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A FEW REFLECTIONS ON DS474 AND THE INTERSECTION OF RUSSIA'S DOMESTIC ENERGY POLICIES AND THE EU'S ANTI-DUMPING COST REPLACEMENT METHODOLOGY

The World Trade Organization dispute DS474, initiated by the Russian Federation (Russia), stands at the intersection of an increasingly important topic in anti-dumping law and certain aspects of Russia's energy management policy. Russia's claims in this dispute are directed against certain "cost adjustment" methodologies applied by the European Commission when determining costs of production in anti-dumping proceedings. The approach taken by the Commission lies in rejecting the cost data contained in the exporters' records and then replacing it with the export price charged by Russia to customers in the European Union. The ground for this is the regulation by the Government of the Russia of price for natural gas when destined for domestic consumption, which results in significantly lower domestic prices when compared to export prices, and thus creates a dual pricing system for Russian gas. A similar approach taken by the EU in other anti-dumping investigations is subject to separate challenges under WTO law by Argentina and Indonesia.

The EU Commission's approaches raises interesting legal questions under the Anti-dumping Agreement. It is not clear whether Article 2.2.1.1 offers a legal basis for the Commission's approach, because its rules about the acceptability of the costs as recorded in the financial records of the exporter appear to revolve around the quality of the financial records, rather than governmental distortions in the market. Article 2.2 and its reference to a "particular market situation" may also be raised by the EU as a defense, but this phrase has never been subject to interpretation by WTO adjudicative bodies. Finally, the cost-replacement methodology raises interesting questions about the relationship between the Anti-dumping and the SCM Agreements, as well as the question whether the Anti-dumping Agreement can be used to address governmental intervention in the market. Refs 47. Fig. 1. Table 1.

Keywords: anti-dumping, anti-dumping agreement, dual pricing, European Commission, gas, Gazprom, cost of production, cost adjustment, WTO.

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НЕКОТОРЫЕ СООБРАЖЕНИЯ ПО ПОВОДУ СПОРА ОБ ЭНЕРГЕТИЧЕСКИХ КОРРЕКТИРОВКАХ И АНТИ-ДЕМПИНГОВЫХ МЕРАХ (DS474) МЕЖДУ РОССИЙСКОЙ ФЕДЕРАЦИЕЙ И ЕВРОПЕЙСКИМ СОЮЗОМ

В запросе о проведении консультаций с Всемирной Торговой Организацией (DS474), поданном Российской Федерацией, поднимается все более и более важный вопрос о применении антидемпингового законодательства и затрагиваются отдельные аспекты российской энергетической политики. Российские претензии в данном споре относятся к методике расчета корректировок, применяемой Еврокомиссией при определении стоимости продукции и демпинговой маржи. В подходе, используемом Комиссией, учитываются не российские цены на энергоносители, указанные экспортером, а экспортная цена, по которой Россия продает продукцию европейским потребителям. Основанием для этого являются постановления Правительства России,

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регулирующие цены на природный газ для внутреннего потребления, что приводит к значительной разнице внутренних и экспортных цен и создает двойную систему цен на российский газ. Подобный подход антидемпинговых расследований ЕС является предметом рассмотрения отдельных заявлений в соответствии с законами ВТО, поданными Аргентиной и Индонезией.

Подход ЕС вызывает правовые споры в связи с Антидемпинговым Соглашением. Возникает вопрос о правомерности применения Статьи 2.2.1.1, в соответствии с которой установлены правовые нормы Еврокомиссии, поскольку ее положения относительно приемлемости цены, указанной в финансовой отчетности экспортера, касаются скорее качества финансовой отчетности, чем правительственного регулирования рынка. Статья 2.2 и ее ссылки на «особую рыночную ситуацию» могут быть использованы ЕС как протекционистские меры, но данное определение никогда не являлось предметом рассмотрения судебных органов ВТО. Наконец, подобная методика корректировки цены вызывает вопросы относительно согласованности *антидемпингового соглашения* и *соглашения по управлению цепочкой поставок*, так же как и сомнения в том, возможно ли применение антидемпингового соглашения в случаях правительственного регулирования рынка. Библиогр. 47 назв. Ил. 1. Табл. 1.

Ключевые слова: антидемпинговые меры, антидемпинговое соглашение, двойное ценообразование, Европейская комиссия, газ, Газпром, стоимость продукции, производство, корректировка цен, ВТО.

1. Introduction

The World Trade Organization (WTO) dispute DS474, initiated by the Russian Federation (Russia), stands at the intersection of an increasingly important topic in anti-dumping law, on the one hand, and certain aspects of Russia's foreign and domestic energy management policy, on the other hand.

In DS474, Russia challenges certain "cost adjustment" methodologies applied by the European Commission (EU Commission) when determining costs of production in anti-dumping proceedings. Normally, cost data for these calculations should be data taken from the investigated exporters accounting records. However, the EU Commission will occasionally reject the cost data contained in an exporters' records, on the grounds that these costs are artificially low and do not accurately reflect "market" data. The EU Commission will then replace that data with what it considers to be more appropriate "market" cost data. In the cases challenged by Russia in DS474, the EU Commission rejected the domestic price of gas, as recorded in the records of e. g. ammonium nitrate and steel pipe producers. Instead, it used the export price of Russian gas charged to customers in the (Western) European Union (EU), a price that the producers at issue never paid.

Not surprisingly, this practice results in a higher cost benchmark and a higher constructed normal value than would be the case if the data in the producer's records had been used. This, in turn, leads to a higher dumping margin.

In the case of Russia, the grounds for considering the actually recorded input prices to be unreliable was the direct regulation of the domestic price of natural gas by the government. In contrast, in another set of EU anti-dumping investigations — biodiesel from Argentina [WTO dispute DS473…] and Indonesia [WTO dispute DS480…] — the facts that prompted the cost adjustment were export restrictions on the input (soybean oil and palm oil) that allegedly led to domestic oversupply and therefore lower raw material sourcing prices for the biodiesel producers.

The EU's practices raise questions as to the legal basis on which investigating authorities may determine that irregular conditions exist in a particular market, such that an adjustment to the prices prevailing on that market is warranted. This topic is interesting for a number of reasons, including because it may have significant impact on anti-dumping investigation practices after the expiry of China's and Vietnam's Protocol of Accession, in 2016 and 2018, respectively. However, as the existing cases show, even countries without a "non-market economy" past can be affected. Moreover, questions also arise in the relationship between the *Anti-dumping* and the Subsidies and Countervailing Measures (SCM) Agreements. The paper is intended to briefly outline these issues.

2. The underlying issue in DS474 — the "dual pricing" of natural gas in the Russian Federation

a. Basic structure of the Russian internal gas market

At the heart of the EU's determination lies the regulation of the Russian domestic natural gas sector. The Russian natural gas sector is technically privatized. However, the dominating natural gas supplier — OAO Gazprom, Open Joint-Stock Society (Gazprom) [http://www.gazprom.com/about/] — is majority Government-owned. Gazprom reportedly holds approximately 70 per cent of the internal market share [http://www.minenergo.gov.ru/activity/gas/].

The remaining 30 per cent are shared between so-called "independent natural gas suppliers"[1]. The largest of these independent natural gas suppliers is OAO Novatek, with a reported market share of approximately 8 per cent [http://www.novatek.ru/en/about/general/]. Approximately 20 per cent of Novatek is held by Gazprom and its affiliates, while another significant percentage of Novatek is held by the French oil giant Total [Total stops buying Novatek…]. A slightly smaller market share of about 5 per cent is held by OAO Rosneft, oil and gas company, which is indirectly owned by the Russian government [http://www.rosneft.com/…]. Hence, the two main competitors of the already dominant state enterprise Gazprom are in turn co-controlled and co-owned by Gazprom itself or the Russian government. The remaining 15 per cent of the market is divided between a number of smaller providers, mainly vertically integrated oil companies[2] and other independent suppliers. The Russian government indirectly controls some of them, too. For instance, the small independent supplier Northgaz is owned in equal shares by Gazprom and Novatek [НОВАТЭК получил…].

The smaller companies tend to focus on large industrial consumers. In turn, Gazprom, in addition to its industrial customer base, supplies virtually the entire household segment of the gas market (approximately 90 per cent), whereas the independent suppliers do so only in selected regions[3] and mainly focus on industrial consumers.

b. The gas transportation pipeline network

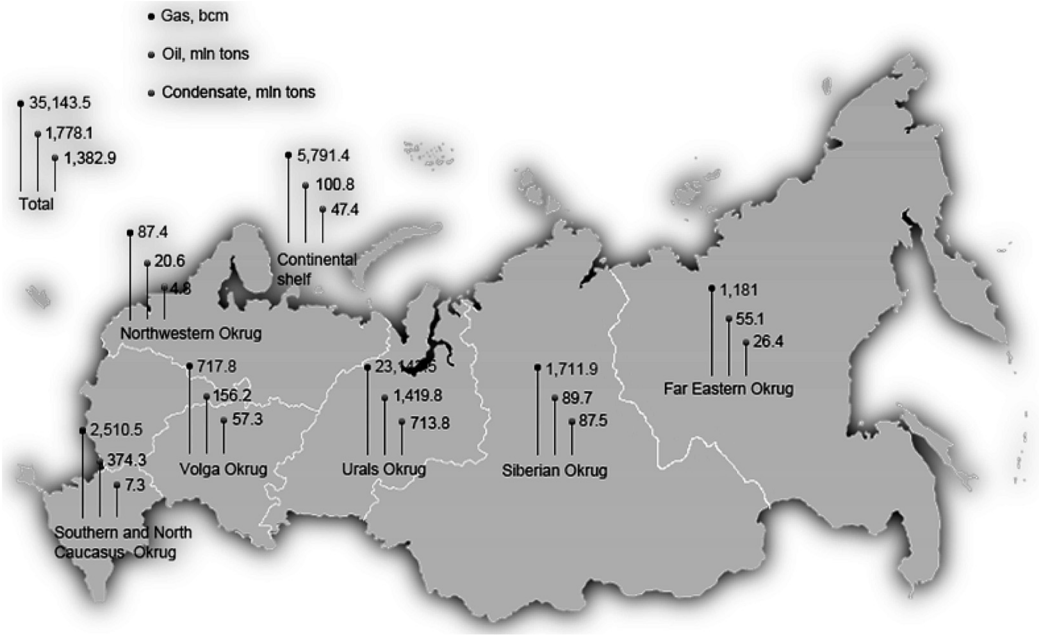
Gas is most typically extracted in the regions of Siberia and North-West of Russia. More than half of reserves are located in Siberia, which is the home for four major gas fields[4]. A map below demonstrates the main gas reserves and their approximate location (Figure 1).

[1] Some of them, however, are indirectly controlled by the government.

[2] E. g. Lukoil, Bashneft, Tatneft, Surgutneftegaz and Gazpromneft.

[3] Novatek almost fully cover household consumers in the region of Kostroma.

[4] Namely, Yamburg, Urengoy, Medvezh'ye and Zapolyarnoe, together accounting for approximately 45 per cent of the country's gas reserves [The world's biggest…].



● Gas, bcm
● Oil, mln tons
● Condensate, mln tons
35,143.5
1,778.1
1,382.9
Total
5,791.4
100.8
47.4
Continental shelf
87.4
20.6
4.8
Northwestern Okrug
717.8
156.2
57.3
Volga Okrug
23,143.5
1,419.8
713.8
Urals Okrug
1,711.9
89.7
87.5
Siberian Okrug
1,181
55.1
26.4
Far Eastern Okrug
2,510.5
374.3
7.3
Southern and North Caucasus Okrug

Figuire 1. Gas and Oil Reserves in Russia.
Source: [http://www.gazprom.com/about/production/reserves/].

Once extracted, gas is transported to the principal urban and industrial centers by an extensive pipeline network which is officially called the United Gas Supply System (UGSS) (Russian — Единая Система Газоснабжения (Edinaya Sistema Gazosnabzheniya)). This pipeline network is owned by Gazprom and is the main gas network in Russia. The share of pipelines outside of the UGSS is negligible. Russian law does not require unbundling on gas extraction, transportation and distribution activities.

Russian law stipulates the right for gas suppliers without their own transmission network to obtain access to the UGSS [On the gas supply…]. Although theoretically Gazprom may refuse access of independent suppliers to the UGSS if granting such access is technically impossible, the general perception appears to be that the independent supplier's access to the UGSS is not smooth: for instance, it is believed that the independent suppliers are forced to burn off significant volumes of associated oil gas because of their limited access to pipelines controlled by Gazprom [Alternative Gas Suppliers…].

c. The regulation of the gas price

The Russian government regulates extensively the natural gas sector, starting with extraction of the gas to transport and delivery to the final customer. The key element of interest for this article in this regulatory framework is price.

In essence, the wholesale, transportation and retail prices of natural gas and associated oil gas, extracted, transported and sold by Gazprom and its affiliates through the UGSS to industrial and retail consumers are subject to governmental regulation. It is useful to note that this price regulation, in principle, does not apply to Gazprom's competitors. To recall, these suppliers jointly hold approximately 30 per cent of the Russian gas market. Nevertheless, due to Gazprom's market power, these suppliers are de facto compelled to follow Gazprom's pricing policy, in order to be able compete with Gazprom[5].

The governmental authority charged by the Government with the implementation and administration of this legal framework is the Federal Tariff Service (FTS) (Russian — Федеральная служба по тарифам) [http://www.fstrf.ru/].

One of the key currently applicable legal instruments — Regulation No. 333 [On the improvement of gas price regulation] — enshrines the principle of gradual transition from governmental price regulation to a price determined by the market. The end of transitional period was initially set as 2011, and was later moved to 2014. The most recent amendment envisages 2018 as a target date[6].

One of the elements of Regulation No. 333 is a formula [On the approval of the gas…] designed to gradually narrow the gap between domestic and export prices through special discount coefficients (indexes). Prices for industrial users are set using this formula. With the introduction of the formula, internal gas prices have gradually risen from about 60 dollars per cubic meter in 2009 to about 100 dollars in 2013 (60 per cent of increase). By way of comparison, the price of gas sold by Gazprom to its European customers increased from approximately 240 dollars per cubic meter in 2009 to 300 dollars in 2013 (25 per cent increase) [Gazprom in Europe].

Gas prices for households are set by another document approved by FTS [On the approval of the minimum…] and have historically been approximately 10–20 per cent lower than those for industrial users. The household prices also differ between regions. The FTS also regulates the fees that Gazprom may charge the independent suppliers for using Gazprom's pipeline network[7].

Finally, it bears repeating, independent non-government owned suppliers are not subject to governmental price controls. Nevertheless, they are practically compelled to price their gas close to the government-set benchmark prices, in order to be able compete with Gazprom.

d. Export of Russian gas

The last remaining aspect of the Russian gas regulation is export sales. Since 2006, Gazprom has held the exclusive statutory right to export natural gas in gaseous state[8]. With the amendments to this law, introduced in 2013, companies were granted the right to export *liquefied* gas, subjecting to obtaining the corresponding licenses.

[5] As a part on an experiment some amounts of gas were sold through organized auctions in 2006-2008 and thus, were exempted from price regulation. Gazprom alone was allowed to sell in 2006–2007 up to 5 billion cubic meters at free market prices, independent producers were granted the same amount to divide between all of them, in 2008 the volume of gas approved for free market transactions was increased to 7.5 billion cubic meters for each party. The total sales volume made up 6.1 billion cubic meters, with almost equal amounts supplied by Gazprom and other independent producers together. The auction gas trade was ceased on 1 January 2009 with the expiry of the experimental period.

[6] Except for gas transmission fees which will continue to be regulated.

[7] Fees have undergone only slight changes during past several years and amount for approximately 13 RUR for 1000 cubic meters for 100 km for the territory of Russia and other Eurasian Economic Union (EEU) countries (Belarus, Kazakhstan, Armenia) and 14 RUR for the rest of countries [On the approval of tariffs…, 2014].

[8] Interestingly, Gazprom as a company is not specifically mentioned in this law. Rather, Article 3 grants the exclusive right to export gas (in the gaseous state) to the owner of the UGSS [On the export of gas].

The export price for gas is negotiated by Gazprom with the foreign customers, in principle free of governmental regulation (with the exception of an export duty, as described below). As a result, export prices for natural gas far exceed the prices prevailing in the domestic market. The result is, in effect, a dual-pricing system. For instance — and as explained in more detail below — the export price to the EU exceeds the domestic price by a factor of approximately 2.8, and to the CIS and Baltic States by a factor of approximately 2 [http://www.gazpromquestions.ru/en/foreign-markets/].

Export prices are based mainly on long-term delivery contracts (up to 25 years) signed under inter-government agreements. Most of the export gas is sold at the border of the importing country to local distributors that subsequently supply it to end consumers[9]. The end-consumer price includes the cost of gas transmission, plus taxes.

Gazprom's export prices are not uniform. Currently, export prices differ between those for the Western Europe, on the one hand, and the Baltic States and the countries that formerly made up the Commonwealth of Independent States (CIS), on the other hand. The differences between the prices charged by Gazprom to customers in those different regions can be substantial.

For instance, the 2013 average price, in rubles (RUR) per 1000m^3, on the domestic market was 3,393.9. In contrast, the corresponding price for the CIS and Baltic States was 7,132.8. The price for the remainder of the EU was even higher, namely, 9,680. The chart below shows the development for the period 2009–2013 of average prices over the years in RUR, USD and EUR respectively[10] (excluding VAT, excise duties and customs duties) [Gazprom in Europe] (Table 1.).

Table 1. **Average gas sales prices, 2009–2013***

	2009	2010	2011	2012	2013
Domestic market	1,885.0 62.3 43.4	2,345.5 77 58.2	2,725.4 92.9 66.7	2,964.2 95 74	3,933.9 106.7 80.3
Europe	7,216.6 238.6 166.3	7,420.7 243.5 184	9,186.6 313 224.8	10,104.4 326 252	9,680.1 304.2 229.0
CIS and Baltic	5,483.7 181.3 126.4	6,416.5 201.5 159.1	7,802.1 265.8 190.9	8,016.4 258 200	7,132.8 224.2 168.7

* Source: [Gazprom in Europe].

Finally, since 2004, Russia has applied an export duty to natural gas exports[11]. Prior to 2004, the same amount was collected as an excise tax. The export duty for natural gas is 30 per cent[12].

[9] The major counterparts of Gazprom Group in Western Europe include the following companies: E. ON Ruhrgas, Wingas, WIEH (Germany), Eni (Italy), Botas (Turkey), PGNiG (Poland), GDF Suez (France), Panrusgas (Hungary), RWE Transgas (Czech Republic), SPP (Slovakia), EconGas (Austria) and GasTerra (Netherlands): [Gazprom in Europe].

[10] Foreign currency data is calculated using exchange rates as at the end of the relevant year.

[11] Export duties were levied pursuant to Article 3 of the Law No. 5003-1 [On Customs Tariff].

[12] The original legal basis for the export duty is the Government Regulation No. 507 dated 19.08.2003 "On the enactment of export duty for natural gas exported in gaseous state outside of the Customs Union" [2003].

e. Dual pricing as a subject of negotiations during Russia's WTO accession

i. The positions of the various negotiating parties during Russia's accession and the resulting agreement

The above section shows that, effectively, a dual pricing system exists for Russian gas, combining a low domestic price with a significantly higher export price. Dual pricing was an important topic during Russia's WTO accessions negotiations. Indeed, it was considered to be one of the major stumbling blocks of the negotiating process, together with agricultural sector support and financial sector commitments[13].

Dual pricing was widely discussed during the negotiations on the accession of Russia to the WTO and was considered as one of the major impediments of the negotiations process. A number of WTO Members were concerned that Russian industrial producers of energy-intensive products, such as fertilizers or metals, benefitted from lower gas prices, claiming that this would give rise to market distortion and unfair competition [Report of the Working Party on the Accession of the Russian Federation to the WTO]. Members also expressed their concerns that the gas export duty produced a discriminatory effect with respect to foreign buyers, acted as a hidden subsidy and had a distortive effect on international trade.

During the accession negotiations these issues points were subject to discussion and were reflected in the Report of Working Party. The thrust of the Russian counterarguments was, in essence that the pricing system was not objectionable since any advantage flowing from it was not specific to a particular industry or sector; that the price, although lower than the export price, nevertheless permitted economically viable production and recovery of costs; that the price regulation was intended, inter alia, to prevent Gazprom from abusing its dominant position; and that the dual pricing conditions prevailing in Russia were not different from circumstances prevailing in certain other WTO members. With respect to Members' concerns regarding export duties, Russian representatives emphasized that export duties did not affect the price at which natural gas was purchased abroad [Report of the Working Party on the Accession of the Russian Federation to the WTO].

The Working Party Report ultimately did not resolve the issue of dual pricing nor did it impose any particular obligations on Russia different from those of other WTO Members.

However, in the 2004 EU — Russia bilateral agreement on Russia's WTO accession — the accession was eventually finalized in 2012 — does impose certain additional commitments on Russia. Specifically, Russia committed to introducing a gas price for industrial users that would cover costs, profit and required investments, and would gradually increase the price for industrial users from 27-28$ in 2004 to 49–57$ by year 2010 [Selivanova, 2004, p. 560]. See also: [EU Agrees Terms…].

As the outcome of the WTO accession negotiations, the steps taken by Russia towards modifying the regulation of gas prices for commercial users were acknowledged by Members. Members expressed their understanding that such a transition required a transitional period and also noted that Russia had reserved the right to continue regulation

Prior to 2004, the export duty was only 5 per cent, but was increased as a result of a fiscal reform as part of which the excise tax was cancelled [Газпром обложили].

[13] On dual pricing of Russian gas and tensions with the European Union [Vitaliy Pogoretskyy and Daniel Behm, 2010, p. 4–11].

price for households and other non-commercial users [Report of the Working Party on the Accession of the Russian Federation to the WTO].

By way of comparison, it is interesting to see the issue of dual pricing was addressed with regard to some other prominent users of dual pricing, namely Saudi Arabia and China.

The Working Party Report for Saudi Arabia contains a statement by Saudi Arabia that prices for goods and services in every sector were freely determined by market forces, with the exception of the goods and services listed in corresponding annex[14]. These goods and services were subject to price regulation within Saudi Arabia to maintain price stability [Report of the Working Party on the Accession of the Kingdom…]. No obligation to abolish price regulation either immediately or gradually was imposed on Saudi Arabia.

It is interesting to note that, in 2003, the EU reached a bilateral agreement with Saudi Arabia, pursuant to which Saudi Arabia would eliminate dual pricing on gas [Accession of Saudi Arabia…]. However, the outcome of this bilateral agreement was not reflected in the WTO accession documents. Subsequently, Saudi Arabia reportedly reneged on this commitment in the light of what it perceived as less ambitious dual pricing commitments that the EU secured with respect to Russia in 2004.

The Working Party Report for China also addresses the issue of price controls. China reserved its right to apply its current price controls in a non-discriminative manner [Report of the Working Party on the Accession of China to the WTO, WT/ACC/CHN/49, para. 64.]. Members took note of China's commitment that price controls would not be extended to goods or services beyond those specifically listed in corresponding annex[15], and China should make its best efforts to reduce and eliminate those controls [Report of the Working Party on the Accession of China to the WTO]. No target date for terminating price regulation was set. Bilateral agreements on China's accession to the WTO covered a range of such topics[16], but did not specifically highlight the issue of dual pricing.

3. The Commission's approach in the anti-dumping determinations in DS474

Against this general background, we describe one of the determinations by the EU Commission that are being challenged by Russia in the WTO disputes at issue. We also briefly describe a ruling by the Court of Justice of the European Union (CJEU) that has confirmed that the EU Commission's approach is consistent with EU law.

a. Council Regulation 661/2008 of 8 July 2008 re ammonium nitrate

In the investigation underlying this particular Regulation, the EU Commission examined alleged dumping by Russian exporters of ammonium nitrate. The production of ammonium nitrate is energy-intensive, and the relevant Russian producers at issue relied on gas as their source of energy.

At the core of the EU Commission's investigation was a calculation of the cost of production of ammonium nitrate. Specifically, the Commission examined whether the domestic sales of ammonium nitrate on the Russian domestic market could be considered as having been made in the "ordinary course of trade". For this purpose, the Commission

[14] Annex A includes such goods as crude oil and natural gas both gaseous and liquid state.

[15] Annex 4 lists natural gas in gaseous state as a subject to governmental price regulation.

[16] For example, the main topics of China-EU bilateral agreement on the WTO accession: [Highlights of the EU-China Agreement on WTO].

established a cost-benchmark and then verified whether domestic sales prices were above or below this benchmark. If domestic sales price are below this benchmark, the sales are deemed to be outside of the ordinary course of trade, and a "constructed normal value" is used.

In the determination at hand, the Commission found that "the prices paid by the Russian producers (of ammonium nitrate), based on governmental regulation, were abnormally low". As an example, the determination states the these prices "amounted to around one-fourth of the export price of natural gas from Russia and were also significantly lower than the gas price paid by the Community producers" [Council Regulation 661/2008…, para 58]. Therefore, the Commission found that the recorded costs for gas did not "reasonably reflect" the actual cost of production.

The Commission then found that there were no "sufficiently representative undistorted gas prices related to the Russian domestic market"; therefore, "other representative markets" had to serve as the source for the relevant information. The Commission chose the "average price of Russian gas when sold for export at the German/Czech border, net of transport costs and adjusted to reflect local distribution costs" (the "adjusted Waidhaus price"). Waidhaus serves as the main hub for Russian gas sales to the EU, and is thus largest market for Russian gas [Council Regulation 661/2008…, para 59].

The Commission subsequently rejected a number of arguments by the Russian exporters. First, it rejected the argument that the domestic price actually did reflect the gas producers' production costs, since a study presented by the exporters was based only on estimated costs and that an actual verification of the costs of Russian gas producers was not possible in the context of the investigation [Council Regulation 661/2008…, para 61]. Council Regulation 661/2008 of 8 July 2008 imposing a definitive anti-dumping duty on imports of ammonium nitrate originating in Russia following an expiry review pursuant to Article 11(2) and a partial interim review pursuant to Article 11(3) of Regulation (EC) No 384/96. In any event, interestingly, the Commission stated that, even if the domestic price covered costs, the Commission would still attach importance to the gap between the domestic and export prices Council Regulation 661/2008 of 8 July 2008 re ammonium nitrate, para. 62. Council Regulation 661/2008 of 8 July 2008 imposing a definitive anti-dumping duty on imports of ammonium nitrate originating in Russia following an expiry review pursuant to Article 11(2) and a partial interim review pursuant to Article 11(3) of Regulation (EC) No 384/96.

The Commission also rejected the argument that its cost replacement approach was not envisaged under EU law, namely, that normal value could not be based on data from a third representative market [Council Regulation 661/2008…, para 63–64].

Third, the Commission rejected arguments against the use of the Waidhaus price as the reference price. For instance, the investigated companies argued that the price was not a good benchmark price, because it was not linked to production costs, but rather was based on long-term delivery contracts. Also, the companies argued that the Waidhaus price was not reliable, because of alleged anti-competitive practices of companies operating in the intra-EU market, as evidenced by certain EU anti-trust investigation proceedings. The Commission rejected both arguments, finding that it considered the Waidhaus price relevant regardless of its link to production cost and regardless of any behind-the-border anti-competitive practices.

2 Fourth, the Commission rejected the argument that it should use non-regulated gas prices available in Russia. The Commission stated that lower non-regulated domestic prices on the Russian market did not render the Waidhaus price inappropriate and that, in any event, the volume of unregulated prices on the Russian market was too low (2 per cent) [Council Regulation 661/2008…, para 67][17].

The Commission also rejected the use of the export price to the Baltic countries, because of the small volume involved and also because data about transportation and distribution costs were not available [Council Regulation 661/2008…, para 70].

The investigated exporters also argued that, even if the Waidhaus price were to be used, it should be adjusted. Specifically, the exporters argued that the 30 per cent export duty should be deducted. The Commission rejected this argument, on the grounds that the export duty did not influence the negotiated export price [Council Regulation 661/2008…, para 72][18].

b. In Council Regulation (EC) No. 1256/2008 of 16 December 2008, on welded tubes and pipes from, inter alia, Russia [2008]

In this determination, the Commission's approach was, for all practical purposes, identical to that in the ammonium nitrate case. The Commission again rejected the recorded production costs with regard to domestically purchased gas and replaced them with the Waidhaus price. This was done on the grounds that the price on the domestic market was artificially low, "far below market prices paid in unregulated markets for natural gas". Therefore, "costs were not reasonably reflected in the exporting producers' records as provided for in Article 2(5).

4. The ECJ's case law

In a judicial challenge of this Commission determination, the CJEU endorsed the Commission's cost adjustment approach. First, the CJEU found that the Commission is in principle entitled to reject recorded costs on the grounds that the underlying market price are artificially low, including due to regulation in the domestic market. In essence, the CJEU confirmed that the EU law equivalent of Article 2.2.1.1 of the *Anti-dumping Agreement*, and the "reasonably reflect" criterion therein, extend to cover allegedly distorted market situations and are not limited to inconsistencies in the accounting records, e.g. inappropriate allocation methodologies [Judgment of the General Court of 7 February 2013…, para 46. Articles 1 and 2 of Regulation (EC) No 384/96 (now Articles 1 and 2 of Regulation (EC) No

[17] As the documents submitted in this investigation are not publicly available, it is not clear what precisely the Commission referred to under the label of "unregulated prices". As discussed above, approximately 30 per cent of the domestic Russian market is supplied by entities that are technically exempt from domestic price regulation but that appear to be compelled, by business reasons, to sell at a price similar to that charged by Gazprom. The Commission may have been referring to the auctions conducted up to 2009 on what we understand was an experimental basis.

[18] The exporters argued that the mark-up of the local distributor should not be added to the export price at Waidhaus, because the profits of the distributors were already included in the Waidhaus price. The Commission rejected that argument, among others on the grounds that the record did not contain sufficient evidence in this regard. However, the Commission held out the possibility that, should further evidence be submitted, that the dumping margin could be reduced. [Council Regulation 661/2008…, para 74–77].

1225/2009))[19]. The Court also ruled that artificially low pricing as a result of governmental regulation may be taken into account in anti-dumping investigations, and not only as an element of "state aid" and countervailing duty investigations [Judgment of the General Court of 7 February 2013…, para 55]. The CJEU has also confirmed the EU Commission's approach in substance with respect to Russian gas prices and the Commission's use of the Waidhaus price.

5. Discussion

In this section, we will provide a few thoughts concerning the EU's approach. We first address certain legal-technical issues under the *Anti-dumping Agreement*; and subsequently reflect on certain policy issues, including on the relationship between the *Anti-dumping Agreement* and the *SCM Agreement*.

a. Does the Anti-dumping Agreement permit the EU's cost adjustment?

Article 2.2.1.1 of the *Anti-dumping Agreement* obliges investigating authorities to rely, in principle, on the financial records of the investigated exporters/producers when calculating cost of production. However, Article 2.2.1.1 makes this obligation contingent on two criteria; *First*, the financial records must reflect the generally-accepted accounting principles (GAAP) of the exporting country; and *second*, the financial records "reasonably reflect the costs associated with the production and sale of the product under consideration". Beyond this general principle, Article 2.2.1.1 specifically addresses cost allocation, attaching significance, inter alia, to whether the exporter has been historically using proposed allocation methods. Finally, Article 2.2.1.1 also specifically addresses non-recurring costs and costs in start-up scenarios.

Article 2.2.1.1 thus appears to focus on technical accounting issues pertaining to the quality of an exporter's financial records and the cost data and calculations contained therein [Graafsma, Adamantopoulos]; its purpose is to resolve tensions between the investigated company's records and alternative approaches contemplated by investigating authorities. Case law has reflected this rather technical nature of Article 2.2.1.1. For instance, in *US — Softwood Lumber V*, the panel and the Appellate Body addressed, the investigating authority's allocation of financial expenses; the allocation of general and administrative expenses [WTO Panel Report, *United States — Softwood Lumber V* (DS264), paras 7.233–245; 7.255–269; 7.275–297]; and the allocation of costs for by-products [WTO Panel Report, *United States — Softwood Lumber V* (DS264), paras 7.306–348; WTO Appellate Body Report, *US — Softwood Lumber V* (DS264), paras 146–181]. In *US — Broilers*, the panel addressed the investigating authority's method of allocating costs to a (by)product that fetched starkly different prices in different markets [WTO Panel Report, *US — Broilers* (DS427), paras 7.112–198]. In *EC — Salmon*, the panel addressed the very concept of cost of production, in particular whether non-recurring costs could be considered as cost of production even if they did not benefit the productive activities of a company [WTO Panel Report, *EC — Salmon* (DS337), paras 7.463–516]. In *Egypt — Rebar*, the panel examined whether short term interest income by the company bore a sufficiently close relationship to

[19] However, the Court pointed out that the relevant textual portion does not feature in Article 2.2.1.1 of the *Anti-dumping Agreement*.

cost of production to be relevant as an offset to these costs [WTO Panel Report, *Egypt — Rebar* (DS211), paras 7.389–426].

However, Article 2.2.1.1 does not appear *prima facie* drafted to accommodate concerns about distortions in the market in which the company operates. In particular, it does not appear to authorize the investigating authority to reject correctly recorded costs (correctly recorded from an accounting perspective), on the grounds that the investigating authority does not consider prices on the exporter's domestic market to be sufficiently high.

One can look at the issue from another perspective: Replacing the sourcing price in a company's records with what one believes this price *should* be is not compatible with GAAP. Although Article 2.2.1.1 does not enshrine the exporting country's GAAP as the only benchmark, it is a stretch to argue that a departure from GAAP is permissible not only on the grounds of technical accounting issues, but also due to an investigating authority's belief that the observable input prices on the exporter's market should be different from what they actually are.

A further interesting aspect is the difference between Article 2.2.1.1 of the WTO's *Anti-dumping Agreement* and the corresponding provision in the EU's Basic Anti-dumping Regulation, which governs anti-dumping investigations and the imposition of anti-dumping measures under EU law. Specifically, the second paragraph of Article 2(5) of the Basic Anti-dumping Regulation provides that, if productions are not reasonably reflected in the exporter's records of the party concerned, they shall be adjusted or established, either on the basis of the costs of other producers or exporters in the same country or "on any other reasonable basis, including information from other representative markets". Hence, the Basic Anti-dumping Regulation appears to envisage explicitly what the Commission did in the instant investigations. However, no such language is found in Article 2.2.1.1 of the *Anti-dumping Agreement*.

b. The phrase "particular market situation" under Article 2.2

Another interesting element in this discussion is the phrase "particular market situation" under Article 2.2 of the *Anti-dumping Agreement*. The corresponding provision under EU law [Council Regulation No. 1225/2009…, Article 2 (3)] does not appear to have been explicitly invoked by the EU Commission in the relevant investigations. However, in one of its determination, the Commission also used the phrase that the gas prices on the Russian market were "abnormally low" [Council Regulation 661/2008…, para 58]. This echoes the reference to "artificially low" prices in Article 2(3) of the Basic Anti-dumping Regulation, which features as an example of a "particular market situation". In any event, as explained below, at least one other investigating authority has previously relied on the "particular market situation" concept to justify an approach similar to that of the EU.

Article 2.2 is one of the key provisions of the *Anti-dumping Agreement*. It authorizes an investigating authority, in particular circumstances, to disregard an exporter's domestic sales prices as the basis for calculating normal value. These scenarios include (1) no sales of the like product in the domestic market; (2) lack of comparability due to the particular market situation or (3) lack of comparability due to low volume of sales in the domestic market. In these three scenarios, the investigating authority is required to use other benchmarks as normal value[20].

[20] Namely, the export price into a third market or cost of production in the domestic market. Investigating authorities overwhelmingly use the second option, namely, cost of production.

There is no WTO case law relating to the second scenario, namely, the "particular market situation" criterion. There also appears some, albeit limited, national practice (some of which we reference below). However, there appears to be some expectation in the international trade community that this clause may become of a more wide-spread use in the future, in particular after 2016, when China may no longer be treated as a non-market economy by virtue of Article Paragraph 15(d) of its Protocol of Accession.

Anti-dumping law and practice of WTO Members appear to contemplate a range of circumstances as falling under the term "particular market situation". One scenario is reminiscent of a non-market economy situation, namely, where extensive government controls exists over pricing in a foreign market that prices in that market cannot be considered competitively set. [United States Anti-dumping Manual, Chapter 8, p. 5; Australia Anti-dumping Commission…, p. 1]. Other examples include a situation where a single sale in a foreign market constitutes five percent of sales to the export market; where there are differing patterns of demand in the destination market and the foreign domestic market [United States Anti-dumping Manual, Chapter 8, p. 5]; where there is significant barter trade, or when there are non-commercial processing arrangements [Council Regulation No. 1225/2009…, Article 2 (3)]. The South African investigating authority in one instance appears to have invoked the "particular market situation" phrase to justify a different cost allocation due to significantly different demand patterns for distinct types of chicken meat [Coleman et al.], a situation somewhat reminiscent of the Chinese government's approach in the *Broilers* investigation, referenced above. We are also aware of one investigating authority (other than the EU, namely, India) that has also invoked the "particular market situation" language where the price of inputs was allegedly too low due to dual pricing of propane in Saudi Arabia [Determination by the Indian Ministry of Commerce & Industry, No. 14/5/2009: Anti-Dumping Investigation concerning imports of Polypropylene originating in or exported from Oman, Saudi Arabia and Singapore, para 80], a scenario closely comparable to the Russian gas set of circumstances.

Given the absence of WTO case-law on this point, it is perhaps premature to speculate on whether a WTO panel or the Appellate Body would agree that the phrase "particular market situation" captures all of these different scenarios. Nevertheless, we would venture to offer two thoughts.

First, a distinction can arguably be drawn between a "particular market situation" involving the *product at issue*; and a "particular market situation" involving *inputs*. These are undoubtedly two different factual scenarios. Nevertheless, at least some investigating authorities have treated them in the same manner. Many of the scenarios listed above — drawn from WTO Members' laws or practice — seem related, first and foremost, to the market of the product at issue, rather than inputs into the production of that product. For instance, scenarios characterized by strong government intervention (say, subsidies or state-owned enterprises) may all relate, first and foremost, to governmental intervention with regard to the product at issue, as opposed to an input. Nevertheless, the *Anti-dumping Agreement* does not draw an explicit distinction between the "market" for the final product at issue and the "market" for an input; it is possible that a WTO panel would agree that the term "particular market situation" could, based on its ordinary meaning, encompass both markets for inputs and for the final product. Moreover, an investigating authority might argue that distorting the market for an input also distorts the downstream market for the final good, such that a sharp distinction between these two markets is not meaningful, at least in some situations. Future case law will clarify which of these arguments — or any other arguments — are most compelling.

The second thought is that the criterion of a "particular market situation" informs an investigating authority's decision whether to determine normal value by relying on domestic sales prices or instead on a different value. To recall, Article 2.2 contemplates a determination by the investigating authority that the domestic selling price of the product at issue is not suitable as the basis for normal value. The "particular market situation" is one of the justifications for abandoning the domestic selling price as the basis for normal value. Thus, the "particular market situation" stands at the analytical juncture at which the authority decides whether or not to construct normal value on the basis of costs. However, the EU practice at hand would appear to rely on the "particular market situation" criterion to justify the subsequent non-use of one of the cost elements when constructing normal value. In other words, if the EU were to invoke this criterion in a WTO proceeding, this would mean that this criterion would unfold its effects further downstream in the analysis than Article 2.2 appears to contemplate. Nevertheless, once again, Article 2.2 does not explicitly preclude the use of the "particular market situation" criterion in these circumstances. An investigating authority could argue that, if market distortions relating to an input give rise to a "particular market situation", it would not be illogical to subsequently rely on that allegedly distorted price when constructing normal value through cost calculations. Again, future case law will clarify which of these arguments — or any other arguments — are most compelling.

c. What broader issues does the EU's cost adjustment approach raise?

Beyond the technicalities of the legal analysis of Articles 2.2 and 2.2.1.1, the cost adjustment methodologies raise certain questions concerning the scope and reach of the *Anti-dumping Agreement* and its relationship with the *SCM Agreement*.

A possible view of the *Anti-dumping Agreement* is that it focusses on individual firm pricing behaviour that leads to international price discrimination, under a given set of governmental policies. Arguably, it is not the government's policies themselves that are to be reached or addressed by anti-dumping measures. In fact, advocates of anti-dumping measures sometimes argue that anti-dumping policies are required because governmental policies segment markets and create the very conditions under which a company may operate behind anti-competitive "walls" and from there dump its goods in foreign markets. From this perspective, governmental intervention that distorts the market is the *raison d'être* of anti-dumping policies. However, one may wonder whether it does not amount to "two bites at the apple" that these policies should, at a subsequent step in the analysis, serve again a reason for discarding objectively verifiable price data. If dumping is "caused" by governmental intervention in the market, this may no longer be the sort of "dumping" that the *Anti-dumping Agreement* is after[21].

[21] Previous discussions under the GATT also reflect the view of many Members that "input dumping" was not actionable under GATT rules. Input dumping refers to a situation where a inputs used in manufacturing an exported product are purchased internationally or domestically at dumped or below cost prices, independently whether or not the product itself is exported at dumped prices (see: "Draft recommendations concerning Treatment of the Practice Known as Input Dumping" Ad hoc Committee on Antidumping Practices (ADP/W/83/Rev. 2)).

In contrast, the *SCM Agreement* serves to address distortions in international trade that arise by virtue of governmental intervention in the domestic market in the form of subsidies. However, the *SCM Agreement* is carefully calibrated not to capture certain types of governmental intervention, for instance export restrictions[22]. This limitation, as clarified by WTO case law, suggests that the drafters did not intend to render actionable any kind of governmental intervention that may affect international trade — even if, economically, that intervention has the effect of providing an advantage to domestic industry.

The argument can sometimes be heard that the EU's — and other investigating authorities' — approach may blur this distinction between the *Anti-dumping* and the *SCM Agreements*. But one may also wonder whether this distinction between the two agreements and their functions is valid and not overly simplistic. The fact that a particular measure is not captured by one agreement (*SCM Agreement*), does not mean that it cannot be relevant for action under another agreement. Hence, the correct multilateral analysis and response to the cost adjustment policies of the EU Commission and other investigating authorities should arguably be sought under the *Anti-dumping Agreement*, and not under the *SCM Agreement* and its alleged relationship to the *Anti-dumping Agreement*.

To use a specific example, the fact that dual pricing or export restrictions in the form of export duties may not *per se* be prohibited e.g. under the GATT 1994 or the *SCM Agreement,* does not *ipso iure* render a cost adjustment in response to dual pricing incompatible with the *Anti-dumping Agreement*. In the end, it is the proper interpretation and application of the *Anti-dumping Agreement* that will decide the matter.

Moreover, the policy concerns underlying the EU Commission's — and other investigating authorities' approach — cannot be taken lightly. The gas pricing policies of the Russian government do provide Russian producers with an economic advantage, and it is obvious that high export prices charged by Gazprom cross-subsidize domestic prices. More generally, any dual pricing system can result in a considerable competitive advantage for domestic producers.

At the same time, the existence of a genuine or legitimate policy concern does not mean that a legal text at the international level must necessarily contain an answer to that perceived problem. WTO agreements occasionally do present explicit or implicit lacunae [WTO Appellate Body Report, *US — Hot-rolled Steel* (DS184)] and it is not unheard of that even very important legal and economic issues are not disciplined by WTO law, are therefore left to a WTO Member's government discretion and may be placed beyond the reach of trade remedy measures.

However, accepting the EU's and other investigating authorities' cost adjustment practices would require WTO panels and the Appellate Body to also set carefully-reflected boundaries. This would be necessary to ensure that cost adjustments do not encroach on lower prices/costs of input that reflect natural comparative advantage and not any (real or perceived) objectionable governmental policy. Finally, assuming that the subject cost adjustments were ruled to be permissible in principles, firm disciplines should govern the investigating authorities' choice of proxy values.

[22] According to [WTO Panel Report, *US — Export Restraints* (DS194)], export restraints do not constitute one of the forms of financial contributions under Article 1.1(a)(1) of the SCM Agreement. Moreover, the benefit and specificity analysis may present challenges. See also [Vitaliy Pogoretskyy and Daniel Behm, 2010, p. 17–20].

6. Conclusions

It remains to be seen how the WTO panels in the disputes at hand — be it DS474 or the biodiesel-related disputes DS473 and DS480 — will address and resolve the fascinating legal issue raised by the EU's cost adjustment methodologies at issue.

As described in more detail above, the big-picture question is whether the *Anti-dumping Agreement* permits investigating authorities to adjust for what they believe is a distorted domestic price. As a guiding principle, it is more the *SCM Agreement* that contemplates action that addresses governmental interventions in the market, whereas the *Anti-dumping Agreement* addresses the pricing behaviour of enterprises and any resulting price discrimination. However, these broader principles may not be dispositive of the issue. If the *Anti-dumping Agreement* permits the type of cost adjustments practiced by the EU, the question is which particular provision provides the legal basis for doing so. We have seen that Article 2.2.1.1 appears to be more geared towards technical accounting issues, rather than to the problem of a distorted market price. We have also considered the possibility that the phrase "particular market situation" may be invoked as justification for the cost adjustment methodology, under Article 2.2. However, given the paucity of case-law concerning this term, as well as the diversity of national practice in WTO Members, it is particularly difficult to estimate how a WTO panel or the Appellate Body would decide this matter.

The rulings of the panels in DS 474, as well as in DS473 and 480, may provide important guidance on the reading of Articles 2.2 and 2.2.1.1. They may moreover have significant impact not only on the industries at hand, but also on the actions of investigating authorities in a range of different factual scenarios in future disputes, including on the treatment of China and Vietnam once these Members are no longer treated as non-market economies. This is because the EU's cost adjustment methodology is in essence an application of a non-market economy situation/methodology within narrow limits, with respect to a particular input.

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