

**The Politics Behind the Application of Antidumping Laws to  
Nonmarket Economies:  
Distrust and Informal Constraints**

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## **Part I. Introduction**

### ***Puzzle:***

"Trade not aid [is] the ultimate guarantor of economic growth in the former Soviet Union."

Vice President Gore, "The United States and Russia: A Vision for the Future," remarks at the U.S. Military Academy West Point, October 17, 1995.<sup>1</sup>

Official U.S. policies stress the important role for trade in supporting the political and economic reform efforts in formerly Communist countries. The connection between trade and development is explicitly recognized by the U.S., EU and Japan in policy statements such as, "We recognize the progress of many countries in transition and their need for improved market access."<sup>2</sup> Even before the dissolution of the Soviet Union, U.S. statesmen publicly proclaimed their commitment to help the transition efforts in Communist countries. Starting with Bush and continuing through the Clinton administration, the normalization of economic and trade relations with China, Eastern Europe and the former Soviet Union has been a recurrent theme.<sup>3</sup> At various G-7 meetings, the economic and political developments of formerly Communist countries are publicly lauded, and programs are initiated to assist with their development efforts. These public affirmations of support sharply contradict the manner in which formerly Communist countries are treated under Western trade laws.

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<sup>1</sup> In *U.S. Department of State Dispatch*, October 30, 1995, Vol. 6, No. 44, p. 783.

<sup>2</sup> "Halifax Summit Communiqué: Creating Opportunities Through Open Markets," *U.S. Department of State Dispatch Supplement*, July 1995, Vol. 6, No. 4, pp. 9-10.

<sup>3</sup> President Bush, "U.S. Assistance to the Soviet Union, Statement at a White House News Conference, Washington D.C. December 12, 1990," *U.S. Department of State Dispatch*, December 17, 1990, Vol. 1, No. 16, p. 331; and President Clinton, "The U.S. and Central and Eastern Europe: Forging New Partnerships: Remarks to Plenary Session of the White House Conference on Trade and Investment in Central and Eastern Europe, Cleveland, Ohio, January 13, 1995," *U.S. Department of State Dispatch*, January 16, 1995, Vol. 6, No. 3, pp. 27-31.

There are various Western trade remedy laws which can address unfairly traded exports from nonmarket economy countries.<sup>4</sup> This paper will focus primarily on U.S. antidumping laws (AD laws), because they are the main source of discriminatory trade protection against NMEs. The U.S. treats nonmarket economies (NMEs)<sup>5</sup> differently than other developing countries under antidumping laws. I will argue this difference amounts to discriminatory treatment against NMEs. NMEs are subject to different formal rules and informal procedures than other types of developing countries, based on the assumption that NMEs pose an extraordinary threat to Western industries.

Since launching market-oriented reforms, most transitional states have both expanded their volume and diversified their composition of trade with the West. Their continued ability to penetrate Western markets represents a leading barometer of successful reform and international integration. However, their necessary reliance on price to maintain competitiveness renders their exports increasingly vulnerable to Western administrative trade action. There is a feeling of discontent among trade officials in Central and Eastern Europe and the countries of the Former Soviet Union at what they perceive as the undermining of their export performance by

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<sup>4</sup> These are numerous trade remedy laws which affect exports from NME countries including: the U.S. antidumping laws, targeted at imports priced at less than fair value; countervailing duty laws, concerning suspected state subsidization {Title VII of the Tariff Act of 1930 as amended, 19 United States Code (U.S.C.) Annotated, Customs Duties, 19 §1671 et. seq. (1982)}; Section 406 of the Trade Act of 1974--market disruption by imports from Communist countries (As amended by section 1411 in the Omnibus Trade and Competitiveness Act of 1988, 19 U.S.C. §2411); Section 201 of the Trade Act of 1974--the escape clause, provides relief to seriously injured domestic industries from fairly traded imports {1974 Act, *supra* note 2, §201, 19 U.S.C. §2251 (1982 & Supp. IV 1986)}; Section 301 of the Trade Act of 1974--dispute resolution, designed to enforce U.S. rights under trade agreements and combat unfair trade practices (Ch. 1, Title III of Trade Act 1974 as amended, 19 U.S.C. §2411); and Section 337 of the Trade Act of 1930--Intellectual Property Rights protection (19 U.S.C. §1337).

<sup>5</sup> Nonmarket economy is the official term used by the U.S. Department of Commerce to describe formerly Communist countries. These countries are now interchangeably referred to as transitional economies or nonmarket economies. In this paper I will use the terms interchangeably. Nonmarket economy is both an economic and political designation. NMEs include: Albania, Armenia, Azerbaijan, Belarus, Bulgaria, Czech Republic, China, Estonia, Georgia, Kazakhstan, Kyrgyz Republic, Latvia, Moldova, Romania, Russia, Slovak Republic, Tajikistan, Turkmenistan, Ukraine, and Uzbekistan.

antidumping actions and "discriminatory trade policies."<sup>6</sup> These countries perceive antidumping actions as politically motivated tools used to combat exports in which they possess a comparative advantage.<sup>7</sup> This discontent reflects the contradiction between the West's stated policy objectives of promoting development in the region and its actual trade policies.

There are two puzzles to be addressed. First, is the "different" treatment of NMEs discriminatory? The U.S. government and the World Bank, after reviewing U.S. trade laws as applied to NMEs, have determined that this different treatment is not discriminatory. I reject the World Bank's findings, and contend that the treatment of NMEs by the U.S. *is in fact* discriminatory. Second, why does the U.S. continue to discriminate against imports from NMEs? I contend that the manner in which transitional economies are treated under existing U.S. trade remedy laws reflects credible commitment problems. The U.S. distrusts the intentions of NMEs and therefore subjects them to different rules and procedures. These raise the cost of trade and prevent the establishment of credible commitments. I examine two cases, the Market Oriented Industry Test and the Market Status Test in order to demonstrate how distrust affects the informal procedures and norms surrounding the application of AD laws. In sum, America's *de facto* policies toward NMEs contradict its stated policy objectives because of the persistent distrust of formerly Communist countries.

## **Hypotheses**

### ***Institutional Approach***

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<sup>6</sup> Ibid., 130 and Chernomyrdin, "Chernomyrdin Criticizes U.S. Trade Policies: Business Speech Before U.S. Executives, San Francisco," *ITAR-TASS*, June 24, 1997.

<sup>7</sup> The Russian fertilizer industry was vocal about the politicization of antidumping actions at a conference on trade and the transition process, documented in OECD 1996, 20.

A World Bank study recently vindicated EU and U.S. antidumping policies toward NMEs. After reviewing the application of unfair trade laws to NMEs, this study concluded that the treatment of NMEs is fair, albeit different.<sup>8</sup> For example, in spite of the fact that China's exports face more antidumping cases than imports from other countries, and in spite of the higher than average dumping margins on Chinese exports, the study concludes this not a result of China being treated as a NME. In fact, the report argues that because China still exports to the US, this is proof that the laws are not excessively onerous.<sup>9</sup>

I disagree with the World Bank's conclusions. The difference in adjudication of NME antidumping cases results in more onerous information requirements, less transparency, and more disregard for the market conditions operating in these economies than in cases involving similarly situated developing countries. Imports from NMEs account for a disproportionate number of the West's "unfair trade" cases and a disproportionate share of trade protection. For example, from 1986-1992 in the case of the U.S., NMEs accounted for an average of 20% of AD cases but only 3% of total imports. Recent trade data for the U.S. demonstrates that there is no relationship between volume of imports and AD cases. (See Chart 1).

Using a cross group comparison of AD cases by region from 1980-1998, NMEs have had a higher percentage of total AD cases than other comparable developing country groupings. (See Chart 2). Moreover, there is a statistically significant difference in the ratio of imports to AD cases across various developing country groupings, suggesting that NMEs *are* treated unfairly (Chart 3). The costs of this "different" treatment are substantial. It is estimated that AD duties cost Russia \$500 million-\$1 billion annually. In addition, the duties resulting from AD

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<sup>8</sup> Ehrenhaft, Hindley, Michalopoulos, Winters, *Policies on Imports from Economics in Transition: Two Case Studies. The World Bank: Studies of Economies in Transformation*. (Washington D.C.: The World Bank, 1997).

<sup>9</sup> Ibid., 26-8.

investigations regularly exceed 100% of the value of imports in the case of trade with China.<sup>10</sup> In the recent AD case against Russian steel, Russia opted for a 70% reduction in steel exports to stop the case which seemed preferable to the estimated 200% tariff levels.<sup>11</sup>

In sum, I reject the World Bank's assessment and argue that AD laws are applied unfairly to NMEs. The World Bank analysis constitutes the null hypothesis, namely that the U.S. does not discriminate against trade with NMEs. In contrast, my hypothesis is that the treatment of NMEs under U.S. trade laws is both different and discriminatory. The source of this discrimination rests on credible commitment problems stemming from a distrust of NMEs' intentions and incentives. NMEs are not simply developing countries, but *formerly Communist countries*. In an interview, an analyst at the Department of Commerce revealed that even if NMEs could pass the same formal criteria as other developing countries, NMEs would still be treated differently because there is a *presumption* that NME trade activities are different and threatening.<sup>12</sup> Developing countries are not subject to the same microscopic scrutiny as NMEs because their intentions are not distrusted. Active distrust of NMEs impedes the development of credible trade commitments.

This paper takes an institutionalist approach to analyzing the application of U.S. trade laws to NMEs. Like many other institutionalists, I examine both informal and formal constraints on behavior, as well as the role of ideas in affecting political outcomes.<sup>13</sup> I define institutions as a "set of rules, compliance procedures, and moral and ethical behavioral rules designed to constrain

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<sup>10</sup> Leonard Santos and Thomas Vakerics, "Chinese Imports Face Tough Antidumping Rules," *The National Law Journal*. September 19, 1994, p.C13.

<sup>11</sup> Thomas Donlan, "Stand Up to Steel: Protectionism Puts Rust in the Economy," *Barron's*. March 1, 1999, p. 47; and "US-Russia Steel Battle Brewing," *Radio Free Europe/Radio Liberty Newslines Reports*, October 10, 1998.

<sup>12</sup> Discussion with Analyst at Import Administration, International Trade Administration, U.S. Department of Commerce, April 7, 1993.

<sup>13</sup> Peter Hall and Rosemary Taylor, "Political Science and the Three New Institutionalisms," *Political Studies*, Vol. 44 (1996), 938-9.

the behavior of individuals in the interests of maximizing the wealth or utility of principals."<sup>14</sup> The use of both formal rules, such as laws and other codified regulations, as well as informal rules and procedures, such as conventions, norms of behavior, culture, and ideology, is critical to understand the application of unfair trade laws to NMEs.<sup>15</sup> Incorporating informal constraints into the analysis will help to explain both the incremental changes in policy and the tenacity of inefficient institutional procedures.<sup>16</sup>

### ***Alternative Hypotheses***

There is very little academic literature on the source of trade discrimination against NMEs. As such, there is not a body of alternative hypotheses to which I am responding. However, there are general economic and political economy theories from which informed alternative hypotheses can be derived. I will briefly explain and refute four potential alternative hypotheses which are grounded in trade theory and IPE literature. These include: institutional inertia, benign neglect, interest group politics, and sunset industry bias. There are empirical problems with all of these hypotheses. I argue that none of these hypotheses is adequate in explaining the treatment of NMEs.

***Institutional Inertia:*** The institutional inertia hypothesis argues that discrimination against NMEs is a vestige from when these countries were Communist and did pose an extraordinary threat to the West. It is difficult to change bureaucratic procedures and laws, therefore there is often a lag while bureaucracies try to catch-up with changes in the international system. This hypothesis seems wrong. The problem is not that trade related bureaucracies have been unable to

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<sup>14</sup> Douglass C. North, *Structure and Change in Economic History* (New York: W.W. Norton & Company, 1981), pp. 201-2.

<sup>15</sup> Hall differentiates informal and formal institutional constraints in these terms. See Peter Hall, *Governing the Economy: The Politics of State Intervention in Britain and France* (New York: Oxford University Press, 1986), p. 19.

change to reflect the market reforms in transitional economies. On the contrary, the U.S. has continued to adjust the application of its AD laws to NMEs since the beginning of reforms in the region. In the U.S. neither the laws nor the procedures remain the same. The U.S. has introduced a dizzying array of new rules and procedures, including the Market Oriented Industry Test, Factors of Production Methodology, Multiple Surrogates Test, and *De Jure/De Facto* Industry Tests, to name a few. The puzzle is why, *in spite of the changes* in transitional economies, does the U.S. maintain and perpetuate through *continued innovation* inefficient methods of administering AD laws to imports from NMEs.

***Benign Neglect:*** This hypothesis suggests that decision-makers in the U.S. are unaware of the potential problems with the application of U.S. trade laws. Discontinuity between trade administrations and the executive results in contradictory policy. I do not think there is any merit to this hypothesis. The discriminatory aspects of AD laws are the subject of vocal international discontent. Trade officials in Central and Eastern Europe and the Former Soviet Union have publicly criticized the West's "discriminatory trade policies," and have accused the West of using AD laws as trade tools to undermine industries in which these transitional economies have a comparative advantage.<sup>17</sup> There are routine reviews of trade policies in the U.S. Both trade policy administrators and political leaders are aware that a problem exists.

***Interest Group Politics:*** This hypothesis argues that the way NMEs are treated is a function of the power of interest groups lobbying the government for protection. Domestic industries can initiate AD cases, and there is an incentive for them to initiate cases against NMEs because of the ease of winning and the high resulting antidumping margins. However, as an explanation for discriminatory treatment of NMEs, this hypothesis appears weak given contrary evidence with respect to Countervailing Duty cases. The government has protected NME exports

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<sup>16</sup>Douglass North, *Institutions, Institutional Change and Economic Performance* (Cambridge: Cambridge University Press, 1990) pp. 6-9.

<sup>17</sup> Victor Chernomyrdin, "Chernomyrdin Criticizes U.S. Trade Policies: Business Speech Before U.S. Executives, San Francisco," *ITAR-TASS*, June 24, 1997.



from countervailing duty cases, despite the vociferous opposition by domestic industries to this practice. In spite of interest groups lobbying for countervailing duty protection, the government has stood firm on its policies. Moreover, at times the U.S. government initiates cases even when domestic industries are not looking for protection, or when protection might harm domestic industries that use imported goods as part of the overall production process. In some cases, like steel or petrochemicals, special interest groups may force high profile cases into the spotlight, but in others like garlic, preserved mushrooms, bicycles, golf carts, and baby dolls there is no powerful interest group lobbying the government for protection. In addition, Goldstein in an analysis of U.S. trade laws has also discredited this hypothesis.<sup>18</sup> In sum, domestic industries do not explain the patterns of trade protection.

***Sunset Industries Bias/Sectoral Analysis:*** This is the strongest alternative hypothesis. This theory contends that NME exports tend to compete with highly sensitive sectors in the U.S., and that this accounts for the unusually high number of AD cases filed against NMEs. It is not the NME status which causes “unfair” treatment, but rather the sectoral composition of trade. Some preliminary studies of EU trade with Eastern Europe have refuted this hypothesis.<sup>19</sup> Also this hypothesis is unable to account for the extraordinarily high antidumping margins slapped on NME exporters. For example, in the recent steel case against Japan, Brazil and Russia, even though all three were investigated together, under the same international economic conditions, the Russian dumping margins were estimated to be substantially higher. Japan’s AD duties ranged from 25% to 67.5%, Brazil’s AD duties from 50% to 71% and Russia’s estimated duties were more than 200%.<sup>20</sup> Since Russia pulled out of the investigation and decided to “voluntarily” limit steel exports, a final actual dumping margin was not determined. However, the estimates suggest a substantial differential in the treatment of the three countries, which results from the different

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<sup>18</sup> Judith Goldstein, *Ideas, Interests, and American Trade Policy* (Ithaca: Cornell University Press, 1993).

<sup>19</sup> P.K.M. Tharakan, “The political Economy of antidumping undertakings in the European Communities,” *European Economic Review*. 35 (1991), pp. 1341-1359.

<sup>20</sup> Donlan, C13.

method of calculating dumping in cases involving NMEs. In sum, while the sunset industries hypothesis may complement aspects of my institutional hypothesis, it is not able to account for the size of dumping margins against NMEs nor the presence of AD cases in sectors which do not compete with domestic industries.

## **Part II. Interests, Institutions, and Transaction Costs**

There are two primary agents involved in the applications of antidumping laws to transitional economies. While this is an oversimplification of the foreign and domestic actors who are either actually affected by the laws or who affect the form and implementation of the laws, I think it adequately captures the process of AD trade law implementation. The two primary agents in this analysis are the International Trade Administration (ITA) and the domestic producers in the Nonmarket Economy (NME). This section will explore the interests and constitutive elements of these two actors. (See Chart 4).

### ***Interests: The International Trade Administration***

The ITA is an agency within the U.S. Department of Commerce tasked with determining if there is dumping and assessing preliminary and final dumping margins. The stated objectives of the ITA are as follows: “to encourage assist and advocate U.S. exports; to ensure U.S. business has equal access to foreign markets; and to enable U.S. businesses to compete against unfairly traded imports, and to safeguard jobs and the competitive strength of American industry.”<sup>21</sup> It is this last component of the mission statement on which this paper will focus.

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<sup>21</sup> Ambassador David L. Aaron, “Missions Statement from the Under Secretary for International Trade,” International Trade Administration Web Site, March 1, 1998 ([http://www.ita.doc.gov/ita\\_home/itaabout.html](http://www.ita.doc.gov/ita_home/itaabout.html)).

The ITA's mission is to administer U.S. trade laws to protect domestic producers of like products from the *unfair* trading practices of foreign competitors. The ITA is not the only agency involved in the application of unfair trade laws, however it plays the critical role in the application of trade laws to nonmarket economies.<sup>22</sup> The ITA receives petitions from domestic producers to initiate AD and countervailing duty investigations in order to discern if goods are in fact being traded fairly. The ITA must also respond to the changing policy agendas set by the Executive branch. The interests of these domestic producers and the executive can be complementary or conflictual. The ITA must reconcile these possibly competing policy signals in administering trade laws.

The domestic producers of like products want protection from foreign imports. The domestic competitors, by and large, do not want to change the present application of the AD laws because they materially benefit from the status quo. Domestic producers always benefit from AD cases either due to positive dumping determinations or the "harassment effect".<sup>23</sup> Dumping margins are generally much higher against imports from NMEs than market economies.<sup>24</sup> It has also been demonstrated that the mere filing of AD petitions may disproportionately inhibit NME exporters.<sup>25</sup> This "harassment effect" persuades the exporter to restrict sales or to raise prices, both because the NME has a low probability of winning a case, and to defend against dumping

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<sup>22</sup> The ITA determines the dumping margin which is the most important component of the administration of trade laws. The U.S. International Trade Commission (ITC) determines separately if the goods in question are causing or threaten to cause material injury to the domestic industry. If the goods are both injurious to domestic producers and the goods are being dumped, then the Department of Commerce empowers the Customs Service to assess a duty. U.S. Department of Commerce International Trade Administration, *United States Antidumping and Countervailing Duty Legislation* (Washington, D.C.: Department of Commerce, January 1991).

<sup>23</sup> See Robert Staiger and Frank Wolak, "Measuring Industry-Specific Protection: Antidumping in the United States," *Brookings Papers: Microeconomics*. (Washington, D.C.: The Brookings Institution, 1994), and comments and discussion from the Brookings conference for a discussion of these various effects.

<sup>24</sup> Discussion with Analyst at Office of Antidumping Investigations, Import Administration, at the International Trade Administration, U.S. Department of Commerce, May 27, 1993.

charges is prohibitively expensive. In the recent Russian steel case, the mere filing of the case caused Russian exports to fall by 90%.<sup>26</sup> In a case against an Hungarian exporter of sulfanilic acid, the Hungarian side had to drop its defense against AD charges because it could no longer afford the legal fees.<sup>27</sup> This fact is well understood by domestic competitors. Therefore just the threat of an AD investigation prompts many NME exporters to reduce or halt exports.<sup>28</sup> Other academics have suggested that the political and technical ease of demonstrating NME dumping accounts for the disproportionate number of complaints against E.E. producers.<sup>29</sup> Therefore the material interests of domestic competitors are advantaged by the present application of the AD laws. In this model I argue that domestic producers want to retain the status quo.

In contrast, the Executive has competing and possibly conflicting interests regarding foreign trade. On the one hand, the President has clearly stated U.S. policy objectives for the transitional economies in E.E. and the N.I.S. “Trade as aid” is an important part of the policy agenda regarding trade relations with transitional economies. On the other hand, the Executive wants to protect and possibly advantage domestic consumers and producers. President Clinton’s speech warning that the U.S. would not tolerate the “flooding of our markets” with low cost imports from Russia that threaten American jobs is simply another example of the tightrope the

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<sup>25</sup> Stuart Brown and Deborah Haas-Wilson. "Centrally Planned Economy Vulnerability to Antidumping Protection," *Comparative Economic Studies*, Vol. 32, No. 4, (Winter) 1990.

<sup>26</sup> “Russia Agrees to Limit Steel Shipments, Avoiding Antidumping Duties by U.S.,” *The Wall Street Journal*. February 23, 1999.

<sup>27</sup> Personal interview with Analyst at International Economic Policy Office of Eastern Europe and Soviet Affairs, United States International Trade Administration, April 16, 1993.

<sup>28</sup> For example, in a recent case against Ukrainian exporters, the Government of Ukraine agreed to restrict sales to the U.S., and therefore suspended the AD duty investigation prior to a final determination of dumping. See *suspension of Antidumping Duty Investigation: Certain Cut to Length Carbon Steel Plate from Ukraine*, 62 Fed. Reg. 61766, November 19, 1997.

<sup>29</sup> Andrzej Olechowski. *Chemicals From Poland: A Tempest in a Teacup. Policy, Research, and External Affairs Working Papers Series* (Washington, D.C.: The World Bank, Country Economics Department, October 1990) 8. This study specifically referred to the EC’s unfair treatment of NMEs in AD investigations. The ITA and the EC have similar methods in place to determine and punish dumping from NMEs.

Executive must walk between supporting reform efforts in NMEs while not sacrificing domestic industries to do so.<sup>30</sup> The Executive's policy interests therefore are potentially conflicting. Trade as aid might not necessarily mean fair trade, and it certainly does not mean preferential treatment for domestic producers.

Since the ITA is officially charged with administering codified trade rules according to formal procedures and regulations, it would appear that the ITA does not have much margin in which to reconcile the possibly conflicting interests of domestic producers and the Executive. However, this paper will demonstrate that the laws are structured to allow the ITA discretionary input. Therefore the ITA is not simply the administer of the laws. It has its own institutional agenda and it receives input from domestic producers and the Executive, from which it enjoys limited autonomy. In sum, the ITA is a partially autonomous actor in the administration of AD laws.

### ***Interests: Nonmarket Economies***

As already mentioned, NMEs and transitional economy designations are used interchangeably. NMEs/transitional economies refer to Communist countries who have enacted political and economic reforms, and centrally planned or Communist countries is the designation for countries prior to the 1989 reform efforts in CEE/FSU. In this paper I do not differentiate the interests of the NME export firm from the interests of the NME state. I assume that the difference between the preferences of the two actors is nominal for the purposes of the discussion. While it may be a contentious assumption that the interests of the exporter and the leaders of transitional economies are synonymous in the long term, I do not think this assumption is problematic in the

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<sup>30</sup> David Sanger, "Clinton Warns U.S. Will Fight Cheap Imports," *New York Times*. November 11, 1998, C4.

short term. The transitional economy exporter is very concerned with establishing a reputation as a reliable supplier. This is particularly important for exporters, since they are trying to shift the direction of trade away from former Eastern Bloc trading partners and toward Western markets. The laws are so punitive and effectively enforced that *intentional* dumping is not a policy preference of most transitional economy exporters. Defection is noticed and punished. Transitional economy exporters expect iterated trade interactions with the U.S., thereby reducing the incentive for single shot defection. Therefore, I argue that developing a reliable reputation and good business contacts is the policy preference of transitional economy exporters in the short term.

The preferences of transitional economy exporters correspond to the short term interests of the transitional economy leaders, who are trying to gain EC membership, or admission to NATO, or the World Trade Organization (WTO), or international funding, etc.<sup>31</sup> There are a plethora of external constraints on the preferences of transitional economy leaders, forcing them to consider long term economic and political relations rather than short term gains. In sum, I contend that the short term preferences of transitional economy exporters and leaders are roughly equivalent and can be assumed as the same for the purposes of this study.

The primary concern of this section should not be whether transitional economy countries and exporters have similar preference structures, but whether the preference orderings of Communist era exporters differ from the preferences of transitional economy exporters. It was widely believed that prior to market oriented reforms, Communist countries had incentives to

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<sup>31</sup>None of the republics of the Former Soviet Union are members of the WTO at this time. These countries have observer status and have applied for membership. The only Eastern bloc countries to receive WTO membership include: Poland, Hungary, the Czech Republic, the Slovak Republic, Bulgaria, Slovenia, and Romania. Latvia and the Kyrgyz Republic are soon to become members but this should not affect if they are treated as market or nonmarket under U.S. trade laws. See World Trade Organization Web Site and Membership List, [www.wto.org](http://www.wto.org).

dump exports in order to unload occasional surpluses in stock, to overcome market entry handicaps, to absorb discriminatory tariff and non-tariff barriers, to fulfill state dictated export plans, and to meet shortages of foreign exchange.<sup>32</sup> These problems were often highlighted in Congressional Reports and Commerce Department reports. When E.E. and the N.I.S. started to experience severe external debt problems in the 1970's and 1980's, dumping exports was a way to quickly raise hard currency reserves and temporarily ameliorate balance of payments deficits.<sup>33</sup> Moreover, it was assumed that the centrally planned economy enjoyed numerous unfair trade advantages, which necessitated special laws to monitor trade with those countries. The trade advantages included: a Ministry of Foreign Trade which helped support and direct trade and exercised a monopoly on foreign trade; multiple exchange rates; domestic price controls; and government credit facilities.<sup>34</sup> The domestic structure of the economy not only gave centrally planned economies a purported unfair trade advantage but also gave them an incentive to dump goods. In sum, the West believed that centrally planned economy exporters had the means and the motive to dump products.

Given the domestic and international changes since 1989, have the structural incentives to dump changed? Is there a difference between centrally planned/Communist countries and NME/transitional economies? Given the altered characteristics of their domestic economies and new economic priorities, do imports from transitional economies pose an unusual threat to the welfare of import competing producers or the importing nation?

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<sup>32</sup> Paul Marer, "United States Market Disruption Procedures Involving Romanian and Other Centrally Planned Economy Products, With Policy Recommendations," in Marvin Jackson and James Woodson, Jr. (eds). *New Horizons in East-West Economic and Business Relations* (New York: Columbia University Press, 1992), p.129.

<sup>33</sup> Egon Neuberger and Juan Lara, *The Foreign Trade Practices of Centrally Planned Economies and Their Effects on U.S. International Competitiveness* (Washington, D.C.: The National Planning Association, 1977), pp. 29-30.

Since most transitional economies have received MFN treatment, there is no need to dump goods to absorb the costs of discriminatory tariffs. Additionally foreign trade organizations have become trade facilitators not directors, and the foreign exchange maximizing exporters of the past are being supplanted by profit maximizing firms operating under hard budget constraints. Nonetheless, within the continuum of reforming economies, some vestigial systemic features of NMEs remain. Transitional economies lack a reputation for quality goods, need to break into new markets, and require large amounts of hard currency. All of these factors contribute to the desire to price goods cheaply. However, all developing countries and many developed countries price exports cheaply in order to break into new export markets. As such, these incentives are not defining characteristics of transitional economies and do not constitute a disproportionate threat to importing nations. Economic and political structures in these countries have changed dramatically, and so have the structurally determined preferences. The institutional structure which previously provided a means and a motive to dump has been dismantled. Therefore, one must conclude that the incentives to dump of NMEs do not differ from other developing countries and therefore do not require extraordinary trade remedy laws.

### ***Institutions***

U.S. antidumping laws and related implementing regulations constitute the formal institutional constraints in this analysis. As per the operational definition of institutions, these laws are designed to reduce uncertainty and detect and punish non-compliance.<sup>35</sup> They include formal and informal institutions in the sense that they are codified rules and informal procedures

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<sup>34</sup> See Paul Gregory and Robert Stuart, *Soviet Economic Structure and Performance* (New York: Harper Collins Publishers, 1990), especially chapter 7 and 8, pp. 163-250; and Peter Murrell, *The Nature of Socialist Economies* (Princeton: Princeton University Press, 1990), especially chapter 3, pp. 25-42.



that dictate both the "rule of the game" and punishment for rule transgression. The ITA maintains an elaborate arsenal of instruments to measure compliance with the rules. The Department of Commerce backed by the U.S. Congress are credible enforcers of punishment in the event of rule transgression. This section will discuss in detail the composition and implementation of the formal rules of the "trade game."

Dumping is the selling of exports at less than fair value. The problem arises in determining what constitutes "fair value." U.S. law provides several ways to determine if dumping has occurred. The preferred method is to compare the U.S. price of imported merchandise to the home market price.<sup>36</sup> If the home market price is less than the U.S. price then dumping is occurring. When home market sales do not exist, the export price to a third country is used to determine the foreign market value.<sup>37</sup> If these two methods are not applicable the constructed value (CV) method, a valuation of production costs including quantity of raw materials, amount of labor, and amounts of energy and other utilities consumed, is used.<sup>38</sup> The amount by which the foreign market value is less than the U.S. price is the dumping margin, and this is used to assess a duty to offset the sale at less than fair value.<sup>39</sup> If dumping can be proven and the dumped good either causes material injury or threatens to cause material injury, an AD margin can be assessed to redress the unfair trade practice.

These methods of determining the foreign market value of imports from market economies have never applied to centrally planned economies, where domestic prices failed to reflect relative

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<sup>35</sup> North, *Institutions, Institutional Change and Economic Performance*, pp. 3-6.

<sup>36</sup> U.S. Department of Commerce International Trade Administration, *Summary of Procedures for Antidumping Fair Value Investigations Under Title VII of the Tariff Act of 1930, As Amended* (Washington, D.C.: Department of Commerce, January 1991), p. 2.

<sup>37</sup> U.S. Department of Commerce International Trade Administration, *United States Antidumping and Countervailing Duty Legislation* (Washington, D.C.: Department of Commerce, January 1991) p. 2.

<sup>38</sup> *United States Code Annotated, Customs Duties, 19* § 1677b (e). Foreign Market Value.

scarcities and were divorced from world prices by a system of price equalization. Instead, alternate procedures have been devised, in part reflecting the traditional Western presumption that NMEs pose a special threat to import competing producers and by extension to the importing country as a whole. This presumption of threat and distrust of the motives of NMEs constitutes one of the informal constraints on behavior and will be addressed at length later in this paper.

With the Polish golf cart case, the ITA began to employ a novel surrogate methodology to calculate the foreign market value for imports from NMEs. Having selected a surrogate market-economy country that is a "significant producer of comparable merchandise and at a comparable level of economic development,"<sup>40</sup> the ITA values the physical factors used in producing the allegedly dumped good in the surrogate country.<sup>41</sup> The resulting constructed value is converted into dollars at the surrogate's exchange rate to arrive at a dollar foreign market value. In 1988, the OTCA adopted this "factors of production methodology," as the preferred method for determining the foreign market value of imports from NMEs even when a third country producer exists.<sup>42</sup>

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<sup>39</sup>U.S. Department of Commerce International Trade Administration, *Glossary of Antidumping Terms and Phrases* (Washington, D.C.: Department of Commerce, January 1991) p. 4.

<sup>40</sup> *Final Determination of Sales at Less Than Fair Value: Oscillating Fans From the People's Republic of China*, 56 Fed. Reg. 60969, October 25, 1991.

<sup>41</sup>The factors of production are valued using published information on factor costs from the selected NME country's surrogate(s). These include labor, energy, and raw material costs. Separate profits (8%) and expenses margins (10%) are also added (see *Final Determination of Sales at Less Than Fair Value: Sparklers From the People's Republic of China*, 56 Fed. Reg. 20588, May 6, 1991).

For example, in the Polish golf cart case, Spain was selected as a comparable surrogate and it was determined that the Polish industry was not dumping golf carts (See Holzman). In recent cases against Romania, Indonesia and Thailand were selected as surrogates (see *Tapered Roller Bearings and Parts thereof, Finished or Unfinished, from Romania; Final Results of Antidumping Duty Administrative Review*, 62 Fed Reg. 31075, June 6, 1997). Recent surrogates for Ukraine include Brazil, Tunisia, Peru, Turkey, and Poland (see *Notice of Final Determination of Sales at Less Than Fair Value: Certain Cut-to-Length Carbon Steel Plate from Ukraine*, 62 Fed. Reg. 61754, November 19, 1997.) Recent surrogates for China include Pakistan, Sri Lanka, Egypt, and Indonesia (see *Notice of Final Determination of Sales at Less Than Fair Value: Collated Roofing Nails from the People's Republic of China*, 62 Fed Reg. 51410, October 1, 1997).

<sup>42</sup> Wendell L. Willkie, chairman. "The 1988-89 Department of Commerce Study on the People's Republic of China and its Implications for Economies 'In Transition'". In *The Department of Commerce Speaks: 1990 The*

A new standard for obtaining and using information on factor inputs has been established to try to increase the consistency and predictability of the investigations. Prices paid by NME manufacturers for inputs imported from market economies are used as a source of information on factor values if there is convincing proof that the information is valid.<sup>43</sup> Then, public information from the first choice surrogate is the preferred source of information, next unpublished information from the first choice surrogate is used, then published information from the second choice surrogate is used and so forth.<sup>44</sup> However, if information is unavailable from the surrogates or the information is "questionable," supplemental factor value information is used and this may be obtained from any source. Obtaining accurate information is quite difficult and this substantially raises the transactions costs.

### Transaction Costs

Transaction costs are the costs of measuring, monitoring and enforcing contracts, and agreements.<sup>45</sup> The transactions costs of the present implementation of AD laws to NMEs are quite high. The costs of monitoring trade with NMEs, measuring AD margins, and enforcing AD duties are particularly onerous. Because of the extra steps involved in adjudication of NME cases, such as determining surrogates, and rendering Market Oriented Industry (MOI), *de jure/de facto*, and NME determinations (to be discussed later), the ITA spends more time and money administering AD laws in NME cases than other types of AD cases.

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*Legal Aspects of International Trade Practicing Law Institute*, Washington, D.C., Corporate Law and Practice: No. 669 (1990), pp. 503-527.

<sup>43</sup> *Final Determination of Sales at Less Than Fair Value: Sparklers from the People's Republic of China*, 28590.

<sup>44</sup> *Preliminary Determination of Sales at Less Than Fair Value: Sulfanilic Acid from the Republic of Hungary*, 57 Fed. Reg. 48206, October 22, 1992.

<sup>45</sup> North, *Institutions, Institutional Change and Economic Performance*, pp. 27-35.

For example, measurement and information problems plague antidumping investigations. There is a problem obtaining accurate, adequate information to use in the investigation. It is often difficult if not impossible to obtain direct evidence both on what is produced in surrogate countries and their production costs. There is a preference for publicly available information over information supplied by the NME. The manner of obtaining this publicly available information, such as valuing a surrogate's exports to a third country and applying this to the NME, becomes a convoluted exercise and often leads to distortions in the information.<sup>46</sup> Scarce information or information which is deemed “indeterminate” because of the presumption that something is economically amiss in transitional economies, raises the cost of obtaining what the ITA determines is usable information.

In addition, it is prohibitively expensive in both time and money for the NME to defend against AD investigations. Even when NMEs submit all known information, it is often inadequate for the ITA's purposes so it is not used. The ITA questionnaire requests information on factor inputs and prices which is time consuming to determine, given that different countries use different accounting methods, and may be costly to acquire. In one case it was reported that the cost of responding to the AD investigation amounted to 10% of the firm's annual export revenue.<sup>47</sup> Defendants often simply do not have the time, the resources, or the ability to supply the ITA with the requested information,<sup>48</sup> which often happens in investigations against NMEs, so the Best Information Available (BIA) is used.<sup>49</sup> While this is the standard used in all antidumping

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<sup>46</sup> *Preliminary Results of Antidumping Duty Administrative Review: Tapered Roller Bearings and Parts Thereof, Finished and Unfinished, From the Republic of Hungary*, 57 Fed. Reg. 36069, August 12, 1992.

<sup>47</sup> OECD, 130.

<sup>48</sup> *Preliminary Determination of Sales at Less Than Fair Value: Ferrosilicon From Kazakhstan, the Russian Federation, and Ukraine*, 57 Fed. Reg. 61876-8, December 29, 1992.

<sup>49</sup> *United States Code Annotated, Title 19 Customs Duties*, 19 § 1677e. Verification of Information, 311.

cases, it is particularly onerous in cases involving NMEs.<sup>50</sup> The cost of defending a NME exporter against AD charges can be so high and the probability of winning so low that the mere filing of a AD investigation can prompt NME exporters to halt exports.

Keohane argues that institutions lower transaction costs by facilitating information flows and decreasing uncertainty.<sup>51</sup> However in the case of the application of AD laws to transitional economies, formal institutional arrangements serve to increase transaction costs. For example in an effort to improve the applicability of the AD laws to transitional economies, the formal institutions have been modified. This modification has over-problematized the choice of a surrogate, resulting in even more measurement problems. The manner of calculating GNP to determine the surrogate is unpredictable, the factors used in the determination of a surrogate and the weights attributed to different factors fluctuate per case, the exchange rates involved in the third country price determination can fluctuate and contribute to the uncertainty involved in determining sales at less than fair value, and the type of industry initiating a dumping investigation affects the time frame of the AD petitions.<sup>52</sup> In addition, the ITA has determined that multiple surrogates can be used in determining the constructed value in NME cases, such that energy prices could be derived from one country, labor prices from a second country, and other factor inputs from a third country.<sup>53</sup> An effort to improve the accuracy of the calculation of fair value has served to further obscure the transparency of the process.

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<sup>50</sup> *Final Determination of Sales at Less Than Fair Value: Sulfur Dyes, Including Sulfur Vat Dyes, From the People's Republic of China*, 58 Fed. Reg. 7539, February 8, 1993.

<sup>51</sup> Robert Keohane, *After Hegemony* (Princeton: Princeton University Press, 1984), 89-95. North also discusses the role of institutions in reducing uncertainty, *Institutions, Institutional Change and Economic Performance*, pp. 3-6.

<sup>52</sup> For example, in a recent AD investigation against Ukraine, Brazil was used as a surrogate for Ukraine even though Brazil's GDP was more than double that of Ukraine, according to World Bank data, and Brazil does not abide by generally accepted accounting principles (*Notice of Final Determination of Sales at Less Than Fair Value: Certain Cut-to-Length Carbon Steel Plate from Ukraine*, 62 Fed. Reg. 61754, November 19, 1997.)

<sup>53</sup> *Notice of Final Determination of Sales at Less Than Fair Value: Sebaic Acid from the People's Republic of China*, 59 Fed. Reg. 28053, May 31, 1994.

These and other factors contribute to the general uncertainty of the entire AD process and greatly aggravate the uncertainty facing exporters. Because no predictable scheme exists for weighting various macroeconomic and industry-specific factors in the choice of a surrogate, the NME exporter must estimate a range of possible foreign market values for each potential export price.<sup>54</sup> Thus unlike market-economy producers who know whether they are technically dumping, NMEs may dump involuntarily simply because they can not know *ex ante* what will turn out to be their product's foreign market value. In sum, the institutional arrangements have increased uncertainty and raised transactions costs.

### Distrust

The formal institutions codifying implementation of the AD laws are highly complex, expensive, and time consuming. The transactions costs to the ITA can be prohibitively high. What explains the fact that the ITA has enacted changes to the laws which increase their complexity, and raise transaction costs while claiming that it is making the laws more clear and fair? I think the answer lies in a profound distrust of the motives of NMEs and the informal procedures to administer the laws which are grounded in this distrust.<sup>55</sup> The informal procedures include “rules of thumb,” norms and patterns of implementing the laws, and ideology. The informal constraints on the implementation of the AD laws are very powerful and in fact, I will argue, determine outcomes.

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<sup>54</sup> Stuart S. Brown, "Export Uncertainty in Centrally Planned Economies and Administered Protection," *Journal of Comparative Economics*, Vol. 13 (1989), 553-565.

<sup>55</sup> Stone, Levy and Paredes also discuss a case in which informal institutions develop and dominate processes due to high transaction costs. See Andrew Stone, Brian Levy, and Ricardo Paredes, "Public Institutions and Private Transactions: A Comparative Analysis of the Legal and Regulatory Environment for Business Transactions in Brazil and Chile," in Alston, Eggertsson, and North (eds.), *Empirical Studies in Institutional Change* (Cambridge: Cambridge University Press, 1996).

The informal institutional constraints are based on a distrust of NME exporters. This distrust influences the manner in which the law is adjudicated, and renders the law consistently biased against exports from NMEs. The informal institutions are informed by the presumption that the NME could not have a comparative advantage in the export product. This presumption is an ideological vestige of the Cold War. It is based on the assumption that a Communist country could not be more competitive than a capitalist economy in the production of any product. It is also based on the assumption that non-capitalist countries necessarily pose a threat to capitalist countries. There is a distrust of the intentions of the NME exporter. This widespread assumptions about the inefficiencies of centrally planned economies and the threat they impose has become embedded in the informal institutional workings of the ITA. In this case ideology serves not only as a “device in order to simplify the world” or satisfice, but as a normative consideration.<sup>56</sup> Communism is bad and capitalism is good, in this constructed normative dichotomy. The ideological biases permeate the informal institutions, and thereby adjudicate this normative distinction.

There are various ways in which this distrust is manifested. In the following two sections I will investigate cases in which the ITA has changed the formal institutions in order to adjust to the acknowledged economic and political changes in transitional economies. Nonetheless, outcomes in AD cases have remained unchanged. Changes in formal institutions should yield changes in outcomes. The fact that it does not suggests something else is going on. I intend to demonstrate that distrust of NMEs ensures static outcomes in spite of formal institutional changes. Informal institutional constraints and procedures are based on distrust of NMEs. As such, they prevent a change in the de facto treatment of NMEs. I will argue that this is not simply a case of informal

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<sup>56</sup> North discusses various uses for ideology including a means of simplifying the world of choices, and as a way to

institutions being “sticky” or of institutional lag.<sup>57</sup> In this analysis informal institutions reflect pervasive ideological biases against NMEs and transitional economies. Formal institutions reflect economic considerations. As such when economic conditions change, formal institutions also change, albeit incrementally and insufficiently. However, because the informal institutions reflect distrust of NMEs they have remained unchanged, and therefore outcomes have remained unchanged.

### **Part III: The Market Oriented Industry Test**

#### ***Formal Institutions:***

The peculiar nature of NME countries has made some revision of the AD law inevitable. As former centrally planned economies in Central and Eastern Europe restructure their economies on the basis of market principles, the traditional Western remedies for suspected nonmarket economy unfair trade practices have grown outdated. Both the U.S. Department of Commerce and the United States Congress acknowledge that certain sectors or regions in a transitional economy will face market prices or begin to operate under hard budget constraints more quickly than others: "attempts by traditional NMEs to evolve toward market-oriented economies may result in a situation in which a sector of an NME may be sufficiently free of NME distortions so that the actual prices and/or costs incurred in the NME could be used in dumping calculations and render meaningful results."<sup>58</sup> Therefore, in an effort to render more accurate judgements in AD

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include normative considerations about fairness. See *Structure and Change in Economic History*, p. 49.

<sup>57</sup> For a discussion of the incremental changes of formal and informal institutions, and the stickiness of informal institutions see North, *Institutions, Institutional Change, and Economic Performance*, p.6. For a discussion of institutional lags see Stephen Krasner, “State Power and the Structure of International Trade,” *World Politics* Vol. 28, 1976, p. 342.

<sup>58</sup> *Final Negative Countervailing Duty Determination: Oscillating Ceiling Fans from the People’s Republic of China*, 57 Fed. Reg. 24018, June 5, 1992.



investigations, reforming sectors could potentially be treated differently from the NME in which they are located. Accordingly, in 1988 Congress amended the AD law with section 773(c)(1)(b) permitting standard market economy methodologies in NME cases under limited circumstances. With these considerations in mind, the Department of Commerce began to consider the possibility of a "bubble of capitalism" within a NME.<sup>59</sup> Acknowledging the possibility of bubbles of capitalism and then developing regulations and a test in order to adjudicate this phenomenon, indicates changes to the formal institutions surrounding unfair trade laws.

The rationale behind the bubble of capitalism or "market-oriented industry" (MOI) argument is to allow those industries in a NME which have converted to market-oriented incentives to be given the ability to prove that their inputs and pricing structures are completely market determined, and therefore to allow them the use of their own prices for factor inputs in AD cases. Use of a MOI standard would be a means by which industries in economies in transition could have more fair and predictable treatment in antidumping investigations against their exports, before the country itself was recognized as a full fledged market economy. This is logical given that there are certain sectors or regions in an transitional economy which will be privatized and operate on forces of supply and demand more quickly than other sectors, due to the nature of how a NME transforms its economy into a market-oriented one.

If an industry was labeled a MOI, it would be subject to antidumping procedures similar to those used for market economies. This would provide a great advantage to the industry. If the

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<sup>59</sup>In the case of *Natural Menthol From the People's Republic of China* (46 Fed. Reg. 3256, January 14, 1981), Commerce began to grapple with both regional and sectoral differences in the pace and scope of reform in economies in transition and what this would mean for the application of U.S. trade laws. In this case it was determined that although there were no direct state controls on the production or sale of menthol, the direct control of the state on other sectors of the economy, such as the agricultural sector, indirectly impacted the production of menthol and influenced the production and sale of menthol. Therefore, the menthol producer's factor values of production could not be used in the investigation. In *Sparklers From the People's Republic of China* ( 56 Fed. Reg.

actual prices that MOI's paid for their factors of production were used, the comparative advantage of an industry in producing a good could be determined. As it now stands, the factors of production method precludes a finding that an industry in a NME has a comparative advantage in the export of a good. Use of the MOI standard would decrease the number of positive final determinations of dumping against NME industries. It may decrease the incidence of dumping complaints against NMEs given that the determination of dumping would be simpler, less subjective and more consistent. It could also provide an incentive for industries in NMEs to push ahead with market reforms in order to garner market-oriented treatment.

In order to be considered a "MOI" an industry must prove that the prices of all inputs used in the production of the product are market determined, this includes all direct and indirect factors of production. While the ITA has not yet found such a "bubble," it has adopted a compromise method. When some of the inputs are unambiguously market determined, the ITA will use those costs and prices in calculating constructed value for AD determinations. Those inputs whose prices cannot be unambiguously proven to be market-determined, will be calculated using surrogate values.<sup>60</sup> The ITA rendered a decision employing the partial use of domestic factor prices which demonstrates the possible distortion which results in the determination of dumping margins for cases involving NMEs. In *Chrome Plated Lug Nuts from the People's Republic of China* the preliminary dumping margin was assessed at 66%; however in the final determination, when some of the inputs were valued using the industry's prices, the dumping margin was only

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20588, May 6, 1991) and *Oscillating Fans From the People's Republic of China* ( 56 Fed. Reg. 55274, October 25, 1991) Commerce clarified its position on bubbles of capitalism.

<sup>60</sup> *Preliminary Determination of Sales at Less Than Fair Value: Certain Carbon Steel Butt-Weld Pipe Fittings From the People's Republic of China*, 56 Fed. Reg. 66833, December 26, 1991.

4%.<sup>61</sup> The partial use of domestic factor prices substantially decreased the final dumping margin relative to the exclusive use of the factors of production methodology.

However, as a result of a challenge in the U.S. Court of International Trade and evolving positions adopted in two countervailing duty cases,<sup>62</sup> Commerce remanded its determination in the Lug Nut case. In *Lug Nuts from the People's Republic of China* the state had a considerable presence in both the steel and chemical industries (two significant production inputs), but it was originally ruled that the industry still sourced the inputs at market-determined prices:

"We recognize that for certain inputs into the production process, market forces may be at work. For example, inputs may be imported from suppliers in market economy countries. Similarly, we may find that market forces are at work in determining the prices for locally sourced goods in the NME. Where this occurs, we believe that it is appropriate to use those prices in lieu of values of a surrogate, market economy producer, because they are market-driven prices and they reflect the producer's actual experience."<sup>63</sup>

In the remanded case the ITA ruled that its previous standard was based on too narrow a scope of inquiry: "The absence of direct government involvement in specific transactions between buyers and sellers does not mean that the terms of those transactions reflect market-determined prices or values." This is especially the case in a nonmarket economy environment which is necessarily "riddled with distortions."<sup>64</sup> This precedent setting case reinforced the presumption that market forces were not at work in a transitional economy. This differs markedly from *the presumption* of market forces in cases involving developing countries.

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<sup>61</sup> 56 Fed. Reg. 46153, September 10, 1991.

<sup>62</sup> *Final Determination of Sales at Less Than Fair Value: Sparklers From the People's Republic of China*, 56 Fed. Reg. 20589, May 6, 1991, and *Oscillating Fans From the People's Republic of China* ( 56 Fed. Reg. 55274, October 25, 1991).

<sup>63</sup> *Final Determination of Sales at Less Than Fair Value: Chrome Plated Lug Nuts from the People's Republic of China*, 56 Fed. Reg. 46154, September 10, 1991.

<sup>64</sup> *Amendment to Final Determination of Sales at Less Than Fair Value and Amendment to Antidumping Duty Order: Chrome-Plated Lug Nuts from the People's Republic of China*, 57 Fed. Reg. 15052, April 24, 1992.

In light of the aforementioned case, the ITA formulated new criteria --the "Market-Oriented Industry Test"--in order to clarify the definition of what precisely constitutes a market-oriented industry in a NME: 1) almost no government involvement in the setting of prices or quantities to be produced, state-mandated production or allocation of output precludes a MOI; 2) private or collective ownership should "characterize" the industry under investigation, although a very small, undetermined, percentage of enterprises could still be state owned; and 3) all significant inputs must be paid for in market-determined prices.<sup>65</sup> The first criterion of the MOI test is designed to address the degree of government involvement in pricing and production decisions, the second criterion addresses how different types of ownership could affect the ability of enterprises to "respond to market signals with respect to investment and divestment," and the third criterion addresses "inputs and market distortions that may result from central planning activities."<sup>66</sup> If the share of state-required production is significant (25-50% qualifies as significant but a smaller percentage could qualify given the loose determination of "significant")<sup>67</sup> an industry would fail the test. While it has been acknowledged that inspecting individual factor inputs for market-orientation increased the fairness of the application of AD laws to NMEs, this increased the complexity and potential subjectivity of the proceedings to the point where it may

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<sup>65</sup> *Preliminary Determination of Sales at Less Than Fair Value: Sulfanilic Acid From the People's Republic of China*, 57 Fed. Reg. 9411, March 18, 1992.

<sup>66</sup> *Final Negative Countervailing Duty Determinations: Oscillating and Ceiling Fans From the People's Republic of China*, 57 Fed. Reg. 24018, June 5, 1992.

<sup>67</sup> Commerce ruled in *Chinese Lug Nuts* that even though there was no direct government involvement in the transactions between the Lug Nut producers and the steel suppliers, the fact that 45% of national steel output could be requisitioned by the government at in-plan prices indicates that "the extent of government involvement in the production and pricing decisions for steel generally affects the demand and supply for individual steel products." The U.S. Department of Commerce indicated in this decision that if 25-50% of production may be government directed for consumption that this is significant and that therefore these steel industries "in very large part, exist to service government demand for their output" ( 56 Fed. Reg. 46153, September 10, 1991).

have rendered this method nearly unadministrable.<sup>68</sup> There are two reasons why the MOI regulations are unadministrable: first, the new procedures have substantially raised transaction costs, since measuring has become so complex as to be practically infeasible; and second, the informal institutional constraints surrounding the implementation of the MOI test render the test empirically meaningless.

### ***Distrust***

The benefits to industries in NMEs from the present application of the MOI test are questionable, both because of the high transaction costs and the informal structure of the test. Specifically, ideological biases about the danger of both nonmarket economies have become embedded in the ITA's institutional structures. This distrust of the intentions and capabilities of formerly Communist countries poses a substantial institutional constraint since it has become embedded in norms and precedents.

For example, the relative openness of the land and labor markets in economies in transition has to be considered before determining if an industry is classified as market-oriented. The degree of state control, whether it be indirect or direct, that would negate the industry from being considered market-oriented was not specified by the ITA, although it did state that "there are no set criteria for judging whether, in a particular case, the degree of state control over an economy is such as to make home market prices inappropriate for purposes of foreign market value."<sup>69</sup> In *Petroleum Wax Candles from the People's Republic of China*, the aspects of the economy which should be looked at for direct or indirect state control were spelled out, but each aspect was

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<sup>68</sup>Discussion with Analyst in Countervailing Duty Investigations of the International Trade Administration, U.S. Department of Commerce, May 27, 1993.

preceded by the phrase "degree of state control over...".<sup>70</sup> What constitutes too much or too little control remains open for interpretation.<sup>71</sup> This discretionary understanding constitutes a informal constraint on the application of AD laws to transitional economies. The ITA is allowing its perceptions and ideological assumptions about NMEs to have causal weight in AD determinations. In this case distrust precludes the findings of market orientation in AD determinations involving NMEs.

Petitioners have contended that the third component of the MOI test requires that the industry under investigation be more market-oriented than current market economies. It requires that all significant inputs, and inputs of inputs be purchased at completely market-driven prices. Since the ITA established that only verifiable documented data will be adequate to prove market-determined prices, this is an impossible hurdle to overcome. The excessively rigorous application of the third criterion of the MOI test and the assumptions made about the macroeconomic environment of a NME will exclude any industry in a NME from receiving this classification. Part

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<sup>69</sup> *Final Determination of Sales at Less Than Fair Value: Chrome Plated Lug Nuts From the People's Republic of China*, 56 Fed. Reg. 46153, September 10, 1991.

<sup>70</sup> *Antidumping Duty Order: Petroleum Wax Candles from the People's Republic of China*, 51 Fed. Reg. 30686, August 28, 1986.

<sup>71</sup> The ITA clarified its policies regarding its interpretation of "degree of state control" (*Study of the Application of U.S. Trade Laws to Countries Developing Market Oriented Economies: Request for Comments*, 54 Fed. Reg. 11985, March 29, 1989). In spite of the fact that the Chinese headwear industries involved operated under hard budget constraints, were responsible for their own losses, could go bankrupt, could fire their workers, distributed bonuses based on the profitability of the firms, freely determined input suppliers, negotiated prices between buyers and sellers, could determine or change the product mix to be exported, and could select to whom they would export their products, it was ruled that the industries still operated in a system with "rigidities." This was primarily due to the fact that the government was the largest purchaser of cotton and cotton cloth in China, and that this indirectly affected the price and volume of cotton. Therefore, the headwear producers could not consider all of their inputs completely market determined. Which "rigidities" actually impede market flows and which do not significantly impair the ability of an industry to be market-oriented must be ascertained. For example, in the U.S. the Department of Agriculture sets the price of cotton each week, and there is a ban on importing any cotton that is produced in the U.S. (Discussion given by Carlos Moore, Executive Vice President of American Textile Manufacturers Institute, at Georgetown University, March 1, 1993). The U.S. cotton textile and apparel industries are considered market-oriented industries and would be judged as such in an AD investigation by another country.

III of the test is the reason why the MOI test "is not a test it is a wall."<sup>72</sup> Developing countries are trusted and therefore not subjected to the same level of scrutiny.

In numerous AD cases the defending foreign industry has contended that the type of proof required to qualify as a MOI is unattainable, and that certain industries in the U.S. would not even be able to satisfy the ITA's rigid criteria.<sup>73</sup> The petitioner in *Oscillating and Ceiling Fans From the People's Republic of China* contended that if this excessively rigorous standard had been held up to industries in certain past countervailing duty involving cases involving "market economies", the cases would have been dropped because the industries under investigation would not have qualified as market-oriented given that their inputs were allegedly supplied by government owned industries at fixed prices.<sup>74</sup> Commerce has even acknowledged that many U.S. industries would not qualify as MOI's if they were held up to this test.<sup>75</sup>

The U.S. Commerce Department recognizes that governments intervene and regulate certain markets or sectors in many countries treated as market economies. However in market economy investigations, "there is a reasonable presumption that market economy influences predominate over the influence of any sector or market in which there is government intervention or regulation."<sup>76</sup> Similarly it is assumed that in NMEs, nonmarket forces permeate the economy.<sup>77</sup>

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<sup>72</sup>Discussion with Analyst in Import Investigation, at the International Trade Administration, U.S. Department of Commerce, 1993.

<sup>73</sup> *Tapered Roller Bearings and Parts Thereof, Finished and Unfinished, From the People's Republic of China; Final Results of Antidumping Duty Administrative Review and Revocation in Part of Antidumping Duty Order*, 62 Fed. Reg. 6189, February 11, 1997.

<sup>74</sup> *Final Affirmative Countervailing Duty Determination: Aluminum Sulfate From Venezuela*, 55 Fed. Reg. 43440, October 25, 1990; *Carbon Black from Mexico*, 41 Fed. Reg. 30385, August 26, 1988; *Preliminary Affirmative Countervailing Duty Determination: Softwood Lumber Products from Canada*, 57 Fed. Reg. 8800, March 12, 1992; and *Preliminary Countervailing Duty Determination: Carbon Steel Products from Brazil*, 49 Fed. Reg. 5157, February 10, 1984.

<sup>75</sup> Discussion with Analyst in Countervailing Duty Investigations, at the International Trade Administration, U.S. Department of Commerce, May 27, 1993.

<sup>76</sup> *Oscillating Ceiling Fans from China*, 57 Fed. Reg. 24021, June 5, 1992.

<sup>77</sup> *Notice of Final Determination of Sales at Less Than Fair Value: Disposable Pocket Lighters From the People's Republic of China*, 60 Fed. Reg. 22359, May 5, 1995.

If transitional economies are always assumed to operate under less than market-determined conditions, then it is impossible to prove the existence of a market-oriented industry in a NME. It has been acknowledged that the basic policy of the ITA is that there will not be any positive determinations of the existence of a MOI in the near future, if at all.<sup>78</sup> The MOI status and the test were designed such that the burden of proof for an industry to demonstrate that it is a MOI is so great as to be insurmountable. While the ITA is going through the motions of trying to find a MOI it is basing its investigations on the supposition that in reality a MOI could not exist in a NME.<sup>79</sup> In effect the formal institutions have little relevance to the outcomes in MOI cases. Distrust of NMEs precludes the finding of a MOI.

What is particularly interesting about the implementation of the MOI test is the dominance of informal institutions in determining outcomes. In this case even though the formal institutions have changed, meaning the law is now designed to treat transitional economy exporters in certain circumstances as market-oriented, informal institutions ensure that the final AD determinations remain unchanged. The transitional economy exporters are not treated any differently than exporters were prior to the dissolution of the Communist bloc. Formal institutions have changed but the *de facto* implementation of the law remains the same. This suggests the power of distrust in shaping outcomes. The interviews with the ITA reflect the power of ideological norms in affecting AD outcomes. The presumption that there is something strange, and unknown going on in transitional economies that were formerly Communist creates a distrust of their motives. This distrust informs informal procedures and decision making.

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<sup>78</sup>Analyst at the International Trade Administration, Office of Import Administration, April 1993.

<sup>79</sup>*Final Determination of Sales at Less Than Fair Value: Chrome Plated Lug Nuts from the People's Republic of China*, 46154.



## **Part IV. The Reclassification of Transitional Economies**

### ***Formal Institutional Constraints:***

There is much to be gained politically as well as economically by transitional economies from a reclassification to “market-oriented countries.” It would be an affirmation by the international community of the phenomenal transformations that the country has undergone, as well as an international stamp of approval which may encourage foreign direct investment or other trade benefits. Thus far the United States has reclassified only Poland<sup>80</sup> and the former German Democratic Republic,<sup>81</sup> and the EC has reclassified Poland, Hungary and the Czech Republic in 1992.<sup>82</sup> The process of reclassification is dominated by distrust of the motives and intentions of NMEs. In this section I will explain the formal rules by which the ITA determines the presence or absence of a market oriented economy. I will then discuss the way distrust affects informal constraints which impact the determination of market/nonmarket status.

The consensus at the Commerce Department is that it would benefit transitional economies to be reclassified as market-oriented economies. In 1988 the OTCA instructed Commerce to consider several factors when trying to determine if a country should be treated as a market or nonmarket oriented country under the law. Subsequent to this Commerce added other factors for consideration. These include: 1) the extent to which the currency of the country is convertible; 2) the extent to which wage rates are determined by free bargaining between labor

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<sup>80</sup> Antidumping Duty Order and Initiation of Changed Circumstance Antidumping *Administrative Review: Certain Cut to Length Carbon Steel Plate from Poland*, 58 Fed. Reg. 44166, August 19, 1993.

<sup>81</sup> *Solid Urea from the Former German Democratic Republic: Initiation of Changed Circumstances Antidumping Review*, 61 Fed. Reg. 27049, May 30, 1996.

<sup>82</sup> The EC does not have a procedure to determine what constitutes a market-oriented country. EC Council Regulation (EC) No. 519/94 simply designated a list of nonmarket economies. The following countries are considered NME's for the purposes of EC antidumping laws: Albania, Armenia, Azerbaijan, Belarus, China, Estonia, Georgia, Kazakhstan, North Korea, Kyrgyzstan, Latvia, Lithuania, Moldova, Mongolia, the Russian Federation, Tajikistan, Turkmenistan, Ukraine, Uzbekistan, and Vietnam. This method mitigates the need for

and management; 3) the extent to which joint ventures or other investments by firms of other foreign countries are permitted; 4) the extent of government ownership or control over the means of production; 5) the extent of government control over the price and output decisions of enterprises;<sup>83</sup> and 6) the degree of centralized government control over the allocation of resources or inputs.<sup>84</sup> There is as of yet no method for weighting these factors, and "there are no set criteria for judging whether, in a particular case, the degree of state control over an economy is such as to make home market prices inappropriate for purposes of foreign market value."<sup>85</sup>

The first criterion in itself does not prove or disprove the market-orientation of an economy. This is especially the case when the number of "market-oriented" economies with inconvertible currencies is considered. While wage rate controls, a temporary feature of heterodox stabilization programs, do eventually distort market signals, on a macroeconomic level the second criterion has been acknowledged as largely insignificant and more a political than an economic consideration.<sup>86</sup> The third criterion is not a sound indicator of market status, as there are many market economies with restricted foreign penetration, and almost all economies have limited foreign investment in specific sectors. The Department of Commerce has stated that the issue of both currency convertibility and degree of foreign investment are macroeconomic indicators and as such have "little effect on internal market forces."<sup>87</sup> Clearly, no single one of

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arbitrary criteria defining "market-orientation," but does not provide any guidelines for indicating when or how one is classified as a market economy. See OECD, p. 141.

<sup>83</sup> *Study of the Application of U.S. Trade Laws to Countries Developing Market Oriented Economies; Request for Comments*, 54 Fed. Reg. 12941, March 29, 1989.

<sup>84</sup> *Petroleum Wax Candles from the People's Republic of China: Antidumping Final Determination of Sales at Less Than Fair Value and Suspension of Liquidation*, 51 Fed. Reg. 25085, July 10, 1986.

<sup>85</sup> *Natural Menthol from the People's Republic of China; Antidumping Preliminary Determination of Sales at Less Than Fair Value and Suspension of Liquidation*, 46 Fed. Reg. 3258, January 14, 1981.

<sup>86</sup> Discussion with Analyst in Countervailing Duty Investigations of the International Trade Administration, U.S. Department of Commerce, May 27, 1993.

<sup>87</sup> *Final Determination of Sales at Less Than Fair Value: Chrome Plated Lug Nuts From the People's Republic of China*, 56 Fed. Reg. 46153, September 10, 1991.

these criteria will conclusively indicate a market or a nonmarket economy. The Department of Commerce has acknowledged that many developing countries presently used as surrogates in NME antidumping investigations could potentially be classified as NMEs based on the above criteria. Therefore, such indicators can not serve as definitive tests of market economy status.<sup>88</sup>

***Distrust:***

If the aforementioned criteria are not in fact definitive formal indicators of market/nonmarket status, on what basis are such decisions being made. The answer to this question lies in an understanding of the ITA's distrust of NMEs. Of paramount importance to an understanding of institutional constraints is the enduring legacy of assumptions about the threat posed by Communist/centrally planned economies.

When adapting antidumping laws to exporters in transitional economies, the U.S. Commerce Department was sensitive to adopt a method which still "addressed the paramount concerns expressed by the U.S. Congress for not using NME prices to determine foreign market value" and which reflected long standing fears of NMEs export capacities.<sup>89</sup> This enduring distrust of Communism has continued to override the ITA's official reports praising the reform efforts in these regions, such as the "significant market reforms and extensive legislation passed toward the development of an economy which can operate based upon free market principles."<sup>90</sup> The ITA reports acknowledge high levels of privatization and laws protecting the free bargaining

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<sup>88</sup>If India, Brazil, or Thailand were subjected to the market economy criteria it is suspect if they would pass. Discussion with Analyst at Import Administration, International Trade Administration, U.S. Department of Commerce, April 7, 1993.

<sup>89</sup> *Chrome Plated Lug Nuts From the People's Republic of China*, 56 Fed. Reg. 46155, September 10, 1991.

<sup>90</sup> *Notice of Final Determination of Sales at Less Than Fair Value: Certain Cut to Length Carbon Steel Plate from Ukraine*, 62 Fed. Reg. 61754, November 19, 1997.

of labor and management. However these congratulatory statements are accompanied by rejections of market status.

The presumptions about economic and political deviance in these transitional economies are implicitly understood to dominate informal institutions, and therefore most countries do not even try to petition for a change in status since the informal constraints facing them are practically insurmountable.<sup>91</sup> Even those countries who have succeeded in being reclassified as market oriented are not free from informal institutional constraints. As previously mentioned, only Poland has petitioned for a change in status to a market economy, and been accepted. However, it was determined that in this case although Poland was not longer classified as a NME, the ITA could not use Polish prices to determine dumping. Informal constraints trumped the formal institutions, and caused the ITA to modify implementation of AD laws to Poland, such that Poland was *de facto* treated as a NME for the purposes of the AD determination.<sup>92</sup> Similarly, even though the EC reclassified Poland, it has still used surrogate prices for energy and raw materials in an antidumping investigation against Poland which increased the dumping margins and therefore conferred greater protection to EC industries.<sup>93</sup> This is further confirmation of the widespread primacy of distrust in affecting the informal procedures surrounding the application of trade laws to formerly Communist countries.

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<sup>91</sup>*Titanium Sponge from the Russian Federation: Preliminary Results of Antidumping Duty Administrative Review*, 62 Fed. Reg. 25920, May 12, 1997 and *Preliminary Determination of Sales at Less Than Fair Value; Certain Cut to Length Carbon Steel Plate from the Russian Federation*, 62 Fed. Reg. 31967, June 11, 1997.

<sup>92</sup> *Antidumping Duty Order and Initiation of Changed Circumstance Antidumping Administrative Review: Certain Cut to Length Carbon Steel Plate from Poland*, 58 Fed. Reg. 44166, August 19, 1993; and *Electric Golf Carts from Poland; Amended Final Results of Antidumping Duty Administrative Review*, 61 Fed. Reg. 29543, June 11, 1996.

Formal and informal institutional constraints are also evident in the EC's AD investigations. Even reclassified, the EC has still used surrogate prices for energy and raw materials in an antidumping investigation against Poland which increased the dumping margins and therefore conferred greater protection to EC industries. See OECD, p.113.

<sup>93</sup> OECD, 113.

The reclassification of transitional economies is not an entirely economic decision. The political liberalization accompanying economic reforms figures decisively in the U.S. Department of Commerce's perception of the extent of reform in the country as a whole. It has even been stated that the reclassification of NMEs to market-oriented economies reflects predominantly political considerations.<sup>94</sup> The institutional approach adopted in this paper predicts that a fundamental ideological shift in perception of transitional economies will be slow to happen. This section has tried to demonstrate that political considerations and ideological biases developed during the Cold War continue to inform the norms and practices of the ITA.

## **Part VI. Conclusion**

Distrust plays an important role in this analysis. It is only by including how distrust informs informal norms and decision-making procedures that we understand why AD outcomes have not changed, even though there have been changes in the law. The fear of Communism and presumptions about unspecified “nonmarketness” or anti-capitalist tendencies are pervasive in legal resolutions and in policy statements related to transitional economies. During the Cold War formal and informal institutions developed to protect the U.S. from unfair trade with Communist countries. Both formal and informal institutions were fueled by a distrust of Communism, and a fear of the disproportionately negative effects of trade with these countries. In fact Congress and the ITA often referred to these countries in legal resolutions and laws as “Communist” instead of non-market. This helped to propagate a widespread belief in the justness of extraordinary trade laws against this strange and possibly harmful alternative economic system.

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<sup>94</sup>Discussion with Analyst at International Trade Administration, U.S. Department of Commerce, 1993.

Political and economic agendas helped to establish what has proven to be an enduring dichotomy: market/capitalist versus non-market/Communist. The ideological polarization of market and nonmarket status has fostered a distrust of formerly communist countries. This dichotomy has limited the ability of the ITA, and the U.S. Government in general, to reconceptualize the status of formerly Communist countries. Thereby preventing the establishment of credible commitments for fair trade between the U.S. and NMEs. This way of viewing market and nonmarket as a dichotomy rather than a continuum may constitute a “boundary for innovation.”<sup>95</sup> In essence, this mental model or understanding of the relationship between market and nonmarket constrains and defines the possibility of new ideas and interests.

Constant references to this fear or presumption of “nonmarketness” are not simply ways to justify the material interests of domestic producers. This distrust has causal weight and affects the ability of the ITA to reconceptualize the nature of the Eastern Bloc. This presumption of “nonmarketness” has constructed boundaries for innovation. Informal institutions infused with these ideological beliefs have enforced the boundaries for innovation. This is a particularly alarming realization, because this suggests that even changes to U.S. trade remedy laws might not be sufficient to effect changes in the treatment of transitional economies. This study has examined trade remedy law changes since 1988, yet in ten years there has been no change in outcomes. This suggests that even when ideologies are inconsistent with empirical reality they may endure.

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<sup>95</sup> Margaret Weir, “Ideas and the Politics of Bounded Innovation,” in Sven Steinmo, Kathleen Thelen, and Frank Longstreth (eds). *Structuring Politics: Historical Institutionalism in Comparative Analysis* (Cambridge: Cambridge University Press, 1992), p. 200.