

| INCEPTION IMPACT ASSESSMENT  |  |                 |              |
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| TITLE OF THE INITIATIVE  | Possible change in the methodology to establish dumping in trade defence investigations concerning the People's Republic of China <sup>1</sup> |                 |              |
| LEAD DG – RESPONSIBLE UNIT – AP NUMBER   | DG TRADE, UNIT H1  | DATE OF ROADMAP | January 2016 |
| LIKELY TYPE OF INITIATIVE  | Response to the expiry of certain provisions of the Accession Protocol to the WTO of the People's Republic of China                            |                 |              |
| INDICATIVE PLANNING  | <i>Insert hyperlink to forecast report</i>   |                 |              |
| ADDITIONAL INFORMATION   | <i>Insert link to "Commission decides" or to the specific website for the initiative</i>   |                 |              |
| <b>This Inception Impact Assessment is provided for information purposes only and can be subject to change. It does not prejudice the final decision of the Commission on whether this initiative will be pursued or on its final content and structure.</b>   |  |                 |              |
| A. Context, Subsidiarity Check and Objectives  |  |                 |              |
| Context  |  |                 |              |
| <ul style="list-style-type: none"> <li>When China joined the World Trade Organisation (WTO) in December 2001, a transitional arrangement for their accession allowed for a specific methodology for the calculation of dumping. This transitional arrangement was introduced in Section 15 of the Protocol on the accession of the PRC to the WTO. Some of the provisions included in the protocol of accession of China will expire in December 2016.<sup>2</sup></li> <li>As a result of this expiry, the Commission services are analysing the possible impact on the EU's anti-dumping legislation<sup>3</sup>. Should an amendment to the current legislation be deemed necessary, it would entail a Commission proposal to be adopted through ordinary legislative procedure by the Council (under a qualified majority vote) and the European Parliament.</li> <li>Shortly after the accession of China to the WTO, a bilateral process with the EU was established in order to give them the possibility to demonstrate that they are a market economy under EU domestic rules. Under this process, the EU would remove them from the list of non-market economy countries in the EU anti-dumping legislation as soon as they demonstrated that they met five criteria set by the EU. On the basis of continuous assessment, to date China have not met these five criteria. Given the impending expiry of certain provisions of the Protocol on the accession to the WTO of China coupled with the fact that they are not yet a market economy in the sense relevant for EU anti-dumping legislation, the implications for the EU's anti-dumping legislation must be examined.</li> <li>There are no other policy initiatives which specifically address the same issue.</li> <li>Though the existing anti-dumping rules specifically concerning non-market economies have not been evaluated as such in isolation, an <i>ex post</i> evaluation of the EU's trade defence instruments was carried out and published in February 2012.</li> <li>This initiative is not part of the REFIT agenda.</li> </ul> |  |                 |              |
| Issue  |  |                 |              |
| Under WTO rules, anti-dumping duties, additional to tariffs, can be imposed on products from third countries if an investigation demonstrates that these products are dumped and causing injury to the domestic industry. The EU has implemented the WTO rules in the form of an anti-dumping basic  |  |                 |              |

<sup>1</sup> This issue arises also in relation to other countries in a similar situation.

<sup>2</sup> The inception impact assessment focuses on China. However, the same issue arises in relation to other countries in a similar situation.

<sup>3</sup> Council Regulation (EC) No 1225/2009.

regulation (Council Regulation No. 1225/2009 of 30.11.2009) and an anti-subsidy basic regulation (Council Regulation No. 597/2009 of 11.6.2009). The initiation of investigations is based on complaints prepared by EU industry and is subject to strict conditions. The complaints must contain sufficient *prima facie* evidence of the existence of dumping or subsidization in the exporting country, and of injury suffered by the EU industry as a result.

Under the standard rules, in normal market circumstances, dumping is calculated by comparing the export price of a product exported to the EU with the domestic prices (or, if these are not reliable, with the costs of production) of the same product in the exporting country.

WTO rules provide for special treatment for countries which have a complete or substantially complete monopoly of their trade and where all domestic prices are fixed by the State. In practice, domestic prices and costs in those countries are not used as the basis to compare with export prices because they are considered unreliable owing to pervasive State influence in the economy. Instead, investigating authorities use data from another market economy country (so called 'analogue country') as the basis for calculating dumping margins. This is the so-called Non-Market-Economy methodology.

In the economies in transition, prices and costs do often still not reflect normal market forces. Therefore, under the relevant language of the Protocol on the accession of China to the WTO, other WTO members are not obliged to consider China a market economy in anti-dumping proceedings. The EU legislation makes use of that possibility, and as a result it mandates to use normally prices or costs from an “analogue country” to calculate the level of dumping of products from China. Certain provisions in the Protocol on the accession of China to the WTO expire in 2016, and this may affect the ability of other WTO Members, such as the EU, to use the Non-Market-Economy methodology automatically.

**The Commission services are exploring a number of possible options to give effect to the expiry of those provisions. Given the fact that, to date, China has failed to demonstrate that they are a market economy under the criteria established in the EU anti-dumping legislation and given the slowdown of the Chinese economy coupled with the significant excess capacities in many sectors, notably in steel, such analysis is of particular importance.**

It is expected that using the standard methodology for calculating dumping margins in anti-dumping cases concerning China will, on average, result in lower anti-dumping duties. This is because this methodology will not take into account the remaining pervasive distortions in their economies. As a result, it is expected that lower anti-dumping duties may not offset the negative effects of dumping and may further increase dumped imports causing further injury to the EU industries concerned. In turn, this further injury to the EU industries concerned is likely to give rise to potential risk to jobs in the EU.

In order to ascertain the level and extent of the impact of applying the standard methodology in anti-dumping investigation concerning China, the Commission services commissioned an external study on this issue. The results of the study should be available in May 2016.

Therefore, the main problem is how to give effect to the expiry of certain provisions of the Protocol on the accession of the PRC to the WTO while, at the same time, minimising negative impact, including potential risk to jobs for the EU.

All stakeholders in Trade Defence investigations will be affected to varying degrees, including Union producers, importers, users, consumers and exporting producers in China. However given that the vast majority of the products under anti-dumping measures are intermediate industrial products, stakeholders in those industries will be most affected.

#### **Subsidiarity check**

The initiative falls under the exclusive competence of the EU according to Article 207 of the Treaty on the Functioning of the European Union (TFEU). Therefore, the subsidiarity principle does not apply.

#### **Main policy objectives**

The objective is to give effect to the expiry of certain provisions of the Protocol on the accession of the PRC to the WTO, while at the same time, limiting negative effects on EU industry and employment.

Within that context the objective is to ensure the continued ability of the EU's trade defence legislation to tackle the remaining distortions in their economies and thereby to ensure the continued effectiveness of the EU trade defence legislation to deal with unfair trade practices from the EU trading partners.

## B. Option Mapping

### Baseline scenario – no EU policy change

The baseline scenario (Option 1) would leave the current legislation and practice, concerning the treatment of the PRC unchanged. The impact of the baseline option will be assessed.

### Options of improving implementation and enforcement of existing legislation or doing less/simplifying existing legislation

There are no possible changes in the implementation or enforcement of the existing legislation which can address the issues.

### Alternative policy approaches

In addition to the baseline scenario described above as Option 1 there are in principle two other possible basic options being considered:

Option 2 Removing China<sup>4</sup> from the list of non-market economy countries in the EU anti-dumping legislation. It would require an ordinary legislative procedure amending the antidumping regulation. If non-market economy conditions continue to prevail in a particular sector, then it may be possible for the Commission to prove that domestic prices and costs in this country must be disregarded and that normal value must be calculated on third country costs on a case-by-case basis. Otherwise, the standard anti-dumping methodology would be applied to investigations concerning their exports, with no account being taken of any distortions in their economy as compared with a normal market economy.

Option 3 Modifying the methodology to calculate dumping in EU trade defence investigations as part of a package including additional measures aimed at meeting the above-mentioned policy objectives. EU anti-dumping legislation would be modified by removing the PRC from the list of non-market economy countries while, at the same time, strengthening other provisions of the trade defence legislation. The additional measures could include:

- Grandfathering, i.e. amending existing provisions to safeguard the definitive anti-dumping measures already in place against the PRC. This approach would not allow any requests for interim reviews for measures concerning China until the initiation of expiry reviews. Expiry reviews and interim reviews would then be carried out under the new rules, but applying the existing principle that, in the absence of a change in factual circumstances, the methodology of the initial investigation is applied. This could extend the effectiveness of the existing measures from the dates mentioned above until the expiry of measures, i.e. for an additional period of up to five years.
- Introducing new or amended provisions in the anti-dumping legislation designed to deal with situations where there are significant distortions affecting prices and/or costs of the exporters in the country of export. The presence of these distortions can create a 'particular market situation' which would result in the following (a) sales prices in the domestic market of the exporting country would be rejected and normal value constructed on basis of costs and (b) costs of exporters affected by these distortions would be adjusted by reference to costs in another representative country. The existence of such distortions may be rebutted by exporters.
- Limiting the use of the 'lesser duty rule' which would not be applied in cases where significant distortions in the export market were found. This would allow (a) to avoid capping the duty at the

<sup>4</sup> N.B. the issue also arises in relation to other non-market economy countries that are in a similar situation.

injury margin, which is not required by the WTO and (b) in case of parallel anti-dumping and anti-subsidy investigations on the same product, to cumulate duties without capping them to the injury margin, thereby allowing an additional possible layer of protection for EU industry.

- Amending the anti-subsidy legislation to allow for the investigation of new subsidies discovered in the course of the investigation.

#### **Alternative policy instruments**

Dumping is practiced by companies as part of a pricing strategy to gain market share in export markets. While it is condemned under international trade law and actionable when causing injury to the industry in the export market, self-regulation or market arrangements are not relevant and in any event would be impossible to implement or monitor. Hence, there are no non-regulatory and market-based solutions available. The envisaged amendments must be included in the legislation to be enforceable.

#### **Alternative/differentiated scope**

This is not applicable as there is no differentiation between small and large enterprises in the application of trade defence legislation (apart from some procedural rules).

#### **Options that take account of new technological developments**

Not applicable.

#### **Preliminary proportionality check**

The options proposed to address the problem respect the principle of proportionality, as they do not go beyond of what is strictly necessary to achieve the main policy objective specified above, that is to give effect to the expiry of certain provisions of the Protocols on the accession of certain non-market economy countries to the WTO and the accession of other non-market economies to the WTO, while at the same time, limiting negative effects on EU industry and employment.

### **C. Data Collection and Better Regulation Instruments**

#### **Data collection**

An external study commissioned by DG Trade assessing the economic impact in the EU of removing the non-market economy methodology in anti-dumping investigations concerning the PRC is ongoing. Preliminary results of this study show that the economic impact of using the market economy methodology in anti-dumping cases concerning the PRC on the basis of a representative sample of recent anti-dumping investigations concerning that country. Using economic modelling and extrapolating from ten selected cases the impact on the anti-dumping margins to employment in the sectors affected the study calculated the short term, long term, direct and indirect effects of this option.

The study needs to be completed with an assessment of the effects of the additional factors (option 3). These can be estimated on the basis of the data already collected for the study just completed.

It is foreseen that the results on the economic analysis would also be broken down at the sectoral and Member State level. Information on the main regions concerned will also be provided, where possible.

#### **Consultation approach**

In the past months, the Commission has received numerous letters and position papers and has held several meetings with the main stakeholders concerned. These include numerous industry representative organisations including AEGIS (a group established to oppose the changes in dumping calculation methodology representing nearly 30 European trade associations), Business Europe, Bundesverband der Deutschen Industrie (BDI), Foreign Trade Association (FTA), European Round Table of Industrialists (ERT). As a result the views of the major stakeholders are already available to the Commission.

Nevertheless, we propose that all TDI stakeholders will again be consulted on the matter. An on-line 10-week open public consultation based on a questionnaire will be carried out (foreseen publication date 10/2/2016). In addition, a public conference will be held in Spring 2016 whereby stakeholders will

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| <p>have opportunity to present their views. Representatives of Union producers, importers, users, consumers and Chinese exporting producers to the EU may attend. The comments and positions of the stakeholders will be taken into account in drafting the IA.</p>   |
| <p><b>Will an Implementation plan be established?</b></p> <p><input type="checkbox"/> Yes <input checked="" type="checkbox"/> No</p>  |
| <p style="text-align: center;"><b>D. Information on the Impact Assessment Process</b></p>   |
| <p>Assessing the impact of this issue is already underway. An external economic study is ongoing and already provided a preliminary analysis of the economic impact of Option 2 was completed in December 2015, but further research will be undertaken.</p> <p>The ISG was set up in February 2016. The following Commission departments and services were invited: Secretariat-General, Legal Service, Agriculture and Rural Development, Economic and Financial Affairs, Taxation and Customs Union, Internal Market, Industry, Entrepreneurship and SMEs, Energy, Environment, Employment, Social Affairs and Inclusion, Competition, Budget, Regional and Urban Policy, European Anti-Fraud Office, Justice, Consumers and Gender Equality, and the European External Action Service.</p>  |
| <p style="text-align: center;"><b>E. Preliminary Assessment of Expected Impacts</b></p>   |
| <p><b>Likely economic impacts</b></p> <p>Given that anti-dumping measures cover only a limited number of specific products imported from the PRC, the economic impact of the various options might be limited in macroeconomic terms e.g. impact on EU GDP. Indeed while some of the options would result in lowering the deterrent effect (dissuading producer from engaging in dumping practices) of trade defence measures, the macro economic impact (i.e. on GDP or investment) would remain limited, while the impact is expected to be mainly felt at micro-economic level. However, anti-dumping measures can be essential to provide relief to certain EU producers. Therefore, the micro-economic effect on those companies injured by dumped imports can be significant, including in certain cases resulting in the closure of factories, the delocalisation of production or the laying off of redundant workers. Hence, in the framework of the impact assessment the likely economic impacts will be focussed on employment in the EU manufacturing industries which are or might potentially be directly and indirectly affected by dumping from the PRC.</p> <p>Concerning the baseline scenario (option 1), approximately 230,000 direct jobs are related to the manufacturing of goods on which there are measures currently imposed on the PRC. There is a clear risk that this option could put the EU in breach of WTO, enabling counteraction according to WTO law. The economic impact of such a scenario depends on a number of factors currently unknown, with potential costs including in employment terms.</p> <p>Regarding option 2, the preliminary results of the ongoing external study obtained in December found that there could be significant potential job losses in industries injured by dumping from China. The total potential impact on jobs increases when indirect effects on upstream sectors are taken into account even if some downstream sectors may benefit from lower cost inputs. The negative effect increases further if the potential entry of Chinese companies' active in other industries, possible due to discontinuation of the deterrent effect AD analogue country methodology, is taken into account.</p> <p>Regarding option 3, the impact of the additional measures needs to be analysed further.</p> |
| <p><b>Likely social impacts</b></p> <p>The social impacts arising from the impact on employment of the various options, as mentioned in the previous section, will be further analysed and quantified in the framework of the impact assessment.</p>  |
| <p><b>Likely environmental impacts</b></p> <p>The impact on the environment in the EU is expected to be minimal. It is possible that, as a result of changing the dumping calculation methodology for the PRC, there could be a change in the level of manufacturing activity in the EU and hence the associated environmental costs. However, it is expected</p>   |

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| <p>that these environmental impacts would be small given the very low level of imports which are affected by anti-dumping measures.</p>  |
| <p><b>Likely impacts on simplification and/or administrative burden</b></p>  |
| <p>The initiative has no significant impact regarding simplification.</p> <p>The initiative does not involve an increase of administrative burden for stakeholders.</p> <p>For the DG Trade services there may be an increased burden depending on the option chosen.</p>  |
| <p><b>Likely impacts on SMEs</b></p>   |
| <p>Changing the methodology for calculating dumping in anti-dumping cases will impact on SMEs as well as large companies. However, given that there is no differential treatment in the substantive AD legislation linked to the size of enterprises, an assessment of the impact on SMEs is not necessary.</p>  |
| <p><b>Likely impacts on competitiveness and innovation</b></p>   |
| <p>The effectiveness of trade defence instruments contributes towards a level playing field. Weaker instruments put EU industries at a competitive disadvantage with the risk that EU industry in certain sectors could disappear. Therefore it is important to have strong trade defence instruments for the EU to maintain investment, R &amp; D and innovation in Europe. On the other hand, cheaper inputs may help increase competitiveness in other sectors.</p> |
| <p><b>Likely impacts on public administrations</b></p>   |
| <p>As trade matters are an exclusive EU competence, no transposition issues arise.</p>   |
| <p><b>Likely impacts on third countries, international trade or investment</b></p>   |
| <p>China expects a change in the dumping calculation method from December 2016. No change in the EU legislation would almost certainly be claimed by China as a breach of EU's WTO obligations. This would probably result in counter action by China.</p> <p>Option 2 may cause trade diversion to the EU from other WTO members should they decide to follow a different path.</p> <p>It cannot be excluded that option 3 may also give rise to further action.</p>  |