APPROPRIATE SELECTION OF SURROGATE COUNTRY IN ANTIDUMPING CASE AGAINST NON-MARKET ECONOMY

Lianlian Lin
California State Polytechnic University - Pomona
APPROPRIATE SELECTION OF SURROGATE COUNTRY IN ANTIDUMPING CASE AGAINST NON-MARKET ECONOMY

Abstract

In responding to a series of antidumping charges against Chinese exports to the US, Chinese companies involved have become more active in defending themselves. A key issue in the US antidumping cases against China is the selection of a surrogate country. According to the 1999 Sino-American Trade Agreement, the US will continue to treat China as a non-market economy for fifteen years, from the date of China’s WTO accession (“Antidumping,” 2000). Whether a surrogate country is appropriately chosen directly affects the calculation of cost of various factors of production and thus determines whether the subject imports are sold at less than fair value. This study takes a recent non-frozen apple juice concentrate (CAJ) case, the first winning case for the Chinese companies, as an example in order to analyze various issues in antidumping cases against a non-market economy. This study will also discuss some lessons the Chinese companies can learn from the case.

CASE SYNOPSIS

Apple juice is the first winning lawsuit in the history of China responding antidumping investigations of foreign countries ("A Perfect Full Stop," 2004). The US Department of Commerce initiated its investigation of AJC production from China in June 1999, in response to a petition filed by several domestic manufacturers. The Commerce chose India as the surrogate country and calculated the costs accordingly. As a result, the Commerce reached a conclusion in its Final Determination that the ACJ from China was sold at less than fair market value. Then, another US government agency, the US International Trade Commission, determined that an industry in the US is materially injured by reason of imports from China of certain non-frozen apple juice concentrate.

However, the nine Chinese companies involved in the case brought the case to the US Court of International Trade. They challenged the Commerce’s selection of India as the surrogate country for China and its use of India prices to value juice apples. The Chinese companies pointed out several errors in the Commerce’s valuation of ocean freight expense, steam coal, selling general and administrative expenses, and factory overhead. In addition, the Commerce failed to amend ministerial errors contained in the Preliminary Determination. At the end, the Court of International Trade remanded the case to the Department of Commerce. In the Commerce’s remand determinations, the four of the nine Chinese companies received 0% weighted average margins while the rest of five Chinese companies received 3.83% margins, reduced from the original 15.36% (see Table 1 below for detail).

Table 1 The US Department of Commerce Amended Final Dumping Margins

<table>
<thead>
<tr>
<th>Manufacturer/Exporter</th>
<th>Original Final Margin (%)</th>
<th>Amended Weighted Average Margin (%)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Yantai Oriental Juice Co.</td>
<td>9.96</td>
<td>0</td>
</tr>
<tr>
<td>Qingdao Nannan Foods Co.</td>
<td>25.55</td>
<td>0</td>
</tr>
<tr>
<td>Sanmenxia Lakeside Fruit Juice Co. Ltd</td>
<td>27.57</td>
<td>0</td>
</tr>
<tr>
<td>Shaanxi Haisheng Fresh Fruit Juice Co.</td>
<td>12.03</td>
<td>0</td>
</tr>
<tr>
<td>SDIC Zhonglu Juice Group Co.</td>
<td>8.98</td>
<td>0</td>
</tr>
<tr>
<td>Xian Yang Fuan Juice Co., Ltd</td>
<td>14.88</td>
<td>3.83</td>
</tr>
<tr>
<td>Xian Asia Qin Fruit Co., Ltd.</td>
<td>14.88</td>
<td>3.83</td>
</tr>
<tr>
<td>Changsha Industrial Products &amp; Minerals Import &amp; Export Percent Corporation</td>
<td>14.88</td>
<td>3.83</td>
</tr>
<tr>
<td>Shandong Foodstuffs Import &amp; Export</td>
<td>14.88</td>
<td>3.83</td>
</tr>
</tbody>
</table>
The Chinese companies appealed this case to the US Court of International Trade on two grounds: the Department of Commerce’s selection of various surrogate factors of production and the ministerial errors the Commerce made in its Preliminary Determination. On the second count, the Court rules that the policy in Commerce’s regulation is in accordance with law and the ministerial errors did not affect the result of the case. Thus, this research will focus on the first count - issues in selection of a surrogate country.

The Commerce’s selection of various surrogate factors of production includes six aspects:
- Selection of a surrogate country: India
- Selection of prices to value juice apple: India prices
- Valuation of ocean freight expenses
- Valuation of steam coal
- Valuation of selling, general, and administrative expenses; and factory overhead
- Inclusion of Detroit freight costs in its east coast surrogate freight calculation

The Court ruled in favor of the Chinese plaintiffs in all aspects above except for the third one: valuation of ocean freight expenses. Those issues are discussed one by one below.

**Surrogate Country - Changed from India to Turkey**

When the Commerce selected India as the surrogate market economy country, it relied on data in a private market study prepared for Petitioners by a paid consultant (“Market Study,” 2000) and data about AJC production from a single government-controlled company in India, Himachal Pradesh Horticultural Produce Marketing & Processing Corp. (HPMC). The Commerce asserts that it found substantial evidence on the record to conclude that India was a significant producer of comparable merchandise and believes that AJC and SSAJ (single strength apple juice) are comparable because both are made from the same basic input (juice apples). However, there is no official country-wide data about AJC/SSAJ production in India. The Commerce accepted the Market Study data

---

**Corporation**

| PRC-wide | 51.74 | 51.74 |

Source: International Trade Administration, Department of Commerce, Effective Feb. 13, 2004
because the Chinese companies have not provided information to reject this market study. Thus, India, the 10th largest apple growing country in the world, is considered as a significant producer of comparable merchandise.

The court finds that Commerce’s conclusion is not in accordance with law (19 U.S.C, sec 1677; World Finer Foods, 2000). The court points out that secondary information may not be entirely reliable and can be used if it has probative value. The Commerce failed to indicate that Market Study is probative of the Indian AJC industry as a whole. The burden of verifying secondary information from independent sources falls squarely on Commerce. Furthermore, Law requires that Commerce must “articulate a ‘rational connection between the facts found and the choice made’”. The Commerce’s conclusion is not based on substantial evidence on the record because it did not adequately explain the connection between the data and conclusions in Market Study, and its own conclusion.

HPMC’s annual report is another source Commerce used to conclude that India was a significant producer of AJC. This conclusion would hold only if one of the following were shown: HPMC produced most of the AJC in India and such output was significant; or significant production of AJC by other Indian producers could be extrapolated from the HPMC information. Since Commerce failed to do so, thus the court remands the case to Commerce for reconsideration. In its remand determinations, the Commerce reviewed the record evidence and decided that Turkey, rather than India, was the appropriate surrogate country (A-570-855, 2004).

**Selection of Prices in Apple Valuation - Changed from Indian Prices to Turkish Prices**

The Commerce chose India prices as a surrogate value for PRC juice apples – 2.25 Rupees (Rs) per kilogram. The Chinese companies contended that the selection was improper because the primary raw material input in making AJC – juice apples – was influenced by a Market Intervention Scheme (MIS), in which the prices of apples were artificially raised by the Indian national and provincial governments in order to provide a subsidy to the apple growers.

However, the Commerce accepted the MIS as an acceptable subsidy program because the subsidy to Indian producers of apples was not large enough to raise the prices of juice apples to no longer reflect a fair market value. In addition, the Commerce stated that the 2.25 Rs/kg price was not the MIS price the growers receive, but a market-driven price actually paid by an India producer of AJC.

When examining whether the value of 2.25 Rs/kg was a market derived price actually paid by an Indian AJC producer – HPMC, the court found the
Commerce’s conclusion is difficult to credit because the MIS raises the value of a factor of production would necessarily raise normal value to the Chinese’s disadvantage. Moreover, when determining juice apple prices, the Commerce relied on data from HPMC, a government controlled company that administers the MIS by purchasing apples to stabilize prices. This company has not historically made a profit because in part MIS has become the company’s main activity. Its losses are made up by loans from the state government and other government sources. Therefore, HPMC activities do not appear to be market driven. MIS caused distortion and tended to increase the price paid for juiced apples. Using such prices as fair market value of Indian apples for purpose of valuation is not supported by substantial evidence. In remand determination, the Commerce used Turkish data to amend its calculations in valuation of juice apples.

**OCEAN FREIGHT EXPENSES VALUATION - USING SAME SURROGATE FREIGHT PRICE**

According to the Commerce regulation regarding a non-market economy, if a factor is purchased from a market economy supplier and paid for in market economy currency, the price paid to the market economy supplier is usually used. The Chinese companies had their goods shipped by market economy companies and paid for the charges in a market economy currency. They thought they met the requirements and provided the documentation of payment to the Commerce.

However, the Commerce did not accept the proof because the payment was made to a PRC freight forwarder rather than to the market economy carrier. In other words, this transaction between Chinese companies was between two entities in a non-market economy. The Chinese companies ignored an injunction in the regulation that the Commerce will normally use the price paid to the market economy supplier (19 C.F.R.). Thus they did not provide any evidence of transactions between the PRC freight forwarder and the market-economy ocean carriers used to transport the merchandise. The Chinese companies cite several instances to indicate that the Commerce has considered transactions involving a freight forwarder (“Notice,” 2000), but the freight forwarder would be acceptable if it is from a market economy. The issue here is whether if the Chinese are directly dealing with an entity from a market economy in the transaction. The Chinese could not find any case that the commerce has accepted a transaction between two non-market entities as proof of the cost of ocean freight expenses. As a result, the court ruled that the commerce’s use of a surrogate freight price in ocean freight expenses valuation is in accordance with law and also consistent with past practice.
STEAM COAL VALUATION - CHANGED FROM INDIAN IMPORT PRICES TO INDIAN DOMESTIC PRICES

The commerce used data for coal imported by India instead of domestically produced coal. The Chinese companies contend that no evidence in the record indicates that Indian domestic coal price is inaccurate or distorted. In fact, the evidence shows that the import price is unrealistic for AJC producers because they have no reason to purchase the higher-priced imported coal. In response, the commerce contends that the data from the Monthly Statistics was deemed the most contemporaneous with the period of review and provided a more accurate surrogate value of coal costs than the resource provided by the Chinese. No evidence suggests that the data is unreliable. Rather, the data is the best available information. Therefore, the use of the data was justified.

However, the court pointed out that the commerce’s discussion fails to explain why its use of imported coal data “best approximate” the cost of coal incurred by Indian AJC producers during the period of review. Neither the commerce explains how the use of more expensive imported coals data is the best available information to establish the actual cost of coal by Indian AJC producers. The commerce provided no evidence to lead to the conclusion that India’s domestic AJC producers would use imported coals instead of domestic coal. Since no indications that the domestic Indian coal market was distorted so that the use of import data was preferred; and that the use of imported coal values “best approximate the cost incurred” for Indian AJC production, the court remanded the case to the commerce. Accordingly the commerce changed its valuation of steam coal by using Indian domestic prices (A-570-855, 2004).

SG&A AND FACTORY OVERHEAD VALUATION – RECALCULATION BASED ON TURKISH DATA

When calculating selling general and administrative expenses (SG&A), and overhead ratios, the commerce relied on the 1992-93 financial data from the Reserve Bank of India Bulletin (RBI) (“Preliminary Determination,” 2000). This financial data falls into a general “basket category.” The Chinese companies contend that the commerce should use the 1998-99 audited financial data of the largest known Indian AJC producer (HPMC) because it was six years more recent than the RBI data and was taken from “multiple and unrelated industries”. In addition, it was inconsistent for the commerce to use HPMC’s 1998-99 financial statements in selecting Indian as the surrogate country and in valuing juice apples, while rejecting same data for calculating surrogate SG&A expenses and overhead ratios.
The commerce responds that although HPMC was the largest producer of juice apple in India, 80% of its revenues came from activities other than the production of fruit juice. Thus its expenses would not be representative of the overhead and SG&A expenses that would be incurred by a PRC AJC producer.

According to the commerce’s regulation (“Code of Federal Regulations”), when valuing “manufacturing overhead, general expenses, and profit, the commerce normally will use nonproprietary information gathered from producers of identical or comparable merchandise in the surrogate country.” In this case, HPMC’s data is from an actual producer of the subject merchandise in the surrogate country. When the commerce used HPMC’s data for purposes of seeking the surrogate market economy and proper value of juice apples, it followed the practice and acted within its discretion. However, when it comes to SG&A and overhead valuation, the commerce rejected the use of financial data from HPMC even though the commerce concluded that HPMC was a producer of comparable merchandise. Instead, the commerce chose to use more generalized RBI data, which was dramatically more outdated than the HPMC data and bore little relationship to the actual costs incurred by an Indian AJC producer. Therefore, the commerce’s decision was not supported by the record.

Even if the HPMC data may not accurately reflect the SG&A expenses and overhead ratios of an Indian AJC producer, the commerce did not show that it made an examination of HPMC’s financial data to determine if reliable SG&A expenses and overhead ratios could be calculated. On the other hand, the Chinese companies have submitted evidence to establish the adequacy of this financial data, which sufficiently detailed to make SG&A expenses and overhead ratios (“Respondent’s,” 2000). Therefore, the court remanded the case and the commerce recalculated SG&A expense and overhead by using Turkish data.

**EAST COAST SURROGATE FREIGHT CALCULATION – WEIGHTED RECALCULATION**

When calculating east coast surrogate freight costs, the commerce included the cost of sending freight to Detroit, a city that is approximately 600 miles away from the East Coast. The Chinese companies pointed out in their respondents’ submission that the Qingdao to Detroit freight rate was provided only to account for certain shipments made by one respondent to a port near Detroit. All other east coast shipments from all other eight respondents were made to coastal ports. Thus, they argue that three rates should have been established in this case: an east coast rate; a west coast rate; and a Detroit rate for those shipments made to that city. Accordingly, the Chinese further argue that the cost of shipping to Detroit should not included in either the east or west coast rates because that would unfairly increase these rates to their disadvantage and
unnecessarily reduce the accuracy of the surrogate freight rates. The Detroit freight cost is 25% higher than the legitimate East Coast freight rates.

The commerce correctly indicated that it would have been inappropriate to include the costs in the west coast rate. But it did not explain why the Detroit costs should be included in the east coast rate, which would be equally distortive. The commerce also failed to consider the volume of freight sent to each port and thus valued the few shipments to Detroit equally to the many shipments to New York. The issued was remanded by the court to the commerce. In its remand determinations, the commerce changed its valuation of East Coast freight by weighting its calculation to reflect accurately the volume of merchandise actually shipped to each destination.

LESSONS FOR CHINESE EXPORTERS

In the US antidumping cases against China, the chance for Chinese to win was 25%. The apple juice was the first winning case the Chinese respondents ever won in history. Therefore, some lessons can be learned for Chinese exporters.

Active response to the antidumping investigation is the first step that Chinese companies must take to fight against antidumping charges. Many Chinese are afraid of responding for a number of reasons. They are not familiar with international trade laws and rules and legal procedures; it is burdensome to provide a large amount of information about their production, prices, and industry; and it costs a huge amount of money to hire best foreign attorneys and to go through legal proceedings. There are over thirty apple juice producers in China. When the antidumping investigation began, 15 companies agreed to respond and then 11 companies paid but one dropped later.

In the apple juice case, the Chinese respondents paid over 30 million RMB (Chinese currency, equivalent to about $3.6 million), which was an enormous figure to Chinese firms. Many Chinese companies are too nearsighted to see the big picture. If they only think of winning or losing the case itself, they are usually discouraged to fight. They should think outside the box. They will definitely lose the case if they don’t respond. Furthermore, they will lose a big export market – US, which would be devastating to the whole industry. The revenue from possible 150,000 tons of apple juice export may reach $10-15 million if the tariff on apple juice remains same. This also means a demand for 1.12 million tons of apple (“Four and Half Years”, 2004). Therefore, the stake is surely worth fighting.

In the petition by American apple juice producers, they requested 91.84% antidumping rate on Chinese apple juice exporters. After they heard that Chinese firms prepared to fight, their requested rate dropped to 51.74%. In the Commerce’s final determination, the responding Chinese firms received a rate of
14.88% in average while non-responding firms received 51.74% rate. One Chinese firm received a zero antidumping rate and thus did not join the appeal to the International Trade Court. The rest of nine Chinese firms continued to appeal the case and finally received an average of 3.83% rate for four firms and a zero rate for other five firms. For those Chinese companies who did not responded, the average antidumping margin was 51.74%. During the period of investigation, the responding Chinese firms increased their export to US and their market share in US market increased from 18% in 1998 to 50% in 2003 (“We Won”, 2004).

Working as a team and being prepared are also critical to win any antidumping cases. When the antidumping investigation started, there was no apple juice association in China. Over 30 apple juice producers held a meeting and decided to fight together, increased their export prices to US, and prepared to form an industry association. Within a year, the apple juice branch was established under China Chamber of Commerce of Imports and Exports of Foodstuffs, Native Produce and Animal Byproducts (also known as CFNA). This branch took the lead in the apple juice antidumping case and took measures to self-regulate the industry to ensure the healthy development of the industry. When the antidumping rate against Chinese firms dropped from 91.84% to 51.74%, the Chinese firms did not compromise; when the commerce decided that the rate was 14.88% in average, they did not stop there. They appealed the case all the way to the US International Trade Court and got a rate of 3.83% in average for responding Chinese firms. Without working as a team, the Chinese apple juice producers would not have such courage to fight to the end; they would not be able to afford such expensive attorney and lawsuit fees; and more importantly, they would not regulate their industry to adopt fair trade practice, which can safeguard them from more future antidumping charges. This case also illustrates the importance and urgency for China to be transformed and recognized as a market economy.

REFERENCE

19 C.F.R. section 351.4085 (c) (1)


Code of Federal Regulations, 19 C.F.R. section 351.408 (c) (4).


“我们打赢了美国商务部” (We Won the Case against the US Department of Commerce”, Renmin Net), http://news.xinhuanet.com/newcenter, 2/22/04.


**Author Biography**
Lianlian Lin, Ph.D, LL.M, is Professor of Management at the College of Business, California State Polytechnic University Pomona.