and Trade (GATT). This decline has resulted in increasing competition for domestic firms from imports. For such firms, and their workers U.S. trade law provides two forms of assistance: Trade Adjustment Assistance and protection under the Section 201 escape clause. Trade Adjustment Assistance consists of training, employment services, job-search and relocation allowances, and other forms of aid to displaced workers in industries adversely affected by increased import competition. The Section 201 escape clause provides temporary protection from imports to give domestic industries breathing room to adjust to increased competition. It contains several restrictions designed to ensure that the protection it provides is used only for such temporary adjustment purposes--not for permanent protection--and only when the adjustment costs are large and the costs of the protection to the economy and the national interest are not large.

In the case of industries unable to become competitive with imports (such as unskilled-labor-intensive industries), temporary breathing room for adjustment may be better than no protection at all, but it is not what the industries really want. Anything short of long-term protection would force painful contractions on them that trade adjustment assistance will not completely ameliorate. Further, those industries want protection from imports that cause *any* injury, not just those that cause substantial injury, and they would rather such protection be automatic, regardless of any harm it might cause to the rest of the economy or to the national interest generally. Not surprisingly, they have found the escape clause to be inadequate.

As the antidumping and countervailing-duty (AD/CVD) laws became more inclusive and protection under them easier to obtain, industries more and more frequently were able to obtain better protection, and to obtain it more easily, under those laws than under the escape clause. Gradually, many groups came to view the laws as an alternative to the escape clause for uncompetitive industries and for those industries unable to meet the stringent criteria that the escape clause sets for the protection it provides.

As more people accepted this view, the laws and the procedures for administering them--especially the antidumping law and procedures--began to serve this more general protective purpose more effectively. If the purpose of AD/CVD laws is to prevent, punish, and offset predatory pricing, subsidies, and other unfair practices relating to U.S. imports, many of the legal provisions and procedures that have evolved--especially those used for calculating dumping margins--are biased against foreign exporters (and against U.S. consumers of foreign goods). But if one believes that the AD/CVD laws should offer more general protection for domestic industries from troublesome import competition, those same provisions and procedures appear more reasonable, even if a bit ad hoc. Moreover, from that perspective, they have been quite effective.

How the Laws Currently Function

The antidumping law, and to some extent the countervailing-duty law, are now a fairly general source of protection from foreign competition. In practice, the main hurdle to an industry seeking protection under the AD/CVD laws is to demonstrate that it has been injured by the imports, not that the imports are dumped or subsidized. The Department of Commerce (DOC) found no dumping in only 7 percent of the cases that came before it from 1980 through 1992, while the International Trade Commission (ITC) found no injury in 34 percent of those cases that subsequently went to final injury determination. From 1988 through 1992, the numbers were even more lopsided: 3 percent for DOC and 41 percent for the ITC. Countervailing-duty cases were slightly less skewed: DOC found no subsidies in 14 percent of cases from 1980 through 1992, and the ITC found no injury in 57 percent of those that went on to final injury determination. For 1988 through 1992, the numbers were 32 percent for DOC and 38 percent for the ITC.

Those statistics suggest that the main hurdle in AD/CVD cases is establishing injury. However, the degree of injury that must be demonstrated in AD/CVD cases is less than in Section 201 cases. For that and other reasons, the Section 201 escape clause is now seldom used. An industry generally finds it much easier to obtain protection under the AD/CVD laws. Unfortunately, using those laws as a general source of protection from imports has several disadvantages.

First, the AD/CVD laws do not have the restrictions that the Section 201 escape clause has to ensure that protection is granted only temporarily for the purpose of aiding adjustment and only in cases where the benefit to the protected industry outweighs the harm to the rest of the country in economic, foreign policy, and security matters. To get an antidumping order revoked, a foreign firm usually must get a determination from the Commerce Department that it has ceased dumping. But that determination is difficult to get because of biases in the Commerce Department's procedures. Hence, protection under the antidumping law tends to be permanent for all practical purposes. Furthermore, permanent protection of industries is almost always detrimental to the economy and is contrary to the basic thrust of U.S. trade policy since World War II, which has supported the philosophy that all countries should eliminate trade barriers.

Second, other countries have begun to follow the U.S. lead. They are now using antidumping laws to protect their industries, and in fact many of them are targeting U.S. exports in retaliation for U.S. use of antidumping laws against them. As a result, although support for U.S. antidumping law and procedures among import-competing firms remains strong, sentiment against them is rising in the growing community of U.S. exporting and importing firms.

Third, even in those cases in which the protection is considered desirable, the AD/CVD laws sometimes provide inadequate protection. They apply only to imports of the product in question from particular countries or firms and not to all imports of the product from any source. Therefore, they can be, and sometimes are, circumvented either by the firm on whose products the duties are imposed or by the impersonal workings of the international market. Consequently, the United States has had to devote considerable attention in recent years to modifying the AD/CVD laws to make them apply to upstream dumping, downstream dumping, dumping routed through third countries, and various other routes by which AD/CVD orders have been circumvented. ("Upstream dumping" refers to the dumping of the intermediate goods or raw materials used as inputs in the production of the product in question. "Downstream dumping" refers to the dumping of products made from the product in question).

Finally, with increasing globalization of markets, it is becoming less clear which firms should be identified with which country. (That problem applies to other forms of protection as well as to the AD/CVD laws.) Increasingly, firms located in foreign countries and wishing to export to the United States are actually U.S. owned or partially U.S. owned. Conversely, domestically located firms that could be protected by trade laws are now often foreign owned or partially foreign owned. Such a melange of nationalities can make it unclear which countries are benefited or harmed most by protection granted by the AD/CVD laws.

A Look at the New GATT Antidumping and Subsidies Codes

Under the final "Agreement on Implementation of Article VI of GATT 1994" (Antidumping Code) and "Agreement on Subsidies and Countervailing Measures" (Subsidies Code) negotiated in the Uruguay Round, the United States and other countries will have to reform some of the more protectionist aspects of their AD/CVD laws. The reforms are modest, but for the United States they are nonetheless significant: they mark a change in direction from the 100-year trend in U.S. AD/CVD policy of ever-increasing protection of particular domestic industries and decreasing emphasis on the welfare of consumers and the economy generally.

Unlike the case for the old codes, which only some GATT signatories signed, all signatories to the GATT will be signatories to the new codes. Among the most important provisions in the new codes are new procedures for settling disputes, which cannot be blocked by a country that receives an adverse ruling. Also important is a sunset provision for automatically terminating

AD/CVD orders after five years unless a likelihood of continued dumping or subsidies and resulting harm is shown. The new codes provide for increased transparency and judicial review. They establish *de minimis* levels of dumping and subsidies that are higher than current U.S. levels, though still quite low, and they establish rigid levels of negligibility for imports, which the United States does not currently have. They also require greater evidence of industry support for initiating AD/CVD investigations than the United States currently requires.

The new codes contain provisions relating to many aspects of AD/CVD policy. A number of provisions attempt to ease the burden on investigated firms in complying with requests for information and ensure that firms know that the so-called "best information available," including information supplied by the domestic industries, can be used against them if they do not comply. Other provisions make it clear that administrative authorities may refuse to accept suspension agreements on grounds of general policy, which U.S. authorities often do.

For the first time, the codes explicitly recognize and legalize the practice of cumulating imports in determining injury, which the United States and other countries have already been doing without explicit legalization from the old codes. The new codes do not, however, allow the current U.S. practice of cross-cumulation of imports from firms subject to either antidumping or countervailing-duty investigations. They urge, but do not require, countries to consider the interests and views of parties in their own countries that might be injured by AD/CVD orders on imports.

The new Antidumping Code requires in most cases weighted-average-to-weighted-average comparisons of import prices with prices in the exporter's home market, which would eliminate a bias in current U.S. methodology. The new code also requires eliminating the current statutory minima that the United States maintains for profit and overhead in constructed-value calculations. It places new conditions on the ability of administrative authorities to eliminate sales below cost in the exporter's home market. Those conditions may reduce such eliminations by U.S. authorities, though it is not entirely clear they will do so since the effects of those conditions and related provisions will be mixed.

Furthermore, the new code requires considering the dumping margin in determining injury. Also, for the first time, the new code explicitly recognizes and legalizes, though subject to certain conditions, the practice of sampling, which the United States and other countries have practiced without explicit authorization under the old code. The conditions may require some changes in U.S. policy.

The new Subsidies Code for the first time defines the terms "subsidy" and "specificity." It incorporates a "traffic-light" approach to subsidies, with "red-light" subsidies, which are prohibited in almost all circumstances; "yellow-light" subsidies, which are prohibited if their effects on trade would cause injury to other countries' industries; and "green-light" subsidies, which are not prohibited and against which other countries cannot retaliate in almost all circumstances. It also establishes new rules for determining serious prejudice and phases out many of the exemptions that developing countries currently have under the old code's restrictions on subsidies.

The Status of Legislation

As this study goes to press, the House and Senate committees with jurisdiction over the GATT are meeting in conference to reconcile different versions of the bill needed to implement the trade agreement. Once the bill has been reconciled, the Administration will submit legislation for Congressional vote. Consideration of that legislation will follow so-called "fast-track" procedures. Under fast-track procedures, the Congress must vote on the bill within a prescribed time limit and the bill cannot be amended.

At present, the House and Senate versions of the bill, with respect to changing antidumping and countervailing-duty laws, differ on numerous points. For example, differences exist in such areas as the method for determining appropriate export prices, the treatment of countries in transition from centrally planned to market-based economies, and the rules to prevent the circumvention of duties. Resolving these and other differences will strongly affect the fortunes of many individual firms, workers, and consumers.

Neither version, however, significantly changes the overall stance of U.S. law. In general, the different versions of the bills either codify or revise the procedures the Department of Commerce and the International Trade Commission already use, or they put into law those agreements reached in the Uruguay Round negotiations. The underlying philosophy and operating procedures of the AD/CVD laws remain unchanged.

Chapter One

Introduction

In the area of international trade, industries and workers often complain of unfair foreign trade practices and regularly appeal to the government for protection from imports. Sometimes the President and the Congress have found particular instances of these problems so important that they have dealt with them individually with specific pieces of legislation or agreements. An example of this is the Multifiber Arrangement, which protects the domestic textile and apparel industries from imports. The problems occur frequently enough, however, and in enough industries that the Congress has passed general laws applicable to all industries and occasions. Those laws--referred to as trade remedy laws--specify how the executive branch should handle the problems and what remedies, if any, should be granted to the complaining industries and workers.

How the Antidumping and Countervailing-Duty Laws Fit in with U.S. Trade Remedy Law

The trade remedy laws can be divided into two broad groups--those assisting adjustment to trade and those combating unfair trade practices (see Box 1). The first group consists of laws to assist firms and workers that are adversely affected by increased competition from imports. The central theme of U.S. trade policy is that free trade generally benefits the country as a whole, and permanent barriers to imports are therefore to be avoided. Rather than being protected, domestic industries and workers are normally left to adjust to any increased competition from imports that may arise. Such adjustment is painful, however, and the pain often leads to opposition to the free-trade policies. Consequently, trade adjustment laws were enacted partly from compassion and partly from concern about maintaining support for free-trade policies.

The particular trade remedy law that is most relevant to this study is Section 201 of the Trade Act of 1974, the escape clause.[1] The escape clause authorizes the President to impose temporary import restrictions in cases where a good "is being imported . . . in such increased quantities as to be a substantial cause of serious injury, or the threat thereof" to the domestic industry producing a like or directly competing good. The purpose of the escape clause is to give the domestic industry breathing room in which to adjust to increased competition.[2] In some cases, such as the restraints on motorcycle imports in the 1980s, the domestic industry can use that breathing room to make itself competitive, thereby avoiding (or at least reducing) the need for re-

1. 19 U.S.C. 2251; 88 Stat. 2011, 93 Stat. 193, 98 Stat. 2988, 102 Stat. 1225.

2. That purpose is made clear in the wording of the law in several places. For example, the name of the chapter of the Trade Act of 1974 that contains Section 201 is "Positive Adjustment by Industries Injured by Imports." The name of Section 201 is "Action to Facilitate Positive Adjustment to Import Competition." Further, rather than specify that the President impose quotas, Section 201 specifies that "the President, in accordance with this chapter, shall take all appropriate and feasible action within his power which the President determines will facilitate efforts by the domestic industry to make a positive adjustment to import competition and provide greater economic and social benefit than costs."

Box 1. U.S. Trade Remedy Laws[1]

Laws Relating to Adjustment by Domestic Industries and Workers to Increased Imports

Sections 201-204 of the Trade Act of 1974, as Amended ("Section 201 Escape Clause"). Authorizes the President to impose temporary import restrictions on a good without regard to the fairness of the imports in cases where the good in question "is being imported . . . in such increased quantities as to be a substantial cause of serious injury, or the threat thereof, to the domestic industry" producing a like or directly competing good. The purpose of the escape clause is to give the domestic industry breathing room in which to adjust to increased competition, not to provide for permanent protection.

Section 406 of the Trade Act of 1974. Authorizes the President to impose temporary duties or quotas on imports from communist countries in cases where such imports are causing market disruption--defined as a significant cause of material injury, or threat thereof, to the domestic industry as a result of rapid increase of imports. Similar to Section 201 except that it applies to imports from individual countries rather than all countries, a lower standard of injury exists, and the relief procedure is faster.

Chapters 2, 3, and 5 of Title II of the Trade Act of 1974, as Amended ("Trade Adjustment Assistance"). Provides for various kinds of aid (such as training, trade readjustment allowances, employment services, job-search and relocation allowances, and so forth) for workers and firms adversely affected by increased import competition.

Laws Relating to Trade Considered to Be Unfair

Dumped Imports

The Antidumping Act of 1916. Prohibits the sale of imported goods at prices substantially below the actual market value or wholesale price "with the intent of destroying or injuring an industry in the United States, or of preventing the establishment of an industry in the United States, or of restraining or monopolizing any part of trade and commerce in such articles in the United States." Violations are subject to criminal and civil penalties.

Subtitle B of Title VII (Sections 731-739) of the Tariff Act of 1930, as Amended. Provides for antidumping duties to be imposed on imports sold in the U.S. market at "less than fair value" if such imports cause "material injury" to the U.S. industry producing a like product.

Subsidized Imports

Subtitle A of Title VII (Sections 701-709) of the Tariff Act of 1930, as Added by the Trade Agreements Act of 1979 and as Amended. Applies to imports from countries that have either signed the General Agreement on Tariffs and Trade (GATT) Subsidies Code or assumed obligations substantially equivalent to the code. Provides for countervailing duties to be imposed on imports benefiting from export or domestic subsidies by the source country if the imports cause "material injury" to the U.S. industry producing a like product.

Section 303 of the Tariff Act of 1930, as Amended. Applies to imports from countries that have neither signed the GATT Subsidies code nor assumed obligations substantially equivalent to the code. Provides for countervailing duties to be imposed on imports benefiting from export or domestic subsidies by the source country regardless of whether the imports cause "material injury" to the U.S. industry producing a like product.

Other Trade Practices

Section 337 of the Tariff Act of 1930, as Amended. Authorizes the International Trade Commission, subject to Presidential disapproval, to issue exclusion orders and cease-and-desist orders in cases of: (1) unfair import practices (excluding those involving only dumping or subsidies) and unfair methods of competition that destroy, substantially injure, or prevent the establishment of an industry in the United States, or restrain or monopolize trade and commerce in the United States, or threaten to do any of those; (2) imports that infringe a U.S. patent, registered copyright, registered trademark, or registered mask work of a semiconductor chip product. Most cases involve patent infringement. Others involve group boycotts, price fixing, predatory pricing, false labeling, false advertising, and trademark infringement.

Sections 301-310 of the Trade Act of 1974, as Amended ("Section 301"). Mandates action by the U.S. Trade Representative, subject to direction by the President, in cases where a foreign practice or policy violates an agreement with the United States or is unjustifiable and burdens U.S. commerce. Authorizes such action when a foreign practice or policy is unreasonable or discriminatory and burdens U.S. commerce. Actions include imposition of duties or other import restrictions, suspension or withdrawal of concessions made in trade agreements, and agreements with the offending country to eliminate the practice or policy or to eliminate the burden on U.S. commerce.

1. This box is abstracted from House Committee on Ways and Means, *Overview and Compilation of U.S. Trade Statutes,* WMCP:103-1 (1993), pp. 53-131.

deploying or writing off capital and for workers to find new jobs in other industries.[3] More often, the protection slows down the required contraction of an industry that is no longer competitive and indeed cannot be made competitive.[4]

Slowing down the required contraction reduces adjustment costs in several ways. It allows more of the needed adjustment to occur through depreciation of nonredeployable capital rather than write-offs and through attrition of surplus workers rather than layoffs. By reducing the amount of unemployment at any given time, it makes it less difficult for those who are laid off to find jobs. It may also save firms from bankruptcy, allowing them to contract rather than go out of business completely.

The law has several provisions to make sure that the protection it authorizes is used to ease adjustment costs and not to eliminate the need for adjustment by providing permanent protection. First, it places a limit on how long the restrictions can last--no more than eight years. Second, it provides an opportunity for the domestic industry to submit adjustment plans to the Administration and instructs the President to consider those adjustment plans in deciding whether to grant protection. Third, the standard of "substantial cause of serious injury" ensures that protection is granted only in cases where adjustment costs are significant. The President is charged with considering the national economic and security interests when deciding whether to grant protection--that is, he is charged with balancing the harm protection might bring to consumers and other industries with the potential benefit to the industry and workers seeking the protection.

Although the escape clause lowers adjustment costs, it does not eliminate them. To further ameliorate the remaining costs, a second law in this group provides for Trade Adjustment Assistance, which consists of various kinds of aid, such as training, trade readjustment allowances, employment services, and job-search and relocation allowances, for workers in industries adversely affected by increased import competition.

3. For a discussion of the improved plight of Harley-Davidson after the temporary imposition of special tariffs in the 1980s, see Gary Slutsker, "Hog Wild," *Fortune*, July 12, 1993, pp. 45-46.

4. See Congressional Budget Office, *Has Trade Protection Revitalized Domestic Industries?* (November 1986), pp. xii-xiii.

The second group of trade remedy laws consists of what are often referred to as unfair trade laws. Those laws prohibit or deter foreign trade practices that U.S. policy deems unfair, or they neutralize the effects of such practices. This group includes the antidumping (AD) and countervailing-duty (CVD) laws that are the subject of this study.

Although the United States has two antidumping laws, the Antidumping Act of 1916 is seldom used.[5] Almost all cases are brought under Subtitle B of Title VII (Sections 731-739) of the Tariff Act of 1930, as amended.[6] Subtitle B provides for imposing added duties on imports sold at prices that are "less than fair value" if those imports result in "material injury" to a domestic U.S. industry. The duties equal the amount by which the import price falls below "fair value." Determining what constitutes fair value is somewhat complicated and will be discussed in more detail in chapters 3 and 4. In most cases, however, fair value is approximately equal to the cost of producing the good or to the price of the good in the home market of the firm that exported it to the United States, whichever is greater. "Material injury" means "harm which is not inconsequential, immaterial, or unimportant."[7] Almost any harm that is not negligible is considered to constitute "material injury."

There are two countervailing-duty laws: Subtitle A of Title VII (Sections 701-709) of the Tariff Act of 1930, as amended, and Section 303 of the Tariff Act of 1930, as amended.[8] Both laws provide for imposing an added duty--called a countervailing duty--on imports that a foreign government has subsidized. The duty equals the amount of the subsidy.

Subtitle A of Title VII applies to imports from countries that have signed, or assumed obligations substantially equivalent to, the General Agreement on Tariffs and Trade (GATT) "Agreement on Subsidies and Countervailing Measures," often referred to as the

5. 15 U.S.C. 71, 39 Stat. 798.

6. 19 U.S.C. 1673; 93 Stat. 162, 98 Stat. 3024, 100 Stat. 2921, 102 Stat. 3806.

7. 19 U.S.C. 1677(7)(A), 93 Stat. 178.

8. Subtitle A of Title VII is 19 U.S.C. 1671; 93 Stat. 151, 97 Stat. 1266, 98 Stat. 3024, 100 Stat. 2921, 102 Stat. 1185, 3807. Section 303 is 19 U.S.C. 1303; 46 Stat. 687, 88 Stat. 2049, 93 Stat. 10, 190, 193.

GATT Subsidies Code. In keeping with the requirements of the Subsidies Code, this law provides for countervailing duties only in cases where subsidized imports are causing material injury to the domestic industry producing a like product. Section 303 applies to imports from countries that have neither signed the GATT Subsidies Code nor assumed substantially equivalent obligations. It provides for countervailing duties on all subsidized imports regardless of whether they are causing such material injury.

Since U.S. policy deems dumped and subsidized imports to be unfair, no presumption exists that domestic industries and workers should have to adjust to them. Thus, no fixed time limits for the antidumping and countervailing duties are specified in Title VII of the Tariff Act of 1930. The duties can go on as long as the dumping or subsidies continue. The law does not provide for the domestic industry to submit adjustment plans or for the President to consider such plans. The standard for injury is lower than that in escape-clause cases--unfair imports need only cause "material injury" rather than be a "substantial cause of serious injury"--and there is no provision for the President to consider the national economic interest. Duties are mandatory once it has been determined that imports are dumped or subsidized and are causing material injury to a U.S. industry.

Why This Study?

The United States has historically argued that dumping and subsidization of imports are unfair and objectionable and that they are significant problems. But most other countries do not agree (notwithstanding the provisions in the GATT that allow for AD/CVD laws). Only the United States, Canada, Australia, and the European Community made substantial use of antidumping laws in the 1980s, and the United States was by far the largest user of countervailing-duty laws. Other countries have begun to follow the U.S. lead in imposing antidumping duties, but in many cases they have imposed them on products of U.S. firms in retaliation for U.S. use of antidumping duties against their own firms.

In the last several GATT rounds, the United States has sought stiffer limits on dumping and subsidies, more freedom to expand the coverage of the laws against them, and, as a result of the increased use of antidumping laws against U.S. firms, greater openness and transparency in how other countries administer their AD/CVD laws. Except for greater openness and transparency, other countries have frequently fought the U.S. position. They have tried to rein in U.S. AD/CVD law and practices.

In the Uruguay Round, the U.S. objectives for AD/CVD provisions were to protect current U.S. laws, increase the transparency and due process of other countries' AD/CVD administration, and expand the powers of countries to move aggressively against firms with histories of dumping many products and against various methods of circumventing AD/CVD orders. The United States was almost alone, however, in trying to expand coverage. The final agreement increases transparency and due process, but it does not expand coverage. Moreover, it imposes only modest restraints on U.S. AD/CVD policies.

This study examines the AD/CVD laws in the United States, their history, their economic effects, and how they currently operate. Its purpose is to shed light on the disputes over them and to inform the debate about the Uruguay Round agreement.

Chapter Two

Predatory Pricing, Price Discrimination, Selling Below Cost, and Government Subsidization

The antidumping and countervailing-duty laws connect U.S. trade policy with U.S. antitrust and industrial policies as they relate to predatory pricing, price discrimination, selling below cost, and government subsidies. To understand the implications of these laws and the changes that have occurred in them over the years, it is necessary to know when and why these economic actions occur and how they affect economic welfare.

Predatory Pricing

Predatory pricing is the practice of selling a good or service at a loss in order to drive competitors out of the market and thereby increase the market power of the predator firm, allowing the firm subsequently to raise prices above the levels that prevailed before the predatory pricing began.

When and Why Firms Engage in Predatory Pricing

Firms engage in predatory pricing in hopes of using the resulting increased market power to raise prices and thereby increase their profits. The practice seldom occurs because the conditions that make it possible and profitable seldom exist. In most cases, any attempt at predatory pricing would either fail or end up costing a firm more money than it would gain back later. (See Appendix A for a discussion of the economic theory and evidence relating to this issue).

One would expect predatory pricing to be even more infrequent in international trade than in domestic commerce because the relevant market is the world market rather than a national one. Suppose a Japanese firm were to attempt predatory pricing of its exports to the United States and succeed in eliminating all other firms in the U.S. market while large German firms still had sizable markets in Germany and other countries. Under such a scenario, the potential competition of those German firms in the U.S. market would limit the Japanese firm's ability to raise prices. To succeed with predatory pricing on a world scale--that is, to eliminate competition in all major markets--would require an extremely large firm with an extremely large share of the world market, which is not likely to happen in many cases.

Effects of Predatory Pricing on Economic Welfare

On the infrequent occasions when predatory pricing does occur and succeed, it has a pernicious effect on the economy because it leads to the formation of monopolies. Monopolies reduce the productivity and efficiency of the economy in at least two ways. First, in order to increase prices, they reduce output and sales below what would occur in a competitive market. Normally, a competitive market produces and sells the optimal amount of a good--enough, but no more than enough, to

cover all uses for which the benefit exceeds the cost of production. Thus, forming a monopoly normally results in a reduction of output and sales to suboptimal levels.

Second, lack of competition leads to inefficiency within firms. Often the only measure of a firm's efficiency is its ability to make a profit. If the firm loses money because competitors profitably sell good products at lower prices, the firm is not efficient. Further, the losses force the firm to become more efficient even if the required changes are not in the personal interest of the firm's managers. If the managers resist change, the firm will go broke. With monopolies, no competition exists, so these mechanisms cannot possibly work.

Monopolies also have implications for social equity. They enrich the owners and workers of the monopoly at the expense of the consumer. Whether that is good or bad depends on the relative value one places on the welfare of consumers of the good in question and the welfare of the owners and workers of the monopoly. In the case of monopolies formed by foreign exporters engaging in predatory pricing in the U.S. market, however, the consumers who are hurt are U.S. citizens, whereas the owners of the monopoly who gain are foreign citizens. Hence, the United States clearly loses.

Price Discrimination

Price discrimination is the practice of charging different prices to different customers for the same product, when the varying prices do not merely reflect differences in the cost of providing the product (such as varying transportation costs, quantity discounts, and the like). Usually the discrimination occurs among broad groups of customers (or markets) that differ in some key characteristic such as geographic location, age, wealth, or urgency of demand for the product.

When and Why Firms Engage in Price Discrimination

Price discrimination allows firms to sell products at high prices to customers that are willing to pay them without at the same time losing sales to customers unwilling to pay them. It thereby raises profits, which is why firms engage in it. Price discrimination can occur only when trade between the markets is difficult or impossible. If trade were not difficult or impossible, customers in the lower-price market would purchase the product and sell it to customers in the higher-price market at prices somewhere between the lower and higher prices, thereby making a profit and preventing the would-be price discriminator from making any sales at the higher price.

Price discrimination falls into three categories based on the motive behind the discrimination. The first category, unintentional discrimination, may be illustrated by a case in which a firm has markets in two different countries, and its product spoils rapidly with age. The firm intends to charge the same price in both markets, but after it produces and ships the product, demand falls off unexpectedly in one of the markets. To sell all of the product that has been shipped before it spoils, the firm must lower its price in that market. It does not lower the price in the other market, however, since demand there has not fallen off. Transportation costs and time prevent shipping the product from the market with excess supply to the other market to take advantage of the higher price there. That kind of discrimination clearly involves no malevolent intent on the part of the discriminator, and one would not expect it to recur frequently.

The second category is intentional price discrimination to support predatory pricing. A firm attempting predatory pricing can reduce its initial losses by restricting its predatory prices to the market of the targeted firms while maintaining its normal higher prices elsewhere. Since predatory pricing does not occur frequently, neither does the price discrimination in this category.

The third category, other intentional discrimination, occurs by far the most often. It takes place whenever three conditions hold. The first is that the firm in question has significant market power in at least one of the markets so that it will lose only some--but not all--of its customers if it raises its price slightly. Such market power is common. It may occur because the firm is a monopoly. More often it results from a firm's having significant market share in an industry in which products vary slightly from firm to firm. (For example, a Ford is different from a Chevrolet. If Ford raised its

prices, it would lose some of its customers to Chevrolet, but not all of them.) The difference in the products might be merely one of location. Thus, a drug store could raise its prices slightly without losing all of its customers to a competing store a few miles away because of the time and gas required to drive to the other store.

The second condition is that the firm has more market power in one market than in the other--again, a very common situation. In general, the market power of a firm increases with its share of the market, and a firm seldom has the same share in different markets. Furthermore, differences in culture, taste, wealth, and other factors lead customers in different markets to value products differently. For example, the Japanese have a greater taste for rice than do Americans and thus would probably be willing to pay more for it rather than accept some substitute such as potatoes. Many of the elderly have tight budgets, and many are retired and have time on their hands to shop for a good price. Therefore, the elderly on average are unwilling to pay as much for a product as other people are.

The third condition is the existence of barriers that prevent customers in the lower-price market from selling the product to customers in the higher-price market. Where barriers exist and the other conditions hold, a firm will charge a higher, more monopolistic price in the market in which it has greater market power, and a lower, less monopolistic price in the other.

Barriers preventing trade between different markets are not unusual. They are particularly common in the service sector, and consequently so is price discrimination. For example, medical services cannot be resold. Therefore, before Medicare and Medicaid, price discrimination appeared in the form of lower doctors' fees to the elderly and the poor. The viewing of motion pictures cannot be resold, which has allowed theaters to charge higher prices for adults' tickets than for children's tickets.

Although such barriers are less common in the goods sector, they are not uncommon. For example, prescription drugs cannot be resold from one customer to another, allowing price discrimination to appear in the form of senior citizens' discounts.

Transportation costs and government-imposed trade barriers can hinder trade between customers in different geographic markets, allowing firms to charge different prices in different locations. Such geographic price discrimination within the United States is limited because of the efficient, low-cost transportation system and the lack of trade barriers imposed by state and local governments. Nevertheless, some examples stand out. Restaurants, food concession stands, and stores in airports and sports arenas are notorious for charging high prices, even when they are parts of chain restaurants or stores that charge lower prices elsewhere.

One would expect geographic discrimination to be much more common on an international scale. There are numerous barriers to trade between countries: transportation costs, transportation time, tariffs, quotas, laws against gray-market imports, and different product standards. Moreover, cultural differences between countries are substantial, and the market shares of firms vary from country to country.

Of particular interest for this study, one would expect international price discrimination often to be of the type that is called "dumping." Usually, firms have greater market share in their home market than in their export markets. Hence, they have greater market power at home and therefore charge higher prices there. That is one kind of dumping.

Effects of Price Discrimination on Economic Welfare

The effect of domestic price discrimination on economic efficiency and output is not the same every time. In some cases, efficiency and output are increased, in others they are decreased, and in still others they are unaffected. The effects on particular economic groups, however, are consistent from case to case. Price discrimination increases the profits of the firm engaging in it at the expense of customers in the higher-price market. Those customers lose from price discrimination. The customers in the lower-price market gain because they receive a lower price than they otherwise would. They do not normally, however, receive a lower price than they would in a competitive market. Discrimina-

tion generally results from a firm's charging a more monopolistic price in the higher-price market and a more competitive price in the lower-price market. In almost all cases, both prices are at least as high as the normal competitive market price. (An exception is provided by cases with substantial economies of scale, where the price in the lower-price market can sometimes be below average total cost, but not below the marginal cost of producing the goods for the lower-price market).

In the international context--that is, where a firm charges different prices in different countries--three cases are possible. In the first, a firm exports from its home country to two other countries and charges different prices in the two export markets. Assume, for simplicity, that the home-country price of the exporting firm is not affected by whether the firm is allowed to discriminate in pricing. In that case, the exporting country and the country receiving the lower price both gain, and the country receiving the higher price loses. In the country receiving the lower price, the customers gain and the competing firms lose. Moreover, the total gain to the consumers is greater than the aggregate loss to the competing firms.

In the second case, the exporting firm is in the same country as the lower-price market. The importing country has the higher-price market. In that case, the exporting country clearly gains from price discrimination, since both its customers and its exporting firm gain from it. The importing country clearly loses, since its customers pay a higher price for the imports.

In the third case, the exporting firm is in the same country as the higher-price market. The importing country has the lower-price market. In that case, the net effect on the exporting country is unclear. The country's exporting firm gains, but its consuming citizens and firms must pay higher prices. It is unclear whether the gain to the exporting firm or the loss to the consumers is larger.

The importing country definitely gains from the price discrimination, since its customers pay lower prices for the imports than they would without price discrimination. The firms that compete with the imports are hurt by the price discrimination because it results in an increase in imports and a lower price. The loss to those firms, however, is normally smaller than the gain to the customers.

The third case is known as dumping. If the United States was the importing country in that case, its antidumping law would impose added duties on the imports in question. Further, if the United States was the lower-price importing country in the first case and the exporting firm had few sales in its home market, the U.S. antidumping law would impose added duties on imports in that case also. Thus, U.S. antidumping law imposes added duties on imports in both cases where price discrimination by the foreign exporter benefits the United States economically. Yet it does not impose added duties when price discrimination harms the United States economically.

Selling Below Cost

Selling below cost means selling a good or service at a price lower than the average total cost of production per unit of output. Depending on the situation, the average total cost may or may not include a reasonable rate of return on capital, which would show up in a firm's income statement as profit.

When and Why Firms Sell Below Cost

Many people think that selling below cost is somewhat nefarious. Since firms are in business to make a profit, the thinking goes, they could not possibly sell below cost intentionally unless they were engaging in predatory pricing. In fact, however, selling below cost is common and seldom has anything to do with predatory pricing. Some of the reasons for it follow.

Recessions and Mispredicted Demand. During recessions, demand for some industries' products can fall substantially below output capacity. In that case, the price often drops below the average total cost for each firm, and thus all firms lose money if they continue to sell their products. Normally, to maximize profits in such situations, a firm continues to sell its product as long as the price remains above average variable cost. By so doing, the firm earns enough revenue to cover the cost of staying open and at least a little of the fixed costs (such as mortgage or other interest payments) that it must pay regardless of whether it remains open or not. Thus, the firm loses less money than it would if it quit selling altogether.

Introduction of New Products. Firms often lose money when new products are introduced. An extreme example is provided by General Motors' Saturn cars, which were still unprofitable several years after they were introduced. New products often do not sell in large quantities until substantial amounts have been spent on advertising and consumers have had time to learn about the products and their quality. Moreover, a steep learning curve is likely to occur when the product is introduced as the firm learns how to produce, advertise, distribute, and sell the product most efficiently. If the firm is competing with products of other firms that are already established, it cannot charge a price high enough to cover its initial high costs at the low initial rates of sale without losing its customers to the competitors.

Loss Leaders. Retail stores frequently advertise individual products for sale at extremely low prices as a means of getting people to come to the store. These products are often called "loss leaders." Although the advertised sales are unprofitable, the store owners expect that many of the people lured into the store will see and buy other products at profitable prices.

In effect, loss leaders are a form of indirect advertising, and the losses on them are essentially an advertising cost. Directly advertising to everyone every product a store sells is expensive and inefficient: not everyone is in the market for the store's products. The people who come into the store for the advertised loss leaders, however, by self-selection are people interested in purchasing either those or similar, more profitable products. Therefore, loss leaders may be more cost-effective than widespread direct advertising to the public.

Life-Cycle Pricing. Sales below cost sometimes occur in the early parts of product life cycles in industries with steep learning curves. For example, in the semiconductor industry, the average cost of producing a given chip usually falls substantially over time as the firm learns through production experience how to increase yields (the fraction of produced chips that are not defective) and otherwise increase the efficiency of production. In such industries, a company may find it worthwhile to price a new chip below the initial average cost at the time of its introduction but higher than the cost averaged over the entire life cycle of the chip. The resulting initial losses are effectively part of the cost of developing the technology to produce the chip. The cost will be recouped when learning-by-doing reduces the cost below the price.

Life-cycle pricing can speed up the pace at which production costs decline and new products are introduced and accepted into the economy. If a firm had to charge prices above production costs on new products for which learning-by-doing is an important part of production technology, initial prices in some cases could be so high as to discourage sales. The resulting low production levels would lengthen the time it takes a firm to learn how to reduce its costs and improve the quality of its product. Thus, consumers would continue to pay higher prices than if the firm had increased production and reduced costs more rapidly.

Legal Constraints. Sometimes legal constraints force firms to sell below cost. For example, in recent years U.S. automobile firms have continued to make subcompact cars even though these cars are usually unprofitable for U.S. firms. The possibility that the new Chrysler Neon subcompact car will prove an exception and actually be profitable has generated considerable attention. One might wonder why U.S. firms continue making these cars if they are unprofitable. Some have argued that at least part of the reason is that the cars help the firms meet the legally imposed corporate average fuel economy standards.

Laws restricting layoffs of workers provide another example. In many cases under U.S. law, a firm must provide a minimum period of advance notice before it can close a plant and permanently lay off its workers. Most likely a firm would not decide to close a plant unless it was losing money. The plant would probably continue to lose money during the legal minimum period between the advance notice and the final closing and layoffs, which means that sales of its products would be below cost.

How Selling Below Cost Affects Economic Welfare

Other than the infrequent cases of predatory pricing, the instances of selling below cost that occur in a free market generally benefit both parties to the transaction. Clearly, consumers benefit from low prices, and firms would certainly not sell below cost if doing so did not provide some benefit to them.

Although both of the parties to the below-cost sales that occur in a free market generally benefit, firms that compete with the seller of below-cost sales may lose sales of their own and thereby be hurt. U.S. policy, however, has generally not recognized this harm as sufficient reason to prohibit below-cost sales by domestic firms in the domestic market. There are good reasons for such a policy. One is that, even though it would help the competitors to the firm selling below cost, such a prohibition would usually hurt consumers and the firm even more.

Another reason is that such a prohibition would defeat one of the major advantages of a free market over a command economy. In order to make good decisions, a command economy requires a vast government bureaucracy with prodigious knowledge of the costs of firms. Because no one person or even a reasonably small group of people can possibly obtain all of that information and process it efficiently and accurately to make good decisions, command economies do not work well. Free markets eliminate the need for such a bureaucracy with such vast knowledge. Left to their own devices, most firms will sell most products at prices that cover total costs most of the time. Those firms that do not will go bankrupt and disappear. Trying to enforce a law requiring that prices cover total costs for all goods all of the time would reinstitute the need for a bureaucracy with vast, unobtainable knowledge.

The reasoning changes slightly in the case of a foreign firm selling below cost in the U.S. market. In that case, the U.S. cost-benefit calculation includes only the consumer, who benefits from the sale, and the competitor firms, which lose. The firm making the sale is not part of the calculation if one is concerned solely with the U.S. self-interest. Nevertheless, the gain to the consumer alone would normally be larger than the loss to the domestic competitor firms.

For a given level of production and sales, a drop in price as a result of competition from below-cost sales by foreign firms will initially help U.S. consumers to the same degree that it hurts competing U.S. producers. Production and sales do not remain the same, however. Responding to the lower price, consumers purchase more of the product and therefore gain more. Also in response to the lower price, competing U.S. producers reduce their sales in order to cut their losses. Thus, the end result is that U.S. consumers gain more than competing U.S. producers lose.

Below-cost sales by a foreign firm in a third-country market could have negative effects on U.S. competitor firms that normally sell in that market. Moreover, those negative effects might not be offset by gains to U.S. consumers (since U.S. consumers do not purchase in third-country markets) or by indirect gains to other U.S. exporters or import-competing firms. Furthermore, U.S. law would not cover such cases, since no sales occur in the United States. Those cases would require a general policy in the General Agreement on Tariffs and Trade requiring all countries to prohibit below-cost imports.

The GATT has no such policy, nor would it be consistent for the United States to favor such a policy while at the same time maintaining its current policy of allowing domestic firms to sell below cost in interstate and intrastate trade. The United States would benefit from such a GATT policy in some cases in which its exporting firms no longer had to compete with below-cost sales by foreign firms in foreign markets. In other cases, however, such as those in which U.S. firms wish to make below-cost sales and those in which U.S. consumers or consuming firms could no longer benefit from below-cost sales by foreign firms, such a policy would harm the United States.

Summing up the costs and benefits, the United States probably would not fare differently from the rest of the world under such a policy. Further, the cost-benefit ratio to the world would be roughly the same as the cost-benefit ratio to the United States for a policy of prohibiting below-cost sales in interstate and intrastate trade. Hence, the cost-benefit ratio to the United States of such a GATT policy would be roughly the same as the cost-benefit ratio to the United States of a policy of prohibiting below-cost sales in interstate and intrastate trade. Therefore, consideration of net economic effects argues for taking the same position on both policies.

Government Subsidies

Government subsidies are difficult to define because they can have so many forms and objectives. Gener-

ally, though, they are grants of some kind made by a government to reduce the price or cost of something below the normal market price or cost--or, in some cases, below what the price or cost should be (whatever that is). The grants may take many forms, such as financial payments, tax abatements, in-kind goods or services, below-market rates on loans, and below-market prices on government-provided goods and services.

Sometimes it is a matter of opinion whether the government is providing a subsidy. The airplane manufacturing industry provides a good example in international trade. The U.S. military paid for substantial amounts of research and development (R&D) in that industry. If the results of the R&D could be used only in military aircraft, that funding would represent government funding of defense, not a subsidy. The European Union (EU) argues, however, that some of the results can also be used in commercial airliners. If so, the cost of the part of the R&D that has both military and civilian uses should be allocated partially to the Department of Defense and partially to the civilian airliner divisions of the aircraft companies. The costs allocated to the civilian divisions should be recovered in the prices of the airliners they sell.

Disagreement between the United States and the EU over what part of the total military payment to airplane manufacturers might be considered a commercial subsidy and over the related question of how much the EU should be allowed to subsidize its own industry to compete with the U.S. industry has developed into a major dispute.

When and Why Governments Subsidize

Governments subsidize for many reasons--including to promote scientific research and development, prevent layoffs or otherwise promote full employment, maintain or increase the tax base, help firms comply with pollution control requirements, promote regional development, keep firms that are considered essential to the national security from going bankrupt, and advance social equity.

All countries subsidize to some degree. In the United States, state and local governments frequently provide tax abatements and other subsidies to encourage firms to locate manufacturing plants or corporate headquarters in their jurisdictions (witness the competition among these governments for the General Motors Saturn plant). Most states also provide free education from kindergarten through grade 12 and subsidize colleges and universities. The federal government funds substantial amounts of research at many colleges and universities. It subsidizes the provision of electricity by the Tennessee Valley Authority and various other hydroelectric power authorities. It gives subsidies to research on technology for producing semiconductors. The space program is largely a research and development program funded almost entirely by the federal government. Moreover, the Clinton Administration recently proposed subsidizing research into electric cars.

Effects of Subsidization on Economic Welfare

To understand the effects of subsidies on economic welfare, consider first the case where the subsidy is granted by the same country that purchases the subsidized good or service and then how the situation changes when another country grants the subsidy.

When the Subsidy Is Granted by the Same Country That Purchases the Output. In most (but not all) cases, subsidies have a net detrimental effect on economic efficiency and output, partly because they distort market prices and partly because financing them requires taxes that also distort market prices.

In a well-functioning competitive market with no government intervention, the prices that prevail tend to reflect both the costs of producing the respective goods and the values that consumers place on them. As a result, the costs of production and consumer valuations are equated, which promotes maximum efficiency and productivity. Economists have formalized that proposition in a rigorously proven theorem--sometimes called the Fundamental Welfare Theorem--that states that under certain conditions that generally correspond with those of a well-functioning competitive market, a free market without government interventions will produce the most efficient and productive outcome possible.

The theorem provides a road map for determining when subsidies can be designed to improve overall economic efficiency and productivity and when they can

only be detrimental. In cases closely approximating the conditions of the theorem, subsidies will generally harm economic welfare because they distort prices so that prices no longer equate consumer value with the cost of production. They may increase output in the subsidized industry, but that in turn causes the industry to use more inputs than it would otherwise. The resulting decline in the output of other industries, which would be deprived of those inputs, would be greater in value than the increase in the output of the subsidized industry. Subsidies can help, but only when they promote a noneconomic goal--such as social equity or national security--that is deemed more important than the decline in aggregate output, or when the conditions of the Fundamental Welfare Theorem do not closely approximate reality, which usually means that well-functioning competitive markets do not exist.

Basic scientific research is an example of the last situation. One of the conditions required for the theorem is that the benefits of the product in question be confinable to the firm producing it. The product of firms doing scientific research is knowledge, which in many cases is difficult or impossible for the research firm that produces it to keep secret from competing firms. In the case of applied product research, patents are granted to help confine the benefits of the knowledge to the firm (or person) developing it. The patents enable the firm to sell the knowledge or the benefits of it (which might be products produced using the knowledge) and thereby be remunerated for producing it.

In basic research, however, patents are generally inadequate or infeasible because the knowledge gained cannot be kept from others. As a result, the people and firms that do basic research receive insufficient remuneration to give them an incentive to do as much of it as would be optimal for society. Hence, subsidies of basic research can improve economic welfare, and many countries have opted to grant such subsidies.

Even in cases where the conditions of the Fundamental Welfare Theorem are not a good approximation, subsidies can be detrimental. Subsidies ultimately require taxes to finance them, and taxes create their own distortions that reduce economic efficiency and productivity. Moreover, it is frequently impossible to know in a given case whether subsidies would be beneficial to the economy as a whole and, if so, how large they should be.

Subsidies and International Trade. The cost-benefit calculus changes when the country purchasing the subsidized good is not the same country as the one granting the subsidy. There are two possible cases: general subsidies equally available to all industries, and specific subsidies available only to (or preferentially available to) individual industries or groups of industries.

Unlikely as it may seem, general subsidies equally available to all industries in proportion to the value of their output have no effect on trade. Such subsidies decrease the prices of all products by the same percentage. If the exchange rate were to stay constant, the decrease in prices would lead foreign countries to purchase more of the products. The exchange rate does not stay the same, however. Increased foreign purchases require increased foreign holdings of the subsidizing country's currency with which to make the purchases. When a foreign country attempts to purchase that currency, it drives up the currency's price (the exchange rate), exactly offsetting the reduction in the prices of the goods caused by the subsidy. As a result, the foreign-currency prices of the goods are the same with the subsidy as without it, and consequently the subsidy has no effect on trade.[1]

Subsidies restricted to or given preferentially to particular industries do affect trade. The exchange rate adjusts enough to offset some average of the price decreases made by all industries. The prices in subsidized industries decrease more than the average, however, so that the exchange rate adjustment does not completely offset them. Further, the prices in unsubsidized industries do not decrease at all, so they are more than offset.

Countries granting specific subsidies on goods that are exported are almost always harmed. Such subsidies result in the country giving away the good for less than it costs to produce. From the perspective of a nonsubsidizing country, the analysis is exactly the same as that for sales below cost. Thus, if a country imports subsidized products, its domestic firms that compete with the imports are harmed, but its consumers generally benefit more than the firms are harmed. Hence, the economy benefits from the subsidized imports. In the case of subsidized sales to third countries, the nonsubsidizing

1. In the case of a fixed-exchange-rate system rather than the floating-rate system that the United States maintains, a different mechanism causes the same result.

country can be harmed because its exporting firms lose sales (or make them at lower prices) to the third-country market, but its consumers do not benefit. Moreover, the subsidizing country is also harmed in those cases, which is different from what happens with sales below cost.

The aircraft industry again provides an example. One study ran simulations indicating that European subsidies to Airbus Industries for the A300 aircraft (which competes with the Boeing 767) may harm both Europe and the United States.[2] The United States is harmed because the competition from Airbus reduces what would otherwise be monopoly profits of the Boeing Company. Boeing's reduced profits are not completely offset by the gains to U.S. purchasers of aircraft since many of the A300 aircraft are sold abroad.

The harm to Europe is less certain. The subsidies are a loss to Europeans, but the reduced market price of aircraft benefits European purchasers of aircraft, who would otherwise have to pay monopoly prices to Boeing. The simulations in the study indicate that the cost of the subsidy may be larger than the gain to European purchasers of aircraft, though this result is not certain.

2. Richard Baldwin and Paul Krugman, "Industrial Policy and International Competition in Wide-Bodied Jet Aircraft," in Robert E. Baldwin, ed., *Trade Policy Issues and Empirical Analysis* (Chicago: University of Chicago Press, 1988), pp. 45-71.

Although the subsidizing country almost always loses economically from subsidizing its exports (or their production), there are exceptions. In the 1980s, a body of economic literature emerged known as "strategic trade theory."[3] According to that literature, in some cases in which industries have economies of scale or positive externalities (which, of course, violate the conditions of the Fundamental Welfare Theorem), it is theoretically possible for a country to gain from subsidizing the industry or from protecting it with tariffs or quotas.[4] The empirical literature to date, which has focused mainly on economies of scale, indicates that the gain from such subsidies and trade barriers is usually small, that determining which industries will yield such gains is difficult, and that the losses from nonoptimal tariffs and subsidies relative to free trade are likely to be significant.

3. Two good collections of writings in this literature are Paul R. Krugman, ed., *Strategic Trade Policy and the New International Economics* (Cambridge, Mass.: MIT Press, 1988), and Paul Krugman and Alasdair Smith, eds., *Empirical Studies of Strategic Trade Policy* (Chicago: University of Chicago Press, 1994).

4. Externalities refers to divergences between the cost of production to an industry and the cost to society. A negative externality exists when the cost to society is greater than the cost to the industry. An example of a negative externality is pollution. The cost of production for an industry is the cost of raw materials, land, and labor. The cost to society is the cost of the materials, land, and labor that the industry uses plus the unpleasantness and damage caused by pollution. There can also be positive externalities when the cost to an industry is greater than the cost to society.

Chapter Three

The Evolution of U.S. Laws: An Economic Perspective

The net economic welfare of the United States would clearly be promoted by treating the pricing practices of foreign producers in the United States similarly to the way the antitrust laws treat the pricing practices of domestic firms. In other words, if the United States prohibited predatory pricing but allowed most nonpredatory price discrimination and selling below cost to go unfettered, the U.S. economy would benefit. That was approximately U.S. policy early in this century. Antidumping law was a reasonably close approximation to a prohibition on predatory pricing to complement the Sherman Act, which made such pricing by domestic firms illegal.

Over the years, however, antitrust law and antidumping law have taken strikingly divergent paths. At least in recent decades, the courts have tightened requirements for proving predatory pricing under the antitrust laws. Their actions reflect economic research indicating that such behavior is infrequent and seldom rational. They have also interpreted the antitrust laws to prohibit mainly the small subset of cases in which price discrimination is predatory. Harm to the economy can be demonstrated reliably mainly for cases in this subset, whereas vigorous prosecution of cases that do not represent predatory price discrimination could diminish the beneficial effects of competition.

Antidumping law has long been moving in the opposite direction. The definition of dumping has been expanded to include most selling below cost, as well as price discrimination in which a lower price is charged in the U.S. market than in the exporter's home market. The law provides for duties on any dumped imports that injure U.S. firms. Seldom does dumping by the current definition have anything to do with predatory pricing, and antidumping duties are not restricted in any way to cases of predatory pricing.

Thus, the pricing behavior of foreign firms, which at one time was treated similarly to that of U.S. firms, is now treated much differently. The emphasis of the law relating to pricing by U.S. firms (antitrust law) is on maximizing consumer welfare and the efficiency and productivity of the economy by preserving competition. Aside from ensuring the survival of enough firms to maintain competition, little or no concern is shown for firms suffering from competitors' low prices. Yet the emphasis of the law relating to pricing by foreign firms (antidumping law) is on protecting domestic industry by diminishing competition--the competition from foreign firms. Antidumping law provides protection regardless--and usually to the detriment--of the consumer and the efficiency and productivity of the economy as a whole.

As is the case with dumping, a foreign country could use subsidies to aid the predatory pricing of its firms' products in the United States. Unlike antidumping law, however, U.S. countervailing-duty law has never attempted to distinguish cases of possible predatory behavior from the much more numerous nonpredatory cases. Currently, the law serves to protect particular domestic industries without regard for the effects on consumers or the trade, efficiency, and productivity of the rest of the economy.

Countervailing-duty law serves other functions, however, besides protection. Although the net effect of foreign subsidies on the U.S. economy is generally ben-

eficial, the subsidies generate pressures for the U.S. government to respond with countersubsidies. U.S. countervailing-duty law acts as a disincentive to foreign governments to subsidize their industries. Further, when it fails to deter subsidization, it alleviates pressure on the U.S. government to respond with countersubsidies. Several reasons account for that effect. Although countersubsidies are less damaging to the economy than are countervailing duties, countersubsidies increase the government's budget problems whereas countervailing duties alleviate them. Further, countersubsidies carry the risk of escalating rounds of tit-for-tat retaliatory subsidies by the United States and other countries.

Antitrust Law

In the last quarter of the 18th century, the spread of the industrial revolution from Britain to Europe, the United States, Russia, and Japan brought with it the development of large industrial concerns with substantial market power.[1] In some cases, that power was enhanced by the formation of trusts, cartels, and other monopolies. Such market power was subject, or thought to be subject, to various abuses, among which were high prices and predatory pricing.

The Sherman Act

In the United States, concerns about monopoly abuses resulted in the passage of a series of antitrust laws. The first such law was the Sherman Act, passed in 1890.[2]

The Sherman Act prohibited "every contract, combination in the form of trust or otherwise, or conspiracy, in restraint of trade or commerce among the several States, or with foreign nations."[3] It also made it illegal to "monopolize, or attempt to monopolize, or combine or conspire with any other person or persons, to monopolize any part of the trade or commerce among the several States, or with foreign nations."[4] Violations of those provisions were misdemeanors punishable by fines, imprisonment, or both. U.S. attorneys could obtain injunctions to prevent or restrain violations. Furthermore, private parties injured by violations could bring suit against the perpetrators and recover treble damages.[5]

The courts have long interpreted the Sherman Act to prohibit predatory pricing. Without a showing of predatory intent, price discrimination and selling below cost are not held to be violations of the law.[6]

In the past two decades, the courts and the Federal Trade Commission have become more skeptical of claims of predatory pricing than they were previously. They tend to look for evidence of such factors as prices below average variable cost (not merely below average total cost), large enough market share and sufficient barriers to other firms' entering the market to make monopoly and subsequent price increases feasible, and local price cutting in particular markets rather than general price cutting in all markets.[7] Mere price discrimination or selling below average total cost are not generally sufficient for demonstrating predatory pricing.

The Federal Trade Commission Act and the Clayton Act

Dissatisfaction with the courts' interpretation of the Sherman Act led to the passage in 1914 of the Federal

1. This section is based on discussions contained in F.M. Scherer and David Ross, *Industrial Market Structure and Economic Performance*, 3rd ed. (Boston: Houghton Mifflin Company, 1990), pp. 449-472 and 508-516; George C. Thompson and Gerald P. Brady, *Text, Cases and Materials on Antitrust Fundamentals*, 3rd ed. (St. Paul, Minn.: West Publishing Company, 1979), pp. 11-16; Jacob Viner, *Dumping: A Problem in International Trade* (Chicago: University of Chicago Press, 1923), p. 239; and the laws in question.

2. 15 U.S.C. 1, 26 Stat. 209.

3. Ibid.

4. 15 U.S.C. 2, 26 Stat. 209.

5. 26 Stat. 209, Sec. 1, 2, and 7.

6. See Scherer and Ross, *Industrial Market Structure and Economic Performance*, pp. 449-472 for a discussion of the history of predatory pricing and other related jurisprudence under the Sherman Act, and pp. 508-516 for a discussion of antitrust policies toward price discrimination.

7. Not all economists are satisfied that the courts have kept completely up to date with the economics literature on predatory pricing. See Alvin K. Klevorick, "The Current State of the Law and Economics of Predatory Pricing," *American Economic Association Papers and Proceedings* (May 1993), pp. 162-167.

Trade Commission Act and the Clayton Act.[8] The Federal Trade Commission Act created the Federal Trade Commission (FTC), which the act empowered to proceed against "unfair methods of competition" in interstate or foreign commerce.[9] The general and undefined nature of the latter power resulted from the view that businesses would always find new ways of suppressing competition that did not violate any given list of prohibited behaviors. The act empowered the FTC to proceed against each new form of unfair behavior as it appears and is recognized as a problem.

FTC proceedings are administrative and prospective (that is, the FTC can proscribe future behavior, but cannot punish past behavior). When the FTC believes a firm is engaging in unfair competition, it issues a complaint that is heard before an administrative law judge. If the judge agrees there is a violation, he or she issues an order for the firm to cease and desist. That order can be appealed to the courts. Assuming the order either is not appealed or is upheld on appeal, the firm is subject to fines if it continues the behavior. On judicial review, a decree to obey the order can be issued, in which case violations make the firm liable to be held in contempt of court.

Section 2 of the Clayton Act was the first law to restrict price discrimination outside the railroad industry.[10] It prohibited charging different prices to different customers when: (1) the price difference did not reflect differences in cost, grade, quality, or quantity; (2) it was not a good faith effort to meet competitive pressures; and (3) "the effect of such discrimination may be to substantially lessen competition or tend to create a monopoly."[11]

The Clayton Act authorized the Federal Trade Commission to enforce the act's provisions through the sort of administrative and prospective proceedings described above.[12] It authorized U.S. attorneys to obtain civil injunctions to prevent and restrain violations of the act, and it gave private parties the right to obtain injunctions to protect them from violations of the antitrust laws generally.[13] It also gave parties injured by violations of the antitrust laws the right to sue for treble damages.[14] Finally, it made individual directors, officers, or agents of corporations violating penal provisions of the antitrust laws guilty of misdemeanor violations, if they directed, ordered, or carried out the corporate violation.[15] In addition, it subjected them to punishment by fines and imprisonment.

The Robinson-Patman Act

In the 1920s and 1930s, the large chain retail stores rose to prominence. The market power of some of these chains enabled them to negotiate lower prices from manufacturers than the traditional small independent retailers could obtain. For that and other reasons, the small retailers found it difficult to compete, leading to pressure for the Congress to do something to help them. That pressure and dissatisfaction with the success of the Clayton Act in preventing price discrimination led to passage in 1936 of the Robinson-Patman Act.[16]

The Robinson-Patman Act amended the Clayton Act to make it unlawful "to discriminate in price between different purchasers of commodities of like grade and quality" where the effect "may be substantially to lessen competition or tend to create a monopoly in any line of commerce, *or to injure, destroy, or prevent competition* [emphasis added] with any person who either grants or knowingly receives the benefit of such

8. The Federal Trade Commission Act is 15 U.S.C. 41, 38 Stat. 717; the Clayton Act is 15 U.S.C. 12, 38 Stat. 730.

9. 15 U.S.C. 45, 38 Stat. 719.

10. Scherer and Ross report that "[t]he Interstate Commerce Act of 1887 prohibited 'undue' discrimination in railroad rates, with special bars against personal discrimination and rates that were lower on the same line for longer than shorter hauls 'under substantially similar circumstances and conditions.'" See Scherer and Ross, *Industrial Market Structure and Economic Performance*, pp. 508-509.

11. 15 U.S.C. 13(a), 38 Stat. 730.

12. 15 U.S.C. 21, 38 Stat. 734. An exception was made for common carriers, for which enforcement authority was placed in the Interstate Commerce Commission. Exceptions were also made for banks, banking associations, and trusts, for which enforcement authority was placed in the Federal Reserve Board.

13. 15 U.S.C. 25, 26; 38 Stat. 736, 737.

14. 15 U.S.C. 15(a), 38 Stat. 731.

15. 15 U.S.C. 24, 38 Stat. 736.

16. 15 U.S.C. 13, 21a; 49 Stat. 1526, 1527. See Scherer and Ross, *Industrial Market Structure and Economic Performance*, p. 509.

discrimination, or with customers of either of them."[17] Exceptions were made for price differences resulting from differences in cost, charging low prices to meet those of a competitor, disposing of deteriorating perishable goods or obsolete goods, and disposing of goods in a closeout or bankruptcy sale. The act also prohibited buyers from knowingly inducing or receiving a prohibited discrimination in price. The act made some violations criminal offenses punishable by fines and imprisonment.

A key issue relates to the phrase emphasized above: "or to injure, destroy, or prevent competition." Does "competition" refer to competitors of the firm engaging in price discrimination or to the vigor of competition between and among the price-discriminating firm and its competitors? The former could make almost all price discrimination illegal, depending on the standard of injury. The latter is a much more demanding standard. If the price-discriminating firm takes away 10 percent of the market share of each of its competitors but does not drive any of them out of the market, each competitor is injured. Yet the loss does not affect the vigor of competition between and among the competitors and the price-discriminating firm.

The courts have decided this question differently depending on the relation of the injured firms to the participants in the low-price sale.[18] The injured firms might be competitors of the price-discriminating firm, competitors of the firm receiving the lower price, or competitors of the customers of the firm receiving the lower price. Injury to the first of these groups--competitors of the price-discriminating firm--is the sort of injury that is at issue in predatory pricing and dumping cases. In cases of such injury, the courts have generally interpreted "injury to competition" to mean "injury to the vigor of competition." Over the years, the standards for proving such injury have evolved to the point that they are now essentially identical with those for predatory pricing cases under the Sherman Act. Thus, the sort of price discrimination that is the domestic analog to dumping is illegal only in cases of predatory pricing.

17. 15 U.S.C. 13(a), 49 Stat. 1526.

18. Scherer and Ross, *Industrial Market Structure and Economic Performance*, pp. 512-513.

The History of Antidumping Law Through World War II

Concern about abuses of monopoly power did not remain restricted to the domestic front. The same abuses could occur in international trade, where they sometimes caused even more concern because they carried collateral implications for national security. The main abuse that is of interest for this study is predatory pricing. Then, as now, international predatory pricing was often lumped together with, and not distinguished from, international price discrimination that charged lower prices on exports than on the same goods sold in the home market. Both were referred to as dumping.

Early on, most dumping was by British firms, since they led the industrial revolution and were therefore the main monopolies in existence. U.S. and German firms became the world's major dumpers in the late 1800s and early 1900s. In the United States, high tariffs protected domestic firms from import competition, allowing them to charge high domestic prices that they could not maintain on their exports abroad where they had competition. In Germany, the firms in various industries joined together into cartels to maintain high domestic prices that they could not maintain on their exports.

Only New Zealand, Australia, Canada, and South Africa passed any antidumping legislation before 1914, which suggests that most countries did not consider dumping to be a problem.[19] Nevertheless, domestic producers pressed for such laws in the United States and other countries. Such laws provided an opportune vehicle for obtaining protection for two reasons. First, with many (if not most) firms having greater market share and monopoly power in their home markets than abroad, they would predictably charge higher prices at home than abroad--that is, much of international trade would be dumped. Second, the possibility of predatory pricing allowed the producers seeking protection to gain support among consumers, whose interests are normally harmed by protection more than producers' interests are benefited.

19. William A. Wares, *The Theory of Dumping and American Commercial Policy* (Lexington, Mass: Lexington Books, D.C. Heath, 1977), pp. 13-14.

The Sherman Act

In the United States, the Sherman Act might be expected to prohibit predatory dumping by foreign exporters, obviating the need for an antidumping law to control it. The act has been interpreted to prohibit predatory pricing, and it explicitly states that it applies to combinations and conspiracies "in restraint of trade or commerce among the several States, *or with foreign nations* [emphasis added]."[20] An early Supreme Court decision, however, held that the United States had no jurisdiction under the Sherman Act over acts occurring in other countries.[21] Thus, presumably, if a foreign firm was to come to the United States and sell its exports at predatory prices, it would violate the Sherman Act. If, however, it sold them in its home country at predatory prices to an exporter (or U.S. importer) who then exported them to the United States at a profit, the act presumably would not apply.[22]

Thus, at least implicitly, the question arose as to how to regulate the pricing behavior of foreign firms in the United States. One way was to amend the Sherman Act (and any other subsequent acts relevant to pricing in the United States) to grant the United States jurisdiction for cases involving goods sold in the United States, even if the violation occurred in another country. The same law would then apply to the pricing of both imports and domestically produced goods. Another way was to pass separate laws for pricing of imports. The Congress chose the latter route, and it proved to be a critical decision.

Although the initial laws regulating the pricing of imports were similar to those regulating the pricing of domestically produced goods, the evolutionary paths of the two sets of laws and policies have diverged drastically over time. Antidumping law has fairly consistently evolved in the direction of making it easier to find foreign firms responsible for dumping. Indeed, it is now much easier to find foreign firms to be dumping than it is to find domestic firms guilty of corresponding pricing violations under the antitrust laws.

Section 73 of the Wilson Tariff Act of 1894

The first law relating specifically to monopolistic practices in international trade was Section 73 of the Wilson Tariff Act of 1894, which used language that bore similarity to that of the Sherman Act. It declared:

> That every combination, conspiracy, trust, agreement, or contract is hereby declared to be contrary to public policy, illegal, and void, when the same is made by or between two or more persons or corporations either of whom is engaged in importing any article from any foreign country into the United States, and when such combination, conspiracy, trust, agreement, or contract is intended to operate in restraint of lawful trade, or free competition in lawful trade or commerce, or to increase the market price in any part of the United States. . . .[23]

Violations were criminal offenses subject to fines, imprisonment, or both.

Collusion by domestic importers in predatory pricing schemes of foreign exporters would appear to qualify as a violation of the act. Normally, however, only the exporter--not the importer--is involved with predatory intent, and the exporter's behavior occurs outside the United States.[24] The law was passed before the Supreme Court had ruled acts outside the United States to be beyond the jurisdiction of the Sherman Act, and the logic of that ruling would appear to apply to the Wilson Tariff Act as well.[25] In any case, proving predatory intent is difficult, and cases under the law were rare.

20. 15 U.S.C. 1, 26 Stat. 209.

21. *American Banana Co. v. United Fruit Co.*, 213 U.S. 347, cited in Viner, *Dumping*, p. 240.

22. More recently the Court has held that the Sherman Act *does* apply to acts committed abroad. For the more recent interpretation, see Joseph P. Griffin, "Extraterritorial Application of U.S. Antitrust Laws Clarified by United States Supreme Court: An Examination of the Jurisdiction Given Courts Under the Sherman Act," *Federal Bar News & Journal*, vol. 40 (October 1993), pp. 564-569, which discusses *Hartford Fire Insurance Company v. California* and the jurisprudence leading up to it.

23. 15 U.S.C. 8, 28 Stat. 570.

24. Indeed, some have argued that the major threat of monopolization of U.S. trade at the time the act was passed came from domestic firms, not from foreign firms, and that predatory pricing of imports was therefore not among the concerns the act was intended to address.

25. Viner, *Dumping*.

Thus, the act provided little protection for domestic producers from low-priced imports.

The Antidumping Act of 1916

Against a backdrop of World War I and accompanying public fears of Germany and its cartels, the Wilson administration--sympathetic to concerns about predatory dumping--recommended further extending the domestic laws against unfair competition (the antitrust laws) to people and firms involved with importing.[26]

The Antidumping Act of 1916 (formally, Sections 800-801 of the Revenue Act of 1916), subsequently passed by the Congress, made it illegal to import goods, or sell imported goods, at prices substantially less than the market value in the principal markets of the country producing the imports, "with the intent of destroying or injuring an industry in the United States, or of preventing the establishment of an industry in the United States, or of restraining or monopolizing any part of trade and commerce in such articles in the United States."[27] Violation of the law was a criminal offense punishable by a fine, imprisonment, or both. Parties injured by a violation could sue for treble damages.

Unlike Section 73 of the Wilson Tariff Act of 1894, this act is clearly directed squarely at something approximating predatory pricing. The approximation is not perfect for several reason. First, whereas the language of the Wilson Tariff Act came about as close to antitrust concepts as is possible, aiming to prevent restraint of trade or free competition, and subsequent higher prices to consumers, the Antidumping Act of 1916 refers to restraint and monopolization of trade but makes no references to higher prices for consumers.

Second, the use of the phrase "or of restraining or monopolizing . . . trade" in the quotation above rather than something such as "in order to restrain or monopolize trade" indicates that low prices with the intent to destroy, injure, or prevent the establishment of an industry in the United States are illegal even when there is no intent to restrain or monopolize trade.

Finally, if the phrase "preventing the establishment of an industry in the United States" is interpreted to mean that foreign firms are prohibited from constantly maintaining low prices so that no domestic firms ever attempt to enter the industry, then the act prohibits "limit pricing"--the practice of pricing at a level sufficiently low to deter the entry of new firms--in addition to predatory pricing. From an economic point of view, limit pricing is less objectionable than predatory pricing, and not objectionable at all when there are no barriers to entry. The low prices cannot end and be replaced by high monopoly prices. As long as there is a threat of a domestic industry's forming, the low prices must continue, thereby providing most or all of the benefits of competition. If, however, that phrase of the act is interpreted to apply merely to low prices by foreign firms that occur only when a new domestic firm appears and begins producing, the phrase indeed prohibits predatory pricing rather than limit pricing.

Despite these deviations from what today would be considered a pure antipredatory pricing act, the Antidumping Act of 1916 was nonetheless a reasonably close approximation to such an act. It still applied only to the importer, however, and not to the foreign exporter. As a result of that limitation and the difficulty of proving the intent described above, the act was seldom used.

Another factor might have contributed to the paucity of cases under Section 73 of the Wilson Tariff Act and under the Antidumping Act of 1916--namely, that the acts were criminal statutes, violations of which were tried in courts with all of the protections that courts provide to defendants. As a result, the laws were strictly construed, and convictions were difficult.[28]

The Antidumping Act of 1916 remains in effect today. It is rarely used because it is easier to get relief from dumped imports under more recent laws.

26. This section of the study draws on discussions in Viner, *Dumping*, pp. 242-245, and House Committee on Ways and Means, *Overview and Compilation of U.S. Trade Statutes*, WMCP:103-1 (1993), p. 63.

27. 15 U.S.C. 72, 39 Stat. 798.

28. See Viner, *Dumping*. Viner also argues that another factor was that no agency other than the Justice Department, which has no special expertise or ability in international trade, was charged with investigating cases. Firms, which had few resources, had to investigate on their own and file civil suits.

The Antidumping Act of 1921

Between 1920 and 1922, 10 countries passed antidumping laws, including the United States and Great Britain, the latter of which had historically been a strong advocate and practitioner of free trade. A number of reasons accounted for this spate of antidumping laws (or at least for the U.S. law), most of them involving national security concerns and protectionist pressures resulting from the just-ended World War I.[29]

One reason was an erroneous fear that Germany had amassed huge stockpiles of goods during the war to dump on the world market in an attempt to win on the economic battlefield through predatory pricing what it had lost on the military battlefield. Another was fear that the cessation of trade during the war had caused the growth of surplus stockpiles of goods in Europe that would be dumped on the world market, and that U.S. industries that were important for national security might be damaged. Still another was increased political pressure from uncompetitive firms. The war had disrupted international trade, which had resulted in the growth of domestic industries in each country that enabled it to supply the products that previously had been imported but no longer could be. With the end of the war, the goods could once again be imported and therefore were a threat to the new domestic industries. These factors played themselves out amidst a wave of isolationism and protectionism that enveloped the United States after the war.

The U.S. law--the Antidumping Act of 1921--was part of the Emergency Tariff Act of 1921. Its basic substance is contained in the following excerpts:

> [W]henever the Secretary of the Treasury finds that an industry in the United States is being or is likely to be injured, or is prevented from being established, by reason of the importation into the United States of foreign merchandise, and that merchandise of such class or kind is being sold or is likely to be sold in the United States or elsewhere at less than its fair value, he shall make such finding public.[30]

> [I]f the purchase price or the exporter's sales price is less than the foreign market value (or, in the absence of such value, than the cost of production) there shall be levied, collected, and paid a special dumping duty in an amount equal to such difference.[31]

The 1921 law differs substantially from previous laws. First, it is not a criminal law with criminal punishments. Determinations of dumping are made administratively by the Department of the Treasury rather than judicially. The change allowed for greater latitude in the procedures used for determining dumping, and so it was likely to (and did) lead to a greater probability of findings of dumping.

A second difference is that no longer was there a need to show intent to destroy, injure, or prevent the establishment of an industry. The mere fact of injury of the industry--or even the likelihood of injury--was enough. Furthermore, actual sales below the foreign market value need not cause the injury or threat of injury of the industry. Mere likelihood of such sales is enough.

A third difference is that the act specified a different kind of relief. Previous laws specified fines, imprisonment, and civil liability, which primarily punish the dumper and only indirectly through deterrence protect competing domestic firms. The new law specified imposing antidumping duties, which primarily protect competing domestic producers and only secondarily (if at all) punish the dumper. Duties punish a dumping firm only if that the firm wishes to continue to dump in the U.S. market. If the firm continues selling in the U.S. market but without dumping, it will pay no duty. If changing economic conditions cause the firm to quit exporting to the United States, it will pay no duty. In either case, the initial dumping that led to the dumping investigation goes unpunished.

A fourth difference is the use of "constructed value." Constructed value is the cost of production that the export price is compared with when few or no foreign prices exist. Its use is consistent with a desire to protect domestic firms from import competition, but it is not consistent with a rationale of preventing, punishing, or offsetting predatory pricing. The reason few or

29. This discussion draws heavily on Wares, *The Theory of Dumping and American Commercial Policy*, pp. 15-20.

30. 42 Stat. 11, Sec. 201(a).

31. 42 Stat. 11, Sec. 202(a).

no foreign prices would be available for comparison is that there are few or no sales in the foreign country. If too few foreign sales exist to make a comparison of prices possible, a firm would be highly unlikely to have such a large market share as to make monopoly, and therefore predatory, pricing possible. Further, a lack of foreign sales also means that low prices in the United States are not merely local price cutting. They are price cutting on all or almost all of the firm's products, which makes predatory pricing unlikely to succeed (see Appendix A).

The History of Countervailing-Duty Law Through World War II

Subsidies existed much further back in history than did dumping. Economist Jacob Viner reports that they were common in the mercantilist era of the 17th and 18th centuries.[32] The earliest attempts to control them (the first known example of which was in 1862) involved placing clauses in trade treaties pledging the countries not to grant various kinds of subsidies.[33] The first countervailing-duty law was a provision in the U.S. Tariff Act of 1890 that applied to certain grades of sugar.[34] The first general CVD law for any and all subsidized imports was enacted by Belgium in 1892.[35]

The first general CVD law in the United States was contained in the U.S. Tariff Act of 1897 (and repeated in the Tariff Acts of 1909 and 1913).[36] It provided that any dutiable import receiving a direct or indirect export subsidy by the exporting country should have a CVD imposed on it equal to the amount of the subsidy. That law was replaced by Section 303 of the Fordney-McCumber Tariff Act of 1922, which broadened the coverage to include imports that benefited from production subsidies as well as those that benefited from export subsidies.[37] The law eventually became Section 303 of the Tariff Act of 1930, but it was not significantly changed until 1974, when it was expanded to cover nondutiable as well as dutiable imports.[38]

Two facets of the CVD law bear note at this time for later reference. The first is the restriction of coverage to dutiable imports. The second is the lack of an injury test. CVDs are imposed on subsidized imports regardless of whether those imports harm U.S. firms.

After the initial general U.S. CVD law in 1897, other countries followed suit: India in 1899, Switzerland in 1902, Serbia in 1904, Spain in 1906, France and Japan in 1910, Portugal in 1921, British South Africa in 1914, and New Zealand in 1921.[39] The Indian law was modeled on the U.S. law. Thus, the United States was a pioneer in the use of CVD law. Further, the CVD laws in most of these other countries made imposing CVDs subject to the discretion of the government, whereas the U.S. law made imposition mandatory. Partly as a result of that difference, the United States has made much greater use of CVDs than have other countries.[40]

The best domestic analog to subsidized products in international trade is the subsidies granted to firms by state and local governments (often in the form of tax breaks) in exchange for the firms' locating in the state or locality. The products the firm then produces in that location and "exports" to other states are subsidized in the same fashion as the subsidized foreign exports on which the United States imposes CVDs. The United States has no law against state- and local-government subsidies, and states are not allowed to countervail the subsidies of other states. In the case of dumping, the policy for imports was originally similar to that for the products of domestic firms and then diverged. From its

32. Viner, *Dumping*, p. 163.

33. Ibid., pp. 166-168.

34. 26 Stat. 567, Schedule E.237.

35. Viner, *Dumping*, p. 169.

36. 30 Stat. 151, Sec. 5; Viner, *Dumping*, p. 169.

37. 19 U.S.C. 127, 42 Stat. 935.

38. The material in this paragraph is taken from Terence P. Stewart, ed., *The GATT Uruguay Round: A Negotiating History (1986-1992)*, vol. 1 (Boston: Kluwer Law and Taxation Publishers, 1993), pp. 812-813; House Committee on Ways and Means, *Overview and Compilation of U.S. Trade Statutes*, pp. 53-54; and Viner, *Dumping*, pp. 169, 187-188, and 268.

39. This paragraph largely follows the discussions in Viner, *Dumping*, pp. 170-172, and Stewart, *The GATT Uruguay Round*, vol.1, pp. 812-813.

40. Another reason that will be discussed in the next section is that most countries disagree with the U.S. contention that subsidies are unfair and should be restricted by international law.

inception, however, U.S. policy on subsidies has been to countervail foreign subsidies but to neither prohibit nor countervail their domestic analogs.

Antidumping and Countervailing-Duty Law Since World War II

The evolution of the antidumping and countervailing-duty laws in the direction of greater protection for domestic industry has continued up to the present day. Since World War II, however, the General Agreement on Tariffs and Trade has played a central role in that evolution. The issue of AD/CVD laws has arisen repeatedly in GATT rounds as a center of controversy. The United States has fairly consistently taken positions in favor of limiting subsidies and allowing for expanded coverage and more aggressive enforcement of AD/CVD laws. In that stand, it has frequently faced substantial opposition from other countries that have viewed U.S. AD/CVD law, or at least certain aspects of it, as unfair protectionism and have sought restrictions on it.

The Beginnings of the GATT

The GATT resulted from a round of negotiations held in Geneva in 1947 to create an International Trade Organization.[41] A major goal of the GATT was to reduce and eliminate barriers to trade, and two of its fundamental principles and policies were and are the most-favored-nation (MFN) principle and tariff bindings. According to the MFN principle, whatever forms of protection a member country maintains should be imposed on a nondiscriminatory basis to imports from all other member countries. Tariff bindings prohibit a country from later raising tariffs that it has agreed to reduce.

U.S. AD/CVD law was seemingly at odds with this goal and these two principles. By insisting that foreign firms selling in the U.S. market not discriminate in pricing or receive subsidies from their governments without demanding the same of U.S. firms selling in the U.S. market, and by imposing added duties on imports from firms engaging in these practices, the United States was in fact imposing trade barriers. Antidumping and countervailing duties varied from country to country, thereby violating the MFN principle. Moreover, by changing from year to year in response to foreign behavior, they would violate tariff bindings.

The original GATT agreement, however, contained an exception to allow for antidumping and countervailing-duty laws subject to certain restrictions. The exception--Article VI--was derived from a U.S. proposal based on the Antidumping Act of 1921. In addition, Article XVI placed restrictions on subsidies.

On its face, Article VI is clearly at odds with the GATT goal and principles discussed above. Yet some analysts believe that at least part of it may be necessary in order to maintain political support for an open international trading system.[42] In particular, it is widely viewed as unfair for unsubsidized domestic firms to have to compete with subsidized foreign firms. If a country such as the United States that generally does not like to subsidize its own firms is not allowed to offset foreign subsidies with countervailing duties, political support for the GATT in that country might deteriorate. Hence, allowance for countervailing duties might be a necessary concession in order to maintain the greater good of the overall GATT. One might make a similar argument for allowing antidumping duties, but the argument is much less compelling: having to compete with products sold at prices below cost or below prices at which they are sold elsewhere is not so widely viewed as unfair as is having to compete with subsidized products.

The negotiators did maintain some deference to GATT principles and economic efficiency by stipulating in Article VI that antidumping and countervailing

41. This section is based on factual material taken from House Committee on Ways and Means, *Overview and Compilation of U.S. Trade Statutes*, p. 63; Stewart, *The GATT Uruguay Round*, vol. 1, pp. 809 and 813-815, and vol. 2, pp. 1405-1410, 1413, and 1417; and J. Michael Finger, "The Origins and Evolution of Antidumping Regulation," in Finger, ed., *Antidumping: How It Works and Who Gets Hurt* (Ann Arbor, Mich.: University of Michigan Press, 1993), pp. 13-34.

42. See, for example, Jagdish Bhagwati, *Protectionism* (Cambridge, Mass.: MIT Press, 1988), pp. 34-35.

measures be duties rather than quotas. (Duties are generally less detrimental to economic efficiency and productivity than equally restrictive quotas.) They also limited the duties to the dumping or subsidy margin--no higher duties to punish the offender--and prohibited a country from levying both antidumping and countervailing duties on the same product for the same offense.

Article VI allows CVDs on subsidized imports only if they "cause or threaten material injury to an established domestic industry, . . . or retard materially the establishment of a domestic industry." U.S. CVD law at the time of the agreement still did not require a showing of injury before CVDs were imposed. It provided for CVDs on any dutiable import that was subsidized. A grandfather provision allowed the United States to continue imposing CVDs without an injury requirement. When and if the United States ever decided to expand the coverage to nondutiable imports, however, it would have to impose a material injury standard for those imports, though it would still not have to impose one for the dutiable imports.

In 1954, responsibility for determining injury in antidumping cases was shifted to the Tariff Commission (the name of which was later changed to the U.S. International Trade Commission), whereas investigating the existence and margin of dumping was left with the Treasury Department.

After the initial round, dumping and subsidies receded as an issue for several decades. The following four GATT rounds were primarily devoted to tariff reduction. In response to a request in October of 1956, the GATT Secretariat made a comparative study of the antidumping laws of the member states. Although 20 member states had AD/CVD legislation of some sort, the study found that only eight of them actually used the legislation.[43] A tally in 1958 showed a total of only 37 antidumping decrees in effect in all GATT member countries except Canada and New Zealand, for which comparable figures were not available.[44]

43. The eight countries were Australia, Belgium, Canada, New Zealand, South Africa, Federation of Rhodesia and Nyasaland, Sweden, and the United States.

44. Finger, "The Origins and Evolution of Antidumping Regulation," pp. 13-34. For comparison, Finger notes that, in December 1989, 530 antidumping decrees were in effect in just Australia, Canada, the United States, and the European Community.

The Kennedy Round and the Antidumping Code

One reason many countries did not enforce AD/CVD laws was that high tariffs adequately protected their firms. As succeeding GATT rounds reduced tariffs, however, more countries began enforcing such laws, which then led to complaints and disputes. As a result, dumping and the laws against it were again an issue in the Kennedy Round of the GATT, which was held from 1964 to 1967.[45]

The antidumping debate in the Kennedy Round brought forth arguments and positions that would crop up again in the Tokyo Round and the recently completed Uruguay Round. U.S. exporters were increasingly facing accusations of dumping in other countries, and they found the judgments of many countries on U.S. dumping to be incomprehensible because the relevant facts and reasoning were not made public. Hence, the major U.S. concern was to improve the "transparency" of the administration of other countries' antidumping laws. In turn, many other countries viewed various aspects of U.S. antidumping law as unfair. The United States was a major (though not the only) target of criticism because of the importance of the U.S. market in the world economy, the advanced state of development and specificity of U.S. antidumping law, and the transparency of U.S. antidumping proceedings, which made the workings of the system visible for all to see and criticize.

The Negotiations Produce an Antidumping Code. The result of the antidumping negotiations in the Kennedy Round was the "Agreement on the Implementation of Article VI," often referred to as the Antidumping Code. The Antidumping Code was a separate agreement from the GATT and only some of the signatories to the GATT became signatories to the code.

The Antidumping Code differed from U.S. law in several ways, not the least of which was its definition of "material injury." According to the code, to find "material injury" in a dumping case, the authorities must determine that the dumped imports are "demonstrably the

45. This section is based on factual material taken from Stewart, *The GATT Uruguay Round*, pp. 1418-1433, and from House Committee on Ways and Means, *Overview and Compilation of U.S. Trade Statutes*, p. 63.

principal cause" of injury to the domestic industry. U.S. policy had a much lower standard.

The Congress Rebels Against the Code's Restrictions on Antidumping Policy. The executive branch took the position that nothing in the new code was counter to existing law and that therefore the code could be implemented without Congressional approval.[46] Many Members of Congress disagreed, and many disliked the new injury standard. In fact, the Congress requested a Tariff Commission study of the issue, which found several areas of conflict with U.S. law. That finding led to the passage of a 1968 law stipulating that the code would apply in the United States only to the extent that it did not conflict with existing U.S. law and policy regarding injury.[47] That issue was a sore point with other countries that would come back in the next GATT round.

The Trade Act of 1974

The Trade Act of 1974 significantly expanded the coverage of U.S. antidumping law.[48] Before the act, dumping meant selling exports at a price below the home-market price. If the volume of home-market sales was too small, the export price was compared with the price of sales in other export markets. Only if the volume of sales was too small in the home market and all other export markets would the export price be compared with the cost of production.

The Trade Act of 1974 required the Treasury, when calculating the average home-market (or third-country export market) price, to disregard any sales that were made in that market in substantial quantities for an extended period of time at prices below the average total cost of production.[49] As a result, the so-called average home-market price would always be above cost even during recessions. The effect of the change therefore was to make selling exports below cost another form of dumping.

46. Much of this paragraph follows the discussion in Stewart, *The GATT Uruguay Round*, vol. 2, pp. 1431-1433.

47. 82 Stat. 1347, Sec. 201.

48. 19 U.S.C. 2101, 88 Stat. 1978.

49. 88 Stat. 2046, Sec. 321(d). For this provision, average total cost does not include an allowance for profit.

As mentioned above, many legitimate reasons exist for selling below cost, and such sales can benefit the selling firm, the consumer, and the efficiency of the economy. Although domestic firms are allowed to sell below cost whenever they like (except in cases of predatory pricing), this change in the law makes foreign firms who do so in the U.S. market subject to antidumping duties. Thus, it puts foreign producers at a disadvantage relative to U.S. domestic producers.

The change also marks a further departure from the original function of antidumping law as a protection from predatory pricing. In most cases, successful predatory pricing requires the foreign firm to restrict its losses during the price-war phase by lowering its prices only in the U.S. market. If the firm must also incur losses in its own market, it will lose much more money during the price war, making it much less likely to drive other firms out of the U.S. market without going bankrupt itself or being unable to recoup its losses through higher prices later. That change in U.S. antidumping law was aimed at precisely the situations--those in which the firm is losing money in its home market--in which predatory pricing is least likely to be successful.

The consistency of the change with the requirements of the GATT was questionable. According to GATT Article VI, a product is dumped if "the price of the product exported from one country to another

(a) is less than the comparable price, in the ordinary course of trade, for the like product when destined for consumption in the exporting country, or,

(b) in the absence of such domestic price, is less than either

    (i) the highest comparable price for the like product for export to any third country in the ordinary course of trade, or

    (ii) the cost of production of the product in the country of origin plus a reasonable addition for selling cost and profit."

Thus, selling below cost could be considered to be dumping only when there is no domestic price for comparison (part (b)(ii) above). The change in U.S. law was defended by arguing that sales below cost in substantial quantities for substantial periods of time were not "in the ordinary course of trade" as stipulated in part (a) of the definition.[50] That argument is at odds with a long list of legitimate reasons for selling below cost (see Chapter 2). Canada had used the argument before in 1971, but it was not universally accepted. The issue again became a subject of controversy in the Tokyo Round.[51]

The Trade Act also expanded the CVD law to cover nondutiable imports as well as the dutiable imports already covered.[52] Since the GATT grandfather rights did not cover changes in the law, an injury test was included for this expansion to cover imports from GATT members, but not imports from non-GATT members and not the dutiable imports already covered by the law. The responsibility for determining injury was given to the International Trade Commission, which already had that responsibility in antidumping cases.

The Trade Act of 1974 imposed time limits within which the Treasury had to reach final determinations.[53] Although understandable and neutral on their face, one of the effects of those limits and their later tightening was to force the Treasury (and later the Department of Commerce) to put tight time limits on investigated firms when they responded to questionnaires soliciting the data required for determining the cost discussed above. Those limits place great difficulties on the firms being investigated (see the next chapter for a more detailed discussion).

The Tokyo Round

The Tokyo Round of GATT negotiations was held from 1973 to 1979.[54] Antidumping law was again an issue, and increasing use of subsidies led to subsidies and CVD law being issues also. On the issues of subsidies and CVD law, the lineup was largely one of the United States against most of the rest of the world.

The United States came in for criticism on several issues relating to its antidumping law. The European Community was unhappy with a provision of U.S. law requiring that at least 10 percent and 8 percent, respectively, be added for administrative overhead and profit in constructed-value calculations. Many countries argued that the U.S. injury standard was too lenient and that the United States began investigations without enough evidence of injury. The latter was viewed as a problem because investigations are a burden on foreign firms. The issue of whether and in what circumstances countries should be allowed to disregard sales below cost because they are not in the ordinary course of trade was a center of controversy, although the United States was not alone on this issue. Those questions would resurface in the Uruguay Round.

Regarding subsidies, the United States wanted to rein in their use by other countries. In particular, it wanted to rein in not only export subsidies but also domestic subsidies that had effects on international trade. Most other countries saw little if anything wrong with domestic subsidies, and many viewed them as important internal policy tools with which there should be no international interference. Those countries wanted to restrain U.S. CVD law. One complaint in particular was the U.S. refusal under its grandfather rights to put a material injury test in its CVD law in line with the requirements of Article VI.

The negotiations on these issues resulted in some modifications to the Antidumping Code and the writing of a new Subsidies Code that (like the Antidumping Code) was not signed by all signatories to the GATT. Among the changes to the Antidumping Code was no longer to require that dumping be the principal cause of

50. Gary N. Horlick, "The United States Antidumping System," in John H. Jackson and Edwin A. Vermulst, eds., *Antidumping Law and Practice: A Comparative Study* (Ann Arbor, Mich.: University of Michigan Press, 1989), p. 134.

51. Stewart, *The GATT Uruguay Round*, vol. 2, pp. 1440-1444.

52. 88 Stat. 2049, Sec. 331(a). This paragraph follows the discussion in House Committee on Ways and Means, *Overview and Compilation of U.S. Trade Statutes*, pp. 54-55.

53. 88 Stat. 2043, Sec. 321(a), and 88 Stat. 2049, Sec. 331(a).

54. This section is based on Stewart, *The GATT Uruguay Round*, vol.1, pp. 815-819, and vol. 2, pp. 1435-1461; and House Committee on Ways and Means, *Overview and Compilation of U.S. Trade Statutes*, pp. 54, 55, and 63.

injury to meet the material injury requirement for imposing duties. Thus, U.S. law was no longer violating the Antidumping Code on that issue.

In large part, the Subsidies Code was a compromise between the European Community, which agreed to limits on domestic subsidies that affect international trade, and the United States, which agreed to an injury test for CVD cases relating to dutiable imports. The code prohibits export subsidies on nonprimary products and primary mineral products (basically all nonagricultural products). It also prohibits export subsidies on agricultural products when they displace the exports of other countries or undercut prices in a market. It contains a new, more detailed description of what constitutes an export subsidy, and it permits countermeasures against domestic subsidies that cause certain injurious trade effects.

The code set up two procedures for handling problem subsidies. One involves CVDs; the other involves government-to-government consultation and negotiation with a provision for appeal to the Code Committee, which can authorize countermeasures. Historically, the United States has generally used the first of these procedures, finding the second ineffective.

Finally, the Subsidies Code attempted to ensure greater transparency in the procedures and practices of both governments granting subsidies and governments administering CVD laws.

Trade Legislation from 1979 to the Present

From 1979 to the present, three major pieces of trade legislation have been enacted in the United States. All three had provisions that continued the Congress' long push for stronger AD/CVD protection for U.S. firms.[55]

55. This section is based on Robert E. Baldwin and Michael O. Moore, "Political Aspects of the Administration of the Trade Remedy Laws," in Richard Boltuck and Robert E. Litan, eds., *Down in the Dumps: Administration of the Unfair Trade Laws* (Washington, D.C.: Brookings Institution, 1991), pp. 256-260; Tracy Murray, "The Administration of the Antidumping Duty Law by the Department of Commerce," in Boltuck and Litan, eds., *Down in the Dumps*; House Committee on Ways and Means, *Overview and Compilation of U.S. Trade Statutes*, pp. 55, 63, and 64; and Judith Hippler Bello and Alan F. Holmer, *The Antidumping and Countervailing Duty Laws: Key Legal and Policy Issues* (Washington, D.C.: American Bar Association, 1987), pp. 104-105.

The Trade Agreements Act of 1979. The main purpose of the Trade Agreements Act of 1979 was to carry out the agreements on nontariff measures negotiated in the Tokyo Round, among them the revised Antidumping Code and the Subsidies Code.[56] The Antidumping Act of 1921 was repealed, and new antidumping and countervailing-duty laws conforming with the revised codes were enacted as a new Title VII to the Tariff Act of 1930.[57] To make U.S. CVD law conform with the Subsidies Code, the 1979 act included an injury test for imports from code signatories and other countries assuming obligations substantially equivalent to those of the code.[58] Other imports remained subject to the imposition of CVDs without an injury test.[59]

To beef up AD/CVD protection for U.S. industry, the act imposed still shorter time limits for the investigation and decision of AD/CVD cases.[60] It also provided for annual reviews to ensure that antidumping and countervailing duties were maintained at the proper levels.[61]

Of particular note, the act permitted moving the investigation and determination of margins in AD/CVD cases from the Department of the Treasury, which tends to favor free trade, to the Department of Commerce (DOC), which is more inclined to protect domestic firms from imports.[62] Such a move was made soon thereafter.

The move reflected a Congressional desire for more zealous enforcement of the AD/CVD laws and for less concern about their being used in a protectionist manner. Its significance goes beyond the difference in insti-

56. 19 U.S.C. 2501, 93 Stat. 144.

57. The repeal of the Antidumping Act of 1921 is in 93 Stat. 193, Sec. 106. The new AD/CVD laws are in 19 U.S.C. 1671; 93 Stat. 151, Sec. 101.

58. Section 701 of the Tariff Act of 1930 as amended by 19 U.S.C. 1671, 93 Stat. 1510.

59. 19 U.S.C. 1303; 93 Stat. 190, Sec. 103.

60. Sections 703, 705, 733, and 735 of the Tariff Act of 1930 as amended by 19 U.S.C. 1671b, 1671d, 1673b, 1673d; 93 Stat 152, 159, 163, 169.

61. Section 751 of the Tariff Act of 1930 as amended by 19 U.S.C. 1675, 93 Stat. 175.

62. The act did this by referring to "the administering authority" rather than "the Department of the Treasury" on these functions throughout Section 101.

tutional sympathies. One of DOC's functions is to serve as an advocate for U.S. firms.[63] Thus, the move placed responsibility for deciding AD/CVD cases in the hands of an advocate of U.S. parties to the cases.

Also of note, determining the cost of production requires the Treasury Department or DOC to obtain relevant data from the firms being investigated. To ensure that such firms were forthcoming, the act allowed the use of "best information available" whenever a foreign firm did not provide needed data.[64] In practice, the "best information available" is usually information supplied by the U.S. industry seeking protection, and therefore can be expected to be biased in the direction of high costs and consequent findings of dumping.

The Trade and Tariff Act of 1984. The Trade and Tariff Act of 1984 required that the International Trade Commission cumulate the imports of all countries subject to an AD/CVD investigation when making its injury determinations if the imports compete with each other and with like products of the domestic industry in the United States.[65] Clearly, firms that compete with each other cannot be a monopoly. Therefore, if one is trying to prevent predatory pricing, imports from different countries should be cumulated in determining injury only if evidence exists that the firms in the different countries are colluding. This provision mandates just the opposite: that they should be cumulated when they compete.

The act also allowed DOC to find an import to be subsidized and subject to CVDs if the inputs used to produce the import are subsidized and the subsidies give a competitive benefit to the producer of the import by lowering the price of the inputs below what others would have to pay.[66] DOC was already doing that, so the provision merely codified DOC practice.

The act also created the Trade Remedy Assistance Office in the International Trade Commission to give information about procedures for filing petitions, and it required all agencies administering U.S. trade laws to give technical assistance to small U.S. firms filing petitions and applications for relief under the laws.[67] Small foreign firms being investigated for dumping or subsidies get no such help. Moreover, as will be discussed in Chapter 4, the burden of AD/CVD investigations on such firms can be quite large. That legal requirement is an example of the administrative agencies' being asked to play an advocacy role in proceedings for which they are supposed to be an impartial judge.

The act also permitted DOC in antidumping investigations to compare the average price in the United States with the average price in the exporter's home market, rather than comparing individual prices in the United States with the average price in the exporter's home market.[68] Contrary to most changes the Congress has enacted in recent years, this change would have made findings of dumping less likely if DOC had made use of it (for further explanation of this issue, see Chapter 4).

The Omnibus Trade and Competitiveness Act of 1988. In the past, AD/CVD orders typically specified that antidumping or countervailing duties were to be levied on particular products from particular countries or on particular products from particular firms in particular countries. Firms sometimes tried to circumvent the duties in various ways. One way was to export only the parts and then conduct final assembly in the United States, changing the country from which the parts were exported to the United States by moving the location of final assembly and slightly altering the product from that specified in the AD/CVD order. The Omnibus Trade and Competitiveness Act of 1988 contained provisions to extend AD/CVD orders to constituent parts, slightly altered products, and products assembled in third countries.[69]

The act also contained a provision for the U.S. Trade Representative to request antidumping action by other countries when products that are dumped in those

63. Baldwin and Moore, in "Political Aspects of the Administration of the Trade Remedy Laws," state that "Some members of the House and Senate want DOC administrators to act more as an 'advocate' of U.S. domestic producer interests. For example, in nomination hearings for Michael Farren, Senator John C. Danforth (Republican of Missouri) stated, 'we count on the Commerce Department in particular to be the advocate for U.S. commercial interests.' "

64. Section 776(b) of the Tariff Act of 1930 as amended by 19 U.S.C. 1677e, 93 Stat. 186.

65. 19 U.S.C. 1677; 98 Stat. 3034, Sec. 612(a)(2)(A).

66. 19 U.S.C. 1677-11; 98 Stat. 3035, Sec. 613.

67. 19 U.S.C. 1339; 98 Stat. 7989, Sec. 221.

68. 19 U.S.C. 1677f-1, 1677b; 98 Stat. 3039, Sec. 620.

69. 19 U.S.C. 1677; 102 Stat. 1192, Sec. 1321.

countries materially injure U.S. firms that export to them.[70] If the country refuses to take action, the U.S. Trade Representative is to consult with the U.S. firms about possibilities for action under other U.S. laws. Whether the provision does much to help U.S. firms competing with dumped goods is not clear, but its mere existence illustrates further how far apart in purpose antidumping law and predatory pricing law now are. The purpose of predatory pricing law is to protect the public from the inefficiencies and high prices that result from monopolization of an industry; it is not concerned with protecting the competing firms, except insofar as it is necessary to do so to protect the public from monopoly. This antidumping provision is concerned only with protecting competing U.S. firms; the U.S. public and consumers are not involved since the markets in question are in other countries.

As Chapter 2 discussed, subsidies that are generally available to all industries do not affect trade. As a result, the 1988 act provides that CVDs can be imposed on subsidized products exported to the United States only if the subsidies involved are specific to certain industries and are not generally available to all industries in the exporting country.[71]

The act also contained a provision to the effect that subsidies that by law are available to all industries but in practice end up going only to one or a few industries should be treated as specific subsidies rather than generally available, and therefore should be subject to CVDs. The Department of Commerce was already doing that on its own, but the law required it to do so. The policy gets around a possible evasion of the CVD law: a country might make its subsidies by law and other appearances available to all industries so that U.S. CVDs would not be applied; it could then make sure by secret bureaucratic machinations that the subsidies go only to a particular industry.

Finally, the 1988 act eliminated drawbacks on antidumping and countervailing duties for firms that import inputs that are under AD/CVD orders and then export the products they make containing them.[72] Before that change, AD/CVD laws protected two groups of U.S. firms: those that produce products for U.S. consumers, and those that produce products for sale to other U.S. firms for use as inputs in the production of goods sold to U.S. consumers. The provision discussed above about the U.S. Trade Representative was intended to provide a modicum of protection to firms that produce products for sale to foreign consumers and firms. The provision at issue here extended protection to the last group of U.S. firms: those that produce goods for sale to other U.S. firms for use as inputs in products sold abroad.

In the tiny percentage of relevant dumping and subsidy cases that actually involve predatory pricing, that provision would protect U.S. export industries from having the prices of their inputs go up as a result of foreign monopolization of the industries producing those inputs. In the vast majority of cases, however, the provision merely places U.S. exporters at a disadvantage in the international market because their imported inputs are more expensive as a result of antidumping and countervailing duties.

70. 19 U.S.C. 1677k; 102 Stat. 1188, Sec. 1317.

71. 19 U.S.C. 1677; 102 Stat. 1184, Sec. 1312.

72. 19 U.S.C. 1677h; 102 Stat. 1209, Sec. 1334.

Chapter Four

Controversies Over U.S. AD/CVD Procedures

As the U.S. antidumping and countervailing-duty laws have evolved over time, so have the procedures for implementing them. The steady decline in U.S. tariffs since World War II in accord with the various negotiating rounds of the General Agreement on Tariffs and Trade has resulted in steadily increasing competition for domestic industries from imports. The Section 201 escape clause provides relief for domestic industries suffering from such increased competition (see Chapter 1). Industries usually prefer, however, to obtain protection under the AD/CVD laws rather than the escape clause whenever they can (see Chapter 5).

As the laws became more inclusive, industries were more frequently able to obtain protection under the AD/CVD laws. Gradually, industry began to view and use the AD/CVD laws as an alternative to the escape clause--that is, as a general source of protection when foreign competition became excessive.

The evolution of the AD/CVD laws and procedures reflects this view and use: the laws and procedures have fairly consistently changed in the direction of eliminating their defects as a general source of protection from all imports, whether fair or unfair (that is, dumped or subsidized). Many of the procedures that have evolved have an ad hoc quality and appear biased if one views the purpose of the AD/CVD laws as protection against predatory pricing or other unfair practices. Consequently, they have drawn considerable criticism from economists and others familiar with the economics of trade. The procedures appear more reasonable if one believes that the AD/CVD laws should provide a general source of protection from any foreign competition that becomes or threatens to become excessive--and if one believes that the fairness or unfairness of imports is less important than the injury they cause to competing U.S. industries.

This chapter discusses a number of the procedures that have been the subject of dispute or criticism. In some cases, an understanding of the dispute requires an understanding of the overall process that the U.S. administrative authorities use to investigate and assess duties in AD/CVD cases. A brief overview of the process appears in Box 2. A more detailed overview is given in Appendix B.

Using Statutory Minima for Profit and Administrative Overhead

Under U.S. antidumping law, the price of an import must be compared with the price charged for the same product when sold elsewhere, or with its cost of production, which can be constructed from available data. When the import price is compared with the constructed value because of inadequate home-market or third-country sales, the constructed value must, by law, include an amount for general, selling, and administrative costs (GS&A) of at least 10 percent and a profit margin of at least 8 percent. In line with this requirement, the Department of Commerce uses either the actual values of GS&A and profits determined from the investigated firm's books or the respective statutory minimum percentages, whichever is greater.

Box 2.
A Brief Overview of the U.S. AD/CVD Administrative Process

Two agencies are involved in administering the antidumping and countervailing-duty laws of the United States. The Department of Commerce (DOC) determines whether or not the imports in question are being dumped (subsidized), and the International Trade Commission (ITC) determines whether or not they are causing material injury to the competing U.S. industry. Each case goes through four determinations: a preliminary determination by the ITC of injury, a preliminary determination by DOC of dumping or subsidy, a final determination by DOC of dumping or subsidy, and a final determination by the ITC of injury.

After being initiated by an industry petition or by DOC on its own, each case undergoes a preliminary determination by the ITC of injury. If the ITC finds no reasonable indication of material injury, the investigation is terminated. Otherwise, the case continues to the next stage, which is the preliminary determination by DOC of dumping (or subsidy). That determination does not affect the final outcome of the case. Its purpose is to determine whether duties must be deposited on the goods in question that are imported while the rest of the investigation continues, and if so, what the duty deposit rate should be.

The case then proceeds to the final DOC dumping (or subsidy) determination. If the determination is negative--that is, if DOC determines that the imports are not being dumped (or subsidized)--the investigation is terminated and any duties that may have been deposited are refunded. If the determination is positive, the case proceeds to the final determination by the ITC of injury. If that determination is negative--that is, if the ITC determines that the dumped (or subsidized) imports are not causing material injury to the competing U.S. industry--then any duties deposited are refunded and no antidumping (or countervailing) duties are imposed on future imports. If the determination is positive, then antidumping (or countervailing) duties are assessed on future imports.

The system is retrospective in nature. When goods under AD/CVD orders are imported, the importer is required to make duty deposits equal to the dumping or subsidy margin determined on previous imports of the good in question. The actual duty is assessed later--within a year and based on the dumping or subsidy margin for the current imports if there has been a review to determine that margin. If the duty is larger than the deposit, the importer must make up the difference with interest. If it is smaller than the deposit, the excess is refunded with interest.

Sometimes investigations are suspended or withdrawn before completion. The suspension or withdrawal often occurs in conjunction with an agreement by the investigated firm or country to cease the behavior in question or with an import quota agreement.

Those statutory minima date from the beginning of the current antidumping law in 1921. Some authors report that they originate from the practice of the Customs Service in customs valuations when it had insufficient data for accurately determining the numbers and when it feared that firms might juggle their books to reduce the values that the service determined.[1] One may debate whether this rationale was valid in 1921 before the Treasury Department (now the Department of Commerce) had the investigative staff and resources it currently has for AD/CVD cases, but the provision currently draws considerable criticism.

If one views the AD/CVD laws as protection against predatory pricing, the minima are clearly inappropriate. GS&A has nothing to do with predatory pricing, and if a firm makes any profit at all it is not engaging in predatory pricing. Assuming a would-be predator firm and its prey both have the same average costs, then the prey's profits will be positive whenever the predator's profits are positive (even if the latter are small). Obviously, the prey will never go broke and be driven from the market with positive profits. Indeed, the prey will have negative profits and be driven out of business only if it has higher average costs than the predator has. That case, however, represents the nor-

1. Michael Coursey, "Comment," in Richard Boltuck and Robert E. Litan, eds., *Down in the Dumps: Administration of the Unfair Trade Laws*, (Washington, D.C.: Brookings Institution, 1991), pp. 243-244; and Terence P. Stewart, "Administration of the Antidumping Law: A Different Perspective," pp. 288-330 in the same volume.

mal desired working of a competitive market--efficient firms driving out inefficient firms--and not predatory pricing.

Even if one views the AD/CVD laws as protection against unfair--but not necessarily predatory--imports, it is not clear what is unfair about low but positive profits and GS&A. In fact, low overhead is usually regarded as an indicator of efficiency and therefore desirable. Clearly, however, the statutory minima make the laws a more effective general source of protection.

Comparing Individual Export Prices with the Average Home-Market Price

When the Department of Commerce compares U.S. import prices with the foreign exporter's home-market prices, it compares individual import prices with the average home-market price. It then sets all negative dumping margins on individual imports to zero before calculating the average dumping margin.

For example, suppose that a foreign firm sold equal amounts of a product in the United States and its home country on three different dates during the investigation period--say, June 1, September 1, and November 30 (see Table 1). Suppose also that prices in both countries were the same on each date but increased over time--from $50 on June 1 to $100 on September 1 and to $150 on November 30. (Such an increase might result from heightened demand brought on by advertising, a shift from recession to boom, changing consumer fads, or many other causes.) Suppose finally that all of the prices covered production costs.

One would think that no dumping had occurred in this example, since prices cover costs and are the same in both countries. The methodology of the Department of Commerce would, however, find dumping. It would first average the prices in the home country to find an average home-market price of $100 (after conversion from foreign currency to dollars). Then DOC would compare each U.S. price with that average $100 price to determine if the sale in question was dumped. Thus, the June 1 sale would have a dumping margin of $50, the September 1 sale would have a margin of zero, and the November 30 sale would have a margin of negative $50. DOC then would set all negative dumping margins to zero (see the far right column of Table 1) and average the dumping margins. The result is the conclusion that the average dumping margin is $16.67. Dividing by the average U.S. price of $100 gives an average percentage dumping margin of 16.67 percent.

Table 1.
Calculating Average Dumping Margins Using the Commerce Department Methodology: An Example (In dollars)

Date	Home-Market Price	U.S. Price	Absolute Dumping Margin	Is the U.S. Sale Product Dumped?	Margin Used in Calculating Average
June 1, 1993	50	50	50	Yes	50
September 1, 1993	100	100	0	No	0
November 30, 1993	150	150	-50	No	0
Average Price and Dumping Margin	100	100	n.a.	n.a.	16.67

SOURCE: Congressional Budget Office.

NOTE: n.a. = not applicable.

In some cases, the results of DOC's methodology are peculiar and create incentives that are at cross purposes with the antidumping law.[2] Suppose that a foreign firm sold 1,000 units of a product at the prevailing market price of $100 in the United States and 1,000 units in its home market at the prevailing price there, which was the home-currency equivalent of $100. Then assume that during the period of DOC's investigation the prevailing market price in the firm's home market increased to $200, while the prevailing price in the United States rose to $175.

If the firm were again to sell 1,000 units each of the product in the United States and the home market at the new prevailing prices, it would be guilty of dumping in the United States. However, the $175 sales in the United States would not be the dumped sales. The average price in the home market would be $150--that is, [(1,000 × $100) + (1,000 × $200)] / 2,000. Thus, the $100 sales in the United States would be the ones dumped, by a margin of $50, and the $175 sales would not be dumped at all. The average dumping margin over all sales (calculated by DOC's methodology) would be $25. Expressed as a percentage of the average U.S. price of $137.50, the average dumping margin would be 18.2 percent.

To avoid dumping, the firm might try two approaches. The first would be to try raising its U.S. price beyond the prevailing U.S. price of $175 to the prevailing home-market price of $200. Even if it was able to sell the full 1,000 units at the higher price, however, the previous example has already shown that DOC's methodology would still find dumping--in this case, by a margin of 16.7 percent. Further, since $200 is above the prevailing U.S. market price, the firm probably could not sell the full 1,000 units at that price. If it was only able to sell 500 units, the dumping margin calculated by the DOC would be 25 percent, which is larger than the margin would be if the firm sold at the lower prevailing U.S. price of $175.[3]

The second approach the firm could take would be to discontinue sales in the United States--that is, to take the 1,000 units that would have been sold in the United States and instead try to sell them in the home market along with the 1,000 units that would have been sold there anyway. Doing so would increase the firm's profits since the $200 price in the home market is higher than the $175 price in the United States. Further, one would think such an action would eliminate any dumping. In fact, however, it would actually be likely to increase the dumping margin that the DOC calculates.

Assuming for the moment that the firm could sell the extra 1,000 units in its home market without lowering the price below $200, the average home-market price would be $166.67--that is, [(1,000 × $100) + (2,000 × $200)] / 3,000. Hence, the $100 sales in the United States would be dumped by $66.67. Expressed as a percentage of the average U.S. price, the average dumping margin would be 66.67 percent. The firm might have to lower the home-market price in order to sell the extra 1,000 units there. If so, that would lower the calculated dumping margin but would be unlikely to eliminate it.[4]

The firm in this example would find it difficult to avoid dumping. Further, the obvious things the firm might try in order to avoid dumping (raising its U.S. price to $200 or switching U.S. sales to its home) *might* actually increase the calculated margin. The firm therefore has an incentive not to do the obvious things to avoid dumping.

The Commerce Department evidently realized the bias in the procedure because it asked the Congress to amend the law to allow it to compare the U.S. average price with the foreign average price, rather than individual U.S. prices with the foreign average price. The Congress did, in fact, so amend the law in the Trade and Tariff Act of 1984. The amended law only allowed a comparison of average prices, however. It did not

2. This example is taken in large part from N. David Palmeter, "The Antidumping Law: A Legal and Administrative Nontariff Barrier," in Boltuck and Litan, eds., *Down in the Dumps*, p. 72.

3. The calculation is as follows: the average foreign price is $150 just as before. Hence, the $100 sales in the United States are dumped by $50 and the $200 sales are not dumped. The average absolute dumping margin is therefore [(1,000 × $50) + (500 × $0)] / 1,500 = $33.33. The average U.S. price is [(1,000 × $100) + (500 × $200)] / 1,500 = $133.33. Thus, the average percentage dumping margin is (33.33/ 133.33) × 100 = 25 percent.

4. If the firm sells all 1,000 units in its home market, the home-market price would have to drop all of the way back to the original $100 in order to eliminate the margin. The reason is that the sales that already occurred in the United States were at $100 and would be considered dumped if the average price of the 3,000 total units in the home market was higher than $100. Alternatively, the firm might sell 500 of the units in the United States and 500 in its home market. As the first example above has shown, however, even if this raised the U.S. price and lowered the home-market price to the point that the two were equal, the Commerce Department's methodology would still find dumping.

require such a comparison, and the Commerce Department has not changed its procedure.

When criticized for the procedure in the Uruguay Round, the U.S. delegation replied that is was necessary to address the problem of targeting. Targeting refers to the practice of dumping products to one or a few customers at a time in order to take the customers away from domestic U.S. producers in piecemeal fashion. That practice is also referred to as "spot dumping" or "rifle-shot dumping."

If the purpose of antidumping legislation is to prevent predatory pricing (or any other pricing behavior that might be a net detriment to the U.S. economy), there is no reason to object to any targeting that a comparison of the average price with the average home-market price would not detect. A successful predatory pricing campaign could not possibly be carried out by such targeting. If the average U.S. price is not lower than the average foreign price, then the fact that dumping is occurring with one or a few customers must mean that the import price is abnormally high with other customers. The U.S. firm should be able to take away those customers from the foreign exporter at the same time that the foreign exporter takes away the other customers by dumping.

If one views the purpose of antidumping law as preventing unfair--but not necessarily predatory--imports, one might be concerned about other negative effects. If targeting occurred repeatedly in one part of the U.S. market after another, it would have frictional costs as firms continually had to expand and contract in various parts of the market. The firm doing the targeting, however, would incur those costs as well as the firm or industry whose customers are targeted, and it would have little if anything to gain from engaging in such behavior.

Furthermore, the United States has not judged such costs--or any other costs of targeting--to be sufficient to merit outlawing or otherwise objecting to U.S. firms engaging in the practice within the United States. U.S. firms target each others' customers without objection (witness, for example, the pricing behavior of U.S. airlines). It is usually characterized as "vigorous competition," which is thought to be good. Why foreign firms should be treated any differently is hard to fathom, unless the reason is to provide a more effective general source of protection for U.S. industries.

Eliminating Below-Cost Sales in the Home-Market Price Calculation

When DOC computes the average home-market price of a foreign exporter, U.S. law requires it to delete sales below cost if they are "made over an extended period of time and in substantial quantities." As Chapter 3 discussed, this procedure effectively expands the definition of dumping to include selling below cost in the U.S. market, even when U.S. firms are doing so and the "dumping" firm is doing the same in its home market. The procedure does more than that, however. It expands dumping to include some cases in which import sales in the United States are neither below cost nor below the average home-market price of the foreign exporter.

To see why, suppose that during the period of investigation, one-third of a foreign exporter's sales in its home market are at a price of $75, one-third are at $100, and one-third at $125, and that sales at all three prices are made throughout the period of investigation. Assume further that the cost of production is $100 per unit and that all sales in the United States are at a price of $100. In that case, the sales in the United States are not below the average price in the home market, and they are not below cost. Thus, ordinarily, one would think the goods are not being dumped.

Deleting sales below cost in the home market, however, would result in a finding of dumping in that case. The sales at $75 would be deleted. Half of the remaining home-market sales are at $100 and half at $125. Thus, the calculated average home-market price would be $112.50. The U.S. price of $100 is below that, so the products in the United States would be found to be dumped.

The current methodology is to delete sales below cost when they are more than 10 percent of home-market sales in the case of industrial products (50 percent

in the case of fresh agricultural products) and occur in three of the six months of the investigation period. Recessions and other legitimate reasons for selling below cost could easily transgress those limits. The problem relating to recessions could be alleviated only if sales below average variable cost were deleted rather than all sales below average total cost. Current methodology, however, as dictated by law deletes all sales below average total cost. From the perspective of the antidumping and countervailing-duty laws as protection against unfair trade, that procedure is clearly biased against foreign firms and U.S. consumers of foreign products. It does, however, improve the functioning of the laws as a general source of protection.

Ensuring Comparability of Foreign and Domestic Prices

In comparing the U.S. price with the home-market price in an antidumping investigation, the U.S. policy is to take the first arm's-length sale in each country--that is, the first sale to a firm or person not owned by the manufacturer, whether that sale is at the level of the manufacturer, the wholesaler, or the retailer--and then make whatever adjustments are required to make the sale prices comparable. Sales between the manufacturer and a wholly owned wholesaler are not considered acceptable because they are subject to manipulation for tax or other purposes. Examples of deductions made to ensure comparability are tariffs and transportation expenses deducted from the U.S. price.

Problems arise in the adjustments DOC makes to ensure that the prices compared are at the same level of sale--that is, factory level with factory level as opposed to factory level with wholesale or retail level. When a foreign manufacturer under investigation sells its product to a wholly owned subsidiary in the United States, which then acts as distributor, DOC takes the price at which the distributor sells to a third party and subtracts from it the direct and indirect selling expenses of the distributor but not its profits. To obtain the home-market price for comparison, DOC takes the first arm's-length sale and subtracts from it the direct and indirect selling expenses incurred in the home market but not the profits. That calculation is referred to as the "exporter's-sale-price" methodology.

On the surface, the methodology seems correct and fair: direct and indirect selling expenses are deducted from both the U.S. import price and the exporter's home-market price, and profits are deducted from neither, so the two are treated the same. The procedure poses problems, however.

First, DOC caps the deduction from the home-market price for indirect selling expenses at the dollar amount (or foreign-currency equivalent of the dollar amount) of the deduction for such expenses made in the U.S. import price. Especially for Japanese firms, which often face high home-market selling expenses because of an inefficient distribution system, the cap biases DOC's finding in favor of dumping.

A second problem arises because profits are not deducted from either the U.S. price or the foreign price. There is good reason for not deducting these profits: they are subject to manipulation by the foreign producer and could therefore be used to hide dumping. Thus, the firm could sell to its wholly owned subsidiary in its home market at an artificially low price. The subsidiary would then sell to the public at the normal price and make artificially high profits. The producer owns the subsidiary, so the profits of the subsidiary belong to the producer. The producer does not care whether it makes its revenue through prices charged to the subsidiary or through profits of the subsidiary.

If DOC was to deduct profits of wholly owned distributors from the domestic and foreign prices before comparing the prices, the artificially high profits in the producer's home market would result in artificially low prices to compare with the U.S. price. Similarly, the foreign producer could sell to its U.S. subsidiary at artificially high prices, causing the wholly owned distributor in the United States to have artificially low profits that would be subtracted from the U.S. price.

Although not deducting profits eliminates that problem, it creates another one. Cases arise in which an antidumping duty is assessed, and the U.S. distributor of the foreign producer simply absorbs all or most of the duty and continues to sell the product in the United States at a price below the producer's home-market price. The foreign producer cannot provide payments to the U.S. distributor because DOC would subtract those from the U.S. price before making the comparison with the home-market price. If the foreign

producer wholly owns the distributor, however, the producer can absorb the cost in the form of lower profits of the U.S. distributor. In such a case, the true margin of dumping would be twice the margin calculated by DOC.

Some people have proposed correcting this problem by treating the antidumping duty as a cost that must be subtracted from the U.S. price before comparing it with the foreign home-market price. That procedure, however, would have problems of its own. The duty owed is calculated from the price charged and thus cannot be determined until after the sale has been made. Hence, the foreign firm would have to predict the duty ahead of time and raise its price by the amount it predicts the duty will be. Alternatively, the rate of duty determined in the last previous investigation or review could be used as the cost. In that case, however, the only way the firm could ever cease dumping and thereby get rid of the dumping order would be to charge a price in the United States that is actually higher than its home-market price by the amount of the dumping duty.

Another problem occurs with the procedure used when the foreign firm sells directly to an independent distributor in the United States rather than to a wholly owned subsidiary. In that procedure, DOC compares the U.S. import price with the first arm's-length sale price in the exporter's home market. The two prices are adjusted for differences in direct selling expenses but not indirect selling expenses. If the first arm's-length sale in the home market is at the same level as the U.S. import sale, the procedure is fair and unbiased. If it is not at the same level, however, the procedure is biased one way or the other.

For example, using the import price means that the direct and indirect selling expenses and the profits of the distributor in the United States are excluded. If the distributor in the exporter's home market is wholly owned, however, the selling expenses and related profits are not deducted. That difference creates a bias in favor of a finding of dumping. The first arm's-length sale in the exporter's home market could be at a higher level than the export sale to the United States. In that case, the bias would go the other way, but that situation is probably less likely than the other case.

Providing Data for Investigations

To carry out its AD/CVD investigations, the Commerce Department needs data from the firms being investigated about their costs, subsidies, and possibly other factors. Firms fearful of having antidumping or countervailing duties imposed on their products might not wish to turn over information that could assist DOC in imposing such duties. U.S. law and police powers cannot force firms in foreign countries to hand the information over, so the law provides that DOC may use the "best information available" (BIA) whenever a firm does not provide needed information. In practice, BIA is the information supplied by the domestic industry petitioning for protection, and one would expect such information to be biased in favor of finding large dumping or subsidy margins. Hence, firms under investigation have an incentive to turn over the needed information.

The possible use of best information available is a fairly strong stick to encourage foreign firms to cooperate. One study examined 224 final dumping determinations by the Department of Commerce.[5] It found that the average final dumping margin in the 36 cases in which BIA was used was 66.7 percent, whereas the average in the 188 cases in which BIA was not used was 27.9 percent.

One might argue that firms with large true dumping or subsidy margins would be more likely not to cooperate than firms with small margins--that being the reason for those numbers. Indeed, sometimes domestic industries have erroneous information regarding the costs of foreign firms and therefore are unaware that the actual dumping margin in a given case is larger than the domestic industry is charging. In general, however, the incentive is for the domestic industry to exaggerate the dumping margin when providing BIA, so even firms with large margins have an incentive to cooperate. Thus, the difference in the average margins is likely to be the result in large part of BIA being biased.

5. Robert E. Baldwin and Michael O. Moore, "Political Aspects of the Administration of the Trade Remedy Laws," in Boltuck and Litan, eds., *Down in the Dumps*, pp. 269-270.

None of this is unfair in and of itself. DOC needs data from the firms it investigates, and some kind of stick such as BIA is needed as an incentive for the firms to be forthcoming. A problem has arisen, however, with the use of BIA--namely, firms find it difficult and expensive to provide the data that DOC needs in the form that the department wants it and within the deadlines set by DOC.

Numerous authors have discussed the problem. Tracy Murray has described the plight of the investigated firm as follows:

> Consider the problem facing the foreign respondent who receives a request for information from the DOC. It arrives in the form of a questionnaire, some 100 pages long, in English, requesting specific accounting data on individual sales to the United States, data needed to adjust arm's-length market prices to net ex-factory prices (that is, packaging costs, shipping costs, selling costs, distributor and other middleman costs, tariffs in the United States, distribution costs in the United States, and any costs of adding value in the United States), and a host of other details (especially if the foreign market value needs to be constructed). There must be enough information for the DOC to investigate nearly every U.S. sale (that is, every transaction) for a period of six months. All this information must be identified, retrieved, recorded, and then transmitted to the DOC in English on hard copy and in a computer-readable format within the short deadline stipulated under the U.S. antidumping statutes.[6]

Responses to the first portions of the request for data typically must be made in 30 calendar days, sometimes within two weeks.[7] If the firm fails to respond fast enough, BIA is used, biasing the determination against the firm. DOC maintains that it is generous with extensions of deadlines when needed. Critics say otherwise, however, and DOC is tightly constrained by the legal deadlines for its determinations.

The burden on domestic firms is considerably less. The Congress has required DOC and the International Trade Commission (ITC) to assist domestic firms filing petitions for antidumping and countervailing-duty relief. The amount of information required of domestic firms is smaller than that required of foreign firms, and the ITC does not require that the data be in computer-readable format because of the burden that would place on small firms.[8]

Calculating the Exchange Rate

Calculating a dumping margin requires comparing the U.S. price of a good, which is denominated in dollars, with the foreign price or constructed value, which is denominated in the foreign currency. To make the comparison, the prices (or price and cost) must be converted to the same currency, which requires using an exchange rate. Since exchange rates change over time, the question arises as to what exchange rate to use.

DOC converts foreign prices and costs into U.S. dollars using the exchange rate for the quarter in question obtained from the Bureau of the Customs, which in turn obtains it from the Federal Reserve Bank of New York. That rate is used even if the actual market exchange rate on the date of a sale during the quarter is different from the quarterly rate, unless the daily rate differs from the quarterly rate by more than 5 percent. In that case, the actual daily rate is used in place of the quarterly rate.

The policy can create errors in the calculated dumping margin as large as 5 percent, and the results can have peculiar effects, as shown by the following example.[9] Suppose the rate for the quarter is 100. If the rates on three consecutive days during the quarter are 104, 106, and 104, DOC's methodology would use 100, 106, and 100, respectively, for those days. If the actual daily rates were 96, 104, and 96, however, DOC's methodology would use 100, 100, and 100.

6. Tracy Murray, "The Administration of the Antidumping Duty Law by the Department of Commerce," in Boltuck and Litan, eds., *Down in the Dumps*, pp. 34-35.

7. Palmeter, "The Antidumping Law," p. 67.

8. Baldwin and Moore, "Political Aspects of the Administration of the Trade Remedy Laws," pp. 268-269.

9. Palmeter, "The Antidumping Law," p. 87.

DOC could use the daily market exchange rate for every day of the investigation, but such a procedure would have problems of its own. Minor exchange rate fluctuations occur frequently. Foreign firms cannot be expected to change their U.S. price on a daily basis to keep up with such fluctuations. To do so would prevent the use of any kind of published list price or the use of the price in advertising. Furthermore, pricing decisions are generally made as parts of long-term strategies, in which case a foreign firm would consider the average exchange rate it expects to prevail over the planning period when making its pricing decisions. Many firms invest considerable time, resources, and advertising money in developing market share and market goodwill. They are not likely to want to give that up by raising their prices to reflect a change in the exchange rate that they view as a temporary aberration.

DOC recognizes these problems at least to some extent. It gives firms up to 90 days to recognize changes in the exchange rate as being permanent and reflect them in their prices. It also makes allowances to ensure that temporary spikes in the exchange rate do not result in findings of dumping. One may argue that these measures are not adequate to take care of all problems in this regard, but they do take care of some of the more egregious ones.

The problem of choosing the correct exchange rate for dumping calculations is difficult, if not intractable. No one rate is valid for all firms and industries because the cost of gaining and losing market share varies from industry to industry. Further, whether the current exchange rate at any given time is permanent or a temporary aberration (and, if an aberration, how far out of line with the permanent rate it is) is subject to opinion and cannot be answered objectively. Probably the best that can be done is to pick a reasonable methodology--such as an average of the exchange rates over several quarters--and then set the *de minimis* level of dumping high enough that firms that use other reasonable methodologies in their business transactions are not found guilty of dumping simply by virtue of that fact. DOC's exchange rate policy is questionable, although it makes some attempt at ameliorating some of the more egregious problems that can occur. The *de minimis* level of dumping, however, is not set high enough to eliminate problems.

Setting *De Minimis* Levels of Dumping

The *de minimis* level of dumping set by DOC--that is, the level above which dumping is considered to exist and below which *no* dumping is considered to exist--is 0.5 percent of the U.S. price of the import. That level has two problems. First, dumping at even twice this margin is highly unlikely to injure U.S. firms at all. Successful predatory pricing would probably require at least 20 times this margin. One might argue that determining injury is the function of the ITC, not DOC. A finding of dumping allows a case to continue, however, thereby continuing the burden on the foreign firm that was discussed above.

A second problem with the low *de minimis* level is that DOC is often unable to determine dumping margins within an error of 0.5 percent. Many products are produced by multiproduct firms. Such firms have overhead costs that are relevant to all products and for which opinions can differ as to how much should be allocated to each of the various products. Similarly, such firms often engage in research producing results that are used in several products, and there is no objective answer to the question of how much of the research costs should be attributed to various products in a dumping investigation. Estimates of depreciation rates and rates of obsolescence are very rough and subject to opinion. How these and many other questions are handled are often dictated by accounting standards that vary from country to country.

With all of these problems, DOC is unlikely to be able to determine dumping margins reliably within an accuracy of several percentage points, much less 0.5 percent. Recall that the exchange rate methodology used by DOC can produce errors as large as 5 percent, which is 10 times the *de minimis* margin.

How the Process Works for Nonmarket Economies

The problem is much worse for cases involving countries with nonmarket economies. In market economies,

the price of a good or service tends to reflect the true cost to the economy of producing it. That is not the case in a nonmarket economy, however, where administrative fiat determines prices. Hence, the cost of producing a product in a nonmarket economy cannot be calculated by adding up the various inputs multiplied by their respective prices. To find the cost, DOC multiplies the quantities of the various inputs used in the country in question by the prices of the respective inputs that prevail in another country that has a market economy, thereby obtaining costs for the various inputs. It then adds up those calculated input costs to obtain the total cost.

That procedure may be the best that can be devised to determine dumping in a nonmarket economy. Yet even at its best--when DOC uses a country with a similar level of development, similar resources, and the like--the procedure is not very accurate. Different countries have different tariff structures, which causes the prices of various goods and services to differ in ways that are too complicated to sort out without detailed models of the economies. Furthermore, different cultures in different countries lead to different patterns of consumption and production, which in turn lead to different prices. In short, even countries that appear to be similar are likely to have significant differences.

In practice, the procedure is often not at its best. Frequently, no market economy similar to the economy under investigation exists, or DOC chooses not to use the most closely similar countries because those countries too are under investigation. Further, the choice of the most similar country has a large element of subjectivity to it, leaving room for DOC to choose a country that would make the dumping margin look large. In some cases, the comparisons have been strained. For example, Robert A. Cass and Stephen J. Narkin report that with the criteria of similar economic structure and similar level of development:

> It would be hard to find (as Commerce has found) that a combination of the Federal Republic of Germany, Japan, France, Canada, Switzerland, and the Netherlands represents a good surrogate for the People's Republic of China or that the United Kingdom or the Federal Republic of Germany are suitable surrogates for the Soviet Union.[10]

In those cases, the surrogate countries are much more developed than the countries being investigated, which means that wages are much higher in the surrogate countries than in the investigated countries. Those higher wages are especially important when one considers that the low wages in the investigated country encouraged the use of less labor-saving capital and more labor than the higher-wage surrogate country would use.

The Commerce Department has argued that the choice of surrogates described in the quotation above could no longer occur because of changes in laws and procedures. Such changes, however, cannot create good surrogate countries when good surrogate countries do not exist. Further, though properly chosen rules could limit the subjectivity involved in picking a surrogate country, it would be difficult if not impossible to eliminate the subjectivity without imposing rules that sometimes lead to bad choices.

How Industries Are Defined

How an industry is defined is important for determining whether or not dumped and subsidized imports cause material injury. Import competition might substantially curtail narrowly defined parts of an industry while the industry as a whole remains healthy and uninjured. If the industry is defined to consist solely of those narrow parts, the ITC is much more likely to find that the imports cause material injury.

An example of that problem is the series of cases concerning fresh cut flowers, which will be discussed in more detail below. In cases where the flower industry as a whole or broad segments of it were at issue, the ITC usually found no injury. When the domestic industry later filed cases for specific flowers, the ITC did find injury. It is not unusual for antidumping and countervailing-duty orders to apply to products that are clearly only a small part of the output of what most people would think of as an industry. For example, one current antidumping order applies to chrome-plated lug nuts but not other varieties.

10. Ronald A. Cass and Stephen J. Narkin, "Antidumping and Countervailing Duty Law: The United States and the GATT," in Boltuck and Litan, eds., *Down in the Dumps*, p. 216.

Applying Retrospective Duty Assessment

The retrospective nature of the U.S. system of antidumping and countervailing duties introduces uncertainty that makes the duties more protective than they would appear. A firm importing goods under an AD/CVD order does not know how much it will ultimately owe in duties.

At the time of import, the firm pays an estimated duty equal to the dumping or subsidy margin determined in the AD/CVD investigation or, if there has been one, the last administrative review. If an administrative review occurs before the imports are liquidated (that is, before the final paperwork on duties owed is completed), however, the firm may find that the actual dumping or subsidy margin for the imports in question was either larger or smaller than the estimated duty paid. If it was larger, the importer will have to make up the difference. To reduce its exposure to this risk, the importing firm is likely to reduce imports of the product from the exporter in question and switch to a different supplier.

Using Administrative Proceedings

As was discussed in Chapter 3, dumping was once a criminal offense tried in a court of law and subjecting violators to fines, imprisonment, and civil suits. Now, however, both antidumping and countervailing-duty cases are decided administratively and involve added duties on the imports rather than criminal and civil penalties.[11] Although cases can be appealed to the Court of International Trade, and from there to the Court of Appeals for the Federal Circuit, the administrative and noncriminal nature of the cases means that the U.S. government has greater latitude in the procedures it can use in determining dumping. As a result of that greater latitude, a firm accused of dumping may find it more difficult to defend itself successfully.

Viewed from the perspective of the AD/CVD laws as an alternative to the escape clause, the change from courts and punishment to administrative agencies and duties is entirely appropriate. DOC and the ITC are more knowledgeable about trade and U.S. industries and their need for protection than are the courts. Moreover, since the emphasis is on protecting U.S. industries rather than deciding the guilt and punishment of foreign firms for misdeeds, there are no defendants and no need for courts to protect defendants' rights.

Clearly, however, though foreign exporters are not subject to criminal conviction and punishment under current AD/CVD law, they are harmed by antidumping and countervailing duties, lending credence to the view that protections similar to those of the criminal law should be maintained. From the perspective of the AD/CVD laws as preventing, punishing, and offsetting the effects of predatory pricing or other unfair trade practices, some of the procedures that have evolved appear unfair and likely to introduce bias against foreign exporters and U.S. consumers.

Decisions Are Made by an Advocate of One Side in the Case

The Office of Investigations in DOC effectively serves as investigator, prosecutor, judge, and jury in dumping and subsidy determinations. It investigates the firms in question--sometimes on its own initiative--and makes the determination of dumping or subsidy. Not even an administrative law judge separate from the investigators makes the decision.

Further, as was discussed in Chapter 3, DOC is expected to be an advocate of U.S. business in general. Thus, DOC, which plays the role of judge in AD/CVD cases and therefore should be neutral, is actually an advocate of one of the parties to the cases. The problem is made more serious by the requirement in the Trade and Tariff Act of 1984 that the agencies administering the AD/CVD laws give technical assistance to small firms desiring to file petitions for relief.

11. That is true provided the cases do not involve predatory intent and therefore are not being pursued under the Antidumping Act of 1916. See Chapter 3.

Some Firms Are Assumed to Be Dumping Until Proven Otherwise

When the number of firms in an antidumping case is so large as to strain its resources, DOC investigates a sample of the firms rather than all of them. For the sample, DOC typically starts with the firm with the largest market share, proceeds to the firm with the next largest share, and so on until it has chosen enough firms to cover 60 percent of the imports in question. For each investigated firm for which the determinations of dumping and injury are positive, an antidumping duty equal to the dumping margin found in the investigation is imposed. Then, an antidumping duty equal to the weighted average of the duties on all the investigated firms is imposed on the firms that were not investigated.

In calculating the weighted-average duty to be applied to uninvestigated firms, DOC, for reasons that are unclear, leaves out all zero and *de minimis* margins found on investigated firms, thereby increasing the calculated average. If one or more of the investigated firms fails to provide information requested by DOC, however, and DOC consequently uses the best information available, the resulting dumping margin determined for that firm is included in the average.

Uninvestigated firms can voluntarily provide information during the investigation and thereby get an individual dumping margin determined. Since DOC chooses the firms with the largest market shares, however, the uninvestigated firms are likely to be the smaller firms that find the cost of meeting DOC's information demands to be the most onerous.

Subsequent administrative review will determine whether each uninvestigated firm is indeed dumping. For each firm that is not, the estimated duties paid will be returned with interest. That does not eliminate the damage to those firms, however. Because the U.S. importer, rather than the foreign exporter, pays the estimated duties, the importer is not likely to know whether the exporter is dumping and therefore would have to assume that the estimated duties might not be refunded. Consequently, it would probably reduce imports of the good from the firm in question and switch to another supplier. Refunding deposits of estimated duties after an administrative review found them unjustified would not restore the sales lost before the review. The firm could lower the price to try to keep from losing the sales, but doing so would virtually guarantee that the administrative review would find dumping.

The sampling procedure effectively means that in cases where both DOC and a defendant firm find an investigation to be too expensive and troublesome to undertake, the firm is assumed to be dumping and punished at least until the first administrative review. That practice is a reversal of what occurs in criminal trials, in which people are assumed innocent until proven guilty, and in civil suits, in which plaintiffs must win in court before receiving monetary damages.

The sampling procedure also punishes uninvestigated firms for the dumping other firms commit. Including cases that involve BIA punishes uninvestigated firms for the failure of investigated firms to comply with DOC's demands for data.

Clearly, from the perspective of antidumping and countervailing duties as punishment of foreign firms for unfair trade and as offsets of the effects of unfair trade, the sampling procedure is unreasonable. If, however, the purpose of the duties is not to punish the foreign firms but to protect domestic industries from intense competition without regard to fairness, the procedure would seem no different than ordinary tariffs and quotas.

Cases Can Be Used as Harassment Against Foreign Firms

In criminal trials, if a defendant is found innocent, the prosecutors cannot bring charges again for the same offense. In trade remedy cases, that prohibition does not provide much protection: each time a given good is imported represents a possible new offense, and several different laws can be used to obtain protection. As long as a good continues to be imported, nothing can stop the domestic industry from trying over and over again to obtain protection under the trade remedy laws.

The industry has several incentives to do just that. First, by using different laws (Section 201 escape clause, antidumping law, countervailing-duty law, and the like) and trying different tactics each time, the industry may eventually hit upon a tactic that succeeds in

getting protection. Furthermore, over time the personnel on the ITC or at DOC may change, possibly resulting in more sympathy for the domestic industry.

Second, repeated cases are expensive for the defending foreign exporters to deal with. The costs of complying with the Commerce Department's requests for information and of hiring U.S. legal help have already been discussed. Moreover, the bias in DOC's methodology and the low *de minimis* threshold it uses mean that a foreign firm is apt to be found to be dumping by at least a small amount.

The foreign firm having been determined to be dumping, the problem of retrospective duty assessment and resulting periods of uncertainty then kicks in. At least until the ITC's final determination of injury, and continuing after that determination if it is positive, imports will not be liquidated until sometime after they enter the country, meaning that the importer does not know the antidumping duty for sure until after it has imported the good. Thus, repeated filing of cases--even if none of the cases result in antidumping or countervailing duties--can be an effective form of harassment of foreign exporters by the domestic industry. They can hinder the imports and persuade the exporter to cease exporting to the United States, raise its prices, or enter into a "voluntary" restraint agreement.

An example is provided by the case of fresh cut flowers.[12] In the 1970s and 1980s, Colombia emerged as a major supplier of fresh cut flowers to the United States. For reasons of climate, soil, and an abundance of low-wage, unskilled labor, Colombian costs in 1970 were 31 percent lower than U.S. production costs, even after factoring in the higher transportation costs. In addition, Colombia's climate allowed growth of flowers without greenhouses during U.S. winter months for such high-flower-sales days as Valentine's Day, Easter, Christmas, Secretary's Day, and Mother's Day.

The growth of imports led U.S. growers to seek protection in 1977 under the Section 201 escape-clause provision of U.S. law. Recall from Chapter 1 that this provision provides for temporary protection from imports regardless of whether they are fairly or unfairly traded, but the imports must be a "substantial cause of serious injury" to the domestic industry. The ITC ruled against the domestic industry. The industry tried again under Section 201 in 1979, and the ITC once again ruled against it.

In the 1980s, the industry tried antidumping and countervailing-duty cases. From 1980 to 1985, it had only limited success in attempting to protect rose growers. A case concerning all cut flowers in 1986 resulted in a determination that Colombian exporters were being subsidized at rates of 4 percent to 5 percent. The Colombian growers agreed not to receive the subsidies, so no duties were applied. Then the domestic industry changed strategy, switching from protection for the industry as a whole or broad segments of it to protection for narrowly targeted segments. In 1986, the industry filed antidumping and countervailing-duty cases against seven types of flowers from 10 countries.

Those cases finally resulted in a number of favorable rulings from DOC and the ITC, and the industry finally received protection after failing many times before. All told, through 1989, 49 unfair import investigations took place concerning fresh cut flowers, 14 of them against Colombian exporters. One can find a similarly protracted history of repeated investigations and appeals relating to consumer electronics beginning in 1959 and extending over 20 years (see Table 2).

Setting AD/CVD Duties to Protect U.S. Firms

In the defense of antidumping and countervailing duties, analysts sometimes argue that they raise the prices of the goods in question back up to where they would be if the dumping or subsidies did not occur, thereby restoring the proper free-market result, which is thought to be optimal.

Some of the fallacies of this argument are evident from previous discussion in this study: dumping is a normal free-market result, both dumping and subsidies by foreign exporters and governments are economically beneficial to the U.S. economy as a whole, and raising the prices back to undumped and unsubsidized levels is

12. José A. Mendez, "The Development of the Colombian Cut Flower Industry: A Textbook Example of How a Market Economy Works," in J. Michael Finger, ed., *Antidumping: How It Works and Who Gets Hurt* (Ann Arbor, Mich.: University of Michigan Press, 1993), pp. 115-116.

Table 2.
History of Consumer Electronics Import Litigations, 1959-1979

Year	Complaint	Agency	Administrative and Judicial Action	Related Diplomatic Action
		Radios		
1959	Transistor radio imports from Japan posed a threat to U.S. national security		Case dismissed, May 1962, after two and a half years of investigations	Japanese government imposed voluntary export quotas on transistor radios to the United States
		Components		
1961	TV tube dumping	Treasury	No dumping found	
1964	TV tube dumping	Treasury	No dumping found	
1970	Fixed resistor, transformer, and capacitor dumping	Treasury	No dumping found	
1970	Tuner dumping	Treasury	Dumping found	
1972	TV tube dumping	Treasury	No injury to the U.S. industry found	
		Television Receivers		
1968	Monochrome and color TV receiver dumping	Treasury	Dumping found, March 1971. Dumping duties imposed retroactively, mid-March 1978	
1971	Escape-clause action claiming injury to the U.S. television industry	Tariff Commission	Case dismissed	
1970-1972	Three separate complaints, claiming that exports of Japanese color TV and other consumer electronic products were subsidized, resulting in injurious trade distortions	Treasury	Case dismissed, with negative determination	
1974	Antitrust violations by Matsushita Electric with the acquisition of Motorola's TV division	Justice	Acquisition not opposed	
1974	Violation of antitrust and antidumping laws	U.S. District Court, Philadelphia	Case pending (as of October 26, 1979)	

**Table 2.
Continued**

Year	Complaint	Agency	Administrative and Judicial Action	Related Diplomatic Action
		Television Receivers (Continued)		
1976	Appeal against the Treasury Department's ruling on export subsidies	U.S. Customs Court, New York	Unanimous decision that commodity tax rebate constitutes export subsidy calling for CVDs	
1977	Appeal against U.S. Customs Court decision	Court of Customs and Patents Appeals and U.S. Supreme Court	U.S. Customs Court decision reversed	
1976	Unfair trade practices, including subsidies for color TV exports and dumping	ITC	Reversal of U.S. Customs Court decision upheld and Treasury Department's dismissal of the case sustained	
1976	Allegations of 14 unfair trade practices coming within the scope of the AD, CVD, and antitrust laws	ITC	"No contest" consent order, under which the ITC would monitor Japanese pricing practices in the United States	
1976	Escape-clause action, seeking to impose import quotas on grounds of injury to the U.S. television industry	ITC	Case dismissed. Recommendation to the President that higher import duties be imposed on color televisions to protect an injured U.S. industry. Recommendations were rejected by the President after conclusion of the Orderly Marketing Agreement	Orderly Marketing Agreement signed between Japan and the United States, under which Japan agreed to limit color TV exports to the United States to 1,750,000 sets annually
		Microwave Ovens		
1979	Microwave oven dumping	Treasury and ITC	The Treasury requested the ITC to rule on the effects of imports of microwave ovens from Japan; the ITC found injury. Dumping investigation by the Treasury under way	

SOURCE: Gene Gregory, "The Profits of Harassment," *Far Eastern Economic Review* (October 26, 1979), pp. 74-79.

NOTE: CVDs = countervailing duties; ITC = International Trade Commission; AD = antidumping.

economically harmful to the U.S. economy as a whole. Even if that were not the case, however, the antidumping and countervailing duties stipulated by U.S. law are larger than they should be to restore the prices that would prevail if there were no dumping or subsidies. Hence, they result in prices that are higher than would prevail if there were no dumping or subsidies, and they thereby protect domestic industry at the expense of the consumer.

In the case of dumping, the reason that the U.S. price is lower than the foreign home-market price is normally (barring a recession in the United States) that the foreign exporter has a greater degree of monopoly power in its home market and is therefore able to charge a higher price than it could in a competitive market. Thus, at least part of the dumping margin, and possibly all of it, results from high prices in the home market and not from low prices in the U.S. market. Hence, the firm could charge a lower price in the home market and still make a profit there.

If the firm was prohibited from dumping, it most likely would do just that. It would eliminate the dumping margin partly by raising its U.S. price and partly by lowering its home-market price. The U.S. price would thus rise by only part of the dumping margin. The antidumping duty imposed by the United States, however, by law must be equal to the entire dumping margin--not just the amount by which the U.S. price would be higher if the foreign firm was prohibited from dumping. Hence, the antidumping duty raises the U.S. price higher than prohibiting dumping would.

Countervailing duties are also frequently too high in the case of production subsidies and subsidies on exports to all countries, at least in the case of competitive industries (see Box 3). Whether they are too high in cases of imperfectly competitive industries is unclear, but DOC makes no attempt (and the law does not allow it) to calculate the proper level of countervailing duty to offset the subsidy exactly.

Regarding limits on the size of antidumping duties, Article VI of the GATT says, "In order to offset or prevent dumping, a contracting party may levy on any dumped product an anti-dumping duty not greater in amount than the margin of dumping in respect of such product." The Antidumping Code says, "It is desirable . . . that the duty be less than the margin, if such lesser duty would be adequate to remove the injury to the domestic industry."

Regarding limits on the size of countervailing duties, Article VI holds, "No countervailing duty shall be levied . . . in excess of an amount equal to the estimated bounty or subsidy determined to have been granted. . . ." The Subsidies Code states, "It is desirable . . . that the duty be less than the total amount of the subsidy if such lesser duty would be adequate to remove the injury to the domestic industry."

Thus, U.S. antidumping and countervailing duties are in accord with the requirements of GATT Article VI and the Antidumping and Subsidies Codes. They are not in accord with what the codes say is desirable, however. The duty is always equal to the margin of dumping or subsidy, even when lesser duties would be adequate to remove any injury to the domestic industry.

Determinating Whether Subsidies Are Specific

The United States does not countervail subsidies generally available to all industries, but rather only those that, according to economic theory, affect trade. DOC, however, has some questionable policies for determinating what is a specific subsidy and what is a generally available subsidy.[13]

In particular, DOC considers regional subsidies--such as regional development programs, urban block grants, and regional job training programs--to be specific subsidies no matter how widely available they are to industries in the region, and it considers general agricultural subsidies to be nonspecific. Those classifications are wrong, and they conveniently exempt the largest U.S. subsidy programs affecting trade--those in agriculture--from countervailing duties while allowing the United States to impose duties against subsidies that are more commonly used by other countries.

13. For the most part, this section of the chapter consists of arguments and examples from Joseph F. Francois, N. David Palmeter, and Jeffrey C. Anspacher, "Conceptual and Procedural Biases in the Administration of the Countervailing Duty Law," in Boltuck and Litan, eds., *Down in the Dumps*, pp. 98-99.

Box 3.
Why the Countervailing Duty More Than Offsets the Subsidy in Cases of Competitive Markets

Suppose that a foreign country subsidizes one of its industry's exports to the United States and a third country, that the subsidy is proportional to the value of the exports in question, that the industry is competitive so that no one firm can significantly affect the market price in any country, and that the firms in the industry have increasing marginal and average costs--that is, increases in a firm's output cause its marginal and average cost per unit of output to increase--as is often the case in the real world.[1]

That situation can be analyzed as the superimposition of two cases: one in which the country subsidizes its industry's exports to the third country but not the United States, and one in which the country subsidizes its industry's exports to the United States but not the third country. In both cases, one must assume that no trade is allowed between the other country and the United States in order to keep subsidized exports to one country from being reexported from that country to the other and thereby undercutting the unsubsidized exports to the second country. This requirement disappears once the cases are superimposed because exports to both countries are subsidized.

Examine first the case in which the foreign country subsidizes its industry's exports to the third country but not its exports to the United States. The subsidized exports to the third country would increase those exports, which would increase the outputs of the firms in the industry and therefore increase their marginal and average costs. The increase in marginal cost would cause the firms to increase the price they charge on exports to the United States (since firms set price equal to marginal cost for profit maximization in unsubsidized markets), and this price increase would decrease the quantity of those exports. Thus, the subsidy on exports to the third country increases the price and decreases the quantity of exports to the United States.

Examine next the case in which the foreign country subsidizes its industry's exports to the United States but not to the third country. The subsidy would lower the price and increase the quantity of exports to the United States if it was not countervailed. U.S. law, however, stipulates a countervailing duty exactly equal to the subsidy margin. Such a subsidy would exactly offset the decrease in price and therefore restore both the price and quantity of exports to their unsubsidized levels.

Finally, superimpose the two cases to obtain the situation of interest: where the foreign country subsidizes its firms' exports to both the United States and the third country. The subsidy on exports to the United States decreases their price and increases their quantity. The subsidy on exports to the third country raises the price of exports to the United States and lowers their quantity, which partially offsets the effect of the subsidy on exports to the United States. Recall from the second case above that the countervailing duty alone is large enough to offset completely the subsidy on exports to the United States. Thus, the countervailing duty plus the effects of the subsidy on exports to the third country together more than offset the effects of the subsidy on exports to the United States. In other words, in this case the countervailing duty stipulated in U.S. law is too large: it more than offsets the net effects of the subsidy on exports to the United States.

The same is true of a production subsidy, but the effect is even larger. A production subsidy effectively subsidizes domestic sales of the subsidizing country as well as exports to the United States and other countries. Thus, both domestic sales and exports to the third country increase, thereby increasing the marginal costs of the producers. Those higher marginal costs result in higher prices for and lower quantities of exports to the United States, which partially offset the lower prices and higher quantities that result from the portion of the production subsidy that subsidizes exports to the United States. Once again, the U.S. countervailing duty is large enough to offset this portion all by itself and therefore is too large when all of the effects are netted out.

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1. The argument presented here is taken from Richard Diamond, "Comment," in Richard Boltuck and Robert E. Litan, eds., *Down in the Dumps: Administration of the Unfair Trade Laws* (Washington, D.C.: Brookings Institution, 1991), pp. 141-151.

In DOC's defense, one can say that if it considered otherwise nonspecific regional subsidies to be specific, an exporting country could abuse the policy by granting a subsidy to all firms in a region whose geographic boundaries were carefully tailored to include only a particular industry. It would seem, however, that DOC could use its subjective judgment to make exceptions for such cases, just as it already uses its subjective judgment to make exceptions for cases in which subsidies by law are nonspecific but appear in practice to go only, or disproportionately, to certain industries.

Chapter Five

The Economic Effects of the Current AD/CVD Laws and Procedures

Statistics indicate that almost all antidumping cases filed by U.S. firms result in findings of dumping, and the vast majority of countervailing-duty cases result in findings of subsidies. In the United States and other major trading countries, domestic firms have found it fairly easy to get protection under the AD/CVD laws. In fact, protection has become so easy that the safeguard laws (such as the Section 201 escape clause), which are designed to provide temporary emergency protection, have largely fallen into disuse. The AD/CVD laws have effectively replaced them and become de facto safeguard laws without the restrictions the General Agreement on Tariffs and Trade places on de jure safeguard laws.

The view that the AD/CVD laws should serve as a general source of protection for uncompetitive industries appears to influence the behavior of several parts of the U.S. government. Evidence suggests that the Department of Commerce and the International Trade Commission more often rule in favor of protection in cases where U.S. firms are uncompetitive than in cases where they are not. Furthermore, recent changes in the laws have made it more difficult for foreign firms to circumvent AD/CVD orders. Such circumvention diminishes the effectiveness of the laws as safeguards.

How much of an impediment to trade do the AD/CVD laws pose? The extent is difficult to assess precisely. Right now, there is no good overall measure. Initial inspection of some obvious measures indicates that the laws are a small and insignificant component of U.S. trade protection. Closer inspection, however, reveals that the laws have a much larger effect than would appear at first glance.

Protection Against Unfair Imports, or Protection of Uncompetitive Industries from All Imports?

Several statistical studies have examined the effects of the AD/CVD laws and procedures. The results of these studies indicate that the AD/CVD system serves as a general source of protection for domestic industries from both fair and unfair imports.

The Commerce Department Seldom Fails to Find Dumping or Subsidies

Though not conclusive, available evidence strongly suggests that the Commerce Department's procedures are severely biased in favor of findings of dumping and subsidies. One major piece of evidence in support of this conclusion is that the Commerce Department seldom fails to find dumping or subsidies in AD/CVD cases.

Cases much more often fail the final International Trade Commission injury test than fail the final Commerce Department dumping or subsidy test. As the numbers in Table 3 indicate, DOC found no dumping in only 11 percent of its final determinations from 1980 through 1984 (9 out of 79 cases), 8 percent of its final determinations from 1985 through 1988 (11 out of 134 cases), and 3 percent of its final determinations from 1989 through 1992 (4 out of 126 cases). For the entire 1980-1992 period, it found dumping in only 7 percent of cases (24 out of 339 cases).

Substantially greater percentages of ITC injury determinations were estimated to be negative. Of preliminary determinations of injury from 1980 through 1992, 27 percent were negative (123 out of 462 determinations), and 34 percent of final determinations were negative (108 out of 315 determinations).

The numbers for countervailing-duty cases are only slightly less striking (see Table 4). DOC found no subsidies in only 9 percent of its final subsidy determinations from 1980 through 1984 (8 out of 93 cases), 18 percent of its final determinations from 1985 through 1988 (9 out of 50 cases), and 32 percent of its final determinations from 1989 through 1992 (6 out of 19 cases). For the entire 1980-1992 period, it found subsidies in only 14 percent of cases (23 out of 162 cases)

Table 3.
Frequencies of Affirmative and Negative Determinations by DOC and ITC in Antidumping Cases

	1980-1984	1985-1988	1989-1992	Total, 1980-1992
Number of Decisions				
Preliminary ITC Injury Determinations Decided Affirmatively[a]	79	134	126	339
Preliminary ITC Injury Determinations Decided Negatively	46	28	49	123
Final DOC Dumping Determinations Decided Affirmatively[a]	70	123	122	315
Final DOC Dumping Determinations Decided Negatively	9	11	4	24
Final ITC Injury Determinations Decided Affirmatively	47	88	72	207
Final ITC Injury Determinations Decided Negatively	23	35	50	108
Percentage of Decisions[b]				
Preliminary ITC Injury Determinations Decided Affirmatively	63	83	72	73
Preliminary ITC Injury Determinations Decided Negatively	37	17	28	27
Final DOC Dumping Determinations Decided Affirmatively	89	92	97	93
Final DOC Dumping Determinations Decided Negatively	11	8	3	7
Final ITC Injury Determinations Decided Affirmatively	67	72	59	66
Final ITC Injury Determinations Decided Negatively	33	28	41	34

SOURCE: Congressional Budget Office based on data compiled by Morris E. Morkre and Kenneth H. Kelly of the Federal Trade Commission, Bureau of Economics.

NOTE: DOC = Department of Commerce; ITC = International Trade Commission.

a. Calculated as an approximate lower bound by adding the affirmative and negative final determinations of the next stage of the determination process.

b. Percentages are calculated based on the numbers of affirmative and negative decisions. Where the number of affirmative determinations is an approximate lower bound, the calculated percentage is also an approximate lower bound, and the calculated percentage of negative determinations is an approximate upper bound.

Table 4.
Frequencies of Affirmative and Negative Determinations by DOC and ITC in Countervailing-Duty Cases

	1980-1984	1985-1988	1989-1992	Total, 1980-1992
Number of Decisions				
Preliminary ITC Injury Determinations Decided Affirmatively[a]	93	50	19	162
Preliminary ITC Injury Determinations Decided Negatively	54	10	8	72
Final DOC Subsidy Determinations Decided Affirmatively[a]	85	41	13	139
Final DOC Subsidy Determinations Decided Negatively	8	9	6	23
Final ITC Injury Determinations Decided Affirmatively	27	25	8	60
Final ITC Injury Determinations Decided Negatively	58	16	5	79
Percentage of Decisions[b]				
Preliminary ITC Injury Determinations Decided Affirmatively	63	83	70	69
Preliminary ITC Injury Determinations Decided Negatively	37	17	30	31
Final DOC Subsidy Determinations Decided Affirmatively	91	82	68	86
Final DOC Subsidy Determinations Decided Negatively	9	18	32	14
Final ITC Injury Determinations Decided Affirmatively	32	61	62	43
Final ITC Injury Determinations Decided Negatively	68	39	38	57

SOURCE: Congressional Budget Office based on data compiled by Morris E. Morkre and Kenneth H. Kelly of the Federal Trade Commission, Bureau of Economics.

NOTE: DOC = Department of Commerce; ITC = International Trade Commission.

a. Calculated as an approximate lower bound by adding the affirmative and negative final determinations of the next stage of the determination process.

b. Percentages are calculated based on the numbers of affirmative and negative decisions. Where the number of affirmative determinations is an approximate lower bound, the calculated percentage is also an approximate lower bound, and the calculated percentage of negative determinations is an approximate upper bound.

As for ITC determinations, 31 percent of preliminary determinations from 1980 through 1992 were negative (72 out of 234 determinations), and 57 percent of final determinations were negative (79 out of 139 determinations).

A study of AD/CVD cases obtained similar results using a slightly different method.[1] That study found that 23 percent of the preliminary ITC injury determinations from 1980 through 1988 were negative (129 out of 573 determinations), 11 percent of final DOC dumping and subsidy determinations were negative (60 out of 544), and 37 percent of the final ITC injury determinations were negative (113 out of 303). Those numbers are reasonably close to the ones in Tables 3 and 4.

Together, these data indicate that the requirements for obtaining relief under the AD/CVD laws have become effectively similar to those for obtaining relief under the escape clause. Legally, the AD/CVD laws require demonstration of dumping or subsidy and demonstration of injury, whereas escape-clause cases require only demonstration of injury (although with a higher standard for injury). Proving dumping or subsidies is not much of a hurdle, however, since DOC's procedures find dumping or subsidies in the vast majority of cases. The main hurdle in AD/CVD cases is the same as in

1. J. Michael Finger and Tracy Murray, "Antidumping and Countervailing Duty Enforcement in the United States," in J. Michael Finger, ed., *Antidumping: How It Works and Who Gets Hurt* (Ann Arbor, Mich.: University of Michigan Press, 1993), pp. 241-254.

escape-clause cases: proving injury. Over four times as many cases fail the ITC injury test as fail the DOC dumping and subsidy test.

Defenders of DOC procedures have argued that other reasons besides biased procedures could explain why so few cases fail determinations of dumping or subsidy by DOC and so many more fail determinations of injury by the ITC. One reason given is that the preliminary ITC determination of injury comes first and eliminates weak cases before they reach DOC's final determination of dumping or subsidy. That sequence might raise the percentage of affirmative DOC final dumping and subsidy determinations somewhat.

Even if one assumes, however, that most cases with low dumping margins are screened out in the preliminary injury test (which is unlikely), that argument cannot completely explain the statistics. The preliminary ITC injury test and the final DOC dumping and subsidy tests should similarly screen out weak cases before they reach the ITC's final determination of injury. Yet the percentage of final ITC injury determinations that are negative is substantially greater than the percentage of final DOC determinations of dumping and subsidy (especially in dumping cases) that are negative.

A second reason that is given is self-selection: domestic industries do not file cases when there is no dumping or subsidization of imports. According to this argument, domestic industries would see no point in incurring the substantial costs of filing a case if lack of dumping or subsidies meant that antidumping or countervailing duties were unlikely to be imposed. Although this argument cannot be dismissed completely, several problems with it make it unconvincing.

One problem is that many industries have an incentive to file AD/CVD cases even when no dumping or subsidies exist. AD/CVD cases provide an effective means to harass and impose substantial costs and uncertainty on foreign competitors--costs that are much larger than the cost to the domestic industry of filing such cases. Because of these costs and the uncertainty, foreign exporters facing AD/CVD cases frequently agree to export restraints even if they are not dumping or receiving subsidies. One of the studies discussed above found that 45 percent of the cases it examined ended in negotiated export restraints.[2] Some of the cases that ended in that way also received final determinations of dumping (or subsidy) and injury. Of those that did, 58 percent failed either the dumping/subsidy or the injury test, meaning that AD/CVD duties would not have been imposed.

Another problem with the argument is that a similar one could be made about the injury test. What is the point of incurring the substantial costs of filing a case if lack of injury makes it unlikely that antidumping or countervailing duties will be imposed? Hence, one would expect the rate of negative determinations of injury by the ITC to be just as low as the rate of negative determinations of dumping and subsidies. One might even argue that uninjured industries are even less likely to file a case than firms competing with imports that are not dumped or subsidized, since the lack of injury means that the industry has little to gain even if duties are imposed. That argument has some merit, but it is not conclusive since even a firm uninjured by recent increases in imports could gain from duties that remove a long-standing foreign presence from the domestic market.

A final reason that defenders of DOC procedures give for the statistics relates to the relative uncertainty on the part of a petitioning firm in predicting the outcome of a determination. According to that argument, well-defined rules govern findings of dumping and subsidies, and therefore the outcomes of such cases are easier for domestic industries to predict than determinations of injury, which are inherently subjective. Hence, firms more often err in filing cases that eventually fail the unpredictable injury test than in filing cases that eventually fail the test for dumping or subsidies.

This argument cannot be completely dismissed. Determinations of injury are indeed more subjective and difficult to predict. However, DOC determinations of dumping and subsidies are unlikely to be so easy to predict that only 7 percent of firms would err in filing a dumping case that would fail the dumping test (or only 3 percent, as happened in the 1988-1992 period).

2. Finger and Murray, "Antidumping and Countervailing Duty Enforcement in the United States."

Uncompetitive Industries Are More Likely Than Others to Receive Protection

Are uncompetitive industries more likely than others to receive protection under the AD/CVD laws? Two studies contain pertinent results. Though their findings are subject to interpretation and thus cannot be considered conclusive, one may reasonably infer from them that uncompetitive industries are indeed more likely to receive protection.[3]

A recent study examined ITC injury decisions for antidumping cases from 1980 through 1986.[4] That study attempted to determine whether ITC commissioners based their decisions solely on factors indicating injury to the industry by dumped imports or whether other factors also entered into their decisions. The author made the examination by estimating an equation that related the votes of individual ITC commissioners to 17 different variables. The 17 included five variables that a commissioner might consider relevant to determining whether an industry was injured by dumped imports--change in production, change in production employment, change in profit-to-sales ratio, change in volume of dumped imports, and the dumping margin--and 12 other variables that did not relate to injury by dumped imports.

Of particular interest here, the 12 others included four variables that could be viewed as proxies for the competitiveness of the industry: changes in volume of all imports (not just dumped imports), the wage rate, whether the imports in question come from a developing country, and whether the imports come from a newly industrialized country (NIC).[5] As to the first of these four variables, one would expect an industry with declining competitiveness to experience increasing competition from all imports--dumped or not. Regarding the other variables, low-wage industries are generally unskilled-labor-intensive industries for which the United States has a comparative disadvantage, and NICs and developing countries in particular have a comparative advantage over the United States in such industries because of their abundant supplies of low-wage, unskilled labor.

The equation the author estimated for preliminary determinations of injury indicates that the ITC was more likely to find injury in cases where the industry had a low wage rate and the imports in question came from a developing country. Whether total imports--dumped or not--increased and whether the imports came from a NIC were not significant. The equation for final determinations of injury indicates that the ITC was more likely to find injury in cases where all imports of the good in question--dumped or not--were increasing and the imports in question came from a NIC or a developing country. The wage rate was not significant. These results support the proposition that the ITC was more likely to favor protection (find injury) for industries that were uncompetitive (or had declining competitiveness) than for other industries.

A related study examined DOC's determinations of dumping and subsidy over roughly the same time period as the study just discussed.[6] The results provide evidence that DOC tends to find larger dumping margins in cases where the U.S. industry is uncompetitive, although the evidence is weaker than that for ITC determinations of injury.

The second study estimated an equation relating the dumping margin found by DOC to 11 variables. The 11 included three of the four variables related to competitiveness that were tested in the first study: changes in the volume of all imports of the good in question (not just dumped imports), the wage rate, and whether the

3. "Competitiveness" is used here to mean the ability to simultaneously maintain market share and profitability.

4. Michael O. Moore, "Rules or Politics?: An Empirical Analysis of ITC Anti-Dumping Decisions," *Economic Inquiry*, vol. 30 (July 1992), pp. 449-466.

5. The remaining eight variables were (1) changes in employment for the four-digit Standard Industrial Classification (SIC) category that includes the industry in question (a broader classification than the industry itself), (2) the national unemployment rate, (3) the profit-to-sales ratio, (4) whether the imports come from Japan, (5) whether the imports come from a member country of the Organization for Economic Cooperation and Development, (6) the number of workers in the four-digit SIC category that contains the industry, (7) whether the industry contains a manufacturing plant in a state represented by a member of the Senate trade subcommittee, and (8) whether the industry contains a manufacturing plant in a Congressional district represented by a member of the House trade subcommittee.

6. Robert E. Baldwin and Michael O. Moore, "Political Aspects of the Administration of the Trade Remedy Laws," in Richard Boltuck and Robert E. Litan, eds., *Down in the Dumps: Administration of the Unfair Trade Laws* (Washington, D.C.: Brookings Institution, 1991), pp. 253-280.

imports in question came from a developing country.[7] The estimated equation indicated that the dumping margins determined by DOC were significantly related to two of those three variables--namely, changes in the volume of all imports and whether the imports came from a developing country.

Among the other variables in the equation was whether DOC used the best information available in its determination; the estimated equation indicated that was the most important factor influencing the size of dumping margins. Consequently, the authors reestimated the equation separately for cases in which BIA was used and for cases in which it was not used.

The three variables on competitiveness were not significant for either type of case when estimated separately this way, but for different reasons. For the non-BIA cases, the coefficients on the competitiveness variables were smaller, indicating that margins in these cases were not as strongly influenced by competitiveness of the domestic industry. For BIA cases, the coefficients were larger, indicating that the margins were more strongly affected. The variables tested as being insignificant because there were so few such cases that the error bars on the coefficient estimates were very large and consequently even large coefficients did not test as being significant.

A reasonable interpretation of the three equations taken together is that the margins determined by DOC are likely to be higher in cases where the domestic industry is uncompetitive than in other cases and that much of the influence occurs through the use of BIA. The evidence is not as strong as was the case for determinations of injury by the ITC. One possible reason is that the greater inherent subjectivity of the ITC's determinations of injury allows more room for considerations such as competitiveness to sway the votes of ITC commissioners. DOC's determinations are more rigidly determined by rules. Thus, for competitiveness to have a substantial influence, it must do so through the design of rules that do not nominally consider competitiveness but that have effects that are correlated with competitiveness.

Safeguard/Escape-Clause Laws Are Seldom Used

One of the studies discussed above points out that if the determinations by DOC of dumping and subsidies were significant hurdles in obtaining protection under the AD/CVD laws, a sizable number of escape-clause cases should have been filed by firms that could not demonstrate that the imports injuring them were dumped or subsidized.[8] In fact, however, relatively few such cases exist (see Table 5). From 1979 through 1988, 427 antidumping cases and 371 countervailing-duty cases were charged in the United States, but only 36 safeguard/escape-clause cases.

The situation is similar in other countries. The only difference between the United States and the other major users of AD/CVD laws in the 1980s (Australia, Canada, and the European Community) was that the other users resorted almost solely to AD laws, making little use of CVD laws. In contrast, the United States made substantial use of both AD and CVD laws. The numbers provide further evidence of bias in DOC procedures. They suggest that it has become easy enough to obtain relief under the AD/CVD laws that most industries use them in place of the safeguard laws.

Large, High-Profile Cases Still Get Negotiated Outcomes with Quotas

The standard prescribed remedies in the AD/CVD laws are antidumping and countervailing duties. Nevertheless, large, high-profile cases can still be settled by quotas rather than duties, and they often are. The escape clause, which often results in quotas, is still available. Further, once instituted, AD/CVD cases can be suspended or withdrawn by the petitioning industry in conjunction with quota protection negotiated with the for-

7. The other variables were (1) changes in the absolute value of the exchange rate, (2) whether "best information available" was used in the determination, (3) changes in the volume of dumped imports, (4) changes in domestic production, (5) the number of production workers in the domestic industry, (6) whether the imports came from Japan, (7) whether the industry contains a manufacturing plant in a state represented by a member of the Senate trade subcommittee, and (8) whether the industry contains a manufacturing plant in a Congressional district represented by a member of the House trade subcommittee.

8. Finger and Murray, "Antidumping and Countervailing Duty Enforcement in the United States."

Table 5.
Import Relief Measures Initiated, by Type and Country, 1979-1988

	Antidumping	Countervailing Duty	Escape Clause	Other	All Actions
United States	427	371	36	44	878
European Community	406	13	37	2	458
Australia[a]	478	22	1	0	501
Canada[a]	447	23	2	0	472
Developing Countries	75	0	0	0	75
Total	1,833	429	76	46	2,384

SOURCE: Patrick A. Messerlin, "Antidumping," in Jeffrey J. Schott, ed., *Completing the Uruguay Round: A Results Oriented Approach to the GATT Trade Negotiations* (Washington, D.C.: Institute for International Economics, September 1990), pp. 110-111.

a. Does not include cases for 1979, for which numbers were not available.

eign country or firms. This second possibility is not trivial. As mentioned previously, 348 of the 774 cases the authors of one study examined were superseded by export restraint agreements. Those cases include the large array of steel cases in the 1980s that ended with quota agreements.

Statistics indicate that the escape clause tends to be used for large, high-profile cases whereas the AD/CVD laws tend to be used for smaller, lower-profile cases. One study compared escape-clause cases with AD/CVD cases (which the authors call LFV, or less-than-fair-value, cases) for 1975 through 1979.[9] It found that the average escape-clause case concerned $331 million worth of imports, whereas the average AD/CVD case concerned only $106 million worth of imports. Excluding the steel and auto cases, which they argue should have been decided under the escape-clause mechanism, the average AD/CVD case involved only $28 million worth of imports. At the end of the study, the authors conclude:

> In law, the escape clause deals with injury to U.S. producers from import competition and the LFV mechanism with the fairness of business practices used in the U.S. market by foreigners. But in economics we find that they both deal with the same thing--injury from imports and the associated gains from trade. The functional difference between the cases which belong on one track or the other is the size and perhaps the degree of public awareness of the interests at stake, not the nature of those interests. Antidumping and countervailing duties are, functionally, the poor (or small) man's escape clause.[10]

Looking only at AD/CVD cases, a similar pattern appears in the differences between cases leading to suspension or quota agreements and cases leading to antidumping or countervailing duties. Seventy-five percent of the U.S. AD/CVD cases against developing countries from 1980 to 1988 led to restrictive outcomes, whereas only 65 percent of the cases against developed countries did so.[11] Nevertheless, 36 percent of the cases against industrialized countries led to negotiated export restraints, whereas only 15 percent of the cases against developing countries did so. The United States has more trade with industrialized countries overall than with developing countries. Cases against the former are likely to involve more trade and have a higher profile than cases against the latter. Hence, these statistics are consistent with the thesis that quota

9. J.M. Finger, H. Keith Hall, and Douglas R. Nelson, "The Political Economy of Administered Protection," *American Economic Review*, vol. 72, no. 3 (June 1982), pp. 452-466.

10. Ibid.

11. Finger and Murray, "Antidumping and Countervailing Duty Enforcement in the United States."

remedies are used more often in large, high-profile cases than in other cases.

Who Benefits and Who Gets Hurt?

Obviously, laws prohibiting foreign firms (and any other firms for that matter) from engaging in predatory pricing in the United States have a net beneficial effect on the U.S. economy. At the same time, laws prohibiting foreign firms from selling below cost in the United States and from selling below the firm's home-market price have a net detrimental effect on the U.S. economy. And when the AD/CVD laws function as a more general source of protection, they also have a net detrimental effect. Looking beyond those net effects, some sectors of the economy benefit from the laws while others are hurt.

Import-Competing Firms

The statistics cited above regarding the frequency of use of the AD/CVD laws and the Section 201 escape clause clearly indicate that import-competing firms generally prefer to use the AD/CVD laws and that therefore the laws must have benefited these firms, which explains why they came to be a substitute for the escape clause. Further, because the escape clause tends to be used more in large, high-profile cases and the AD/CVD laws in other cases, one can fairly infer that import-competing firms in the latter cases benefit more than those in the former cases. By examining the advantages and disadvantages of the AD/CVD laws relative to the escape clause from the perspective of an import-competing firm, the reasons for those patterns become clear.

To such a firm, the AD/CVD laws have several advantages over the escape clause. One advantage is a lower standard of injury. With the escape clause, imports must be "a substantial cause of serious injury" before protection can be granted; with the AD/CVD laws, they need only cause "material injury," which is much easier to prove. Before the Trade Agreements Act of 1979, countervailing-duty cases had no injury requirement at all.

Consider a second advantage for firms seeking protection under the AD/CVD laws. If dumping or subsidies can be proved and material injury proved also, protection is automatic under those laws. The President has no say in the matter, and effects on foreign relations and the welfare of consumers and other domestic industries are irrelevant. Under the escape clause, protection is at the option of the President, who is charged with considering the national interest in his decision. That difference is important. Between 1975 and 1985, the ITC forwarded 33 affirmative escape-clause decisions to the President, and the President rejected 15 of them.[12] The difference probably has its greatest effect in the case of smaller industries that are less important to the economy and are therefore less likely to be able to persuade the President that their protection is worth the cost to consumers, consuming industries, and U.S. foreign relations.

Other advantages for a firm seeking protection under the AD/CVD laws are that the firm has the public relations advantage of being able to label the imports "unfair," and that the protection provided can go on as long as the imports are dumped or subsidized, whereas the protection under the escape clause is limited to eight years. The purpose of the escape clause is to provide breathing room for the firm to adjust to import competition, either by becoming more competitive or by redirecting its resources to some other line of business or both. The firm is encouraged to submit an adjustment plan to the ITC and the U.S. Trade Representative, and the President considers any such plan in his decision about protection. With the AD/CVD laws, the firm need not worry about trying to adjust.

Offsetting those advantages of the AD/CVD laws is a disadvantage: the normal prescribed remedy is an import duty rather than the quotas available under the escape clause. Quotas are a more secure form of protection than are duties. That disadvantage helps explain why large, high-profile cases are more likely than others to be decided under the escape clause rather than the AD/CVD laws, and barring the escape clause, to be settled by suspension agreements or withdrawn in conjunction with a quota agreement rather than taken to the point of imposing duties. Such cases often involve industries with sufficient importance to the economy to

12. Baldwin and Moore, "Political Aspects of the Administration of the Trade Remedy Laws," p. 255.

persuade the President that the benefits of quota protection are worth the costs.

Consumers, Consuming Firms, and Exporting Firms

Although AD/CVD laws prevent predatory pricing, consumers are hurt by such laws and by any increase in the ease of obtaining protection under them.[13] AD/CVD laws raise prices and thereby decrease the amounts that consumers can purchase.

Consuming firms--that is, firms that purchase the imports or competing domestically produced goods for use as inputs in their production processes--are generally helped by low-priced imports and hurt by any kind of trade barriers put up against them. The higher prices resulting from trade barriers raise their costs and thereby make them uncompetitive with their own foreign competition. Thus, in general, consuming firms have been hurt by the expansion of the unfair trade laws and the implementation of the procedures to administer them.

U.S. trade restrictions do not directly affect exporting firms. Other countries, however, are following the U.S. lead in imposing antidumping duties, and some of these countries have imposed such duties on the products of U.S. firms in retaliation for the antidumping and countervailing duties the United States has imposed on their firms. Those duties hurt U.S. exporting firms, and the only way to stop them may be to negotiate limits in the GATT, which would also require the United States to limit its own AD/CVD actions.

A less visible mechanism also hurts exporting firms. By an accounting identity, the trade balance must equal the difference between saving and investment. Trade protection has little effect on saving or investment, so it cannot have much effect on the trade balance. Therefore, if such protection reduces U.S. imports, it must also reduce U.S. exports. By way of explanation, the exchange rate appreciates, which has the effect of making U.S. exports more expensive to foreigners. To put it another way, foreigners cannot buy U.S. exports if they do not have any dollars to buy them with, and the only way they can get those dollars is by selling their exports to the United States. If the United States refuses to buy imports (puts up trade barriers), foreign countries will have no dollars to buy U.S. exports.

Thus, consumers, consuming firms, and exporting firms have been hurt by the use of AD/CVD laws and policy as a general source of protection. According to one of the basic conclusions of trade theory and research, the total benefit of trade protection to import-competing firms is usually less than the total harm it inflicts on those other groups. As the U.S. economy becomes increasingly globalized, the numbers of consuming and exporting firms are multiplying and the harm to them is therefore becoming more significant to the economy as a whole.

Foreign Countries and Firms

U.S. protection hurts foreign countries and firms that export to the United States. They would normally prefer that protection cases be decided under the escape clause rather than the AD/CVD laws. The escape clause allows the President to take foreign policy and other considerations into account, which gives the foreign country greater leeway to try to influence the decision.

The escape clause also offers the possibility that trade restrictions will take the form of quotas rather than duties. Trade restrictions raise the price of the good in the United States. The quantity of imports after the restriction is imposed, multiplied by the amount by which the price is raised, is a rent that goes to the U.S. government in the form of duties if the restriction is a duty, or to the foreign exporter in the form of higher prices if the restriction is a quota. Thus, it is in the interest of foreign exporters that a trade restriction take the form of a quota rather than a duty.

Finally, the GATT allows foreign countries to impose restrictions of their own against the country

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13. For studies that examine the effects of trade barriers on consumers, see Gary Clyde Hufbauer and Kimberly Ann Elliott, *Measuring the Costs of Protection in the United States* (Washington, D.C.: Institute for International Economics, January 1994); U.S. International Trade Commission, *The Economic Effects of Significant U.S. Import Restraints, Phase I: Manufacturing*, USITC Publication 2222 (October 1989); and Congressional Budget Office, *Trade Restraints and the Competitive Status of the Textile, Apparel, and Nonrubber-Footwear Industries* (December 1991), pp. 50-57.

putting up a safeguard, whereas it does not allow that with antidumping and countervailing duties. Even though such restrictions are not in the overall net economic interest of the foreign countries, foreign political leaders find them attractive for the same reason U.S. leaders find U.S. restrictions attractive--they help domestic import-competing firms.

Consider protection for the steel industry in the 1980s, which provides an excellent illustration of how both domestic industries and foreign countries prefer that U.S. protection take the form of quotas rather than duties. The U.S. industry filed a massive number of cases in order to try to force the negotiation of quotas. Some people argue that the filing was an attempt to overload the abilities of DOC to investigate the cases, but why that would force the negotiation of quotas is not clear. A more likely reason, however, is that a large number of cases would cause foreign-relations problems with a large number of important trading partners. That effect would give the Administration an incentive to negotiate quotas that were more to the liking of both the trading partners and the domestic industry.

How Much Do the AD/CVD Laws Impede Trade?

To what extent do the AD/CVD laws impede trade? The question is difficult to answer because no good overall measure exists. Initial inspection of some obvious measures could lead one to conclude that the effects of the laws are fairly trivial--and yet on closer examination, they are not. The duties imposed under the laws frequently are quite high and substantially reduce the imports in question. Further, the use of the laws is growing. Thus, the substantial attention the laws have drawn in the Uruguay Round may indeed be warranted.

In fiscal year 1992, AD orders covered only 0.61 percent of imports ($3.2 billion out of a total of $513.0 billion), and CVD orders covered only 0.70 percent ($3.6 billion out of $513.0 billion). Similarly, revenues from AD duties made up only 1.0 percent of total revenues from all import duties ($173 million out of $17.2 billion), and revenues from CVDs constituted only 1.1 percent ($181 million out of $17.2 billion). The trade-weighted average AD duty imposed was only 5.5 percent, and the trade-weighted average CVD imposed was only 5.0 percent.[14] If those statistics were complete, accurate, and reliable indicators of the protective effect of the AD/CVD laws, one could safely conclude that the AD/CVD laws are a fairly insignificant component of the array of U.S. trade barriers.

In fact, however, those statistics substantially understate the laws' significance for several reasons. First, in cases where many of the duties involved are high (as is true for U.S. AD/CVD orders), trade-weighted averages of the duties are likely to understate their typical magnitude substantially. Duties reduce the quantity of imports. The higher the duty, the more the quantity is reduced. In the extreme, duties can be so high as to completely eliminate imports. With imports eliminated, the duty would get a zero weight in a trade-weighted average and thus would not be counted. Without going to that extreme, more generally the higher a duty is, the more the duty will reduce the quantity of imports, and therefore the more that duty will be undercounted in a trade-weighted average.

One study calculated a modified trade-weighted average that does not suffer from this bias.[15] It took the duty rates for outstanding antidumping orders on January 1, 1992, and weighted each rate by the level of trade that existed just before its respective AD order was put into effect rather than by the level of trade on January 1, 1992. The result was an average duty rate of 46.1 percent for nonsteel-product cases and 27.5 percent for steel-product cases. Those percentages are substantially higher than the standard trade-weighted average of 5.5 percent given above.

Many antidumping and countervailing duties are indeed high (see Table 6). DOC found dumping margins greater than 50 percent in one-fifth of the dumping cases that received affirmative final determinations of injury by the ITC from 1980 through 1988 (20 out of 99 cases). The margins were greater than 25 percent in almost 40 percent of the cases (39 out of 99 cases), and were greater than 10 percent in almost two-thirds of the

14. See Department of Commerce and Department of the Treasury, *Annual Report on the Status of the Antidumping/Countervailing Duty Program* (1993).

15. Hufbauer and Elliott, *Measuring the Costs of Protection in the United States*, pp. 118-119.

Table 6.
Trade-Weighted Average Final Dumping and Subsidy Margins for AD/CVD Investigations Receiving Affirmative Final Injury Determinations by the ITC, 1980-1988

Trade-Weighted Average Dumping or Subsidy Margin per Investigation	Antidumping Investigations		Countervailing-Duty Investigations	
	Number	Cumulative Percentage	Number	Cumulative Percentage
Less than 3 Percent	11	11.1	12	30.7
3 Percent to 5 Percent	9	20.2	6	46.2
5 Percent to 10 Percent	16	36.4	5	59.0
10 Percent to 25 Percent	24	60.1	11	87.2
25 Percent to 50 Percent	19	79.8	4	97.4
50 Percent or Greater	20	100.0	1	100.0
Total	99	n.a.	39	n.a.

SOURCE: Congressional Budget Office based on data compiled by Morris E. Morkre and Kenneth H. Kelly of the Federal Trade Commission, Bureau of Economics; taken from the final-phase investigation reports of the International Trade Commission.

NOTE: AD/CVD = antidumping and countervailing duty; ITC = Interntional Trade Commission; n.a. = not applicable.

cases (63 out of 99 cases). In countervailing-duty cases, DOC found subsidy margins greater than 25 percent in almost 13 percent of the cases receiving affirmative final determinations of injury in those years (5 out of 39 cases) and margins greater than 10 percent in 41 percent of the cases (16 out of 39 cases).

Another study examined the effect of AD/CVD orders imposed in 1981 and 1982 and found that imports of goods on which AD/CVD orders were imposed in 1980 were 56 percent lower on average in 1981 than they were in 1980.[16] For AD/CVD orders imposed in 1981, it found imports were 16 percent lower in 1982 than they were in 1981.

Even given that the typical antidumping and countervailing-duty rates are much higher than the trade-weighted averages detailed at the beginning of this section, one might argue that the low percentage of imports subject to AD/CVD orders (0.61 percent subject to AD orders and 0.70 subject to CVD orders in fiscal year 1992) mean that the AD/CVD laws cannot be very significant and that, correspondingly, the low percentages of total revenues that antidumping and countervailing duties represent mean that AD/CVD laws are insignificant in comparison with other U.S. trade barriers (tariffs in particular). Those numbers too are misleading, however, for at least three reasons.

First, like trade-weighted averages of duties, they are distorted by the effects of the duties on trade. The share of imports covered by AD/CVD orders is biased downward by the reduction in imports caused by the antidumping and countervailing duties. It is difficult, if not impossible, to tell much of anything from the share of total duty revenue that antidumping and countervailing duties make up. High AD/CVD rates would get undercounted in total revenue measures and so would high tariff rates. Whether the bias is greater for the average of the AD/CVD duties or for the average of the tariffs is impossible to tell without examining the individual duties and tariffs in more detail, which defeats the purpose of using the averages.

Second, not all of the trade restrictions that result from AD/CVD cases take the form of duties. Almost 70 percent of the cases filed from 1980 through 1988 led to restrictive outcomes, but since 45 percent were superceded by quotas or suspension agreements, less than 25 percent of cases led to antidumping or countervailing duties. In other words, the total number of cases with restrictive outcomes was almost three times the number in which antidumping or countervailing

16. T.J. Prusa, "Why Are So Many Antidumping Petitions Withdrawn?" *Journal of International Economics*, vol. 33 (August 1992), pp. 1-20.

duties were imposed. The AD/CVD laws were at least partially responsible for both the semiconductor arrangement with Japan and the steel quotas negotiated with many countries in the 1980s.

Of course, the number of suspension agreements in effect varies over time, and the massive array of steel quotas of the 1980s has expired. As of June 1, 1993, 10 suspension agreements were in effect; seven agreements were completed in fiscal year 1992.[17]

17. Department of Commerce and Department of the Treasury, *Annual Report on the Status of the Antidumping/Countervailing Duty Program.*

A third reason that the low percentages of imports covered by AD and CVD orders is a misleading indicator of how much the AD/CVD laws impede trade is that the existence and enforcement of the antidumping law has a deterrent effect that spreads beyond the firms actually required to pay duties. Many firms are likely to refrain from vigorous competition in order to avoid becoming ensnared in the antidumping law. That effect is magnified because even in cases where dumping or injury is not found and hence duties are not imposed, firms subject to AD/CVD investigations have to incur considerable expense defending themselves and complying with DOC requests for data.

Chapter Six

The Uruguay Round Agreement

As in previous negotiating rounds of the General Agreement on Tariffs and Trade, the antidumping and countervailing-duty laws were a major issue in the Uruguay Round. The negotiations produced new Antidumping and Subsidies Codes with a number of changes from the old codes. This chapter discusses the changes in the codes.

Provisions of the Agreement

In the Uruguay Round, the objectives of the United States included protecting its current AD/CVD laws and extending the antidumping provisions to allow retroactive duties and possibly a reduced standard for injury in cases of diversionary dumping (input dumping or downstream dumping), repeat corporate dumping (in which a firm has a history of dumping one product after another), and country hopping (in which a firm changes the country of production repeatedly to avoid antidumping duties). U.S. objectives also included increasing the transparency and due process of AD/CVD adjudication by other countries. That objective reflected the increasing use of AD/CVD laws against U.S. firms.

The United States was virtually alone in trying to extend the scope of restrictions against dumping and subsidies; most of the rest of the world lined up against it. The United States, Canada, Australia, and the European Union represent the four major users of AD/CVD legislation--and of these, Canada supported restrictions on AD/CVD legislation and duties until late in the negotiations. Significantly, Canada initially lined up against the United States, and Australia and New Zealand have eliminated the use of antidumping laws on trade between them in favor of antitrust laws.

The final "Agreement on Implementation of Article VI of GATT 1994" (Antidumping Code) and "Agreement on Subsidies and Countervailing Measures" (Subsidies Code) take some modest steps toward making the AD/CVD laws of the United States and other member countries less protectionist, but they leave much of current U.S. law and policy intact.

The new codes, unlike the old ones, will be signed by all signatories to the GATT. Perhaps the most important provisions in the new codes are new procedures for settling disputes that cannot be blocked by a country receiving an adverse ruling, and a sunset provision for automatically terminating AD/CVD orders after five years unless a likelihood of continued harm from dumping or subsidies can be shown. The new codes also provide for increased transparency and judicial review.

Definition of Subsidy and Specificity

Until now, the term "subsidy" has never been defined in a GATT agreement. The new Subsidies Code changes that. It defines a subsidy as existing in two situations.[1] The first is when a government or public body makes a financial contribution where:

1. Article 1, paragraph 1 of the Subsidies Code.

- A direct transfer of funds occurs (for example, grants, loans, equity infusions) or a potential direct transfer (for example, loan guarantees);

- Government revenue is forgone (for example, tax credits);

- A government provides goods or services (other than infrastructure) or purchases goods;

- A government makes payments to a funding mechanism or entrusts or directs a private body to carry out one of the above.

The second is when there are income or price supports in the sense of Article XVI of the GATT and a benefit is thereby conferred.

That definition would appear to include the vast majority of subsidies that might be encountered, but actually it does not include all of them. For example, Argentina once embargoed the export of leather hides, causing the price of hides in Argentina to decline and thus in effect subsidizing the Argentine tanned leather industry. Under the new definition, the tanned leather industry would not be considered to be subsidized.

The code stipulates that only specific subsidies are subject to being prohibited, retaliated against, or countervailed, and it provides the following principles for determining whether a subsidy is specific:[2]

- Explicit limits of subsidies to certain enterprises by the granting authority or legislation make a subsidy specific.

- If there are objective criteria governing eligibility for the subsidy that are clearly spelled out and strictly adhered to, specificity does not exist.

- Notwithstanding appearances of the first two principles, if in fact a subsidy goes to a limited number of enterprises or goes disproportionately to particular enterprises, it may be specific anyway.

- Subsidies limited to enterprises in regions smaller than the jurisdiction of the government granting the subsidy are specific. (Thus, a subsidy by a state or provincial government in the United States or Canada that is limited to enterprises in the state or province is not specific, but subsidies by the respective federal governments that are limited to a state or province are specific.)

- "Red-light" subsidies (discussed in the next section) are specific.

Those principles do not significantly change U.S. policy. The United States does not impose countervailing duties on nonspecific duties, and this definition of specificity is largely the same as the one the United States currently uses.

Which Subsidies Are Allowed and Which Are Not: The Traffic-Light Approach

The Subsidies Code makes a number of changes regarding which subsidies are allowable and which are not. It takes a "traffic-light" approach, with so-called "red-light" subsidies being prohibited in almost all circumstances, "green-light" subsidies being allowed in almost all circumstances, and "yellow-light" subsidies being allowed or not allowed depending on their effects on trade.

Red-Light Subsidies. Except as provided in the GATT Agreement on Agriculture, the category of red-light, or prohibited, subsidies includes all subsidies that depend, in law or in fact, at least partially on export performance, and all that depend at least partially on how much the manufacturer of the good uses domestically produced inputs over imported inputs.[3]

This category of red-light subsidies is an expansion of the prohibited one in the old Subsidies Code. In the old code, only export subsidies fell in this category, and moreover only export subsidies on products other than certain primary ones. Export subsidies on primary products were prohibited only when they resulted in an inequitable share of world trade or prices materially below those of other suppliers to the same market. Subsidies depending on the use of domestic inputs were not in this category.

2. Article 1, paragraph 2, and Article 2, paragraphs 1-3.

3. Article 3 of the Subsidies Code.

Green-Light Subsidies. The green-light category of subsidies is new to the Subsidies Code.[4] These subsidies are nonactionable in almost all cases, meaning that countries are free to impose them without being retaliated against and that countervailing duties cannot be imposed against them.[5] The old code did not explicitly spell out any subsidies as being carte blanche nonactionable. Under the new code, the following subsidies are nonactionable:

- Nonspecific subsidies;
- Assistance for research--up to 75 percent of the cost of industrial research and 50 percent of the cost of precompetitive development activity, subject to certain limitations, where precompetitive development activity refers to development from the stage at which research brings results through the creation of a first prototype not capable of commercial use;
- Assistance to disadvantaged regions that is otherwise nonspecific, subject to certain restrictions; and
- Assistance for adapting facilities to new environmental requirements, subject to certain restrictions.

The United States already exempts nonspecific subsidies from countervailing duties. The other subsidies in this category may require a change in U.S. policy. The extent to which research subsidies belong in this group has been a matter of some dispute. Most people agree that basic research is a legitimate activity for governments to subsidize. The question is when research stops being basic research and starts being applied product research, which many people believe should not be subsidized.

Yellow-Light Subsidies. All other specific subsidies except those for agriculture fall into the yellow-light category.[6] Agricultural subsidies are covered by the Agreement on Agriculture and will not be discussed in this study. Other GATT members can take action against yellow-light subsidies in accord with other provisions of the code (described below) only if the subsidies cause one or more of the following: injury to a domestic industry of the member taking action, nullification of benefits of the member under the GATT, and serious prejudice to the interests of the member. Those stipulations are the same as in the old Subsidies Code, but the new code contains new provisions relating to what constitutes serious prejudice.

Serious Prejudice. Under Article 6 of the new code, serious prejudice is presumed to exist in any of the following cases: ad valorem subsidization exceeding 5 percent;[7] subsidies to cover operating losses of an industry; subsidies to cover operating losses of an enterprise other than one-time measures to give the firm time to adjust; and direct forgiveness of debt and grants to cover debt repayment.

The subsidizing member can rebut that presumption by demonstrating that none of the following trade effects apply to the subsidy:

- It displaces or impedes imports by the subsidizing country;
- It displaces exports of another member from a third country;
- It causes significant price undercutting compared with another member or lost sales by another member in the same market; and
- It increases world market share of the subsidizing member in a subsidized primary product or commodity.

A contingency does, however, come into play--namely, that certain conditions that could cause the above effects but have nothing to do with the subsidy do not apply. Those conditions are listed in the code.

If the four cases in Article 6 do not apply, then serious prejudice *may* still exist if the complaining member satisfactorily demonstrates one or more of the trade effects listed above. In effect, if at least one of the four cases holds, the burden of proof is on the subsidizing

4. Article 8 of the Subsidies Code.

5. As a safeguard, remedies are allowed in certain restricted circumstances as described in the subsection on Remedies, Consultation, and Dispute Settlement Relating to Subsidies.

6. Article 5 of the Subsidies Code.

7. The code stipulates that this case is not to apply to civil aircraft, which are to be covered by a separate agreement yet to be negotiated.

country to show that none of the four trade effects apply. If none of the four cases hold, the burden of proof is on the complaining country with regard to the trade effects.

Provisional Application. Under Article 31 of the Subsidies Code, the green-light subsidy provisions and the four factors giving a presumption of serious prejudice apply for five years. The Committee on Subsidies and Countervailing Measures must review the operation of the provisions over that period to determine whether to extend them for a further period, either in their present form or in modified form.

Remedies, Consultation, and Dispute Settlement Relating to Subsidies

Under the old Subsidies Code as well as other parts of the GATT, decisions to take action against unfair trade practices involved lengthy procedures for settling disputes and required consensus, which meant that the country committing the unfair practice could block action. The difficulty of meeting that requirement is a large part of the reason that the United States has relied so much on countervailing duties rather than consultating and settling disputes by consensus.

The new Subsidies Code (as well as other parts of the Uruguay Round agreements) changes that. It shortens the dispute settlement process, and it changes the decision rule in most cases from one in which no action is taken without a consensus to one in which action is taken barring a consensus not to take action. It makes Articles XXII and XXIII of the GATT, as elaborated and applied by the Understanding on Rules and Procedures Governing the Settlement of Disputes, applicable to subsidy and countervailing-duty disputes except as otherwise specifically provided in the code.[8] The major exceptions, specifically provided, follow.

Red-Light Subsidies. When a member thinks another is granting a prohibited subsidy, it can request consultations with the member. If no mutually acceptable solution is reached in 30 days, either party may refer the matter to the Dispute Settlement Body (DSB) to establish a panel immediately unless the DSB decides by consensus not to do so.[9]

Under the old Subsidies Code, after 30 days of consultation, the dispute went to the Committee on Subsidies and Countervailing Measures rather than the DSB. The committee would attempt to mediate conciliation between the parties. If conciliation did not solve the matter after 30 days, the committee would appoint a panel. The new code eliminates this 30-day period of conciliation and goes directly to the appointment of a panel. The decision to appoint a panel under the old code had to be made by consensus, but it has been the practice not to deny a complaining country access to a panel.

Under the new code, the panel may request assistance from the Permanent Group of Experts (PGE), which is a new group provided for in the new code. The PGE decides whether the subsidy is prohibited, and the panel must accept its conclusion. The panel must also issue a report with its finding within 90 days of its establishment. If the finding is that the subsidy is prohibited, the panel report must recommend dates by which the subsidy should be withdrawn. The Dispute Settlement Body must adopt the report within 30 days unless it is appealed or the DSB decides by consensus not to adopt it. If it is appealed, the Appellate Body must issue a decision within 30 days, and the DSB must adopt the decision barring a consensus not to do so.

Under the old code, the committee could decide to adopt a panel finding only by consensus--the opposite of the new procedure under which the report is adopted barring a consensus not to adopt it. As a result, the subsidizing country could block the adoption, which is not possible under the new code. Also, the previous code contained no provision for appeal.

If a country ignores a panel report adopted by the DSB under the new code and refuses to withdraw the subsidies in question, the DSB must grant authorization for appropriate countermeasures unless it decides by consensus not to. Parties can request arbitration under the Understanding on Rules and Procedures Governing Settlement of Disputes to determine the appropriate-

8. Article 30 of the Subsidies Code.

9. Article 4 of the Subsidies Code. (The establishment of the Permanent Group of Experts is provided for in Article 24, paragraphs 3-4 of the Subsidies Code.)

ness of countermeasures. Under the old code, a decision by the committee to grant authorization for countermeasures required consensus, which meant that the subsidizing country could block it. There was no provision for arbitration beyond the deliberations of the committee.

Yellow-Light Subsidies. Under Article 7 of the Subsidies Code, if a member believes a subsidy by another member causes injury to its domestic industry, nullification or impairment, or serious prejudice, it may request consultations. If no mutually acceptable solution is found within 60 days, the procedure for settling the dispute is essentially identical to that for red-light subsidies.

The differences between this remedy process and the process in the old code are analogous to the differences in the case of red-light subsidies. First, the DSB handles disputes rather than the committee. Second, the old code had a 60-day period of conciliation mediated by the committee after the 60 days of consultation and before any settlement of the dispute by the committee. In contrast, the new code skips conciliation and goes directly to settlement of the dispute. Third, at each step along the way where a decision by the DSB is required, action against subsidies is taken under the new code unless the DSB decides by consensus not to act, whereas under the old code the committee could not take action without consensus. Thus, the subsidizing country could block action under the old code but cannot under the new code. Finally, the new code includes provisions for appeal and arbitration about the appropriateness of countermeasures, whereas the old code did not.

Green-Light Subsidies. Under Article 9 of the Subsidies Code, although green-light subsidies are generally nonactionable, a safeguard provision does exist. If a member thinks one or more of its domestic industries has suffered severe adverse effects as a result of such a subsidy, it may request consultations with the subsidizing member. If no mutually acceptable solution is reached within 60 days, the requesting member may refer the matter to the Committee on Subsidies and Countervailing Measures. If the committee determines that the harmful effects do exist, it may recommend a modification of the subsidy program. It must, though, present its conclusions within 120 days of the referral. If the recommendation is not followed within six months, it must authorize appropriate countermeasures.

Unlike the case for red-light and yellow-light subsidies, in which action against subsidies is taken unless the committee decides by consensus not to, the converse is true for green-light subsidies: the committee does not take action unless it decides by consensus to do so. Hence, the subsidizing country could block action if it so desired.

Consultation and Dispute Settlement Relating to Dumping

Like the new Subsidies Code, the new Antidumping Code makes the Understanding on Rules and Procedures Governing the Settlement of Disputes applicable to disputes under the code except as otherwise provided.[10] Disputes are referred to the Dispute Settlement Body rather than to the Committee on Antidumping Practices as they are under the old code. The DSB does the same thing that the committee did under the old code except that the three-month period of conciliation is eliminated. Settlement goes immediately to the appointment of a panel by the DSB to settle the matter. The DSB must accept the findings of the panel barring a decision by consensus not to accept it, so an offending country cannot block action as it could under the old code.

The U.S. government has been unhappy with the propensity for dispute panels to overturn the findings and rulings of the Department of Commerce and the International Trade Commission on dumping cases. Until now, the United States could block the adoption of such panel reports if it was sufficiently unhappy with them. With the new code, it will not be able to do so. Because of concern over this fact, the United States insisted on including the following restrictions on when the panels can overturn the decisions of national authorities:

(i) If the establishment of the facts [by the national authorities] was proper and the evaluation was unbiased and objective,

10. Article 17 of the Antidumping Code.

even though the panel might have reached a different conclusion, the evaluation shall not be overturned; and

(ii) Where the panel finds that a relevant provision of the Agreement admits of more than one permissible interpretation [in accordance with customary rules of interpretation of public international law], the panel shall find the authorities' measure to be in conformity with the Agreement if it rests upon one of those permissible interpretations.[11]

On the one hand, previous chapters of this study have demonstrated a rather pronounced bias in U.S. antidumping procedures. On the other hand, the main GATT agreement and the GATT Antidumping Code allow many of the biased procedures. Thus, it is not clear how much protection these provisions will provide for the decisions of the relevant U.S. authorities.

The possibility that a panel may someday overrule U.S. authorities in an antidumping or countervailing-duty finding brings up another issue that the Congress must consider. Such a ruling would mean one of two things: the United States would have to eliminate or change the duty imposed in the case at issue, or the complaining country would be authorized to retaliate against the United States. Thus, the Congress must consider whether it wants to grant blanket authority--perhaps with some restrictions--to the Department of Commerce and the International Trade Commission to change rulings and policies as required by DSB rulings, or whether it would prefer to decide on its own whether to change policy or allow retaliation to occur in each case as it arises.

Determination of Dumping

The new Antidumping Code has several changes that will affect U.S. methodology in calculating dumping margins.[12]

Individual to Weighted-Average Price Comparisons. Under the new code, DOC will have to compare the weighted-average import price over the period of investigation with the weighted-average home-market price of the foreign exporter over the same period, or compare individual import prices with individual home-market prices of the foreign exporter.[13]

The current U.S. practice in antidumping investigations of comparing individual import prices with the average home-market price of the foreign exporter over the six-month period of investigation will not be allowed unless the authorities find a pattern of price differences among different purchasers, regions, or time periods (such as targeting or rifle-shot dumping), and explanation is provided.

That change will eliminate a bias in current U.S. methodology that increases the likelihood of affirmative determinations of dumping and inflates dumping margins. The provision requiring the change mentions only investigations and not administrative reviews. Hence, the new code would appear to allow the current U.S. policy for administrative reviews to continue. That policy is to compare individual import sales with average foreign home-market sales on a monthly basis (rather than a six-month investigation period). Some people have argued, however, that a later provision of the code makes the change applicable to administrative reviews as well.[14] Such an interpretation would require changing the U.S. policy in administrative reviews, thereby eliminating another bias in U.S. procedure.

Administrative Selling Costs and Profits. The new code requires that profits and administrative selling and other costs that are used in computing constructed values be based on actual data on production and sales in the ordinary course of trade. If that is not possible, the code gives three alternatives and stipulates that the amount used for profit cannot exceed the profit normally realized by other exporters and producers of the product.[15]

The new provision will require the United States to eliminate the statutory minima for administrative over-

11. Article 17, paragraphs 17.6 (i) and (ii) of the Antidumping Code.

12. Article 2 of the Antidumping Code.

13. Article 2, paragraph 4.2 of the Antidumping Code.

14. The provision in question is Article 18, paragraph 3.

15. Article 2, paragraph 2.2 of the Antidumping Code.

head and profits. In line with those statutory minima, DOC normally uses the administrative overhead and profit from the firm's financial statement unless they are less than 10 percent and 8 percent, respectively; if they are less than those figures, DOC uses 10 percent and 8 percent. Eliminating the 10 percent and 8 percent minima will decrease the constructed value whenever the minima would have kicked in.

In the opposite direction, the new code requires the use of data on the ordinary course of trade. The code in many situations allows sales below cost to be considered not in the ordinary course of trade. Thus, one would expect the profit calculated from such data to be higher than the profit on the financial statement, which includes all sales whether above or below cost.

Overall, the effects of this provision of the new code will be mixed: it will decrease calculated dumping margins in some situations and increase them in others.

Disregarding Sales Below Cost. The new code for the first time explicitly allows the U.S. policy of disregarding sales below cost when computing the average home-market price of the exporter.[16] The conditions under which it allows such disregard, however, are somewhat different from those in U.S. law, and probably more stringent overall. The new code allows disregard only if the sales "are made within an extended period of time in substantial quantities and are at prices which do not provide for the recovery of all costs within a reasonable period of time," where:

- "Extended period of time" is normally one year, but in no case less than six months;

- "Substantial quantities" means that the weighted-average price is less than weighted-average cost or that the volume of below-cost sales is at least 20 percent of sales under consideration; and

- Prices that are above the weighted-average cost for the period of investigation must be considered to provide for costs to be recovered within a reasonable period of time. Adjustments must be made for startup costs or other one-time costs during the investigation period that are not otherwise accounted for by the ordinary capitalization and depreciation of the firm's accounting statement, and the adjustment for startup costs must "reflect the costs at the end of the startup period."

Current U.S. law stipulates that sales below cost be disregarded if they are "made over an extended period of time and in substantial quantities." To carry out the law, DOC performs a two-part test. It determines if below-cost sales occurred in three of the six months covered by the investigation, and if the below-cost sales represent more than 10 percent of the sales volume during the six months.

Thus, on the one hand, the new code will increase the period of investigation from six months to one year and raise the percentage of sales in the investigation period that are below cost from 10 percent to 20 percent. As a result of both of these stipulations, sales below cost are less likely to be disregarded. On the other hand, if these conditions are met, the new code would allow below-cost sales to be disregarded if they were concentrated in one of the 12 months under investigation rather than distributed over three of the months as with current U.S. policy. That provision would make disregard of sales more likely.

The third condition above could be open to several interpretations. As DOC interprets it, costs during a suitably defined startup period would be ignored, and if the weighted-average price is higher than the weighted-average cost after that startup period, below-cost sales could not be disregarded. Current U.S. policy is to distribute high startup cost over a suitably long period. In theory, the current U.S. policy makes more sense than the new code as interpreted by DOC, although some analysts have argued that DOC distributes costs over periods that are too short and thereby leads to findings that sales are below cost when they in fact are not.

Assuming that DOC's interpretation is correct, the question remains as to what the length of the startup period should be. Too short a period would lead to findings that sales are below cost when they actually are not, and too long a period would lead to findings that sales are not below cost when they actually are. Leaving this issue aside, the changes required by the new code are likely, though not certain, to reduce the frequency with which below-cost sales are disregarded. Even if they do, however, the changes will not even

16. Article 2, paragraph 2.1 of the Antidumping Code.

come close to eliminating the problems with this procedure.

Cost Calculations Based on Records of Exporter. The new Antidumping Code requires that costs "normally be calculated on the basis of records kept by the exporter or producer under investigation, provided that such records are in accordance with the generally accepted accounting principles of the exporting country and reasonably reflect the costs. . . ."[17] In theory, that statement represents DOC's current policy, so the provision should have no effect on U.S. policy. In practice, disputes between DOC and the investigated firms as to whether various details in the records reasonably reflect costs are common. Undoubtedly, those disputes are the reason for this provision. Presumably the provision would enable a firm that is sufficiently unhappy with a DOC decision in this regard to appeal it through the new dispute settlement process to have it overturned. Thus, the significance of the provision depends on the fairness of DOC's decisions, on which the Congressional Budget Office has no basis to judge.

Determination of Subsidies: A Benefit to Recipient Standard

The new Subsidies Code specifies that the rate of subsidy in countervailing-duty cases be calculated on the basis of the benefit the subsidy provides to the recipient rather than on its cost to the government.[18] That stipulation reflects the professed U.S. view that subsidies are objectionable primarily because they distort the workings of the market--not because they cost governments money.

Cost, however, may indeed be a major reason (perhaps even *the* major reason) U.S. policymakers object to subsidies. Certainly subsidies in most cases reduce the efficiency and output of the world economy. The effect on the economy of the importing country, however, is not the same as the effect on the world economy. Countries generally benefit from the distortions caused by foreign subsidies of their imports. Such subsidies lead to political pressures from competing domestic industries for assistance, however, and the assistance that is least detrimental economically (though still detrimental) to the importing country is its own countersubsidies. Current pressures for balancing the budget make such countersubsidies difficult for the U.S. government to provide. Thus, the cost of a subsidy is an important consideration for U.S. policymakers.

In the past, other countries have complained about cases in which DOC changed its methods of calculating subsidies for a given case, resulting in the finding of a subsidy when the previous method used by DOC would not have. Therefore, the new Subsidies Code specifies that the method a country uses to calculate the benefit of a subsidy must be provided for in the country's legislation or regulations, and its applications to individual cases must be transparent. The code also specifies that:

- Government provision of equity capital does not confer a benefit unless it is inconsistent with the practice of private investors;

- Government loans do not provide a benefit unless the amount the firm must pay on the loan differs from that for commercial loans;

- A loan guarantee provides a benefit only if it results in the firm paying less than it would on a comparable loan without the guarantee; and

- Providing or purchasing goods and services does not confer a benefit unless they are provided without adequate remuneration demanded of the firm or purchased at higher than market prices.

Of these four requirements, only the last is inconsistent with current U.S. policy. Under current U.S. policy, the price at which a good or service is provided (or at which the government purchases the good or service) is compared with the price charged to (or paid to) other firms, not with the price required for adequate remuneration (or the market price).

17. Article 2, paragraph 2.1.1 of the Antidumping Code.

18. Article 14 of the Subsidies Code.

Determining Injury

Several new provisions in the codes relate to determining injury in AD/CVD investigations.[19]

Cumulation of Imports. The old codes make no mention of cumulating imports--that is, adding together all dumped or subsidized imports from all countries when determining injury. The new codes for the first time explicitly allow it when:

- The margin of dumping or subsidy in each country is not *de minimis* and the volume of imports from each country is not negligible, and

- "[C]umulative assessment of the effects of the imports is appropriate in light of the conditions of competition between imported products and the conditions of competition between the imported products and the like domestic products."[20]

In and of itself, the first of these conditions would have little or no effect on U.S. policy. U.S. law does not require cumulation when imports are negligible, and cases with *de minimis* dumping or subsidy margins do not reach the ITC for final determination of injury because they fail DOC's dumping or subsidy determination. As will be discussed shortly, however, the new codes set new *de minimis* margins and levels of negligibility.

The significance of the second condition is unclear, since no standard is given for determining what is appropriate. From the standpoint of the economic well-being of the country as a whole, the only condition of competition for which cumulative assessment would be appropriate would be *lack* of competition among imports--that is, one firm supplies the imports from all countries or there is collusion among the suppliers. Only under such lack of competition could predatory pricing occur. Since that interpretation of the provision is directly contrary to U.S. law (which calls for cumulation when the imports compete with one another and with U.S. production) and the United States has not objected or paid much attention to it, that is probably not the meaning intended. The meaning that *is* intended is unclear.

The Antidumping Code allows cumulating imports from all countries subject to antidumping investigations for the product, and the Subsidies Code allows cumulating imports from all countries subject to countervailing-duty investigations for a product. Neither code allows the current U.S. practice of cross-cumulation--that is, cumulation of imports from all countries subject to either antidumping or countervailing-duty investigations.

***De Minimis* Margins and Negligible Imports.**[21] Current U.S. policy considers dumping and subsidy margins of 0.5 percent or less to be *de minimis*. The new codes raise the level for dumping to 2 percent and the level for subsidies to 1 percent for developed countries. For developing countries, the *de minimis* level of subsidies is 2 percent. For developing countries that eliminate export subsidies before the eight-year limit imposed on them, the *de minimis* level is 3 percent. Clearly, the U.S. *de minimis* standards will have to be changed, resulting in fewer positive determinations of dumping and subsidies. The new standards remain quite low, however.

The United States has no fixed level of imports that it considers negligible; rather, it determines negligibility of imports by their effects. Under the new Antidumping Code, imports from a particular country are negligible if both of the following are true: the imports are less than 3 percent of total imports of the same product from all countries, and the imports from all countries that each supply less than 3 percent total up to no more than 7 percent of all imports of the same product. The new Subsidies Code does not stipulate any fixed level of negligibility for developed countries. For developing countries, it stipulates that imports are negligible if both of the following are true: the imports represent less than 4 percent of total imports of similar products from all countries, and the imports from all countries that each supply less than 4 percent total up to no more than 9 percent of all imports of similar product.

19. Article 3 of the Antidumping Code and Article 15 of the Subsidies Code.

20. Article 3, paragraph 3 of the Antidumping Code, and Article 15, paragraph 3 of the Subsidies Code.

21. Article 5, paragraph 8 of the Antidumping Code, and Article 11, paragraph 9, and Article 27, paragraphs 9-10 of the Subsidies Code.

The effect of the required changes in U.S. negligibility standards depends on the changes that the United States chooses to make. The codes stipulate that imports below the indicated levels must be considered negligible, but they do not require that imports above the indicated levels be considered nonnegligible. If the United States keeps its current standard except for cases in which import levels are below the negligibility levels set in the new codes, the effect will be fewer findings of injury, although the effect should be small.

If, however, the United States scraps its old standard and replaces it with one in which imports below the new levels are considered negligible and imports above the new levels are considered nonnegligible, findings of injury might increase. The new levels in the codes are indeed trivial. They constitute small percentages of total imports, which in turn might be a small percentage of the U.S. market for the product in question. Thus, the current U.S. standard might find levels of imports above the current negligibility limits under the new codes to be negligible. Predatory pricing would require much higher levels--imports from one firm (no cumulation among countries and firms) equal to perhaps 70 percent or 80 percent not just of total U.S. imports but of the entire U.S. market.

Factors That Must Be Considered in Determining Injury. The new Antidumping Code adds the margin of dumping to the list of factors that must be considered in determining injury.[22] Under current U.S. law, the ITC has discretion about whether to consider the dumping margin. Some commissioners consider it; others do not. Presumably, considering the margin would reduce the likelihood of finding injury in cases in which imports clearly injured an industry but the margin of dumping was very small. In such cases, a commissioner could conclude that the dumping is having little effect on either prices or the level of imports and therefore is not responsible for the injury.

Initiating Investigations

AD/CVD investigations are very expensive for the firms under investigation even if they end up with negative dumping, subsidy, or injury determinations. Consequently, the new codes have several provisions to make sure that investigations are not started without adequate justification and support.[23] Each code devotes a half page to discussing the evidence that AD/CVD authorities must require in applications for relief by domestic industries, and they require the authorities to check the accuracy and adequacy of the evidence. The old codes had merely stated that applications should include sufficient evidence of dumping or subsidy, injury, and a causal link between them. The new codes also require authorities to verify that an application for initiation is supported by at least 50 percent of the industry (as measured by production) that expresses an opinion and at least 25 percent of the total industry (as measured by production).

Under current U.S. policy, DOC assumes that an application for relief by some firms in an industry is supported by the rest of the firms unless they say otherwise. Requiring DOC to actually verify the industry support and check the accuracy of the evidence supplied with the application may mean that DOC will be unable to initiate investigations within the 20-day time limit set by U.S. law.

"Best Information Available" and the Difficulty of Fulfilling Demands for Information

The new codes have several provisions relating to the difficulty investigated firms have providing the information requested by AD/CVD administrative authorities and the use of "best information available" against such firms when they are not sufficiently forthcoming with information.[24]

Both new codes go into greater detail than the old codes about the requirement that exporters accused of dumping and their governments be informed and given a chance to provide all the evidence they consider relevant. They require that firms be given at least 30 days to reply to questionnaires and that requests for exten-

22. Article 3, paragraph 4 of the Antidumping Code.

23. Article 5, paragraphs 2-4 of the Antidumping Code, and Article 11, paragraphs 2-4 of the Subsidies Code.

24. Article 6, paragraphs 1, 1.1-1.3, 8, and 13 of the Antidumping Code, and Article 12, paragraphs 1, 1.1-1.3, and 11 of the Subsidies Code.

sions be given due consideration. They further require that "authorities . . . take due account of any difficulties experienced by interested parties, in particular small companies, in supplying information requested and provide any assistance practicable."

Under current U.S. policy, foreign firms are given two weeks to respond to an initial questionnaire asking for basic general information and 30 days to respond to a questionnaire asking for more detailed information. Clearly, the two-week deadline is inconsistent with the new codes. DOC believes that it is generous with extensions, but in fact it has only limited flexibility on deadlines and extensions, since it operates under the constraint of tight deadlines for decisions imposed by law. Current law requires DOC and the ITC to provide assistance to domestic firms filing petitions for relief under the AD/CVD laws, but it has no similar requirement for assistance to foreign firms being investigated. The new codes require some assistance, but how much and of what kind is not clear.

The new Antidumping Code (but not the new Subsidies Code) contains an annex with a detailed list of restrictions related to questionnaires and use of BIA. Some of the restrictions are as follows:

- Authorities should ensure that investigated firms know that BIA can be used if they do not supply information in a reasonable time and that BIA can include information contained in the application for relief made by the domestic industry.

- Authorities should not: (1) request a company to use a computer system for its response other than that used by the firm, (2) maintain a request for a computerized response if the interested party does not maintain computerized accounts and if presenting the response as requested would result in an unreasonable extra burden on the interested party, and (3) maintain a request for a response in a particular medium or computer language if the interested party does not maintain its computerized accounts in such medium or computer language and if presenting the response as requested would result in an unreasonable extra burden on the interested party.

- In their determinations, authorities should take into account all information that is verifiable and appropriately submitted.

- Even if submitted information is not ideal in all respects, it should not be disregarded if the party has acted to the best of its ability.

- Parties should be informed when their information is not accepted and given an opportunity, if possible, to provide further explanations.

In the past, critics of AD/CVD policy in the United States have complained about the difficulty of meeting DOC deadlines for responding to questionnaires, the requirement that information be provided in particular computer formats when foreign firms do not maintain computer records, and DOC's propensity to disregard information provided for various reasons.

Sampling and Other Cases in Which Duties Are Imposed on Firms Not Investigated

Until now, the Antidumping Code has not mentioned sampling, but the United States and other countries do use it. Strictly speaking, the normal U.S. practice is to examine a sufficient number of the largest suppliers to account for 60 percent of the imports in question. Regardless of whether that meets the definition of sampling, it may be affected by provisions in the new code.

The new Antidumping Code (but not the new Subsidies Code) for the first time allows sampling, but it does so only in cases where the number of firms to be investigated is so large as to make individual determinations for all firms impracticable.[25] In other cases, all firms must be investigated individually. That stipulation may require the United States to use the 60 percent rule less often than is currently the practice. When sampling is used, the new code requires that:

25. Article 6, paragraphs 10 and 10.1-10.2 of the Antidumping Code. The reason the Subsidies Code does not contain such a provision may be that the United States, which is the largest user of countervailing duties, does not often use sampling in subsidy cases. In CVD cases with many firms, DOC typically calculates an aggregate countrywide rate rather than rates for individual firms.

- o The sample chosen be statistically valid or be the largest volume of exports that can be investigated;
- o The selection preferably be chosen in consultation with and with the consent of the exporters, producers, and importers concerned; and
- o If possible, any firm that submits the necessary data in a timely fashion receive an individual margin even if not chosen for the sample.

As to the third requirement, DOC now does not absolutely refuse requests for individual rates made by countries not chosen for the sample (or for the 60 percent rule), but it tries to discourage countries from making such requests. Thus, this requirement might have some effect.

When sampling is used, the new code places limits on the antidumping duties that may be applied to imports from firms not included in the sample.[26] Of interest to the United States, the code mandates that any such duty shall not exceed the weighted-average margin of dumping of firms examined. Moreover, any zero and *de minimis* margins and any margins calculated on the basis of BIA must be disregarded in calculating the weighted average.

Current U.S. policy is to apply duties equal to the weighted-average margin. Zero and *de minimis* margins are disregarded but margins calculated on the basis of BIA are included. Excluding the zero and *de minimis* margins biases the calculated margin upward. Including margins based on BIA also biases margins upward and penalizes uninvestigated firms for the failure of other firms to comply with information requests. Thus, this provision of the new Antidumping Code would require eliminating part of the bias in current U.S. methodology but not all of it, and would thereby result in lower antidumping duties being applied to firms not investigated.

Both the new Antidumping Code and the new Subsidies Code require expedited reviews for exporters that did not supply exports during the period of investigation.[27] The new Antidumping Code (but not the new Subsidies Code) prohibits imposing antidumping duties while the review is carried out, but it allows retroactive assessment if the determination is positive. That prohibition would affect U.S. policy. Current policy requires a deposit of duties on imports from such firms that is equal to the margin estimated for the countries investigated until the normal administrative review (or the date of the first opportunity for someone to request such a review).

Suspension Agreements

The codes have several new provisions relating to suspension agreements (referred to in the codes as "undertakings").[28] Of interest to the United States is a provision stating that general policy concerns are legitimate reasons for not accepting such agreements.[29] U.S. law provides for suspension agreements, and the statistics indicate that the United States has made substantial use of them (see Chapter 5). DOC claims, however, that normal U.S. policy is not to accept such agreements and that the statistics are distorted by the large number of steel import cases, for which exceptions were made. Thus, this provision makes clear that the new code allows the "normal" U.S. policy.

Sunset Provisions for Antidumping and Countervailing Duties and Suspension Agreements

The new Antidumping and Subsidies Codes require terminating antidumping and countervailing duties not later than five years from imposition, or five years from the date of the most recent review covering both dumping or subsidy (whichever is applicable) and injury.[30] An exception is made if a review determines that such termination would be likely to lead to continuation or recurrence of the dumping or subsidy and consequent injury. The codes also set the same requirement for

26. Article 9, paragraph 4 of the Antidumping Code.

27. Article 9, paragraph 5 of the Antidumping Code, and Article 19, paragraph 3 of the Subsidies Code.

28. Article 8 of the Antidumping Code, and Article 18 of the Subsidies Code.

29. Article 8, paragraph 3 of the Antidumping Code, and Article 18, paragraph 3 of the Subsidies Code.

30. Article 11 of the Antidumping Code and Article 21 of the Subsidies Code.

terminating price undertakings negotiated instead of antidumping and countervailing duties.

The sunset provision will require changes in U.S. law and policy. Under current U.S. policy, a foreign exporter has difficulty getting an AD/CVD order terminated. (See Appendix B for a discussion of how AD/CVD orders can be terminated.) As a result, orders often remain in place for long periods of time. Some outstanding antidumping orders have been in effect for more than 25 years, and some countervailing duty orders have been in effect more than 15 years. The sunset provisions of the new codes should result in terminating a number of outstanding orders.

Transparency and Judicial Review

As other countries have begun to follow the U.S. lead in using AD/CVD laws to protect their industries, U.S. exporters have begun to feel the effects of those policies. In many countries, the administration of such laws is not as open as it is in the United States, leaving U.S. firms in the dark regarding the basis for decisions against them. Further, U.S. firms view the opportunities for appeal of such decisions in many countries as inadequate.

To answer those problems, the new codes greatly expand requirements that administrative authorities give public notice of, or inform interested parties of, such things as initiations of investigations, firms and countries involved, preliminary and final determinations, the data on which such determinations are made, and various other important aspects of antidumping and countervailing-duty cases.[31] They also require that countries provide for judicial, arbitral, or administrative tribunals, independent of the administrative authorities, to review AD/CVD administrative actions.[32]

31. Article 6, paragraph 9, and Article 12 of the Antidumping Code, and Article 12, paragraph 8, and Article 22 of the Subsidies Code.

32. Article 13 of the Antidumping Code and Article 23 of the Subsidies Code.

Subsidies in Developing Countries and Formerly Communist Countries

The current Subsidies Code treats the subsidy programs of developing countries more leniently than those of other countries, placing greater restrictions on countermeasures against them than is the case for the subsidy programs of other countries.[33] It states that developing countries *should endeavor* to phase out export subsidies (the current code's red-light subsidies) and protects them from countermeasures if the developing country is committed to such a phaseout, but the code does not *require* such a phaseout. Further, it makes no mention of phasing out yellow-light subsidies.

The new code provides similar restrictions on countermeasures against the subsidy programs of developing countries. Rather than state that developing countries should endeavor to phase out such programs, however, it stipulates rigorous phaseout requirements. Thus, many subsidy programs in developing countries will with time either be eliminated or become subject to U.S. countervailing duties or other countermeasures in line with the provisions of the code for subsidy programs of other countries.

As discussed above, the new code requires larger *de minimis* values for subsidies by developing countries and larger negligible values for subsidized imports from developing countries. It also makes exceptions for certain temporary subsidies connected with privatization programs, and it provides for a seven-year period for countries in transition from centrally planned economies to market economies, during which time many subsidies are not actionable and subsidies must be phased out or brought into conformity with the code.

Transition to the New Antidumping and Subsidies Codes

The new codes apply to all investigations and reviews of existing measures initiated in response to applications made after the codes enter into force.[34] Subsidy

33. Articles 27 and 29 of the Subsidies Code.

34. Article 18 of the Antidumping Code and Articles 28 and 32 of the Subsidies Code.

programs existing before a country signed the Agreement Establishing the World Trade Organization (WTO) and inconsistent with the provisions of the Subsidies Code must be brought into conformity with the Subsidies Code within three years of entry into force of the WTO agreement for the country. Until then, the program is not subject to the provisions of the Subsidies Code or to red-light subsidies.

The Status of Legislation

Because they are typically granted so-called "fast track" status, trade bills usually follow different procedures from other legislation. As this study goes to press, the House and Senate Committees with jurisdiction over the GATT are working to reconcile different versions of the bill needed to implement the trade agreement. After those differences are reconciled, the Administration will submit legislation for a Congressional vote. Under fast-track procedures, the Congress must vote on the bill within a prescribed time limit and the bill cannot be amended.

The House and Senate versions of the bill, with respect to changing antidumping and countervailing-duty laws, differ on numerous points. Those points include the method for determining appropriate export prices, the treatment of countries in transition from centrally planned economies to market-based economies, and rules to prevent the circumvention of duties. Neither version, however, significantly changes the overall stance of U.S. law. In general, the different versions of the bill either codify or revise the procedures already in use by the Department of Commerce or the International Trade Commission, or put into law those agreements reached in the Uruguay Round negotiations. The underlying philosophy and operating procedures of the AD/CVD laws remain unchanged.

Appendixes

Appendix A

The Frequency of Occurrence of Predatory Pricing

Although economists do not completely agree as to exactly how frequently predatory pricing occurs, for the most part they agree that it is not very common. More important for this study, nearly all economists would agree that it is substantially less common than price discrimination and selling below cost and that, correspondingly, most price discrimination and selling below cost do not constitute predatory pricing. Chapter 2 mentions many of the nonpredatory reasons for price discrimination and selling below cost. This appendix discusses some of the conditions that must hold for predatory pricing to be possible and profitable.[1]

The Predator Initially Loses Money

In any predatory pricing war, both the predator firm and the firms it drives (or attempts to drive) out of the market initially lose money. If the predation is successful, the predator can use its increased market power afterward to regain its losses and then some by raising its price above the previously prevailing level. The same increase in market power and price could be accomplished through merger, however, without the initial losses that a price war entails.[2] A purchase price could always be negotiated that would make both the would-be predator firm and its prey better off financially than they would be with a predatory pricing war. Therefore, in any country where the law does not prevent horizontal mergers that create monopolies, predatory pricing is unlikely because it is less profitable for both parties than a negotiated merger. In the United States, such horizontal mergers run contrary to the antitrust laws, but other factors make predatory pricing uncommon in countries that outlaw such mergers.

For predatory pricing to succeed, the predator firm must be larger than the firms it competes with and start off with most of the market. Otherwise, the predator would probably go broke before it could ever finish driving other firms from the market. Even if the predator did not go broke, it would take so long to drive the others out of the market that the predator would be unlikely to earn large enough profits afterward to recoup the initial losses.

The long length of time needed to drive out competitors makes recouping the losses difficult for two reasons. First, it increases the size of the losses. Second, it is not sufficient that the dollar amount of the monopoly's profits be at least equal to the initial losses; the present discounted value of the monopoly profits must also be at least equal to the present discounted value of the initial losses. The further into the future the monopoly's profits are to accrue, the smaller is their present discounted value. Hence, the present discounted value of the profits is unlikely to be larger than the present discounted value of the initial losses from the price war.

For readers unfamiliar with the concept of present discounted value, the problem can be explained as follows. As an alternative to engaging in predatory pricing, the firm could take the money it would lose in the initial price war and invest it in bonds. A year later, the firm would have an amount equal to the investment (which is equal to the initial loss in the predatory pric-

1. This appendix is based on discussions in Robert H. Bork, *The Antitrust Paradox: A Policy at War with Itself* (New York: Basic Books, 1978), pp. 149-153; Louis Phlips, *Predatory Pricing* (Luxembourg: Commission of the European Communities, 1987), pp. 1-37; and Janusz Ordover and Garth Saloner, "Predation, Monopolization, and Antitrust," in Richard Schmalensee and Robert D. Willig, eds., *Handbook of Industrial Organization*, vol. 1 (New York: Elsevier Science Publishing Company, 1989).

2. Although predatory pricing is unlikely in these cases, there are situations in which the dominant firm may find it profitable to lower prices for the purpose of "softening up" the firm it intends to purchase so that the purchase price will be lower.

ing scheme) plus interest. Thus, for a predatory pricing scheme in which the monopoly profits are one year down the road to make sense, the monopoly profits must be equal to at least the initial losses plus the interest that would be earned on bonds. Otherwise, investing the money in bonds would be better and more profitable than investing it in the initial losses of the predatory pricing scheme. The longer it takes before all other firms are driven out of the market and the monopoly profits start coming in, the more years of interest would have been earned on the bonds and so the higher the monopoly profits must be to make predatory pricing a rational choice over investing in bonds.

New Competitors Can Undercut Price Increases

Another requirement for the success of predatory pricing is the existence of barriers that make it difficult for new firms to enter the market after the predator has driven out all of its competitors. Otherwise, the predator could not raise its prices above the competitive level after the other firms had been driven out because new firms would enter the market and undercut the high prices. The barriers to entry must be substantial enough to enable the predator to earn sufficiently high profits to recoup the losses from the price war.

If Costs Are Known, Predation Can Be Thwarted

Even if these requirements are met, predatory pricing will not occur if the costs of relevant firms are known to everyone involved and each firm behaves in such a manner as to maximize its own profits. If the average cost of production of the predator firm is lower than that of the prey firm, predatory pricing will not occur. The predator firm can and will take over the market by charging a price high enough to make a profit but low enough that the "prey" firm will lose money. That is ordinary competition, not predatory pricing.

If the average cost of the predator firm is as high as or higher than that of the prey firm and if the prey firm and others know that to be the case, the prey firm will know that the cut in price by the predator must be a predatory pricing attempt and that higher prices will follow. Therefore, the prey will have just as much reason as the predator firm to continue the war to the end and receive the subsequent higher prices. If it does not have the resources to do so, it will borrow them. Thus, both firms will continue the war to the end, with the result that no monopoly is formed and no monopoly profits occur. Before the war started, however, the potential predator would realize that that would be the result, so it would not attempt predatory pricing in the first place.

A key element in this argument is that the prey firm is able to continue the war to the end, even if it needs to borrow the money to do so. That argument breaks down if the firm cannot borrow because the lenders are uncertain as to whether what is going on is a predatory pricing attempt or the "predator" firm actually having lower average costs. If it is the latter, the prey would ultimately lose the war and would be unable to repay the loan. Thus, if uncertainty exists, the lender might not be willing to lend money, in which case the winner of the price war would be determined by which firm had the "deepest pockets" relative to its losses in the war.

Many people believe that large firms have deep pockets that make them better able than small firms to survive a predatory pricing war. In fact, however, in most cases a would-be predator's resources are likely to be more strained than are the prey's resources.

For example, one may assume that a firm's resources are proportional to its size in terms of sales. Thus, if a predator firm starts out with 90 percent of the market and the prey firm has 10 percent, the predator firm will have approximately nine times the resources that the prey firm has to draw on in a price war. However, because a successful predator will grow larger (and its average cost of production be likely to increase) as its prey shrinks, the predator firm will most likely face losses that are more than nine times those of the prey firm during a predatory pricing war. As a result, it will most likely exhaust its resources before the smaller firm does.

The problem just described does not completely eliminate the possibility of predatory pricing. Cases may arise in which the prey firm is financially weak because of previous mismanagement or other reasons. In such cases, the ratio of the prey's resources to the predator's resources would be less than the ratio of the prey's normal sales to the predator's normal sales. Thus, it would be easier for the predator to succeed.

Furthermore, if the predator firm has sales in another market in addition to the one of the prey firm, and the prey firm cannot get access to this other market (say, because of trade barriers), the predator firm could lower its prices only in the market of the prey firm and not in the other one. That technique is called "local price cutting" and is an example of price discrimination (see Chapter 2). In such a case, the resources of the predator firm are likely to be roughly proportional to its total sales in the two markets together. At the same time, its losses in the predatory pricing war are likely to be proportional, or a little more than proportional, to its sales in the one market in which the pricing war takes place.

That strategy cannot work, however, unless barriers prevent the prey firm from entering the other market. If no such barriers exist, the prey firm can cease selling in the market of the price war and switch to the predator firm's other market, where prices are at their normal level. Thus, the predator firm would be forced to lower prices in both markets to succeed, thereby restoring its original disadvantage in terms of cost relative to resources.

Because U.S. antitrust laws prevent the predator firm from purchasing the prey firm, the predatory pricing battle must continue until the prey firm's physical capital is gone. The prey firm's going bankrupt is not sufficient. The airline industry discovered in the 1980s when several airlines went bankrupt that the airplanes, airport gates, landing slots, and sometimes the entire corporate organization below the upper management of the bankrupt airlines did not disappear but were instead purchased by new owners with better financing. As a result, the intense competition and low prices continued. Similarly, a predator firm may see the capital assets and organization of a prey firm that is driven bankrupt sold to a better-financed group in a distress sale, with the result that the predatory pricing battle and the ensuing losses continue.

Dissipation of assets and dispersal of the organization are most difficult and least likely in industries such as the airline industry in which the major capital assets are specific to the industry and cannot be used in others. In some industries, such as retailing, the major capital assets (buildings, for example) are not specific to the industry and can be sold, making it easier for a predator firm to drive the prey firm and its capital out of the industry. Such industries often have low barriers to entry, however, since a firm wishing to enter the industry can easily buy existing capital from firms in other industries. With low entry barriers, predatory pricing is unlikely to be profitable, even if it is easily accomplished, and thus it is unlikely to occur.

Uncertainty Can Lead to Successful Predation

Since the late 1970s, a number of journal articles have been published that use game theory to explore further the implications for predatory pricing of various kinds of information asymmetries--that is, where each actor possesses different information.[3] Those articles have demonstrated that predatory pricing can be a rational, profitable behavior in several situations. One is the situation discussed above in which the prey firm (or its sources of financing) lack knowledge about the predator firm's cost of production.

3. See, for example, J.P. Benoit, "Financially Constrained Entry into a Game with Incomplete Information," *Rand Journal of Economics*, vol. 15 (1984), pp. 490-499 (this article demonstrates that having "deep pockets" can deter entry by providing a credible threat of post-entry predatory pricing); D. Fudenberg and J. Tirole, "A 'Signal-Jamming' Theory of Predation," *Rand Journal of Economics*, vol. 17 (1986), pp. 366-376; D. Kreps and R. Wilson, "Reputation and Imperfect Information," *Journal of Economic Theory*, vol. 27 (1982), pp. 253-279; P. Milgrom and J. Roberts, "Predation, Reputation, and Entry Deterrence," *Journal of Economic Theory*, vol. 27 (1982), pp. 280-312; D. Kreps and others, "Rational Cooperation in the Finitely Repeated Prisoners' Dilemma," *Journal of Economic Theory*, vol. 27 (1982), pp. 245-252; D. Easley, R.T. Masson, and R.J. Reynolds, "Preying for Time," *Journal of Industrial Organization*, vol. 33 (1985), pp. 445-460; and G. Saloner, "Predation, Merger, and Incomplete Information," *Rand Journal of Economics*, vol. 18 (1987), pp. 165-186.

Table A-1.
Percentage of Private Antitrust Cases Alleging Various Illegal Practices

Practice	Primary Allegations	Combined Primary and Secondary Allegations
Refusal to Deal	12.0	25.4
Horizontal Price Fixing	15.7	21.3
Tying or Exclusive Dealing	9.6	21.1
Price Discrimination	5.0	16.4
Predatory Pricing	3.1	10.4
Vertical Price Fixing	3.5	10.3
Restraint of Trade	4.3	10.0
Dealer Termination	4.4	8.9
Monopoly or Monopolization	3.7	8.8
Conspiracy	3.0	5.9
Vertical Price Discrimination	1.7	5.8
Merger or Joint Venture	2.6	5.8
Asset or Patent Accumulation	2.5	5.6
Inducing Government Action	0.5	0.8
Other	8.6	8.9
No Information	25.2	13.4

SOURCE: S.C. Salop and L.J. White, "Private Antitrust Litigation: An Introduction and Framework" (paper presented at the Georgetown Conference on Private Antitrust and Litigation, Airlie House, Virginia, November 8-9, 1985; revised draft, January 1986).

NOTE: Percentages add to more than 100 percent because a complaint may have more than one allegation.

Another is a situation in which the prey firm does not know the dominant firm's motives. In particular, predatory pricing by a dominant firm can sometimes be rational (profitable) in cases in which the prey firm believes that the dominant firm may be irrationally predatory--that is, the prey firm believes that the dominant firm will engage in predatory pricing even if doing so is unprofitable. In some models, the probability that the prey firm assigns to the possibility of the dominant firm's being irrationally predatory does not have to be large in order for predatory pricing to be a rational strategy for the dominant firm.

The theoretical developments in the late 1970s and 1980s have shifted the views of economists somewhat in the direction of believing that predatory pricing is less rare than was thought in the mid- to late 1970s. Most economists would still argue, however, that it is not very common, and it is clearly much less common than price discrimination and selling below cost.

Studies of Predatory Pricing Show Its Infrequency

The frequency of predatory pricing is difficult to measure empirically. There have been some empirical studies, however. One study by Roland Koller examined 23 historical cases in which firms had been found to have engaged in predatory pricing.[4] He concluded that predatory pricing probably was attempted in only seven of the cases, that it succeeded somewhat in four of the cases, and that only three of the cases resulted in harmful effects on resource allocation.

4. Roland H. Koller III, "The Myth of Predatory Pricing: An Empirical Study," *Antitrust Law and Economics Review*, vol. 4 (1971), pp. 105-123.

S.C. Salop and L.J. White examined data on all of the private antitrust cases filed from 1973 through 1983 in the United States, of which there were 1,959.[5] They found that plaintiffs in only 10.4 percent of the cases listed predatory pricing as either a primary or secondary allegation, which ranked predatory pricing as the fifth most commonly complained about practice out of 14 (see Table A-1). Plaintiffs in only 3.1 percent of the cases listed it as the primary allegation, which made it the ninth most commonly complained about practice out of the 14.

5. S.C. Salop and L.J. White, "Private Antitrust Litigation: An Introduction and Framework" (paper presented at the Georgetown Conference on Private Antitrust and Litigation, Airlie House, Virginia, November 8-9, 1985; revised draft, January 1986).

Salop and White also found that predatory-pricing allegations as a percentage of all antitrust allegations declined substantially from 1979 through 1983. Their decline probably reflects the spread of the Areeda-Turner rule in the courts, by which a large firm must set prices below the average variable cost before there is a presumption of predatory pricing. Salop and White further found that plaintiffs in predatory-pricing cases less frequently received favorable judgments than the average for all plaintiffs in antitrust cases.

Many discussions of predatory pricing point to various famous cases in which substantial evidence of predatory intent exists. It is not possible to draw reliable conclusions about the frequency of predatory pricing from a few individual cases. To a large degree, the various discussions tend to point to the same famous cases. One would think that if predatory pricing was common, there would be many individual cases to discuss.

Appendix B

An Overview of Current U.S. Antidumping and Countervailing-Duty Procedures

To understand some of the disputed procedures discussed in Chapter 4, one needs an understanding of the overall process of investigation and assessment of duties in antidumping and countervailing-duty (AD/CVD) cases. This appendix provides an overview of the process.[1]

Antidumping Procedures

Antidumping duties are assessed retrospectively.[2] At any given time, firms importing goods under an antidumping order must pay a deposit equal to the dumping margin determined for previous imports of the good. Later, an administrative review will determine the actual amount by which the imports in question were dumped. If the deposit was larger than that amount, the excess is returned; if it was smaller, the importer must make up the difference. The Department of Commerce (DOC) determines dumping margins, and the International Trade Commission (ITC) makes determinations of injury. The overall procedure for investigating, settling, and reviewing antidumping cases and determinations involves a number of steps.

Initiation of Investigation

DOC may initiate investigations on its own (usually referred to as "self-initiated" investigations) or in response to a petition by the domestic industry.

Preliminary Determination of Injury by the ITC

Within 45 days of the petition or self-initiation date, the ITC must determine whether there is a reasonable indication of material injury to tne domestic industry. If there is not, the investigation is closed.

Preliminary Determination of Dumping by DOC

Within 160 days of the petition or self-initiation date, DOC must determine whether there is a reasonable basis to believe or suspect that the goods in question are being dumped or are likely to be dumped. If so:

- It must order the Customs Service to suspend liquidating the imports in question (that is, completing the final paperwork regarding duties owed) from the date of publication of that determination--in other words, the final determination of the total duty owed on the import is suspended;

- It must order the posting of a cash deposit, bond, or other security equal to the estimated dumping margin for each subsequent import of the good in question; and

1. This appendix is abstracted in large part from House Committee on Ways and Means, *Overview and Compilation of U.S. Trade Statutes*, WMCP: 103-1 (1993), pp. 53-71.

2. Since the Antidumping Act of 1916 is almost never used, this subsection concentrates on the procedures relating to Subtitle B of Title VII of the Tariff Act of 1930, as amended.

- The ITC must begin its final determination of injury.

If there is no reasonable basis to believe or suspect that the goods in question are being dumped or are likely to be dumped, then liquidation proceeds but the investigation also continues.

Final Determination of Dumping by DOC

Within 75 days of its preliminary determination of dumping, DOC must make a final determination of whether dumping has occurred. If a timely request for extension is made and granted, the limit is 135 days. If DOC determines that dumping has not occurred, then the investigation is ended, liquidation of imports is resumed (if it was suspended), and any cash deposit, bond, or other security that may have been posted as a result of the preliminary determination is refunded or released.

If dumping has in fact occurred, DOC suspends liquidation and orders posting of a cash deposit, bond, or other security equal to the dumping margin on future imports of the good if that action was not already taken after the preliminary determination.

Final Determination of Injury by the ITC

Within deadlines specified in law, the ITC must make a final determination of whether the dumped imports are materially injuring the U.S. industry.[3] If they are not, then the case ends, liquidation of imports is resumed, and any cash deposit, bond, or other security posted on imports during the investigation is refunded or released.

If the imports are injuring the U.S. industry, DOC must issue an antidumping duty order within seven days. The order must require the deposit of estimated antidumping duties on future imports, pending their liquidation. That deposit must be equal to the most recently estimated dumping margin. Finally, the order must direct the Customs Service to assess antidumping duties equal to the dumping margin.

Administrative Review and Final Assessment of Duties

Once a year, if requested, DOC must conduct a review to determine the actual dumping margin of the goods that entered during the year. If no review is requested, the actual dumping margin is assumed to be the same as the rate on which the estimated-duty deposit was based. Based on the actual dumping margin, the final antidumping duties for the imports are assessed and the imports are liquidated.

For imports that entered between the preliminary and final determinations, any excess amount of the cash deposit, bond, or security posted on those imports over and above the final estimated dumping margin is refunded. If the cash deposit, bond, or security is less than required to cover the final estimated dumping margin, the deficit is disregarded. For imports entering after the final determination, if the estimated duties deposited are larger than the final assessed duties, the excess is returned to the importer with interest. If they are smaller, the importer must make up the deficit with interest. For future imports, the deposit of estimated antidumping duties must equal the new dumping margin determined in the review.

Termination of Antidumping Orders

Antidumping orders can be terminated in three ways. The first is a cessation of the dumping as indicated by findings of no dumping in three consecutive administrative reviews. The second is lack of interest as indicated by failure to request an administrative review for five consecutive years. The third is changed circumstances, which means either that the domestic industry that petitioned for the relief no longer wants the order or that the ITC has determined that the dumping is no longer likely to lead to injury of the domestic industry. The ITC will grant a review to make such a determination only when the foreign exporter has shown good cause.

3. A final determination of injury must be made within 120 days of an affirmative DOC preliminary determination of dumping or 45 days of an affirmative DOC final determination of dumping, whichever is later. If the preliminary DOC determination of dumping was negative but the final one was positive, then the ITC has 75 days rather than 45 from the date of the final DOC determination to make its final determination of injury.

In general, a foreign exporter will find it difficult to get an antidumping order terminated without ceasing the dumping.

Termination and Suspension of Investigations

If the petitioning industry withdraws its petition, DOC or the ITC may terminate an investigation before it reaches the point of the final determination of dumping or injury. DOC may also stop an investigation on its own authority if the case was self-initiated. DOC may suspend an investigation, subject to certain restrictions in law, if an agreement--referred to as a "suspension agreement"--is reached with the exporters to cease exporting the goods in question or to revise their prices to eliminate the dumping or eliminate the injury.

Countervailing-Duty Law and Procedures

The procedure for investigating, settling, and reviewing CVD cases and orders is essentially identical to that for antidumping cases and orders. DOC makes the preliminary and final determination of subsidies, as it does for determinations of dumping. The only significant differences are different time constraints and that no ITC injury determinations occur for cases in which the imports are from nations that have not signed the Antidumping Code.

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