

**ECONOMIC STATECRAFT: UNITED STATES ANTIDUMPING AND  
COUNTERVAILING DUTY POLICY**

**Submitted by Karen Philippa Malmgren for a Ph.D in International Relations at The London  
School of Economics and Political Science, University of London, July 1991.**

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**ABSTRACT: Economic Statecraft: United States Antidumping and Countervailing Duty Policy.** Ph.D submitted by Karen Philippa Malmgren in the Department of International Relations, The London School of Economics and Political Science.

The Antidumping and Countervailing Duty laws are competition policy instruments with which the United States ostensibly seeks to promote the role of market forces, enhance competition and thereby uphold the post-war international economic order. However, through a combination of administrative pragmatism and statutory emendation, these trade laws have evolved into instruments with which the United States impedes market forces and insulates its domestic economy from the very competition these laws supposedly aim to encourage. This is a paradox.

Important political issues arise from this paradox which are obscured by the traditional methods of examining trade policy. This dissertation demonstrates that the political aspects can be made apparent if the laws are thought of as instruments of economic statecraft. Through an original application of the theoretical framework David Baldwin has developed in Economic Statecraft, it is argued that the trade remedy laws utilize state power for the purpose of changing the behaviour, beliefs, policies and propensities to act of foreign governments or firms.

By examining the detail inherent in the two statutes it is demonstrated that far from compelling foreigners to abide by market forces and undertake competitive trade practices, the US penalizes them for doing so. On the pretext that foreigners' trade practices are "unfair", the US is compelling them to engage in genuinely anticompetitive practices. Competition is the central mechanism of the post-war international trade system. Therefore, the United States is undermining that order with its use of these instruments of statecraft. Further, remedy policy is generating political conflict between the US and its major trading partners because there is fundamental disagreement as to the normal and appropriate role for governments and firms to play in a modern market economy. Differences of opinion about what is "unfair" in this context arise, as is demonstrated, on political grounds rather than economic ones.

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## PREFACE

I would like to thank my father in particular for providing me with the means to embark upon and finish this dissertation. His intellectual guidance and moral support throughout have inspired me to think harder and better than I would have been able to without him. My mother too gets my thanks for being an unerring support to me during the course of this project. Without her, this dissertation would have been much less easy to read.

To Susan Strange I owe a great debt. Without the Politics of the World Economy program she created at the London School of Economics I would undoubtedly have struggled indefinitely to draw the links between economics and politics. She taught me to always consider the assumptions behind arguments, patterns of thinking and policy. As my first supervisor she levelled deserving criticism at my ideas and work which inspired me to cast off dogma and explore beyond the "official" borders of social science disciplines. That is how I have come to write a thesis which covers economics, law, politics and international relations. I would also like to thank Michael Hodges for supervising my work. And, finally, I owe a very great debt of thanks to James Mayall who guided me to completion. The care he took in reading and criticizing my work was invaluable to me. Without his encouragement I would no doubt have taken longer to complete this dissertation.

I must also thank the members of the International Political Economy Seminar, all Doctoral candidates, whose rigour and wide knowledge and constant encouragement helped me to hone my own ideas and envisage the wider field of international political economy.

Outside the University of London there are others who were especially helpful to me in the course of researching and writing this thesis. Gary Horlick was extremely encouraging. He helped to confirm that the path on which I was travelling was accurate. I thank him for his advice. Rodney Grey too talked with me at length and guided me through the thorny field of trade policy. I am endlessly grateful to both of them. Others, those in government, law and the diplomatic corp, who gave me assistance, guidance and advice, also deserve my warmest thanks.

Of course, the work that follows, and any errors of fact or logic in it, are my own, alone.

Philippa Malmgren  
July 1991





## CHAPTER ONE -- TRADE REMEDY POLICY: ECONOMIC STATECRAFT

### THE PROBLEM

It is common knowledge that the United States has played an active part supporting the post-War (WWII) international trade system. In this system, competition, rather than colonial claims, for example, is the central mechanism by which the gains from international trade are distributed internationally. In addition to enforcing and abiding by the General Agreement on Tariffs and Trade (GATT), the international agreement which sets out the rules that support competition, the United States government employs its own trade measures to enforce competition policy internationally. Two of these competition policy measures, the antidumping law (AD) and the countervailing duty law (CVD) have been used by the United States increasingly aggressively since the 1960's. These competition policies supposedly aim to promote competition.<sup>1</sup> They are ostensibly intended to increase the play of market forces in the international trade system and to reduce the distortions to trade caused by both foreign corporate dumping practices and foreign government subsidization of foreign firms. But, in practice, these policies are having the opposite effect. This raises fundamental questions about whether the United States is now supporting or undermining the post-war international economic order which it had been instrumental in building.

American political rhetoric repeatedly emphasizes the United States' commitment to promoting both competition and market forces in international trade, especially among the signatories to the GATT. But, a schism has emerged between this rhetoric of "free(r) trade" and the trade-restrictive manner in which these two competition policy measures are effectively used.

How has this happened? The United States has "enhanced the enforceability" of these laws, especially since the late 1960's, through statutory emendation and pragmatic administration. This appears to have been done with the conviction that improved efforts

to dissuade foreign firms or governments from engaging in "unfair" anticompetitive trade practices would serve to promote free(r) and fair(er) competition.

However, the process of "enhancing" the statutes has actually subverted them. Though perhaps well-meant, the statutory and administrative changes have blurred the distinction between fair and unfair trade practices. Increasingly the United States has labelled fair trade practices as "unfair" and anti-competitive. On that pretext the alleged perpetrator has been compelled to remedy the unfair trade practice by paying a tax on their exports to the United States, voluntarily restrain the level of their exports, adopt quotas, change their prices, or otherwise engage in genuinely anticompetitive behaviour.

In reality, the AD and CVD laws have evolved as instruments with which the United States reduces the play of market forces, undermines the role of competition, and insulates the American economy from the very forces these laws ostensibly serve to promote. The free trade rhetoric cloaks this reality. Further obscuring the subverted policy from public view is the dense technical detail inherent in the statutes. Combined, these factors have insulated them from scrutiny, especially by students of international relations, for whom these laws have appeared remote technicalities, distant from the political arena that is the focus of their attention.

That the United States is acting in this manner is a paradox. It has been the United States, even before the end of the Second World War<sup>2</sup>, that has long promoted the conception of economic order based on competition. It has been the United States that has consistently taken the lead in international negotiations to reduce barriers to trade. Now it is the United states which is leading a movement of policy administration which runs directly counter to the avowed goals of United States multilateral diplomacy.

The significance of this paradox extends far beyond the simple point which has been highlighted in recent years mainly by economists, namely that the United States is being protectionist. Rather, its significance begins to emerge if these competition policy measures are seen not as "technical" trade measures but as instruments of economic statecraft.<sup>3</sup>

As developed by David Baldwin, economic statecraft is a framework for conceptualizing about how economic policy instruments, such as trade policy, are actually employed in the exercise of state power. With the AD and CVD laws the United States compels foreign firms and foreign governments to change their behaviour in commercial affairs. That is to say that these laws involve the use of power; state power is used to get foreigner actors to do that which they otherwise would not, to change their actual or potential behaviour in compliance with the demands of the United States. Here power meets politics.

An attempt by one state or government to change a foreign actor's behaviour is a political act. The so-called unfair trade laws, then, mark a point at which policy, power and politics come together. Starting from this point questions relevant to international political relations become apparent. What is the United States compelling foreign actors to do and on what grounds are they compelled to comply?

For those who come from a background of liberal economics the insinuation that trade policy is a political phenomenon involving the use of power may at first seem controversial. After all, according to liberal economic thought, politics is what interferes with the market's ability to function efficiently. It may be argued that traditional well-accepted free market conceptual frameworks already exist and have served their purpose: to distinguish free trade versus protection, and non-intervention versus intervention (by governments in markets and economic affairs). Some traditionalists may say that it is simply a question of identifying who is being protectionist and who is encouraging free trade. Or, it is simply a question of identifying which governments are "intervening" unfairly in economic affairs and which are not.

The problem with the traditional frameworks is that they are misleading. They obfuscate the central political issues that are at the heart of the modern controversies about competition policy.

The main purpose of this study is to illuminate the political issues arising from the way in which the United States uses these laws. This can be done by examining these laws

as instruments of economic statecraft. These political issues give rise to controversy, contention, and conflict in international relations. It is the profound differences of perception and opinion among the peoples and governments of the world's market economies over the appropriate role of government and the appropriate behaviour of firms that is at issue.

Although the subject matter appears to be economics, the essential aims of policy are political. With the AD and CVD laws the United States aims to change the actions, opinions, beliefs, policies and even propensities to act of a foreign firm or government. As such, this is a study not of the links between economics and politics but of the inseparability of economics and politics.

Further, economic statecraft emanates from domestic politics. Through statutory and administrative change the United States sets the terms by which foreign actors, whether firms or governments, must abide in order to avoid penalties. These modifications result from the interaction of domestic political forces. They are a consequence of domestic political processes. This study does not seek to explain the history of the procedures by which the laws came to be changed. That would entail an exhaustive history of the domestic influences which come to bear on trade policy, ranging from the origins of minute bits of statutory language to the reasons why those officials administering the law exercised the discretion available to them in a particular manner at a particular time. The domestic sources of trade policy are extremely important. But, there has been a tendency in studies of domestic and international politics to focus on the policy-making process to the exclusion of the final product. Here we seek to understand: what is the policy? In the end, the policy is to compel foreigners to do what?

## **PURPOSE**

The purpose of this study is threefold. First, it will be demonstrated that the economic statecraft framework is a more useful and accurate way of unravelling and

resolving the problems posed by developments in United States antidumping and countervailing duty law and policy than the traditional "free trade versus protection" and "non-intervention versus intervention" frameworks.

Second, using the economic statecraft framework the study examines the content and administration of these laws, focusing on the years 1968-1988, with a view to confirming the divergence and subsequent contradiction between the rhetoric of free trade and actual trade policy. Equally important, the laws' role as instruments of economic statecraft can be substantiated by examining the laws' technical details.

Third, this study seeks to demonstrate that developments in the antidumping and countervailing duty laws mean that the United States is actually undermining the post-war international economic order with the very instruments that were designed to uphold it. This necessitates a full discussion of what is generally meant by the "post-war international economic order".

In addition, this study seeks to fulfill four broader tasks. First, it is a response to the academic calling of Professor David Baldwin, who developed the notion of economic statecraft that is employed in this study:

"Indeed, it is precisely the routine day-to-day uses of trade as a technique of economic statecraft which are least well understood and most in need of illumination."<sup>4</sup>

Second, Professor Baldwin explains that his research on economic statecraft emphasizes "how rather than what to think about such matters",<sup>5</sup> opening the way for new analysis. Hopefully, by applying his framework to a specific problem, this study will carry his approach much further, by illuminating what to think about United States trade remedy<sup>6</sup> policy.

Third, this study seeks to provide an analysis of the trade remedy laws in which the political issues and questions predominate over economic ones.

Finally, one of the most important objectives is to illuminate and clarify what is known about the American enforcement of competition policy through utilization of the antidumping and countervailing duty laws. Analysts of international relations have

neglected these trade laws since they are highly technical and do not appear to be particularly relevant to the realm of world politics. Even for those who accept that trade policy is a political element in international relations, these laws undoubtedly seem obscure in comparison with many other more visible, timely phenomena in the world of politics. Antidumping and countervailing duty cases have moved in recent years from the small columns of the business pages to the front pages in the international press, and controversies between governments and corporations over "unfair" trade practices have become increasingly contentious. It is no longer possible for analysts to ignore these laws and policies. Nor can traditional conceptions any longer adequately explain the political forces set in motion internationally by these seemingly technical areas of law and policy. The trouble is not only what people don't know it is also that what they do know ain't so.<sup>7</sup>

## METHODOLOGY

This study is written in the classical tradition of international relations. The central and subordinate theses are argued rather than tested. The classical approach, as defined by Hedley Bull,

"... is characterized above all by explicit reliance upon the exercise of judgement and by the assumption that if we confine ourselves to standards of verifications and proof there is little of significance which can be said about international relations."<sup>8</sup>

The economic statecraft framework requires a classical approach. It allows the anticompetitive aspects of AD and CVD policy to be demonstrated through analysis and argument. Its advantage is that it allows us to focus on the non-quantifiable, political aspects of competition policy, which are obscured or ignored under the traditional frameworks. There is nothing in the thesis to test. Rather, the power and propriety of the central and subordinate theses are dependent wholly on evidence and logic, judgement and persuasion.

This study examines only the United States. It is not the only country which has an antidumping or a countervailing duty law, nor is it the only place where policy and rhetoric have gone in opposite directions. But, as Raymond Aron has said,

" ... the structure of the international system is always oligopolistic. In each period [of history] the principal actors have determined the system more than they have been determined by it."<sup>9</sup>

The United States has been the leading multilateralist and arguably the most ideological nation in its pursuit of enhanced market forces. Whether intentional or not, if the United States has changed that position, it is bound to have profound effects on the structure of the international trade system.

In addition, more often than not, United States trade law and practice have formed the basis for the concepts and language employed in international trade agreements, and in the laws of other nations. In recent years many trading nations, most notably the European Community, but also newly industrializing countries such as Brazil, have adopted the emerging American ideas and practices in this area. Thus, the significance of this analysis goes beyond the United States. This dissertation serves as an introduction to the kind of economic statecraft increasingly being pursued by the major trading nations of the world. By studying the United States we can learn much about the structure of the international trade system. If the American trade policy concepts and language are at odds with the internationally agreed-upon trade rules then, again, this poses important problems within the international trade system.

Only the United States' side of the story is examined here. Economists regularly attempt to determine whether or not foreign firms are in fact dumping and whether or not foreign governments are in fact subsidizing their industries. However, attempts to determine such "facts" are elusive since it is the unilateral judgement of United States authorities which is used to invoke and administer the remedy measures. This judgement is based on national interpretation and application of extremely vague and highly ambiguous international agreements. So, whether or not a violation is "in fact" taking place is not as important as whether or not the United States authorities say that it is. For this



reason the changes which have been made to the definitions in these statutes and changes concerning the methodology employed in administering these statutes will be examined in detail with care.

Thus, the study seeks to establish: What is dumping? What constitutes a subsidy? When are such practices actionable under United States trade law? In addition the study examines the significant changes which have been made in the methodology which is used to determine whether (and by how much) dumping or subsidization is occurring.

Finally, the remedies available under these laws have changed. The study seeks to ask what are foreigners being compelled to do under these laws? What remedies are they compelled to adopt?

This study also examines the administrative history of these statutes. Through pragmatism, official discretion and creative interpretation, administrative practice is a powerful influence on the applied content of these statutes. An examination of the administrative history will help demonstrate how the laws are applied to induce changes in the behaviour of foreign actors.

The materials employed in the argument are various. The discussion in Chapters One to Three (Section One) mainly rely on the original intellectual and scholarly work others have done. By building on the useful concepts, terms and definitions, others have developed, it is possible to understand and address the problem in the realm of international relations. The bulk of the thesis, however, makes use of both primary and secondary sources. The primary resources are mostly legal citations because the dissertation is about American trade law. In the United States, law review articles, which serve to interpret and define the meaning of developments in American law, are considered primary sources. They are employed as such here. Similarly, because the perception of what the law means is usually more important than what the law actually says, references are made to the secondary materials comprised of writings by scholarly, professional and journalist observers in the field.

## **STRUCTURE**

The dissertation is divided into four sections. Section One (Chapters One, Two and Three) argues why the economic statecraft framework is a better way of addressing the central paradox than the traditional frameworks. Section Two (Chapters Four, Five and Six) examines developments in the antidumping law, carrying on with the central thesis: By "strengthening" the law United States trade remedy policy has diverged from, and ultimately has come to contradict the statutes' intended aims. As such, the United States is undermining the GATTsystem, and indeed the post-war international economic order, with its use of the antidumping law. Section Three (Chapters Seven, Eight and Nine) argues the same for the countervailing duty law. Because these two statutes are similar in their structure and content, the chapters on subsidies will not repeat the technical features presented in Chapters Four, Five and Six. Instead, it will explore the more complex theoretical issues posed by the countervailing duty law. Section Four (Chapter Ten) provides the conclusion. There the argument will be reexamined in light of the analyses provided in earlier chapters. In addition, the final section will examine some of the broader implications of the study's thesis.

The dissertation falls within the prescribed 100,000 word limit which is inclusive of endnotes and appendices but exclusive of the bibliography.<sup>10</sup>

1. Laws are different from but related to policy. As Robert Pastor notes, "'Policy' has come to mean administrative discretion more than laws". Congress and the Politics of US Foreign Economic Policy: 1929-1976, (Berkeley: University of California Press, 1980) page 31. This dissertation examines both AD and CVD law and policy.
2. For the best description of the United States' role in the creation of the post-war international economic order see Richard Gardner, Sterling Dollar Diplomacy: The Origins and the Prospects of Our International Economic Order (New York: MacGraw-Hill Book Company, second expanded edition 1969).
3. The economic statecraft concept is developed by David Baldwin in his prize-winning study of power, politics and economics, Economic Statecraft (Princeton: Princeton University Press, 1985).
4. David Baldwin, Economic Statecraft, page 60.
5. *ibid.*, page 5.
6. The AD and CVD laws are only two of many trade remedy laws. They are called remedy laws because each serves to "remedy", to fix, to correct, the distortions to international and domestic trade caused by a foreign government's or foreign firm's anticompetitive trade practices such as dumping and subsidization.
7. This is a twist on an old quote. "The trouble ain't what people don't know it's that what they do know ain't so." It is, no doubt, apocryphal, but, Kenneth Boulding attributes this quote to Will Rogers in a lecture Boulding gave about the problems ignorance causes in the study of economics. See "The Economics of Knowledge and the Knowledge of Economics" Richard T. Ely Lecture Papers and Proceedings of the Seventy-Eighth Annual Meeting of the American Economic Association, New York, December 29-30, 1965, The American Economic Review Vol. LVI, No. 2, May 1966, page 1. In contrast, Milton Friedman attributes it to Josh Billings in Bright Promises, Dismal Performance: An Economist's Protest WR Allen ed., (Sun Lakes Arizona: Thomas Horton and Daughters, 1972 reprint 1983).
8. Hedley Bull, "International Theory and the Case for the Classical Approach" World Politics, XVIII. April 1966, page 361.
9. Raymond Aron, Peace and War: A Theory of International Relations (New York: Doubleday, 1966) page 95.
10. The London School of Economics Calendar 1990-1991, page 374.

## CHAPTER TWO -- TRADE REMEDY POLICY

### WHAT IS TRADE REMEDY POLICY?

I export. He dumps. This common expression vividly reveals the misconceptions surrounding "unfair" trade practices. They are so pervasive, and so little-examined by analysts of international relations that it is essential to clarify what constitutes an unfair trade practice, and what are deemed to be appropriate remedial actions in trade remedy policy.

The liberal free market economic theory of international trade posits that international competition is the most efficient means of distributing resources and creating wealth. Traditional international trade theory assumes that trade is generated by comparative national advantages in the production of goods.<sup>1</sup>

Actions by governments and firms to alter the comparative advantage distort competition and thereby degrade economic performance. In early theory comparative advantage was thought to be a relatively static condition based on factor endowments of a nation, especially land, labour and resources. Most liberal trade theorists acknowledge that comparative advantage is a dynamic condition which can be affected, and even altered in the long run -- for better and for worse -- by "unfair" trade practices, namely the presence of monopoly power and government assistance to industry.<sup>2</sup> Acceptance of the notion of dynamic comparative advantage has led to increased attacks on "unfair" trade. Stephen Magee and his co-authors clearly sum up the connection between anti-competitive trade practices and "unfairness".

"Wealth comes from two sources: production and predation. Production increases wealth whereas predation transfers wealth. Production is a cooperative effort in which direct actors may gain; predation is a noncooperative effort in which the economic prey lose. Production is cooperative; predatory behaviour is selfish."<sup>3</sup>

Two principal "unfair" means of altering the effects of competition and free market forces are "dumping" and official government subsidization. Originally the term dumping described the act of price discrimination, that is, selling a product to one buyer

at a different price than to another -- internationally, selling in a foreign market at a different, lower price than in the home market. The idea is that high domestic prices generate profits which allow the seller to "subsidize" low-priced exports. This "unfair" advantage allows the company to undercut foreign competitors and gain a greater global market share.<sup>4</sup> Ultimately the competitors are driven out of business. As a result, the level of competition is reduced, and the dumper is then able to exploit world markets through monopolistic behaviour. Hence, dumping is predatory and anticompetitive.

The working definition of dumping, that is, the definition of the level of price discrimination is actionable under the law, has changed dramatically since the first antidumping statute was enacted in 1894. It has, for example, at various times been defined as sales (at prices which are) "below normal value", "sales below home market value", "sales at less than fair value" and "sales below costs".<sup>5</sup>

Subsidization by governments poses another form of economic distortion. There has never been any agreement among governments nor, frankly, among economists, as to what exactly constitutes a subsidy. Broadly, the term subsidy is used to describe the artificial aids governments provide to their domestic industries in the production, manufacture or export of products. It is unclear what constitutes an "aid". Price discrimination has never been the central issue in these cases. Rather, subsidies reduce the recipient firm's costs. Reductions in costs may result in reduced prices or enlarged profit or operating margins instead. The law recognizes that the domestic price may be subsidized as well as the export price. A subsidy is actionable because it effectively allows firms to lower their costs unfairly.

Subsidies appear in an almost infinite number of forms. For example, a subsidy can come in the form of payments which are made directly by governments to firms, or in the form of state ownership of firms. But, subsidies can also include "non-actions" such as exempting a firm from taxation to which others are subjected. The common feature is that all subsidies are believed to create artificial cost advantages. Again, as with dumping,

the working definitions of what constitutes a subsidy has changed since the countervailing duty statute was enacted in 1890.

The important point to keep in mind is that differences in prices and costs are what give rise to international trade<sup>6</sup>. If an imported good is less expensive than a domestically produced good it is not necessarily dumped or subsidized. An imported good may be much more expensive than any domestically produced good and still have benefited from a subsidy. Only unfair trade practices should be penalized.

## THE PURPOSE OF REMEDY POLICY

The AD law serves to "remedy" foreign firms' dumping practices, that is to repair the ill effects of dumping. The CVD law serves to repair the ill effects of foreign governments' subsidy practices. What is meant by remedy, in practice, as we shall see, can be very different from the ostensible meaning of "remedy".

It is now widely agreed that the original and intended or, at least, the appropriate purpose of the AD and CVD laws is to extend domestic competition policy to foreign actors. This "competition policy" interpretation is somewhat dependent on revisionist history. Both laws, though the CVD law in particular, contained a "tariff policy" approach, which was essentially protectionist in character. Both laws contain elements of these two competing philosophies, one of encouraging competition and the other of building protection against foreign competition.

Before 1916, when a federal income tax was created, the vast majority of the federal income came from tariffs on trade.<sup>7</sup> When Congress originally legislated against foreign unfair trade practices it was motivated partly by the desire to increase federal revenue generated by tariffs, or at least prevent its diminution.<sup>8</sup> Thus, from the beginning a tariff philosophy was inherent in the AD and CVD laws. In other words, the purpose of these laws was to protect American industry from import competition and to generate revenue for the federal coffer.

However, the economic rationale for such protectionist policies was subject to increasing attacks in the 1880's and 1890's. The rise of domestic antitrust legislation generated concern regarding impediments to competition -- namely the creation and abuse of monopoly power. Subsidies and dumping encourage the creation of monopoly power. The competition policy philosophy carried over from domestic competition policy laws to international trade policy. According to this interpretation the remedy laws are competition policy measures which aim to prevent the creation and abuse of monopoly power. Thus, those who subscribe to the antitrust interpretation, claim that the only economic rationale for the AD and CVD laws is the protection of domestic competition, not domestic competitors, from anticompetitive foreign trade practices.

The United States lacks the legal jurisdiction to criminally prosecute foreign companies or foreign governments for violating American competition law. It was necessary to create separate AD and CVD statutes to overcome this lack of jurisdiction. Rather than attacking the actions or intent of the foreign actor, as is done under domestic competition law, the remedy laws allow American authorities to offset the anticompetitive effects of targeted trade practices (dumping and subsidization). This is achieved by the application of a tax (called a duty) to the "unfairly" priced or "unfairly" produced import at the border. In theory the amount of the duty should be exactly equal to the unfairly achieved price advantage caused by the practice. This procedure allows authorities in the United States to protect competition -- that is, the domestic competitive environment -- from anticompetitive trade practices.

The two conflicting philosophies, the competition policy and tariff approach, continue to give rise to differing interpretations about the purpose of these laws. Domestic industries which believe they are being damaged by "excess" import competition -- fair or unfair -- tend to subscribe to the tariff policy origins of the law. They believe that the remedy provisions exist to provide them with "relief". For them the laws should serve to protect competitors and not competition. Harvey Applebaum explains.

"Domestic industries do not view the problem as one of fitting injurious practices into the import relief laws. That is the Government's orientation". Instead, they want the "best possibility for victory, and thereby relief."<sup>9</sup>

The inherent conflict between these two standards, the protection of competition and the protection of competitors is extremely important. Domestic competition law and policy has adopted the first standard while trade policy has adopted the second. The conflict between the domestic and international enforcement of competition policy is a continuing theme in this study. The two sets of laws are supposed to serve the same purpose. Their divergence provides an important perspective on understanding how trade rhetoric and trade policy have come to contradict each other.

There are many trade remedy laws.<sup>10</sup> This dissertation examines only two. However, it is important to note that there is another trade remedy law which is designed to protect American industry from fair but "excess" import competition; it is called Section 201 (of United States trade law). It corresponds to Article 19 of the GATT, which is entitled "Emergency Action on Imports of Particular Products", and commonly referred to as the "escape clause" by Americans. Article 19 allows any member country to take emergency action against

"products which are being imported in such increased quantities and under such conditions that they cause or threaten to cause serious injury to competing domestic producers."<sup>11</sup>

In such cases, if a government wants to protect the home market for a specified period of time, to facilitate modernization or restructuring of its industry, the government is permitted by the GATT provision to do so. On the other hand, other governments which might feel adversely affected have the right, under the same GATT provision, to take remedial action. Such governments may request compensation in the form of tariff relief in other economic sectors, or if adequate compensation is denied, such governments are permitted to retaliate. Thus, the price for taking a section 201 action is either paying compensation to other member countries whose benefits under the Agreement are "nullified or impaired" by the action, or, accepting retaliation from them.



The United States, has, in the past, used Section 201 more often than many other countries, but there is always a sting in having to pay compensation. Retaliation is also unpleasant. A Section 201 action tends to imply that the United States is being protectionist since it is acting against fairly priced or produced goods. In recent years the US has declined to use Section 201, preferring to threaten action, or take action under the AD and CVD laws.

There is no compensation or retaliation requirement under the AD and CVD laws. If the imports are "unfair" then the United States can act against them with impunity.

The concept of what constitutes an "unfair" trade practice under the American AD and CVD laws has been substantially broadened over the last twenty years. This has happened for two main reasons. First, by using the AD and CVD laws, rather than 201, the United States ensures that the implication of "unfairness" and protection falls on foreigners, not on Americans. This is why Senator Danforth reputedly has said, "201 is for suckers".<sup>12</sup> Second, it is a politically attractive option. It costs nothing. Foreigners do not vote.

However, it would be wrong to imply that there has been a conspiracy to subvert the statutes. Certainly some involved in the policy-making process have wanted to protect American firms from imports, fair or unfair. They have encouraged back-door protection. But, it appears that Congress has amended the remedy laws in the hopes of making them more "effective" because there was a genuine belief that "unfair" imports were, and are, a real problem. There seems little doubt that political representatives have modified the laws and allowed the officials who administer the laws wide discretion in applying the broadened notion of unfairness because they thought this would promote freer and fairer trade.

The common perception of the problem helps to explain the actions that have been taken. Rising concern among domestic companies about successful imports, the appearance of a large trade deficit and structural change in the international economy,<sup>13</sup> have led many Americans to one conclusion. If America is not as competitive as it once

was it is because foreigners are engaging in unfair play. Robert Baldwin sums up this view.

"The view that gradually gained the support of the major public and private interests concerned with trade matters was that much of the increased competitive pressure on the United States was due to unfair foreign policies such as government subsidization, dumping by private and public firms, preferential government purchasing procedures, and discriminatory foreign administrative rules and practices relating to importation." He goes on to say: "By placing the blame for their decline in competitiveness on unfair foreign actions, U.S. managers and workers could avoid the implications that this decline might be due to lack of efficiency on their part. Finally government officials could maintain that the United States was still supporting the rules of the liberal international trade regime that the country had done so much to fashion."<sup>14</sup>

It is not the competitive system which is at fault. It is the unfair abuse of the system. Therefore the AD and CVD laws must be strengthened so that further unfair foreign trade practices can be prevented and punished.

## THE ARGUMENTS

Why should we use the economic statecraft framework when thinking about these developments in trade remedy policy? Isn't it simply a question of identifying who is damaging free trade through unfair or protectionist trade practices? Or, in the case of subsidies, isn't it just a matter of identifying which governments are intervening in economic affairs? The central contention of this study is that the problems posed by remedy policy cannot be fully understood within the context of "free trade versus protection" nor of "non-intervention versus intervention".

The nature of the relationship between states and markets remains unclear, even after several centuries of debate. The appropriate role of government in the economy remains a contentious issue even among the GATT signatories. In addition, one's view of the proper behaviour of a private firm in a market economy is a highly subjective matter. However, the desire by analysts for a world in which economic forces can function unfettered by the actions of government, and undisturbed by monopoly power and other

manifestations of imperfect competition, a situation which would simplify analysis immensely, is not the same as the existence or even possibility of such a condition.

## FREE TRADE VERSUS PROTECTION

Little appears to have changed since EH Carr observed in 1939,

"even today some "classical economists" insist on regarding free trade -- an imaginary condition which has never existed -- as the normal postulate of economic science, and all reality as a deviation from this utopian prototype."<sup>15</sup>

Going further back in history we find that even Adam Smith, the doyen of all "free traders" said,

"To expect, indeed that the freedom of trade should ever be entirely restored in Great Britain is as absurd as to expect that an Oceana or Utopia ever be established in it."<sup>16</sup>

Yet, a recent cover story the Economist proclaimed: "More than at any time since the second world war, the maiden of free trade is in mortal danger."<sup>17</sup> President Bush should, according to the article, "tell his officials to just say no to protectionism." The free trade paradigm continues to dominate popular opinion. Free trade is "good" and protection is "bad".

It is not the intention here to sway opinions in the long-standing debate between the free trade camp and the mercantilists, between the liberals and the protectionists, between the choice of individual economic freedom versus state control, but rather it is to argue that the traditional "free trade versus protection" framework, which posits these options, is easy to comprehend, but fails to accurately portray the problems posed by trade remedy policy.

One of the consequences of rhetoric is that it establishes the assumptions upon which we base our analysis and it sets the parameters of discussion.<sup>18</sup> If we conceptualize in terms of free trade versus protection then we inherently limit our inquiry to economic issues. Free trade is a term describing an extreme economic condition which is marred by the existence of barriers to trade and distortions in international competition.

Therefore, to use such a framework is to focus on the problem of barriers and distortions. The central assumption is that free trade is preferable to protection.<sup>19</sup> This is why most economic analysts have focused on the problem of barriers to trade.

Tariffs are barriers to trade which have been successfully reduced, by nearly 90% on average, among GATT signatories through successive negotiations since the 1940's. As tariffs have been reduced it has been widely noted that non-tariff barriers have become a more pressing problem. It remains debatable whether this is because tariff reduction has exposed already existing NTB's (the falling water level hypothesis) or whether they have been created to replace tariffs as instruments of protection (the rising reef hypothesis).<sup>20</sup>

Barriers are not the only problem. Increasingly it has been recognized that certain corporate and government practices cause distortions to trade although they cannot be classified as barriers. Consider the example offered earlier in the study of a decision by government not to tax a firm. Such a policy is not a barrier but it can cause a distortion. Similarly, when a firm sells its wares below the cost of production, the practice cannot easily be described as a barrier to trade. It is better described as a trade-distorting practice.

Robert Baldwin has developed the most widely adopted modern definition of non-tariff distortion (NTD's):

"any measure (public or private) that causes internationally traded goods and services, or resources devoted to the production of goods and services, to be allocated in such a way as to reduce potential or real world income."<sup>21</sup>

Having said that, it is necessary to ask what is meant by a "reduction" in potential or world real income? It is not clear. Professor Baldwin recognizes this definition is "not manageable" and comments that only those NTD's which "significantly distort international trade" should be redressed. But, the key term, "significantly", is left undefined.

Dumping and subsidies are NTD's. The desire to eliminate these NTD's has been the primary force behind the increased use of these trade remedy laws. NTD's are commonly referred to as a manifestation of the "new protectionism". Old protection took

the form of tariffs. However, the new protectionism, consisting of non-tariff protection, is an old problem.

Looking back in history we find that non-tariff distortions caused by dumping and subsidization did not preoccupy international trade negotiators nearly as much as the non-tariff protection which was provided by government anti-dumping and anti-subsidy measures! Writing in 1936 EM Winslow explained that international experts had then already found that non-tariff protection posed "one of the most baffling questions that has ever appeared in commercial policy".<sup>22</sup> It remains so.

As early as 1923 there was an international attempt to attack the problem. Economic "experts began in earnest about 1927 to define and formulate the problem in relations to other types of trade barriers and to commercial policy in general."<sup>23</sup> The heading of "non-Tariff Questions" appeared for the first time on the League of Nations Commercial Policy Talks in 1929/30. At first the experts addressing this problem stressed the purpose of the measures, which was to "evade international obligations" and "render what otherwise appears to be a liberal policy in reality highly protectionist"<sup>24</sup>. But proving intent to protect or discriminate was impossible.

Non-tariff protection was then defined in terms of its origins in administrative systems. Finally, non-tariff protection was defined in terms of its discriminatory nature. None of these definitions proved workable. The definitional net was cast too widely and too clumsily. Certain practices were labelled under its terms which should not have been and those which should have been included were left outside its scope. "Thus" Winslow explained "the problem of definition trailed off into one of classification"<sup>25</sup> No progress had been made on this problem by 1969, when the GATT drew up its first comprehensive list of NTB's, as determined by the member governments in complaints about practices of other governments. The initial list reputedly numbered in the thousands of complaints before its compression into coherent categories. To this day there is no internationally agreed method of determining what constitutes a non-tariff distortion. Instead governments continue to draw up lists of objectionable practices. On these lists

are predatory trade practices (dumping and subsidization) as well as administrative NTB's (including the abuse of AD and CVD law).

The earliest treatment of administered protection, considered the standard treatment in the pre-World War II years, is Economic Protectionism, a commentary by Josef Grunzel written in 1916. He explained that;

"means have been sought for by which to place in the hands of the administrative authority such control over the applications of laws regulating economic activity that an actual, though of course not a formal, protection might be afforded to domestic production against foreign competition."<sup>26</sup>

The use of administrative mechanisms, including trade remedy policy, has long been seen as an NTD. Jagdish Bhagwati has drawn attention to the problem of administrative protectionism most recently. He says that the remedy laws have been "captured" by protectionists and are used for the purpose of import protection and not for promoting competition.<sup>27</sup> As such, the remedy provisions are themselves NTD's. Finger, Hall and Nelson explain that such administrative protection arises from,

"the creation of quasi-judicial bureaucratic structures which hear requests for protection and, on the basis of previously established administrative mechanisms determine the appropriate level of additional protection".<sup>28</sup>

The administrative remedy itself can be seen as a form of non-tariff protection. The problem with the free trade versus protection framework is that it leads us to this dead end. Dumping and subsidies NTD's which must be eliminated by remedies. Yet those very remedies can themselves be NTD's. A report on competition and trade policy from the Organization for Economic Cooperation and Development made this point succinctly:

"Although designed to redress competitive disequilibria, laws relating to unfair trade practices, if improperly used, can act as barriers to trade and restrain competition on domestic markets."<sup>29</sup>

The NTB/NTD debate has understandably divided observers of remedy policy into two camps. If it is not possible to distinguish non-arbitrarily between a significant and an insignificant distortion then almost anything can become a target. The United States has been suggesting in recent years, for example, that the Japanese language is a non-tariff barrier to trade and that the Japanese distribution system constitutes one huge non-tariff

distortion. The European Community has suggested that the homogeneous nature of the United States market may also be a non-tariff barrier to trade. By relying on a framework of free trade versus protection there is a tendency for the term unfair to become so broadened that it becomes meaningless.

One camp perceives trade remedy measures as means of eliminating non-tariff distortions. The other camp sees trade remedy measures themselves as important non-tariff distortions.

Yet, the two camps ostensibly aim for the same goal. They are both in pursuit of "free trade". The cause of free trade has been, as a former Chief Canadian trade negotiator has noted, "harnessed in the attack on "unfair" trade".<sup>30</sup> It has been the desire to eliminate NTB's and NTD's in the name of free trade which has led to changes being made to the trade remedy statutes. It is these changes, undertaken in the interest of free trade, that have rendered the statutes more trade-distortive than the practices they were meant to counter.<sup>31</sup>

## **NON-INTERVENTION VERSUS INTERVENTION**

Conceptualizing about the problem in terms of intervention versus non-intervention creates a similar confusion. The notion that perfect competition is an optimal condition has created the widely-held assumption that markets create order and intervention by governments in markets creates disorder. This notion leads many observers to comment that many of the ills in the international trade system are due to governments interfering in economic affairs. Dumping is practised, as we have seen, by firms, over whose actions governments have little control, and therefore is not relevant here. Although, think of how commonplace it is to hear, for example, accusations that "Japan dumps" or the "Europeans dump". Here are just a few examples of the non-intervention framework which demonstrate how commonly it is used.

Robert Keohane, "... the increasing involvement of governments in the operation of modern capitalists economies have created more points of potential friction."<sup>32</sup>

Paul Krugman, "The best government policy is non-intervention."<sup>33</sup>

Richard Gardner, "... the cause of peace is assisted by the reduction of government interference in economic life."<sup>34</sup>

William Cline, "An underlying cause of trade conflict is the (probably growing) tendency of government intervention in economic activity".<sup>35</sup>

Robert Gilpin, "Which will prevail -- national economic interventionism or the rules of the international market economy?"<sup>36</sup>

This way of thinking causes us to focus on the problem of intervention by governments. By conceptualizing in this way we assume that any government role in economic affairs, though it may be unavoidable, is not an optimal economic condition. This biases us against any government activity in economic affairs from the outset.

Such a conception is ridiculous. Trade remedy policy itself is an intervention by government. How can the problem be intervention by states in the economy when that is the very basis of organizing freer trade? Karl Polanyi articulated this point in 1937. "The road to the free market was opened and kept open by an enormous increase in continuous, centrally organized and controlled interventionism."<sup>37</sup> Not only are states and markets not opposed, but, he explains, "For as long as that system (the market system) is not established, economic liberals must and will unhesitatingly call for the intervention of the state in order to establish it, and once established, to maintain it"<sup>38</sup> Peter Drucker echoes this point. "Not only was it (the market) not opposed to a rule of the market; it required the development of such a rule."<sup>39</sup> William Corden explains: "The link between laissez-faire and free trade has been broken by this process."<sup>40</sup> Free trade requires intervention.

This is not a new idea. Even Adam Smith made clear that for market forces to function optimally governments had various roles to play.<sup>41</sup> Jagdish Bhagwati points out that "any sensible economist will point out the need to distinguish between those state interventions that correct market failure and those that create it."<sup>42</sup> However, making



this distinction has been a source of great aggravation to many earnest economists. It is notoriously difficult to distinguish between interventions which are undertaken for purely domestic reasons and those which have a distorting effect on international competition. An intervention to "correct" market failure can be (and usually is) perceived by others as a distortion.

## DEAD ENDS

Neither of these traditional ways of conceptualizing about remedy policy are capable of resolving our paradox. The United States uses remedy policy, itself potentially an NTB or NTD, to eliminate the NTB's/NTD's of unfair trade practices. Because all governments pursue some protection and all governments intervene, these frameworks only exacerbate what Susan Strange calls the "politics of blame"<sup>43</sup>. Everybody accuses everybody else, and all are "guilty" of protection and government intervention.

These frameworks do help us to identify that protection is occurring in various forms in the international trade system. But is this all we can say? Protectionism tends to be seen as the sickness rather than the symptom. Prolific calls are made to strengthen the international rules to prevent governments from engaging in protectionist practices. Since the remedy laws are perceived as competition policy measures similar calls are made to strengthen them too. But here our problem surfaces again. The problem is that by strengthening the remedy provisions the United States is undermining the international rule system. President Reagan struggled with this thin edge when he said;

"There's a fundamental difference between positive support of legitimate American interests and rights on world trade and the negative actions of protectionists. Free trade can only survive if all parties play by the same rules. " He went on, "Defending workers in industries from unfair and predatory trade practices is not protectionism. It's legitimate action under US and international law."<sup>44</sup>

## AN ALTERNATIVE FRAMEWORK: ECONOMIC STATECRAFT

Let us try instead the economic statecraft way of thinking. What are trade remedy laws actually used for? Remedy laws are instruments which are used to get others to change their behaviour. They are employed to get foreign actors to stop dumping and to stop subsidizing.

Trade remedy laws and policies are instruments of statecraft; they are means of conducting the affairs of state. David Baldwin developed the definition of statecraft employed here. He draws from the definitions a few other thinkers have produced in the field of international relations. According to Harold and Margaret Sprout,

"statecraft embraces all the activities by which statesmen strive to attain desired objectives vis-a-vis other nations, and/or international organizations".<sup>45</sup>

KJ Holsti further refines this definition to,

"organized actions governments take to change the external environment in general or the policies and actions of other state in particular to achieve the objectives that have been set by policy makers".<sup>46</sup>

David Baldwin enlarges upon these definitions. He includes non-state actors as "possible targets of influence attempts"<sup>47</sup> and he broadens changes in behaviour to include "beliefs, attitudes, opinions, expectations, and/or propensities to act."<sup>48</sup>

This concept of statecraft depends on a traditional understanding of power relations. The notion of power used here was developed by Robert Dahl in his work on domestic politics.<sup>49</sup> It is one of the simplest and most widely adopted usages. He argues that power is the ability of A to get B to do something B would not otherwise do.<sup>50</sup>

There are three elements in this notion of power. First, A, a state, uses a certain kind of policy instrument to commit the act of statecraft. Like Professor Baldwin we will rely on the fairly standard classification of foreign policy instruments Harold Lasswell created to distinguish between economic and non-economic. Baldwin points out that most activities by governments, indeed the organization of governments, correspond to this taxonomy. In World Politics Faces Economics<sup>51</sup> Lasswell devised a taxonomy which includes propaganda, diplomacy, economic statecraft, and military statecraft.

First, we must ask, A uses the economic policy instrument to do what? In this study we are interested in how A uses the policy tool to affect the flow of trade in goods and services. This accurately describes the purpose of trade policy. But, how is the flow affected? It is affected by changing B's behaviour.

Second, who is B? B is a foreign actor such as a state, a firm, etc. That is, the act is directed at some domain. Influence or power is exercised over that domain. Third, why is A influencing B? A attempts to get B to do something. Changing, or even maintaining, some dimension of B's actual or potential behaviour is what A attempts to achieve. A is able to change the trade flow in some way by changing B's behaviour.

This concept of economic statecraft implies that trade policy is, as Richard Cooper has argued, foreign policy.<sup>52</sup> Economic statecraft requires the use of economic, as opposed to military, policy tools. As such, it is foreign economic policy.

This term, foreign economic policy, is so widely used and so little defined that it is necessary to explain what is generally meant by it here -- especially since the economic statecraft definition differs from traditional definitions.

Robert Pastor has best described the different attempts to define foreign economic policy.<sup>53</sup> He cites (publishing in 1980) the lack of any "guide or conceptual framework"<sup>54</sup> which allows us to understand its "political process". Benjamin J. Cohen provides the "only attempt at definition" Pastor could find. Cohen defines it as "the sum of actions by the nation state intended to affect the economic environment beyond the national jurisdiction."<sup>55</sup> IM Destler, however, defines it as "government actions with important impact on US relations with other governments and on the production and distribution of goods and services at home and abroad."<sup>56</sup> Stephen D Cohen uses the term "international economic policy" instead of foreign economic policy because such policy "defies simple classification as "domestic" or "foreign".<sup>57</sup> It is what governments use to "to modify what would otherwise be the ways that goods, services and capital would flow across national boundaries if a completely free market situation prevailed."<sup>58</sup>

All of these define foreign economic policy in terms of its impact -- its economic impact. Baldwin contends that such definitions are simply useless, if not (one infers) actually silly. He wryly explains:

"Thus, a nuclear war could be labelled as "foreign economic policy" if it had any important side effects on foreign economic matters. **Any conception of foreign economic policy which cannot differentiate between nuclear attack and trade restrictions is hopelessly at odds with common usage.** Any conception of "policy" which ignores both means and ends is unlikely to be of much use in assessing the rationality of a given policy."<sup>59</sup>

Economic statecraft describes a method or means of conducting foreign economic policy. In this study we are looking at trade policy as an instrument of economic statecraft.

"In each case" of economic statecraft, Professor Baldwin makes clear, "a political act is taking place insofar as a state is attempting to affect the actual or potential behaviour of another international actor."<sup>60</sup> This idea of international politics is similar to the standard definitions of international politics offered in by specialists in international relations. For example, KJ Holsti explains that,

"the international political process commences when any state seeks through various acts or signals to change or sustain the behaviour of other states."<sup>61</sup>

AO Hirschman was, of course, the first to establish that this link between trade policy and politics holds true regardless of the structure of the trade system. He wrote,

"We have now reached the result that international trade remains a political act whether it takes place under a system of free trade or protection, of state trading or private enterprise, the most favoured nation clause, or of discriminating treatments."<sup>62</sup>

By thinking about remedy policy as an instrument of power, the use of which represents a political act, we are in immediate conflict not only with the traditional ways of conceptualizing about trade issues but also with standard treatments of remedy policy.

Let us take this second issue first since it can be dealt with more quickly. Trade remedy policy, if it is practised in accordance with theory, allows United States authorities to penalize the imported good, not the producer. The lack of legal jurisdiction forces the United States to offset the effect of the unfair trade practice, rather than to challenge the motives or actions of the perpetrator. To correct the trade distortion the duty should equal the degree of dumping or the amount of the subsidy. In this way the United States does

not challenge the actions or motives of foreign actors. But who bears the cost of the remedial action? The foreign actor bears the financial burden.<sup>63</sup> If nothing else the remedy allows the United States to create a pecuniary penalty.

Tariffs, duties and financial penalties are forms of economic statecraft. Although, they are always portrayed as being neutral as regards foreigners. It is usually emphasized that they are imposed for domestic reasons, to protect domestic interests. Klaus Knorr, for example, says:

"...protective tariffs may be introduced to the benefit of" domestic "interests". "Any effects on other states is purely coincidental; there is no intent to wield power internationally."<sup>64</sup>

However, it is difficult to identify any foreign policy undertaking which is not ultimately undertaken "for domestic reasons". It is worth quoting Baldwin at length on this point.

"American foreign policy makers do not -- generally speaking -- threaten the Soviet Union with nuclear attack solely, or even primarily, because of some sadistic desire to instill fear in foreigners. They do it because they believe -- rightly or wrongly -- that such threats make the domestic populace safer. 'In short they do it for domestic reasons.' Thus the logic of denying that protective tariffs are attempts to influence foreigners would require similar treatment of most other foreign policy undertakings. Almost everything would become a 'domestic matter' and precious little would be left of 'foreign policy'."<sup>65</sup>

In addition, the effect of the duty is to neutralize the practice. By eliminating the unfair advantage (through the application of a duty) the United States dissuades the foreign actor from continuing with the practice. Making the actor pay is a way of changing its behaviour. Dissuasion is an attempt to change behaviour. If the duty is larger, even much larger than the degree of dumping or the amount of the subsidy, then the dissuasion is even more powerful. So, the traditional treatments of remedy policy are not accurate insofar as they deny that the United States exercises power over others with remedy policy.

Now, to return to the first point. The first objection by most readers is probably going to be that "normal" trade relations between contracting parties to the GATT (this study focuses on these) ought not to be characterized in terms of statecraft or power. Keeping in mind that "the term normal is one of the vaguest and most equivocal we have in political economy"<sup>66</sup>, there is still no doubt that it is unorthodox to suggest that

international trade relations, particularly those among signatories to the GATT, can or should be viewed in terms of power. Charles Kindleberger sums up the traditional view.

"The glory of free trade is that it decentralizes decisions about trade to non-political levels."<sup>67</sup> "Intervention is inescapable in this view; the task is to keep it optimal and as free as possible of puerile political nonsense, such as the mercantilism which most of us harbour in our intuition".<sup>68</sup>

For those who subscribe to the traditional view, the argument that trade policy is a political act involving the use of power reminds of the days before the GATT rules were established. Albert O Hirschman said of that time, "the extensive use of international economic relations as an instrument of national power has been, together with a "war of nerves" one of the main characteristics of the period preceding the outbreak of the current war (World War Two)".<sup>69</sup> Economic destruction was wrought not just by military aggression during the first half of the 20th century but also because "all the weapons of commercial warfare were brought into play."<sup>70</sup>

It has long been believed that if states ceased to exercise power in international economic relations then unfettered market forces could bring prosperity. Klaus Knorr made this point most succinctly by claiming:

"It must be understood that after World War Two the world's leading trading countries, which are also the premier capitalist societies, agreed to disarm themselves regarding the power uses of trade .. between themselves".<sup>71</sup>

In his view free trade is disarmament. But, is it?

Power can be defined in a mind-boggling number of ways. It has been the subject of more scholarly work than any other theoretical concept for students of international relations. John Kenneth Galbraith comments on the futility of trying to discuss all the relevant literature on the subject in one study. Like him, this author does not pretend even to have read all of it; he remarked from his study of the subject that, "no life is that long."<sup>72</sup>

It is important to note, however, that until recent years the role of power within the realm of international economic relations has been relatively neglected by scholars, particularly by economists. Melville J Ulmer went as far as saying,

"Perhaps no subject in the entire range of the social sciences is more important , and at the same time, so seriously neglected as the role of power in economic life."<sup>73</sup>

Various attempts have been made to address this problem. Quincy Wright argued, not only do "the fields of politics and economics overlap" but "economics can be used as an instrument of politics".<sup>74</sup> Bertrand Russell was convinced that "Economics as a separate science is unrealistic, and misleading if taken as a guide in practice. It is one element -- a very important element -- in a wider study, the science of power".<sup>75</sup> EH Carr emphasized that "the science of economics presupposes a given political order and cannot be profitably studied in isolation from politics".<sup>76</sup> AO Hirschman demonstrated that "foreign trade can be used as an instrument of national power".<sup>77</sup> EH Carr concluded that "Power, which is an element of all political action, is one and indivisible. It uses military and economic weapons for the same ends." "In the long run one is helpless without the other."<sup>78</sup>

There has to date been no general acceptance among students of international relations of any framework which fully takes account of the role of power and politics in trade relations. Randall Bartlett, in his study of economics and power finds that economists too have attempted to address the role of power in economic affairs. "Yet they do so," he says "with no commonly accepted definition or understanding".<sup>79</sup> The application of the economic statecraft framework must thus be seen as an important innovation. It provides us with a way to think about trade relations that incorporates the role of power in economic affairs.

Even if the economic statecraft framework is accepted, the notion of power in economic affairs, even in the simple form of A exercising power over B, is nearly universally regarded as necessarily predatory rather than productive. Is this true? From his studies of the phenomena of power in economic life in 1944 J.B. Condliffe concluded,

"There seems no valid reason to regard power as necessarily malevolent rather than beneficent. Not the fact of power, but the use made of it, is significant for good or evil."<sup>80</sup>

Trade policy can be used to induce changes in foreign behaviour which engender order and prosperity. In contrast to Klaus Knorr, David Baldwin concludes,

**" ... rather than disarming itself, the United States used its policy of free trade to shape the postwar international political and economic order."**<sup>81</sup>

He continues,

**" ... trade policy -- at least from 1944 to 1962 -- was the principle economic technique of statecraft employed by American policy makers."**<sup>82</sup>

Professor Baldwin argues "that it is wrong to depict threats, coercion, punishment, conflict and power as peculiar to politics while viewing promises, rewards, cooperation and exchange as the special province of economics".<sup>83</sup>

Studies of trade remedy policy often rely on the distinction John Jackson makes between two "basic philosophies of methodology of international (trade) diplomacy". He says "rule diplomacy" in international trade is distinct from "power diplomacy". "Rule diplomacy is the technique of establishing international rules for the behaviour of governments and institutions that will ensure a certain measure of compliance with the rules." Power diplomacy, on the other hand, is diplomacy which occurs in the absence of rules (or effective rules) and is based more on the relative power position of the participants (national or other entities).<sup>84</sup> Such a distinction denies the possibility that power can be used to establish rules and to enforce them. For this reason it must be abandoned.

This point is crucial to this study. It is one thing if the United States is using power to compel foreign actors to abide by the internationally agreed-upon rules for international trade. Study of this use of power is worthy of students in the field of international relations if only to see how rules and order are maintained within the trade system. It is another thing altogether, however, if the United States is using power to compel those who are perpetrating unfair trade practices to engage in further anti-competitive behaviour, as in the case of unwarranted duties, especially excessive ones, or, orderly marketing arrangements, which, while not technically illegal according to the international rules, are fundamentally at odds with the competitive process. It is yet



something else if the United States uses remedy policy to label legitimate and normal foreign business practices "unfair" and on this pretext force foreigners to engage in anti-competitive behaviour. This last use of power is particularly of note since it is absolutely at odds with the foundation of the post-war international economic order -- competition. Clearly, power can be used to sustain or undermine the post-war international economic order.

Of course, there is no guarantee that the foreign actor will capitulate to the United States' demands in any given instance of economic statecraft. But, any firm or state that wishes to maintain access to the lucrative United States market will be susceptible to the United States' economic statecraft. Certainly a foreign firm or government must either comply with the finding made in any given AD or CVD investigation or its goods will be denied access. Firms and governments must avoid transgressing the laws if they do not wish to become entangled in an AD or CVD investigation. Therefore, they modify their behaviour to comply with the legal framework, even if there is no specific petition or investigation.

## **RETURN TO NON-TARIFF BARRIERS AND NON-TARIFF DISTORTIONS**

Remedy policy as an instrument of power and politics takes on great significance when we reexamine the NTB/NTD problem. The term non-tariff barrier to trade connotes a purely economic phenomenon, one which according to the traditional arguments ought to be minimized if not eliminated. But, is the economic description accurate or the only description possible? Working experience in NTB negotiations led a former United States Deputy Trade Ambassador, Harald Malmgren, to conclude;

"The NTB problem is essentially one of conflicting national economic and social policies".<sup>85</sup>

This, he says, is why NTB's cannot be reciprocally negotiated like tariffs. Efforts to eliminate foreign NTB's, therefore, are efforts to exercise power over the economic and

social policies of foreign states and over the production and pricing strategies of foreign firms.

The political implications of the American use of remedy policy can no longer be ignored because remedy policy has shifted, or been transformed. Avinash Dixit has "argued that a broader interpretation is necessary to encompass precautionary actions undertaken in anticipation of others' policies and strategic moves like threats and promises intended to alter their future choices."<sup>86</sup> This broader interpretation has already occurred. Remedy policy is often used to preempt foreign behaviour and to change it.

Matthew Marks and Harald Malmgren together sketched out the political issue.

**"The central substantive problem will be in defining which domestic economic measures are legitimate, in view of their international trade repercussions and those which are not. How far into these questions can one penetrate without overstepping the bounds of national sovereignty?"<sup>87</sup>**

Richard Cooper too made this point clearly when he said:

**"... the central problem of international economic cooperation.....is how to keep the manifold benefits of extensive international economic intercourse free of crippling restrictions while at the same time preserving a maximum degree of freedom for each nation to pursue its legitimate economic objectives"<sup>88</sup>**

The traditional methods of conceptualizing, as noted earlier, lead us into a classification exercise. This task has substantially widened the list of NTB's, which is now so broad as to include practices which are normal and legitimate in the country in which they occur. In taking action against foreign actors the United States challenges the legitimacy of their actions. The danger is that United States remedy policy increasingly oversteps the bounds of foreign autonomy and sovereignty.<sup>89</sup> For example, in a recent study two Canadians, Smith and Lipsey, explain that "...the target of US countervailing duties is shifting from specific, clearly trade-distorting subsidies to policies that are more general."<sup>90</sup> They continue, "In this broadening of the scope of countervail, many Canadians see the current US approach as a direct attack on their sovereignty". So we see that the NTB problem is a political problem, not just an economic one. But, the traditional arguments obscure this from view.

More important, the traditional arguments lead us in the direction of one obvious but dangerous conclusion. Is the answer to "harmonize" domestic institutions? This option requires broadening of the reach of remedy policy on foreign sovereignty and autonomy, perhaps a dangerous course to pursue in the post-war international trade system. For example, another international economic order, the 19th century gold standard, owed its downfall in major part, according to Karl Polanyi, to this problem of autonomy and sovereignty in economic affairs. Under the gold standard states had no powers in trade or monetary affairs as they were "bound" by the gold standard. The "anarchistic sovereignty" which occurred through the "enforced uniformity of domestic systems hovered as a permanent threat over the freedom of national development..."<sup>91</sup> He believed that with the disappearance of the gold standard it would:

"... become possible to tolerate willingly that other nations shape their domestic institutions according to their inclinations, thus transcending the pernicious nineteenth century dogma of the necessary uniformity of domestic regimes within the orbit of the world economy"<sup>92</sup> Through this process two "cornerstones of the New World can be seen to emerge: economic collaboration of governments and the liberty to organize national life at will".<sup>93</sup>

Perhaps the developments in American trade remedy policy being addressed here are symptomatic of a much bigger problem. The United States may no longer be willing to tolerate the ways in which foreign governments and firms behave in their domestic environment.

States may choose to alter their domestic structures in order to collaborate with other states. The member countries of the European Community, for example, have all chosen to limit their sovereignty and autonomy to some degree. In contrast, the use of remedy policy by the United States challenges this liberty of choice. With remedy policy the United State unilaterally forces changes in behaviour. Thus AD and CVD policy poses a threat to sovereignty and autonomy if used to compel foreigners to do things which they do not want to do. Such infringement is warranted, even necessary, in order to maintain the post-war international economic order if the US is compelling others to abide by the internationally agreed-upon rules of the international trade system. But, such

infringement is dangerous if the US is requiring that foreigners behave in a manner which undermines the rules of the international trade system.

If harmonization of domestic structures and ideology is a prerequisite for international diplomacy then the international trade system is in even more trouble than is commonly thought. After all, the world consists of a variety of states<sup>94</sup>. The ideological and practical differences among the GATT signatories about the appropriate role of government in economic affairs, the "best" methods of regulating the economy, the "best" economic outcome vary profoundly.

When states conflict over trade issues, particularly over what constitutes an "unfair" trade practice, the conflict arises from their differing views about what is economically normal, legitimate and desirable. The United States and the European Community, for example have profound differences over the legitimacy and desirability of the Airbus project, standards for pollution control, of inflationary economic policies. Henry Kissinger's comments on diplomacy seem hauntingly relevant even though he was referring to the East-West conflict during the cold war.

"When domestic structures -- and the concept of legitimacy on which they are based -- differ widely, statesmen still meet, but their ability to persuade has been reduced as they no longer speak the same language"<sup>95</sup> "Ideological conflict compounds these instabilities....A similar outlook about aims and methods eases the tasks of diplomacy -- it may even be a necessary pre-condition for it. In the absence of such a consensus diplomats can still meet, but they lose the ability to persuade. More time is spent on defining contending positions than in resolving them. What seems reasonable to one side will appear most problematical to the other."<sup>96</sup>

This is an accurate description of non-tariff barrier negotiations. The acrimony which arises from allegations of unfair trade practices is symptomatic of these differences of opinion, perception, and ideology. What seems to be a legitimate and non-negotiable domestic structure to one state often appears problematic and negotiable to the other.

## ELUSIVE SOLUTIONS

Faced with such an intractable problem -- after all, how is it possible to "harmonize" policies, priorities, institutions and economic structures of many different states -- it seems that the only available solution is, in response to prolific calls, to strengthen the international rules. But, international rules and international organizations are only as powerful as the member states allow them to be. Though an unpopular view this has long been acknowledged by those closest to trade policy in practice and by more pragmatic observers. Even Richard Gardner, one of the earliest commentators on the post-war trade system, whose book Sterling Dollar Diplomacy traces the origins of international attempts to regulate trade after the Second World War, was convinced of the correctness of this view. Confidence that legal structures could and would bind states with legal chains, a phenomenon which he called "legalism", was an "error which underlay wartime and post-war economic diplomacy".<sup>97</sup>

Even if the rules could be made more binding would the post-war trade system be based on free trade or on a philosophy of no intervention? A careful examination of the post-war international economic order, how the rules work, the underlying philosophy, further strengthens the case for the economic statecraft argument.

1. The whole doctrine of comparative costs is nothing but an academic dilution of this [a] short and obscure footnote by Ricardo." Charles Gide and Charles Rist, A History of Economic Doctrines from the Time of the Physiocrats to the Present Day, (London: George Harrap and Co. Ltd., 1915) page 646.
2. James Brander, "Rationales for Strategic Trade and Industrial Policy" Strategic Trade Policy and the New International Economics, Paul Krugman, ed., (Cambridge: MIT Press, 1986). "Specifically there is an international market for some good or closely related set of goods, but there are relatively few firms in the market. As a consequence it is possible for firms to earn profits above the rate of return earned in purely competitive industries. Trade policy then emerges as a national attempt to obtain as large a share of these international profits as possible. In effect trade policy by other countries might enable them to capture returns that would otherwise accrue to the US, or US policy might allow the US to capture returns that would otherwise go elsewhere." Page 25.
3. Stephen Magee, William A Brock and Leslie Young, Black Hole Tariffs and Endogenous Policy Theory: Political Economy in General Equilibrium, (Cambridge: Cambridge University Press, 1989) page 1.
4. It tends to be assumed that the firm is able to charge a high price domestically because the market is protected from competition, namely import competition, thus implying further "unfairness".
5. These are offered in chronological order.
6. Peter Kenen, The International Economy (New Jersey: Prentice-Hall, 1985) page 229.
7. It has been estimated that well over 90% of the United States' federal revenue came from tariffs before the creation of a federal income tax. EE Schattschneider explains that the Democratic Party's main platform on trade was that tariffs should exist only for the purpose of revenue from 1876 to 1920. The Republican platform from 1860 until 1912 supported tariffs for revenue and for the purpose of protecting American industry. EE Schattschneider, Politics, Pressures and the Tariff, (New York: Prentice Hall, 1935) page 8, Note 3.
8. Evidently, foreigners were thought to be undervaluing their exports so as to reduce the payable duty. This reduced the federal revenue.
9. Remarks by Harvey M Applebaum, Interface One, Conference Proceeding on the Application of Antidumping and Countervailing Duty Laws to Imports from State Controlled Economies and State-Owned Enterprises, Don Wallace Jr., et. al., eds., (Washington: Institute for International and Foreign Trade Law Georgetown University, 1980) page 153.
10. Copyright and patent infringement, for example.
11. General Agreement on Tariffs and Trade: What it is and What it Does. GATT Secretariat, 1984, page 14.
12. 131 Congressional Record 315315 (daily edition Nov. 13, 1985) Statement of Senator Hollings.
13. Peter Drucker, "The Changed World Economy" Foreign Affairs Spring 1986.

14. Robert E Baldwin, "The New Protectionism: A Response to Shifts in National Economic Power", The New Protectionist Threat to World Welfare, Dominick Salvatore ed., (New York: North-Holland, Elsevier Science Publishing Company, 1987) page 104.
15. EH Carr, The Twenty Years Crisis:1919-1939 (London: Macmillan, 1939, second edition 1946 reprint in 1984), page 7.
16. Adam Smith, An Inquiry into the Nature and Causes of the Wealth of Nations, RH Campell, AS Skinner ed.s., (Oxford: Clarendon Press, 1976) Vol. 1, page 471.
17. Economist "The Ravishing of Free Trade" March 25, 1989, page 13-14.
18. Arjo Klammer, Donald N McCloskey and Robert M Solow, ed.s., The Consequences of Economic Rhetoric (Cambridge: Cambridge University Press, 1988).
19. Because it is more efficient means of distributing resources and therefore leads to the creation of greater wealth.
20. Gary Clyde Hufbauer "Subsidy Issues After the Tokyo Round" Trade Policy in the 1980's (Washington, D.C.: Institute for International Economics, 1983).
21. Robert Baldwin, Non-Tariff Distortions in International Trade (Washington, D.C.: Brookings Institution, 1970) page 5.
22. EM Winslow "Administrative Protectionism: a Problem in Commercial Policy" Explorations in Economics: Notes and Essays in Honour of FW Taussig (New York: McGraw-Hill, 1936) page 179.
23. *ibid.*, page 181.
24. *ibid.*, page 180.
25. *ibid.*, page 187.
26. Joseph Grunzel, Economic Protectionism (Oxford: Clarendon Press, 1916) page 179.
27. Jagdish Bhagwati, Protectionism (Cambridge, Massachusetts: MIT Press, 1988).
28. Douglas Nelson, The Political Structure of the New Protectionism World Bank Staff Working Paper No. 471, 1981, page 3.
29. Competition and Trade Policies: Their Interaction (Paris: OECD, 1984) page 13.
30. Rodney Grey, Trade Policy and the System of Contingency Protection in the Perspective of Competition Policy, unpublished paper Commissioned by the OECD, Paris 1986.
31. John Barcelo, "Antidumping Laws as Barriers to International Trade -- The United States and the International Antidumping Code" Cornell Law Review Vol 57, No. 4, April 1972, page 494.
32. Robert Keohane, After Hegemony (Princeton: Princeton University Press, 1984) page 5.

33. Paul Krugman, ed., Strategic Trade policy and the New International Economics (Cambridge: MIT Press, 1988) page 23.
34. Richard Gardner, Sterling Dollar Diplomacy (New York: McGraw-Hill, 1969) page 15.
35. William Cline, "Introduction and Summary" Trade Policy in the 1980's (Washington, D.C.: Institute for International Economics, 1983) page 26.
36. Robert Gilpin, The Political Economy of International Relations (Princeton: Princeton University Press, 1987) page 63.
37. Karl Polanyi, The Great Transformation: the Political And Economic Origins of Our Time, (Boston: Beacon Press, 1957, 2nd reprinting 1962), page 140. WM Corden too has explained the break between free trade and laissez-faire in Trade Policy and Economic Welfare (Oxford: Oxford University Press, 1974).
38. Karl Polanyi, The Great Transformation, page 143.
39. Peter Drucker, The End of Economic Man (London: William Heinemann, 1943) page 40.
40. William M Corden, Trade Policy and Economic Welfare, page 4.
41. Adam Smith, Wealth of Nations, Vol. 2, page 723. Full quote is given at note 58 Chapter 7 page 186 infra.
42. Bhagwhati, Protectionism, page 126.
43. Susan Strange often made this comment in her lectures at the London School of Economics.
44. President Ronald Reagan, "The Trade Challenge for the 1980's", March 4 1983, speech before the Commonwealth Club San Francisco California, Current Policy No. 463, US Department of States Bureau of Public Affairs.
45. Harold and Margaret Sprout, Toward a Politics of the Planet Earth (New York: Van Nordstrand, 1971) page 135.
46. KJ Holsti, "The Study of Diplomacy" World Politics JN Rosenau, KW Thompson, ed.s., (New York: Free Press, 1976) page 293.
47. David Baldwin, Economic Statecraft, page 9.
48. *ibid.*, page 9.
49. Robert Dahl, Modern Political Analysis (New Jersey: Prentice Hall, 1963, third edition 1976).
50. This includes changing or maintaining a behaviour.
51. Harold Lasswell, World Politics Faces Economics (New York: MacGraw-Hill, 1945) page 9.
52. Richard N Cooper, "Trade Policy as Foreign Policy" Foreign Policy, 9 Winter 1972-73.



53. Robert Pastor, Congress and the Politics of US Foreign Economic Policy: 1929-1976, (Berkeley: University of California Press, 1980) pages 7-12.

54. *ibid.*, page 8.

55. Benjamin J Cohen, American Foreign Economic Policy: Essays and Comments (New York: Harper and Row, 1968) pages 1, 10.

56. IM Destler, Making Foreign Economic Policy (Washington, DC: Brookings Institution, 1980) page 7.

57. Stephen D Cohen, The Making of United States International Economic Policy: Principles, Problems and Prospects (New York: Praeger, 1988) page xi.

58. *ibid.*, page 3.

59. David Baldwin, Economic Statecraft, page 34.

60. *ibid.*, page 42.

61. KJ Holsti, International Politics: a Framework for Analysis (New York: Prentice-Hall, 5th edition, 1988) page 141.

62. Albert O Hirschman, National Power and the Structure of Foreign Trade (Berkeley: University of California Press, 1945), page 78.

63. It should be noted here that a distinction is made between a foreign exporter and the domestic importer. It is possible that the domestic importer has to pay the duty because it has purchased the goods prior to their arrival in the United States. Although, usually the domestic importer, if unrelated to the exporter, demands reimbursement from the foreign exporter. If the domestic importer is related to the exporter (let's say a subsidiary of a German automobile manufacturer) then the foreign firm is still having to pay.

64. Klaus Knorr, The Power of Nations: The Political Economy of International Relations (New York: Basic Books, 1975) p. 80.

65. David Baldwin, Economic Statecraft, page 49.

66. Charles Gide and Charles Rist, A History of Economic Doctrines from the Time of the Physiocrats to the Present Day, (London: George Harrap and Co. Ltd., 1915) page 280.

67. Charles Kindleberger, Power and Money: The Politics of International Relations and the Economics of International Politics (New York: Basic Books, 1975) page 12.

68. *ibid.*, page 132.

69. A.O. Hirschman, National Power and the Structure of Foreign Trade, p. ix.

70. Clair Wilcox, A Charter for World Trade (New York: Macmillan, 1949) pages 5-9.

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72. John K Galbraith, The Anatomy of Power, (London: Hamish Hamilton, 1974) see the foreword.

73. Melville J Ulmer, "Economic Power and Vested Interests" Power in Economics KW Rothschild ed., (Harmondsworth, England: Penguin Books, 1971) page 245.
74. Quincy Wright, A Study of International Relations (New York: Appleton, 1955) page 239.
75. Bertrand Russell, Power: a New Social Analysis (New York: WW Norton, 1938) page 135.
76. EH Carr, The Twenty Years' Crisis, page 117.
77. AO Hirschman, National Power and the Structure of Foreign Trade, page 13.
78. EH Carr, The Twenty Years Crisis, page 132.
79. Randall Bartlett, Economics and Power: an Inquiry into Human Relations and Markets (Cambridge: Cambridge University Press, 1989) page 7.
80. J.B. Condliffe, The American Economic Review, "Economic Power as an Instrument of National Policy" Volume XXXIV, No. 1, Supplement, Part Two, March 1944, page 306.
81. David Baldwin, Economist Statecraft, page 46.
82. *ibid.*, page 207.
83. David Baldwin, Paradoxes of Power (Oxford: Basil Blackwell, 1989) page 5.
84. John J Jackson, "GATT Machinery and the Tokyo Round Agreements" Trade Policy in the 1980's, William Cline ed., (Washington D.C.: Institute for International Economics, 1983) page 160.
85. Harald B Malmgren, Economic Peacekeeping in Phase II (New York: Quadrangle Books, 1972), page 85.
86. Avinash Dixit, "How Should the United States Respond to Other Countries Trade Policies?", US Trade Policies in a Changing World Economy, Robert M Stern ed., (Cambridge: MIT Press, 1987) page 265.
87. Harald B Malmgren and Mathew Marks, "Negotiating Nontariff Distortions to Trade" Law and Policy in International Business, Vol 7, No. 2, 1975, page 329.
88. Richard Cooper, The Economics of Interdependence: Economic Policy in the Atlantic Community (New York: McGraw-Hill, 1968) page 5.
89. Richard Cooper distinguishes between these two. "National autonomy is used here to mean the ability to frame and carry out objectives of domestic economic policy which may diverge widely from those of other countries". This is not to be "confused with the notion of sovereignty, which represents the formal ability of countries or other political units to make their own decisions -- and renounce decisions previously made -- but not necessarily to achieve their objectives". *Ibid.*, page 4.
90. Murray Smith and Richard Lipsey of the CD Howe Institute quoted by Bob Vincent, "US Criticized for Interpretation of Trade Laws" Financial Times, Wednesday July 15, 1987.
91. Karl Polanyi, The Great Transformation, page 253.

92. *ibid.*, page 253.

93. *ibid.*, page 254.

94. James Mayall, "The Variety of States" The Condition of States Cornelia Navari ed., (Milton Keynes: Open University Press, 1991).

95. Henry Kissinger, American Foreign Policy, (New York: WW Norton and Co., Inc, 1977)  
page 12.

96. *ibid.*, page 55.

97. Richard Gardener, Sterling-Dollar Diplomacy, page xxxviii.

## **CHAPTER THREE -- THE POST-WAR INTERNATIONAL ECONOMIC ORDER**

The central problem this study addresses centres on order within the post-war trade system. America's paradoxical use of the AD and CVD laws stands as a threat to the post-war international economic order. So, it is necessary to explain what is meant by order, to describe its role and form. Certain terms need to be defined, working assumptions about the nature of the international trade system made clear. This exercise will help clarify the limitations and strengths of the three frameworks: free trade versus protection, intervention versus non-intervention and economic statecraft.

### **INTERNATIONAL TRADE SYSTEM**

What do we mean by international trade relations? Essentially relations occur among two actors: private parties (firms and individuals) and governments.

Adam Smith said "The propensity to truck, barter and exchange one thing for another ... is common to all men".<sup>1</sup> Such transactions between private parties occurring across national borders constitute international trade. International relations at this level occur, on the whole, between non-state actors. Joe Bloggs in Chicago sell his widgets to Ralph Schmidt in Bavaria. Or, General Electric Co. of the United States sell refrigerators to the French public. Governments, on the whole, do not engage in commercial transactions.<sup>2</sup> This is especially true of GATT signatories.<sup>3</sup>

Governments do, however, attempt to control or influence private transactions by using (among other mechanisms) national trade laws and trade policies. At this level governments interact with private persons. Firms are considered persons under US law. Private international trade law is the term used to describe those nationally legislated laws which regulate the actions of private persons in international commercial transactions. The "essential object of private international law" Clive Schmitthoff, a leading scholar of

international trade law, makes clear, is "a body of rules applicable to private persons in their international relations."<sup>4</sup>

For the United States Government the trade laws provide the statutory foundation upon which trade policy is made. Trade policy is generally defined broadly, as is done by IM Destler: "all actions of the US government directly affecting the movement of goods between nations."<sup>5</sup> Benjamin Cohen adds to this definition state actions "intended to affect the extent, composition and direction of its imports and exports of goods and services."<sup>6</sup> These definitions are so broad that, for example, the United States' attempt to reduce its bilateral trade deficit with Japan by manipulating the Yen Dollar exchange rate in 1983 is an example of trade policy. This, however, is a borderline case. Our concern is with two traditional trade policy instruments -- antidumping and countervailing duty measures. Trade remedy policy serves to affect the movement of goods (in some cases also services), and the terms of their movement.

International relations in commercial affairs also occur between governments. William Linglebach said in 1930;

"The political consequences of economic policies are not always easy to determine or estimate. Nevertheless, it has been fairly generally accepted by historians that commercial policies and the control of imports and exports through tariffs and other devices have been a fruitful source of international friction and even of war."<sup>7</sup>

That is to say when statesmen use trade policy to achieve incompatible goals conflict can arise. Equally, harmony can be produced when statesmen seek mutually beneficial goals and they coordinate their trade policies. To this end states have attempted to reach agreement about how states can regulate trade.<sup>8</sup> Internationally negotiated agreements serve this purpose.

Together, these three variables combined create the international trade system: private international trade transactions, state attempts to influence these transactions (private international trade law and foreign economic policy) and the international attempts to regulate national trade policies (international trade law and diplomatic arrangements).

Systems, in international relations, are characterized by the fact that some relationship exists between the variables<sup>9</sup>. But, a mere relationship is not sufficient to create or sustain order in a system. Students of international relations, for this reason, have traditionally been concerned with rules, laws, and norms, as well as the causes and management of conflict and cooperation in international systems.<sup>10</sup>

Order, in international relations, depends largely on agreement about methods and objectives. It is well known that law alone cannot create order.<sup>11</sup> The international community creates laws and rules to uphold what Henry Kissinger describes as a "legitimacy". He defines this as;

"no more than an international agreement about nature of workable arrangements and about the permissible aims and methods of foreign policy."<sup>12</sup>

That the system of rules in this instance addresses economic aspects of foreign policy does not render this usage less valid. Legitimacy, rests on consensus about the goals states seek to achieve. Hedley Bull, a lifelong student of order in international relations, in a similar fashion emphasized that order is:

"a pattern of activity that sustains the elemental or primary goals of states."<sup>13</sup> However, "common interests in achieving the elementary goals of social life may be vague and inchoate, and does not in itself provide any precise guidance as to what behaviour is consistent with these goals and what behaviour is not." "Order in any society is maintained not merely by a sense of common interests in creating order or avoiding disorder, but by rules which spell out the kind of behaviour that is orderly"<sup>14</sup>

Order, orderly relations is, ultimately, what a legitimacy for commercial affairs is established to engender. International trade can flourish, it is supposed, in a stable and predictable environment in which private parties can do business. States want to encourage the creation of wealth for their nationals and, at the same time, presumably, hope to avoid conflict with other states over the methods they have chosen to encourage the creation of wealth. Sterling-dollar diplomacy, for example, was "a shorthand designation for the struggle to build a viable world economic order."<sup>15</sup> Place the emphasis on the word "viable". There are some "orders" that are not viable.

A primary goal of economic order is that it ought to result in the generation of wealth and prosperity and a rising standard of living. Sometimes we forget that

historically there have been different conceptions about how to achieve these goals. For example, when post-war planning began<sup>16</sup> Winston Churchill argued that the Imperial Preference system should be maintained, although the Americans wanted an open trade system based on non-discrimination. He felt an economic order which gave Britain preferential access to trade was better for Britain than one that did not. Remember also that fascist economic nationalism was "paraded by German economists as more stable, efficient, and rational in its operation than the anarchy of competing private enterprise and the non-regulated international economics of free multilateral trading."<sup>17</sup> J B Condliffe called the battle between differing conceptions of economic order "the real economic war."<sup>18</sup>

To be "viable" the choice of an economic order must sustain the desired political order. The question of who has access to rising standards of living and the gains from trade must be addressed in the construction of economic order. Peter Drucker pointed out in the late 1930's that the Germans and Soviets challenged the interwar economic order partly because they believed their access to the gains from trade was limited by then existing colonial preferential trading systems.<sup>19</sup>

A good description of the order that was adopted in the post-war period, the one we live under now, was offered by The Economist in 1942. It described the United States proposals as,

"a genuinely new conception of world order. It is an inspiring attempt to restate democracy in terms of the twentieth century situation, and to extend its meaning in the economic and social sphere."<sup>20</sup>

It is based on the dynamic of free and fair competition which is itself predicated on the efficacy of market forces.<sup>21</sup> Market forces are freed by reducing barriers to trade. The gains from trade made possible by this are open to all nations as long as they adhere to certain rules of competition. The political foundation of this concept of order is that all states have an equal opportunity to reap the gains from trade. They do not all have the same ability, but they have similar opportunities.

Standard descriptions of the post-war international economic order echo these points. For example Gottfried Haberler describes it as follows.

"By liberal order we mean the order of the market or capitalist economy, of the modern mixed variety, relying predominantly on private enterprise and competition ..." He continues: "More specifically, the liberal international economic order is the largely American-inspired post-World War Two system of freer trade, of low, nondiscriminatory tariffs (most-favoured nation clause and the absence of quantitative restraints), and of currencies freely convertible into each other in the exchange market at either fixed or variable exchange rates (absence of exchange control) -- the system symbolized and institutionalized by the GATT and the International Monetary Fund."<sup>22</sup>

When we speak of the "rules" of international trade we refer to the complex of internationally negotiated agreements centred on the General Agreement on Tariffs and Trade but also including treaties, protocols, codes and letters of understanding and interpretation (both formal and informal) which together provide the framework for national regulation of international trade. This serves as a guide for governments in their choice and use of trade policy. These rules set out the legitimate aims and methods of national trade policy.

The GATT, the Antidumping Code<sup>23</sup> and the Subsidies Countervail Code<sup>24</sup> are the international agreements (relevant to this inquiry) which set out which policy tools can be used, and how governments can use them.

## GENERAL AGREEMENT ON TARIFFS AND TRADE

For those countries which are party to it the General Agreement on Tariffs and Trade is the central element of the complex of international trade law. It is the cornerstone upon which the "architects", as the post-war planners were called, attempted to build a viable post-war economic order.

Though, as a cornerstone, the GATT is only a rather whittled down leftover from the Havana Charter<sup>25</sup>. The Charter was intended to be the foundation for the International Trade Organization. But, the Charter was never realized.<sup>26</sup> It was so dense with obligations and constraints that the United States Congress failed to ratify it.<sup>27</sup>



Parts of it were salvaged, namely the chapter on commercial policy. This provided the anchor for the GATT. The General Agreement itself emerged from a bilateral reciprocal tariff cutting exercise which had begun in 1947<sup>28</sup>. Together these two ingredients were forced together by necessity and by the absence of an alternative to create the Provisional Protocol of the General Agreement on Tariffs and Trade. It entered into force in January 1948. The protocol is genuinely provisional.<sup>29</sup> This is why the signatories to it are called contracting parties. This is also why contracting parties are not fully bound by the text on every occasion.

The GATT is a diplomatic arrangement. As such, the GATT does not deprive states of policy instruments but rather sanctions the use of tools and principles and procedures which utilize the market mechanism. It discourages the use of those instruments which undermine the market mechanism, such as quotas. Thus, the GATT represents an accumulation of attempts to regulate the ways in which national trade policy is used rather than proscribe the use of national trade policy. Protectionism is not prohibited, nor is free trade required under its terms. Rather it distinguishes between pro-market and anti-market tools.

It was agreed that certain policy tools, namely tariffs, were legitimate even though, technically, they constitute protection. Recent publicity from the GATT Secretariat explicitly states;

"Where protection is to be given to a domestic industry, it should be extended essentially through a customs tariff, and not through other commercial measures (emphasis added). Among other things the aim of the rule is to make the extent of protection clear."<sup>30</sup>

The GATT neither intends a free trade system nor one which denies government a role in the regulation of commerce. Rather, it is a diplomatic arrangement which sets out the legitimate aims and methods of national trade policy. That is to say that the GATT does not eliminate power or politics from the international trade system. Economic statecraft is merely limited to legitimate activities. Legitimacy is accorded to those aims and methods which employ and enhance the market mechanism and which apply the principle of non-discrimination, national treatment, most-favoured nation treatment and

which do not violate national sovereignty. Influence and power are an integral part of the trade system in that some states may need to be persuaded to behave in a manner conducive to market forces and to be dissuaded from behaving in ways which undermine market forces.

We see that the GATT is not a free trade agreement, as it is often portrayed, but rather a diplomatic agreement about how states may legitimately regulate trade affairs. This interpretation is supported by the fact that certain principles are endorsed under the Agreement to allow all parties like access to the benefits of competition. The GATT is designed, John Ruggie tells us, to promote "non-discrimination and multilateralism rather than the complete abandonment of national controls over trade barriers".<sup>31</sup> The most-favoured nation principle, in unconditional form under the GATT, allows all states to benefit from reductions of tariff barriers by any single state. The principle of non-discrimination holds that a state may not discriminate among nations in taking action against imports. National treatment means that once goods have entered the domestic market they are treated similarly to domestic goods. In the same vein, the GATT seeks the gradual reduction of tariffs but not their elimination.<sup>32</sup> This would deprive states of one of the most important legitimate tools they have for regulating trade.

So, legitimate protectionism is allowed. Illegitimate protection is discouraged. John Ruggie, for this reason, correctly describes the GATT system as one of "embedded liberalism."<sup>33</sup>

Finally and most importantly, state sovereignty is protected under the GATT system. Harry Hawkins, the principle United States trade negotiator and post-war planner made clear that no state would join if a promise to give up sovereignty was necessary. The "escape clauses" were included into the GATT for this reason. These effectively allow contracting parties to escape their international obligations if domestic circumstances require it.

The pragmatic conception of the trade system that has been sketched out above renders one of the great "puzzles"<sup>34</sup> about the GATT more understandable. Even if the

international rules could be strengthened this would not necessarily strengthen order in the international trade system. **This is because the rules are often not enforced as they are written.** Some observers of the GATT have never been able to understand why this is so. If we view the GATT as a diplomatic arrangement it makes more sense. The procedures for enforcing the obligations are deliberately "fraught with ambiguity".<sup>35</sup> "The point", according to the GATT scholar Robert Hudec, is "that these legal obligations were not meant to be enforced to the letter."<sup>36</sup> "The key to understanding the GATT legal system is to recognize that GATT's law has been designed and operated as an instrument of diplomacy."<sup>37</sup> Therefore it is wrong to believe that the GATT or other international arrangements describe the actual nature of the international trade system. Instead, we must consider international arrangements as they are applied, not as they are written. As an example, the GATT defines dumping, but it is the United States' interpretation of that definition which is used to enforce the rule.

It is useful to know that there is no requirement that the United States abide by the Antidumping Code, the agreement negotiated in 1967 and 1979 which elaborates on the GATT and most explicitly sets out what has been agreed internationally on dumping and the use of antidumping measures. Under United States law the administering agencies are directed to:

**"resolve any conflict between the International Antidumping Code and the Antidumping Act, 1921, in favour of the Act as applied by the agency administering the Act." (emphasis added)**<sup>38</sup>

**"Nothing contained in the International Antidumping Code ... shall be construed to restrict the discretion of the ... Tariff Commission in performing its duties and functions under the Antidumping Act." (emphasis added)**<sup>39</sup>

Administering agencies are directed to,

**"take into account the provisions of the International Antidumping Code", but "only insofar as [Code provisions] are consistent with the Antidumping Act 1921." (emphasis added)**<sup>40</sup>

John Barcelo points out that the real issue is not a conflict of differing language, the words in the Code and domestic AD law are the same, but of interpretation.<sup>41</sup>

## SAFEGUARDS

The safeguard clauses are a perfect example of the flexibility<sup>42</sup> inherent in economic diplomacy. As we have seen, the GATT system was constructed so as to avoid infringements upon states' sovereignty. Clearly membership in the GATT system implies a certain degree of acceptance of market principles; one can assume a certain harmony of interests among the members. But, actions taken by a state which are not in conformity with the rules are treated under the GATT but not necessarily challenged or eliminated. Hence, the "offsetting" procedure which trade remedy policy incorporates is consistent with the principle of sovereign freedom the GATT recognizes. Trade remedies allow a state to offset the margin of dumping or subsidization of an import at the border, thus neutralizing the unfair trade practice without directly challenging the actor who perpetrated it.

It was clear to the architects of the GATT agreement that if keeping GATT obligations meant a country's domestic industry might sustain injury, then governments must be allowed to deal with the problem through some action, even if only temporarily. Otherwise further tariff liberalization becomes politically unsustainable. Similarly, without a means of reneging on obligations at least temporarily, states would be reluctant to commit to any agreement. Article XIX, entitled "Emergency Action on Imports of Particular Products" allows states to "impose import restrictions or suspend tariff concessions on products which are being imported in such increased quantities and under such conditions that they cause or threaten to cause serious injury to competing domestic producers".<sup>43</sup> There is a trade remedy law in the United States which corresponds to the escape clause. It is called section 201. It allows the United States to take action against fair imports under these circumstances.

Of course there is a price to be paid for taking such action. That price is the payment of compensation to those countries whose benefits under the Agreement are

"nullified or impaired" by it. If there is no agreement about compensation then countries affected can retaliate.

While the United States has invoked this clause more often than most contracting parties it has also pioneered the development of "surrogates" for the Article XIX actions. Instead of applying an across-the-board tariff to the import in question or withdrawing a tariff concession, the United States often negotiates an orderly marketing arrangement with the principal supplier countries. The importers agree under such an arrangement, for example, to change their price (usually to raise it) or limit the amount of their exports. Surrogates are often referred to as gray area measures because they do not explicitly violate the GATT Agreement but they are discriminatory and often take the form of a quantitative restrictions. Surrogates are of particular interest to us because the antidumping, countervailing duty and market opening provisions are often used to implement such gray area measures.

Alan Wolff, a former United States Trade Negotiator, explains why surrogates developed.<sup>44</sup> Firstly, the United States does not want to have to pay compensation or accept retaliation for limiting imports. Second, it does not want to appear to be protectionist and reneging on obligations gives that impression. The foreign policy "cost" of admitting inability to cope with an import problem is often very high. But more significantly, escape clause actions do not allow discrimination. While it is possible to target a select group of imports, such as milk coming only from cows which graze above one altitude and not below another, it is not acceptable to discriminate between countries of origin, such as between Belgian and Canadian milk. For these reasons United States negotiators have creatively taken advantage of the safeguard loophole to achieve policy that circumvents the rules.

Where article XIX describes a situation involving import problems generally (fair imports which cause injury) the antidumping and subsidy article (Article VI) spells out how states may deal with the problem of "unfair" imports. The loopholes inherent in this article are even more flexible than in Article XIX.

Article VI of the General Agreement allows states to impose antidumping duties (a tax) on certain imports if dumping is found and if the dumped imports injure or threaten to injure the domestic industry or "retard materially the establishment of a domestic injury"<sup>45</sup> or if the dumping "causes or threatens to cause material injury to an industry in the territory of another contracting party exporting the product concerned to the territory of the importing contracting party."

The grandfather clause of the GATT allows all previously existing domestic trade legislation to remain intact (indeed the agreement would never have been accepted by many states had not this provision been included). This is why in the United States the antidumping and countervailing duty laws are always amended and never rewritten. However, the problem of defining dumping and subsidization are effectively left to national discretion.

As in the case of escape clause actions, there are surrogates for Article VI actions. The resolution of an antidumping case, for example, may be something other than the imposition of a non-discriminatory tax on all of the targeted imports. The AD investigation may be terminated (or suspended) by an agreement which is deemed by the United States authorities to stop the problem. Hence it may be agreed that a voluntary export restraint among only the key suppliers will stop the problem. Or, it may be that if the dumpers agree (undertake) to raise the price of the targeted export to a level deemed acceptable by the United States then the antidumping action will be terminated.

We can see from these examples that the loopholes in the GATT Agreement, as Hudec explains, "open the door to creative jurisprudence which can reach well beyond the written rules."<sup>46</sup>

As an institution, the GATT provides the machinery for the resolution of trade disputes. One must ask why the United States usually resolves dumping problems through its own administrative procedures instead of submitting them to international arbitration.<sup>47</sup> Again, most of the same constraints which dissuade it from taking Article XIX actions hold true. The risk of having to pay compensation or accept retaliation is too

high. And, the possibility of taking discriminatory action is reduced. Robert Hudec has observed that the United States and the European Community use the GATT dispute resolution process far more often than any other countries<sup>48</sup>. But he demonstrates that they use it as a "soft" option through which the threat of hostile action placates domestic interests while the process itself is a "good way to buy time."<sup>49</sup> since the complaints are usually drafted so that they "self-destruct". The dispute resolution mechanism can only work if the United States submits cases to it. Most trade remedy cases are resolved by national procedures.

It was well-recognized that states would continue to use national trade remedy procedures when the Antidumping and the Subsidies Countervail Code was negotiated in 1968. These Codes were intended to further elaborate on Article VI of the General Agreement. The scope for protection and harassment through Article VI procedures had been found to be large. The purpose of these Codes was to harmonize certain procedures and definitions so as to limit the possibilities for abuse.

But, the Codes failed to provide any legally or administratively workable definition of key terms such as what constitutes dumping, injury, a subsidy, etc.. In any case, the United States has required, through legislation, that the relevant administering agencies must, when faced with a contradiction between the domestic statute and these international agreements, that the domestic statute takes precedence.<sup>50</sup> In practice it has been left to national discretion to define these basic terms.

Under the GATT system the administration of trade policy remains national. The international legal framework is interpreted and applied at the national level in a discretionary fashion. Even the choice of whether to submit a problem to international arbitration is a matter of discretion.

Where discretion was not intended to come into play was in the area of sovereignty. The GATT envisaged a relatively simple world in which trade problems occurred, and could be resolved, at the border. By using remedy policy to change or preempt policies or behaviour which occur within other states the United States is

extending an area of discretion which the GATT planners never anticipated. This constitutes a new problem in international relations.

## **DOMESTIC POLICYMAKING**

If the rules exist in international commercial affairs not as they are written but as governments interpret and apply them then we must look at domestic policy-making. For to interpret and to apply the international arrangements is to exercise economic statecraft as David Baldwin makes clear;

**"Attempts by statesmen to influence the pattern of international trade through manipulating this legal and political framework in which trade takes place can be regarded as acts of economic statecraft."<sup>51</sup>**

Who in the United States, then, is practising economic statecraft? Who is responsible for making the actual, the applied, rules?

The United States Constitution divides the authority to regulate foreign trade between two branches of the government. Under Article One Section 3 the Congress is explicitly given the authority to regulate commerce with foreign nations and under section 10 to lay and collect duties or consent to states doing so. Article Two provides the Executive branch with the authority to manage foreign relations by virtue of its sole ability to receive ambassadors, and other public ministers, to negotiate executive agreements with foreign nations without the consent of the Congress and to negotiate treaties with the consent of the Congress. The problem of the "separation of powers" refers to the ambiguity as to where the authority of one branch leaves off and the other begins, and source of authority for one branch of government to challenge the actions of another. It remains one of the most contentious problem areas for students of the American political and legal system. In trade policy matters the Congress is generally responsible for providing the statutory basis for the Executive to administer trade policy.



Through Congressional legislation and delegation " ... the United States, has, over the years, created extensive legal and administrative machinery for the control of foreign trade."

"Unfortunately," Frederick Davis so clearly observed, "this machinery has not been assembled in a systematic or logical way: like a classical cathedral, the structure is composed of bits and pieces originating in different eras and representing different reactions to problems or concerns which often are of no immediate significance in today's world."<sup>52</sup>

It is not the aim of this Chapter to describe the entire machinery of American trade regulation but rather to emphasize that attempts by both the Congress and the Executive to influence the pattern of international trade by manipulating the legal and political framework in which trade takes place are acts of economic statecraft. This does not imply that economic statecraft is the product of focused deliberation and consensus between the Executive and the Congress. Even within the Congress, between the relevant Executive Agencies and among the independent agencies there are substantial differences of opinion about the methods and objectives policy should achieve. Conflicting and competing statecraft is a problem.

It would be exaggerating to say that the economic statecraft of remedy policy emerges as the end product of deliberation and compromise. Compromises do occur, particularly among those who are actively involved in the process of emending and interpreting the legislation. But many of the changes made to the statute, either in emendation or interpretation, have been designed with reference to a specific issue or interest. As a result the law's broad shape and aim have been altered by the simple accumulation of narrowly defined and small alterations.

Many others have written about the process of making trade policy. That task is not undertaken here. But, it is important to understand the haphazardness of the process. Trade bills are often more than 1000 pages long. Those pages are awash with technical details. Not only is difficult to get through 1000 pages of proposed trade law. There is a tendency for people to believe that technical changes are not political. Therefore the changes are not very important. But, as this study will demonstrate, this is wrong. All of

the politics is in the technical detail. All of the technical detail is politics. That is why the bulk of this dissertation is devoted to exploring the technical details of the two statutes in question.

This haphazardness of the policy-making process raises an important question. How can we apply the term "statecraft" to the policy outcome of this process if there is no "rational" actor creating it? Statecraft tends to imply that statesmen or someone is deliberately pursuing a particular policy. But, most policy emerges out of complex set of influences and desires. The domestic and even international actors who influence the policy-making process may have no clear picture of the overall policy. Nonetheless, in the end, there is a policy. Whatever that policy is, whatever the legislation actually says, that is what foreigners must abide by. Therefore, in answering the question posed in this dissertation, "What is the United States actually asking foreigners to do under the AD and CVD laws" it is important to understand that this is a different question from "What does the United States think it is asking foreigners to do under these laws?" One of the main purposes of this study is to demonstrate that the ostensible and the actual purpose of these laws have become contradictory. Because this is a study of international relations and international politics, it seems appropriate to focus on the policy outcome and examine how that policy, intended or not, compels foreigners to change their behaviour.

## THE CONGRESS

Before a substantial income tax was introduced in 1913 income from tariffs accounted for 50% to 90% of all federal revenue and Congress was the preeminent branch involved in trade regulation. Trade policy was tariff policy. Since then, revenue from tariffs has declined to about 1% of federal income and the Congress has gradually delegated authority and responsibility for the administration of trade matters to the Executive and independent agencies. The first step in this process was the 1934 Reciprocal Trade Agreements

Act which delegated authority to the President to negotiate the reduction of tariffs by up to 50% in return for reciprocal tariff cuts by foreign states.

As the emphasis has shifted from the setting of tariff rates to the internationally negotiation of trade matters, the Congress has faced a dilemma. A former United States Trade Ambassador explains, "Their dilemma is that they are not organized to handle all trade policy and to deal with it in a way that makes sense in negotiations, and yet they have the constitutional authority."<sup>53</sup> Hence, they have delegated administrative responsibilities for remedy policy to the Executive and independent agencies.

The main role of the Congress in trade remedy policy is that it makes the trade remedy laws -- it provides the statutory basis for policy. It defines the terms of the laws, the reach, the scope. Also, it sets the procedures for administering the law, it designates the agencies which will administer the law, the level of discretion available to those agencies, the criteria and procedures the agencies must use in their application of the law, etc. In that the Congress sets the terms of what behaviour is actionable and how every element related to remedy policy of each trade bill constitutes an exercise in economic statecraft.

One might say that these capabilities do not give Congress direct control over foreign behaviour but rather set the terms for the Executive and the independent agencies to do so. It should be said that many legal commentators have noted that the remedy provisions are effective not only when they are actually applied but they also have an immeasurable but real prophylactic effect. Peter Ehrenhaft says: "The laws may have a prophylactic effect, however, by encouraging by encouraging foreign producers to price goods shipped here at "fair" value and dissuading governments from providing "bounties and grants" that is a proposition difficult to prove or disprove."<sup>54</sup> Would the Congress bother to amend the remedy laws unless they were making them more effective? By altering the statutes Congress hopes to improve its ability to manipulate foreign actors and check behaviour it finds objectionable.

Most of those who have attempted to describe or explain the process of producing trade legislation have commented on its haphazardness and complexity. EE Schatt-

schneider captured this aspect better than any other. In reference to trade legislation he noted, "Congress writes bills which no one intended."<sup>55</sup> Robert Pastor points out that there are no theories about Congressional foreign policy-making generally nor foreign economic policy though narratives and descriptions of the process abound.<sup>56</sup>

Trade policy, as anyone who has ever been closely involved in the process will confirm, is about detail. It is difficult to discern, leaving aside describing, the significance or effective meaning of developments in trade law. Trade lawyers are paid a great deal to do exactly this. The potential for the abuse of trade policy is inherent in the morass of detail which make up its substance.

There is a tendency for most commentators to describe any given trade bill as either "free trade" or "protectionist". There is a well-accepted assumption that the Congress is inherently protectionist, although Robert Pastor has found that there has been no "bias" on the part of Congress toward protection from 1929 to 1976.<sup>57</sup> Each time a trade bill is formed speculation that it will be "protectionist" grows until the final conference proceeding when, generally, the "blatantly protectionist" elements are removed. That they were put in specifically to be removed for public relations reasons is unknown by most of those outside the legislative process. The final bill is so long and complicated that very few bother to read it, or its fine print. Instead there is a tendency to rely on the Executive branch's appraisal of the bill.<sup>58</sup> Hence, every trade bill from the 1974 Trade and Tariff Act to the 1988 Trade and Competitiveness Act has been hailed as an affirmation of the American commitment to free trade.

Indeed, every attempt to pass "protectionist" trade bills, from the Burke-Hartke bill in 1971 to the Gephardt Amendment in 1987 have failed. Since it has not been possible to gain a large enough coalition for legislated protection, those who wanted protection turned their efforts to the trade remedy provisions. They greet efforts to "tighten up" the remedy provisions with enthusiasm.

But what is meant by "blatant protectionism"? No one seems able to say. It is a subjective question. We can ask, however, what does the law consider actionable, how does

the law allow actionable behaviour to be penalized, how is the law invoked in trade policy to achieve the goal, what are the goals the administrators are seeking to achieve with remedy policy?

For example, what is considered "unfair" trade under United States law has been substantially broadened. The ad hoc process of altering the laws has transformed and subverted them. This development has been neglected not only because of the complexity of the detail but also because the process of producing trade legislation is generally portrayed as a "technical" rather than "political". For example Michael Finger explains:

"Low- or technical-track decisions are those defined by "rules". Cases here are "determined" not "decided" according to criteria established by law, administrative regulations, precedent and tradition. Higher track decisions are less circumscribed by rules and regulations and require considerable attention by government officials entrusted with discretionary authority and subject to political accountability. The antidumping and countervailing duty mechanisms in the United States, for example, are technical procedures."<sup>59</sup>

Such faith in the inflexibility of law, not to mention the impartiality of the bureaucrats, reveals misunderstanding of how these provisions work. There has been controversy, for example, about the way Congress has limited the discretion available to the Executive on remedy policy. While the Executive may have less discretion about the application of the law -- ever since the 1974 trade act the machinery for commencing a complaint has become increasingly automatic -- but few have acknowledged the high level of discretion available to the Executive branch bureaucrats in the calculation of injury and the determination of the causal link between an unfair trade practice and injury. Great discretion is also available to the Executive branch as to the means of settling a case. They can apply an across-the-board tariff, or force the supplier to change their prices (at home or for exportation) or force the foreign industry to agree to buy more goods from the United States or to limit their exports, etc.

The belief that remedy policy is "technical" a direct result of the free trade framework which assumes there some distinction can be made between "technical" and "political". In a introductory reader on international relations the authors, Dougherty and Pfaltzgraff, confirms this attitude.

**"To move from a political to a technical framework is to limit drastically, or even eliminate the potential for conflict."<sup>60</sup>**

**The desire to relegate trade policy matters to technical procedures has a long history in the United States. It dates from the days when the Tariff Commission (now the International Trade Commission) was created to take "the tariff out of politics"<sup>61</sup> The term technical is applied to minimize the existence of power or of a conflict on interests in the making of United States trade remedy policy. EH Carr explained that the distinction between the two terms is necessary for political reasons. Economics is technical.**

**"But as soon as an issue arises which involves, or is thought to involve, the power of one state in relation to another, the matter at once becomes "political".<sup>62</sup>**

**The "technical" details of United States trade remedy law and policy is where both the power and the politics rest.**

## **THE EXECUTIVE**

**Administration of these technical details is in the hands of three agencies: the Commerce Department, which is part of the Executive and the International Trade Commission (ITC) which is an independent agency.**

**Once a complaint that a foreign government is unfairly subsidizing exports or a foreign firm is dumping exports has been lodged with the government an investigation ensues. The complaint takes the form of a petition. It can be submitted by a domestic industry or, in recent years, by the government itself (meaning the Commerce Department or the United States Trade Representative).**

**The Commerce Department has been given responsibility for conducting investigations in order to substantiate that dumping is actually occurring. Its staff must also determine the amount of the dumping and the amount of the subsidization. From that determination Commerce arrives at a duty which the respondent will be required to pay if there is a positive finding rendered against it.**

The ITC is responsible for determining that injury has been not only incurred by the domestic injury but also that the injury is caused by the dumping or the subsidization. The ITC Commissioners are appointed by the President and approved by Congress. There are six of them, three being Republicans and three being Democrats. In the event of a tie vote the vote automatically turns against the foreign respondent.

If dumping or a subsidy is substantiated and ITC confirms that it was the cause of injury to the domestic industry then a positive determination is rendered against the respondent. The foreign firm or government must then comply with what the United States requires. Usually, it must pay a duty equivalent to the dumping or the subsidy.

## **THE JUDICIARY**

The United States Courts have not played a major role in the formation or administration of trade policy precisely because of the political content of the statutes and the role of power involved in their application. Historically, the judiciary has been extremely reluctant to render review over the administration of trade policy.<sup>63</sup> Consistently this branch of government has claimed that questions pertaining to international trade matters are non-justiciable;

**"involving as it almost always must economic, military and foreign policy considerations of the type which tradition has assigned to other branches of the government."(emphasis added)<sup>64</sup>**

More importantly to our argument, the judicial branch has, accordingly, held that the Act of State Doctrine precludes domestic courts from having the jurisdiction to review actions taken by foreigners abroad<sup>65</sup>. Therefore such issues are not meet for Supreme Court review.

The judicial branch has tacitly recognized the political nature of trade policy. For this reason it refuses to be directly involved in the trade policy process. This is why Judicial review has not generally been available in policy proceedings. This is in marked contrast to the exercise of power by government on other issues which are subject to judicial

scrutiny. Abuses of remedy policy have, therefore, mostly gone unremarked.

All of the Federal Court cases that are cited in the following chapters occurred because questions about the administration of the law by an Agency were at issue. In none of these cases are questions about the original allegation of an unfair trade practice at issue.

If a petitioner or a respondent wished to challenge the finding made by the administering agency it could appeal to the Customs Court. The Customs Court is part of the Customs Service which, we recall, originally had the authority to administer the AD and CVD laws. But, there was no genuine judicial review until the Congress made judicial review available in the early 1980's. Congress established the Court for International Trade. This new Court has the same powers as a Federal District Court (under article 3 of the Constitution) under 1980 Trade Act. The CIT has functioned only since 1981. Many observers have commented that the Court has been very conservative so far, tending to confirm the judgement of the Customs Court. A further agency, the Court of Appeals for the Federal Circuit Court (CAFC) was made available for appeals from the CIT in 1982. The Supreme Court, being the highest Court in the land, may hear appeals from the CAFC. But, the Supreme Court, being reluctant to become involved in trade cases for the reasons cited above (in note 65) has never yet accepted a trade case.

Most studies of American trade policy make little if any reference to the Judicial Branch, but not just for the reasons outlined above. It is also that, at bottom, the law is not very supportive of trade policy, particularly trade remedy policy. The concept of trade remedy policy is based on the implicit assumption that American producers have a right to a marketplace that is untainted by unfair trade practices. This concept works well enough when applied to domestic competition policy which is aimed at domestic competitors who are wholly subject to domestic laws. It does not apply very well to international competition. After all, the primary canon of United States trade law is that no individual has a Constitutionally-given right to engage trade with other nations. The Supreme court has held:



**"No individual has a vested right to trade with foreign nations."<sup>66</sup>**

The Constitution does not grant the right to import or export. What the Constitution does not prohibit, however, is permissible.

Because there is no right a firm or individual can invoke, the United States government must act on behalf of its citizens with regard to international trade matters. The trade remedy provisions allow private citizens<sup>67</sup> to invoke a "right" to be protected from certain actions by foreign actors.<sup>68</sup> But the right being protected is the nation's right not the industry's, the firms' or the individual's. Two interesting factors arise from this. First, once the complainant's cause has been taken up by the government the complainant no longer has any control over the process, and its interests are entirely subordinate to the interests of the parties in government pursuing action. Even if the complainant seeks to terminate the action the government may carry on with it if it is deemed to be in the national interest. Second, it is not even necessary for there to be a complaint from the private sector. The Executive can initiate an action itself.

## **FIRMS AND SPECIAL INTERESTS**

Firms and industry play a part in the economic statecraft of remedy policy primarily in three ways. First, they can invoke the laws by filing petitions against foreign respondents. Second, domestic industry often provides the draft language which is adopted in the statutes. Often technical changes in the language are submitted by companies to their political representatives. The politicians then submit the proposed change into the pending legislation. The third part played by industry is more general. Private industry can generate political response to their special interests. They can attempt to influence the content of the statutes, the administrative regulations or even the course of an individual investigation by lobbying the relevant politicians, the administering officials, and general public opinion.

This is probably the time to briefly take note of the sources of the "heat", the

political pressure, which has prompted the changes to the content and administration of these statutes. The sources of pressure on United States trade authorities to apply the remedy provisions emanate from developments from within the United States and from abroad.

United States trade (the value of imports and exports combined) now constitutes about 18% of total world trade. This would appear to be a precipitous drop from the 1955 figure of 37%; and that is how it is most often portrayed and perceived. However we must remember that the United States found that it could not survive as an island of prosperity in a sea of poverty. It's huge share of world trade, of wealth, was artificially magnified by the decline of the European economies and all other countries which had been affected by the second world war. So the United States embarked on an ambitious program to enrich the rest of the world. Those policies worked.

It is no coincidence that the trade remedy laws were not substantially amended between the time of their inception at the turn of this century and the 1974 Trade and Tariff Act. It is widely acknowledged that there was little need even to employ them before the 1960's because nobody was in a position to compete with the United States -- there was little possibility of foreign monopoly power abuse.

However, the dramatic growth of various foreign economies since the 1960's, the creation of productive capacity abroad and foreign competition with American trade is now perceived to reflect the relative decline of the United States. Why this development is never portrayed as the relative rise of foreign economies remains unclear. Certainly, though, the perception has grown that the United States may not be better off as an island of prosperity in a sea of prosperity.

The willingness in the United States to forge a link between increased competitiveness abroad and the use of "unfair" trade practices is pervasive. That link is tenuous but politically attractive.<sup>69</sup>

It is this political attractiveness which has led Congress to amend the remedy laws in the attempt to make them more effective -- a process which will be examined in detail

for both of the provisions under review. Similarly it is at least partly responsible for the pressure from domestic industry to not only amend the law but also to administer it in a pragmatic way.

Little distinction appears to be, or have been, made between the ill effects of domestic economic policy<sup>70</sup>, rapidly changing technology<sup>71</sup>, poor management, an increased willingness to use bilateral relationships which are statistically incapable of reaching a balance<sup>72</sup> and a variety of other factors which have contributed to economic stagnation and the huge growth of the United States trade deficit since the late 1960's. Instead, there has been a tendency for the United States to blame foreigners for pursuing unfair trade practices. On the basis of such allegations, it has been able to force foreigners to readjust, to use the remedies as a means of limiting foreigners' exports or profit margins, rather than asking Americans to readjust.<sup>73</sup>

When we think of all those people who are involved in drafting the details in trade law and those who are involved in administering the statutes we must remember that if the end result of all that activity is to compel some foreign government or company to alter, or even to maintain, its behaviour -- whether in a particular instance or through the manipulation of the general legal and political framework in which they must operate -- then economic statecraft is at play. It is actually hard to think of what else all those officials, bureaucrats and statesmen involved in trade policy could possibly be doing if not attempting to get others to do what the United States wants them to do.

## THE UNITED STATES: THE PARADOX

Whatever the cause, there is no denying that pressures build up over import "problems" and eventually something must be "done" about them. But, what to do? Jacob Dreyer neatly summarized the potential danger.

"It ought to be recognized, however, that policies designed to countervail foreign use of monopoly power may result in departures from the free trade arrangement and may be the source of further distortions in the national economy concerned and in the world economy as a whole. Thus, a country espousing a liberal

economic philosophy faces a philosophical and practical dilemma when confronted by the foreign use of monopoly power."<sup>74</sup>

Joseph Grunzel, who was mentioned earlier as the first to study the problem of administered protection, was certain that philosophy would yield to pragmatism. "Though strange at first sight" he found that it was in "those countries most committed to the doctrine of free trade (emphasis added)." He cites England and a country which had the doctrine of free trade imposed on it by Germany, Hungary, as states in which this phenomenon reached "the greatest development".<sup>75</sup> In those countries;

"the free trade doctrine had become so firmly established on account of its theoretical background and its tactical advantages, that in the course of time corrections which had become necessary could be carried out only in the application of the principle and not by modifying the principle itself"<sup>76</sup>

This "characteristic fact"<sup>77</sup> of administered protection is the source of our paradox. Remember our paradox. The United States is using trade remedy policy not to uphold competition but to undermine it. Although committed to the doctrine of free trade and the principle of competition, the United States has been compelled by circumstance to develop what Morkre calls "covert" as opposed to "overt" protection.<sup>78</sup> Rodney Gray explains that the

"developing trade policy system ... is best understood as a system of highly detailed, discriminatory legalistic intervention and that the literature of trade liberalization should best be viewed as part of the rhetoric of political presentation, rather than as an accurate description of trade policy in practice, or of the motives of the players."<sup>79</sup>

The traditional frameworks obscure from view many of the international relations issues posed by United States trade remedy policy. Although they are useful in identifying a general shift toward greater protection in the international trade system they do not allow us to see the broader political implications of this shift. The threat to national autonomy and indeed to the "legitimacy" of the post-war economic order are profound problems. The traditional paradigms simply do not acknowledge the role of power and politics which is central to an understanding of trade remedy policy. How one state compels another to behave differently, whether we regard the compelled behaviour as "bad" (as when trade-restrictive measures are implemented) or "good" (as when anti-

competitive practices are eliminated) is a phenomenon central to the study of international relations.

The economic statecraft approach to international commercial relations is particularly rewarding since it allows us to understand the post-war economic order as it is, rather than as we would wish it to be. It allows us to address the "actual" as opposed to the "possible, probable, or desirable"<sup>80</sup> within this system in international relations. That system is not, as is commonly accepted, an exercise in disarmament. It is more like an exercise in arms control.<sup>81</sup> The remainder of this study looks into the United States armoury containing trade policies and examines how the weapons have been upgraded and deployed since the 1960's.

Finally, the economic statecraft concept allows us a more sophisticated understanding of the threats to international economic order. We can leave aside the simplistic idea that the problems can be described or understood in terms of free trade versus protection or non-intervention versus intervention. Writing in 1936 EM Winslow took the first step in this direction,

"As a problem in commercial policy it (administrative protectionism) was entirely different from the old controversy over protection and free trade. Tariffs had come to appear relatively honest and liberal in comparison with the new protectionism; and if they were still quantitatively more important in their effect on trade, the latter had a far more serious qualitative effect on international relations because of its essential dishonesty. The problem in short, had become one of good versus bad protectionism, rather than a question of good versus bad commercial policy as understood in the old quarrel between the liberals and the protectionists."<sup>82</sup>

Where he concluded, this study begins;

"Administrative protectionism in short seems to be symptomatic of a transition in commercial policy not from free trade to protection but from orderly protection to complete autarchy."<sup>83</sup>

1. Adam Smith, An Inquiry into the Nature and Causes of the Wealth of Nations, RH Campell and AS Skinner ed.s., (Oxford: Clarendon Press, 1976) Vol. 1, page 25.
2. The problem of public procurement is not addressed here as it constitutes only a fraction of trade among GATT signatories.
3. Although, government procurement issues and state trading continue to raise important trade policy questions and controversies.
4. Chia-Jui Cheng, ed., Clive M Schmitthoff's Select Essays on International Trade Law, (Dordrecht: Martinus Nijhof, 1988) page 539.
5. IM Destler, Making Foreign Economic Policy (Washington, D.C.: Brookings, 1980) page 129.
6. Benjamin J Cohen, American Foreign Economic Policy: Essays and Comments (New York: Harper and Row, 1968) page 20.
7. William E. Lingelbach, "Commercial Policies as Causes of International Friction" The Annals of the American Academy of Political and Social Science, Volume 150, July 1930, page 117.
8. There has never been any doubt on the part of most governments that the state should play a role in regulating trade.
9. JW Burton, Systems, States, Diplomacy and Rules (Cambridge: Cambridge University Press, 1968). James E Dougherty "The Study of the Global System" James Rosenau et al., ed.s., World Politics: An Introduction (New York: Free Press, 1976).
10. James E Dougherty and Robert L Pfaltzgraff, Jr., Contending Theories of International Relations: a Comprehensive Survey (New York: Harper and Row, second edition, 1981).
11. Witness the failure of the world peace through world law approach in the interwar years.
12. Henry Kissinger, A World Restored: Metternich, Castlereagh and the Problems of Peace, 1812-1922 (Boston: Houghton Mifflin, 1964) page 1.
13. Hedley Bull, The Anarchical Society: A Study of Order in World Politics (London: Macmillan, 1977) page 8.
14. *ibid.*, page 54.
15. Richard Gardner, Sterling Dollar Diplomacy (Oxford: Oxford University Press, 1956) page xviii.
16. At the Atlantic Conference in August 1941.
17. JB Condliffe, "The Real Economic War" The American Economic Review Vol. 218, November, 1941, page 24.
18. *ibid.*, page 20.
19. Peter Drucker, The End of Economic Man (London: William Heinemann, 1943). See also E H Carr, The Twenty Years Crisis 1919-1939.

20. Economist "The American Challenge", cxliii (1942) page 67. As cited by R Gardener in Sterling Dollar Diplomacy page 1.
21. "The GATT system of trade liberalization was based on the idea of permitting the market to determine the international location of economic activity." Robert Gilpin, The Political Economy of International Relations, (Princeton: Princeton University Press, 1987) page 228.
22. Gottfried Haberler, "The Liberal International Economic Order in Historical Perspective" Challenges to a Liberal International Economic Order, Ryan Amacher, Gottfried Haberler and Thomas Willetts, ed.s., (Washington, D.C.: American Enterprise Institute, 1979) page 43.
23. The Agreement on the Implementation of Article VI of the General Agreement on Tariffs and Trade (Geneva: GATT Secretariat, 1967).
24. The Agreement on the Interpretation and Application of Articles VI, XVI and XXIII of the General Agreement on Tariffs and Trade.
25. The commercial policy chapter.
26. William Diebold, "The End of the ITO", Essays in International Finance (Princeton: Princeton University Department of Economics and Social Institutions, 1952).
27. See Richard Gardner, Sterling Dollar Diplomacy, for the best recounting of the failure of the Havana Charter.
28. Signed 30, October, 1947.
29. The Provisional Protocol allows legislation pre-existing the Agreement to remain intact.
30. General Agreement on Tariffs and Trade: What is and What it Does, (GATT Secretariat, November 1984) page 3.
31. John Ruggie, "International Regimes, Transactions and Change: Embedded Liberalism in the Post-War Order", International Organization 36, 1982, page 396.
32. See the prologue to the GATT.
33. John Ruggie, "International Regimes" page 196.
34. John H Jackson, "The Puzzle of the GATT: Legal Aspects of a Surprising Institution" Journal of World Trade Law, 1967, page 131.
35. Robert E. Hudec, "The GATT Legal System: A Diplomat's Jurisprudence" Journal of World Trade Law, Vol. 4, No. 5, Sept.: Oct. 1970, page 615.
36. *ibid.*, page 619.
37. *ibid.*, page 665.
38. Section 201 (a)(1), 82 Stat., 1347, 19 USC Section 160 note (1970).
39. Renegotiation Amendments Act of 1968. Pub. Law No. 90-634, Sect. 201(a), 82 Stat. 1347, 19 USC Sect. 160 (1970).

40. John Barcelo, "Antidumping Laws as Barriers to Trade: The United States and the International Antidumping Code" Cornell Law Review, Vol. 57, No. 4, April 1972, page 536.

41. *ibid.*, page 535.

42. Hudec, The GATT Legal System: A Diplomat's Jurisprudence, " ... the insistence that the law's coercive pressures be applied in a controlled fashion which allows room for manoeuvre at every stage of the process." page 665.

43. "General Agreement on Tariffs and Trade: What it is and What it Does" GATT Secretariat, page 14.

44. Alan Wolff, "The Need for New GATT Rules To Govern Safeguard Actions" Trade Policy in the 1980's (Washington, D.C.: Institute for International Economics, 1983).

45. Article VI.

46. Robert Hudec, The GATT Legal System and World Trade Diplomacy, (New York: Praeger Publishers, 1975. p. 185-186.

47. Dispute resolution machinery exists not only in the GATT forum but also in the Organization for Economic Cooperation and Development.

48. Of the 80 GATT lawsuits filed from 1960 to 1985 one third were between the US and EC (26), 45 of the remaining 54 had either the US or the EC involved as one of the parties, only 9 involved neither. Robert Hudec, "Legal Issues in US-EC Trade Policy: GATT Litigation 1960-1985" Issues in US-EC Trade Relations RE Baldwin, CB Hamilton and Andre Sapir, ed.s., page 18.

49. Robert Hudec, "Legal Issues in US-EC Trade Policy" page 39.

50. See Chapter Three, page 57, notes 38-41 *infra*.

51. David Baldwin, Economic Statecraft page 46.

52. Frederick Davis, "The Regulation and Control of Foreign Trade", Columbia Law Review, Volume LXVI, 1966, p. 1428.

53. Hon. Amb. William D Eberle, "Trade Policy and the Trade Representative" Trade Policy and US Competitiveness Claude E Barfield and John H Makin, ed.s., (Washington: American Enterprise Institute, 1987) page 23.

54. Peter D Ehrenhaft's Review of Professor Lowenfeld's Public Controls on International Trade in Law and Policy in International Business No. 1, 1984.

55. EE Schattschneider, Politics, Pressures and the Tariff (New York: Prentice Hall, 1935) page 13.

56. Robert Pastor, Congress and the Politics of United States Foreign Trade Policy (Berkeley: University of California Press, 1980) page 26.

57. *ibid.*, page 3.



58. For a classic example of reliance on Executive review see S Lande and C Van Grassek, The Trade and Tariff Act of 1984: Trade Policy in the Reagan Administration (Lexington, Massachusetts: Lexington Books, 1986).
59. J Michael Finger, "Ideas Count, Words Inform" Issues in World Trade Policy RH Snape, ed., (London: Macmillan, 1986) page 264.
60. James E Dougherty and Robert L Pfaltzgraff, Jr., Contending Theories of International Relations: a Comprehensive Survey, (New York: Harper and Row, second edition, 1981) page 419.
61. John Dobson, Two Centuries of Tariffs: The Background and Emergence of the United States International Trade Commission (Washington: US Government Printing Office, 1976) page 86
62. EH Carr, Twenty Years Crisis, page 102.
63. Frederich Davis, "The Regulation and Control of Foreign Trade" page 1459.
64. *ibid.*, page 1459. See the opinion of Justice Douglas in Panama Canal Co. v. Grace Line 356 US 309 (1958).
65. Johnstone v. Pedlar, 1921, 2 A.C. 262.
66. Butterfield v. Strahan, 192 U.S., 470, 493 (1904).
67. Citizen includes companies and industries which are seen as corporate persons under the law.
68. According to Rodney Grey the trade remedy provisions therefore constitute an elaborate system of private rights through which private parties can invoke government protection. Trade Policy and the System of Contingency Protection unpublished paper commissioned by the OECD, Paris 1986.
69. Robert Baldwin, "The New Protectionism" page 104.
70. The tax reforms implemented by the Reagan administration and the explosion in the trade deficit, etc..
71. "Materials for Economic Growth" Scientific American Vol. 255, No.4, October 1986.
72. Such as between the United States and Japan.
73. Jeffery Garten, "Gunboat Economics" Foreign Affairs 1985.
74. Jacob S Dreyer, "Countervailing Foreign Use of Monopoly Power" Challenges to a Liberal International Economic Order Ryan C Amacher, Gottfried Haberler and Thomas D Willett, ed.s., (Washington, D.C.: American Enterprise Institute, 1979) page 319.
75. Joseph Grunzel, Economic Protectionism (Oxford: Clarendon Press, 1916) page 179.
76. *ibid.*, page 180.
77. *ibid.*, page 179.
78. M Morkre, The New Protectionist Threat to World Welfare (New York: Elsevier, 1987).

79. Rodney Grey, "Contingency Protection" page 9.

80. Quincy Wright, A Study of International Relations (New York: Appleton, 1955) page 26.

81. The author is grateful to James Mayall for this idea.

82. EM Winslow, "Administrative Protectionism: a Problem in Commercial Policy" Explorations in Economics: Essays in Honour of FW Taussig (NY:McGraw-HillBook Co., 1936) page 183.

83. *ibid.*, page 189.

## **SECTION TWO**

## CHAPTER FOUR -- ANTIDUMPING POLICY: ECONOMIC STATECRAFT

The antidumping law is best understood as an instrument of economic statecraft. American policymakers use this economic policy tool to compel foreign firms, whether publicly or privately owned, to modify their behaviour in compliance with the United States's demands. Put simply, the law is designed to compel foreigners to stop dumping or not to start dumping. It is asserted that dumping distorts competition internationally and domestically. Official American rhetoric emphasises that the law is used not only to enhance competition in the domestic economy but also to enforce the international trade rules embodied in the GATT. Thus, when the United States applies the law, the actions are justified as creating free(r) and fair(er) trade and, in this way, contributing to the maintenance of the post-war international economic order.

With this sense of justification, United States policy-makers "strengthened" the antidumping law through a combination of emendation of the Antidumping Act and pragmatic administration of that Act. However, this process of change has subverted the statute. In effect, as we shall see, antidumping law and policy undermine competition, not enhance it. In practice the law is now more trade-restrictive than the dumping practices it is supposed to counter.<sup>1</sup>

The central issue, however, is not simply that the statute has been used to undermine competition, i.e. in a protectionist manner. Rather, we must ask, what are foreigners being compelled to do under the statute? To what end is power being exercised by the United States over the corporate citizens of foreign states? What kinds of behaviour have become actionable under the statute? The post-war international economic order rests upon the foundation of competition. The United States efforts to compel foreigners to undertake anticompetitive behaviour, pose serious political questions in international relations.

Compliance is achieved through the exercise of power. American efforts to influence the actions, the range of options and the policy choices of foreign actors, infringe on foreign autonomy. Here the schism between American trade rhetoric and actual American policy becomes a significant issue in international politics. American trade policy rhetoric invokes the language of competition and free trade. The US emphasises that liberalized markets are universally in every state's best interest, not just in America's best interest. Foreigners should adopt market standards of behaviour because it is in their own best interest, not because it is America's best interest. Under this cover of legitimacy, however, the reality is that antidumping policy, as we shall see, is not used to compel foreigners to abide by pure market standards but rather to behave, as the United States thinks they "should". Students of international relations ought, therefore, to study how the antidumping law is used by one state to exercise power and influence on the autonomy and sovereignty of foreign actors, whether those actors are firms or governments.

The purpose of this chapter is to examine how the United States employs antidumping policy as a means of compelling foreign firms to do things they would not otherwise, such as changing their prices or policies, paying duties or in more extreme cases, restricting the volume of their exports. Ostensibly, only genuinely unfair trade practices are actionable under the statute. By examining the administrative and statutory changes in the law which have been made, it will become clear whether or not only genuinely unfair trade practices are actionable. It is necessary to examine what changes in behaviour are being demanded and on what grounds. What exactly is dumping? Given the existence of the antidumping provisions and the steady efforts to make them more "effective" since the 1960's, it is reasonable to ask exactly what are they used to achieve?<sup>2</sup>

Sinister and derogatory overtones have accompanied the term dumping from the beginning. One industrious writer found that the term originates from the Old Icelandic word "thumpa" ("d" and "th" being phonological reflexes) which means to thump or hit somebody.<sup>3</sup> Perhaps, the fact that a "dump" has come to mean a temporary depot for

munitions<sup>4</sup> is linked to the way in which dumping as a commercial practice is commonly referred to as "a species of international economic warfare".<sup>5</sup> Such derogatory connotations make it important to be clear about what we mean by dumping.

The precise definition of dumping has changed rather dramatically under the antidumping law since the creation of an antidumping statute in 1894. Each change in the definition is an act of economic statecraft since with each innovation the United States changes the legal environment in which foreign companies must operate. For this reason, it is crucial to explore the details of these changes. As Brian Hindley recently noted, "The phrase 'the devil in the detail' might have been invented for the anti-dumping law."<sup>6</sup>

Allegations of dumping, whether levied in an official industry complaint or rather more loosely in the press, are often sufficient to imply culpability. Allegations alone can be enough to compel the foreign company to change its behaviour just to escape opprobrium and the prospect of an investigation. As early as 1958 Peter Eherenhaft argued,

"Indeed, it is said that the trade-restricting effect of the Antidumping Act should not be measured by the relatively few findings of actual dumping, but rather by the much larger number of investigations that have been undertaken pursuant to the act."<sup>7</sup>

Once a dumping investigation commences, the foreign respondent is subject to the United States' definition of dumping as well as the methodology it employs to determine whether dumping exists, and if so, by how much. The respondent cannot challenge the decision to initiate an investigation until after the final determination is made.<sup>8</sup>

Therefore, there are two reasons why the applicable definition of dumping must be carefully examined. First, it is necessary to demonstrate that altering the definition of dumping and modifying the methodology by which dumping is calculated are acts of economic statecraft. These acts change the environment in which foreigners must function. Second, having demonstrated that ad policy is economic statecraft, it is necessary to determine whether American antidumping policy is used to compel foreigners to behave in a manner which enhances competition -- the basis of orderly international commercial

relations -- or undermines it. In this way it is possible to distinguish between the legitimate and the illegitimate use of this instrument of economic statecraft.

## **WHAT IS DUMPING?**

The term dumping describes certain pricing policies.<sup>9</sup> Traditionally, dumping is the act of price discrimination. Price discrimination means selling the same good to different buyers at different prices. Dumping, as an international trade concept has usually referred to the practice of reducing the price of exported goods below the price offered for the same goods in the home market.

The GATT defines dumping as "sales below normal value". "Normal" was not defined until the Antidumping Code was negotiated in 1967, when "normal" was established as meaning sales occurring "in the ordinary course of trade".<sup>10</sup> It is effectively left to national discretion to define what is "ordinary".

## **A BRIEF HISTORY OF THE ANTIDUMPING STATUTE**

It is necessary to review the statute's history for three reasons. First, its history reveals that it is intended to serve as a competition policy measure; it is supposed to be used to enhance market forces and competition. Second, the history shows that the law has evolved as an administrative measure. The United States judiciary has refused to allow dumping to be remedied through the domestic courts. In other words, there has been a tacit recognition by the judiciary that the law is an instrument of statecraft. For this reason, matters relating to it are non-justiciable.<sup>11</sup> Therefore, an administrative system has been constructed to allow the United States to scrutinize, judge and remedy foreign firms' economic behaviour. Third, a historical review demonstrates how the statute has evolved into an essentially anti-competitive measure; fair, normal and legitimate trade

practices have become actionable under it; market forces and competition are being reduced and not enhanced through its application.

There is some confusion as to whether the antidumping law was intended to be a competition policy measure or a tariff measure. Adams and Dirlam note that the law is comprised of an "unclear union of disparate elements drawn from tariff and antitrust law".<sup>12</sup> The tariff element reflects the desire to create a law that would prevent any underselling of the United States prices by imports. Seen this way the law was intended to preserve the "tariff wall" that the United States maintained and used to derive the substantial part of its federal revenue from the time the first antidumping law was created, in 1894.

But, the modern view is that the law arose as an extension of domestic competition policy (anti-monopoly and anti-trust policy). The American historian Samuel Elliot Morrison tells us that after the 1860's trusts and "gentlemens' agreements"<sup>13</sup> to maintain prices and divide business became common in the United States. These arrangements were designed to eliminate if not all competitors at least the uncooperative ones. Those who engaged in such restrictive business practices hoped to gain monopoly power at the expense of competition.

Standard Oil used its monopoly power to practice the kind of price discrimination which is most commonly referred to as dumping.<sup>14</sup> The high profits which were obtained in regions where there were no competitors allowed them to "subsidize" price cuts in their competitors' selling territory. This was kept up sufficiently long to drive competitors out of business and thereby obtain "the lion's share of the business".<sup>15</sup>

In 1890 the Sherman Act made monopolies and business practices undertaken in restraint of trade unlawful -- namely price discrimination.<sup>16</sup> The first antidumping statute targeted the same practices (monopoly power and price discrimination). It attempted to establish jurisdiction by requiring that the conspiracy (to restrain trade) be formed on United States territory and that it involve at least one United States citizen.<sup>17</sup> Under this Act dumping was defined as the act of selling in the United States at "prices



substantially less than actual market value."<sup>18</sup> United States industries took private actions through the United States District Courts. The same criminal penalties which were meted out to transgressors of the Sherman Act were available, plus up to one year of imprisonment.

It soon became frustratingly clear that it was legally impossible to criminally prosecute foreign nationals for committing such acts abroad if there were no American counterparts, i.e, through imports alone. The Supreme Court confirmed this in the 1909 case American Banana Co. vs United Fruit Co.<sup>19</sup> That ruling made clear that the Act was not applicable to foreigners if the named actions were not illegal in their home territory.

Lack of jurisdiction caused an important difference to emerge between the two competition policy measures. Antitrust policy targets the existence of monopoly power. Since there is no jurisdiction in antidumping legislation to target the existence of monopoly power, the 1916 statute instead aims at the intent to use monopoly power to destroy competition. Predation was the explicit target of the Antidumping Law of 1894 and the antidumping provisions of the Revenue Act of 1916.<sup>20</sup>

Predatory intent was, as far as economists of the day were concerned, the sole reason for providing a legislated remedy.<sup>21</sup> Jacob Viner, widely considered the leading expert on dumping, argued that dumping should be divided into three categories. His reasoning, though not put into print until 1923 in his seminal work Dumping: A Problem in International Trade<sup>22</sup>, was the logic behind early antidumping legislation. He showed that not all price discrimination is harmful to competition.<sup>23</sup>

He describes three kinds. Sporadic dumping, Viner found, occurs when a foreign business has a surplus of goods which it releases onto the international market at any price the market will bear. Such dumping is without predatory intent. Persistent dumping, he explained, is when exports are sold at a price, though profitable, which is lower than the price offered in the home market. This situation arises from the existence of differing elasticities in the home and foreign markets and also does not constitute predatory

behaviour. In contrast, he found, that only intermittent (also known as short-run) dumping is predatory and harmful. This occurs when foreign firms sell products abroad at prices which are not at all profitable. It is assumed that a firm cannot sustain a lack of profit for very long. Therefore, the only rationale for such sales is to destroy the existing competitors. The resulting reduction of competition potentially allows the firm to gain a greater market share. Having established control in the market it is assumed that the firm will raise prices to a profitable level, indeed much more profitable than would have been possible in the presence of other competitors.

Dumping under the 1916 Act, which was defined as "sales less than home market value", for this reason, was a "manifestation of illegal unfair competition" and it subjected violators to criminal penalties<sup>24</sup> fines and treble damages,<sup>25</sup> if, and only if, it was done with the:

"Intent of destroying or injuring an industry in the United States or 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."<sup>26</sup>

Intent, however, is difficult to prove. The 1894 Act was never applied. Even though the 1916 Act strengthened the reach of the law, the government never brought an action under the statute. Actions brought by private companies in the United States never resulted in a judgement against the plaintiff.

A profound change occurred with the implementation of the antidumping provision in the Revenue Act of 1921. Predation, which alone had warranted the creation of legislation to remedy dumping<sup>27</sup>, was no longer required. Instead, the 1921 Act, which remains the basic statute, targeted the effects of predatory dumping. It requires that price discrimination cause injury. Dumping had come to be defined not as any price discrimination<sup>28</sup> but as sales at prices which were "below fair value". This standard was codified in the 1921 Act as "sales at less than fair value" (LTFV). There is no precise statutory definition of LTFV. Instead the definition is established through administrative interpretation and practice.

In practice, for the meantime, "less than fair value" had come to mean any price lower than the domestic price in the home market. Injury, which the statute requires for a positive finding, would occur "if an industry is hurt or likely to be or prevented from being established by imports which involve price discrimination".<sup>29</sup>

Targeting the effects of predation is a complex and illusive task. After all, fair price competition can be injurious. Injury is considered a healthy side-effect of normal competition. Some price discrimination may be healthy even if it is injurious. Differences in supply and demand conditions between different national markets actually require price discrimination according to traditional economic theory. After all, prices are supposed to be determined by supply and demand conditions in market economies. These conditions vary from country to country. Therefore, a single firm's prices should vary too.

If normal price competition -- unsubsidized, undumped, imports -- can cause injury, and if not all dumping is injurious, then a question arises. How does one tell the difference between the effects of injurious dumping and the effects of injurious, but healthy competition? This question is crucial. If they are not distinguished then the law can be used to penalize healthy and normal price competition. Generally, this problem has been resolved by asking another question. Who is injured? Is there injury to competition or injury to competitors?

Domestic competition policy has adopted the injury to competition standard. Divergences from it have been vigorously condemned by the Courts. The central purpose of the 1936 Robinson-Patman Antitrust Act was to make this standard explicit. The report issued by President Johnson's White House Task Force on Antitrust Policy in 1968, confirmed,

"The reference to injury to competition with specific persons has focused the attention of courts and enforcement authorities on the plight of the individual competitors, and enforcement designed to preserve competitors is at odds with the workings of a competitive system. The proper focus is the effect on competition in the market as a whole."<sup>30</sup>

The judiciary has further confirmed the "competition, not competitors" standard, as Diane Wood notes<sup>31</sup>, in Brown Shoe Co. v. US<sup>32</sup> and Cargill Inc. v. Monfort of Colorado Inc.<sup>33</sup>.

Domestic competition policy requires that the injury be sustained by the customers.<sup>34</sup> Antidumping policy, in contrast, has adopted an injury to competitors standard. The impact on customers is mostly ignored. As a result, Klaus Stegemann argues, "Antidumping measures almost always adversely affect the interests of consumers."<sup>35</sup> When measuring injury the investigator<sup>36</sup> is statutorily required to examine the following:

"... output, sales, market shares, profits, productivity, return on investments, utilization of capacity, cash flow, inventories, employment, wages, growth, investment, existing production and development efforts including the ability to develop a derivative or more advanced version of the product and the ability to raise capital."<sup>37</sup>

These indicators reveal little about the "disfavoured customers"<sup>38</sup>, who are the focal point of domestic competition policy. They reveal more about performance of individual firms than the industry as a whole. In addition, many of these indicators, such as return on investments, reflect the management decisions of domestic firms. Thus one reaches the conclusion reached by Bart Fisher. Given that there is no requirement under the AD or CVD law that the complainant's firm be managed efficiently, such criteria are bound to reveal little about the reasons for changes in the indicators.<sup>39</sup> The causal link between dumped imports and, for example, return on investments seems tenuous at best.

The divergence between the two competition policy measures has generated literature which cannot be fully addressed here.<sup>40</sup> Harvey Applebaum most succinctly confirms the judgement of most of this writing. The antidumping and antitrust laws, he says, "cannot realistically be reconciled"<sup>41</sup>;

"the antitrust laws are designed to promote free and open competition .... " "In contrast the trade laws are designed to protect United States industries, companies, and workers from unfair import competition, or in one statute (Section 201 of the Trade Act of 1974) from fair import competition. In other words, they are, in general, designed to protect United States competitors without regard to the impact on competition or competitive markets" (emphasis added).<sup>42</sup>

Recognizing the importance of this divergence the Organization for Economic Cooperation and Development produced a report on it in 1984. Diplomatically the purpose of the report was described as follows.

"[T]o examine, in particular, possible long-term approaches to developing an improved international framework for dealing with problems arising at the frontier of competition and trade policies."<sup>43</sup>

The OECD did not explain why there should be a frontier between the international and domestic policy tools. After all, their objective is supposed to be the same: the enhancement of competition.

The contradiction between domestic and international competition policy objectives is significant because it means the antidumping laws are no longer merely "potential hatchets of rear guard protection"<sup>44</sup> as former Trade Commissioner Peter Ehrenhaft prophesied in 1958 they might be. It means that there is a long history to what Jagdish Bhagwati calls the "protectionist capture" of the AD law.<sup>45</sup> Claims by the United States that it uses antidumping policy to enforce a "market standard" of behaviour and claims made by the general rhetoric of free trade and competition are plainly refuted by the contradiction between antidumping policy objectives and domestic competition policy objectives. If the United States is not asking others to abide by a market standard then what is it asking them to do?

The shift from targeting the intent of dumping to targeting its effects is important for another reason. This shift makes the distinction between fair trade, and unfair trade less clear. The impact of anticompetitive behaviour is the focus, not the source. If the United States is defining dumping so that fair and legitimate trade practices are actionable under the law then it is acting to undermine competition.

Another profound change occurred with the passing of the 1921 antidumping provision. Because jurisdiction had proved to be such a problem, the 1921 Act eliminated the criminal remedy on which all former antidumping law had been based. Instead, it provided an administrative remedy. That is, instead of punishing or deterring the foreign

producer through a criminal procedure, the new law, and all subsequent antidumping law, targets and penalizes the actual imports.

In theory, the administrative procedure works as follows. When American industries allege that imports are dumped an official AD investigation is undertaken to substantiate that claim. If dumping has occurred then the amount of dumping must be determined -- that is, the difference between the dumped price and the home market price. The result is called the dumping margin. If injury caused by the dumped imports is also found, then the standard procedure is to issue a positive finding and levy a tax on the dumped imports. The tax (which is called a duty) is then applied to the goods at the border which should be equal to the dumping margin. In this way the United States authorities can equalize the terms on which the imports enter the market. The tax offsets the dumping. The imports are then available at a "fair" price and do not compete "unfairly" with domestically produced goods. Theoretically, all this can and should be done without questioning or passing judgment on the foreign firms' motives or pricing policies and without subjecting foreigners to the United States domestic legal system.

The administrative procedure removes culpability in the legal sense. It also eliminates the necessity of substantiating predatory behaviour. But, the application of the term "unfair" to dumping practices, John Barcelo explains, "has origin in tort law where they (references to unfairness) have been used by plaintiffs to obtain relief against various deceptive and unscrupulous business practices".<sup>46</sup> The original subjection of foreigners to criminal proceedings has imbued dumping with a criminal quality which is legally and economically meaningless under the current administrative procedure. In practice, however, dumping is still popularly considered "unfair".

The belief that foreigners are being "unfair" fuels the broadening definition of dumping. It is ironic, but an increasing number transgressors has been seen as a good indicator of the law's effectiveness. "Protectionists", who are well aware that the law can be used to tax, limit or exclude both fair and unfair imports (that is, any injurious imports) have sought to strengthen the law. "Free traders", believing that they are serving

the cause of free and fair competition, have pressed for the same goal. As a result, there has been a tendency to stretch the law to further increase both the number of actors and the kinds of activities which are actionable under it.

This tendency has been neither steady nor the result of concerted action. Rather it is the result of an accumulation of often unconnected but deliberate changes, which, in the tradition of common law, result in the ramshackle structure suggested by Frederich Davis' allusion to a cathedral.<sup>47</sup> Nevertheless, the fairly constant direction of change in the law is easily discernible. One result is that the law allows the United States to pass judgement on foreign actions with greater ease and justification in spite of the administrative procedure. The increased authority to take action against foreigners who are perceived to be transgressing the law. In this next section we examine other statutory and administrative changes in the law which have broadened the scope and the reach of the antidumping law.

There is one particularly interesting feature of this process of change. As the law is made more "effective" it's original purpose, the enhancement of competition, is subverted. Yet, American politicians and diplomats have continued to claim that the law has been changed only to further the interests of "free trade". The rhetoric obscures the reality and justifies actions which are in opposition to the laws' supposed aims.

1. John Barcelo, "Antidumping Laws as Barriers to Trade -- The United States and the International Antidumping Code" Cornell Law Review Vol. 57, No. 4, April, 1972, page 494.
2. John Barcelo poses the question as follows: "Given the existence of these antidumping laws, countervailing duty laws, escape clause laws -- we must begin by asking what we want to achieve with them." Interface One, Conference Proceedings on the U.S. Antidumping and Countervailing Duty Laws from State-Owned Enterprises, Don Wallace ed., (Washington: Institute for International and Foreign Trade Law, Georgetown Law Centre, 1980) page 181.
3. William Arthur Seavey, Dumping Since the War: The GATT and National Laws, Doctoral Thesis, Harvard Law Library, 1970. Cited by Toby S Myerson in "A Review of Current Antidumping Procedures: United States Law and the Case of Japan" Columbia Journal of International Law Vol. 15 No. 2, 1976, Note 2, page 168. Often cited as Dumping Since the War (Oakland: Office Services Corporation, 1970).
4. The Concise Oxford Dictionary of Current English, HW Fowler and FG Fowler ed.s., (Oxford: Clarendon Press, 1929)
5. Congress HR Rep. No. 1, 67th Congress 1st. Sess. 23 (1921).
6. Brian Hindley, "Protectionism in the GATT" Financial Times Friday June 7, 1991.
7. Peter Ehrenhaft "Protection Against International Price Discrimination: US Antidumping and Countervailing Duties" Columbia Law Review Vol. LVIII, 1958, page 60.
8. Gary Horlick, "The United States Antidumping System", Antidumping Law and Practice: A Comparative Study John Jackson and Edwin A Vermulst ed.s., (New York: Harvester Wheatsheaf, 1990) page 130.
9. States do not dump. When states dump it is called "subsidizing". The Countervailing Duty law, which is used to remedy subsidization, is discussed in Chapters Seven to Nine. Although, there is an obscure and never used and undefined stipulation in the countervailing duty law for "private subsidization".
10. Article 2 paragraph 1.
11. See the earlier discussion of non-justiciability in Chapter Three, page 69, especially note 64, *infra*.
12. Adams and Dirlam, Note "The Antidumping Act -- Tariff or Antitrust Law?" 74 Yale Law Journal, 1965, page 709.
13. Samuel Elliot Morrison, The Oxford History of the American People (New York: Oxford University Press, 1965) page 762.
14. Standard Oil vs US, 221 US1 (1911).
15. Samuel Elliot Morrison, The Oxford History of the American People page 762-3.
16. SE Morrison explains that it took long because: "These exactions and abuses were long tolerated by Americans, so imbued were they with laissez-faire doctrine, so proud of progress, improvement, and development, and so averse from the increasing power of government." *Ibid.*,



page 764.

17. See Roy Prosterman for further support of the notion of antidumping as anti-trust. Lampadephoria "Withholding of Appraisal Under the US Anti-Dumping Act: Protectionism or Unfair Competition Law?" Washington Law Review, Vol 41, 1961. Also see Barbara Epstein, "The Illusory Conflict Between Anti-Dumping and Anti-Trust" 18 Antitrust Law Bulletin, 1974.

18. Report of the Boggs Committee, Report to the Committee on Ways and Means from the Subcommittee on Customs, Tariffs and Reciprocal Trade Agreements, US Customs, Tariff and Trade Agreements Laws and Their Administration, 85th Congress, 1st Session 95-96, 1957.

19. 1909 213 US 347, 29 S. Ct. 511, 53 L. Ed. 826.

20. 1916 Revenue Act (64th Congress) Sept 8, 1916.

21. Rodney Grey, Trade Policy and the System of Contingency Protection in the Perspective of Competition Policy unpublished paper commissioned by the OECD, Paris 1986.

22. Jacob Viner, Dumping: A Problem in International Trade (Chicago: University of Chicago Press, 1923).

23. Price discrimination may involve selling abroad at prices higher than those charged for the same goods domestically. Dumping implies selling abroad at a price which is lower than the domestic price.

24. Alexis Coudert, "The Application of the US Antidumping Law in the Light of a Liberal Trade Policy" Columbia Law Review, Vol. 65, No. 2, February 1965, pages 190-191.

25. John Barcelo, "Antidumping Laws as Barriers to Trade" page 519. Toby S Myerson, "A Review of Current Antidumping Procedures: United States Law and the Case of Japan" Columbia Journal of Transnational Law Vol. 15, No. 2, 1976, page 173.

26. 15 USC Sect. 72 (1970).

27. Rodney Grey, Contingency Protection.

28. The Sherman Act and Clayton Act refined such notions.

29. Cite the law for "if an industry is hurt or likely to be or prevented from being established by imports which involve price discrimination".

30. From the Neal Report, 1968, President Johnson's White House Task Force on Antitrust Policy. Cited in Unfair Trade Practices and Consumer Protection: Cases and Comments S Chesterfield Oppenheim, et al., ed.s., (St. Paul, Minn.: West Publishing Co., 1983) page 761.

31. Diane P Wood, "'Unfair' Trade Injury: A Competition-Based Approach" Stanford Law Review, Vol. 41, 1988-89.

32. Brown Shoe Co. v. US, 370 U.S. 294, 320 (1962).

33. Cargill Inc. v. Monfort of Colorado Inc., 479 U.S. 104,115 (1986).

34. This is called secondary line injury.
35. Klaus Stegemann, "Anti-Dumping Policy and the Consumer" Journal of World Trade Law, Vol. 19, No 5, Sept:Oct 1985, page 467.
36. The responsibility for injury determinations has shifted from the Treasury to the Trade Commission in 1954.
37. 19 USC Section 1677 (7)(c) as amended by Section 1328 of the 1988 Trade and Competitiveness Act.
38. Harvey Applebaum and David Grace, "US Antitrust Law and Antidumping Actions Under Title VII of the Trade Agreements Act of 1979", Antitrust Law Journal Vol. 56, Issue 2, Proceedings of the 35th Annual Meeting 1987, page 509
39. Bart Fisher, "The Antidumping Law of the United States: A Legal and Economic Analysis" Law and Policy in International Business Vol 5, 1973.
40. Harvey Applebaum and David Grace, "US Antitrust Law and Antidumping Actions Under Title VII of the Trade Agreements Act of 1979" Antitrust Law Journal Vol. 56, Issue 2, Proceedings of the 35th Annual Meeting 1987. Rodney Grey, Trade Policy and the System of Contingency Protection in the Perspective of Competition Policy, (Paris: OECD, 1986). Competition and Trade Policy: Their Interaction, OECD 1984. Diane P Wood, "'Unfair' Trade Injury: A Competition-Based Approach" Stanford Law Review, Vol. 41, 1988-89.
41. Harvey Applebaum, "The Interface of Trade/Competition Law and Policy: An Antitrust Perspective", Antitrust Law Journal Vol. 56, Issue 2, 35th Annual Meeting San Francisco California, August 10-12, 1987.
42. *ibid.*, page 409.
43. Competition and Trade Policies: Their Interaction, page 9.
44. Peter Ehrenhaft "Protection Against International Price Discrimination", page 76.
45. Jagdish Bhagwati, Protectionism, page 52.
46. John Barcelo, "Antidumping Laws as Barriers to Trade", page 502.
47. See the relevant quote from Frederick Davis, "The Regulation and Control of Foreign Trade" Chapter Three, page 63, Note 52 *infra*.

## **CHAPTER FIVE -- OPERATIVE TERMS**

There are several terms with which it is crucial to be familiar if we are to understand AD policy. In addition to the term dumping, there are other operative notions in the antidumping statutes. For a positive finding the statute requires that an industry exist in the United States and that the industry as such is injured. Of course, injury can be caused by fair imports or domestic competition or recession or many other factors. Therefore, the statute requires that injury must be caused by dumped imports. The domestic industry qualifies for standing, that is the right to file an AD petition, only if the imports are "like" the product(s) made by the domestic industry. During the investigation injury only to the producers of "like" products can be examined. To reiterate, the main operative notions, as they are referred to by the legal community, in the AD law are "dumping", "domestic industry", "injury", the causal link between imports and the injury incurred by the "domestic industry", "like" product. There are other operative terms as well which will be examined. The important point about these terms is, as John Barcelo makes clear,

"Each concept .... can be infused with a different meaning depending on the objective in mind ... "<sup>1</sup>

The definition of the term dumping and these other terms (i.e., like product, domestic industry, injury, cause) is for this reason, extremely relevant to an understanding of the objectives sought with this technique of economic statecraft.

### **DUMPING AS SALES AT LESS THAN FAIR VALUE**

Of the very different definitions of dumping which have been used in domestic law two are important. The first is "sales at less than fair value" (LTFV) which the statute has applied since 1921. The 1974 Trade Act added a new statutory standard: "sales below costs" (SBC). Both LTFV and SBC are consistent with the GATT "normal" standard since

sales at prices which are below these standards are not considered (by the United States) to be "normal in the ordinary course of trade".

Dumping defined as sales at LTFV allows the United States authorities try to compel foreign to provide their merchandise at a "fair" price. But, what is a "fair" price?

Dumping by firms from non-market economies always poses a ridiculous problem. How can one determine the home market price, let alone a "fair" one, when there is no price mechanism? Why should a such a company be expected or required to have a particular pricing policy anyway? The absurdity of calculating dumping margins for non-market economies was finally recognized in the 1988 Trade and Competitiveness Act. Now imports need only exceed trigger levels to be considered dumped or subsidized. There will no longer be any need to fabricate non-existent prices since the presence of margins is not necessary to execute the law.

The problems of measuring "normal" and "fair" prices are inherent in market economy cases as well. William Taussig, one of the great trade experts, posed the same question that we now face as early as 1930. "In all such discussions," he explained, "we are confronted with the question, is there a "fair" profit or a "normal" price?"<sup>2</sup> Is there a universal "normal" value or a "fair" price among the market economies? Differing shareholder expectations, differing inputs costs, differing management strategies among many other factors mean that a "fair" price for a foreign firm is bound to be less or more than for a United States firm. There is no inherent and universal "fair" price. Nor is there a single legitimate set of priorities firms must pursue when making pricing decisions. When investigators calculate the dumping margin they do not have a fixed point of comparison. Not only do corporate pricing policies vary. Costs vary -- this is supposed to be the reason why international trade occurs in the first place. And market elasticities vary. The supply and demand conditions, which determine prices, vary from one national market to another. For this reason, traditional economic theory posits that international competition actually requires price discrimination.

By assuming that prices or all pricing policies should be the same, the law becomes a mechanism with which the United States imposes its own ideas on foreign firms about how those firm ought to price their goods.<sup>3</sup> Antidumping policy is used to compel foreign firms to behave in the market the way the United States authorities think they "should". Here politics confronts us as the major issue. Ideological differences are profound among states and diverse firms as to how firms "ought" to behave in commercial affairs. If foreign firms will not change their opinions about the "proper" way to do business, anti-dumping policy is an effective means of compelling foreign firms to modify their behaviour in compliance with the United States' demands.

There is no express statutory definition of "fair value". That is left to administrative interpretation. "Fair value", at least from 1921 until 1955, was interpreted to mean "foreign market value"<sup>4</sup>, which was defined as the price available in the home market or, if there were no home market sales, then it was the price "freely offered ... to all purchasers" in a third market.<sup>5</sup>

In 1955, the interpretation changed when an amendment from the 1954 Act required that the volume of home market sales be "sufficient to form an adequate basis for comparison".<sup>6</sup> This opened the door for United States authorities to use sales in third countries as the benchmark and to "construct" the foreign market value. However, it was assumed that the prices in third markets might also be dumped prices. Not wanting to rely on foreign conceptions of a "fair" price, the United States began to mathematically define fair value. Peter Ehrenhaft explains that this was a "novel departure" from the previous practice. "But", he went on, "it is difficult to see how a mere exercise in arithmetic can suffice to determine whether dumping, in its predatory sense, exists."<sup>7</sup>

We know that predation was no longer technically necessary under the law. Ehrenhaft was objecting to the way in which all sales which were less than the home market price, whether predatory or not, whether they were less than the home market price for the long-run, the short-run or sporadically, regardless of differing market elasticities, would now be considered unfair and actionable. So we see that as early as 1955

the concept of "unfair" trade had begun broadening to cover previously fair trade practices.

Pricing policy is a complex subject, although antidumping policy assumes that it is not. In a market economy prices are supposed to be determined by supply and demand. Under conditions of perfect competition, which have not often been found to occur in this world, firms ought to offer a product at a price which is just high enough to cover marginal costs (the cost of making the thing). Paul Samuelson states:

"Only when prices of goods are equal to marginal costs is the economy squeezing from its scarce resources and limited knowledge of technology the maximum of outputs."<sup>8</sup>

Ostensibly competition keeps the price from rising above that level. However, firms engage in business for one major reason -- profit. Marginal cost pricing does not allow for a profit margin. Since competition is rarely perfect, i.e. sufficient to keep prices at the level of marginal costs, firms can raise the price to allow for a profit margin. Under these conditions cost-plus pricing is considered to be, theoretically, the most efficient way to price goods.

Cost-plus pricing means prices are determined by calculating the average cost of producing the good and then adding an allowance for profit. How much allowance for profit is "fair"? Turning to a layman's guide, we find that the Penguin Dictionary of Economics explains that the profit margin is "loosely determined by market conditions".<sup>9</sup> Since there is no universal figure for the plus part of cost-plus pricing, nor is there any universal criteria for determining what a profit margin should be, the antidumping law is a means of holding foreign firms to a theoretical standard of behaviour which has little substance in reality.<sup>10</sup> Very few American firms would escape legal action if they were legally compelled to adhere to strict cost-plus pricing.<sup>11</sup>

Under the LTFV standard the antidumping law the United States assumes that profit maximization is the sole or major goal for all firms. However, not all pricing theories assume this. Many firms put other priorities such as increasing the market share, new product development, and return on investments above profitability. The

"discrepancy"<sup>12</sup> between theory and practice is very real. The problem is exacerbated by the fact that conceptions of profitability depend upon the time frame applied. American firms are often required to show profitability on a quarterly basis. Shareholders, particularly institutional funds, demand dividends or capital gains which arise from these quarterly profits. German and Japanese firms, in contrast, do not risk their capitalization as long as profitability appears in the long run, such as over the course of one year. As such, the law is a means by which the United States can put pressure on foreign firms to behave as if profit maximization in the short run is the only normal and legitimate goal around which pricing policy should be shaped.<sup>13</sup> But, there is absolutely no international consensus that profit is the only legitimate objective firms should aim to achieve.

AD policy raises a couple of profound questions. What is the appropriate function of firms in a market economy. In whose interest is a firm run? These questions stand at the centre of the current debate on industrial competitiveness. For example, in the American model of capitalism the firm serves the shareholders. These shareholders invest in the firm primarily for one reason. They wish to make a profit. This can be achieved either through dividend payments or by selling the shares. If the firm fails to increase its profit then shareholders tend to abandon the firm.

But, in the Japanese model the firm is run in the interests of the "stakeholders". These include shareholders but also "employees, suppliers, customers and neighbours" according to W. Carl Kester in his study of Japanese firms.<sup>14</sup> Dividends in these firms are often extremely low. The management of Japanese firms often emphasise growth and sustaining relationships between the firm and its suppliers and customers.

If we look at Germany we see yet another model of capitalism at work, though in the following respects it is similar to the Japanese model. In Germany ownership of firms is often held by a variety of other firms and banks through strategic cross-holdings. Individual firms can afford to sacrifice short term profitability for other goals without fear of a hostile takeover or of losing their investors. As in Japan, German shareholders

are willing to let the firm retain its profits (instead of giving them out to shareholders as dividends as is done in the United States). Thus, firms are often able to build up large cash mountains. This cushion of capital allows them to sacrifice profitability during a downturn or in favour of growth or enhanced market share or other objectives.

We should now recall the quote by Henry Kissinger offered earlier in this dissertation. He referred to the fact that differences in domestic structures, and differences in the concept of legitimacy upon which those structures are based, can lead to antagonism when attempts are made to address the problems which arise from the very existence of those differences.<sup>15</sup> Differences in opinions and perceptions about the appropriate role of firms in a market economy among the industrialized countries are increasingly giving rise to contention. Though it may seem controversial to put it this way, there are profound ideological differences among the market economies. John Zysman points out, the US has been "... slow to recognize that there was more than one form of capitalist market economy". "After the war (WWII) the United States tended to view deviations from its own form of capitalism as either only partial modernization or apostasy."<sup>16</sup>

Nevertheless, there is more than one model of capitalism. Firms are bound to behave differently according to the model in which they operate. The nature of a given model of capitalism may vary, for example depending on the structure of the financial market. John Zysman tells us "... Japan and Germany, chose to emphasize investment in production over consumption." "Those differences in policy and institutional structure created distinct patterns of market logic, and thus certain types of firm strategies." <sup>17</sup>

AD policy then, is an ideological instrument. It aims to convert foreigners to the American model of capitalism. The implicit message conveyed with AD policy is that firms ought to behave in conformity with the American model. There is bound to be increasing conflict among the capitalist countries over these issues. Not only is there no agreement as to which model is "best". Now that Japan and Germany and other market



economies have begun to rival the United States, which model is best is even more subject to question.

Now let us return to the methodology employed in AD investigations, keeping this ideological question in mind. Since "fairness" is mathematically defined, it is important to explore the calculation methodology carefully. It sounds simple enough; the Commerce Department (since 1974, before then Treasury had this responsibility) determines the margin of dumping by comparing the United States sales price to "fair value". But it is not simple. Fair value is generally taken to mean the home market value of "such or similar" merchandise. Value is too subjective a concept to be easily applied in AD investigations. Value actually refers to a specific price in AD cases. Although it is not required by law to do so, the Commerce Department usually takes individual sale prices in the foreign market to calculate a weighted average for each firm in the foreign nation which is allegedly dumping. Against this weighted average Commerce then compares the US price of the product in question. The US price is either the "purchase price", the price at which an unrelated buyer purchased the good before it entered the United States, or the "exporters sale price"(ESP)<sup>18</sup>, meaning the ex-factory price, which is used when the seller and the importer are the same (in which case the sale of the good occurs after it enters the United States).<sup>19</sup> Commerce "adjusts" the ex-factory price, the ESP, for direct and indirect costs so that differences in the circumstances of the sale can be balanced. This allows "apples" to be compared to "apples" and not to "oranges". Traditionally, counsel (both the petitioner's and the respondent's) devote the majority of their time to issues involved in the determination of injury, and these price and cost adjustments.

It is telling that this methodology differs from that employed in domestic competition policy cases. Until 1950, the Federal Trade Commission attempted to establish the difference between the actual invoice price and the delivered price. If customers in New York and California were both charged a \$10.00 invoice price but the shipping cost to New York was only \$1.00 while it cost \$3.00 to ship it to California then the FTC held that the firm was using the New York sales to subsidize the California sales. This notion

of price discrimination was abandoned in 1950.<sup>20</sup> Since then, only the actual invoice price has been used.<sup>21</sup>

In contrast, the ESP is always adjusted for direct costs such as shipment costs, packaging, insurance and indirect costs such as overhead, advertising, salesmen's salaries.<sup>22</sup> When the Treasury was responsible for antidumping determinations it did not bother to make adjustments. They did not compare apples to oranges. They simply issued findings of no injury.<sup>23</sup> So the AD investigations resulted in negative findings. By 1958 the Congress became alarmed that too many cases were being dismissed in this way. That year, the authority to determine injury (as opposed to dumping) was transferred to the Tariff Commission and required that adjustments be undertaken so that a determination could be made. But foreigners started claiming many expenses. Hendrick explains;

"The resultant home market price calculations were claimed by them to be reduced to a point where initial apparent disparities again and again would, if the claims were allowed, completely disappear."<sup>24</sup>

In response, various administrative practices were implemented to allow a fair comparison to be made which, at the same time, would prevent the elimination or reduction of dumping margins by the administrative procedure. Clearly this objective implies that distortions to real prices will be entertained by United States officials when necessary. For example, in 1960 a Treasury regulation was implemented which required that expenses bear a "reasonably direct relationship to the sales".<sup>25</sup> These include different credit terms, warranties, technical assistance etc., but not including differences in advertising costs. "Reasonably" is not statutorily defined. In effect, this ambiguity as to the term "reasonably" allowed indirect costs to be entirely excluded from the ESP. While this was done only for the sake of simplicity and administrative convenience, it was implemented "at the expense of fair price comparisons under the Act".<sup>26</sup> As a result, the United States officials have been more likely to find a different "fair price" when the United States purchase price is used than when the ESP is used. But, the circumstances of the sale should not change the fairness of the home market price. Paul Victor and Thomas Ehrgood carefully argue;

"... the goal of making a fair comparison appears to have been compromised by, first, the Treasury Department and, subsequently, by the Commerce Department, arguably in the interest of administrative simplicity and convenience in light of the extensive claims which were being made."<sup>27</sup>

Identifying which costs are going to be included (whether direct or indirect) and deciding how those costs will be calculated, constitutes a very large area of discretion. For example, Commerce assumes that direct selling expenses are very low because goods are sold in arms-length transactions to the domestic importer. Salaries for salesmen, which are usually accepted as a direct expense, is considered an indirect expense, and therefore not subtracted from the price to price comparison. Commerce "caps" the value of indirect expenses from the foreign price but full deductions from the United States price are allowed. Bart Fisher explained in 1973 that "carte blanche authority" was available to administrative authorities to preclude almost any circumstances of sale due to ambiguously defined regulations.<sup>28</sup> This means that comparisons are made between prices which reflect very different conditions of sale. As a result, the ensuing dumping margins reflect administrative discretion more than real price differences.

Paul Jameson condemns United States AD methodology for focusing on costs altogether. He says, "... the ITC should recognize that producers do not generally set prices with a view to a myriad of small costs -- prices are set more by the market than by the cost of production."<sup>29</sup>

Robert Herzstein demonstrates most persuasively that administrative discretion with regard to adjustments alone can create a dumping margin.

"The technical rules used in antidumping proceedings can, and often do, result in findings of dumping where there is no price discrimination between markets. For example, even if the prices and terms and conditions of the sale are identical in both markets, an administering authority might find dumping margins."<sup>30</sup> He elaborates in an attendant footnote, "Such a finding can result from the limitation on the adjustment for indirect selling expenses. Dumping margins might also be found, when prices and terms and conditions of the sale are identical in both markets, if the prices of transactions in the home market are averaged, but the price of export transactions are not averaged and are compared individually with the average home market price."<sup>31</sup>

Where do the United States authorities get the information which allows them to make appropriate adjustments? The respondent firms are often unwilling to provide in-

depth information since the petitioners, their American competitors, have access to a great deal of the material submitted to both Commerce and the ITC. Commerce makes all of the "non-sensitive" information available to all of the parties when an investigation commences, primarily legal and economic counsel, if such counsel sign what is called an Administrative Protective Order (APO).<sup>32</sup> Under the terms of an APO, which are "routinely issued",<sup>33</sup> lawyers who divulge information gleaned from the proceedings can be disbarred. However, how likely is it that the chief corporate counsel upon learning about the opposition's costs and market structure, is not going to relay the information to his firm? Who in his own firm would report him anyway? The ITC, in contrast, does not allow access to the entire record for precisely this reason.

The terms of access to the information is very important, as Donald Cameron and Susan Crawford highlight.

"Since the bulk of the material received by the ITC comes from US industry, while Commerce receives the majority of its data from foreign respondents, what has occurred since the enactment of the Tariff Act (of 1979) is a basic inequity in the treatment of confidential information."<sup>34</sup>

Even if accurate information is provided by the respondent, are adjustments made to compensate for differing accounting standards and practices? Evidently, Commerce uses foreign information, when it can get a hold of it. But, it will use the foreign respondent's information only if the information corresponds to "Generally Accepted Accounting Principles". But, differences in national accounting practices are substantial, to say the least. Instead, Commerce often relies on information about the respondent which the petitioner must supply when making the allegation.

Given the number of judgments which come into play in determining the ESP alone it seems safe to say that "adjustments" mark the entrance to a battleground of numbers. The discretion available to American officials to manipulate, to include or exclude, to verify or to not verify the figures is large. Where there is discretion there is susceptibility to political pressure. The more "technical" the procedure becomes the more political it is. This is truer still because the American judiciary has upheld the administrative authorities' freedom to change the calculation methodology<sup>35</sup> not only

from one case to another but during a single investigation. The United States courts have held that Commerce may use its discretion in calculating the margin. Indeed it has confirmed Commerce may even recalculate the margin immediately after final determination.<sup>36</sup> As such, antidumping policy becomes a means of pressing upon foreign firms actions which the United States desires.

Once the ESP has been adjusted Commerce compares each individual US sale to the single weighted average foreign market value (FMV). The decision to use individual US sales or a weighted average determines the outcome.<sup>37</sup> When the FMV is higher than the US price (this is absurdly called "negative dumping") Commerce does not balance these higher prices against the sales which are below the US price. Effectively this means that if there is a single instance when the US price is lower than the home market value a dumping margin will be found. The only way a margin can be avoided is if every single US sale price is equal to or higher than the weighted average. The prices which are below the home market value are converted into a percentage of the US price. After each single US price is compared in this manner a weighted average of the US prices is constructed. The weighted US average and the weighted foreign market value average are then compared to determine the final dumping margin.

Harvey Applebaum and David Grace have proved that this procedure is mathematically likely to result in a dumping margin even when the "average price charges by an importer in the US meets or even exceeds the average price charged abroad". They provide this telling example. The foreign market value for each unit (each widget) is \$100. The single US prices (already adjusted) are found to be \$75 for 10 units in one instance, but \$100 for 10 units in another instance and \$125 for 10 other units in another. The \$75 units are therefore found to be dumped by \$25 per unit. The \$100 units are not found to be dumped and there is no margin. The \$125 units are priced \$25 each over the foreign market value so there is no dumping margin. Only the \$75 units are used in the final dumping calculation; the others are examples of "negative dumping" (such an unhappy phrase) since they are not below the foreign market value. Ten units dumped by

\$25 equals a value of \$250. The total dollar average of US sales is ten units times \$75 (\$750) plus ten more units times \$100 (\$1000) plus ten more units times their value at \$125 (\$1250). Added together this equals a value of \$3000. When the \$250 dumping margin on the single sales is divided by \$3000 (the value of all the US sales) the result is an overall dumping margin of 8.34%. In spite of the fact that two third of the imports were not dumped, and one third of the imports were above the home market price, it was still possible to find a margin of 8.34%.

Brian Hindley points out yet another bias towards a finding of dumping inherent in the methodology. He asks: What is "the" home-market price or "the" export price? Prices fluctuate over time. The Home Market price is the reference price, representing an average price. But, when choosing which prices to include in that average the United States does not include sales which, according to the US, are made below cost (as long as such sales do not exceed 10% of all sales). This is done because sales below cost are not considered "normal" "in the ordinary course of trade". Thus, reference price is composed of average of "normal" prices. In other words, the US cuts out the lowest priced of the home sales and in doing so raises the home market price. This procedure is bound to make the export prices look worse than they would otherwise. The procedure is, as far as he is concerned, "absurd".<sup>38</sup>

There is one more step which renders the calculation methodology flexible. The foreign market value must be converted into US dollars before the comparison with the US prices are made. In an era of floating exchange rates which exchange rate is used? Apparently only "actual exchange rates" are used. David Palmeter points out, however, that there are several exchange rates at any one time. For example, there is the exchange rate for interbank lending, there is the exchange rate which is recorded by the International Monetary Fund, there is the commercial exchange rate which is available to the firm when making the transactions in question. The choice of rate, Palmeter shows, can alone create a dumping margin.<sup>39</sup> In addition, spikes and lags in the rate are ignored; this raises a question about what is included in the rate. Actually, whether a single day's rate or an

average of daily "actual" exchange rates is used is not the central issue. Firms do not adjust their prices to reflect daily or even monthly exchange rate fluctuations and it would be ridiculous to expect them to do so. But, the antidumping margin calculation methodology makes no exception. As such, margins can be created by fluctuations in the value of a national currency; and they often are.

Nowadays the policy is as follows. If major fluctuations eliminate a previous (allegedly) existing margin then the rate from the previous quarter is used to calculate the margin. Fluctuations which create a margin where none previously existed are acceptable. In the case Melamine Chemicals<sup>40</sup> (1979) it was made clear that it is unclear as to how many quarters back US officials can go. The decision implied the US can go as far back as it likes within reason.<sup>41</sup> What "within reason" means is, as usual, not defined.

The administrative agencies must comply with deadlines, which it is universally acknowledged are extremely short. Congress has attempted to make the law more "effective" particularly since 1974 by shortening these deadlines. Peter Ehrenhaft, a former ITC Commissioner confirms that the shortness of time in investigations means true FMV cannot be calculated.<sup>42</sup> If the allegation is levied against many dumpers, either in one country or several, Commerce cannot possibly investigate all of the firms in the specified time period. The deadlines have been shortened partly to increase the possibility of higher margins and partly to encourage respondents to arrange a settlement before the investigation commences with a quantitative orderly marketing arrangement.<sup>43</sup> In other words, the shortened deadlines alone are a major contributing cause of anticompetitive solutions to allegedly dumped imports.

To the outsider, the mathematical procedure gives the appearance of precision. From the technicality of the procedure one tends to assume that it is equitable and impartial. But, the procedure is not only biased against the petitioner. The numbers are not "hard"; they are actually quite pliable. The calculation process is automatic in the sense that an investigation must ensue once a petition has been launched. And the investigation must be completed within certain fixed deadlines. But, in fact, the calculation process

itself, once the investigation has commenced, is susceptible to various judgements. Having examined closely the technical procedure by which the numbers are manipulated, it is apparent that there is a clear political imperative which motivates the calculation process. Within the technical procedure a political desire to compel others to behave in a way that the United States finds "normal" is clear. The mathematical calculation procedure exemplifies the way in which the United States is, as Gary Horlick suggests, "... indulging in the fiction of measuring some degree of unfairness."<sup>44</sup> David Palmeter rightly tried to draw attention to this when he said, "economically meaningless measures of fair value are often used".<sup>45</sup>

Let us now remember that home market value is only used if home market sales account for at least 5% of all exports during the period under review.<sup>46</sup> If there are less than 5% then third market prices are used. This immediately raises a question. How can the firm possibly be subsidizing its exports from home sales which account for only 5% of sales? Presumably sales to the United States are subsidized by sales in third markets. However if there are also insufficient third market sales to form a basis of comparison then Commerce officials must "construct" the foreign price.

Since existing figures and information are malleable enough, the Commerce Department has generally tried to avoid having to construct FMV. However, in recent years United States petitioners have increasingly asserted that the home market prices used by Commerce are invalid either because they are fictitious or because they reflect sales at prices which are below the cost of production.

Ever since the definition of dumping was broadened to cover SBC in 1974, there have been more examples of constructed value. The next section of this chapter addresses the complex issues involved in determining costs, whether for SBC or constructed value determinations.



## DUMPING AS SALES BELOW COST

A sales below cost standard of dumping was first introduced in the 1921 Act. It was feared that foreigners would undervalue their exports in order to reduce the level of tariff duties payable upon entry into the US. To counter this possibility, the law provided that fair value, when it had to be constructed due to lack of sales in the home market, would be based on the foreign firm's fully allocated cost of production plus a minimum of 8% for profit and 10% for general expenses. This SBC standard was made available as a definition of dumping alongside the LTFV standard in the 1974 Trade Act, with surprisingly little discussion, as a more stringent statutory standard.<sup>47</sup>

Under the SBC standard, dumping occurs when the producers' home market price is below the cost of producing the good. For the first time, dumping need no longer entail price discrimination. The price offered in the United States is relevant only insofar as provides the petitioner with the grounds for making an allegation that the foreign firm is dumping. The sales in the United States do not need to be below cost, such sales can be at LTFV.<sup>48</sup>

The dumping margin in SBC cases is determined by finding the difference between the home market price and the cost of production. Investigations set out to establish the foreign firm(s)' "true" cost of production. Under the SBC standard the antidumping law is used to compel foreign firms not to sell below their costs of production -- at home or abroad.

When the United States constructs a foreign firm's costs it employs the following formula: the cost of materials and fabrication + 10% for general expenses + 8% of the sum of costs and expenses as profit + packaging costs for shipping to the United States. In effect, then, the officials are not trying to find the actual cost of foreign production. Rather they are trying to determine what foreign costs ought to be. Profits ought to be at least 8%. The fact that many American firms consistently make far less than an 8% profit is ignored.

Differences in costs are the basis for international trade. Therefore, the development of a SBC standard is extremely important. At first, the endeavour seems simple enough. Prices are compared to costs. But, the relationship between prices and costs of production is, as JM Clark put it, "quite complex", "obscure and varied".<sup>49</sup> His opinion on this subject is important because he was the first person to systematically demonstrate, in 1923, in his work Studies in the Economics of Overhead Costs<sup>50</sup> that it is impossible to determine the "true" cost of producing any one item in a multiproduct firm.<sup>51</sup>

Firms generally employ a financial accounting system and a (or several) cost accounting system(s). Financial accounts balance the amount of money paid out over some period of time, daily, yearly, with the amount of money earned. Financial accounts do not tell the business anything about the relationship of prices to costs or the allocation of costs among different departments or product lines. Cost accounting systems are employed to do this.<sup>52</sup> Firms incur two kinds of costs -- direct and indirect. Direct costs include, for example, the cost of the leather from which a pair of shoes are made. Indirect costs are those which are "chargeable to his (the firm's) entire business but not chargeable to any particular sale".<sup>53</sup>

Clark makes clear that the direct costs can be accurately discerned only if allowance is made for differences in their allocation, volume and character. For example, the cost of the leather for the shoes, the labour and the necessary fuel can vary according to the level of output.<sup>54</sup> In addition, the cost of the leather varies depending on the suppliers pricing decisions or materials bought at different prices at different times.<sup>55</sup> And, costs can rise or fall depending on the quality of the final product. Direct costs, if they are to have any hope of being accurate, must be adjusted for these fluctuations. This means having accurate information about overall output -- information which is generally beyond the purview of antidumping investigations.

Indirect costs are infinitely more complex. Their determination is completely a matter of discretion. They cannot be traced to any single unit of production yet, the

burden of paying the cost remains independent of output.<sup>56</sup> The interest on the capital borrowed, the rent, the cost of the labour and the machinery etc. can be added up but, the key question is how to allocate these cost to the whole business. Clark explains,

"The overhead costs must be levied on such parts of the business as will stand the burden, while other parts of the business, which cannot otherwise be had at all, are charged whatever they can pay, regardless of overhead costs."<sup>57</sup>

The allocation question is critical to antidumping investigations since they usually aim at only one single product made by a multiproduct firm. The question for the United States officials is not whether the firm operates below its cost of production but rather whether the particular item is sold below its cost of production. This is why very profitable firms can be found to be dumping.

To describe the question of allocation Clark uses the terms "estimate"<sup>58</sup>, "judgement"<sup>59</sup>, "imagination"<sup>60</sup>, "unconscious calculation"<sup>61</sup>, and "ambiguous"<sup>62</sup>. As a question, he says, it "creates more problems than it solves."<sup>63</sup>

"Any selection that may be made is in the nature of a compromise..." particularly "since some (indirect) expenses vary more directly with labour time, others with direct expenses, others with machine hours and so on."<sup>64</sup>

Overhead costs must include the cost of idleness. This is the cost of turning away business which might not repay all costs. The cost of idleness can only be determined if all the indirect costs could be isolated, which, Clark explains, they cannot.<sup>65</sup> If allowance is made for the "cost of idleness" then, it is at times necessary to sell at prices that are below the cost of production.

Of course, the difficulties in ensuring that all the cost information is correct assumes that it is possible to discern the costs in the first place. Even the foreign firm may itself not be able to determine its costs of production with any precision. WF Taussig noted this problem existed back in 1930.

"The striking thing is that those engaged in industry speak without hesitation about ascertainable cost and reasonable price." "The truth seems to be that they have in mind very much what the economist has in mind, not something which is ascertainable with strict accuracy, -- even the most refined system of cost accounting gives at best a basis for inferences, -- but rough approximation."<sup>66</sup>

In reading Schattschneider it becomes clear that there is a long history of difficulty in defining costs for the purpose of enforcing trade policy. Back in the 1920's and 1930's many American industries and firms tried to convince Congress that tariffs should be raised in order to offset foreigners' low cost advantages. Schattschneider explains,

"It is unnecessary to enter upon a discussion of the refinements and technical differences of determining these [foreign] costs [of production] because neither of the [Congressional] Committees at any time in the course of hearings made an attempt to define what was meant by costs, either domestic or foreign, or prescribe a formula for making the calculations. No effort was made to audit statements of costs, and the data were submitted in almost every conceivable form, more or less habitually violating every known rule of sound statistical and accounting practice. Under these circumstances statistics became the handmaiden of the unconscious process of wish fulfilment."<sup>67</sup>

He goes on to cite often hilarious language from 23 testimonies offered in the Congressional hearings. Most of the speakers asserted that these lower foreign costs were real. But, all were utterly unable to substantiate what the foreigners costs actually were, as is made evident by the most honest statement that Schattschneider records.

"I cannot tell you what their cost of production is. I wish I knew."<sup>68</sup>

Viner addressed the problem of selling below cost very clearly. It is worth quoting him at length. He explained that the theoretical grounds for SBC are actually stronger than those for LTFV. But, the practical difficulties of administering a SBC standard are insurmountable.

"But the administrative problems which would be presented by a law requiring the determination of foreign costs on a comprehensive scale and with any degree of precision would be almost insuperable."<sup>69</sup> Even in a simple case, he went on, with, "full access to all the books and records and all the information possessed by the owners of this industry, the determination of the cost of production is scarcely possible of accomplishment with the degree of precision and certainty which is desirable, if not essential, for the purpose of uniform and equitable assessment of duties."<sup>70</sup>

The problem of precision and certainty is further exacerbated by the fact that the foreign firm itself may not know exactly what its costs are, and if they did they might not want to reveal that information. Rodriguez highlighted this same point recently when he asked the central question. "Absent the disclosure of actual cost account data by the investigated firm (which may be unobtainable even by the firm itself), how does the

Treasury determine whether the data is reliable?"<sup>71</sup> According to a leading trade lawyer;

**"It (Commerce)" routinely accepts "claims of dumping (often with little more than US import statistics and petitioners' own costs, and frequently ignoring the statutory requirement of all information be "reasonably available," 19 USC Sect. 1671a) as petitions sufficient for initiation of an investigation."**<sup>72</sup>

The information provided in the original petition or subsequently by the petitioners is often the source from which foreign costs are determined. Even if the respondents have a clear idea of their costs and they are willing to submit that information to the US, that may not be enough. According to Vermuslt, the reporting procedure,

**" ... places a heavy burden on foreign respondents: it essentially requires them to submit the information in exactly the form that Commerce desires it. Failure to comply will make Commerce equate their position to that of a party who did not respond at all."**<sup>73</sup>

There are no external verification checks made on the information whether it is supplied by the respondent(s) or the petitioner(s).

Viner thought it unlikely that United States officials could gain access to secret corporate records. For this reason, he believed that distortions would undoubtedly occur since certain important factors would be unknown, such as:

**"genuine salary payments and distribution of proper depreciation allowance; the inclusion or exclusion from costs of interest borrowed and on invested capital, respectively, and variations in the cost of production of differing portions of output."**<sup>74</sup>

**"In the case of an industry producing from the same plant and equipment a variety of kinds and grades of products, the exact determination of costs of production is impossible. All that is attained in ordinary business practice is the reaching of an estimate resting on theoretical assumptions of necessarily disputable validity with respect to what are the proper items to include in cost, and what are the most satisfactory bases of apportionment of joint costs to the different products from the point of view of guidance of price-policy and of future production."** (emphasis added)<sup>75</sup>

Viner would clearly have been opposed to SBC as a definition of dumping. He concludes;

**"The development of comprehensive tariff legislation dependent upon the accurate determination of costs of production, whether foreign or domestic, for its administration is a dream incapable of even partial realization."**<sup>76</sup>

These arbitrary, unverified or unverifiable, figures are made very malleable by the next step in determining the cost of production -- the allocation of the costs over a period

of time. It would be ludicrous to expect a firm to recover all of its costs and a reasonable profit from a product on the first day of sales. Any single sale or even day of sales could not recover all costs. So, the time period used to judge costs is decisive.

The 1974 SBC statutory standard required that sales be below fully allocated costs.<sup>77</sup> That is, one full product lifecycle must be considered and for an extended period of time.<sup>78</sup> A normal business cycle includes the amortization period for capital and development costs, degree of expectation of full recovery of costs plus profit in a reasonable period of time. Obviously with any new, market-leading good, the R&D costs alone, leaving aside all the other indirect costs, will not be recovered in the first six months. One only need think of a new generation of computer chips. On this basis the United States is bound to find a huge dumping margin on any product which will not recover costs before, let's say, two years. As such, the SBC standard renders the antidumping law a powerful weapon.

In practice, however, United States officials argue that they cannot divine the future. They can only look at the past. Since the 1977 Case, Carbon Steel Plate from Japan<sup>79</sup> the practice has been to calculate the cost over most recent fiscal year or 6 months from the date when the petition is filed. In the 1984 case Titanium Sponge from Japan<sup>80</sup> it was confirmed that it is not even necessary to consider a business cycle. The six month practice could continue. Similarly, in the 1987 case Timken Co. v. US et al.<sup>81</sup>, the CIT left the phrase "over an extended period" subject to wide interpretation. As it stands, Kaplan and Kuhbach explain, "... no clear cut rule of thumb jumps from the pages of these decisions."<sup>82</sup> But, it is clear that in the modern business world profitability is dependent upon projected changes in costs and/or the level of production. As such, the six month procedure is bound to penalize normal, or typical, pricing policies. Kaplan and Kuhbach offer a good analysis of the essential problem.

"One of the most troubling aspects is the prominent role the Court has assigned to expected costs in determining whether costs will be recovered over a reasonable period. When a case is in the investigatory stage, data are collected for the period beginning five months prior to the investigation and ending approximately five months before the preliminary determination. Thus, any analysis of future costs must necessarily be speculative.

For example, assume that a responding firm argues that it intends to increase production by 100% over the next two years with the result that fixed costs per unit will halve. How is the administering agency to evaluate that claim? Should it be accepted at its face value? Or, should the Department make an independent judgement as to whether such a decision makes sound business sense? It is likely that the decision to expand production will depend, in part, on <sup>83</sup>ex difficult <sup>83</sup>des. Should the agency attempt, with the petitioner's help, to predict future prices? As other dumping law administrators well know, there are enough difficult decisions in a case, particularly cost cases, without adding to the burden.<sup>83</sup>

Domestic antitrust law, in contrast, penalizes only sales below average variable costs.<sup>84</sup> Ironically, this standard was adopted in the same year that antidumping law began to apply sales below fully allocated costs, 1974. Imports therefore have not been treated on the same basis as domestic goods after they have entered the market since 1974. The SBC standard not only violates the principle of national treatment; it has great implications, as Horlick points out, in an era when imports are often the price setters.<sup>85</sup> Fred Smith cleverly captured the significance of this issue;

"if the same anti-dumping laws applied to US companies, every after-Christmas sale in the country would be banned".<sup>86</sup>

Complicated as this all is, measuring and comparing costs among different products from different factories within firms and among different firms, it gets even more complicated when the firms in question are located in different countries. The target of the antidumping exercise is clearly a foreign firm or firms. Yet, foreign firms are being pressed to change behaviour which to a large extent reflects the economic environment in which they operate. Firm's costs reflect, for example, government fiscal and monetary policy (the cost of capital). This means that the United States is actually pressing the foreign enterprise or industry or even the foreign government to alter the business environment. Clark recognized that costs were a function of the general economic environment. He said,

"One of the most stimulating things in the study of overhead costs -- one which compels the imagination -- is the fact that the content and behaviour of such costs are governed by the form of industrial contracts. They differ from industry to industry as a result of differences in the forms of contract used and they are capable of being revolutionized by that non-revolutionary method."<sup>87</sup>

It is worth noting that cost accounting methodology was developed in an era when labour accounted for the majority of incurred costs. Overhead costs were minimal in comparison. But, Peter Drucker tells us now that labour has dropped to as little as 8% or, at most, to 25% of manufacturing costs.

"The remaining costs -- and that can mean 80% to 90% -- are allocated," he emphasises "by ratios that everyone knows are purely arbitrary and totally misleading: in direct proportion to a product's labour costs, for example, or to its dollar volume."<sup>88</sup>

The traditional cost accounting methodology used in antidumping investigations in the modern world of manufacturing renders the numbers more flexible since the majority of costs are indirect.

With the SBC and the LTFV dumping standard, the United States determines, in the relatively arbitrary manner described, what a foreign firm's costs ought to be. Though the original purpose of the law was to encourage or enforce a market standard in pricing policy, the law has been transformed through changes in the statutory definitions definition and, more significantly, by administrative practice. Under the law foreign firms ought to price their goods not according to market forces but according to an abstract, flexible and arbitrary ideal of what is fair, normal, and desirable.

In spite of the fact that there are many reasons for selling below cost, the US continues to assume that all SBC sales are not "normal" "in the ordinary course of trade", as Horlick has pointed out. But, there are rationale for selling below cost, as Vermulst makes clear.<sup>89</sup> Most of the reasons for selling below cost have nothing to do with predatory or anticompetitive objectives. For example, Vermulst cites the following reasons why firms might sell below cost other reasons other than those implying predatory behaviour. In some instances, "the firm was not aiming at maximizing profit but its market share (this could be in the long-run but of course unless the firm received some other form of income it could never make a profit on that particular product)."<sup>90</sup> Or, in another example, he explains;

"Some products have huge fixed overheads which compel a factory to work at near or full output all the time. In this situation firms will produce as much as they can and sell for whatever above marginal cost they can get."<sup>91</sup>



The issue under the AD law now, in short, is no longer the process by which prices are determined, nor is it whether home and export prices are different, but rather, whether the result, the chosen price itself, causes a real or perceived problem for American industry or even individual American competitors.

## **DUMPING MARGINS AND UNDERSELLING**

The existence of a dumping margin should, theoretically, be independent of underselling, price suppression or price depression. Underselling refers to a situation in which the price of the foreign good is below the price of comparable US goods. Underselling can be caused, obviously, by plain old competitiveness. Underselling does not necessarily imply unfairness. Price suppression refers to the inability of American producers to raise their prices because the low-priced imports holds prices down. Price depression refers to a situation in which the American firm must actually reduce its price to meet the low-priced import competition. In theory, only unfairly priced, not just less-expensively priced, merchandise should be subject to dumping duties. In practice, before 1981, the ITC compared (for the purpose of determining whether an American industry has been injured) the dumping margin to margin of underselling. Jameson explains that a high dumping margin in comparison to the margin of underselling would render the ITC more likely to make a positive finding of injury.<sup>92</sup> This practice appears to stem from the Asbestos Cement Pipe Tube from Japan<sup>93</sup> case in which the ITC said: "LTFV imports caused injury if either lost sales or price depression occurred."<sup>94</sup> After 1981, the ITC simply stopped taking the size of the dumping margin into consideration when making injury determinations.<sup>95</sup> Evidently, the ITC's concern is "whether the import volume is significant, not whether the magnitude of the margin is significant."<sup>96</sup>

In one intriguing case in 1987 a Korean respondent argued that it was not possible for their exports to the US to have caused injury. Although their imports into the US were priced 30% below comparable prices offered by American manufacturers, the imports had

a dumping margin of only .9% to 1.47% by the Commerce Department's own investigation. But, Jameson explains, the ITC said "The statute speaks only of material injury "by reason of" imports, not by reason of dumping margins."<sup>97</sup> In appeal, the ITC position was affirmed. "When it comes to considering margins, the Appeal Court said, the ITC can do whatever it wants."<sup>98</sup> The exemption from its ostensibly primary responsibility (to substantiate injury as caused by dumped imports) was ignored by most observers but it provoked David Palmeter to this declaration.

"Such a grant of unbridled discretion to an administrative agency, such a self-ouster of jurisdiction, is very unusual in a system specifically providing for judicial review of agency determinations to insure their conformity with the evidentiary record and with principles of law."<sup>99</sup>

In short, the presence of injury is derived from the fact that the actual price of the imports in question is lower than the US price. In other words, whether injury is caused by competitiveness or dumping is no longer the primary criteria for applying the law.

## INJURY

As we have seen, the antidumping law is supposed to target the effects of dumping rather than the existence of monopoly power in a foreign market or the intent of foreign exporters. The most obvious effect of dumping is injury. Dumping is not actionable unless it is injurious whether it is defined as sales LTFV or SBC. Until 1954, the Treasury was responsible for making the determination of injury. However, Congress shifted this responsibility in 1955 to an independent body, the International Trade Commission. Congress felt that the ITC was not only independent within the domestic political structure; the ITC was also considered independent from the foreign policy considerations which had made the Treasury cautious in making its injury determinations.

What is meant by injury? How is it measured? Injury is incurred by whom? There are three concerns addressed by the International Trade Commission when it makes an injury determination in antidumping cases: (1) the amount of injury required, (2) the

definition of domestic industry (which incurs the injury), (3) the causal relationship between the injury and the dumping.

The law is activated if "an industry in the United States is injured or is likely to be injured"<sup>100</sup> due to dumping. After the GATT was created, in 1947, the United States came under greater pressure to adopt its "material" injury standard.<sup>101</sup> Material injury, however, has never been clearly or workably defined in the GATT. Instead, the Treasury borrowed the term "serious" injury from the escape clause of the 1943 United States Mexico Trade Agreement. This remained the antidumping injury standard until 1951.

Injury has been defined most clearly in escape clause cases (section 201). There has been a tendency to rely on the escape clause standard when determining injury in AD cases. For this reason it is necessary to cite all the relevant developments, even if some arose in 201 cases. It is worth making note of Barcelo's comment: " ... less injury is required for antidumping than for safeguard relief."<sup>102</sup>

Attempts were made to incorporate the "material" standard into the United States Trade Agreements Act of 1951. They failed.<sup>103</sup> The 1962 Trade Expansion Act adopted the term "serious injury." It is unclear whether "material" injury should be considered a higher threshold than "serious" injury. The Commission's General Counsel apparently agreed that the Commission would define "serious" injury (in practice) as "material" injury, in the same way as the Treasury had done. Titanium Dioxide from France<sup>104</sup> in 1963 was one of the last cases in which the Commission used the GATT material injury standard. Specific reference to it was even made to it. But, by 1967, the Commission interpreted material injury in Soil Pipe from Poland<sup>105</sup> to be any injury greater than de minimis. By 1970 "serious" injury was interpreted in Whole Dried Eggs from Holland as "a showing of anything more than a trivial or inconsequential effect on the domestic industry".<sup>106</sup>

Having diluted the injury standard this far through administrative interpretation, the Congress had little compunction about diluting the statutory standard in the 1974

Trade Act. "Significant"<sup>107</sup> injury was now sufficient to pass for material injury. In 1979 the term "significant" injury was interpreted by the Commission to mean, **"harm which is not inconsequential, immaterial or unimportant"**(emphasis added). The 1979 Trade Agreements Act incorporated this new standard into the statute.<sup>108</sup> From 1980 Commission practice has been to find lower levels of imports injurious, even though the legislative history suggests the Commission should use the same standard as it applied during the period 1975-1979.<sup>109</sup> In a 1986, case one Commissioner's dissenting opinion has caused some further reassessment of the injury standard.<sup>110</sup> In his view, dumped cement imports from several countries<sup>111</sup> prevented domestic prices from rising, therefore, the imports should be considered injurious. This minority interpretation signalled a lowering of the injury threshold to harm which is not "unimportant". It also signalled the new emphasis on price suppression, depression and underselling.<sup>112</sup>

Slowly but surely, the level of injury has been reduced so that it is easier to make a finding of injury. The drop from "serious as material" to "serious" to "de minimis" to "more than trivial or inconsequential" to "significant" to "harm which is not inconsequential, immaterial or unimportant" is precipitous.

When making the injury determination, the ITC usually looks at a period of three years. This is done in spite of the fact that Commerce has established that dumping occurred on the basis of information which covers a period of only six months or so. Both Commerce and the ITC argue that they cannot read the future. Yet, for Commerce to go too far back into the past would potentially diminish the dumping margin (because there would be fewer instances of unfairly-priced sales).<sup>113</sup> The ITC assumes that the dumping occurred at the level specified by Commerce steadily, not for the six months but for the entire period during which the petitioners allege dumping was occurring. As a result, when an allegation is made that dumping occurred over three years, Commerce uses six months of information to make a positive finding of dumping, but the ITC determine whether there was injury on the assumption that dumping occurred for the entire three years.

Apparently, Horlick explains, Commerce excludes imports which were not at all dumped (i.e. there was no single instance of price underselling even allowing for exchange rate fluctuations). "But, if Commerce finds that 50% of a given exporters exports were dumped by 40%, the ITC assumes that 100% of the exports were dumped by 40%."<sup>114</sup>

The final duty, of course, is applied on the assumption that dumping occurred at the level specified by Commerce for three years.

## **DOMESTIC INDUSTRY AND LIKE PRODUCT**

Let us now look at the operative notion of the domestic industry. As noted earlier, the domestic courts have found that measuring injury to competitors is unequivocally inconsistent with competition policy objectives. Injury under domestic competition law must occur to competition and not competitors. How, then, has the antidumping law defined "domestic industry"?

The definition of the industry generally follows from the definition of the likeness of the competing products. Until 1988, the legislation required that the petitioner produce "such" or "similar" merchandise as the targeted import. In Bicycles from Czechoslovakia,<sup>115</sup> a case in 1960, the Commission defined the domestic industry by holding that the product produced by the importer is "similar" if that product is "identical" to the targeted imports. In that same year, however, the Commission held that makers of feldspar in the United States could petition against foreign producers of nepheline syenite since these products were "substantially comparable."<sup>116</sup>

The Antidumping Code of 1968 defines "like product" as one which is "identical [that is] alike in all respects to the dumped product under consideration" or that have "characteristics closely resembling those" which are allegedly being injured.<sup>117</sup> The Code and United States law do not attempt to judge likeness by asking whether the products compete in the same product market. For example, wood and bricks are both used to build houses. They may be considered competitive products since people make a

choice between them when building houses. Instead, likeness is judged by the physical likeness of products. So, one kind of brick is compared with another. For this reason, the GATT ruled in 1987 that cattle and beef products are not "like". However, firms have tried to circumvent antidumping duties and orders by making slight changes to the product in question so that it is exempt because it is not "like".

Fears that circumvention will render the remedy laws ineffective have exacerbated the broadening trend in the provision. To counter circumvention the Commission apparently developed a two part test sometime in the 1970's to determine what constitutes the domestic industry. First, the products must be "like". Second, most or all of the input used must be integral to the final product. This second test was developed because of special problems arising originally from agriculture cases. It was difficult to tell if a livestock industry was being injured by an industry which produced processed livestock. (The cattle industry claimed it was being injured by imports of beef products like beef jerky.) The second test has provided the justification for a broader notion of "domestic industry". For example, in 1984 the United States grape growers attempted to bring a case against the European wine industry. The 1984 Trade Act broadened the definition of the wine industry to include grape growers. Even though this violates the "like product" definition in the Code The Senate Finance Committee confirmed that this was acceptable since most of the grapes were used in making wine.<sup>118</sup> It is worth noting that these changes were made even though the domestic wine industry was opposed to the antidumping investigation of European wine makers.

In the 1988 Trade and Competitiveness Act, the Congress provided new statutory language. "Such or similar merchandise" was replaced by "comparable merchandise".<sup>119</sup> Clearly the new language is much broader. In addition, Section 1321 of the 1988 Trade and Competitiveness Act broadens the definition of a "like product" so that later versions of the product and products assembled in third countries can be made subject to existing orders. This, it is hoped, will prevent firms from making slight changes, either in the product or the place of its production, which might exempt products from antidumping

orders. Horlick and Oliver point out that this amendment contravenes the Antidumping Code since it allows the United States "to extend an existing antidumping .... order to non-"like" products".<sup>120</sup>

It is worth looking at one case in particular, on this subject of like product and domestic industry. According to Patrick Macrory in Forklift Trucks from Japan the price to price comparisons raised the like product problem.

"In that case, the Department selected home market comparison models on the basis of a ranking of twelve separate physical characteristics. Before the investigation began, it would have been impossible for a foreign manufacturer to predict the particular ranking chosen by the Commerce Department and hence, to determine which home market prices to compare with US prices, in order to ascertain whether it was selling at fair value."<sup>121</sup>

So, "like product" is a concept which is wide enough that even the producers of the product cannot always tell which products and therefore which prices will be used in an investigation.

What then is the domestic industry? The conception of domestic industry is important for two reasons. First, the domestic industry must produce a "like" product to qualify for standing, that is, the right to file an AD petition. Second, the definition of the domestic industry, whether broad or narrow, in effect defines the area which will be examined for the injurious impact of the dumping. Petitioners often want to define the industry as broadly as possible so that all injurious effects of dumping can be investigated. This tactic, though, is no guarantee of success. By broadening the conception of the domestic industry the actual impact of the injury may be weakened. For this reason petitioners are often counselled to adopt a narrow product and industry definition so that the impact of the dumping will be sure to pass the injury threshold. It is worth remembering that there must be evidence of injury to the domestic industry, real or potential, for the government to commence an investigation. This judgement is often made on the basis of information submitted by a single firm, (often the one most injured) though that firm may represent itself as the whole industry. The information provided by the firm is often neither statistically significant<sup>122</sup> nor independently verified.

Treasury had always used a nationwide definition of domestic industry. However, when the ITC was given the responsibility for injury determination, the definition began to broaden. In the 1955 case Cast Iron and Pipe from the United Kingdom<sup>123</sup> the Commission found that the producers of "like" pipe in California constituted an industry. The domestic industry was defined as a "competitive market area". This decision was heavily criticized. The Joint Committee on Economic Report in 1956 had this to say.

"...the challenged imports had no more than four-tenths of one percent of the domestic production of cast-iron soil pipe, and the domestic industry during the period in question had expanded its production, sales, capacity and prices. The Tariff Commission reached its conclusion regarding injury by deciding that the approximately 8% of national production located in California constituted a separate industry. But only one California producer who was represented at the hearings had shown losses during the period of imports, and these losses apparently were not the first he had experienced".<sup>124</sup>

Soon the Commission began to divide "competitive market areas" into segments for the purpose of injury determination. In the Dominican Cement<sup>125</sup> case of 1963 the "segment" rationale led the Commission to say that the producers of cement in the New York metropolitan area constituted the domestic industry. On this basis the Commission made a determination of "likelihood of injury" to the industry. However, in four other cases in 1963, involving imports of Steel Wire Rod<sup>126</sup>, the Commission rejected the "regional industry" concept. Except for these main exceptions the trend continued. In Carbon Steel Bars and Shapes from Canada,<sup>127</sup> Chromic Acid from Australia,<sup>128</sup> Steel Reinforcing Bars from Canada,<sup>129</sup> Alexis Coudert tells us the Commission was criticized by its Chairman and one other member for making a determination of injury on the basis of a "'competitive market area" that had only a tenuous relation to any industry recognizable as such".<sup>130</sup> In that same year in Chromic Acid from Australia<sup>131</sup> the Commission found that the domestic chromic acid industry was being injured since the prices in the West Coast area were being depressed by dumping. The Commission defined the West Coast "competitive market area" as the domestic industry because it constituted a "major share" of "a major United States market". This logic was applied even though, as the Chairman pointed out in his dissent, all the of the domestic American producers were located on the East Coast.<sup>132</sup> Also in 1964 in Carbon Steel



Bars and Shapes from Canada<sup>133</sup> injury was found by determining that only 3 domestic producers constituted the domestic industry. The 1966 case, Steel Jacks from Canada,<sup>134</sup> one firm was found to represent the industry.

A dissenting opinion in White Portland Cement from Japan<sup>135</sup> best indicates the degree to which the definition of a domestic industry had been attenuated.

"If some producer or producers are injured by imports at less than fair value, it follows that the national industry may be materially injured because such producers are part of the national industry. An injury to a part is an injury to the whole."<sup>136</sup>

This logic was applied, in fact, six years later in Steel Bars, Reinforcing Bars, and Shapes from Australia<sup>137</sup> in 1970. In this "watershed"<sup>138</sup> decision apparently only two states, in which only three domestic firms made sales (only one of which made national sales, and one of which was not registered in the complaint), were determined to constitute the domestic industry.<sup>139</sup> Given this, and the fact that imports reached only 5.5% of consumption in that "domestic market" as compared to 0.05% nationally, the Commission's conclusion was, as John Barcelo put it, "breathtakingly simplistic".<sup>140</sup>

Soon after, the Commission, having pushed to its extreme the logic of market segmentation -- the "breaking up of an industry into smaller pieces to measure impact (of injury)" -- began to adopt "a newly advanced theory",<sup>141</sup> Toby Myerson explains. Injury could be found more easily by enlarging the industry. In 1975, in Lock in Amplifiers and Parts thereof from the United Kingdom<sup>142</sup> the Commission said that the antidumping act uses the term "an" industry and not "the" industry. Therefore, the Commission could determine injury by looking at more than one industry.

One of the ways in which this broadening has been achieved has been the reinterpretation of "like product". As mentioned earlier, the "likeness" was broadened in the 1984 Trade Act so that the grape growers could bring a case against wine makers. The injury was found by examining the grape growers, not the domestic wine makers. The 1988 Act confirmed this trend by granting standing to file petitions to coalitions of firms, unions and trade associations.<sup>143</sup>

Let us stop here and look at the Antidumping Code criteria. Article Four of the Code defines a domestic industry as one "whose collective output ... constitutes the major proportion of the total." The word "major" was added after long negotiations during the Kennedy Round. Rodney Grey, the Chief Canadian Trade Negotiator during the Kennedy Round, explains that the "major proportion" language was interpreted as a "substantial proportion, but not invariably or necessarily, more than half the production of the goods in question".<sup>144</sup>

Of course, the Code has no real standing in American law.<sup>145</sup> It is up to the administering authorities to implement and or interpret the Code as they see fit. Even if the authorities choose to apply the Code, it is possible to define the terms in the Code freely due to their ambiguity.

Let us now return to the definition of the domestic industry for the purpose of determining whether a petitioner has standing to make an allegation.

## STANDING

A complaint must be brought "on behalf of the (domestic) industry"<sup>146</sup> by the industry, not a firm. The United States government also can initiate a case on behalf of an industry. Sometimes the government initiates or pursues a case even though the industry in question does not support the investigation or opposes it.<sup>147</sup> The Commerce Department, which is responsible for the determination of standing, assumes standing is valid, unless the majority of the industry opposes it. But, Commerce refuses to solicit support for the petition. It checks only those who actively oppose the petition in determining whether the share of the domestic industry the opposition represents is significant. There is no statutory requirement that a majority support the petition. Commerce has only once found lack of standing.<sup>148</sup>

Amendments to the 1974 Trade Act require the American to provide very specific information about the dumper, for example the "fair value" of the goods in the home

market, the injury to the domestic industry. In some cases, this allows a single firm the ability to make allegations based on information which may be dubious either in its source or interpretation.

## **AGAINST WHOM IS THE ALLEGATION LEVIED?**

Early on, allegations were made against single firms. But, since 1974, complaints can be levied against the country of the dumpers rather than against the specific firms. There is little logic in this. States do not dump. There is little likelihood that all the producers of the good in question are dumping. Thus, Toby Myerson notes,

"The allegation of dumping of goods becomes a basis for imposing burdens of the Antidumping Act on all suppliers from the countries named -- a distinct protectionist advantage to an American manufacturer -- where in fact the offender or offenders may be only one or a few of the individuals implicated."<sup>149</sup> "Because of the disruption of commercial activity caused to a non-dumping exporter, there is no logic in permitting a blanket indictment against all suppliers without some indication of their culpability".<sup>150</sup>

In addition, allegations are often levied against several countries at once. Again, this assumes that many firms in many different countries are in collusion. It would be a strange coincidence if all firms were selling at LTFV or below cost at the same time.

When antidumping orders can be applied to all exporters from a country this necessarily becomes a domestic political issue. The foreign government is called in by the foreign industry to protect its industry from the assault. The foreign government advises or negotiates on behalf of its own domestic industry. Governments are drawn in because antidumping investigations create financial penalties and jeopardize the earning power of their domestic industries.

The antidumping law is thus an instrument which can be used to compel governments to change their behaviour. A list of the most politically powerful industries and firms in each foreign country is maintained by the Commerce Department and the United States Trade Representative. If a foreign government does not comply with American demands (or press its domestic industry to comply) then the US can use the threat of an

antidumping investigation to create political problems for the foreign government at home.

On this point Viner said;

"When an antidumping law is administered in this manner (by naming a country instead of a firm or firms), the country specified in an antidumping order has clear grounds for protest that its treaty rights to equality of treatment are being violated. Treaty contracts are made by governments, and governments are ordinarily not responsible for the dumping practised by their citizens."<sup>151</sup>

When an AD petition simply lists countries, many small firms get caught in the net of the investigation. There simply is not enough time to make a full investigation of all the firms. So the investigation concentrates on certain targets and the smaller firms are not. Instead of engaging in a full investigation, Commerce assesses these smaller firms at the "all other rate". Gary Horlick offers this telling example of the injury determinations likely to result from this procedure. Commerce finds 60% of the dumped exports were sold at 20% less than fair value (home market price) and, therefore, Commerce issues a finding that the dumping margin is 11.1%. The ITC assumes that all the imports were sold at 11.1% LTFV.

"Thus, it is perfectly possible for Commerce to find one large company (with 50% of the imports) dumping by 20%, three small companies (with a total of 10% of the imports) dumping by 5%, and not investigate 40% of the total imports (which could be hundreds of companies, not sampled scientifically). The Department in its order setting estimated deposit rates would apply a weighted average margin of 17.5% to those 40% other imports (which had not been investigated), and the ITC will assume that they were dumped, when in fact no investigation of those 40% of imports has ever been conducted, and there is every possibility that they would be found not to be dumping during the actual duty assessment process a year and a half later (if the small exporting companies can work their way through that process).<sup>152</sup>

Thus, not only is it easier to make a positive finding of injury if the ITC ignores the fact that the imports were proved dumped for only six months, it is also possible to count non-dumped imports, even ones which have never been investigated, as dumped and injurious. And, if we recall the earlier discussion of underselling versus dumping, it becomes even more apparent that it is likely that injury will be established under the current administrative interpretations.

## CAUSALITY

Having explored the ways in which the terms "dumping", "injury", "like product" and "domestic industry" have been attenuated, let us now examine the causal link the law requires between the injury and the dumping. Remember, that there are three central operative notions behind the law: (1) the amount of injury required, (2) the definition of domestic industry, (3) the causal relationship between the injury and the dumping.

According to GATT and United States antidumping law, injury must be incurred "by reason of" (emphasis added) dumped imports. If no causal link can be established between the injury and the dumping then injury resulting from fair imports, or from other causes, may be used to condemn the exporters. Such a result would be economically senseless. To condemn foreign actors for injury they did not cause is also politically problematic. Why should foreigners change their "fair" behaviour under such circumstances?

Rodney Greytells us that there are two concepts of injury: overall and separable. The significance of these concepts here is that they define the breadth of the causal link between injury and dumping. Injury in a separable sense means injury caused by a specific event, resulting in a specific injury. The fact that the industry is suffering from cyclical downturn in the economy at the time of the dumping is separable from the actual injury incurred by the dumping alone. The United States applies injury in an overall sense. That is, injury is caused by an event or an accumulation of factors which result in an overall lack of health or well-being of the industry. Under United States law the Commission is prohibited from "weighing" the importance of differing causes.<sup>153</sup> Investigations merely attempt to determine whether dumping was one of the causes of injury. As in the case of injury language, the causality language sets out minimum thresholds. This causality threshold, like the others we have seen, has been lowered by administrative interpretation and statutory change. The United States does not apply the

separable conception because it would make it more difficult for those industries which happened to be suffering from other causes, such as general economic downturn, and therefore are easier targets for dumping, to receive relief from dumping. Though it may seem counterintuitive, Greydemonstrates that the overall conception does not necessarily make it easier to find injury.<sup>154</sup>

Traditionally, the antidumping law has borrowed heavily from the causality language used in Section 201 of United States trade law (the escape clause which allows action against fairly-priced but injurious imports). The "escape clause" statute, Section 201, sets the terms on which fairly-priced imports can be legitimately excluded from the domestic market. In 1955 the escape clause established the causal link with the language "contributed substantially towards causing".<sup>155</sup> The Trade Expansion Act of 1962 changed this escape clause language to "major cause".<sup>156</sup> This was in practice, but never expressly, interpreted by the Commission to be "a cause greater than all other causes combined."<sup>157</sup> This was soon found to be an onerous standard. After 1962 the causation language requires that injury be caused "in major part" by trade agreement concessions (remember, this is the language of the escape clause) and must be "a major factor" in causing injury. After 1962 major factor came to mean that dumped imports had to be a cause of injury more than the aggregate of all other factors causing injury. No cases qualified for this high standard.

Negotiators of the 1968 Antidumping Code attempted to prevent further diminution of the causality language. The Code required that dumped imports be "demonstratably the principal cause" in order to curb the overall (as opposed to separable) injury interpretation employed by the United States.<sup>158</sup> Senator Long, speaking on behalf of the Senate Finance Committee, explained that dumped imports under the Code "must be a cause of material injury, and such injury is greater than the injury traceable to all other causal factors".<sup>159</sup> This support for well-defined causality was soon overtaken.

By 1970 a "cause" is interpreted to be a "major factor."<sup>160</sup> The 1974 Trade Act changed the language to "substantial cause".<sup>161</sup> This was defined as "a cause which is important and not less than any other".<sup>162</sup> This language implies that the dumping as a cause must be both.

In 1971 the Commission became willing to minimize the importance of a causal link in order to ensure a positive finding of injury. In Pig Iron from Canada, Finland and West Germany,<sup>163</sup> it was reasoned,

"it is not necessary to show that imports were the sole cause nor even the major cause of injury as long as the facts show that LTFV imports were more than a de minimis factor contributing to the injury."<sup>164</sup>

In that same year, in Elemental Sulphur from Mexico,<sup>165</sup> it was declared that dumped imports need not be a cause "sole, major, or greater than any other -- identifiable cause was sufficient". "The relationship between LTFV and injury must be merely "identifiable."<sup>166</sup> This "identifiable" reasoning was confirmed in the 1975 case Electric Golf Carts from Poland.<sup>167</sup>

In 1979 Senator Heinz provided some encouragement to the Commission in the direction of a weaker causal link. Speaking in favour of the 1979 Trade Act he said,

"subsidized imports need not be a principal cause, a major cause or a substantial cause of injury to an industry when other factors may also be contributing to industry to an industry."<sup>168</sup>

However, the Commission ignored this offering in the 1980 case Certain Motor Vehicles.<sup>169</sup> The industry had suffered in the Commission's view not from dumped imports but rather from a general cyclical downturn which affected the whole economy. It ruled that the downturn was the cause of the injury and not dumped imports. The ITC came under heavy criticism and in 1982 it adopted the broader notion of causality which Senator Heinz had provided. It did so in Harley Davidson<sup>170</sup> and Specialty Steel<sup>171</sup> in 1982. In the Harley Davidson case the Commission spelled out this new reasoning:

"There is no basis in concluding that the current recession is the principal cause of injury. Industry under import assault or threatened by such an assault should not be denied relief simply because the assault happens to coincide with an economic slowdown."<sup>172</sup>

## CUMULATION

The causality concept has been further attenuated by changes in the ways in which causal factors are measured and grouped together. Injury must occur, as we have said, "by reason of"<sup>173</sup> dumping. But, Horlick explains, "being injured in many nibbles at once is just as bad as being injured in one large bite".<sup>174</sup> On this reasoning, the Commission has increasingly cumulated the effects of dumping.

Evidently, dumped imports from many firms in one country, Portugal, were cumulated for the first time in Portland Grey Cement from Portugal.<sup>175</sup> By 1968, imports coming from diverse firms in different countries were cumulated together for the first time. The Commission measured injury in Pig Iron From East Germany, Czechoslovakia, Romania and the USSR<sup>176</sup>, by cumulating the injurious effect from each country. There was no suspicion of collusive activity among these producers.<sup>177</sup> Cumulation was merely a convenient method of surpassing the minimum injury threshold. In the 1971 case Ferrite Cores from Japan<sup>178</sup>, we will remember, it was held that anything greater than de minimis injury is sufficient to make a positive finding of injury. In order to reach the de minimis level in this case it was necessary to employ the following relaxation of the causal linkage.

"If injury is attributable in part to the LTFV sales ... and such injury is more than de minimis, we must make an affirmative determination."<sup>179</sup> "The relative importance of such injury to injuries caused by other factors is irrelevant"<sup>180</sup>

Traditionally the Commission had discretion to cumulate. The 1984 Trade Act made cumulation of "like" and "competing" products mandatory.<sup>181</sup>

Cumulation has since been stretched even further. The 1988 Trade and Competitiveness Act allowed the Commission the discretion to cumulate when there is only the threat of injury. In 1986 the Court of International Trade held that the 1984 Act made cumulation mandatory. Astoundingly, it was held in Bingham Taylor v US<sup>182</sup> that the 1984 Act requires cumulation between like dumped and subsidized goods.<sup>183</sup>



The ITC also made cumulation of dumped and subsidized imports mandatory. This is called cross cumulation. Evidence of collusive behaviour between governments and firms is not required for cross cumulation even though the cumulation of dumped and subsidized imports implies collusion.

The 1988 Act also makes another kind of cumulation mandatory. Under the new law the injury caused by imports which have been found to be dumped in the past and "which resulted in a final order, suspension agreement, or termination based on a quantitative restraint agreement"<sup>184</sup> in the previous year can be cumulated with the injury caused by the same imports in a new investigation. In other words injury from previous "offenses" is added to the injury from the alleged dumping under examination.<sup>185</sup>

## CONCLUSION

Now it should be clear that it is impossible to understand the AD statute without acknowledging that the operative terms are imbued with various meanings at various times. And, at any given time, the operative terms are defined so as to improve the possibility of a positive finding against the foreign respondent.

Further, it should be kept constantly in mind that the act of interpreting and applying each of the operative terms is an act of economic statecraft. For changing the rules of the game changes the environment in which foreigners must do business. What is the United States compelling others to do with the AD law? This question can be answered only by delving into the detail as has been done here.

1. John Barcelo, "Antidumping Laws as Barriers to Trade -- The United States and the International Antidumping Code" Cornell Law Review Vol. 57, No. 4, April 1972, page 521.
2. William Taussig, Some Aspects of the Tariff Question: A Examination of the Development of American Industry Under Protection (Cambridge: Harvard University Press, 1930, third edition 1931) page 210.
3. It is worth asking why the United States assumes that the home market price and the United States price should be the same?
4. Antidumping Act 19 USC 64.
5. In effect, according to JP Hendrick, this meant the highest foreign price became the basis of comparison. "The US Antidumping Act" The American Journal of International Law Vol. 58, No. 4, October 1964.
6. Treasury Decision 53773. Cited by JP Hendrick, *ibid.*, page 916.
7. Peter D Ehrenhaft, "Protection Against International Price Discrimination: United States Countervailing and Antidumping Duties" Columbia Law Review Vol. LVIII, 1958, page 66.
8. Paul Samuelson, Economics: An Introductory Analysis (New York: MacGraw-Hill, 1961) page 467.
9. *ibid.*, page 325.
10. John Barcelo explains that the "Fallacy of Cost-plus Pricing" is that foreign companies usually face a single marginal cost curve but two marginal revenue curves (home and foreign). Thus prices at home and abroad differ. "Antidumping Laws as Barriers to Trade" pages 503-506.
11. Barcelo, "The suggestion here is that only cost-plus pricing is economically defensible. In this view "genuine" pricing requires a ratable distribution of variable and fixed costs to each item of production sold in each market." But, the subsidy argument "fails to give proper weight to the demand or revenue side of pricing decisions" page 504. Optimal pricing occurs when marginal costs are equated with marginal revenues. When marginal revenue just equals marginal costs, profits will be maximized. Barcelo explains that sales below marginal costs are the only plausibly dumped sales. *Ibid.* page 504.
12. Dictionary of Economics, Penguin, page 325.
13. Price-under takings settlements are often employed as an alternative to duties. They involve the setting of a price by the United States which is deemed reasonable. As such the law becomes a means of forcing foreign companies to revise their prices in accordance with American demands.
14. "Stakes, Shares and Digestible Poison Pills" The Economist February 2, 1991, page 75. W. Carl Kester, Japanese Takeovers: the Global Contest for Corporate Control (Cambridge: Harvard Business School Press, 1991).
15. Chapter Two, page 42, note 96 *infra*.
16. John Zysman, "US Power, Trade and Technology" International Affairs 67, 1, 1991, page 91.

17. *ibid.*, page 91.
18. 19 USC Sect. 1677a (1982).
19. 19 USC Sect. 1677b(a)(1)(A) (1982).
20. S Chesterfield Oppenheim, *et. al.*, ed.s., Unfair Trade Practices and Consumer Protection Cases and Comments (St Paul Minnesota: West Publishing Co., 1983) page 778.
21. For an explanation as to why this was done see S Chesterfield Oppenheim *et al.*, *ibid.*, page 778.
22. Salesmen's salaries are the major proportion of these in determining ESP.
23. Paul Victor and Thomas Ehrgood, International Trade Policy: The Lawyer's Perspective John H Jackson, Richard O. Cunningham and Claude GBFontheim, ed.s., Committee on International Trade Section of International Law and Practice, American Bar Association, (New York: Mathew Bender, 1985) page 7-11, Section 7.03.
24. "Given sufficient imagination, lawyers and accountants can produce surprising results!" JP Hendrick "The United States Antidumping Act" The American Journal of International Law Vol. 58, No. 4, 1964, page 922-923.
25. 95 Treas. Dec 229 (1960), T.D. 55118, cited by Victor and Ehrgood "Circumstances of Sale Adjustments in Antidumping Investigations: A Reevaluation" page 7-14, Section 7.03.
26. *Ibid.*, page 7-15 Section 7.03. From Treasury Department memorandum relating to the Antidumping Act, 1921, Howard C Peterson at 24 (Aug 1961).
27. *ibid.*, page 7-2, Section 7.01.
28. Bart Fisher, "The Antidumping Law of the United States: A Legal and Economic Analysis" Law and Policy in International Business Vol 5, 1973, page 99.
29. Paul Jameson, "A Critique of the Department of Commerce's "Study of Antidumping Adjustments Methodology and Recommendations for Statutory Change"" Law and Policy in International Business, Vol. 19, No. 4, 1987, page 715.
30. Robert Herzstein, "Dumping and Trade Liberalization: A Two Tiered Approach to Reducing Antidumping Disciplines between Open Trading Partners" Antidumping Law and Practice, Jackson, John H and Vermulst, Edwin A, ed.s., (New York: Harvester Wheatsheaf, 1990) page 343.
31. *ibid.*, page 343, Note 1.
32. 19 USC Sect. 1677f (1982 and Supp. III 1985).
33. Robert A Anthony and James E Byrnes, "Safeguarding Confidential Information in ITC Injury Proceedings: Proposals to Reduce the Risks of Disclosure" Law and Policy in International Business, Vol. 17, No. 1, 1987, page 11.
34. Donald Cameron and Susan Crawford, "An Overview of the Antidumping and Countervailing Duty Amendments: A New Protectionism?" Law and Policy in International Business, Vol. 20, No. 3, 1988, page 484.

35. Smith-Corona Group, 713 F.2d 1568 (CAFC 1983) and Silver Reed, 753 F. 2nd 1033 (Fed. Cir. 1985). See the discussion on Smith-Corona in Paul Jameson, "A Critique of the Department of Commerce's "Study of Antidumping Adjustments Methodology and Recommendations for Statutory Change", pages 700-705.

36. 19 USC Section 1675 as amended by Section 1325 of the 1988 Trade Act. Expedited review is made available under Section 736(c).

37. Gary Horlick "The United States Antidumping System" Antidumping Law and Practice: A Comparative Study John H Jackson and Edwin A Vermulst, ed.s., (New York: Harvester Wheatsheaf, 1990) page 148.

38. Brian Hindley, "Protectionism in the Gatt" Financial Times 7 June, 1991. He believes that it is yet more absurd because negative dumping figures are also excluded from the US price. See discussion infra pages 105-106.

39. David N Palmeter, "Exchange Rates and Antidumping Determinations" Journal of World Trade Vol. 22, No. 2 April 1988.

40. Melamine Chemicals, 44 Fed. Reg., 65,517 (1979).

41. "The EX rate fluctuated violently during the entire period under investigation." William B Mange, "Antidumping -- Application of Preceding Quarter's Foreign Exchange Rate to Fair Value Determinations: Melamine Chemicals, Inc. v US, 732 F. 2nd., 924 (Fed. Cir. 1984)" Texas International Law Journal, Vol. 20, No. 1, 1985, page 427.

42. Peter Ehrenhaft "What the Antidumping and Countervailing Duty Provisions of the Trade Agreements Act [Can] [Will] [Should] Mean for United States Trade Policy" Law and Policy in International Business Vol 11 No. 3. Page 1366.

43. Settlements, suspension agreements and other ways of terminating an investigation are discussed at the end of the chapter.

44. Gary Horlick, "The United States Antidumping System" page 126.

45. Richard N Palmeter, "The Capture of the Antidumping Law" Yale Journal of International Law Vol. 14, No.1, 1989, page 187.

46. Section 1319 of the 1988 Act allows Commerce to disregard foreign market price if it suspects that a price is "fictitious".

47. 19 USC Section 164(b) was passed as 321(d) of Trade Act of 1974. Harvey M Applebaum and David R Grace "US Antitrust Law and Antidumping Actions under Title VII of the Trade Agreements Act of 1979" say that more than half of the recent AD petitions have included allegation of SBC in the foreign home market, page 508.

48. *ibid.*, page 514.

49. John M Clark, Studies in the Economics of Overhead Costs (Chicago: University of Illinois, 1923) page 235.

50. *ibid.*

51. Usually a firm can only produce any one product because it produces several others. It is worth remembering that firms engaged in international trade are likely to be multiproduct firms.

52. JM Clark points out that the requirements of the two often contradict each other, Overhead Costs, page 247.

53. *ibid.*, page 4.

54. "[T]here are questions of allocation even with direct costs." *Ibid.*, page 246.

55. *ibid.*, page 248.

56. *ibid.*, page 250.

57. *ibid.*, page 23.

58. *ibid.*, page 228.

59. *ibid.*, page 231.

60. *ibid.*, page 228.

61. *ibid.*, page 218.

62. *ibid.*, page 228.

63. *ibid.*, page 23.

64. *ibid.*, page 231.

65. *ibid.*, page 253.

66. WF Taussig, Some Aspects of the Tariff Question: An Examination of the Development of American Industry Under Protection, (Cambridge: Harvard University Press, 1930, third edition 1931) page 210.

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106. Whole Dried Eggs from Holland, 35 Fed. Reg. (Tariff Comm'n. 1970).

107. "The Commission shall take into account all economic factors which it considers relevant, including (but not limited to) the significant idling of production facilities in the industry, the inability of a significant number of firms to operate at a reasonable level of profit, and significant unemployment or under-employment within that industry". Escape Clause, Trade Act of 1974. From Rodney Grey, Contingency Protection, page 21.

108. Trade Agreements Act of 1979 Sect. 771(7)(A).

109. Sen. Rep. No. 96-249 at page 87.

110. Commissioner Eckes.

111. Portland Hydraulic Cement and Cement Clinker from Columbia, France, Greece, Japan, Mexico, the RO Korea and Venezuela USITC Pub. 1925 (1986).

112. Ever since the 1979 Trade Agreements Act, the ITC has been directed to consider the volume of imports, their effect on US prices and the impact of those imports on domestic producers. Section 771(7)(B), 19 USC 1677(7)(B).

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133. Carbon Steel Bars and Shapes from Canada, 29 Fed. Reg., 12599 (Tariff Comm'n. 1964).
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162. Grey, Contingency Protection page 28.
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177. Myerson, "A Current Review of US Antidumping Procedures", page 187.
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179. *ibid.*,
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181. 19 USC Sect. 1677(7)(c)(iv) (Supp IV 1986).
182. Bingham Taylor v US 627 F. Supp. 793 (CIT 1986).
183. See Scott E Hayes, "Antidumping and Countervailing Duties -- Trade and Tariff Act of 1984 -- 19 USC Section 1677(7)(C)(iv) -- Mandates Use of The Cross Cumulation Standard. Bingham Taylor Div., Va. Indus. v US, 815 F. 2nd., 1482 (Fed. Cir. 1987) Texas International Law Journal Vol. 23, 1988.
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185. Previously the ITC included injury incurred during the most recent 8 months.

## **CHAPTER SIX -- REMEDIES**

Ultimately, an antidumping case must reach a conclusion. If Commerce fails to substantiate that dumping actually occurred and/or the ITC fails to determine injury was caused by the dumping then the investigation results in a negative finding. When there is a negative finding no remedy is applied to the respondent. As explained in the Chapter One, most AD investigations result in a negative finding. Most respondents are not found to be dumping, in spite of all the efforts to facilitate positive findings.

However, just because an investigation is terminated with a negative finding does not mean that the respondent has paid no price. Allegations of dumping and the ensuing investigation are highly disruptive to the firms involved. Further, we recall, the respondent has had to pay the preliminary dumping duty which was estimated before the Commerce commenced with its investigation. That preliminary duty is paid for in cash or with bond (not with an I-owe-you as was allowed until 1984). The respondent pays this duty in order to ensure that the respondent's allegedly dumped merchandise will not be held in the Customs warehouses until the end of the investigation (often investigations take at least one year to complete). The respondent has also had to pay the preliminary duty under to the terms of AD investigations. We recall that respondents cannot challenge the investigation process, or the grounds upon which the investigation itself was launched, until after a final determination has been made.

Of course, during the investigation, the accused firm(s) have had to spend managerial time and money on the AD case. Further, firms will have had to pay for the specialized legal and economic counsel which play such an important role in influencing the applied definitions and calculation procedures employed in AD cases.

AD investigations are usually focused only on the major suppliers. As we know, small firms are assessed at the "all other rate". In spite of the fact that many, if not all, of the small firms will never even be formally investigated, these small firms will be liable

for the preliminary and, if there is a positive finding, a final duty payment. As a result, these small firms are subject to financial penalties just for being named, or for being a producer in a country which is named, in an AD petition. The dumping margins for these smaller firms may be less than those for the major firms but, the smaller firms will be subject to financial uncertainty which is proportionally greater for them than for the larger firms.

Similarly the financial penalties, though less than those levied on the major firms being investigated, are proportionately more onerous for the smaller firms. In addition, few small firms can afford the large fees charged by legal and economic counsel. Thus small foreign respondents, have less opportunity to influence AD investigations in hearings.

It is worth noting that an AD investigation can reach a positive finding even if the foreign firms in question never even exported merchandise to the United States. AD investigations can be directed at the mere "threat of injury".

Having paid the preliminary duty, and then having been cleared by the investigation, the foreign firm traditionally has been entitled to have its money back. But, in twist to the old procedure, the preliminary duties are no longer automatically refunded or refundable just because the investigation results in a negative determination. Cameron and Crawford elaborate on this new development:

"Since the Antidumping Act of 1921, the Antidumping Law has provided that Antidumping duties should be handled on the same basis that Customs duties are, that is they should be eligible for duty drawback." Duty drawback means the right to get the money back if the firm is absolved in the investigation. But, they continue, Section 1334 of the 1988 Trade and Competitiveness Act,

"... reverses 60 years of practice and prohibits the refund of antidumping and countervailing duties placed on imported merchandise under drawback provisions. In passing this amendment, Congress eliminated equal treatment of customs and antidumping or countervailing duties, thereby demonstrating that dumping and countervailing duties are indeed punitive despite all statements to the contrary."<sup>1</sup>

Now, a respondent will have had to pay a very large price just for having been

accused of dumping. Respondents must pay regardless of the fact that the US authorities have failed to prove that the foreign firm(s) engaged in dumping.

## **DUTIES**

If an investigation results in a positive finding of dumping and injury then a remedy is applied. The typical solution is to apply a duty to the imports. Usually the ITC directs Customs to collect a specified amount of duties on the merchandise.

Requiring a foreign firm to pay a duty is, as it was explained in Chapter One, a form of economic statecraft. Duties are applied in order to neutralize the effects of the dumping. They are designed to dissuade the firm from continuing to dump. The impact of duties is not "incidental, unintended and perhaps even unwanted".<sup>2</sup> Duties are designed and intended to help the petitioner(s) by hurting the respondent(s).

If the duty is applied to goods which are priced "fairly", that is, the merchandise is genuinely competitive (and, by extension, the firm that produced and priced it), then the duty acts as a tax on productivity. In such instances, foreigners are compelled -- to put it simply -- to pay for being more competitive than American firms. In this sense it is arguable that the antidumping law actually serves as a flexible tariff.

The duty is supposed to be commensurate with the margin of dumping. A duty that is larger than the dumping margin acts as an anticompetitive restraint on trade. Similarly, a margin that is generated more by administrative methodology and discretion than by firms' genuine pricing policies will result in a duty which is anticompetitive.

Duties, as examples of economic statecraft, imply the exercise of power by one actor over another. This use of power is not, to reiterate, in itself a bad thing. To the contrary, it is in the interests of the international community that power is used to prevent breaches of responsibility and enforce appropriate behaviour. Here lies the central point. What has the international community agreed is responsible and appropriate behaviour in international commercial affairs? We return again to the concept of competition. The

legitimacy, that is, the objectives and methods the members of the post-war international economic order have agreed upon centre on competition. Duties, then, are legitimate if those duties offset genuinely anticompetitive pricing behaviour. But, AD duties are illegitimate if they are used to penalize competitive behaviour. The legitimacy of AD duties, is dependent on whether the dumping in any particular case is real and genuinely anticompetitive or a fabrication arising from administrative methodology and discretion.

There is no sunset clause on antidumping orders (the order imposes the AD duty). The exporter must show no sales at LTFV or SBC for two years or no sales in the United States at all for three years.<sup>3</sup> And there must be no likelihood that the dumping will resume.<sup>4</sup> In effect, as Horlick points out, this puts a price tag on obtaining a revocation of an order, even after compliance.<sup>5</sup>

Duties can be also applied retroactively up to seventy days if there is a "history of dumping".<sup>6</sup> A dumping order can be revoked only after there is an official review.<sup>7</sup> Usually it takes at least 2 years from the date of the antidumping order just to initiate the revocation process. Then, the order can only be revoked after an administrative "review" by Commerce. These reviews used to happen annually. But, since 1984, Commerce no longer engages in reviews unless the petitioner, or, though it is unlikely, the respondent, actually asks for a review.<sup>8</sup> Once granted, the review procedure assumes "guilt". That is, the respondent or petitioner (depending upon who asked for the review) must prove that there have been no sales at LTFV (since the dumping order was put in place) which would create more than a de minimus (0.5%) dumping margin. If we remember how margins are calculated (just one instance of LTFV sales will generate a dumping margin because sales at prices above fair value (FMV, the home market price) are ignored, and sales below cost in the home market, if not more than 10% of the home sales, are excluded from the weighted average that is used to create the home market price) then, this de minimus requirement effectively means that the importer must not undersell its American competitors for the two years and then prove that it has not. Revocations of AD orders are also contingent upon proof that sales at LTFV are not likely to resume.

Respondents costs can reach \$50,000 for each annual review and \$100,000 for a revocation.<sup>9</sup> It is possible to get an expedited review<sup>10</sup> (thus eliminating the need to wait for one year) but Commerce has not granted any since 1984. The 1988 Trade and Competitiveness Act restricts the authority to grant an expedited review even further. Now it is impossible to get a review unless a case is extraordinarily complicated or unless the final decision by Commerce was postponed.

If a dumping order stays in place the respondent must continue to pay the set duty. The amount of the duty is supposed to be calibrated regularly to changing prices. But, this is rarely done due to bureaucratic slowness. So, while new technology and increasing management efficiency puts downward pressure on market prices the imports remain subject to the initial (relatively higher) dumping duty.

If the firm tries to eliminate the margin by raising its prices for the future the firm will now be penalized under the 1988 Trade Act. Crawford and Cameron explain that Section 733(a)(1) of the 1988 Trade and Competitiveness Act<sup>11</sup>

" ... now provides Commerce with the authority to examine movements for different forms of a product sold in the home market, when the product is subject to an antidumping duty in the US. If the movements appear to reduce the dumping margin, the sales of the merchandise selected for comparison would be disregarded as well. The concern to those familiar with the workings of the antidumping statute and the tendencies of the Commerce Department is that the provision is ripe for abuse. This provision potentially penalizes companies for doing what the law allegedly wants them to do, eliminate dumping margins. This provision can be characterized as a "got ya" provision -- "got ya" if you do, "got ya" if you do not."<sup>12</sup>

In addition, exchange rate fluctuations, as we have seen, can create or eliminate margins. If foreign firms want dumping orders against them to be revoked the foreign firms must be vigilant about repricing so no sales can appear to have been made at LTFV. No allowance is made in an annual review for exchange rate fluctuations.

When an order is revoked, however, the foreign firm is by no means free from the order. Commerce is authorized under Section CFR 353.54(e) to demand that the foreign firm promise in a written agreement to accept a reimposition of the AD order if there are any sales at LTFV. In other words it is not difficult for Commerce to reimpose AD orders even after such orders have been revoked. As such, the respondent

remains subject to the terms set in the order even after it has been revoked.

Another new penalty imposed on those who are or have been subject to antidumping duty orders. According to the terms of Section 1323 of the 1988 Trade and Competitiveness Act, foreign firms which are subject to two or more dumping orders (or suspension agreements, these will be explained further on) and who have dumping margins in excess of 15% within an 8 year period, are considered second offenders. Those firms with three or more AD orders against them are multiple offenders. Second and multiple offenders automatically have the injury caused by each past instance of dumping now cumulated in future AD investigations.

In spite of the broad-reaching penalties duties can provide, duties have one fundamental failing. That failing is exactly the reason why duties are supposed to be used to offset unfair trade practices in the first place. Duties continue to allow competition to occur and market forces to play upon the American market. The duty merely adjusts the price difference. By charging a duty the US hopes to raise the foreign firm's costs, and thereby (hopefully) the price will be raised to the level that the price would have been in the absence of dumping.

To many petitioners, duties can appear ineffective and cause unsavoury results. There is no guarantee that the duty will be passed on to the customers. A foreign firm may absorb the cost of paying the duty. This is another reason why duties are often unsatisfactory to those US firms that feel they are being injured by dumping. Let's say the foreign firm raises its price to cover the cost of paying the duty. If consumers are buying the imports for quality reasons instead of price considerations alone then the import competition will not only remain intense, the foreign firm's profits will swell. Such a result only reinforces the market power of the foreign firm(s).

In addition, only the largest firms can usually afford to pay the duties, particularly very high duties. Smaller firms cannot pay. As a result, duties can reinforce monopoly power among the largest foreign exporters rather than reducing monopoly power. In some



instances duties only encourage the foreign firms to operate more efficiently so they can maintain or increase their market share in spite of the added expense.

There is another reason why duties are not always perceived as the best way to resolve the problem -- if the problem is perceived to be not the unfairness of the imports but the very presence of competitive imports in the market. Even if duties are paid, the merchandise in question is still entering the American market. The real or perceived injury remains. Domestic industry will continue to generate pressure on politicians to "do something" about the imports. Since politicians find dealing with such pressure difficult and time consuming, and the bureaucracy is not easily able to handle such pressure, AD cases are sometimes resolved through settlements.

It is exactly because duties allow market forces to continue to function that they are not the solution of choice in politically-charged situations. The consensus among those closely involved with the administration of the AD law can be summed up as: when the heat is on we will do what we have to stop the imports. In other words, there are times when market forces via import competition are best eliminated. For this reason investigations are sometimes terminated or suspended in lieu of duties on the basis of settlements such as quotas, voluntary restraint agreements, price assurances, and other fundamentally anticompetitive arrangements.

## **SETTLEMENTS**

Increasingly the United States has used large dumping margins as a means of forcing foreign firms into settlements. A settlement is a means of concluding an antidumping investigation. Technically a settlement is reached after the AD investigation has commenced but before the investigation results in a final order. An order is the remedy which the US applies to the firms which have been found to be dumping. Duties can be made large enough to endanger the foreign firms' access to the US market.

Threatened with an exorbitant duty, foreign firms are often willing to reach a negotiated settlement.

In some instances a foreign firm will reach a "settlement" before an AD petition is filed. In these instances the settlement is not official, it is for this reason quotation marks are used around the term. Foreign firms, knowing how capricious an investigation can be, knowing that the methodology and definitions are tilted against them, will often respond to the mere threat of an AD petition. According to Horlick, the Press is often used as a forum for not very subtle signalling by a potential petitioner. The message, or rather, the threat, received by the potential respondent, often compels the respondent to change its behaviour in some way. Quite often the foreign firm(s) will raise the price of the merchandise in question. It is not unheard of for foreign firms to shift the focal point of their sales in the US from one location to another.

Donald de Keiffer, explains this "settlement" by threat procedure.

"Often cases are brought to the attention of either Commerce or (USTR) and we (government officials), by discussing the case with the foreign company or foreign producer and the domestic industry, can resolve the problem. Such a negotiated settlement is cheaper, more effective, and more pragmatic in both the short and long run, than bringing a case. We already have literally scores of cases that have been resolved by settlement."<sup>13</sup>

Once an petition has been presented and standing granted it is now virtually automatic that an investigation will commence. When many observers refer to the fact that the AD procedure vests little discretion with the law's administrators, they are referring to this automaticity in the procedure.

After the investigation commences it is possible for the case, either before, but more commonly after, the final determination, to culminate in a settlement. Such settlements are extremely rare. But, since they offer concrete examples of instances in which foreigners were compelled to engage in anticompetitive behaviour, which otherwise they would not, it is worth looking at such settlements. Plus, since we don't know much about unofficial settlements, it is helpful to see what has been done officially. There are two mechanisms for settlement. The investigation can be suspended or terminated. Suspension is dependent upon the respondent's promise to cease exporting to the United

States completely or, to raise the export price so that the margin is eliminated.<sup>14</sup> A suspended AD investigation can recommence at any time if the conditions laid down by the US are not met by the respondent.

When the government self-initiates an investigation<sup>15</sup> the government may terminate that investigation if termination is "in the public interest". That is, termination is deemed to provide a better result for American industry than continuation of the investigation.

Before the Antidumping Code was first negotiated (1967) it was relatively easy for a case to be terminated before a final determination even if there was a likelihood that the United States authorities would find (or had found) both injury and dumping. Treasury could terminate AD investigations if the respondent eliminated the price discrimination either by raising the export price or reducing the home market price (such price changes are called price assurances), or if the respondent agreed to stop exporting the merchandise in question to the United States altogether.<sup>16</sup> The Code allows price assurances only allowed when the dumping margin is "considered minimal in relation to the total volume of sales".<sup>17</sup>

Treasury allowed suspensions when a price assurance settlement could be negotiated. The respondent would approach Treasury with an offer. "If we do X (raise our price) will the investigation be dropped?" The petitioner would be queried. It would reply with a request. "No but if you do X and Y we will request that the investigation be dropped." Treasury would then terminate or suspend the investigation. In essence a price assurance means that the importer's price has been approved if not actually set by the United States government in collaboration with American industries (or individual firms). The respondent was compelled to adopt that price. So, the government in cooperation with private American firms set the price of the imported goods in question.

Terminations and suspensions, however were soon perceived to be more beneficial to the foreign respondent(s) than to American industry. The lack of a final dumping order seemed to vindicate the respondent. Since 1984 Commerce can terminate a case only if it

self-initiated the complaint.<sup>18</sup> But, if the petitioners withdraw their complaint then Commerce can allow termination of the case.

Since 1979, when the authority for substantiating dumping shifted from Treasury to Commerce, an investigation can only be suspended if the investigation is "complex", meaning the case involves either new issues, or a large number of firms or a large number of transactions or a large number of adjustments. Suspensions are prohibited unless they are "in the public interest" (which is interpreted by Commerce). They are supposed to be more beneficial to United States industry than the completion of the investigation. It must also be practical to monitor the imports in question under a suspension agreement. Technically, a suspension agreement must preclude any surges in imports (meaning rise in the number of imports) for a maximum of six months.

Officially, suspension agreements can take three forms. First, the respondent(s) can eliminate the sales at LTFV (or SBC). Second, the respondent(s) can eliminate the injurious effects of the imports. Third, the respondent(s) can completely cease exporting to the United States. These options are available only if exporters accounting for "substantially all" of the imports in question agree to one of these options. All suspensions require that the exporters ensure that there will be no price underselling and no price suppression. Prices must be raised so that at least 85% of the dumping margin is eliminated.

Suspensions are extremely rare. The problems involved in monitoring and enforcing suspension agreements are immense. For example, there has never been a suspension based on the elimination of the injurious effects of dumping because it is virtually impossible to get 85% of all the private suppliers (who are competing with each other) to agree on anything let alone to ensure that they will never undercut or suppress US prices.

There have been only a few suspension agreements in AD cases.<sup>19</sup> All have been based on agreements to eliminate the sales at LTFV or SBC. In practice this means that the importers must agree never to sell at a price which is below the "fair market value"(FMV).

FMV is a flexible amount which is determined by Commerce. Three of these suspension agreements have not worked, as Elaine Frangedakis put it, because the importers

"... have no way of knowing what the fair market value is at any particular time, and thus have no way of ensuring that they are complying with the agreement."<sup>20</sup>

In two other instances, Dynamic Random Access Memory Semiconductors of 25 Kilobits and Above from Japan<sup>21</sup> and Erasable Programmable Read Only Memory Semiconductors from Japan<sup>22</sup>, however, the threat of massively large duties compelled the Japanese semiconductor producers to reach a suspension settlement which has subsequently resulted in bilaterally negotiated quota arrangements between the US and Japan.

Withdrawals provide broader scope for agreement since there is no requirement that an agreement be reached at all.<sup>23</sup> In return for dropping a petition the foreign parties agree to settle "out of court" as it were. Most common is an agreement that the government of the foreign nation(s) in which the respondents reside will voluntarily agree to restrain the amount of imports into the United States and/or some third market or to ensure a quota arrangement. Even though AD cases are generally directed at changing the behaviour of foreign firms, foreign governments are often pulled into the negotiating process, and eventually the enforcement of any subsequent agreement. In this way they become the domain at which influence and power are aimed. Withdrawals provide the freedom to negotiate on highly political cases. Governments are drawn into the proceedings as a way of pressuring the foreign respondents into an agreement.

Four examples of such settlements are the 1982 voluntary restraints on steel exports to the United States, the 1983 quota on Polyester Fabric from Japan, and the special pricing schemes used for steel in 1982 (namely the Trigger Price Mechanism) and semiconductors in 1986.

In the Lightweight Polyester Filament Fabrics from Japan<sup>24</sup> case the Japanese government agreed to ensure the amount of exports of certain fabrics to The United States by Japanese exporters. It was a market-sharing arrangement based on a quota.

In return for dropping over forty antidumping and countervailing duty petitions against steel producers in many countries, the governments of Germany, France, Japan, Korea, Sweden, and others agreed to ensure that steel exports to the United States from their countries would not exceed the level specified by the United States. In effect a government-enforced quota was established by a voluntary export restraint.

Special pricing schemes were used in two instances. Part of the 1982 steel settlement was an agreement that the respondents would be subject to new antidumping and countervailing duty petitions if the price of their steel imports exceeded the "trigger price". The trigger price was set by United States officials. In the semiconductor agreement the United States was able to get the major importers to change the price of semiconductors available in the US, in Japan and in third markets as well. Although, the US denies that it was able or even attempted to effect a change in the home market price. In return Commerce recalculated the alleged dumping margin which subsequently dropped by half according to those involved in the negotiation. Unfortunately none of the original figures for the initial final amount of the dumping margin have ever been made available to the public.

## CONCLUSION

Settlements, duties applied to fair trade and excessive duties all inhibit market forces. They are all fundamentally anticompetitive. As such, they are illegitimate in the sense that they are not in keeping with the internationally agreed upon methods and objectives of the post-war international economic order. These objectives are mainly to promote competition with trade policies which enhance or at least make use of market forces.

Legally, settlements require collusion among unrelated foreign firms, indeed suspensions imply conspiracy on the part of American firms and the US Government to act in restraint of trade. Arthur George explains that AD investigations do not often

culminate in settlements because such settlements are anticompetitive under domestic American competition law:

"This is partly because the antitrust laws may prohibit the restraints on competition that would necessarily result from a settlement arrangement between petitioners and respondents."<sup>25</sup>

For this reason, he says, there is a need to ensure that conduct governed by suspension agreements is "immune from attack under the antitrust laws."<sup>26</sup>

One of the most fascinating characteristics of antidumping settlements is they would constitute a violation of domestic antitrust laws if a case was ever brought against them. Trade negotiators who contribute to anticompetitive settlements or anticompetitive duties could be legally prosecuted under domestic competition law for acting in restraint of trade. For example, settlements based on price assurances (read price-fixing) or on agreements to limit the quantity of imports are blatantly in restraint of trade. If committed domestically such actions would be punishable by very large fines and prison sentences. The major reason why this has never happened is because the Justice Department has chosen to ignore such violations. In addition, the Justice Department has actively advised trade officials about how they must conduct their negotiations to avoid prosecution under antitrust law.

It was at the insistence of the Justice Department that the "foreign compulsion doctrine" has been adopted in trade negotiations of this kind. According to this doctrine American trade officials must ensure that it appears that foreigners are engaging in the trade-restrictive practice on a purely "voluntary" basis.<sup>27</sup> Agreements to limit the amount of imports are called "voluntary restraint arrangements" (VRA's) for this very reason. In some instances it has been necessary to provide statutory language offering trade officials immunity from prosecution for acting in restraint of trade. As early as the 1974 Trade Act it was provided that, "no person shall be liable" under "the Federal Trade Commission Act or Anti-Trust Acts" for having negotiated a "voluntary limitation on exports of steel or steel products to the US."<sup>28</sup>

In other words, the foreign compulsion doctrine saves American officials from prosecution for acting in restraint of trade by explicitly requiring that the foreign actor be compelled to act in restraint of trade. In the exercise of this economic statecraft the United States compels the foreign actor to engage in the anticompetitive activity.

It is ironic that the AD procedure allows petitions to be filed against many unrelated firms in one country or in many countries -- which implies that those firms are colluding to dump, a highly unlikely scenario -- while the settlement procedure (either officially, or, if before the petition is filed, unofficially) requires that those same foreign firms collude on prices or sales volume in order to escape greater penalties under the American AD law.

Some have argued that settlements provide a "safe harbour" for respondents who are behaving competitively, legitimately, and yet are found to be transgressing the antidumping law.<sup>29</sup> But, once caught in the net cast by the AD law, a foreign firm gains little solace from the fact that a settlement appears to be a penalty less severe than the alternative. In the end all settlements are anticompetitive. All settlements require the foreign actor to change its behaviour when the United States has said that it has engaged in unfair trade practices.

Settlements are also outside the GATT rules. This is why they are called "grey area" measures. By compelling foreigners to undertake anti-competitive actions in the form of agreements which fall outside the purview of the internationally agreed upon rules the United States undermines not only the market principles it espouses but also the legal structures which support the post-war international economic order.

The problem is not simply that settlement agreements are generally bilateral. It is legitimate for the United States to use its power on a bilateral basis to compel foreigners to abide by the rules and act competitively. It is, however, illegitimate for the United States to use its power on a bilateral basis to compel foreigners to act against the internationally agreed upon rules and in restraint of trade.



Finally, when examining what the United States is compelling others to do, we must keep in mind that the "remedy" reinforces all of the messages which are implicit in the investigation. The pressures on foreign firms to make profitability in the short run their central goal (as opposed to growth or increased market share), or never to undersell US prices, are reinforced by the final remedy whether that remedy takes the form of duties or settlements. Antidumping policy thus becomes a means by which the United States compels foreign firms to modify their behaviour and even the agenda of options from which those firms can choose. In other words, the antidumping law is a mechanism which allows the United States to cross the boundary of foreign autonomy and exert power and influence over autonomy. It seems that this use of power is aimed at breaking down competition, breaking down rules and breaking down autonomy.

1. Donald B Cameron and Susan M Crawford, "An Overview of the Antidumping and Countervailing Duty Amendments: A New Protectionism?" Law and Policy in International Business, Vol. 20, No. 3, 1988, page 488.
2. These are the terms which David Baldwin notes are the most commonly applied to the effects of duties. Economic Statecraft (Princeton: Princeton University Press, 1985) page 48.
3. 19 CFR Sect. 353.54(b).
4. 19 CFR Sect. 353.54(c).
5. Gary Horlick, "The United States Antidumping System" Antidumping Law and Practice: A Comparative Study John Jackson and Edwin Vermust ed.s., (New York: Harvester Wheatsheaf, 1990) page 129.
6. 19 USC Sect. 1673d(a)(3) (1982 and Supp. IV 1986).
7. Annual reviews were required under the terms of the 1979 Trade Act.
8. Section 611 Trade Act of 1984.
9. Gary Horlick, "The United States Antidumping System" page 129.
10. Expedited Review (Sect. 736(c)).
11. 19 USC Sect. 1677b(a)(1) (1982); 19 CFR Sect. 353.18 (1988).
12. "In the end, Section 1319 could well become the "cost of production" provision of the 1988 Trade and Competitiveness Act." Donald B Cameron and Susan M Crawford, "An Overview of the Antidumping and Countervailing Duty Amendments: A New Protectionism?" Pages 490-491.
13. Donald de Keiffer, Panel III, Dumping and Subsidies, Current Legal Aspects of International Trade Law, Section of International Law, American Bar Association (Washington, D.C.: American Bar Association, 1982) page 61.
14. Permitted under US law only if the exporter ceases exporting to the US or revises prices to eliminate the margin.
15. Commerce or USTR.
16. John Barcelo "Antidumping Laws as Barriers to Trade -- the United States and the International Antidumping Code" Cornell Law Review, Vol. 57, No. 4, April, 1972, page 543. CFR Sect. 14.7(b)(9) (1967) Pre-Antidumping Code.
17. Post-Antidumping Code, 19 CFR Sect 53.15 (1969) amended 19 CFR Sect. 153.15 (1971).
18. Section 604 1984 TTA also requires that all parties be informed.
19. Certain Electric Motors from Japan, 45 Fed. Reg., 73,723 (1980). Truck-Trailer Axle-and-Brake Assemblies and Parts Thereof from Hungary, 47 Fed. Reg., 66 (1982). Carbon Steel Plate from Romania, 48 Fed. Reg., 58,328 ( 1983). Leather Wearing Apparel from Argentina, 46 Fed. Reg., 23009 (1982).

20. Elaine M Frangedakis, "Suspension Agreements" International Trade Policy: The Lawyer's Perspective, John H Jackson, et al., Committee on International Trade Section of International Law and Practice, American Bar Association (New York: Matthew Bender, 1985) page 11-19, Section 11.04.
21. Dynamic Random Access Memory Semiconductors of 25 Kilobits and Above from Japan, 51 Fed. Reg., 28,369 (Dep't. Comm. 1986).
22. Erasable Programmable Read Only Memory Semiconductors from Japan, 51 Fed. Reg., 28,253 (Dep't. Comm. 1986).
23. Section 604 of the 1984 Trade Act statutorily authorizes quantitative restraint arrangements as the basis for terminating (as opposed to suspending) antidumping investigations.
24. Lightweight Polyester Filament Fabrics from Japan, 48 Fed. Reg., 35,976 (Dep't. Comm. 1983) (affirm prelim), and 49 Fed. Reg., 4021 (Dep't. Comm. 1983) (termination).
25. Arthur L George, "Settling AD Cases: Practical and Policy Analysis" Law and Policy in International Business Vol. 19, No. 3, 1987, page 455.
26. *ibid.*, page 490.
27. It is also the reason that such arrangements are legally unenforceable; a fact which causes great frustration among American trade officials.
28. Rodney Grey, Trade Policy and the System of Contingency Protection in the Perspective of Competition Policy unpublished paper commissioned by the OECD, Paris 1986, page 51. Trade Act of 1974 Public Law 93-610, 93rd Congress, HR 10710, Jan. 3, 1975 Sect. 607 at page 96.
29. Gary Horlick, "The United States Antidumping System" page 114, Note 47.

### **SECTION THREE**

## **CHAPTER SEVEN -- COUNTERVAILING DUTY LAW: ECONOMIC STATECRAFT**

The countervailing duty law (CVD) is best understood as an instrument of economic statecraft. With this economic policy tool, the United States compels foreign governments to cease pursuing those economic policies which, according to the United States, subsidize the manufacture or exportation of domestically produced goods. To countervail a foreign government's domestic policy is to penalize a government for having a subsidy policy, to prevent that government from pursuing that policy. CVD law is, therefore, an instrument with which the United States exercises power over sovereign acts of foreign governments.

Government subsidization of domestic industry has become an increasingly contentious issue among the Contracting Parties to the GATT, particularly among the industrialized signatories. That such controversies should arise among nations which can be generally described as having market economies may seem odd. But, the substantial differences of perception between these countries about the appropriate role of government in a modern market economy has given rise to questions that country, in fact, each government, answers differently. What is a subsidy? When is it legitimate to employ subsidies? When is it legitimate to countervail subsidies?

In the absence of any agreement on these questions, and ignoring (or perhaps ignorant of) the profound philosophical and political differences of opinion that prevent agreement, the United States has unilaterally and aggressively applied its CVD law, particularly since the late 1960's, in an attempt to stop foreign governments from subsidizing domestic industries.

Subsidies are some of the more obvious and controversial forms of government "intervention" in economic affairs. The so-called distortions caused by subsidies have become more apparent and pressing as tariff barriers have been progressively reduced (the falling-water level theory). Governments appear to have found that national comparative advantage can be enhanced by such government interventions and have engaged

increasingly in subsidy practices (the rising-reef theory).<sup>1</sup> In response, the United States has stepped up its attacks on foreign subsidy programs. The CVD law has been the primary instrument employed in this cause.

United States trade rhetoric claims that government "interventions" such as subsidies are "unfair" because they allow a foreign industry or firm to reduce costs, and perhaps prices as well, and thereby gain a larger market share either in the export market, or at home through import-substitution. The United States emphasises that the elimination of subsidies serves the interests of the international trade system as a whole, as well as American domestic interests. By preventing governments from creating or maintaining such distortions to competition, the United States acts to uphold the post-war international economic order. This order, as we have seen, is based on the premise that competition should determine the international pattern of trade. The conventional wisdom holds that by reducing foreign government "intervention" in economic affairs the United States helps the international economy to function more efficiently.

On the strength of this conviction, American policy-makers have substantially modified the countervailing duty law through statutory emendation and pragmatic administration. However, this process of change has subverted the statute. The American CVD law has evolved into a measure which is inherently anti-competitive both in principle and in practice. It probably generates greater "distortions" than the distortions the law was created to eliminate.

As a result of this process of change, a divergence developed between United States rhetoric of ensuring "free(r) and fair(er) trade" by the reduction of foreign government "intervention", United States countervailing duty policy which is, in reality, aimed at reducing the play of market forces and limiting the role of competition. It is now apparent that this divergence between rhetoric and policy has emerged as a profound contradiction between the supposed and the actual objectives of CVD policy.

This contradiction poses serious political problems in the realm of international relations. The most troubling aspect of this contradiction is not simply that the CVD law

has been "captured by protectionist forces"<sup>2</sup>, which some economists have put forward as the main issue.<sup>3</sup> Rather, the real issue is that CVD law is an instrument of power, a technique of economic statecraft, which the United States uses to compel foreign sovereigns to change their behaviour, to change their economic policies, to change their economic ideology. The contradiction between the CVD law's supposed aims and the actual aims makes it necessary to ask: is this economic statecraft being used by the United States to uphold or to undermine the principle of competition?

A second problem posed by United States CVD policy arises with regard to the rules of the international economic order. Rules, as Hedley Bull demonstrated, help to sustain order. They define what kind of conduct is consistent with that order. One of the most striking aspects of the international rules on the use of subsidies is that the few rules that exist are highly circumscribed. Essentially the rules on subsidies aim not to eliminate the use of subsidies, nor even necessarily to reduce them, but rather to provide a means of regulating the use of those subsidies that distort trade patterns and injure competition.<sup>4</sup> However, while what is internationally agreed-upon under the GATT and the Subsidies Code is often vague and ambiguous and therefore subject to controversy; what is not agreed-upon is definitely not agreed-upon. United States CVD policy, as we shall see, is aimed, for the most part, at the practices and issues on which there is no internationally agreed upon rule, nor even any agreed definitions. In short, this technique of statecraft is used to establish unilaterally, according to the judgement of the United States, what a legitimate trade practice is (subsidy practice) and what is not.

A third political problem also arises. In practice the CVD law is an instrument which works by infringing upon foreign governments' sovereignty and autonomy. Sovereignty, Richard Cooper explains, represents foreign governments' formal ability "to make their own decisions -- and to renounce decisions formerly made".<sup>5</sup> Autonomy, in contrast, describes "the ability to frame and carry out objectives of domestic policy which may diverge widely from those of other countries."<sup>6</sup> With the CVD law, the United States limits the range of options available to a foreign government when that government makes

domestic policy choices. The very existence of a CVD law encourages foreign governments to capitulate to its terms if governments wish to avoid transgressing it.

We need to ask whether the methods and objectives of United States CVD policy are consistent with the legitimacy established under the post-war international economic order. Legitimacy in that context, we will remember, is defined by international agreement about the permissible aims and methods of trade policy.<sup>7</sup> The central permissible aim of trade policy is to enhance the role of market forces and competition in the international economy. The primary permissible methods are that trade policies should be applied on a most favoured nation basis, and according to the principle of national treatment. One of the most important tenets of the post-war economic order is that states and their governments have wide freedom to define their own economic best-interests and to pursue domestic economic policies which are in accordance with those interests.<sup>8</sup> The sanctity of sovereignty is, then, also an important element of the GATT order.

The CVD law serves to induce foreign governments to modify their policies, in effect to change the definition of their "best interests". The United States stresses that national and international interests on this issue (intervention through subsidies) converge. All countries will be best served by reducing the role of government in economic affairs, specifically, by eliminating subsidies. However, this convergence of interests is neither certain nor necessarily served in practice. The United States' rhetoric emphasizes "market ideology" and "market standards". Yet, if we strip away the rhetoric we shall see that it obscures from view many policy actions that are in complete opposition to that rhetoric. It is easy but dangerous to confuse rhetoric and reality, especially because rhetoric is always tailored for political presentation.

To get at the substance of CVD policy, it is necessary to examine the CVD law in detail. It is necessary to examine how CVD policy is used to compel foreign governments to change their behaviour, to ask, on what grounds a change is demanded and to determine, to what end power is exercised?



In this chapter the central thesis is explored with regard to the CVD law. Rhetoric and policy have not only diverged, rhetoric and policy contradict each other. By strengthening the CVD law, the United States has increasingly undermined -- not enhanced -- market principles, competition and, as a result, the post-war international economic order.

## **WHAT IS A SUBSIDY?**

There has never been any international consensus about what constitutes a subsidy. Governments have fundamentally disagreed with one another over definitions, according to their respective notions of the proper role of government in economic affairs. Due to this lack of consensus the numerous international negotiations that have tried to define and negotiate subsidies have typically, as two frustrated American trade negotiators put it, got "nowhere" "slowly".<sup>9</sup> The lack of consensus is caused primarily because many governments believe that most subsidies are "strictly a question of national or internal policy."<sup>10</sup>

For the most part there is agreement that those subsidies that have "trade effects" should be regulated. When do subsidies have "trade effects"? Subsidies that governments use specifically to improve export performance obviously will have trade effects on export markets. For this reason it has been agreed that export subsidies on primary and non-primary products should be regulated and reduced if not eliminated. Indeed, under the GATT, export subsidies on manufactured goods are prohibited. There are some entire sectors of commerce which are not subject to the GATT rules such as textiles and much of agriculture. A separate set of rules has been developed to address these sectors. But, governments provide many subsidies domestically for domestic reasons. It is often difficult, if not impossible, to discern whether such subsidies have trade effects. It is even more difficult to get those engaging in domestic subsidy programs to admit to trade effects. In the end, all governments that pursue subsidy programs, whether the subsidies

are domestic or export, do so for "domestic reasons". No agreement on the definition of a subsidy has been reached because a definition would constrain governments from using subsidies to achieve their domestic objectives.

Neither the General Agreement on Tariffs Trade nor the Subsidies Code explicitly define the term subsidy. Instead, the GATT rules allow contracting parties to use nationally legislated CVD law as a means of resolving subsidy problems that arise between nations. In practice it has been left to national discretion to define what constitutes a subsidy and to determine when subsidies are actionable.

Oddly, in spite of this lack of a common definition for the term subsidy, it has been widely accepted for some time that subsidies can be divided into two categories: export subsidies and domestic subsidies. For the purpose of opening our examination of subsidies, we can very broadly define an export subsidy as a payment or an aid which is given by government to a domestic industry or firm, and is itself contingent upon the exportation of merchandise. A domestic subsidy, in contrast, is most broadly conceived of as any aid or benefit, such as payments or exemptions from regulatory schemes, bestowed by government on domestic industry or firm. However, broad definitions of subsidies, as we shall see, are impractical.

International efforts have concentrated on regulating the use of export subsidies. It is not possible to relate the entire history of these international attempts here. Basically, the GATT rules require that signatories relinquish the use of export subsidies<sup>11</sup> on both primary and non-primary products.<sup>12</sup>

In contrast, domestic subsidies are not only unregulated, they are expressly authorized as long as they are paid exclusively to domestic producers and do not aim to affect the pattern of international trade.<sup>13</sup> Countries whose subsidies do create trade effects on the economies of other contracting parties are required to notify the GATT if those subsidies result in increased exports (whether by accident or design). According to the GATT, Contracting Parties should be willing to negotiate about the limitations of subsidies that produce trade effects. As one would imagine, there is little incentive for a

government to admit that its subsidy policy has trade effects on other national economies. Given the difficulty of establishing the link between the cause and the effect in international trade,<sup>14</sup> there are few instances when governments have been willing to admit the effects of their policies, let alone change the policy.

National governments are free under the international agreements to countervail any sort of subsidy they like, whether such subsidies are strictly in violation of the GATT or not. There has been greater international consensus and agreement about regulating the procedures by which national governments countervail than about what they countervail.

In lieu of definitions, governments have instead developed lists of those specific subsidy practices which are considered objectionable. For example, the Subsidies Code, to which not all the Contracting Parties are a signatory, includes the Illustrative list of Export Subsidies that simply describes certain objectionable subsidy practices.<sup>15</sup> Often, though, the listed practices are considered more objectionable by some governments than others.

It has been left to individual governments (at the insistence of individual governments) to define what constitutes a subsidy, to set the terms on which a subsidy becomes actionable under their laws, and also to choose the method used for determining the size of both the subsidy and its commensurate countervailing duty.

However, even national governments have been unable to define subsidies in any easily apparent or fixed manner. In United States trade law there is now no express statutory definition of a subsidy, nor has there ever been. Rather, the applicable definition has been established by administrative interpretation. The target at which the statute is actually aimed remains vague and ambiguous.

There are too many different kinds of trade practices that can and have been labelled "subsidies" to discuss all of them fully in this study. Instead, we will engage in a rough overview of the methods the United States has used to define subsidies. The implications of CVD law and policy in international affairs will become evident from this overview.

## A BRIEF HISTORY OF THE STATUTE

Before examining how subsidies have been defined in practice it is necessary to briefly review the statute's history. This will clarify why there is no fixed definition of a subsidy in United States trade law. Also, it will reveal the intended and perceived purpose of the law. It will also demonstrate how the law has evolved as a technique of statecraft. Finally this review will outline the process of transmutation by which the law has been modified and thereby subverted.

Lack of inter-governmental consensus in the late 19th century about how, or even whether, to regulate foreign governments' subsidies on sugar exports prompted the United States to create a countervailing duty law in 1890.<sup>16</sup> If the United States could not diplomatically compel foreign governments to stop giving cash bounties and grants to their domestic sugar producers upon exportation the United States could at least countervail against such subsidies.

Like the antidumping law the CVD law draws from two competing traditions. It is a confusing mishmash of concepts and aims drawn from competition policy and from tariff policy. Peter Buck Feller points out that subsidies, at the time the first law was passed, were viewed chiefly

"as a means of negating the effect of the US tariff wall. The countervailing duty law, therefore, was intended to function as a repair mechanism to insure the integrity of that wall in the face of threatened breaches." "They [subsidies] were not considered evil in the antitrust sense". "In brief the thrust of the countervailing duty law was at the outset to protect domestic interests, rather than to protect competition as such."<sup>17</sup>

However, this tariff policy interpretation has been wholly superseded by a competition policy interpretation. After the Sherman Act was passed (the first anti-monopoly, competition law) it was recognized that foreign trade practices could have anti-competitive effects on the domestic commercial environment. A subsidy can allow the export price to be lower than the domestic price. The early law, according to this, now predominant view, envisaged subsidies as a form of price discrimination. The effects of price discrimination were well accepted to be anticompetitive.<sup>18</sup> Subsidies were

actionable under the law solely because they resulted in anti-competitive price discrimination. Prices lowered by such "artificial" means (government payments) allow exports to "unfairly" gain a greater share of the export market at the expense of unsubsidized domestic merchandise.

It is now the accepted wisdom (though this interpretation is reliant on revisionist history) that the CVD law was created to serve -- and that it now ought to serve -- as a competition policy measure.<sup>19</sup> The purpose of the CVD law is to protect competition (not competitors), rather than to restrict competition.<sup>20</sup>

The CVD law could not function exactly like the Sherman Act. As a criminal statute, the Sherman Act targeted the predatory intent of commercial actors. However, the United States judiciary has consistently refused to allow any questions involving foreign governments' sovereign acts of states to be redressed from the United States court system. According to the Act of State Doctrine the United States courts do not have the legal jurisdiction to challenge foreign acts of state.<sup>21</sup> The United States is not legally able to subject foreign governments to criminal proceedings for having violated American domestic competition law. The judiciary has thus from the earliest days tacitly recognized that the CVD law is an instrument of statecraft since the United States aims to challenge foreign acts of state with the law. For this reason, the original CVD law was structured as an administrative, not a criminal, procedure. Instead of attacking the policy itself, the foreign act of state, or attacking the government's intent in pursuing the policy, the administrative procedure allowed the United States to "countervail" or offset the effects caused by the subsidy.

It might be said that the practice of offsetting the effects of subsidies should not be conceived of as statecraft. However, as was argued in the case of antidumping policy, offsetting or countervailing effects of foreign governments' trade practices allows United States authorities to exercise power over those foreign governments. The application of a countervailing duty neutralizes the advantage the foreign government had hoped to achieve for its exporters. As a result, the duty dissuades the foreign government from

continuing with the subsidy. Dissuasion and persuasion are employed to modify a foreign government's policies. Adams and Dirlam confirm this view by pointing out that an antidumping duty (the comment is also valid for a countervailing duty) is a duty "...of a very curious sort. It is applied specifically rather than generally."

"Thus while the duty resembles a tariff in form, on a functional level it more closely resembles a sanction intended to punish or deter a particular undesirable act, such as a violation of an antitrust law."<sup>22</sup>

Frankly, even if no duty is applied the investigation procedure subjects foreign governments to the scrutiny and judgement, and therefore pressure and power, of another state. Whether the foreign government likes it or not, once it has been petitioned as a respondent in a CVD case, it is completely subject to the United States' definition of what constitutes a subsidy. Therefore, governments tailor their trade practices -- that is, change their behaviour -- to avoid transgressing United States CVD law.<sup>23</sup> In this sense the law provides a means of exercising power over foreign governments; the United States sets the terms of what is acceptable behaviour in the international commercial environment.

It should be noted that the original CVD law contained a provision for targeting private subsidies (subsidies provided by non-government sources) which has remained in the statute. However, it seems that this language was included only to make the law as comprehensive as possible. Private subsidies generally come under the antidumping law. No case has ever been brought against private subsidies. The law's central focus is foreign governments policy.

The first and second CVD laws, of 1890 and 1894, were applicable only to certain types of sugar imports.<sup>24</sup> Both allowed United States authorities to apply a relatively small fixed surtax to specific sugar imports which had been subsidized upon exportation. But, by 1897 a consensus had formed that it would be useful to make the procedure applicable to all merchandise that benefitted from foreign subsidies. In 1897 coverage was broadened to include all dutiable merchandise. The breadth of coverage was not extended again until the 1974 Trade Act which designates all imports, whether dutiable or not, as countervailable.

It was the 1930 Trade Act, which is still the basic CVD law, that codified the current CVD administrative procedure (in Section 303). In this statute the fixed import surcharge was abandoned. It is at this point that the "tariff wall" interpretation was superseded by the "competition policy" interpretation. A flexible, discretionary approach was adopted. By virtue of its existing control over the Customs Bureau, where all imported merchandise was identified and could be controlled, the Treasury Department was given the authority to determine whether a foreign subsidy existed and, if so, to judge how large it was and to apply a commensurate remedy. This procedure is codified in Section 303 of the Trade Act of 1930:

"[T]hen there shall be imposed on such merchandise a countervailing duty .... equal to the amount of the net subsidy."

The countervail procedure allows American authorities to tax subsidized imports so that the price or cost of the imported merchandise is raised to the level it would have been, had no subsidy been available. This remedy thus allows the imports to enter the United States on equal terms with domestically produced goods.

However, the administration of the law has from the beginning begged the central question; what is a subsidy? Since the law specified neither a definition, nor the criteria which should be used to determine whether a subsidy exists, the administrative authorities have had wide freedom to use their discretion. "Nowhere in our foreign trade regulation," Frederick Davis wrote in 1966, "is the amplitude of administrative discretion wider than in the countervailing duty arena."<sup>25</sup> He characterised the CVD law as a "sleeping giant," "[o]wing to the absence of really effective legal controls governing its availability."<sup>26</sup> The law provides the authority to act but does not explicitly specify the grounds on which action should be taken.

Even if the law is used only to offset the effects of a foreign government's subsidy programs the CVD law is made a powerful instrument by this lack of specificity with regard to grounds. Administering authorities can aim at a wide variety of practices, unilaterally claiming that the practice in question constitutes a subsidy. A duty can then be applied to the imports in question and a foreign government can be, thereby, dissuaded

from continuing to engage in the practice in question.

But, the lack of legal jurisdiction to change a foreign government's behaviour is often perceived as a mere legal technicality. For many jurisdictional problems have never been a wholly satisfactory reason not to use the law more aggressively. There have long been two competing interpretations of the statute arising respectively from the "tariff wall" and the "antitrust" background in the law.

According to the antitrust interpretation, the economic rationale for the administrative system dictates that distortions caused by subsidies should only be "corrected" or neutralized by countervailing duty taxes. The tax ought to equal exactly the net subsidy (as required by the statute). A tax that is larger than the net subsidy would only create a new distortion. According to this "antitrust" interpretation, the statute should be used solely to counteract or "neutralize" the effects of a foreign subsidy on competition. The law does not aim to circumscribe the prerogatives of foreign governments. As in the case of antidumping policy, the government's traditional orientation, derived from the antitrust reading, is to protect competition from anti-competitive trade practices, not competitors.

In contrast, the "tariff wall" interpretation gives rise to a very different conclusion. Seen as a protectionist measure, the law appears as a means of securing relief for American competitors who are damaged by foreign government's subsidies. Those who subscribe to this view have long favoured a competing approach to the "antitrust" interpretation. Not only should the law be used to reduce or stop unfair imports from entering the United States, the law should be used to deter, challenge and change (read eliminate) foreign governments' subsidy programs. A remedy should imply a penalty. According to this "relief" approach, the roots of which are embedded in the "tariff wall" background, the object should be to just plain stop foreign governments from subsidizing industries, to proscribe the actions of foreign governments, to deter foreign governments from providing subsidies in the future.

In recent years, as subsidy questions have become more pressing, the United States



government's orientation has shifted substantially toward the "relief" approach. For example, the United States Trade Ambassador confirmed in 1988:

"The one essential target of our strategy is to get government out of business: out of the business of making steel, selling grain, growing beef, building ships, and the hundreds of other ways that governments distort trade." She emphasized that the CVD law would be used to "get foreign governments out of business".<sup>27</sup>

When I queried the Ambassador about this shift in the aim of policy she appeared to be unaware that there was any significant difference between targeting the effects of foreign governments' policies and targeting the policies themselves.<sup>28</sup> This shift renders the law an more important instrument in United States trade policy. This instrument can be dangerous, however, because it suffers from the lack of guidance or controls over its aim. At which practices is this powerful instrument aimed?

## EXPORT SUBSIDIES

The early statute was directed only at merchandise which was subsidized "upon exportation".<sup>29</sup> In the simplest case a subsidy would be paid for every unit of merchandise as long as the merchandise was exported. The subsidy would allow the seller to provide the exported good at a lower price than costs would normally require. The result of this subsidy would be to allow the export price to be lower than the domestic price. Or, if the "tariff wall" interpretation is applied, the imports would be undervalued and therefore subject to a lower import tariff, thus reducing tariff income for the United States. In such instances the countervailing duty law could offset the subsidy by requiring that a tax be paid on the subsidized imports.<sup>30</sup>

For example, in 1937 the Italian government passed a Royal Decree officially proclaiming that cash payments would be given to any domestic silk producers contingent directly on the export of silk. This program was countervailed by the United States in 1937.<sup>31</sup>

However, most subsidies do not take the form of direct payments. Instead,

governments have been very resourceful in creating a variety of indirect export subsidies which are less easily identifiable. Indirect export subsidies occur when funds or benefits which aid exportation are made available through some means other than a direct payment from government. For example, governments have sometimes created multiple exchange rate systems to favour exportation or have manipulated their currency to enhance export performance. Or, governments have exempted a domestic firm (or industry) which produces mostly for export, from tax(es), even though other domestic have had to pay the same tax(es). In other words, as subsidy can exist even if there is no actual budgetary expenditure for it.

The early CVD legislation gave express authority to countervail both direct and indirect subsidies precisely because many subsidy programs could be camouflaged through the use of indirect means. The majority of CVD cases since 1934, when records were first kept, have been brought against these indirect export subsidies.

However, there are two fundamental problems with targeting indirect export subsidies. First, in some indirect export subsidy cases the export price and the domestic price may be the same. The existence of the subsidy may be ascertained only by looking at its impact on the costs of production. For example, in the case of a tax exemption the cost of producing the good is not as high as it would have been had the product been sold in the domestic market. Second, it is difficult if not impossible to draw a clean distinction between indirect subsidies which intend to aid exportation and domestic subsidies which do not intend improve export performance, but in fact do. Therefore, a domestic production subsidy is often also an indirect export subsidy.

The domestic subsidy problem was envisaged in the early 1920's. New language for the statute was drafted which broadened the statute to cover all indirect export subsidies even when such subsidies did not create price discrimination. It would be folly, however, to grant that the drafter(s) had the foresight to anticipate the emergence of domestic subsidies as a major international trade problem. Domestic subsidies, are now one of the single most contentious issues among governments, were not seen as a major issue when

the law was changed to include them. Even Jacob Viner, whose ideas so deeply influenced international thinking on international trade problems, and continue to do so, clearly did not think domestic subsidies were or would be problematic. He wrote;

"The grant of official bounties on production has rarely, if ever, occurred, and it is altogether unlikely that it should ever attain importance as a factor in international competition."<sup>32</sup>

As with so many crucial changes in the trade remedy laws, this important change was made with no discussion or debate.<sup>33</sup> In the 1922 Trade Act the Congress profoundly changed the CVD statute by dramatically altering the language. Jacob Viner explained.

"But without any emphasis in the various committee reports on the bill while in progress and without any mention in the Congressional debates the clause was modified."<sup>34</sup>

The words "upon exportation" were changed to: "upon the manufacture or production or exportation of any article or merchandise manufactured or produced in ... such country".<sup>35</sup>

The primary issue would now be the impact of a subsidy on a firm's costs. Reductions in a firm's costs allowed unfair changes in prices and/or operating margins. The effects of these changes in costs would be felt by American competition.

The inclusion of domestic subsidies required that the statute be changed in another way. Since the act of providing a subsidy could not be legally challenged by the United States, the statute could not continue to use the words "upon exportation". Not all exports go to the United States. It was the "effects" of subsidies on United States competition which was now important. This is why the 1930 Trade Act replaces the words "upon exportation" with,

"upon the importation of any such article... into the US, ....there shall be levied and paid, ... an additional duty equal to the net amount of such bounty or grant" (emphasis added).<sup>36</sup>

So, ever since the 1930 CVD law was passed, the actionable phenomenon has been the trade effects on United States commerce caused by the subsidization of exports.

How does the United States target the effects of foreign subsidy programs?

Unlike antidumping law, the CVD statute did not require or allow the presence of injury (to competition as caused by the unfair trade practice) to be a relevant factor until 1979. No linkage needed to be shown between the subsidy and incurred injury. This saved officials who administered the statute from the problem faced under antidumping law, namely the need to distinguish between the injurious effects of healthy, normal and fair competition, and the injurious effects of predatory and unfair competition. As we have seen, the AD law's administrators have resolved this problem badly. Under the AD law the test is not usually injury to competition but injury to competitors -- a standard that is contrary to the protection of competition from the adverse effects of predatory trade practices.

But, how are adverse trade effects found to exist, let alone measured, if injury is irrelevant? Under the law a price differential between imports and exports is superfluous. There are only two choices. Either a subsidy can be found and then it must be argued that the subsidy has trade effects, or trade effects can be found, which prompts an investigation to establish that a subsidy exists. But, subsidies exist in many forms and it needs to be emphasised again, there is no substantive definition as to what constitutes a subsidy.

The law's administrators have never been statutorily required to justify the criteria that is used to label and condemn a practice as a subsidy. The mere existence of a subsidy, as defined and determined unilaterally by the United States, is sufficient to activate the statute and bring pressure to bear on a foreign government. While Treasury administered the statute its practice was, as Butler notes, "to announce that it believes that a subsidy is being granted and that it intends to impose countervailing duties unless satisfactory evidence is presented to negate its tentative conclusion".<sup>37</sup>

It was left to the discretion of the Treasury department to determine when a subsidy existed, whether export or domestic, direct or indirect. As long as the statute was

not actively applied it remained a fairly academic question to ask, and a few academics did ask, how Treasury defined subsidy and how Treasury determined whether a subsidy existed.

But, as this formerly obscure law was taken off the shelf, dusted down, and put to work in the 1960's,<sup>38</sup> the arbitrary nature of the decision-making process has become an increasingly important problem. Now that the statute has emerged as one of the primary trade policy tools employed by the United States Government it is crucial to ask: What is a subsidy? How is it substantiated that a subsidy is real?

It is difficult to tell what criteria Treasury used to define the term subsidy because CVD orders were accompanied by only a terse explanation, if by any at all. In 1955, a Congressional investigating committee concluded,

"in the absence of any reports from the Treasury Department as to the basis on which its determinations of the existence of subsidization have been made, it is difficult, if not impossible, to analyze the administration of Section 303 (the CVD law)."<sup>39</sup>

Until 1979, the United States Courts upheld the Treasury Department's authority to omit complete explanations. The ambiguity and broad flexibility allowed appears to have been perceived by Congress as favourable to American interests. While academic and professional observers criticized the lack of controls over the decision-making process at Treasury, the very arbitrariness of the process, industry and Congress assumed, worked in favour of the domestic petitioner.

After 1968, when the statute was more actively being brought into play, Congress appears to have become increasingly frustrated by Treasury's freedom. Only a single countervailing duty order was issued by Treasury between 1954 and 1969. Fear grew that Treasury's decisions were being driven more by international considerations, Treasury's agenda being more driven more by foreign policy concerns than by domestic concerns. In 1979, Congress transferred the authority to make CVD determinations to the Commerce

Department because the consensus in Congress was that Treasury was not being tough enough on foreigners.

The lack of a fixed definition for the term subsidy is important not only because the law has emerged from its former obscurity as an important policy tool. Once subsidies began to be seen as an increasingly important trade issue, in the late 1960's and early 1970's, Congress and various frustrated petitioners wanted to broaden the range of actionable subsidies. This was partly because foreign governments were becoming more adept in obscuring and camouflaging subsidy programs, it was also partly because the fast-growing impact of imports, whether subsidized or not, on the American economy. Legislators began to take the breadth of the 1922 language seriously for the first time.

The line between indirect export subsidies and domestic subsidies had always been blurry. But, the line of demarcation appeared clearer the farther away Treasury kept from it. Now that the United States began to venture toward that line, it became apparent that the line was a very murky area indeed. While export subsidies have remained a major target of American CVD policy, and all countervail investigations until 1968 were aimed at export subsidies<sup>40</sup> (almost entirely indirect ones), domestic manufacturing and production subsidies have increasingly become the focal point of CVD policy in the 1970's, 1980's and will continue to be in the 1990's. The distinction between an export subsidy and a domestic subsidy has deteriorated. If an indirect export subsidy or a domestic subsidy has an effect on exports to the United States and, therefore, an effect on American competition then the subsidy is actionable under the statute.

## **A STATUTE SUBVERTED**

If we look at the CVD law as an instrument of economic statecraft the lack of a definition for the term subsidy is a singularly important issue. The modifications made to the 1930 statute magnify the law's importance. The statute is codified as an administrative procedure that targets the "effects" of a subsidy without defining what constitutes either a trade effect or a subsidy.

Though the law is supposed to serve as a competition policy measure, the alterations made in the statutory language have subverted it.

As the scope of the statute has been broadened the notion of a "distortion" has shifted away from specific phenomena, the trade effects direct export subsidies cause, to an undefined range of phenomena: the effects of subsidized imports on the United States (export subsidies, indirect export subsidies, domestic subsidies). The distinction between an export subsidy and a domestic subsidy remains artificial since there is no statutory definition to provide substance. In short, the statute provides the administrators the authority to unilaterally judge whether or not any foreign government policy can be construed to be a subsidy. And, it allows those authorities to take action against subsidies. But nowhere is it made clear what a subsidy is.

There can be little doubt that the United States uses CVD policies to exercise power over the sovereign acts of foreign governments. The private American firms and industries which invoke the law are well aware of this. For example, in a guide to CVD law Donald E. deKieffer, well-informed from his experience at the United States Trade Representative, made the point unequivocally.

"Countervailing duty actions provide an administrative ... mechanism to attack the domestic economic policies of foreign governments ... "41

In applying CVD, law the United States challenges the validity, the legitimacy of foreign acts of state ( the term "legitimacy" is used here in a more general sense than we have been using it with reference to international economic order in earlier Chapters). The American authorities decide when a foreign government's economic policy constitutes a subsidy and when it doesn't. The critical point is that the countervailing duty law, as it is currently structured, requires American authorities to decide whether a foreign government's subsidy programs are legitimate (it is supposedly the economic legitimacy of such programs that is in question). But, American officials are required to undertake this task using a law that provides no specific criteria or rules by which such judgements should be made.

How can it be determined that a particular foreign government program is actionable under the CVD law if there is no definition of a subsidy? The lack of substantive and legal constraints or guidelines provides those who invoke the law with wide leeway to simply attack foreign economic policies which the United States does not "like". This can be justified by arguing that these policies cause "distortions" to trade or are an example of "inefficient government intervention". However, a "distortion" to one government often appears to be a "correction" to another. "Inefficient" policy to one is often undertaken by another to "correct" market failure. Judgement on such controversies is a question of perception, ideology and, above all, politics. We shall return to this fundamental point in greater detail later.

So, we must ask what is the United States compelling foreign governments to do or not to do? On what grounds are foreign economic policies actionable under the CVD law? We return to that same question. What is a subsidy? On what grounds is the United States compelling foreign governments to change their behaviour? The law is supposed to be a competition policy measure, that is, it is supposed to protect competition from anti-competitive trade practices. But, what, under the law as it has been structured, is an "anti-competitive" trade practice?

## **SUBSIDIES: THE INTERVENTION VERSUS NON-INTERVENTION APPROACH**

Although the statute provides no explicit definition of the term subsidy, it does contain certain implicit assumptions which guide policy-makers and administrators in their interpretation of what constitutes a subsidy. The main guidance provided, as Daniel Tarullo points out, is in the law's implicit assumption that "governmental non-interference in the market" is both desirable and "normal".<sup>42</sup> Goetz, Granet and Schwartz similarly point to the law's inherent assumption of "public sector neutrality".<sup>43</sup> These assumptions derive from the law's theoretical basis.



Sometimes it is said that orthodox neo-classical international trade theory, or free trade theory, has become irrelevant, assuming it ever was relevant, to understanding how the international trade system actually works. Even though this is may be true in one sense, it is surely false in another. While theory has been so abstracted that it often fails to portray real problems in the real world very accurately, policy-makers have nonetheless created policies and laws which are based on the abstract theory. CVD law is a classic example of this. To understand what a subsidy is under the law one must first look to the theoretical foundation of the CVD law.

## **ORTHODOX TRADE THEORY**

International trade theory has historically been a relatively neglected offshoot in the study of economics. International trade theory has generally been created by extrapolating the most idealized conditions possible in microeconomics and narrowing their application to special cases. Ricardo, for example, who is considered the founder of (liberal) international trade theory, developed the doctrine of comparative costs.<sup>44</sup> This theory was based on the assumption that under conditions of perfect competition two nations, England and Portugal, each of which could produce cloth and wine (respectively) with less labour and more cheaply than the other, would be better off by buying the desired goods from one another than by attempting to produce them at home. Of course conditions of perfect competition exist only in the imagination. It is now acknowledged that comparative advantage is a dynamic, not a static, condition.<sup>45</sup> Even though international trade theory has vastly improved in this century it still tends to explain what will happen under special and idealized circumstances.

The concept of subsidies under the CVD law is also based on the highly idealized concept of perfect competition. This assumes that there are a large number of buyers and sellers in the market, all of whom have perfect information about all the available prices, and none of whom can either demand or offer a quantity large enough to affect prices. In

addition, the pure theory of international trade assumes that there is a tendency towards general equilibrium in the market. This is often referred to as "Pareto optimality". According to this notion, equilibrium occurs when the value of national exports is just equal to the value of national imports. This notion would seem to be subject to serious doubts today.

Both of these concepts, perfect competition and Pareto optimality, themselves rest on the assumption that governments and markets are separate entities which should be kept separate. Orthodox neoclassical economic theory posits that competition which is unfettered and undisturbed by government "intervention" or monopoly power will create the most "efficient" economic outcome. Extrapolated to international trade, this notion is the heart of free trade theory: reliance on genuine comparative advantage will give rise to the most productive and efficient economic outcome. Interventions by governments, especially interventions which are designed to favour some sector or producer, provide artificial advantages which create distortions to the most efficient pattern of trade. This, in turn, creates a less than optimal economic outcome.

Subsidies, particularly those which enhance export performance, are considered "anti-competitive" within this model of perfect competition for several reasons. Subsidies are predatory in that they deliberately attempt to artificially displace the sale of non-subsidized goods in the export markets. If the subsidy is made available domestically then sales of domestically-produced goods are encouraged at the expense of non-subsidized imports (this is called import-substitution). The upshot of this, as far as the theory goes, is that the pattern of trade is distorted. Artificially created changes in the pattern of trade forces the restructuring of markets. This means changes are effected to the pattern of production, the pattern of sales and employment and income. Ultimately these "distortions" lead to inefficient alterations in the structure of industry.

The intended purpose of the United States CVD law is to "correct" the distortions caused by foreign government's attempts to create artificial advantages for their domestic industries through subsidies, thus returning world trade to its state of perfect competition

and Pareto optimal terms.<sup>46</sup> But, orthodox trade theory and non-interventionist ideology leave certain issues unresolved. What exactly is a distortion? What exactly is a subsidy?

## **EFFICIENCY ONLY**

By one interpretation the CVD law envisages any benefit conferred by governments on domestic industry that either aids exportation or increases import substitution in the home market as a subsidy which distorts the normal, desirable, most efficient economic pattern. The so-called "efficiency-only" school of thought reckons that perfect competition is disrupted by subsidies. The solution is to use the CVD law to offset the effects of subsidies through the application of a border tax to the subsidized imports. Seen this way the CVD law serves the interests of efficiency by "correcting" the distortions caused by foreign government intervention.

The purpose of a subsidy is, as Robert Gilpin has comments "to create comparative advantage and internationally competitive industries especially at the "high-value added" end of the industrial spectrum, and also to promote an export-led growth strategy."<sup>47</sup> Much of the modern rhetoric surrounding the use of CVD law emphasises the inefficiency of foreign government subsidies.<sup>48</sup> Intervention via subsidies is associated with mercantilism. It has become popular in recent years to refer to subsidies as a manifestation of the so-called New Protectionism, a modern form of mercantilism.

There is another camp in the "efficiency-only" school of thought. Some say that CVD law itself causes greater distortions than subsidies. The law has been captured by protectionist forces. The CVD law has been abused to the degree that it no longer serves efficiency objectives but undermines them. It has become common among this wing of the "efficiency-only" school to refer to the recent irresponsible use of the CVD law itself as a manifestation of the "New Protectionism". This is not a recently discovered angle. True laissez faire economists, such as those of the Austrian School have often claimed that competition policy is itself an unnecessary "intervention" since the abuses of market power

it is supposed to police are not generally that severe. The "free market" solution it is believed works even with regard to the abuse of monopoly power.

Both camps in the efficiency-only school agree on one point. The law should be used only to serve the cause of efficiency.

For the efficiency-only school a subsidy is any government intervention that confers a benefit on the production or purchase or exportation of domestically produced goods. A subsidy can take the form of a payment, or a regulatory scheme which confers a benefit on domestic industry, or an exemption from a regulatory scheme or taxes, among others. Any government aid which benefits domestic industry leads to a less efficient outcome is a subsidy. Subsidies are defined by the fact that they are "inefficient".

The official rhetoric used to justify the use of the CVD law tends to emphasise that subsidies are bad because they are inefficient. The purpose of the law is to eliminate inefficiencies created by subsidies.

## **INJURY ONLY**

There is another, competing, interpretation of the CVD law. This interpretation is that it is unrealistic to start by assuming that there is perfect competition. Since the early part of this century, certainly with the work of Joan Robinson<sup>49</sup>, many economists have accepted that markets are "imperfect". Once the underlying conditions of the market are relaxed in this manner then it becomes much more difficult to simply condemn any intervention by government. In fact, it becomes obvious that government must play an active part in "correcting" the imperfections present in the market. Since the so-called first-best solution (that the market can function perfectly all by itself) is unavailable there is a need to turn to the second-best solution (governments must help markets to function perfectly, or as well as possible). A distinction must be made between interventions which correct market failure and interventions which cause or sustain market failure.

CVD law, interpreted in this light, is an instrument to be used to attain or

approach a situation of perfect competition. It should be used to correct foreign subsidy policies which create market failure, distortion, which are anticompetitive. The only trick is determining the criteria on which the distinction between policies that correct or cause market failure can or should be made.

Subsidies are defined in the same way for the injury-only school as for the efficiency-only school. The difference is that the injury only school, drawing from an antitrust reading of the statute, promotes the idea that only inefficient subsidies, those which cause or sustain market failure, should be actionable under the law. Market failure usually manifests itself in the form of injury to competition. Therefore, subsidies are actionable when they cause "injury" to competition.

Both schools have several points in common. Both aspire to reduce the role of government in economic affairs in order to allow competition to function more perfectly. For both the CVD law is a means of achieving this. For both the CVD law should not be abused and transformed into a protectionist instrument.

## **THE FAILURE OF THE EFFICIENCY-ONLY AND INJURY ONLY SCHOOLS**

United States CVD law is based on the implicit assumption that perfect competition, even if it is not attainable, at least is something for which we ought to strive. Economics can be separated from politics. Or, politics should be made to serve economics. When governments intervene it should be to foster competition not impede it.

It is nothing new to claim that subsidies are a fundamentally political phenomenon. It is the political nature of subsidies which has long made them so objectionable. A foreign government's decision to provide special support for a particular industry is political, though it may be manifest through economic policy (the granting of a subsidy), since it necessarily involves making choices about who will get support.<sup>50</sup> Subsidies which aid

exports are considered pernicious political acts. Subsidies are, as John Jackson points out, an,

"obvious attempt to impose burdens on other countries (burdens which are more political or producer-oriented than they are economic in a broader sense),..."<sup>51</sup>

Governments provide subsidies, whether for exports or for domestic production, for only one reason; it is precisely because they want to alter the economic pattern which market forces left alone would create. They want to change the economic outcome. State power (via subsidies) is aimed at improving the terms of trade. This is traditionally considered the distinguishing characteristic of mercantilism. Therefore, subsidies are political acts. They "politicize" economics.

The problem with the intervention versus non-intervention approach is that it culminates in the following dead end. Subsidies are a form of the "New Protectionism"; and, CVD law, if abused, can be a form of the "New Protectionism". This traditional line of analysis -- intervention versus non-intervention -- renders the problem and the solution indistinguishable. The apparent end result of the traditional approach is to depoliticize economics by simply eliminating government intervention altogether, whether the intervention takes the form of either subsidies or trade restrictive CVD policy.

Here we reach the traditional point at which economics and politics are considered to be at odds with each other. Given that this theoretical position has been so well developed and so widely accepted for at least 300 years, one would think that a definition, a good solid economic definition of subsidies ought to have emerged from this purely economic "intervention versus non-intervention" approach. But it has not. Why not?

## GOVERNMENTS AND MARKETS

Daniel Tarullo has eloquently demonstrated that the implicit assumption that states can be separated from markets is counterfactual.<sup>52</sup> It is not possible to separate interventions by governments from the market system. After all, it is the very existence

of government which allows the market to function. It is government that guarantees and protects the property rights and the contract rights without which a market cannot exist. When government plays this role it "aids" the production and manufacture of goods and services. Even F.A. von Hayek<sup>53</sup>, one of the most virulent defenders of market principles and competition, concluded;

**"In no system that could be rationally defended would the state just do nothing".<sup>54</sup>**

Under the CVD statute, administering authorities attempt to determine what the cost of producing a subsidized import would have been in the absence of the subsidy. The difference between the subsidized cost and the "true" unsubsidized cost equals the amount of the countervailing duty. This procedure assumes that there is an inherent discernable true cost which would be apparent but for the intervention by government. But Daniel Tarullo's argument shows that this is false. He explains;

**"Basic choices about the kind of contract system to be adopted affect the costs of the activities under analysis ... "<sup>55</sup>**

**"So there is no coherent concept of costs that is not associated with choices about the form of state intervention that will create property and contract rights."<sup>56</sup> (emphasis added).**

There is no inherent true cost that would appear in the absence of government intervention because the market itself could not function (or, at least, not very well) without government to protect basic property and contract rights. Costs are heavily influenced by the role of government; how government protects contract and property rights affects the whole economic environment in which firms must function.

In addition to basic legal structures, states provide infra-structure support, as recommended by Adam Smith.

**"Government has the duty of erecting and maintaining certain public works and certain public institutions which it can never be to the interest of any individual to erect and maintain because the profit could never repay the expense to any individual or small number of individuals though it may frequently do much more than repay a great society."<sup>57</sup>**

Governments perform those activities which the market does not deem profitable but

which are in the public interest. States build roads and schools, set up income tax systems to redistribute wealth, and create regulatory schemes, among other things. This "aids" the production and manufacture of goods and services.

The "cumulative effects" of these roles are so great, Tarullo emphasizes, that we cannot reasonably "disentangle these effects from some hypothetical underlying, undistorted, market" (emphasis added)<sup>58</sup>; especially since no underlying, undistorted market, free from government intervention exists. Without government no free competitive market exists. Any market that did exist would be an example of competition that was far from perfect, since, at a minimum, contract and property rights would be uncertain.

There is no good, solid, workable definition of subsidies because it is impossible to make a clean distinction between the state and the market. If any government aid to domestic industry is a subsidy then the very existence of a government that provides market-promoting legal structures, can be construed as subsidy.

It is highly ironic, then, that the United States should be aggressively applying the countervailing duty statute, and attempting to impose a tough "non-intervention" market ideology on its major trading partners in the post-war period. For this is exactly the period in history when there has been near universal agreement among economists, politicians, and the general public that the pure "free market solution" not only does not work (in economic terms) but also that it does not meet social needs (in political terms).

"What must be clear," the economic historian Lord Roll tells us, "is that the acceptance of responsibility by governments -- elected governments in one or other form of democratic system -- for the maintenance of a high level of economic activity, for avoidance of major economic fluctuations, perhaps even by implication, for some progress towards greater economic equality, is one of the major turning-points in modern history."<sup>59</sup>

This "staggering change"<sup>60</sup> was achieved not only for political reasons. The majority of contributions to economic theory and thinking in this century, particularly since the Second World War have confirmed that "the spontaneous tendencies of the market can now be shown as by no means inevitably leading to an optimal distribution of scarce resources."<sup>61</sup> Nor would it inevitably lead to stability, growth, a stable or high



level of employment, or an optimal or stable cost of money (inflation and interest rates).

Economists have differed, of course, over the appropriateness of various methods of achieving these goals. But, the major controversies, for example the one between those who favour broad macroeconomic management by means of fiscal expenditure (neo-Keynsians) versus those who favour macroeconomic management by means of a controlled supply of money (monetarists), have been caused by differences of opinion about how and not whether to achieve these economic and political goals. Almost no one would argue that government should not seek, as Lord Roll explains, "to subserve the broad objectives of economic policy as now commonly accepted: full use of resources, growth, stability, international balance."<sup>62</sup>

So, during the post-war period governments have been increasingly actively engaged in altering the economic pattern which market forces left alone would create. Governments have deliberately sought to improve the economic outcome. To condemn in total these efforts as "inefficient" or anti-competitive would be ludicrous in the modern world.

Even if the political requirements necessary to manage a democratic economy could be reduced or even eliminated, economic theory still would not be able to resolve the essential problem. Harry Johnson's explanation makes this clear.

"One implication" (of the efforts made by Meade, Lipsey, Lancaster and others to relax the Pareto optimal conditions and develop a theory of second-best options) "of that theory is that it is impossible to predict on a priori grounds -- that is, without comprehensive information about the tastes and technology of the economy -- whether the substitution of one violation of the Pareto optimality conditions for another will worsen or improve economic welfare."<sup>63</sup>

There is no purely economic method of determining whether a particular intervention enhances or reduces efficiency when efficiency is defined by political criteria. Macroeconomic management is undertaken mostly to improve the quality of peoples lives. A policy that "corrects" market failure in the view of one government "distorts" the market in the view of another. Making distinctions about the "efficiency" of interventions, or what constitutes an improved economic outcome, really boils down to political issues. The problem is exactly as Harald Malmgren explains.

"Perceptions of private and social costs and benefits vary and thus pose a fundamental analytical problem."<sup>64</sup>

The reason why no workable definition of a subsidy has emerged from economic theory is because the central assumptions of liberal economic theory, that states and markets, and politics and economics can be separated, and that perfect competition is attainable, are faulty. How, under the "intervention versus non-intervention approach" can we make an economically sound distinction between the building of schools and roads, national health programs, regional development incentives and the exemption of certain exports from domestic taxes? All are "subsidies" in the sense that they provide "aids" to industry which, without government would not exist or would not exist on such preferential terms.

How does one make a sound economic distinction between those government policies which aim to achieve broad macroeconomic goals and those which "subsidize"? The answer is that it is not possible. Any solution is made according to political and not economic criteria. And this is, in reality, how subsidies are defined under the countervailing duty law: according to political criteria and political expediency. Neither the efficiency-only nor the injury-only schools of thought identifies or addresses this point.

Proponents of the injury-only school accept that some interventions correct market failure and some create it. Some subsidies correct distortions caused by market failure. Some subsidies cause distortions. The trick is deciding which subsidy is which -- a most intractable problem. How does one distinguish between pro-competitive and anti-competitive subsidies when all subsidies are justified by the government employing them as a necessary means of achieving the broad macroeconomic goals required by modern democratic society?

The answer, for this school, has been to concentrate on the "injury" to competition caused by subsidies.<sup>65</sup> Only those inefficient subsidies that cause injury should be countervailed. But, as we saw in the antidumping chapter, normal, healthy and fair

competition cause injury. Again, how does one distinguish between the two? This tack brings us no closer to a definition of a subsidy.

## **THE ANALYTICAL PROBLEMS**

The analytical problems inherent in subsidy and countervailing duty issues are, to reiterate: (a) how to define a subsidy when a line cannot be unarbitrarily drawn between the state and the market, and, (b) how to distinguish between market-correcting and market-distorting subsidies, especially when most government interventions are defended and justified as a necessary means of achieving the macroeconomic goals necessary to the management of a modern industrial democracy. No definition of a subsidy can emerge from purely economic analysis because there is no coherent concept of costs that is independent from the political role governments play in a national economy. This is perhaps the greatest analytical problem of all. We continue to treat subsidies within an economic context, when the issues involved in subsidy questions are primarily political.

As long as policy-makers and economists focused mainly on export subsidies the analytical problems could mostly be avoided. Everybody could agree that a direct export subsidy was relatively easily identifiable and definitely injurious (even though the statute required no finding of injury until 1979). An expenditure for it could be found in the government budget, or the laws or administrative procedures that were created to implement the subsidy could be identified (although this required US authorities essentially to interpret foreign law, an undertaking which was not always done easily or accurately), or price discrimination could be identified. The old subsidy arguments, regarding international trade matters, stopped at export subsidies. Arguments were made for and against them in the case of infant industries, situations in which currencies were over or under-valued, and income redistribution. Governments and liberal economists were able to agree generally that export subsidies should be condemned.

Where there was a need to apply a subsidy to "correct" a market failure in the

domestic economy for domestic reasons, whether political or economic, it was commonly accepted that a production subsidy was a lesser evil than an export subsidy. Thus, governments were encouraged to use production subsidies in lieu of export subsidies. H.G. Johnson emphasised this point:

**"The point of central importance is that the correction of domestic distortions required a tax or subsidy on either domestic consumption or domestic production or domestic factor use, not on international trade."**<sup>66</sup>

However, subsidies are increasingly considered actionable under the statute because of their trade effects. Indirect export subsidies and domestic subsidies have increasingly been seen to have trade effects. As indirect export and domestic subsidies have become the target of United States CVD the fundamental analytical problems have emerged. There is no unarbitrary economically-sound way to distinguish between those subsidies which governments may undertake in their attempts to achieve broad macroeconomic goals and those which are injurious or aimed at improving export performance. Tarullo emphasises this point.

**"[T]hus in administering the (countervailing duty) statute the Commerce Department must determine the propriety and presumptive efficiency of foreign governmental policies. Analysis of the market correction norm embodied in the countervailing duty law is particularly significant for differing conceptions of proper and efficient governmental policies are at the root of much contemporary debate on international trade competition."**(emphasis added)<sup>67</sup>

The "legitimacy" of domestic economic policies thus becomes a central point of contention. Legitimacy here refers not to the internationally established legitimacy but is used in a more general sense. According to the international legitimacy, governments have wide freedom to pursue their domestic political objectives as they see fit. Domestic subsidies are not illegitimate in that sense. How is "legitimacy" in the general sense, then, defined?

If all governments had the same macroeconomic objectives and methods of achieving them perhaps this point would not have become contentious. But governments do not. This is not just a matter of disagreement on policy questions. It arises partly

because governments guarantee contract and property rights in different ways. von Hayek articulated this point though probably without realizing that it would become an important issue in international politics:

"... in order that competition should work beneficially, a carefully thought-out legal framework is required ..." But, he went on. "It is by no means sufficient that the law should recognize the principle of private property and freedom of contract; much depends on the precise definition of the right of property and freedom of contract as applied to different things."<sup>68</sup>

## **DIFFERING MACROECONOMIC GOALS**

Differing visions on policy questions, differing views about which macroeconomic goals to aim for and which methods should be used to achieve them, give rise to greater disagreement among the GATT contracting parties than differing legal structures. Harald Malmgren captured the point when he said,

"the role of government is pervasive, and where subsidy begins and socially necessary legislative and administrative conditions and constraints end will never be entirely clear."<sup>69</sup>

Here it is relevant to recall the comment by Henry Kissinger introduced in Chapter Two.<sup>70</sup> He explains that it is extremely difficult to resolve problems through negotiation when ideological differences exist among players. Germany and Japan differ from the United States in the ways in which their governments guarantee and protect contract and property rights. For example, in Japan there are very few lawyers and legal disputes are extremely rare. Problems in Japan tend to be settled through negotiation. In the United States, in contrast, contract and property rights are protected by a large and frequently-invoked legal framework. These differing legal structures affect the costs of doing business. Further, the Japanese legal system only allows a few hundred new lawyers to pass the required exams each year, and, as a result very few Americans become fully qualified lawyers in Japan. The Japanese cannot understand why they should change their legal system to comply with American demands that more Americans be allowed to practice law

in Japan. The Americans cannot understand how business can be conducted, i.e., contracts and property protected, without lawyers. Also the differences in national approach to managing the domestic economic environment are profound. Note that for many years the United States has been trying to get Germany to abandon its anti-inflationary policy of tight control of the money supply. The United States wants Germany to grow faster and thereby generate greater economic activity in the world economy, read the United States wants the Germans to buy more from American firms. The Germans cannot understand why they should abandon a policy which they believe to be prudent and Germany has failed to comply with American demands. Both believe the other to be less committed to the "market" than themselves.

The differences in opinion and perception about the "appropriate" role of government in the domestic economy and "appropriate" policies are the cause of great debate and political struggle even within each country among domestic political parties and among government ministries and the public.

Already we can see that the differences between the most powerful economies have given rise to intense debate over which "model" best serves the ideal of a market economy. The American model of capitalism, the Japanese model and the German model differ substantially. As the United States broadens its definition of subsidies, it opens the door to these questions: what is the "legitimate" model, what is a legitimate macroeconomic objective, what is a "legitimate" method of achieving such objectives?

To date one of the most complex problems the CVD law's administrators have had to grapple with is how to define what constitutes a subsidy in a non-market economy. They have struggled to reconcile the different philosophies of the market economies with the non-market ones so that the CVD law could be applied in non-market economy cases. How could a "normal" or true market price or cost be determined when there are no market forces at work, when there is no price mechanism? This was a problem of the past.

The problem now, and the problem of the future, is reconciling the differing

philosophies among the market economies. How can we tell what the true market price or the true cost of production would be in the absence of a subsidy when the differing methods and objectives governments pursue in managing their domestic economies means that the market conditions present in one country are not really comparable to those in another? There is not only no true price or cost discernable in the absence of government. The presence of different governments with different efficiency objectives -- when efficiency is defined by political considerations -- means that there is no universal true price or cost.

When one government says another has a policy that unfairly "subsidizes" a domestic industry, the real issue is not economic efficiency. The real issue is that one government objects to the political role and/or political objectives another has set out to achieve. The CVD law is the mechanism the United States uses to veto or penalize the political choices made by foreign governments. All the rhetoric about market standards and efficiency objectives obscures this fundamental point.

Harald Malmgren explains that the reason why no international or multilateral body would ever be allowed the authority to judge when or whether a government's internal measure constituted a subsidy<sup>71</sup> is because:

"This would be tantamount to asking an international body to evaluate and approve the economic, social and political objectives of a particular country."<sup>72</sup>

Yet, this is exactly the purpose of the CVD law. With it, the United States unilaterally judges, approves or disapproves, of a foreign government's domestic economic, social and political objectives. In effect, the law is used to unilaterally establish when a foreign government's objectives are acceptable and when they are not. The CVD law is itself a political instrument since its effective aim is political: to compel foreign governments to change their conception of their proper and efficient role. Or, it is to penalize foreign governments when they do not change their view.

The key questions are these: what changes are being demanded? Are those changes consistent with what has been internationally agreed?

1. Gary Clyde Hufbauer, "Subsidy Issues After the Tokyo Round" Trade Policy in the 1980's William Cline ed., (Washington, DC: Institute for International Economics, 1983) page 327.
2. Jagdish Bhagwati, Protectionism (Cambridge: MIT Press, 1988) page 52.
3. As we saw in Chapter Three, protectionist policies are quite legitimate as long as they make use of the market mechanism (like tariffs) or they are implemented in accordance with the internationally agreed upon rules.
4. John S Sciortino, "Calculating Subsidy Values in Countervailing Duty Cases: The use of the Present Value Methodology" International Trade Policy: The Lawyer's Perspective John H Jackson, et al., ed.s., Committee on International Trade Section of International Law and Practice, American Bar Association (New York: Mathew Bender, 1985) page 8-25 Section 8.06.
5. Richard N Cooper, The Economics of Interdependence: Economic Policy in the Atlantic Community (New York: McGraw-Hill, 1968), page 4.
6. *ibid.*, page 5.
7. See Chapter Three, page 52, notes 11-15 and pages 55-56 *infra*.
8. *ibid.*
9. Richard Rivers and John Greenwald, "The Negotiation of a Code on Subsidies and Counter-vailing Measures: Bridging Fundamental Policy Differences" Law and Policy in International Business Vol. 11, 1979, page 1449. This is how these two American trade negotiators, described their experience.
10. *ibid.*, page 1449.
11. Both direct and indirect export subsidies.
12. Article 8 of the GATT: Section 1: "Signatories recognize that subsidies are used by governments to promote important objectives of social and economic policy. Signatories also recognize that subsidies may cause adverse effects to the interests of other signatories." Section 2: "Signatories agree not to use export subsidies in a manner inconsistent with the provisions of this agreement."
13. Article III Paragraph 8(b). In accordance with the so-called trade effects doctrine.
14. John Hicks, Causality in Economics (Oxford: Basil Blackwell, 1979).
15. Illustrative List of Export Subsidies, 31 UST 513 TIAS 9619 (1979).
16. Peter Erenhaft, "Protection Against International Price Discrimination: United States Antidumping and Countervailing Duties" Columbia Law Review Vol. LVIII, 1958, page 52.
17. Peter Buck Feller, "Mutiny Against the Bounty: An Examination of Subsidies, Border Tax Adjustments, and the Resurgence of the Countervailing Duty Law" Law and Policy in International Business Vol. 1, No. 1, Winter 1969, page 22.



18. The extrapolation of domestic price discrimination to international does not work. Domestically the price discrimination occurs within one market. Internationally the seller is merely adjusting prices to the conditions prevailing in different national markets.

19. Peter Feller believes that the confusion between the antitrust and the tariff policy elements arose, "Because the dumping debates included references to "bounty dumping" and because the anti-subsidy provision was brought before the Congress for amendment during the same period, the countervailing duty law was seen by many as an antitrust device aimed at price discrimination, despite the fact that considerations of price were and are immaterial to the application of countervailing duties." "Mutiny Against the Bounty" page 23. However, considerations of price were and are material to the law particularly in comparison with the cost of production. For it is the impact of the subsidy on the cost of production that is mainly at issue.

20. "Thus, while the countervailing duty is a protective instrument, it is not a barrier to freer competition in international trade." Bruce E Butler "Countervailing Duties and Export Subsidization: A Re-emerging Issue in International Trade" Virginia Journal of International Law Vol. 9, No. 1, December 1968, page 83.

21. Act of State Doctrine.

22. Adams and Dirlam, "The Antidumping Act -- Tariff or Antitrust Law? 74 Yale Law Journal 1965 707 - 724, page 709.

23. This is the "prophylactic effect", which means that the law affects the behaviour of foreign governments just because it exists.

24. Jacob Viner explains that the 1890 CVD law applied only to refined sugar above Dutch standard 16 in colour. The law called for a countervailing duty of one-tenth of one cent per pound on such sugar which was exported from any country which paid a bounty, directly or indirectly, upon exportation. The 1894 CVD law made this procedure applicable to all subsidized sugar. Dumping: A Problem in International Trade (Chicago: University of Chicago, 1923) page 168.

25. Frederick Davis, "The Regulation and Control of Foreign Trade" Columbia Law Review, Vol. LXVI, 1966, page 1445.

26. *ibid.*, page 1446.

27. Speech by The United States Trade Ambassador Carla Hills before the American Chamber of Commerce and the Royal Institute of International Affairs, "The Uruguay Round and US Trade Policy: A Foundation for the Future" September 14, 1989.

28. During a question and answer session after the speech by The United States Trade Ambassador Carla Hills. *Ibid.* How this shift in policy came to pass will become apparent when the definition of a subsidy is examined later in Chapter Eight.

29. 1913 Act Section IV Par. E.

30. Once the administrative procedure was established in 1921 the duty was applied commensurate with the subsidy. As a result the firm's cost would be raised to the level that it would have been had no subsidy been available. It is assumed that firms pass on these costs to customers. Thus the price will be raised to the level it should have been had no subsidy been available.

31. Italian Royal Decree, T.D. 49,909 75 Treas. Dec. 12 (1939).
32. Jacob Viner, Dumping: A Problem in International Trade page 270.
33. Viner says "...without any emphasis in the various committee reports on the bill while in progress and without any mention in the Congress debates the clause was modified." Ibid., page 269.
34. *ibid.*, page 269.
35. *ibid.*, page 269. Section 303, Trade Act of September 21, 1922. Trade Act of 1922 September 21 Section 303. Section 303 of the 1930 Trade Act
36. Tariff Act 1930, Section 303, 19 USC Sect. 1303 (1965).
37. Bruce E Butler, "Countervailing Duties and Export Subsidization: A Re-Emerging Issue in International Trade" Virginia Journal of International Law, Vol. 9, No. 1, December 1968, page 131.
38. Which occurred for the reasons given in Chapter Two page 24, note 14 by Robert Baldwin and Chapter Three, pages 72-73 *infra*.
39. Boggs Report 95, US Department of State, General Agreement on Tariffs and Trade, Present Rules and Proposed Revisions 76 (1955). This quotation is cited by Peter Ehrenhaft, "Protection Against International Price Discrimination", page 55.
40. Butler, "Countervailing Duties and Export Subsidization" page 97.
41. "Countervailing duty actions provide an administrative and judicial mechanism to attack the domestic economic policies of foreign governments without the interventions on foreign policy grounds of the President or any other administrative body." Donald E. deKieffer, "When, Why, and How to Bring a Countervailing Duty Proceeding: A Complainant's Perspective" North Carolina Journal of International Law and Commercial Regulation Vol. 6, No. 3, 1981, page 364.
42. Daniel K Tarullo, "Beyond Normalcy in the Regulation of International Trade", Harvard Law Review Vol. 100, No. 3, January 1987, page 547.
43. Charles J Goetz, Lloyd Granet and Warren F Schwartz, "The Meaning of Subsidy and Injury in the Countervailing Duty Law" International Review of Law and Economics Vol. 6, No. 1, 1986. They rightly mention that the law ignores the possibility "that a firm which benefits from one provision may be burdened by many others." Page 18.
44. David Ricardo, On the Principles of Political Economy and Taxation (1821) reprinted in P Saffra ed., Vol. 1 (1970).
45. It is now better described, but still not fully, by the Hecksher-Ohlin-Samuelson economic model. See Jagdish Bhagwati, International Trade (Harmondsworth: Penguin, 1969) pages 9-12.
46. Since the world is not in a condition of perfect competition and Pareto optimality when most CVD petitions are filed, this raises a question. Is the CVD law used to sustain existing distortions in markets?

47. Ribert Gilpin, The Political Economy of International Relations (Princeton: Princeton University Press, 1987) page 211.

48. According to this interpretation the United States is to be commended not only for using the law to "correct" distortions arising from subsidies. In addition the United States is doing foreign governments a favour by saving them the expense of subsidies (where an expense would be incurred). Ultimately, then, the United States uses the law to compel foreign governments to do what is truly in their own best interest, to seek free market solutions, to allow the freest play of market forces in their domestic economy.

49. Joan Robinson, The Economics of Imperfect Competition (London: Macmillan, 1933, reprint 1965).

50. Butler, "Countervailing Duties and Export Subsidization" page 83

51. John H Jackson, The World Trading System: Law and Policy of International Economic Relations (Cambridge, Mass.: MIT Press, 1989) page 250.

52. Daniel Tarullo, "Beyond Normalcy" page 558.

53. FA von Hayek, The Road to Serfdom (London: Routledge and Kegan Paul Ltd., 1944, reissued 1971).

54. *ibid.*, page 29.

55. *ibid.*, page 558.

56. *ibid.*

57. Adam Smith, An Inquiry Into the Nature and Causes of the Wealth of Nations, RH Campbell and AS Skinner (Oxford: Clarendon Press, 1976) Vol. 2, page 723.

58. Daniel Tarullo, "Beyond Normalcy" page 558.

59. Eric Roll, A History of Economic Thought (London: Faber and Faber, 1938, fourth edition 1973, reprinted 1983) page 534.

60. *ibid.*, page 566.

61. *ibid.*, page 477.

62. *ibid.*, page 540.

63. HG Johnson, "Optimal Trade Interventions in the Presence of Domestic Distortions" International Trade: Selected Readings Jagdish Bhagwati ed., (London: Penguin Books, 1969) page 192.

64. Harald Malmgren, International Order for Public Subsidies, Thames Essay, Trade Policy Research Centre, London, 1977, page 36.

65. This concept of injury is used mainly by economists. Traditionally there was no requirement under the statute that injury to the domestic industry be shown. In 1979 an injury requirement was added to the CVD law for certain circumstances.

66. Quoted by Harald Malmgren in International Order for Public Subsidies page 31, Note 3.

67. Daniel Tarullo, "Beyond Normalcy" page 556.

68. FA Hayek, The Road to Serfdom, page 28.

69. Harald Malmgren, International Order for Public Subsidies page 22.

70. Page 41, Note 96 *infra*.

71. "If a production subsidy is granted by a government, the multilateral body which provides surveillance or arbitration or other dispute-settlement functions should not, in most instances, be required to decide whether or not the production subsidy is "justified" from the point of view of the country implementing the subsidy." Harald Malmgren, International Order for Public Subsidies page 42.

72. *ibid*.



## **CHAPTER EIGHT-- COUNTERVAILING DUTY POLICY: A BETTER APPROACH**

The traditional economic arguments against "mercantilism" deprecate the use of state power in economic affairs. But the maintenance of international rules, of international order, requires that states use their power to prevent others from breaking the rules or undermining order. It is wholly legitimate under the post-war international economic order to use the CVD law as a technique of statecraft, as a means of upholding the internationally-agreed upon principle of competition.

The important issue, then, is not the use of power but the use to which power is put. This crosses the political question. What is the United States compelling foreigners to do? Are they being asked to behave in a manner which enhances competition, or one which reduces competition? Is power used in a manner which upholds the internationally-agreed upon aims and methods of foreign policy goals or not?

### **HOW SUBSIDIES ARE DEFINED IN PRACTICE**

There is no explicit definition of a subsidy in the CVD statute. One must look to examples of Congressional and administrative interpretations to establish the applied definition. In 1965, for example, a Joint Economic Committee of Congress concluded that a subsidy was:

"[A]n act by a governmental unit involving either (1) a payment, (2) remission of charges, or (3) supplying commodities or services at less than cost or market price, with the intent of achieving a particular economic objective, most usually the supplying to a general market a product or service which would be supplied in as great quantity only at a higher price in the absence of the payment or remission of charges."<sup>1</sup>

More recently, in 1984, the Commerce Department, stated:

"we believe a subsidy .... is definitionally any action that distorts or subverts the market process and results in a misallocation of resources, encouraging inefficient production and lessening world wealth".<sup>2</sup>

According to these definitions a wide variety of foreign government activities should be actionable under the statute. Governments provide aids to the general domestic market in a multitude of ways. The provision and enforcement of regulatory standards "aids" the general domestic market. When governments seek to fulfil broad macroeconomic goals this "aids" the general market. When governments provide direct "aid" in the form of state financed roads, dock facilities, schools and federally insured loans, when they allow tax breaks or benefits to certain industries, when they guarantee bank deposits, when they provide export insurance or bailout failed companies, to give only a few of many examples, these or the benefits accruing from them are available to the general market.

If a subsidy is defined by the fact that it causes the "misallocation" of resources, then who defines what constitutes a misallocation? This question is particularly important in the post-war period when the reallocation of resources is a specific government objective that is undertaken precisely because a market-led allocation would have undesirable economic and social effects.

## THE LINE

And so, all of those who have administered the CVD law have had to draw a line between those subsidies that would be actionable under the statute and those that would not. The law's administrators did not have nearly the resources that would be necessary to countervail all of the ways in which foreign governments "aid" their domestic economies. Frankly, Treasury also lacked the conviction that all "subsidies" should be countervailed. As Barcelo notes, the United States cannot simply proscribe all subsidies.

To be actionable, a subsidy must have trade effects on the United States. Until 1974, Treasury had the discretion to reject CVD petitions if the subsidy in question had no trade effects. But, too many foreign government policies and activities were actionable under the statute for this procedure to be practicable. Rather than attempting to enforce

a literal reading of the statute Treasury attempted to limit actionable subsidies, purely for the sake of practicality.

The act of drawing the line between actionable and inactionable subsidies, or redrawing it is, of course, an act of economic statecraft. For to change the line, is to change the rule by which foreign governments must abide to avoid transgressing American CVD law. Such statecraft changes the environment in which others must conduct their affairs.

The line is important for several reasons. First, wherever the line is drawn, as Tarullo rightly points out, the United States introduces an "inchoate notion of the appropriate functions of government."<sup>3</sup> Actionable subsidies are those which go beyond the "appropriate" functions. In other words, some government activities have been accepted as "normal" and others have been labelled "subsidies". The initial distinction was made simply between actionable and inactionable subsidies. This distinction has encouraged a belief that actionable subsidies are "unfair" and inactionable subsidies are "fair".

The very existence of a line confirms the fact that the standard being enforced is not a market standard. A true market standard, which, as we have seen, would be impossible to enforce short of eliminating the existence of government altogether, would require that all subsidies be actionable. By drawing a line the United States creates a standard based on implicit notions of what is a "normal" and "appropriate" role for government to play. However, when the test is not "pure efficiency by market standards but normalcy", Tarullo elegantly concludes,

**"This is ideology, not economics."**<sup>4</sup>

How is this normal standard defined and applied in practice? Why do we ask this? If the "normal" standard is not pro-competitive, or enforced in a way that enhances the play of market forces, then the United States CVD law is clearly at odds with the central internationally agreed-upon aim of the post-war international economic order, which is: competition.



It is difficult to tell how or why Treasury drew this line while it administered the statute from 1930 until 1974. Even though Treasury was responsible for defining what constituted a bounty or a grant, Treasury "refused to disclose or make public the standards or criteria which move its judgement".<sup>5</sup> It would require extensive interviews with Treasury officials from that period to discern exactly how Treasury defined a bounty or a grant whether direct or indirect. Even more research would be necessary to understand the reasons why some subsidies were considered actionable but not others. Since the focus of this study is developments in CVD policy since the late 1960's, and since the law was not widely or actively applied until 1967/1968, only a brief discussion of the early definition of subsidies seems necessary.

Two aspects of Treasury practice are important since these aspects set the tone for subsequent CVD policy. The first is the arbitrariness of the way in which subsidies have been defined. The second is the selectivity of enforcement.

## NORMAL SUBSIDIES

It was essential for Treasury to narrow the focus to some manageable set of trade practices. A pure market standard was not practicable. So, a "normalcy" standard was gradually introduced. Because trade effects have to be present to activate the statute Treasury focused on export subsidies. Direct export subsidies, those involving payments, were clearly actionable. Nobody could claim that direct payments from government to firms, payments which were contingent upon the exportation of merchandise were not bounties or grants. However, as mentioned earlier, few examples like the Italian Royal Decree case ever occurred.

Official export credit, which would seem the most obvious form of aiding exportation, has been regulated by international agreements ever since the Berne Union in 1934. Any breaches of the international credit arrangements, such as providing credit

on more preferential terms than was agreed acceptable, could be countervailed as a direct export subsidy.

It was in the area of indirect export subsidies that judgement was necessary. It is here that we start to see the line begin to follow an arbitrary path. Treasury officials had little to guide them except a precedent set by the judiciary, and a vague notion that if the United States government did not engage in a particular activity with regard to the economy then that activity was probably not "normal" or "appropriate". Treasury did not explicitly define what constituted a bounty or grant, but rather "carved out" its definition(s) on a "case-by-case basis".<sup>6</sup>

It is, perhaps, necessary to emphasize here that the problem with this exercise in line drawing is not that it is done in an piecemeal manner. The common law tradition which entails addressing and resolving problems as they arise is well-suited to this difficult area of policy. The problem with the line drawing exercise is rather that the line has been drawn in such a way as to achieve policy objectives which are inconsistent with the ostensible purpose of CVD law. By tracing the way in which the line between actionable and inactionable subsidies has been drawn over time it is possible to see how this development has come to pass.

The law expressly permits the countervailing indirect export subsidies. But, many "normal" practices in which most governments engage in such as remitting internal taxes upon exportation, can act as indirect spurs to exportation.<sup>7</sup> Treasury tried to limit the range of targetable export subsidies by aiming only at those that deliberately intended to promote exports. For example, it considered the official manipulation of currency for the purpose of promoting exports to constitute a subsidy. During the Interwar period, (between World War One and World War Two) the Germans and the Russians in particular were countervailed for this practice. Or, in another case, the Lithuanian Government was countervailed in 1937 for maintaining a price support system which ensured that no export sale of butter received less than the guaranteed minimum domestic price.<sup>8</sup> Other export subsidies included currency retention plans, tax benefits and the rebate of domestic direct

axes such as income taxes and payroll taxes. But Treasury tried to exclude those practices that accidentally or only incidentally helped to promote exports.

In doing so, Treasury relied on a "precedent" provided by the Judiciary. In two tax cases the Supreme Court established the most explicit definition of a grant or a bounty available when Treasury began to administer the statute in its current form. Treasury relied on the judiciary's interpretation not because it was legally bound by the precedent but because it was the only "precedent" available.

The Supreme Court interpretation of a bounty or a grant (these were the terms used to describe a subsidy before the term subsidy was brought into current use) was established in Downs vs US in 1903 and Nicholas and Co vs US in 1919. In Downs the question at issue was whether a Russian government plan to regulate the domestic price of sugar by refunding internal taxes upon exportation, taxes which would have been required if the sugar had been sold domestically, constituted a bounty or a grant. In Nicholas the question was similar. Did the British government's rebate of a domestic tax on all exports of spirits distilled in Great Britain constitute a bounty or a grant? The rebate was only large enough to offset the excise tax imposed in Great Britain. The Supreme Court reached the same conclusion in both cases. Unfortunately, its conclusion in both cases was equivocal.

In both cases the Court held that an export subsidy existed only if the remission of the internal tax is larger than the original internal tax paid. Simply remitting the exact amount of internal tax upon exportation, the court held, is not a subsidy. However, in Downs, the Court "proceeded beyond a consideration of the Russian program to embrace a broad definition of a bounty, a definition which had been reported by a Committee at the Brussels Convention of European Powers in 1898," according to Craig Brown (who's review of the history of this controversy is excellent).<sup>9</sup> According to that broader definition, any remission of internal taxes constitutes a bounty or grant. The holding, (which provided the narrow definition of a subsidy in Downs) according to Black's Law Dictionary,<sup>10</sup> is: "The legal principle to be drawn from the opinion (decision) of the

court. Opposite of Dictum (the singular of Dictum). It (the holding) may refer to a trial ruling of the court upon evidence or other questions presented at the trial."<sup>11</sup> This is in contrast with the Dicta (which provided the broader definition in Downs) which are: "Opinions of a judge which do not embody the resolution or determination of the specific case before the court. Expressions in the court's opinions which go beyond the facts before the court and, therefore, are individual views of the author of the opinion and not binding in subsequent cases as a legal precedent."<sup>12</sup>

Ever since Downs, the administrative courts have struggled over whether to follow the broad definition of a subsidy as defined by the holding, or the broad definition as defined by the dicta. The pundits have been wrangling about whether any rebate of internal taxes alone ought to be considered a bounty or a grant or a subsidy or whether only the excessive remission of internal taxes is a subsidy.

Treasury chose to follow the Court's holding, which, in this case, constituted the narrow definition. Treasury followed the logic that even though tax remissions do aid exportation such remissions do so only incidentally, whereas, remissions that are larger than the original duty are clearly deliberate attempts to enhance export performance. Both practices aid exportation. But, the Treasury made a decision to draw the line to enclose only the narrower ground. The rebate of direct taxes such as payroll taxes, income taxes, social security taxes were considered actionable. To rebate such taxes is to provide manufacturers with overall lower operating costs than normally would be possible. Article VI of the GATT confirms that rebates of direct taxes are subsidies.

These efforts to draw the line in such a way as to narrow the actionable range of subsidies were essentially arbitrary. This does not mean that these decisions were not well thought out. It simply means that there is only one reason, as the law has been written since 1930, why subsidies should be narrowed to only these phenomena. That reason is simply pragmatism. The line was drawn where it was for the sake of practicality. Again, this is not necessarily bad. But, the practical forces pushing the line ended up steering the law in a direction opposite to the intended purpose of the law.

When we consider the law as a technique of statecraft this element of "practicality" takes on great significance. Though many believe that the law is used to compel foreign governments to act "fairly" and abide by "market standards" and "market principles", it is not. The law does not enforce a market standard. It enforces a normalcy standard. The line is drawn according to what the United States finds "normal" and "abnormal" behaviour for governments -- in other words, according to political and not economic considerations. Normal and appropriate behaviour are defined by the United States' political and ideological vision.<sup>13</sup> The line is further controlled by purely pragmatic considerations. Subsidies are actionable not primarily because they are anticompetitive but because the United States objects to a given practice on primarily political and pragmatic grounds.

One of the most intriguing aspects of CVD law enforcement is that the United States has often attempts to underscore the belligerence of foreign trade practices by highlighting the fact that the United States Government does not engage in the subsidy in question, when in fact, the United States maintains a very similar program, often for similar reasons. For example, Tarullo points out that the United States countervails government grants to firm. But, the United States government has guaranteed private loans to Chrysler Corporation and to bailout the Savings and Loan Banks.<sup>14</sup> Recently the Pentagon invested \$4 million in Gazelle Microcircuit, a semiconductor company that was strapped for cash.<sup>15</sup> The United States Federal Government, as well as most individual states, maintains regional development programs, provides research and development aids to industry (mostly in the form of defense contracts), and aids in the production of harbour facilities. Yet, it has applied the CVD law to foreigners for engaging in all these activities.

Perhaps a short digression is necessary here. This apparent double standard arises at least partly from the fact that the United States' subsidy programs are usually highly camouflaged. Public opinion in the United States is overwhelmingly committed to the ideology of free markets, at least in comparison with public opinion in most other countries. Great pride is taken in domestic industry's lack of reliance on government. For

this reason, subsidy schemes in the United States reflect the need to achieve the desired results through mostly invisible means.

Amitai Etzioni argues that this need reflects an American preoccupation with the "immorality" of government intervention in economic affairs. He provides this telling example. American sugar growers needed subsidies to survive but the growers considered "government handouts and subsidies as a source of shame. Therefore, they fought to obtain a less visible form of government support."<sup>16</sup> The sugar growers and the United States Government devised a plan. The sugar growers put up their sugar as collateral for securing loans from the government. These loans, which would not otherwise have been available, were provided on very soft terms (i.e., the interest rate on the loans was lower than market conditions warranted). In effect, a subsidy was made available, but the subsidy was obscured by the ways in which traditional lending techniques were employed. Overall, the cost of this program, Etzioni finds, was substantially higher than if subsidies were given outright. But the program was consistent with what the sugar growers believed to be the "morally proper take-no-handout position."<sup>17</sup>

This same commitment to "market principles" has overwhelmingly prevented the passage of blatantly protectionist legislation such as the Burke-Hartke Bill and the Gephardt amendment.

In spite of this ideological commitment, practical solutions to pressing trade problems must be found. As a result of the two competing factors -- ideology and pragmatism -- the United States has become adept at creating less visible means of achieving the desired result.<sup>18</sup> One instrument which has been harnessed and even subverted in this cause is the CVD law.

And so we see Grunzel's phenomenon at work. We recall that he found that those most committed to free trade or market ideology are the ones most likely to resolve problems by manipulating these market principles in application, not by modifying the principles as such.<sup>19</sup> Accordingly, as early as 1956, The Randall Commission labelled United States CVD policy "Janus-faced".<sup>20</sup>

It is in the law's application that the CVD law has itself become a means of achieving desired "corrections", that is, of reaching pragmatic solutions to trade problems. Imports can be investigated, taxed and restricted from entering the United States on the grounds that the imports are "unfairly" aided by government assistance. However, allegations are made on the specious grounds we are in the midst of exploring. But our attention to the reality of policy is diverted by the rhetoric which is used to justify actions taken pursuant to the law. Reference to market principles and market standards prevent us from seeing that in practice such actions are in complete opposition to the goals the CVD law ostensibly seeks to serve.

Double standards are nothing new in the realm of international affairs. That they exist here is not especially surprising. It may also be reasonable to argue that it is not that important. It may be worthwhile to enforce "good" policy abroad even if the enforcer is lax in policing itself at home.

This double standard has important implications for our study of statecraft. The fact that the United States itself engaged in many "subsidy" practices by its own definition has from the beginning forced the United States to be selective in its enforcement of CVD policy. It has actively tried to avoid having to face retaliatory countervailing duty proceedings from foreign governments. It has always been important not to establish a precedent which could ricochet the United States' own standards right back at the United States. As a result, the CVD law has been enforced selectively. For example, Uruguay was countervailed in 1963 for maintaining a multiple currency system which, though approved by the International Monetary Fund<sup>21</sup>, was designed to improve export performance.<sup>22</sup> The case ended up in an appeal Court case, Energetic Worsteds.<sup>23</sup> Judge Richardson, in his dissent, noted that the nearly identical multiple exchange rate scheme created by Argentina that "stood squarely behind the initial influx of wool tops (from Argentina) .... has escaped the condemnation". The fact that sixteen other nations also maintained a similar system, but only Uruguay was countervailed demonstrates this element of selectivity.<sup>24</sup> Similarly, the United States has refused to countervail widely

available agricultural subsidies because the United States fears being countervailed for its own policy of providing cheap water to American agriculture.

## THE PLIANT LINE

To return to our exploration of the line between actionable and inactionable subsidies, we will now look at the first major shift in policy. Treasury's early efforts to draw the line in such a way as to limit the target to a narrow range of practices began to change in the 1950's. It was then that pressures for a more expansive reading of the statute began to gain momentum. Some wanted to broaden the range of actionable indirect subsidies and to start countervailing domestic subsidies. It is then that Treasury's line began to buckle.

It appears that Treasury realized that any attempt to redraw the line (which put fiscal export subsidies on the actionable side and other "subsidies" on the non-actionable side) would open up the messy analytical problems. It avoided wading into the murky territory in many cases by simply not acting at all. It issued only one CVD order between July 1954 and April 1966.<sup>25</sup>

Treasury officials took the position that certain "subsidy" questions were primarily political. Such questions, they believed, ought to be resolved through diplomatic channels and not with the CVD law. Some of the first petitions against the European Community's Common Agricultural Policy give a good example of this (even though these petitions occurred later than the 1950's). The National Milk Producers Federation filed petitions from 1968 until 1973 asserting that European Economic Community's Common Agricultural Policy was subsidizing dairy exports into the United States. These petitions were simply ignored.<sup>26</sup> At the time, the Department of Agriculture was actively maintaining import quotas against the relevant dairy products, so political pressure did not arise over the Treasury's neglect on the petitions. But, when the quotas ended in 1973 and 1974 Congress began to pressure Treasury into acting. Congress forced Treasury to take



action within a specified time period and, in the 1974 Trade Act, provided petitioners with the right to subject Treasury to judicial review by the Customs Court for not having acted promptly.

By 1963 a change in policy became apparent in the case Uruguayan Wool Tops.<sup>27</sup> In this case, we can clearly see the line between actionable and inactionable indirect subsidies being redrawn. Treasury countervailed Uruguay for maintaining a multiple exchange rate system which allegedly provided better exchange rates for exported wool tops than was warranted. Even though the exchange rate program was fully sanctioned by the International Monetary Fund, Treasury determined that it constituted a bounty or grant.

The initial positive finding of a subsidy by Treasury was challenged on administrative grounds by an American importer, Energetic Worsteds. Judge Richardson's vitriolic 10 page dissent to the final Customs Court ruling highlights Treasury's changed and broadened definition of a subsidy. Richardson recalls the Spanish Almond case in which Spain was countervailed for paying Spanish exporters a fixed fee for every pound of almonds exported. But, he recalls, Treasury retroactively revoked the duty in November 1948 because the Spanish government scrapped the direct payments in favour of a multiple exchange rate system. That system was very similar to the one allegedly provided by Uruguay in the wool tops case. Under the system the official exchange rate was 10 pesetas to the United States dollar but the exchange rate for almond sales was 19.75 pesetas to the U.S. dollar. In 1948 Treasury had given tacit approval to such a scheme. By 1963 such a scheme was considered an actionable subsidy.

Treasury's narrow interpretation of a tax remission as a subsidy also came under pressure in 1963. Controversy over the Judiciary's equivocal opinion in Downs and Nicholas resurfaced in the Canada Automotive Products<sup>28</sup> case. The initial question in this case was related to the rebate of import duties rather than internal taxes. But, the

principle in question was the same: were the rebates excessive and therefore actionable as a subsidy?

The Canadian Government had instituted a plan under which Canadian automobile manufacturers were rebated the duty the manufacturers had paid on imports of raw and semi-finished automobile parts. The availability of the rebate was conditional upon the exportation of automobiles. In effect the program provided duty free entry for imports of automotive components, conditional upon their subsequent exportation as part of whole automobiles. As a result, the plan encouraged exports by removing a barrier to trade, namely the firm's cost of paying the import duty. The United States argued both that the remission was excessive and that the remission was not directly related to the original levy. A CVD investigation commenced, but little evidence of the alleged practices materialized.

The central point of concern for the Americans was that the program encouraged exports even if there was no excessive rebate. The rebate itself promoted exports. Thus, the broader definition of a subsidy was raised in debate. But, the subsidy essentially amounted to duty free importation. The manufacturers benefitted from the removal of a barrier to trade. They did not benefit from a payment since they received no more than they had initially paid. As the line was drawn there was no way to define this as a subsidy. Bruce Butler has explained in reviewing this case, "the removal of an obstacle to trade did create an advantage over previously existing situation." But, he went on,

"to characterize this removal ... as a subsidy would be intolerable since any trade concession could then be classified as a subsidy. The expansive reading of the CVD statute to include any such advantage or concession must be rejected as unworkable, because this would engender chaos in international trade as a result of the retaliation which would undoubtedly occur."<sup>29</sup>

Ultimately the pressures of the investigation helped to force the Canadian government into the United States-Canada Automotive Products Agreement of 1965. Under its terms Canada agreed to broaden its duty free policy to more automotive products and automobiles. In return the United States abandoned the investigation. In this way the United States ensured that there were fewer duties to rebate and therefore fewer

opportunities to grant excessive rebates. The importance of this case was that it directed attention to the whole question of rebates and remissions which could encourage exportation even if they were not excessive.

These pressures for a broadened definition of a subsidy influenced the 1967 case Italian Transmission Towers.<sup>30</sup> Article VI of the GATT specifies that the rebate of direct taxes such as income taxes, payroll, social security taxes etc., constitute a subsidy. Until this case, Treasury had not countervailed against rebates of direct taxes. In this case, however, Brown explains, Treasury countervailed the Italian government for the full amount of its rebate on indirect taxes paid to the exporters of transmission towers and not just for an excessive rebate. Originally the taxes had been levied as direct taxes. The taxes included: customs duties/import charges, registration duties, stamp taxes, stamp taxes on transportation documents, insurance taxes, mortgage taxes, advertising and publicity taxes, government licenses and authorizations, taxes on the registration of motor vehicles and surtaxes on all of the above.<sup>31</sup> But, the Italian Government had evidently recast these taxes as indirect taxes by the time of the United states' CVD investigation. Brown explains that Treasury was "motivated by the fact that the technically indirect taxes resembled direct ones."<sup>32</sup>

"By countervailing against the full amount of the remission," Guido and Morrone confirm, "the Treasury Department had for the first time abandoned its policy of focusing solely upon excessive indirect tax rebates."<sup>33</sup> Treasury made a positive finding.

In an appeal the next Federal Court, in American Express vs the United States,<sup>34</sup> it was established that Treasury treated the "taxes" in the Transmission Towers case according to their underlying nature (as direct taxes on general overhead) not the illusory form given them by the Italian government (indirect taxes on specific products)", therefore, Treasury could "justify the imposition of a countervailing duty to offset Italy's remission of the taxes upon exportation".<sup>35</sup> In other words, in the Italian Transmission Towers case, Treasury countervailed against the full amount of indirect tax rebates, thus

adopting the broader interpretation of a subsidy. It was easier for Treasury to do this since the taxes were treated as being direct taxes in effect.

By 1970 the pressures for broader definition of a subsidy -- that any rebate of indirect export taxes was a subsidy -- began to win over. That year Zenith, an American electronics company, filed a CVD petition against the Japanese government.<sup>36</sup> Zenith claimed that the Japanese Commodity Tax Law provided a subsidy within the meaning of the countervailing duty statute. At issue was essentially the same question as was posed in the Canada Auto case; was the rebate of an internal tax, even if not excessive, a subsidy? After a six year investigation Treasury found that no subsidy existed. The length of time it took to reach a conclusion is probably indicative of Treasury's reluctance to officially redraw the line. Zenith appealed to the Customs Court which reversed Treasury's finding.

John Barcelo recalls that the Custom's Court finding "stunned the rest of the world,"<sup>37</sup>. Its decision was stunning, "since virtually all countries rebate internal production taxes".<sup>38</sup> Treasury then appealed to the Customs Court of Patent Appeals (CCPA), which had newly acquired the authority to hear such appeals. The CCPA backed Treasury's initial finding of no subsidy.

Not surprisingly, given the potential ramifications of such a decision -- which would be that all governments would have to abandon the longstanding policy of remitting indirect domestic taxes, a policy which had been designed to prevent subjecting commerce to double taxation, in order to avoid transgressing the American CVD law -- there was an appeal to the Supreme Court. Justice Marshall delivered the opinion in Zenith Radio Corp v US.<sup>39</sup> He confirmed that Treasury's narrow interpretation of a subsidy was appropriate. Although the Downs opinion was "admittedly opaque", Justice Marshall stressed:

"Regardless of whether this legislative history absolutely compelled the Secretary to interpret 'bounty or grant' so as not to encompass any nonexcessive remission of an indirect tax, there can be no doubt that such a construction was reasonable in light of the statutory purpose."

This case received wide publicity. The two positive determinations by the Customs Court and the Customs Court of Patent Appeals fuelled the hopes of those who wanted to

"get tough" on foreign subsidy programs. But the Supreme Court decision appears to have settled this particular subsidy issue. Ever since then, efforts to broaden the range of actionable subsidies have been aimed at other kinds of subsidies.

There are too many subsidy practices in existence to permit a comprehensive classification and analysis and discussion. Instead of describing all of the subsidies the United States has countervailed, it will be more productive to concentrate on two aspects of American CVD policy. The first is the way in which the United States has drawn a line between actionable and inactionable subsidies. The second is how the United States has broadened the term subsidy.

The central logic behind the statute is that the United States has a right to challenge or correct foreign subsidy practices that have "trade effects". Given the ease with which a causal link between an unfair trade practice and trade effects can be established, this logic provides the rationale for continually increasing the kinds of practices that can be labelled actionable subsidies. The next step from indirect export subsidies is to tackle domestic ones.

## **DOMESTIC SUBSIDIES**

Intent is notoriously difficult to prove. The CVD law does not require its administrators to judge the intent behind foreign governments' policies. But the way Treasury had drawn the line, the alleged intent of the foreign government had, in practice, become an important relevant matter. Treasury countervailed those indirect export subsidies that reflected the intent to promote exportation. Treasury did not, or tried not to, countervail those that only accidentally or incidentally promoted exportation. But its heavy reliance on the concept of trade effects encouraged potential petitioners to argue that certain practices which may not have intended to create such trade effects were, in fact, giving rise to them. Petitioners began to countervail foreign governments' domestic subsidies by the 1970's on the grounds that domestic subsidies create trade effects.

Petitioners turned to the 1922 domestic subsidies language. But petitions invoking this language forced the law's administrators to face the sticky analytical problems.

The first important domestic subsidy case occurred in 1972. The Greek government had paid a subsidy to domestic producers of tomato paste to promote its production.<sup>40</sup> The subsidy was not intended to aid exportation but, as it happened, much of the tomato paste produced under the benefit of a subsidy was exported to the United States. Therefore, the United States construed the subsidy to be an indirect export subsidy. But to make all domestic subsidies actionable under the CVD law (just because some portion of the subsidized product is exported) is to give the United States a direct veto over the domestic policies, the sovereign acts of foreign governments.

The Greek Tomato Paste case raised an important question. How much of the subsidized product had to be exported for the subsidy to be considered to have trade effects and therefore to become actionable under the CVD law?

The Michelin Case,<sup>41</sup> raised the same question. In this case the national, regional and local Canadian Governments cooperated to encourage the Michelin Tire company to move to a plant site in the largely underdeveloped part of Canada, Nova Scotia. This effort was part of a national commitment to encouraging regional development. Michelin was given loans (which were guaranteed by the national, regional, and local government agencies), a plant site by the local community and other real incentives to move there.

The plan did not aim to aid exportation. Its primary purpose was to achieve a domestic political objective -- the enrichment of a depressed region. As it happened, 80% of the manufactures produced in this factory were exported to the United States. The United States countervailed on the grounds that the subsidy was effectively an export subsidy. Again, the question in the Tomato Paste case appeared. How much of the production needed to be exported for the domestic subsidy to be considered an export subsidy by the United States? The difficulty of this point can be appreciated when looking at the way in which William Walker grappled with it in his focused study of the problem.<sup>42</sup> He concluded that any time the subsidized merchandise is destined

"primarily" for export and is subsidized, it is countervailable.<sup>43</sup> But he leaves the crucial question unanswered. How much is "primarily"? Is 2% sufficient? Is 80% sufficient?

The Michelin Company challenged the positive determination of a subsidy made by the United States in X Radial Steel Belted Tires from Canada<sup>44</sup>. That Court did not use the trade effects rationale upon which the administrators had relied. Rather, the Court judged that the central question was the "reasonableness of the benefit conferred". Reasonableness was determined by reference to whether other nations engaged in such programs.<sup>45</sup> It is unclear to this author how the Court concluded that the Canadian program was not "reasonable". Guido and Morrone clearly explain:

"The Canadian practices countervailed against in Michelin are embarrassingly similar to US programs designed to achieve similar goals. Only by reading the terms of Section 303 of the Tariff Act of 1930 without reference to 70 years of administrative precedent and by relying on the dicta of two early 20th-Century Supreme Court tax rebate cases can legal basis for, the Michelin decision be fathomed."<sup>46</sup>

This case, then, is a perfect example of the United States using the CVD law to challenge foreign governments' political goals. In spite of the fact that the United States, among other nations, maintained a similar program with similar aims and similar methods, the Court rendered a judgement in favour of the Treasury.<sup>47</sup> The message was clear. The Courts would uphold Treasury's definition of a "normal" domestic subsidy. The Canadian regional development program was not a "normal" activity for government.

The same problem appeared again in 1975 in Float Glass.<sup>48</sup> Though the level of exports from the subsidized factories was lower than the level of exports found in previous cases in which positive findings were made, Treasury made a positive determination. Float Glass is important, Gary Hufbauer explains, because in it Treasury established a "rule of reason" for future reference. If the domestic subsidy had a "de minimus" trade effect on United States commerce then it would be actionable under the CVD law. Where de minimus falls on the scale between 100% and .001% of the firm's exports is unclear. But, it is fairly easy to prove that a de minimus trade effect exists. By drawing the line at this place, Treasury opened up the possibility of countervail petitions against many foreign governments' domestic subsidy programs. But Treasury realised that the pressure would

be too great if such a rule was maintained. Challenges to normal, legitimate and appropriate management of the domestic economy by foreign governments would begin to appear. So, Treasury created the specificity test.

## **SPECIFICITY TEST**

Although there is no record, it appears that Treasury began to apply a "specificity test" sometime in the early 1970's. It has been required by the statute since 1979.<sup>49</sup> The specificity test provides a means for separating actionable subsidies from non-actionable ones. According to the terms of the test a domestic subsidy is countervailable only if it is not "generally available" but is made available only to some specific industries or firms in the domestic economy. As the test has evolved, it has come to mean that subsidies which are made available to specific industries or firms are countervailable.

Tarullo explains; the United States seeks the "soft efficiency aims" which are best described by Alfred Kahn in The Economics of Regulation.<sup>50</sup> Kahn demonstrates that the only practical way to address the central problem, where to draw the line, is to look for distortions, "given the existing schemes of private and public law."<sup>51</sup> All states, it is reasoned, build roads and schools. All governments pursue macroeconomic goals. These activities confer benefits on all participants in the domestic economy. They are part of the "given framework". Therefore the United States does not attempt to countervail them. Using this "soft efficiency" reasoning, the United States employs the specificity test to distinguish between actionable and inactionable domestic subsidies. Only those subsidies which confer a benefit on some industries are subject to countervail.<sup>52</sup> The test serves as an "Ockham's razor", as Gary Hufbauer has said.<sup>53</sup>

The specificity test was adopted into the statute and made mandatory in 1979.<sup>54</sup> Perhaps, by now, we should not be surprised to find that the legislative history is "...surprisingly silent on Congressional motives for enacting the specificity test ...".<sup>55</sup> It is likely that the test was borrowed from the test suggested in the Subsidies Code. A



countervailable domestic subsidy under the Code is one that is "granted with the aim of giving an advantage to certain enterprises, ... either regionally or by sector."<sup>56</sup>

As one might expect of such an arbitrary method of dealing with the analytical and administrative problems raised by domestic subsidies, the specificity test has been challenged. The test distinguishes between "fair" and "unfair" subsidies but it does so in a manner which makes little economic sense. Just because a subsidy is generally available does not mean that no benefit has been incurred by the recipients.<sup>57</sup> As such, the test ignores whether competitive advantage has been created by a subsidy.

This was the issue in the 1983 case Cabot Corp vs US.<sup>58</sup> Unfortunately, as with so many trade cases which end up in appeal, the Court's opinion in Cabot was equivocal. The opinion has given rise to several interpretations. The Court clearly rejected the "generally available" test on the grounds that such subsidies may benefit all but they do not benefit all equally. That is, even a generally available subsidy confers a benefit on some more than others. The Court concluded that the statute's administrators should look for a de facto benefit which accrues to a specific industry or group of industries.

The Court created a new set of administrative and analytical problems by raising the point that a subsidy should be countervailable if it has a real effect on competitiveness. How does one determine if a de facto competitive benefit exists? Gary Horlick points out that three interpretations of the problem arose from the Cabot case. "First, if individual recipients of a program could be identified, any benefits they received would be countervailable."<sup>59</sup> It is fairly easy to find individual recipients of any program, so this interpretation was the broadest. "Second, even if the individual recipients could be identified, the Commerce Department would have to analyze the operation of the program to determine whether certain recipients benefitted more than others."<sup>60</sup> "Finally, Commerce merely had to confirm that, in addition to being generally available, the program was also widely used."<sup>61</sup>

Being subject to such divergent interpretations, the specificity test soon came under intense speculation and pressure. The general consensus endorsed the view that the

main point in domestic subsidy cases should not be a subsidy's availability, which is what the "generally available" test confirms, but rather the effect of the subsidy on competitiveness.

In 1987 the Court appears to have sanctioned the third interpretation of the Cabot decision in PPG Industries Inc. v. United States.<sup>62</sup> In PPG the Court judged that the appropriate test was a de facto specificity test, although the particulars of administering such a test were not addressed. However, the Court rejected the concept of a "competitive benefit" test. Under a competitive benefit test, petitioners would claim that a wide variety of foreign governments' domestic economic policies created a competitive benefit. This would give rise to huge administrative and, more importantly, political difficulties. Such a test would clearly be a nightmare to administer. What criteria would be used to identify or measure the existence and degree of a competitive benefit? But, there is another reason -- perhaps it is the major reason -- that the de facto specificity test has been maintained and the competitive benefit test rejected. Redrawing the line by employing the competitive benefit test would mean that many activities engaged in by the United States would blatantly transgress its own standard.

So the specificity test stands, but it is subject to discretion. A subsidy may be generally available but it may be benefitting only a few in practice. Therefore, it constitutes a de facto subsidy which passes the specificity test.

We see in the particulars of the Cabot and PPG cases that judgement and discretion must be used to substantiate the existence of a de facto subsidy. Both cases involved the sale of natural resources to the domestic market. In Cabot the state-owned and state-controlled firm Petroleos Mexicanos, a natural gas producer and processor, provided one of the natural gas spinoff products, carbon black, at prices that were substantially below the going rate in the world export market. It was "generally available" in the broadest meaning. However, there was only one real user of the subsidized product. The Court's decision implied that normally this would be interpreted as the de facto existence of a subsidy. In this particular case the Court found that it was owing to the underdevelopment

of the Mexican economy and the manner in which the government made the substance available that more users did not exist.

In PPG the sales of natural gas at prices below the going rate in world markets was made possible in Mexico by a government plan that restructured the Mexican natural gas industry. Many different industries and firms benefited from these reduced rates. Therefore, no de facto subsidy existed.

In 1988 the statute was amended so that the law requires the administrators to countervail not only de jure subsidies but de facto ones. This is an extremely important change in the statute. For substantiation of the existence of a de facto subsidy is wholly dependent upon the discretion of the investigators. The test requires no mathematical constructs. How would one mathematically determine who all the potential users might be in order to substantiate that fewer than that in fact benefitted? Instead, as Alexander points out, the test requires Commerce to "exercise judgement and balance various factors in analyzing the facts of a particular case in order to determine whether a countervailable benefit has been conferred."<sup>63</sup> In other words, Alexander makes it explicit that "the determination of what constitutes a significant distortion of an economy requires line drawing on a case-by-case basis."<sup>64</sup>

This brings us back to the central point about the CVD law. It allows the United States to judge the "appropriateness" of foreign governments' domestic policies.

We see the United States doing just this in two cases which were brought against the Canadian Government, Certain Softwood Lumber Products from Canada (1983)<sup>65</sup> and Certain Softwood Lumber Products from Canada (1986).<sup>66</sup> In both cases it was alleged that the Canadian Government subsidized lumber sale prices to well below the world price both domestically and internationally. The wood products in the 1983 case were not found to violate the specificity test. They were not sold to any specific firms or industries. The wood was sold to all comers. The United States had no grounds under the specificity test for a case. No subsidy was found.

The Canadian Government was countervailed again, in 1986, on the same allegation. This time the de facto test was applied. The United States argued that in practice the Canadian government had administered the program in a manner that ensured that only some firms and industries benefitted from the subsidized lumber. In short, the Canadian Government's intent was to provide a subsidy to those specific industries. On this basis, the United States made a preliminary determination that the subsidy existed and was countervailable. In response to the American decision to reverse its earlier finding of no subsidy the Canadian government agreed to implement a scheme that taxed the lumber products upon their exportation. In return for this settlement the United States terminated the investigation.

The de facto test, then, rests on the discretion and judgement of the administrators and investigators. Judgements are made about a foreign government's intent in pursuing domestic subsidy policies. In short, the United States officials have the authority and discretion to judge whether a foreign government's domestic policy is reasonable. It allows the United States to penalize a foreign government for its intent in pursuing domestic economic and political objectives.

The specificity test and the de facto specificity test provide a seemingly hard rule for isolating actionable domestic subsidies. In practice, however, these tests do not provide a hard rule. They are dependent upon the judgement of the investigators and those administering the law. And, they are in practice, highly flexible. These tests render the Countervailing Duty law an instrument with which the United States exercises broad power to judge and influence the foreign governments' domestic policy choices.

## **UPSTREAM SUBSIDIES**

There has been one other effort to broaden the range of actionable subsidies. That has been to countervail so-called upstream subsidies. It is argued that a producer may benefit from using subsidized inputs. Even if the manufacturing or exporting process is

not subsidized, it should still be possible to countervail against imports if any of the inputs used in making the imports have been subsidized. Cheaper inputs allow manufacturers and/or exporters to artificially reduce their costs. Therefore, upstream subsidies should be countervailed.

The term upstream subsidy refers to a subsidy which has been given to a product before it is used by a manufacturer or exporter. For example, if a maker of wood furniture uses subsidized wood in its products then it benefits from an upstream subsidy and may be countervailed. According to the 1988 Trade and Competitiveness Act a subsidy is bestowed when the;

"input price is lower than the price that the manufacturer or producers of merchandise which is the subject of a CVD proceeding would otherwise pay for the product in obtaining it from another seller in an arms-length transaction."<sup>67</sup>

What is the use of countervailing imports which have benefitted from upstream subsidies? Why not just countervail the upstream subsidy directly? It is because most upstream subsidies would be generally available. Many buyers in many different industries would purchase and benefit from the subsidized input. Therefore, the upstream subsidy would not be eligible for countervail. Generally available subsidies, we recall, are not countervailable under the terms of the specificity test.

One way of getting around the restriction imposed by the specificity test is to countervail the users of upstream subsidies. Their products might very well pass the specificity test. A separate three part test was introduced by the Commerce Department in the early 1980's which was codified in the 1984 Trade and Tariff Act. Three questions were asked to determine if an upstream subsidy was countervailable. First, was the upstream input subsidized? Second, was the subsidy available to all or only to a specific industry? Third, did the subsidy confer a benefit on the downstream producer? If any of the questions were answered no, then a negative determination was made. But in recent years the practice has been the opposite. If any of the questions can be answered yes, then the subsidy is countervailable.

One can imagine the difficulty of investigating all the potential input subsidies on all exports. The potential targets, Peter Koenig points out, "might include a cast of thousands".<sup>68</sup>

Not surprisingly, it has been found administratively convenient to rely on a de minimus doctrine. Koenig explains that this means that, "only those inputs whose cost is significant relative to the total cost of the exported good"<sup>69</sup> will be actionable. Of course, as we have seen before with the use of de minimus doctrine, there has been little effort to define the term "significant".

Subsidies, then, are defined less by genuine economic criteria than by non-interventionist ideology heavily tempered by pragmatism. If the law was used to compel foreign governments to abide by a pure market standard then it would require the virtual elimination of government altogether. Once government even begins to create and protect contract and property rights in a market economy it aids domestic production and manufacturing. So, instead of a market standard the United States defines the term subsidy by drawing a distinction between the normal and appropriate activities in which governments should engage, and abnormal interventionist ones. In this way the term subsidy is defined by non-interventionist ideology. The United States permits, or does not penalize, all of the ways in which foreign governments confer benefits upon its domestic industries' production, manufacture and export; only some government activities transgress the law.

The United States draws a line between actionable and inactionable subsidies. Which subsidies are which have been established by various tests which serve to separate one from the other pragmatically. Initially the test was simply whether the goods benefiting from the foreign government's subsidy were exported to the United States. But, a mere de minimus amount of exports was sufficient to trip the line. As a result this test placed too many subsidies on the actionable side. So the test was abandoned. In its place the specificity test draws the line based on whether the subsidy is available to specific industries. If so, the subsidy is actionable. The specificity test is not based on economic

logic. It ignores whether the subsidy actually confers competitive benefits. But, in practice this test has tended to draw the line a little too conservatively. Some subsidies which in practice confer a benefit have been left on the inactionable side of the line because the subsidies are widely available. For this reason the statute has been modified to allow the test to be applied in a manner that allows the subsidy's de facto specificity to be established. Such a test requires judgement to determine who effectively benefits from the subsidy.

Ultimately, then, even with the assistance of these pragmatic tests, the determination of what constitutes an abnormal and actionable practice is subject to discretion. In other words, a subsidy is not a fixed term under the law. Rather that term is applied to those foreign government practices or policies that are determined to confer benefits and to which the United States objects. Objections are based not on pure economic market standards. Normalcy is not even defined by the United States' own practices and policies. In the United States subsidies are defined by broad ideology but constrained by practicality.

## **WHAT IS THE VALUE OF THE SUBSIDY?**

Once it is established that an actionable subsidy exists -- however a subsidy is defined -- it is then necessary to determine its size or value. The duty is supposed to be commensurate with the magnitude of the subsidy -- at least in theory. Remember, in principle, it is not the act of subsidizing nor the government's intent that the United States countervails; it is the trade effects of subsidized imports on the United States market that are countervailed. The United States can countervail a subsidy only insofar as it affects imports into the United States or third markets where the subsidized goods have trade effects on American exports. Therefore, the law does not require that the administrators determine the size of the whole subsidy. Rather, they must determine that portion of the subsidy which reduces the cost of producing those specific exports which enter the United

States or otherwise have trade effects on American commerce. This is called the net subsidy. As Goetz, Granet and Schwartz have put it, the

"fundamental issue [is] of how a benefit paid to induce the introduction of some input, like a plant, is attributed to a particular unit of output exported to the USA."<sup>70</sup>

For example, if a government provides an actionable subsidy of \$1,000,000 either in cash or in value, to a firm or an industry, it is within its rights as a sovereign power to do so (unless the action contravenes international agreements). But, if any of the produce from the beneficiary firm or industry is exported to the United States, or exported to some third market where it competes with comparable American-made products, then the subsidy will be subject to the American CVD statute. An investigation will ensue if a petition is filed against the subsidy. But only the portion of the \$1,000,000 that affected those specific exports is actionable.

This procedure raises several questions that are crucial to our understanding of the CVD law as a technique of economic statecraft. First, how is the size of a subsidy determined? Second, how is the subsidy attributed to the exports? Third, how is the size of the countervailing duty determined?

These questions are crucial because the size or value of the alleged subsidy determines the amount of the countervailing duty. The duty is in effect a penalty for behaving "unfairly" in international trade. The size of the duty determines the size of the penalty. The severity of the penalty determines how forcefully the foreign government is compelled to do whatever it is that the United States wants the foreign government to do. Also, the larger the subsidy is (as determined by the United States) the greater the implication of "unfairness". These questions are important because in answering them it will become clear whether in practice there is any genuine relationship between the amount of subsidy received and the amount of duty paid.

The single link between the subsidy received and the countervail is the calculation methodology. It determines whether that link is genuine or fabricated. For these reasons the calculation methodology needs to be explored with some care. It is worth noting that,



**"In CVD cases, the possibility that Commerce will completely change its method between its preliminary and final determination without giving all the parties notice, arises more frequently than in antidumping cases."<sup>71</sup>**

## **THE CALCULATION METHODOLOGY: A QUESTION OF COSTS**

**Government subsidies to industry are considered "unfair" under the current CVD law (since the 1960's) primarily because they allow recipient firms to lower their costs. It is assumed that there is a "normal" cost of producing the exports in question which would be apparent under market conditions and determined by "market forces". Then there are "subsidized" costs. When American officials have determined that a subsidy does indeed exist the next step is to establish the impact of the subsidy on the recipient firms' costs of producing or supplying the merchandise exported to the United States. They compare the "normal" cost to the "subsidized" cost. The difference between these two is the subsidy. The subsidy must then be apportioned to the exports in question. This is the net subsidy. The countervailing duty should equal the net subsidy.**

**A firm may or may not alter its prices to reflect reduced costs. It may maintain a price in spite of the subsidy, thus enlarging its operating and or profit margin. Unlike in dumping cases, price competition is not, therefore, the main issue under the CVD law. The subsidy does not need to bring the import price down to or below the level of comparable American-made goods to be actionable. For example, widgets from country X cost \$10 per unit to make and the firm sells them at \$20 per unit. But with the benefit of a subsidy the cost of making the widget is only \$8 per unit. The fact that the price of the widgets exported to the United States is \$20, whereas the highest price of a comparable American made widget is only \$10, is not germane to the investigation. Although, in practice, the administering officials have sometimes declined to investigate or countervail those subsidized imports whose price has been substantially above the American market price.**

Costs, as we have seen in the last chapter, are elusive creatures. But, before we begin to explore whether it is even possible to discern the relevant costs in CVD cases we should note that the CVD procedure assumes not only that there is a relationship between subsidies and costs but that the relationship is proportionate. These assumptions are tenuous at best and probably often false.

A few sharp observers, such as Goetz, Granet and Schwartz, have pointed out that a subsidy usually causes a firm to increase its costs. For example, a firm may build a plant that it would not have built without the subsidy. Obviously a new plant or increased capacity will increase the firms' costs.<sup>72</sup> It will probably also change the "normal" variable costs of production.

Further they argue that the size of the subsidy and the magnitude of the impact on costs may not have a proportionate relationship;

**"...the net effect on cost will only be some highly variable fraction of the apparent subvention paid out by the government. As a result there exists no simple relationship between the magnitude of the subsidy and the reduction in variable costs, the crucial variable in determining the competitive effect of the subsidization."**<sup>73</sup>

If the American authorities do not take the real impact of the subsidy on costs into consideration, but rely instead on the assumption that subsidies always reduce costs (an "at least partially mythical" assumption) then, these authors conclude, "this approach tends to provide substantially greater protection than is actually justified..."<sup>74</sup> In effect, the assumption allows the United States greater leverage to penalize the foreign actor.

Even if Commerce officials knew the full amount of the subsidy because a specific expenditure for it exists in the foreign government's budget, still Commerce officials must apportion the amount of the subsidy among many recipient firms. But this task is done without making any allowance for the fact that a subsidy of the same value probably will not have a uniform impact on the cost structure of different firms. Costs are, of course, determined in no small part by economies of scale and size. The impact on a small firm or a firm with relatively high variable costs is bound to be different from the impact of the same subsidy on the costs of a very large highly diversified firm or one with relatively

low variable costs.

Further, a subsidy will undoubtedly have a very different impact on the cost structure among various factories within a single firm.<sup>75</sup> If the law is used to countervail all the allegedly subsidized imports from one country at the same rate the duty will obviously not correspond to the subsidy's genuine impact on costs.

Thus, countervailing duties paid by each firm cannot and do not exactly equal the value of the subsidy the firm received. Rather, the amount of the duty is based on the conjectural impact on costs, by the average, not the genuine, value of the alleged subsidy.

## **"NORMAL" COSTS**

The law rests on the assumption that it is possible to discern the "normal" cost of producing that portion of a firm's produce that is exported to the United States. The firm's overall cost of production is not at issue.

Is there a "normal" cost of producing something? When the amount of the subsidy is not easily apparent Commerce officials sometimes construct a foreign firm's costs so that a comparison can be made between the "normal" cost and the "subsidized" cost. In this way it is possible to isolate the value of the subsidy. Commerce officials use the same formula here as is used in antidumping cases. Costs include the cost of materials and fabrication, plus 10% for general expenses, plus 8% of the sum of these costs and expenses for profit, plus the packaging and shipping costs. This formula describes the "normal" cost of production as defined by United States. However, by using such a fixed formula the officials then are not trying to determine the firms' actual costs but rather to determine what their costs ought to be. The CVD law, then, is used to send a message to foreign firms: it is used to tell foreign firms what their costs should be.

The fact that market conditions or efficient production may allow a reduction in costs below the level specified by the United States' cost formula is completely ignored.

Market forces and their impact on foreigners' costs -- the very forces that the law ostensibly seeks to enhance -- are denied significance under the CVD procedure. Foreign firms' are penalized if they respond to such market forces by reducing their prices below the level of costs specified by this formula.

The CVD procedure then makes the implicit assumption that it is possible to determine both "normal" costs and "subsidized" costs. Costs, however, as we have seen in the last chapter, are difficult if not impossible to discern. Rather costs are isolated through a variety of arbitrary (and often outmoded) accounting procedures.

We recall Tarullo's fundamental point that there is no coherent concept of costs that is independent from the role government plays in supporting the market structure. From police protection to education policy to regional development policy the state pursues a variety of actions which affect the costs of doing business. The role government plays varies from state to state. Therefore, "normal" costs must vary from state to state. So, there is no universally "normal" market-determined cost of production. "Normal" costs of production must vary from state to state.

In addition, costs are bound to vary from state to state depending simply on the differing conditions of supply and demand. To require that all firms from several countries be held to the same cost criteria is to deny that competitive conditions vary, that market elasticities vary, and that such variance is precisely what gives rise to comparative advantage and international trade.

Even if US authorities accepted that there is no universal "normal" cost of production, and even if it were possible to gather enough information to calibrate the US cost formula to allow for differing government and market structures in different states, administering officials would still not be able to determine the costs relevant to CVD investigations in an unarbitrary manner. Because, as explained in reference to the sales below cost standard in AD investigations, there is no unarbitrary way of determining the cost of producing a single unit in a multiproduct firm.

It may be possible to determine direct costs. Although, in determining the cost of the leather which is used to make a single pair of shoes, it would be necessary to know the exact price which was paid for the specific batch of leather used. The price of the leather may change over time due to genuine market fluctuations or the negotiation of discounts on bulk purchases. Investigating officials would generally not have access to the information that would be required to discover the actual direct cost nor the time to process it within the investigation deadline. As a result, even direct costs are cast in a somewhat arbitrary manner under a CVD investigation.

Indirect costs, which, according to Peter Drucker, usually account for the majority of incurred costs in modern manufacturing operations, are much more elusive. Overhead costs account for all those costs that must be paid regardless of the level of production. These costs can vary according to many factors including the pace of product innovation and the learning curve, as well as the volume and character of production.

The concept of "normal" costs is empty, devoid of meaning. Applying it in practice is, as Jacob Viner made clear, an absurdity.<sup>76</sup>

## **"SUBSIDIZED" COSTS**

The "normal", supposedly "market-determined", cost of production must then be compared with the "subsidized" cost. In some cases the full amount of the subsidy is known. In export subsidy cases the size of the subsidy is sometimes apparent either because the subsidy is paid on a per unit basis or because the full amount of the subsidy is evident in foreign law or policy.

In the first instance, an export subsidy paid on a per unit basis, it is assumed that there is no need to determine the "normal cost" because the "normal cost" is simply that which would have been necessary had the subsidy not been available. In such a case determination of the duty is, according to most observers, a "routine matter". As John Sciortino put it:

"Because the subsidy is already allocated on a per product basis, Commerce need only find an appropriate rate of exchange to calculate the dollar value of the subsidy by the amount of the product exported to the United States."<sup>77</sup>

This procedure raises problems. First, which exchange rate is used when rates are floating? Obviously the choice of exchange rate becomes the crucial factor in determining the magnitude of the duty. The same constraints, or lack of them, placed on the administrators in AD cases hold true in CVD cases. That is, the administrators can allow exchange rate fluctuations alone to create the appearance of a subsidy when none really exists. Or, such fluctuations can be allowed to magnify the size of a genuine subsidy.

One more step is required before the net subsidy figure can be reached. Traditionally, as in dumping cases, the subsidy figure was adjusted to allow for circumstances of the sale. Expenditures, such as application fees or export taxes and duties which were designed to offset the subsidy received, could be subtracted from the figure. Or the United States would adjust the figure downward to account for a loss in the value of the subsidy arising from its late receipt.<sup>78</sup> But it is not necessary to delve into the details of circumstances of sale adjustments because the 1979 Trade Act eliminates them from the procedure. Few or no circumstances of sale adjustments are now made.<sup>79</sup>

What about the majority of CVD cases in which the subsidy is not available on a per unit basis? In the case of indirect export subsidies and domestic subsidies Commerce may be able to discern from foreign law or policy the full amount of the government expenditure. For many years Treasury and Commerce refused to countervail against a subsidy unless there was an identifiable expenditure for it. More recently, however, the administering agencies have been under pressure to interpret foreign law and policy in an attempt to determine the de facto existence and de facto value of the subsidy. Clearly interpretation of foreign law and policy requires judgement and discretion. This implies that the subsidy's value, particularly since it is a de facto subsidy, will be more attributable to discretion than genuine economic factors.

Either way, having determined the size of the subsidy, Commerce must then apportion the full subsidy among the recipient firms. In addition to apportioning the

subsidy among the recipient firms, Commerce ought also, in theory, to determine the impact of the subsidy on the cost of producing those exports that went to the United States. The impact of the subsidy on the firms overall costs is irrelevant.

It is virtually impossible, theoretically or practically, to isolate the effect of a subsidy on the cost of producing a few products in a multiproduct firm. Further, it is even less possible to isolate the cost of producing those few products which are actually exported to the United States. Neither the firm itself nor modern accounting procedures can provide an unarbitrary way of determining the impact of the subsidy on overall production costs.

"Subsidized" costs are just as elusive and meaningless as "normal" ones. Whether due to analytical difficulty, lack of all the relevant information, or neglect in accounting for the fact that there is and can be no universal normal or subsidized cost, the final "normal" and/or "subsidized" costs are bound to have only the most tenuous link to reality and will inaccurately represent it. Any figures created on the basis of costs or cost information are the product of judgement, discretion and are bound to suffer from faulty and/or false input. As a result, such figures are almost entirely the product of invention.

## **ALLOCATING DUTIES**

Usually a subsidy is too large to be countervailed all at once. Take the case of a large one-time subsidy. If the firms that received the subsidy were required to pay the entire countervailing duty either at once, or in the course of a single financial year, it might well drive them out of business altogether. For this reason the United States allocates the duty over a period of time. The allocation procedure raises and intermingles with questions about the value of a subsidy. The allocation gives the firm time to pay the duty. But, is the subsidy worth more or less over time?

Traditionally Treasury allocated the duty over half the useful life of the equipment used to produce the subsidized exports. It was assumed that newer equipment would be

more valuable than older equipment. That is, the subsidy would be worth more to the firm in the early than in the later days. United States officials apportioned the duty through a simple straight line depreciation so that the amount of duty paid would be front-loaded and reduced over time.

As pressures to countervail increased, this methodology became subject to question. The value of the subsidy over time issue appeared in the 1982 Michelin case. Michelin argued that the duty should have been allocated over the full useful life of the equipment that had been purchased with the subsidy. The Court queried whether "any justification exists"<sup>80</sup> for the half-the-useful-life method. This method was rejected by the Court because it was "arbitrary and not in accordance with the law."<sup>81</sup> The Court ruled in Michelin:

"the use of a period of half the accounting life of the capital assets amounts to a procrustean<sup>82</sup> method, unrelated to the facts and unsupported by law or rule."<sup>83</sup>

Congress appears to have agreed that the old methodology was not useful, but, for a different and opposing reason. By 1980 Congress was concerned that "current methods of amortizing subsidy values should more accurately reflect the competitive advantage gained from subsidies..."<sup>84</sup> They turned to the now popular Time Value of Money Theory which posits that money received today is worth more than money received tomorrow. On this assumption it was argued that the value of a subsidy increases over time. Commerce officials began to use Net Present Value methodology (NPV is the accounting term for the time value of money). It was argued as we see in Carbon Steel Products from Belgium,<sup>85</sup> that the new methodology would maintain the desired front-loading effect.

"However, so long as we allocate the subsidy in equal nominal amounts over the entire useful life, it will still be effectively front loaded [sic] in real terms (as long as a positive discount rate is used) since money tomorrow is less valuable than money today."<sup>86</sup>

Once adopted, this new methodology raised new issues in subsidy cases. Now the primary concern in assessing the duty was determining the value of the subsidy both at the time of receipt and in the future. For example, a \$1,000,000 loan or grant from



government was probably worth more than that in real terms. Commerce began to ask how much it would have cost the company to raise the same amount on commercial terms. The fact that the grant was given precisely because no commercial alternative would have been available is ignored. Instead, US officials have often determined that the subsidy was worth the commercial rate. So, if a commercial loan would have required \$300,000 in interest payments then the full value of the subsidy is \$1,300,000. Or, in some cases, they have determined the government's cost of money and held that the subsidy was in fact worth that amount. The government's rate of interest is generally lower than the commercial rate.

The new methodology was first generally employed in 1982, most notably in the one hundred and fifty Carbon Steel<sup>87</sup> CVD petitions. The issue of the actual cost of money arose most vividly in Ceramic Tile from Mexico.<sup>88</sup> It was decided in this case and in three others, Certain Pig Iron from Brazil,<sup>89</sup> Ferroalloys from Spain,<sup>90</sup> and Leather Wearing Apparel from Argentina,<sup>91</sup> to use the commercial cost of obtaining the relevant funds. This sounds simple enough. But is there a standard commercial cost for funds? In connection with this methodology Hufbauer and Erb ask: why do corporate credit ratings matter to commercial banks? It is because not everybody is eligible for loans. Even if a loan equivalent to the subsidy was possible it would be offered at a different rate of interest and/or on different terms from one customer to the next, depending upon differing risk factors and credit ratings. So, while the cost of money is "administratively convenient" as Hufbauer and Erb point out, in reality there is no uniform commercial rate. The link between subsidy and cost of commercial funds to a firm is "tenuous"<sup>92</sup> for these reasons.

The decision to use the commercial cost of money or the government's cost of money is clearly an important one. And it is one which is not constrained by the statute or administrative regulation. It is interesting to note that the United States makes a great effort to determine the real nominal value of a subsidy. US officials look at commercial borrowing rates and the cost to government of lending or giving the money. Yet, those

officials ignore the fact that subsidies in "real" terms are worth different amounts to different firms depending upon how the subsidy was employed.

In addition, there is no effort made to determine whether the recipient used the subsidy wisely or effectively and therefore got the full value out of it. In other words, as John Sciortino points out, the genuine nominal value of the subsidy depends upon how it was used.<sup>93</sup> One firm may choose well and get the full value out of the subsidy in their investment. Another firm might make a bad choice and only get half the value of the subsidy in real terms. If the United States wants to isolate the genuine nominal value of the subsidy, then the US has to take account of the fact that value depends on the investment decisions made by the recipient firms. But, the United States CVD law, regulations and officials do not acknowledge this in such calculations.

Having arrived at a figure for the nominal value of the subsidy how, then, does Commerce allocate that value? After determining the nominal value of the grant or loan or subsidy, by using the procedures that have just been outlined, Commerce then allocates the subsidy over the useful life of the assets. It is unclear who decides what constitutes the "useful life". The physical depreciation of assets that had figured so prominently in the old methodology is now completely ignored. The current practice,

"to spread the benefit received over the output for the useful life of the asset, purchased wholly or in part with the proceeds of the subsidy, is employed to arrive at a subsidy per unit of importation into the USA."<sup>94</sup>

Goetz, Granet and Schwartz believe that:

"such an approach, however, is wholly arbitrary if the purpose of the attribution is to capture the effects of the subsidy on competition in the American markets."<sup>95</sup>

They argue,

"To calculate the present value of a physical asset over time without taking into account the parallel depreciation of that asset simply ignores reality."<sup>96</sup>

According to most accounting experts Net Present Value methodology can be useful only if very restrictive conditions are applied.<sup>97</sup> Commerce is very loose with this methodology.

Instead of relying on depreciation to determine the value of money over time, Commerce chooses a discount rate to reflect the projected changed value of money over time. The discount rate (also known as an interest rate) is also chosen arbitrarily. In different cases Commerce has employed different interest rates. These have included the long-term average corporate debt rate, the long-term government debt rate, and a weighted cost of capital devised by Commerce itself. Thus, Goetz, et al., draw attention to the problem:

"Whatever (discount) rate Commerce chooses, it is clear that the use of such a rate ... has no rational connection to the benefit conferred by a subsidy. Use of this rate only makes sense if the facts follow assumptions to be made as to alternative uses of the subsidy or as to whether the investment would be made in the absence of the subsidy. In none of the reported cases has Commerce articulated these assumptions, much less established a rational basis for making them."<sup>98</sup>

There is no requirement that a particular time period be used to calculate the present value. Commerce's method does not determine the benefit of the assets for which a subsidy is used. Rather, it determines the benefit of a subsidy received in the year the grant was made.

"There is no relationship between the life of the assets and this financial subsidy. The use of the useful life of the assets merely engraft onto Commerce's chosen methodology a concept that is required legislatively but has no inherent connection with the theoretical basis of the financial subsidy benefit calculation."<sup>99</sup>

Net Present Value methodology is a technique which enhances the power of the CVD law as an instrument of statecraft. Although it appears to be sound as a mathematical procedure, in practice it allows the introduction of discretion in the production of a figure for a subsidy's nominal value which does not and cannot accurately reflect a subsidy's genuine value. Sciortino reaches this same conclusion.

"As used by Commerce, the present value methodology involves a series of assumptions which operate in a manner apparently designed to maximize to the extent possible, without regard to logic, the subsidy value attributable to foreign governments practices."<sup>100</sup>

## **DE FACTO VERSUS DE JURE**

One important ramification of the present value methodology has been to focus attention on nominal value. As a result, subsidies which were previously avoided by United States officials, namely those for which no expenditure exists, have increasingly been perceived as having nominal value. The 1984 Trade and Tariff Act directs the administering authorities to countervail not only de jure subsidies but also those which exist de facto (that is, they pass the de facto specificity test described earlier). In other words, the United States can now look beyond the expenditure in a foreign government's accounts, it can look beyond a mere legal description of a subsidy. It can determine that a subsidy exists even if there is no expenditure or legal description of it. If such a "subsidy" is widely used it can be countervailed under the amended statute. The inclusion of de facto subsidies under the statute pushes the whole CVD process further into the messy analytical problems inherent in subsidy cases. If the line between actionable and inactionable subsidies seemed murky before, continuing in this direction pitches the whole problem further into darkness.

## **INJURY, DOMESTIC INDUSTRY**

Since the 1979 Trade Act it has been necessary to substantiate that the subsidy causes injury to the relevant American industry. A final positive determination requires that a subsidy exist and that it causes injury to the domestic industry be substantiated. The definitions of injury and terms relevant to it, such as "like product", "domestic industry", "causal" links between "injury" and a "subsidy", are the same as those applied in the AD procedure. Similarly the same attenuated thresholds for each of these operative terms

apply. As we have seen in AD policy, there is a strong tendency to interpret these terms broadly, as broadly as is practicable and necessary to best ensure a positive determination.

## **CONCLUSION**

As with the AD law, CVD law and policy can only be clearly understood by a careful examination of the ways in which the operative terms and calculation methodologies are applied in practice. Every act of statutory and administrative change, every act of interpretation and application, is an act of economic statecraft. Each act is designed to affect the behaviour of foreign governments. By examining the details in the CVD law it become clearer what the United States is compelling foreign governments to do under the law.

1. Subsidies and Subsidy-Effect Programs of the US Government, materials prepared for the joint Economic Committee, 89th Congress, 1st. Session 1965. Cited by Bruce Butler, "Countervailing Duties and Export Subsidization: A Re-emerging Issue in International Trade" Virginia Journal of International Law Vol. 9, No. 1, December 1968, page 82.
2. Carbon Steel Wire Rod from Czechoslovakia, 49 Fed. Reg., 19,370, 19,371 (Dept Commerce) (1984).
3. Daniel K Tarullo, "Beyond Normalcy in the Regulation of International Trade", Harvard Law Review Vol. 100, No. 3, January 1987, page 567.
4. *ibid.*, page 570.
5. Frederick Davis, "The Regulation and Control of Foreign Trade" Columbia Law Review page 1445
6. Matthew Marks and Harald Malmgren, "Negotiating Non-Tariff Distortions to Trade" Law and Policy in International Business Vol. 7, No. 2, 1975, page 348.
7. Internal taxes are remitted to prevent the product from being taxed twice, at home and in the sale market (double taxation).
8. Lithuanian Butter, TD 49,122, 72 Treas. Dec. 241 (1937). Peter B Feller explains that a similar export promotion program was pursued by the Dutch government in 1939. A Dutch government monopoly bought pork from exporters at the domestic price. The pork was then sold it back to the pork monopoly at the lower world price. Dutch Pork, TD 49809, 74 Treas. Dec. 366 (1939). "Mutiny Against the Bounty: An Examination of Subsidies, Border Tax Adjustments, and the Resurgence of the Countervailing Duty Law" Law and Policy in International Business Vol. 1, No. 1, Winter 1969.
9. Craig M Brown, "Bounty or Grant" a Call for Redefinition in the Light of the Zenith Decision" Law and Policy in International Business 1977.
10. Black's Law Dictionary, 6th Ed. Centennial Ed., 1881-1991.
11. *ibid.*, page 731.
12. *ibid.*, page 454.
13. This raises a question. Are the ideological visions of the United States and the United States' administrative bureaucracy the same?
14. Robert Reich provides a fascinating discussion of the different ways in which various governments bailout failing firms in "Bailout: A Comparative Study in Law and Industrial Structure" Yale Journal of Regulation Vol. 2, 63, 1985. He raises one particularly interesting point: does the timing of the bailout (such as government guarantees on private loans given before or after the company is closed) affect whether the bailout is a subsidy?
15. Andrew Pollack, "Pentagon Invests in Small California Chip Maker" International Herald Tribune, April 11, 1990.
16. Amitai Etzioni, The Moral Dimension: Toward A New Economics, (New York: The Free Press, 1988) page 73.
17. *ibid.*, page 73.

18. *ibid.* Amitai Etzioni concludes that this is a distinguishing characteristic of societies where liberal economic theory is confused with reality.
19. See Chapter Three, page 74, Notes 75-77 *infra*.
20. CFR sect. 16.24(f) (Supp 1956).
21. Multiple exchange rates are permitted under Article VIII of the IMF Treaty.
22. Uruguayan Wool Tops, T.D. 53, 257 88 Treas. Dec. 105 (1953).
23. Energetic Worsteds Corp. v United States, 224 F. Supp. 606 (Cust. Ct. 1963).
24. 18 International Monetary Fund: Report on Exchange Restrictions, 5-6 (1967).
25. Butler, "Countervailing Duties and Export Subsidization", page 86.
26. Marks and Malmgren, "Negotiating Non-Tariff Distortions to Trade" page 359.
27. Uruguayan Wool Tops, T.D. 53, 257 88 Treas. Dec. 105 (1953).
28. Canada Automotive Products, 29 Fed. Reg., 7249 (1964).
29. Butler, "Countervailing Duties and Export Subsidization" page 105.
30. Italian Transmission Towers, T.D. 67,102, 32 Fed. Reg., 6274 (1967).
31. Craig Brown, "Bounty or Grant" a Call for Redefinition in Light of the Zenith Decision Law and Policy in International Business, 1977, 1229-1257, page 1242 Note 86.
32. *ibid.*, page 1242.
33. RV Guido and MF Morrone, "The Michelin Decision: A Possible New Direction for United States Countervailing Duty Law: X-Radial Steel Belted Tires from Canada" Law and Policy in International Business, Vol. 6, 1974, page 249.
34. American Express v. US, 322 F. Supp. 191 (Cust. Ct. 1971), *aff'd*, 472 F. 2nd. 1050 (CCPA 1973).
35. Craig Brown, "Bounty or Grant", page 1242.
36. Zenith Radio Corp. v US, 437 US 443 (1978).
37. John Barcelo, "Subsidies and Countervailing Duties -- Analysis and Proposal" Law and Policy in International Business Vol 9, 1977 page 780.
38. *ibid.*, page 780.
39. No. 77-19 (CCPA July 28, 1977) Pet. for Cert. filed, 46 USLW 3263 (October 18, 1977) (No 77-539). Sup. Ct. No. 77-539.
40. Tomato Paste, as discussed by William N Walker, International Limits to Government Intervention in the Marketplace: Focus on Subsidies to the Private Sector, (London: Trade Policy Research Centre, 1976) page 11.

41. Michelin Case, known as X-Radial Steel Belted Tires from Canada, Fed. Reg., 38 (1983).
42. William N Walker, International Limits to Government Intervention in the Marketplace: Focus on Subsidies to the Private Sector.
43. *ibid.*, page 11.
44. X-Radial Steel Belted Tires from Canada, Fed. Reg., 38 (1983).
45. Guidoand Morrone, "The Michelin Decision" page 252.
46. *ibid.*, page 258.
47. *ibid.*, page 256.
48. Float Glassfrom Begium, the Federal republic of Germany, France and Italy, 40 Fed. Reg., 2718 (1975).
49. Trade Act of 1979 Section 771(5). "if provided or required by government action to a specific enterprise or industry, or group of enterprises or industries". USC 19 Sect. 1677(5)(B) 1982.
50. Alfred Kahn, The Economics of Regulation: Principles and Institutions (New York, Wiley, 1970) 2 Vol.s.
51. Tarullo, "Beyond Normalcy" page 560.
52. The Subsidies Code says that subsidies "granted with the aim of giving an advantage to certain enterprises, ...either regionally or by sector" are actionable. Judy Hippler Bello and Alan Holmer, "Subsidies and Natural Resources: Congress Rejects a Lateral Attack on the Specificity Test" GeorgeWashington Journal of International Law and Economics Vol 18, 1984, page 305.
53. Gary Hufbauer, "Subsidy Issues After the Tokyo Round" Trade Policy in the 1980's William Cline, ed., (Washington, D.C.: Institute for International Economics) page 352.
54. Sect 771(5) Trade Act of 1979. A domestic subsidy that has trade effects is actionable, "if provided or required by government action to a specific enterprise or industry, or group of enterprises or industries". USC 19 Sect 1677(5)(B) (1982).
55. Judy Bello and Alan Holmer, "Subsidies and Natural Resources: Congress Rejects a Lateral Attack on the Specificity Test" page 305.
56. *ibid.*, page 304.
57. Defending the test on this second point, Pieter Alexander argues that the benefits from a subsidy that is generally available are "mitigated or counterbalanced by other macro-economic factors." Pieter Matthijs Alexander, "The Specificity Test Under US Countervailing Duty Law" Michigan Journal of International Law Vol. 10, page 822.
58. Cabot Corp v. United States, 620 F Supp 722 (CT. Int'l Trade 1985).
59. GaryHorlick and GeoffreyOliver "AD and CVD Law Provisions of the Omnibus Trade and Competitiveness Act of 1988" Journal of World Trade page 8.



60. *ibid.*,

61. *ibid.*

62. PPG Industries Inc. v. United States, 662 F. Supp. 258 (Ct. Int'l. Trade 1987). See also Al Tech Specialty Steel Corp v. United States, 661 F. Supp. 1206 (Ct. Int'l. Trade 1987) and Can-Am Corp. v. United States, 664 F. Supp. 1444 (Ct Int'l. Trade 1987).

63. Pieter Matthijs Alexander, "The Specificity Test Under US Countervailing Duty Law" page 826.

64. *ibid.*, page 826.

65. Certain Softwood Lumber Products from Canada (1983), 48 Fed Reg 24, 159, 24, 167 (1983).

66. Certain Softwood Lumber Products from Canada, (1986) 51 Fed. Reg., 37,453 (1986) (preliminary determination).

67. 19 USC 1677-1 (Supp. IV 1986).

68. Peter J Koenig, "Upstream Subsidies: United States Countervailing Duty Law" International Trade Policy: the Lawyer's Perspective Committee on International Trade Section of International Law and Practice, American Bar Association, John Jackson *et al.*, ed.s., (New York: Mathew Bender, 1985) page 9-6, Section 9.02.

69. *ibid.*

70. Goetz, Granet and Schwartz, "The Meaning of "Subsidy" and "Injury" in the Countervailing Duty Law" International Review of Economics, Vol. 6, No. 1, June 1986, page 28.

71. Gary Horlick, "The United States Antidumping System" page 11, Note 33.

72. *ibid.*, pages 20-21.

73. *ibid.*, page 24.

74. *ibid.*

75. Also, in a firm with several factories, costs are not independent to each factory. Peter Drucker says because of this: "In effect, traditional cost accounting can hardly justify a product improvement, let alone a product or process innovation." Peter Drucker "The Emerging Theory of Manufacturing" Harvard Business Review May-June 1990, page 97.

76. Jacob Viner, Dumping: A Problem in International Trade (Chicago: University of Chicago Press, 1923) see quote in Chapter Five, page 115, Notes 75-76 *infra*.

77. John Sciortino, "Calculating Subsidy Values in Countervailing Duty Cases: The use of the Present Value Methodology" International Trade Policy: the Lawyer's Perspective, John Jackson *et al.*, ed.s., Committee on International Trade Section of International Law and Practice, American Bar Association John Jackson *et al.*, ed.s., (New York: Mathew bender, 1985) page 8-3, Section 8.02.

78. As long as the late receipt was mandated by the government in question.

79. 19 USC Sect. 1677 (6).
80. 3 ITRD 1177 (1981).
81. Michelin Tire Corp v US, 4 ITRD 1450, 1451 (1982).
82. Maybe it would be useful to quote the Oxford English Dictionary definition of "procrustean". "Tending to produce uniformity by violent methods. Literally a stretcher, the name of a fabulous robber who fitted victims to his bed by stretching or mutilation".
83. Cited by John Sciortino, "Calculating Subsidy Values" page 8-14, from Michelin Tire Corp vs US, 4 ITRD 1450, 1451 (1982).
84. *ibid.*, page 8-12.
85. Carbon Steel Products from Belgium, 47 Fed. Reg., 39304, 39317 (1982).
86. Final Affirmative Countervailing Duty Determination, Carbon Steel Products from Belgium, 47 Fed. Reg., 39304, 39317 (1982).
87. Carbon Steel Petitions of 1982.
88. Ceramic Tile from Mexico, 47 Fed. Reg., 20012, 10 May, 1982.
89. Certain Pig Iron from Brazil, 44 Fed. Reg., 67554, 26 Nov 1979.
90. Ferroalloys from Spain, 45 Fed. Reg., 25 2 January 1980.
91. Leather Wearing Apparel from Argentina, 46 Fed. Reg., 23009, 23 April 1982.
92. John Sciortino, "Calculating Subsidy Values" page 8-34, Section 8.07.
93. This "would be to include in calculation of its value the impact of how the company uses the funds, thereby penalizing the company for its commercial activities." *Ibid.*, page 8-16, Section 8.04.
94. Goetz, Granet and Schwartz, ""The Meaning of "Subsidy" and "Injury" in the Countervailing Duty Law" page 28.
95. *ibid.*
96. Sciortino, "Calculating Subsidy Values" page 8-12, Section 8.05.
97. See Richard A Brealy and Stewart C Myers, Principles of Corporate Finance (New York: MacGraw-Hill, 1981).
98. Sciortino, "Calculating Subsidy Values" page 8-34, Section 8.07.
99. *ibid.*, page 8-30, Section 8.07.
100. *ibid.*, page 8-37, Section 8.08.

## CHAPTER NINE -- COUNTERVAILING REMEDIES

In the majority of CVD cases, Commerce is unable to substantiate that the subsidy exists and/or the ITC is unable to substantiate that injury was incurred to the domestic industry by reason of the dumped imports. However, if dumping and injury are substantiated then a positive determination is made against the respondent. Most often the subsidy is countervailed with a commensurate duty. The duty is levied on the subsidized merchandise. The firms that benefitted from the subsidy are required to pay that duty. There is no way to make the foreign government(s), which provided the subsidy, directly responsible for the duty payment.<sup>1</sup> It is hoped that the penalized firms will bring pressure to bear on their governments' to cease with the subsidy program, or that the reduction of export sales and revenue will induce the foreign governments' to cease with the subsidy practice. Or, as often happens, the foreign firms will refuse to participate in the program. As such, the CVD law sometimes evokes a change in the behaviour of foreign firms, not just governments'.

If the investigation terminates before a final determination is rendered or, if the final determination is negative, the firms that allegedly benefitted from the subsidy will be refunded the deposits which were paid upon the commencement of the investigation. This short-term financial penalty is sometimes sufficient to create pressures which lead to a change in government policy. It is worth noting that the initial deposits could be paid in the form of a bond until 1984. This meant that firms could avoid a cash outlay pending the final determination. But, under the 1984 Trade Act the deposits must be made in negotiable instruments, thus requiring a cash outlay. As a result, the firm incurs a financial penalty between the beginning and end of the procedure. Since the 1988 Trade and Competitiveness Act, the firms are no longer automatically eligible for a refund of these initial deposits.<sup>2</sup>

The United States maintains lists of the most politically powerful industries and firms in every foreign country precisely because a CVD procedure, or for that matter an AD procedure bring pressures to bear on the government. The threat of provoking a government's most powerful industry constituents and thus creating a domestic political problem is a potent one. As a result, the fact that the government may not be directly responsible for the payment of duties does nothing to diminish the persuasive force of duties on that government.

## **SETTLEMENTS**

CVD investigations may be terminated or suspended as in AD cases. In lieu of duties the foreign government may be requested or compelled to agree to a settlement. Large margins are the most common means of forcing foreign governments to change their policy or modify their behaviour in compliance with the United States' demands. Large margins imply large duties which will jeopardize the firm's viability in the United States market.

Suspension agreements can be reached if the foreign government(s) agree to eliminate or offset the subsidy entirely. Or the government(s) must ensure that the subsidized goods cease being exported into the United States. In other words, government to government quotas must be negotiated or voluntary restraints of exports must be undertaken. The statute requires that 85% (substantially all) of the exports in question cease being exported for quotas. A third option specifies that the investigation can be suspended in "extraordinary circumstances" if the government(s) ensure the elimination of all the injurious effects caused by the subsidy.<sup>3</sup> Under this last type of suspension all price suppression and price undercutting must also be eliminated.

If the settlement under the suspension fails to meet the United States' requirements the case can be resumed. A final determination will be made. If the determination is positive duties will then be imposed.

It is almost impossible to eliminate a subsidy's injurious effects. For this reason, this kind of suspension agreement has never been reached in a CVD case. It is too difficult to negotiate an agreement among 85% of all the governments in question and to ensure no price underselling or suppression. Governments simply lack the authority (in market economies) to control their domestic firms' pricing policies sufficiently to guarantee compliance. And there is always the possibility that the government(s) in question will provide another subsidy to offset the effects of the settlement. This kind of suspension, though allowed, has never been done.

In contrast, governments' have often agreed to offset or eliminate the subsidy entirely. That is, the foreign government(s) accept the judgement of US officials that their subsidy policy is not appropriate. For example, in 1983 the Government of Singapore agreed to apply an export tax on its exports of subsidized refrigerators.<sup>4</sup> But Section 611 of the 1984 Trade Act prohibits the termination of a suspended case based on such offsets. So, the foreign government's export tax must remain in place as long as the United States believes the subsidy exists.

Export restraints can be negotiated between governments. But such arrangements are rare. It is necessary to protect those United States officials who negotiate quotas from prosecution under domestic competition policy for acting in restraint of trade. Generally, the Justice Department counsels them about how to negotiate. Voluntary export restraints have been the preferred method for implementing quotas. These arrangements are purely voluntary on the part of the foreign government. Therefore American officials cannot be liable under such arrangements for engaging in anticompetitive practices. But voluntary restraints are difficult to police since there is no legal requirement that the foreign government maintain voluntary restraints.

CVD investigations can also be terminated. Usually this happens when the petitioners agree to withdraw their complaint. Again, voluntary export restraints or voluntary commitments to eliminate the subsidy are the most common means of settling. After a termination the case cannot be reopened as it can under a suspension. Withdrawal

terminations are particularly interesting instruments of economic statecraft. Once the petition has been withdrawn the negotiators are not bound to adhere to the terms of the petition. Therefore, the foreign government can be compelled to address issues or exports that are beyond the scope of the petition. Elaine Frangedakis mentions the steel settlement of 1982 as an example. Steel pipes and tubes, which had not been mentioned in the petition, were included in the voluntary quota to which the major steel producing nations agreed.<sup>5</sup> The 1984 Trade Act Section 604 allows termination of CVD cases based on governmental understandings and agreements to limit the volume of exports to the United States.

The majority of suspended or terminated CVD cases rest upon the foreign government's agreement to abandon its subsidy.

## **COMPETITION POLICY: ANTICOMPETITIVE ENDS**

The political aspect of CVD policy should be clear. As a technique of statecraft the CVD law aims to change a foreign government's policies, behaviour, actions, beliefs, ideology and propensity to act. Power is an integral element of this political aim. Foreign governments are compelled to do what the United States demands or, at the least, to abide by the standards of commercial behaviour the United States is enforcing.

If the United States was promoting market standards and penalizing genuinely anticompetitive behaviour then this use of power and the implicit political aim would be legitimate. That is, the use of power and the aim of politics would be in accordance with the internationally agreed upon methods and objectives of conducting trade policy. But, as we have seen, the CVD statute is not used to enforce market standards. It does not draw distinctions between competitive and anticompetitive commercial behaviour based on any sound economic criteria. Instead, the criteria is based on market ideology -- governments should not "intervene" in economic affairs -- tempered by pragmatic considerations.

Most analyses of CVD policy and competition policy take these pragmatic constraints as given. But for analysts of international relations and international politics this is the most interesting and important aspect of CVD policy. Why is it that pragmatic constraints exist? Why can't the United States hold foreign governments to a pure market standard? It is because the United States recognizes that it cannot call for the elimination of governments altogether. Once government begins to protect contract and property rights it becomes impossible to distinguish between the state and the market unarbitrarily.

But in establishing a normalcy standard to distinguish between actionable and inactionable subsidies, the United States abandons economics as the central issue. At issue is the validity, the legitimacy, of foreign acts of state, in particular their economic policies. As the countervailing duty law is currently structured, American authorities are required to judge the legitimacy of foreign governments' subsidy programs but the CVD law does not provide specific criteria or rules by which such judgements should be made. The lack of substantive and legal constraints or guidelines provides those who invoke the law with wide leeway simply to attack foreign economic policies to which the United States objects. On what grounds are such objections levied?

Export subsidies, all agree, are illegitimate means of achieving political or economic goals. Domestic subsidies, in contrast, are perceived as a legitimate means of achieving such goals within the context of a market economy. In the modern world, given that the governments of all the market economies have accepted the broad responsibility to manage macroeconomic affairs, legitimacy and efficiency are defined by political criteria. To one government its domestic subsidy policy (regional development, income transfer, infrastructure support) appears to correct a market failure. To the other it creates a market failure. In short, there are no workable competition criteria available to help us reasonably decide why a particular domestic subsidy practice is objectionable.

Matthew Marks and Harald Malmgren got the nearest to identifying the central political problem at stake. They encapsulated it as the

"broad problem of what constitutes a legitimate internal measure."<sup>6</sup>

No agreement on this question can be reached by way of purely economic logic.

It is not only the specific differences between various internal measures among the GATT signatories that causes the problem. After all, the same measures used by the United States are often the ones it seeks to countervail when others undertake them.

The problem is more that there is no universal agreement as to the appropriate role of government in a modern industrial market economy.<sup>7</sup> Everybody agrees that government must act to subserve broad political and economic goals through macroeconomic management. But the governments of the market economy countries, and for that matter all of the economists and politicians within each of these countries, disagree about the best means of achieving political and economic goals through macroeconomic management. In turn, this divergence arises from the fact that the various market economies actually perceive the concept of a market economy differently.

Although this is not the central contention in this study, it would seem that more research about the differences between the various models of a market economy needs to be done before any agreement can be reached as to what constitutes a legitimate internal measure. In the meantime, the ideological and practical differences among the market economies will continue to give rise to conflict, particularly if the United States continues to penalize foreign actors with the CVD law and, for that matter the AD law, for engaging in economic policies which are not perceived by those actors to be illegitimate, abnormal or anticompetitive. This problem is bound to become more apparent once the formerly Socialist and/or Communist Eastern block countries make the transition to a "market economy" and try to enter world markets. Further, this will continue to be a contentious issue among the industrialised market economies particularly as competitive advantage is seen more and more to be a function of the general economic environment within a nation rather than a function of an individual firm's behaviour.

The United States uses the CVD law as a means of penalizing foreign governments for pursuing particular policies not because those policies are inherently anticompetitive, and not because those policies exemplify a type of intervention not practised by the



United States (because they sometimes do), but because the United States objects to the practice on what appears to be economic grounds but which are in fact ideological and political grounds. By labelling a foreign policy a subsidy the United States can exercise power, if not a veto, over foreign governments' political objectives or the means foreign governments have chosen to achieve those objectives.

The technical aspects of the law's administration clearly reveals that it has been subverted into an anticompetitive measure. The law depends upon the identification of foreigners' cost of production; but, no theoretical or workable method exists:

- for accurately determining the overall "normal" or "subsidized" costs of production (because states and markets cannot be separated)
- for accurately calibrating the differences between states in their cost of production which arise from the varying ways in which their governments protect contract and property rights, not to mention fiscal and infrastructure policy.
- for accurately determining the cost of producing any single item in a multiproduct firm.
- for accurately apportioning the value of the subsidy among the recipient firms, or for apportioning the value of the subsidy among different factories within a single firm all of which are necessary in order to reach a figure for the net subsidy.
- for accurately determining the impact of the subsidy on producing the specific exports that had trade effects on United States commerce.

In establishing a universal "normal" cost formula, which, we recall, includes a minimum of 8% profit, the cost of fabrication and materials (determined by the United States without calibrating it for fluctuations in direct and indirect costs, etc.), the United States denies that costs should, indeed, must vary from country to country, from firm to firm and from factory to factory. Differences in relative costs, or the cost formula, which is single most important factor which causes international trade, are penalized under the law.

In addition, the exchange rate which is used to calculate any figures resulting from the CVD investigation can, by itself, magnify or minimize the amount of the alleged subsidy. Similarly, the new Net Present Value (NPV) methodology, with which the genuine (nominal) value of a subsidy is determined, inflates the value of the alleged subsidy. In NPV calculations, the discount rate reflects judgement and discretion more than real economic considerations.

Any cost or net subsidy figures compiled and employed in CVD petitions bears only a tenuous relationship to any economic reality.

Furthermore, the terms "domestic industry" and "like product" have been defined under the statute so that the injury is measured for its impact on competitors not competition. This standard is absolutely at odds with the maintenance of a competitive environment, as the US Courts have consistently insisted in their reviews of domestic competition policy.

## CONCLUSION

In conclusion, the criteria used to define what a subsidy is, to assess its impact and value and to administer the CVD law against foreign governments' trade practices ignores genuine competition policy objectives. In practice, the CVD law relies on inherently anticompetitive criteria. By utilizing figures which have been arrived at through doubtful methods, the United States penalizes foreign governments for engaging in the apparently unfair trade practices. The penalties or remedies are themselves anti-competitive in practice. CVD policy cannot be reconciled either with domestic competition policy objectives or, more importantly, with the rhetoric which emphasises the United States' commitment to the principle of competition in the post-war international economic order.

This would be concern enough. But the CVD policy, more importantly, raises a challenge to the post-war concept of sovereign freedom. As an instrument of statecraft this economic policy tool is used not only to compel foreign governments on specious grounds to change their attitudes, behaviour, propensities to act, and to limit their policy options but, in addition, this economic statecraft challenges the freedom of foreign governments to choose the macroeconomic goals, or the means of achieving them, which are necessary to the maintenance of a modern industrial democracy. As it now stands, American CVD law and policy challenge the freedom to determine what a government's proper and efficient role is within the context of a market economy.

1. A government might even be liable to another countervail proceeding if the government itself attempted to pay the duty or finance the duty for the firm(s) in question.
2. Section 1334 Omnibus Trade and Competitiveness Act of 1988. See Chapter Six, page 147, Note 1 *infra*.
3. Section 704 of the Tariff Act of 1930, Pub. L. No. 71-361 Stat. 590 as amended.
4. Certain Refrigerators from the Republic of Singapore, 48 Fed. Reg., 15,167 (1983).
5. Elaine M Frangedakis, "Suspension Agreements" International Trade Policy: The Lawyers Perspective, John Jackson, *et al.*, ed.s., Committee on International Trade Section of International Law and Practice, American Bar Association (New York: Mathew Bender, 1985) page 11-25, Section 11.05.
6. Matthew Marks and Harald Malmgren, "Negotiating Nontariff Distortions to Trade" Law and Policy in International Business Vol. 7 No. 2, 1975, page 357.
7. We recall Tarullo's comment that "differing conceptions of proper and efficient governmental policies are at the root of much contemporary debate on international trade competition." Daniel K Tarullo, "Beyond Normalcy in the Regulation of International Trade", Harvard Law Review Vol. 100, No. 3, January 1987, page 556.

## **SECTION FOUR**

## CHAPTER TEN -- ECONOMIC STATECRAFT AND INTERNATIONAL RELATIONS

The purpose of delving so deeply into the minutiae of the American AD and CVD laws has been to demonstrate that remedy policy in practice is utterly at odds with its intended and propagated purpose. The technical details which have in the past served to conceal meaningful developments in the laws from public scrutiny now, being clearly depicted, serve to reveal this deep contradiction. It is always worth pointing out that what is actually happening is the opposite of what everybody thinks is happening. But the consequences of this particular contradiction are extremely important to both our theoretical and practical understanding of international relations.

This dissertation opened with an exercise in critical theory.<sup>1</sup> That is, attention was drawn to the fact that the traditional paradigms, or frameworks of thinking about trade policy, were insufficient because they denied or obscured the role of power in, and the inherent political quality of, trade policy. Where the free trade versus protection and the non-intervention versus intervention frameworks lead us to the conclusion that the remedy laws are now instruments of protection, the economic statecraft framework allows us to see that protection can be achieved only by generating a change in the commercial behaviour, opinions, policies of foreign governments and foreign firms.

Having adopted a new framework of analysis, David Baldwin's economic statecraft framework, the dissertation then embarked upon solving the problem at hand.<sup>2</sup> If AD and CVD policy are aimed at reducing the play or market forces and limiting competition then the US must be undermining and not, as is commonly believed, upholding the Post-War international economic order. It is not just that the US is subverting the GATT rules by creatively manipulating the definitions of operative terms such as "injury" or "like product". The rules have meaning because they provide a structure which supports the internationally agreed-upon legitimacy; it is that legitimacy which gives definition, form and purpose to the rules for international trade. The legitimacy of the Post-War

international economic order holds that in comparison with the known alternatives, competition provides the most appropriate, impartial and just mechanism for determining the distribution of wealth internationally. Trade policy, especially for Contracting Parties to the GATT, is supposed to promote this legitimacy. That legitimacy sets out the methods trade policy should employ and the objectives trade policy should aim to achieve. Not only is the oblique use of the remedy laws as covert methods of protection illegitimate but the aim of the policy is to impede competition, and that is illegitimate.

With the AD and CVD laws, in their current subverted form, the United States selectively reneges on the implicit promise made under the Post-war international economic order. That promise is that access to wealth is secured by the peoples of the world by competitiveness, the ability to produce superior or desirable goods (and services) for which others wish to pay. To renege on this promise is to challenge the very economic basis of international civil society.

Further, the United States' use of these laws provokes conflict among its trading partners. Granted, even the most virulent conflict between, for example, the US and Japan or the US and the EC on dumping and subsidy issues is unlikely to escalate into the kind of conflict that traditionally dominates the attention of international relations analysts, i.e. war. But conflict is divisive, even if small. One of the most fascinating aspects of US and CVD policy is that it has ideological substance, and that that substance is provocative to many foreigners. AD and CVD policy is essentially aimed at converting foreigners to the economic vision being imposed by the United States.<sup>3</sup> Remedy policy aims to change foreigners' beliefs and opinions about the appropriate role and behaviour of firms and governments in a market economy. No genuine market standard is enforced with these laws. Rather, in the case of the CVD law, the US is imposing a vision of the acceptable and appropriate role of governments in managing their market economies. In the case of the AD law, the US is imposing a vision of the acceptable and appropriate behaviour of firms in managing their commercial affairs in a market economy. But the visions being imposed have neither been agreed-upon internationally nor accepted even in the US

itself.<sup>4</sup> By forcing others to change their domestic structures, opinions, perceptions, policies on this basis, the United States challenges the very political basis of international civil society, i.e. the freedom to shape and run domestic institutions and policy according to national inclinations.

The political and the economic questions of international civil society overlap, as Cordell Hull noted in his memoirs.

"Over and above the economic side of our foreign policy, but closely tied with it, I believed, hung the political side. To me it seemed virtually impossible to develop friendly relations with other nations in the political sphere so long as we provoked their animosity in the economic sphere."<sup>5</sup> "The political line-up followed the economic line-up."<sup>6</sup>

Traditionally, analysts of international relations have puzzled over where the line should be drawn between the demands of international civil society and national sovereign prerogatives. This problem was evident, for example, when the South African Government insisted that apartheid was an internal matter beyond the reach of the international community. Now attention must be turned to this new source of conflict. It must be determined where or whether a line can or should be drawn when it comes to the central question which is at stake when remedy policy is exercised -- that question is, what is the range of commercial behaviour governments and firms in market economies can pursue without being a threat to international civil society?

More work needs to be done on the problem of whether it is really possible (or practicable) to make a distinction between genuine and artificial competitive advantage.<sup>7</sup> Further, given that such significant practical and ideological differences among the market economies patently exist, there needs to be a much more sophisticated study and understanding of the various extant and possible forms "capitalism" or "market-economies" can take. For the differences of perception and opinions which create and or arise from these different forms of capitalism are what will continue to prevent agreement and make negotiation difficult. In addition, such study and understanding may make it possible to move beyond the current proclivity to blame others for not being as "market-oriented"

as those doing the blaming would like. At least one commentator thinks that this is the way to go on subsidy questions. Jacob Dreyer believes

"...the legitimacy of certain national objectives ought to have a seal of international approval, with the aim of limiting the gray areas of differing interpretations of this concept (subsidy) by national authorities. An international agreement on this subject, though remote at present, could be incorporated in principle into the GATT. The range of internationally agreed-upon "legitimate" national interests would probably be wider than the US government would advocate, but there is no reason to fear that any attempt to reach such an understanding would be doomed to failure."<sup>8</sup>

Such a discussion could also be applied to the question of firms and dumping. In short, the concept of "fair" needs to be examined in greater detail.

It has been the belief that foreigners were engaging in "unfair" commercial behaviour which prompted the US authorities to create and actively enforce the AD and CVD laws in the first place. As the dynamic sources of commercial advantages have become a more pressing issue there has been a tendency to do more than just make accusations of unfairness. There has been an increased tendency to try to "level the playing field".

William Cline explains that "A "level playing field" .... becomes especially important where comparative advantage is arbitrary."<sup>9</sup> But the playing field, as it were, cannot be levelled. The technical differences in national accounting procedures, corporate structures, subsidy policies, etc., all arise from differences of opinion as to the appropriate nature and role of governments and firms in a market economy. Already we can see, as Robert Baldwin points out, "The need for a "level playing field" or "to make foreign markets as open as US markets" have become the basic justification for the greater use of trade distorting measures by the US."<sup>10</sup> Cameron and Crawford make the point this way. "These amendments (made to the AD and CVD laws)" .... " have further tilted the playing field against respondents and foreign enterprises under the guise of levelling that field."<sup>11</sup>

But, study should not be focused on the concept of fairness because it is simply untenable in the realm of commercial affairs. It is impossible to measure. Fairness is in the



eyes of the beholder. Attempts to measure it are economically meaningless exercises in fiction.

This is the main problem with United States AD and CVD laws. Unwilling to abandon the principle of free trade, the United States has instead modified the statutes so that fair trade practices can be made to appear "unfair". Normal trade practices are labelled "unfair" not because they are anti-competitive, but because they are genuinely competitive. Noel Hemmendinger captures the tension between America's commitment to the principles of competition and its need to be seen to be "doing something" about trade problems.

"One element of the tendency to treat unwelcome competition as "unfair" is a genuine desire, as a matter of principle and international obligations, to avoid countermeasures unless a finding of unfairness can be made."<sup>12</sup>

So, the laws have been stretched so that a finding of unfairness is rather easy to make. The end result is an ideological conviction that the foreigner's behaviour is somehow wrong. Specific countermeasures are difficult to make against such allegations. This is especially true because the respondent cannot challenge the decision to make the allegation until after a final judgement has been rendered in any given case. Nonetheless, the very unfairness of the allegation is an important problem. Hemmendinger highlights it.

"If, however, the results are capricious, or there is no international consensus on the alleged unfair practice, lip service to the principle accomplishes nothing and makes trouble internationally."<sup>13</sup>

The more aggressively the United States invokes these laws the more trouble will appear internationally. The more the US continues to "enhance" these statutes in the manner which has been described here, the more it will undermine order when it invokes them.

This raises a question which this dissertation has not fully addressed. Why has the policy in practice diverged from the intended or propagated policy?

Perhaps Joseph Grunzel was right.<sup>14</sup> Those most ideologically committed to the doctrine of "free trade" are the ones most likely to modify the doctrine, not in principle, but in its application. Oxymoronic notions abound in the realm of competition policy.

What is free trade is labelled protectionism. What is protectionism is labelled free trade. Fair is said to be unfair. Just as the Queen told Alice in Wonderland that she had to be capable of thinking up ten impossible things before breakfast, one must believe many impossible things to accept that the AD and CVD laws serve to promote competition. One must believe that it is possible to accurately determine the cost of producing one item in a multiproduct firm, that the American industry can be constituted by a single company or region of the country, that it is possible to draw a line separating states from markets, or if not, that an economically sound line can be drawn between good government interventions and bad ones. The AD and CVD laws are a fine example of Grunzel's theory.

Perhaps disinterest and misinformation combined have allowed the subversion of the statutes. Trade remedy policy is not the sexiest subject in politics, economics or even in law. Certainly the prolific technical details inherent in the AD and CVD statutes have shielded them from intense scrutiny. But, even those most closely involved in the passage of trade legislation often do not have the time to read carefully through the hundreds or thousands of pages which make up a trade bill. Members of Congress must rely on their staff to interpret and explain the meaning of proposed modifications. Some things may be lost in translating the technical terms into plain English. Or, the staff members or the Congressmen, accept the judgement of their colleagues who serve on the relevant committees.<sup>15</sup> Chinese whispers<sup>16</sup> usually lead to mistranslation and end up causing misunderstanding.

Sometimes, no doubt, propagation of misinformation is intended. There are those who know full well that a proposed amendment or an attendant administrative regulation is undeniably protectionist. After all, much if not most of the language put forward to be considered for inclusion in a trade bill is crafted by the corporate community. Some political representatives promote the inclusion of this language because they may confuse what is good for the country with what is good for their corporate constituents. Bill Boyarsky cleverly captures the manner in which much trade legislation is produced.

**"One of the oldest tricks in the legislative business is mumbling a bill through the legislature. You mumble when you want to sneak through something that wouldn't stand public scrutiny. You employ technical, sometimes impenetrable language. The summary that accompanies the bill is vague and misleading. In explaining the bill to fellow lawmakers you mumble that it makes "technical changes" or "eliminates obsolete language." Colleagues, with thousands of bills before them, usually take the explanation at face value and vote aye."<sup>17</sup>**

Perhaps ignorance accounts for the subversion. Proposed changes are adopted because no one foresees its ramifications. This might explain why so many critical changes have been made to the laws without Congressional discussion at all. We remember that there was absolutely no official debate, for example, with regard to three of the most consequential innovations ever made. One was the adoption of a sales below cost standard in 1974 under the AD law. Another was when domestic production subsidies were included as actionable subsidies in 1922 under the CVD. A third example is found in the requirement for a specificity test under the CVD law which was adopted in 1979.

It may be that few have a proper understanding of the economics of competition. The failure to distinguish between injury caused by healthy competition and injury caused by anticompetitive trade practices is a good example, as is the failure to correctly distinguish between injury to competition and injury to competitors. Or, it may be that even a perfect understanding of economic theory would not solve the problem because the theory is so imperfect. Competition policy theory and international trade theory bear only a tenuous relationship to reality.<sup>18</sup>

There are those, often the ones who have been closest to the policy-making process, who believe that the subversion of these statutes can and should be accounted for only by the deliberate and cognizant actions of the authorities who have modified these laws in content and in application. Brian Hindley says, "the other, sadder, possibility is that ministers' commitment is to a liberal world trading order in rhetoric, but to protection in practice."<sup>19</sup> According to this view the many "technical" revisions over the years are not accidental. The draft revisions being almost invariably suggested by representatives of groups desiring increased protection either in industry, or in the government itself in response to protectionist pressures.

Whether this is true or not, the economic statecraft framework has allowed us to see that the bureaucratic organizations and officials responsible for applying these laws have modified their administrative regulations so that the procedure and methodology is biased, and/or can be manipulated, in favour of petitioners. Our heightened awareness of the discretion available in the AD and CVD procedure might help us understand this phenomenon better in future. By focusing on the actual policy content, it has been possible to clarify the important role played by those who modify the statutes' and those who interpret and apply them. Once it is accepted that the laws are instruments of statecraft then it is necessary to accept that attempts to make or change AD and CVD policy constitute acts of economic statecraft.<sup>20</sup>

This contrasts with the current popular perception that administered protection is a better alternative to the more political alternative of protectionist legislation because it is a low-level technical procedure. For example, Michael Finger says:

"The antidumping and countervailing duty mechanisms in the US , for example, are technical procedures. There, determinations are defined by hundreds of lines of legislation and thousands of lines of administrative regulations."<sup>21</sup>

Similarly, Douglas Nelson argues:

"In the US, with its strong process orientation, the "low politics" aspect of administered protection is established by the creation of a large body of technical rules (the administrative regulations) which constrain, at a very low level, the amount of discretion available to the bureaucrats who handle administered protection cases."<sup>22</sup>

Seen this way, it is easy to agree with the conclusion which is typically reached. Nelson puts it best.

"Yet, they are low-visibility mechanisms which attempt to provide incremental protection without resource to the more political mechanisms. As a result, this administered protection tends to enhance stability in international economic relations."<sup>23</sup>

If we examine these laws as instruments of economic statecraft, however, it quickly becomes apparent that the technical procedures are not as innocuous as they appear. It is crucial to ask what the United States is compelling foreigners to do. This makes it necessary to look closely at the technical details. We see, for example, that the central operative terms can be imbued with various meanings at different times. The

methodology is flexible even within the context of a single investigation. There is great freedom for the various administering officials to use their discretion within the limits of the statutes and regulations. For example, Michael Finger says that a technical bureaucrat's job is to "accumulate technical knowledge and apply it accurately, as the rules and regulations direct."<sup>24</sup> He does not see the political power wielded by those who write and administer the statutes. As a result, he undermines his own case. In explaining that: "Pressure group politics does not come to bear on them [the bureaucrats]."<sup>25</sup> he claims, as the person responsible for calculating the Steel Trigger Prices for the United States, he could have chosen the figure of \$650 or \$690 per ton within the limits of the regulations but even still he didn't get a single invitation to lunch.<sup>26</sup> That he could have chosen any figure between these two limits is evidence of the discretion available to him. The freedom to administrative officials to exercise discretion in their interpretation and application of these statutes plays an important role in the content of the policy.

Granted, there are more constraints on administering officials now than there were in the past. There are those, Gary Horlick tells us, who would prefer the "good old days when margins could be manipulated for the greater good of the country."<sup>27</sup> Perhaps the margins could have been manipulated but the real question is whether they actually were. John Jackson recommends,

"... whatever system exists should leave to those government officials as much elbow room as possible to make the necessary decisions because those officials inherently feel that they will make the best decisions possible ..."<sup>28</sup>

But what is the definition of the "best decisions possible"? Before answering this question we should perhaps look at the bigger picture. By highlighting the political aspects of trade remedy policy the economic statecraft framework brings us to another conclusion which is opposite to the popular wisdom. It is commonly accepted that the United States Government has no political agenda when it comes to trade remedy policy. Alan Wolf, for example, explains:

"The United States government has no general mandate to structure either America's trade or its production of manufactured goods. Instead, the government is given the primary role of a neutral referee -- an enforcer and arbiter of the laws."<sup>29</sup>

But, in reality, as we have seen, the very act of setting the rules, either through legislation or interpretation and application of the statutes is an act of statecraft. The United States government is neutral neither in setting or enforcing the laws. It has an active interest in achieving political objectives: affecting the way in which foreign actors conduct themselves in the international trade system. The economic statecraft framework brings us to a conclusion which contradicts that reached by many commentators on trade remedy policy. Administered protection, as it now occurs, tends not to enhance stability in international economic relations, but to undermine it. Yes, the United States has an active interest in achieving political objectives via these instruments. But, the objectives that have been sought, to reiterate, are inconsistent with the legitimacy established by the international community.

Perhaps the best proof of the contradiction between the policies' supposed and actual aim, as Harvey Applebaum makes clear<sup>30</sup>, is the fact that American domestic and international competition policy are so hopelessly at odds. Rodney Grey captures the essential point.

"What is required by [United States] trade policy, what is profitable under trade policy, would, under [United States domestic] competition policy, bring substantial fines and prison sentences".<sup>31</sup>

If domestic competition policy and international competition policy are so at odds that those conducting the international version require special advice from the Justice Department about how to avoid liability under the domestic law, special statutory immunities from prosecution, and special tools, such as VRA's, by which the foreigner appears takes the blame for acting in restraint of trade, then something is clearly awry.

From the foregoing discussion it may be possible to infer that the economic statecraft that is in play is exercised by a single, or a single group, of rational actors. But, actually, the concept of statecraft does not necessarily require that the policy is created or applied by rational actors. Like most policy remedy policy emerges from a variety of sources and a variety of influences come to bear upon it. But, the important point is that in the end, regardless of the intentions of those exercising the policy, foreigners must

abide by whatever the policy actually is. The scope for being subject to the power wielded with the AD and CVD laws, whether intentional or not, is very wide. From the mere threat of invoking these laws to the application of a settlement order, foreigners must submit to the policy if they wish to maintain access to the lucrative United States market and/or a good official relationship with the United States. That is why it is so important to examine the actual policy content rather in addition to the policy-making process. But, it should also be clear that where there is discretion there is susceptibility to political pressures.

And so we return to the issue of political objectives. If all those involved in modifying the AD and CVD law are doing making what they believe to be the "best decisions possible" then it is probably necessary to more closely examine the perceptions which lead to these decisions.<sup>32</sup> The United States has supported the modern trade system due primarily to its conviction that competition constituted the best mechanism for international trade. Raymond Aron reminds us,

"one must accept that an international system is established for the same reason that any social or political system is created; actors enter into relations to advance particular sets of political, economic or other types of interests."<sup>33</sup>

There is now a perception in the United States that this mechanism has not always distributed the gains from international trade as beneficially to the United States as it might. This brings us back to the initial reason why the AD and CVD laws were brought into more active use. There was a perception in the United States that unfair foreign trade practices, not the competitive system itself, have been responsible for the perceived deterioration of the United States' position in the world economy.<sup>34</sup>

Perhaps, though, unfair trade practices have not been to blame. Perhaps, Robert Keohane is correct when he concludes that the economic order has ceased sustain the desired political order.<sup>35</sup> There are no guarantees that American industry will always "win" in the game of international trade. Or, it may be that the perception of decline needs to be re-examined. Recently some analysts such as Henry Nau<sup>36</sup> and John Makim<sup>37</sup>

have begun to criticize and cast substantial doubt upon this view. George Will is wise to note that "competitiveness requires as much soulcraft as statecraft".<sup>38</sup>

Certainly this issue of "perception" deserves greater attention. If the United States continues to "strengthen" and "enhance the enforceability" of the AD and CVD laws in the same manner as this dissertation has described, on the basis of perceptions of decline, or unfairness, the United States will be further undermining the foundation of the post-war international economic order.

This study of one small set of policies has shown us that trade laws can be applied with different severity, contingent upon the circumstances. Thus the economic statecraft framework lends credence to the view held by many trade negotiators, which Rodney Grey has best articulated.<sup>39</sup> The international trade system has not been as liberalized as the Common wisdom holds.

The majority view is, he says: that "under the leadership of the US the industrialized nations have been slowly but systematically reducing barriers to trade; the successive GATT negotiations resulting in agreed reductions in tariffs, and the increase in world trade, are called in evidence that this is the case. On this view, it is urged that the remedies for "unfair" trade, and the "safeguard" or "escape clause" mechanisms must be refined, because it is only if these are well designed and working effectively that it will be politically possible to negotiate further reductions in tariffs. Thus the cause of "free trade", or "freer trade", has been harnessed in the attack on "unfair" methods of competition in importation."<sup>40</sup>

This view has, it seems, been the prevailing view in the US Congress, as evidenced in the various hearings over the period say, from 1967 (after the Kennedy Round) to 1984 (the passage of the most recent trade legislation).<sup>41</sup>

"However, there has also been a minority view, to the effect that what has been happening has been not so much trade liberalization, but rather a widespread recourse to discrimination in trade policy and, in parallel, a shift from reliance on the tariff, (in the fashion of the early 1950's) to reliance on an armoury of other measures, which have been lumped together under the heading of "contingency protection".<sup>42</sup>

That the single most important member of the international trade community is paradoxically aiming to achieve objectives which are exactly opposite to those which the international community has agreed are legitimate poses a danger to the post-war international economic order. The danger is all the greater because, as mentioned in Chapter One, the United States is not the only country in which this paradox has developed. The European Community has been particularly adept in mimicking US



practice in this area.<sup>43</sup> Many other nations have seen how useful these laws can be and have implemented their own. Brazil has created and employed an AD law in the last few years. Australia and Japan too have begun using their remedy laws more than ever before. In essence, the United States' practices are being widely emulated, leading to a general deterioration in the international economic order. The endless pursuit of "unfairness" is perversely bringing about the dissolution of the framework of order, leaving a troubled, volatile world ahead of us, characterised by growing unilateralism, the US the teacher and others learning fast.

A comprehensive review of United States trade remedy law and policy is urgently needed. This has never been done. Over the last 100 years, since the creation of these two statutes, they have been clearly transformed into something which, if examined and understood, the United States probably does not want. But, a decision as to whether America wants to uphold the Post-War international economic order or not needs to be made one way or the other. It is important for the United States to confirm or refute its commitment to the principles of free trade and competition.

The international rules undoubtedly need to be reassessed as well. Perhaps the rules need to be strengthened by a more careful, narrower defining of operative terms. As Horlick, Quick and Vermulst note,

"It is clear that the lack of definition of the term subsidy in the Code and in the GATT may have negative effects: signatories are free to extend their definitions of domestic subsidies to include any new practice they find particularly disturbing."<sup>44</sup>

The same is unquestionably true of the terms in the Antidumping Code. In contrast, it is also argued that the international rules do more harm than good. For example, the Economist recently argued,

"The anti-dumping Code is already a protectionist's charter. Broadening it would be a crippling blow to free trade. Ideally the code should be struck out of the GATT; genuine cases of predatory behaviour (which are extremely rare) could be handled under existing competition rules."<sup>45</sup>

To continue along the current path is to hasten the deterioration of orderly international commercial relations. As EM Winslow had the prescience to see, the

breakdown of legitimacy is indicative of a transition not from free trade to protectionism but from order to its dissolution.<sup>46</sup>

By further understanding the role of power in trade policy and the political nature of trade policy we will be better equipped to prevent the diminution or dissolution of order. Apparently Keynes said of the kind of behaviour which used to be described as mercantilism, and which today is described as a new form of mercantilism (that is the way in which the subverted trade remedy measures are now used),

"We, the faculty of economists prove to have been guilty of presumptuous error in treating as a puerile obsession what for centuries has been a prime object of practical statecraft."<sup>47</sup>

Perhaps, with this new understanding of trade policy the truth in the following apt poem can be more greatly appreciated.<sup>48</sup>

### ANYONE FOR TENNIS?

*In the good old days we played,  
Like decent chaps, the game of trade.  
So, what the umpire said was that,  
According to the rules of GATT,  
Was taken, in the name of sport,  
As ruling sanctions out of court;  
And no ungentlemanly shout  
Disputed when the ball was out.*

*But now, alas, the urge to win,  
Has brought a breach of discipline;  
With all the seeded players free  
To denigrate the referee.  
And go for game, and set, and match  
By any rules their leaders hatch  
Which give their overseas accounts  
The better of the trading bounce.*

*For all the players it is vital  
That no one else should win the title,  
Though, what they can themselves produce,  
May get them, at the best, to deuce;  
So beggaring my neighbour's trade  
Is how the winning lobs are made,  
While players, point-by-point, dispute  
Who brought the game to disrepute.*

*Americans, for whom it's sin  
To play the game unless they win,  
Are most inclined to hedge their bet  
By doubling up the height of net;  
This stops the European ball  
From entering their court at all,  
While Europe threatens to retire,  
Or raise its own a sanction higher.*

*But both accuse the Eastern set  
Of dirty play around the net,  
And call the Japanese a menace  
Unworthy of the game of tennis;  
Or fight about the repercussions  
Of playing doubles with the Russians,  
In case the Eastern Bloc attack its  
Service game with Western rackets.*

*The players, to a man, deplore  
The ones who call the game a war;  
Insisting it is only played,  
Within the spirit of free trade,  
By gentlemen who don't resort  
To cheating in the name of sport;  
It's simply not the game for fools  
Who keep insisting on the rules!*

**Bertie Ramsbottom**

1. Robert Cox, "Social Forces, States and World Order: Beyond International Relations Theory" Millennium, Journal of International Studies, Vol. 10., No. 2, 126-155. Roger Tooze explains that critical theory is used to examine or provide alternatives to a given paradigm or perspective or framework of thinking. "Critical theory challenges the very "framework of action" that problem solving theory works within and takes for granted." Roger Tooze, "Perspectives and Theory: A Consumers' Guide" Paths to International Political Economy Susan Strange ed. (London: George Allen and Unwin, 1984) page 10.
2. Problem-solving theory, according to Roger Tooze, "takes the current framework of action as a given and derives meaning and policy from this context." Ibid.
3. This vision is often different from the one Americans actually live by at home, as we have seen.
4. Which is evident from the fact that the US sometimes maintains a similar policy or program as the ones it attacks abroad with the remedy laws.
5. Cordell Hull, The Memoirs of Cordell Hull (New York: Macmillan Co., 1948). page 355.
6. *ibid.*, page 365.
7. The OECD has posed the problem this way: "Thus, the basic issue in the application of these trade laws is the legitimacy or illegitimacy of various competitive advantages which foreign producers enjoy over domestic firms and the resultant harm to domestic industry". Competition and Trade Policies: Their Interaction (Paris: OECD, 1984) page 113.
8. Jacob S Dreyer, "Countervailing Foreign Use of Monopoly Power" Challenges to a Liberal International Economic Order Ryan C Amacher, Gotfried Haberler and Thomas Willett ed.s., (Washington, D.C.: American Enterprise Institute, 1979) page 346.
9. William Cline, "Summary and Introduction" Trade Policy in the 1980's William Cline, ed. (Washington, D.C.: Institute for International Economics, 1983) page 17.
10. Robert Baldwin, "The New Protectionism: A Response to Shifts in National Economic Power" The Protectionist Threat to World Welfare Dominick Salvatore ed. (New York: North-Holland, 1987) page 105.
11. Donald B Cameron and Susan M Crawford, "An Overview of the Antidumping and Countervailing Duty Amendments: A New Protectionism?" Law and Policy in International Business, Vol. 20, No. 3, 1988, page 499.
12. Noel Hemmendinger, "Shifting Sands: An Examination of the Philosophical Basis for US Trade Laws" International Trade Policy: The Lawyers Perspective J Jackson, Cunningham and Claude Fontheim, ed.s., page 2-5, Section 2.02.
13. *ibid.*
14. See Chapter 3, page 74, notes 75-77 *infra*.
15. The House Ways and Means Committee or the Senate Finance Committee.
16. Chinese whispers is the name of the childrens' game in which messages are passed from one person to the next. The person who gets the message last must say it out loud and the vast difference between the final and the original message is very funny.

17. Bill Boyarsky in his Los Angeles Times column. Reported in the International Herald Tribune, 9 July 1990.

18. There is no doubt that much more work needs to be done on the whole concept of competition in economic life. But it is not being suggested that the concept should be abandoned.

19. Brian Hindley "Protectionism in the GATT" Financial Times Friday June 7, 1991.

20. This raises an important problem which will be addressed further on in the conclusion. There may be conflicting sources of such statecraft. But, at least, this approach allows us to better understand the influence the contributing actors have. And, it allows us to see the politics, the political objectives, the policy is used to impose on foreign actors, which are submerged but inherent in the technical detail and the methods by which that detail is applied.

21. Michael J Finger "Ideas Count Words Inform" Issues in World Trade Policy RH Snape, ed. (London: Macmillan, 1986) page 264

22. Douglas R Nelson, The Political Structure of the New Protectionism Staff Working Paper No. 471, July 1981, page 3.

23. *ibid.*, page 17.

24. Michael J Finger, "Ideas Count Words Inform" page 265.

25. *ibid.*

26. *ibid.*

27. Gary N Horlick, "The United States Antidumping System" Antidumping Law and Practice: A Comparative Study John Jackson and Edwin A Vermulst ed.s., (New York: Harvester Wheatsheaf, 1990) page 126.

28. John Jackson, "Perspectives on the Jurisprudence of International Trade: Costs and Benefits of Legal Procedures in the United States" Michigan Law Review, 82 (1984) page 1583 cited by Vermulst, "The Antidumping Laws of Australia, Canada, the EEC and the USA: Have Antidumping Laws Become a Problem in International Trade?" Antidumping Law and Practice: A Comparative Study John Jackson and Edwin A Vermulst, ed.s., (New York: Harvester Wheatsheaf, 1990) page 442.

29. JH Jackson, RO Cunningham and Claude GB Fontheim, ed.s., International Trade Policy: The Lawyer's Perspective Committee on International Trade Section of the International Law and Practice, American Bar Association (New York: Mathew Bender, 1985) page 3-10, Section 3.04.

30. Harvey Applebaum, "The Interface of Trade/Competition Law and Policy: AN Antitrust Perspective" Antitrust Law Journal Vol. 56, Issue 2, 35th Annual Meeting, San Francisco California, August 10-12, 1987.

31. Rodney Grey, "Contingency Protection" page 1.

32. Or, if the political objective is to promote competition but the actual outcome is the restraint of competition then we need to carefully examine why the aim and the outcome are diverging.

33. Raymond Aron, Peace and War: A Theory of International Relations (New York: Doubleday, 1966) page 9.
34. See remarks by Robert Baldwin in Chapter Two, page 24 at note 14.
35. R Keohane, "The World Economy and the Crisis of Embedded Liberalism" in Order and Conflict in Contemporary Capitalism: Studies in the Political Economy of Western European Nations (Oxford: Clarendon Press, 1984).
36. Henry Nau, The Myth of America's Decline: Leading the World Economy into the 1990's (Oxford: Oxford University Press, 1990).
37. John Makim, "International Imbalances: the Role of Exchange Rates, Finance and the International Economy" American Express Bank Review Prize Essays Richard O'Brien and Ingrid Iverson ed.s., (Oxford: Oxford University Press, 1990).
38. Claude Barfield and John Makin, ed.s., Trade Policy and US Competitiveness (Washington: American Enterprise Institute, 1987).
39. Rodney Grey, "Trade Policy and the System of Contingency Protection in the Perspective of Competition Policy" unpublished paper commissioned by the OECD, Paris 1986.
40. *ibid.*, page 7.
41. *ibid.*
42. *ibid.*, page 8.
43. For an explanation of EC AD and CVD policy see Beseler, JF and Williams, AN, Anti-Dumping Law and Anti-Subsidy Law: The European Communities (London: Street and Maxwell, 1986) and Edwin A Vermulst, Antidumping Law and Practice in the United States and the European Communities (Amsterdam: North-Holland, 1987) and John Jackson and Edwin A Vermulst, ed.s., Antidumping Law and Practice: A Comparative Study (New York: Harvester Wheatsheaf, 1990).
44. Gary Horlick, R Quick, E Vermulst, "Government Actions Against Domestic Subsidies, an Analysis of the International Rules and an Introduction to United States Practice" 1 Legal Issues of European Integration 1986, page 22.
45. "Repeal the Protectionist's Charter" Economist June 15, 1991, page 20.
46. See Chapter Three, page 75, notes 82-83 *infra*.
47. Quoted by Charles Wilson, Mercantilism (London: Routledge and Kegan Paul for the Historical Association, 1958) page 9.
48. Cited by Sidney Golt, Trade Issues in the Mid-1980's (London: British-North America Committee, 1982) page vii. The poem was written by Ralph Windle and reproduced courtesy of the author and the editor of the Financial Times.



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