

**Binational Panel Decision on Remand  
Flat Coated Steel Products  
MEX-94-1904-01**

**I. SUMMARY OR PRIOR PROCEEDINGS**

1. On September 27, 1996, this binational panel issued its decision and order in the above captioned proceeding. In that decision, this panel remanded the case to SECOFI (the Investigating Authority) and directed SECOFI to comply with various requirements set out in the panel's order. Those requirements related to issues affecting the competence of certain officials of SECOFI and to specific aspects of SECOFI's definitive resolution of August 2, 1994. The original deadline for the remand (120 days) was ultimately extended to April 30, 1997, due to disputes over access by representatives of one of the interested parties to the confidential record, and other considerations.

2. On April 30, 1997, SECOFI presented the results of the remand to the panel and to the interested parties. Challenges to the remand results were filed by only two interested parties, New Process Steel Corporation, and Inland Steel, on May 29 and May 23, 1997, respectively. Those comments were limited to SECOFI's compliance with this panel's decision as it related to recalculation of dumping margins, and to an issue that related procedurally to SECOFI's remand results. A response to the challenges was filed by SECOFI on June 16, 1997.

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In an order executed by the panel and issued by the Secretariat on July 3, 1997, the deadline for the panel's decision on the remand was extended to September 15, 1997, to allow completion of English translations of key documents and their study by the panelists. This decision was made pursuant to Rule 73(6) of the NAFTA Article 1904 Rules of Procedure.

### **II. SCOPE OF THIS DECISION**

3. None of the interested parties challenged the remand results as they related to SECOFI's determination of injury or threat of injury, and there were no challenges to many of the dumping issues addressed in the remand results. New Process has challenged certain of the dumping determinations, and Inland seeks only to have its dumping margin conformed to any new calculation of New Process's dumping margin. Consequently, this decision is limited to the issues raised by New Process and Inland.

### **III. ISSUES RAISED BY NEW PROCESS**

4. In its decision of September 27, 1996, the panel, *inter alia*, directed SECOFI to use the cost data and export prices provided by New Process to determine dumping margins. The Panel also suggested, "as guidance," that

"it is not unreasonable to expect that each of these different types of steel to have different costs...[and] to the extent prime steel products, secondary steel products

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are analogous to separate product codes, consistency of treatment would suggest that separate reconstructed values be determined for these different types of steel.”<sup>1</sup>

5. New Process’ substantive challenge to the remand results is focused on the accounting methodologies used by SECOFI in that they allegedly

“do not meet generally accepted accounting principle [GAAP] requirements... and do not take into account the common sense principle that one should expect different goods to have different costs. Thus, these methodologies fail to calculate appropriate individual costs for prime, secondary and scrap.”<sup>2</sup>

6. New Process further alleges that the errors in SECOFI’s methodology create huge dumping margins where none would otherwise exist, and that the methodology was not in accordance with Generally Accepted Accounting Principles (GAAP). New Process contends that raw material costs and indirect manufacturing costs should be allocated on the basis of relative sales value of prime, secondary and scrap products; that New Process’ hand labor cost allocations, actual profit and overhead expenses be used; and that New Process’ credit expense data be accepted and used in the calculations.<sup>3</sup>

7. SECOFI, in its rebuttal comments of June 16, 1997, has defended the

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<sup>1</sup> *Flat Coated Steel Products*, case no. MEX-94-1904-01, at paras. 224, 225.

<sup>2</sup> New Process Submission of June 29, 1997, at 3.

<sup>3</sup> *Ibid.*

**NON CONFIDENTIAL**

methodology used in the remand results for calculation of costs for New Process, as being consistent with GAAP and otherwise appropriate.

8. The panel review these issues under Article 238 of the Federal Fiscal Code, the applicable standard of review for this panel.<sup>4</sup> We consider raw material costs first.

**A. Raw Material Costs**

9. 1. SECOFI calculated a single raw material cost for prime and secondary coils produced by New Process. This was an average cost, which SECOFI allocated on a per ton basis to each ton of non-scrap steel that New Process sold. Whether the item sold was prime or secondary steel, it was accorded the same per ton cost. New Process also sold a category of product called “scrap.” SECOFI treated scrap as a by-product. This meant that SECOFI essentially allocated a zero raw material cost to scrap, but, at the same time, it deducted from the per ton materials costs of the other products (prime and secondary coils) the per ton revenue that New Process received from the sale of scrap.<sup>5</sup> The remaining materials costs were then allocated between primary and secondary products.

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<sup>4</sup> Article 238 is the central portion of the applicable standard of review in NAFTA, Annex 1911. See our September 27, 1996 decision, pages 15-19.

<sup>5</sup> See Remand Results, paras. 42, 47, 48. SECOFI excluded scrap steel from the case, because it is imported under different tariff headings than those applicable to the products covered by the case. Remand Results of April 30, 1997, para. 35.

**NON CONFIDENTIAL**

10. In its application to this Panel, New Process limits its challenge to the method SECOFI used to allocate an average raw material cost across all products that New Process sold. New Process essentially claims that International Accounting Standard No. 2 mandates that raw material costs in the circumstances of this case be allocated on the basis of the average sales dollars generated from sales of each of these products- prime, secondary and scrap. In particular, New Process argues that GAAP, International Accounting Standard 2(12), requires the use of relative sales value to allocate costs that are not separately identifiable. (New Process Challenge to the Determination on Remand, at 5-6.).

11. Paragraph 12 of International Accounting Standard 2 provides in pertinent part as follows:

A production process may result in more than one product being produced simultaneously. This is the case, for example, when joint products are produced or when there is a main product and a by-product. When the costs of conversion of each product are not separately identifiable, they are allocated between the products on a rational and consistent basis. The allocation may be based, for example, on the relative sales value of each product either at the stage in the production process when the products become separately identifiable, or at the completion of production.

12. As the language itself indicates, Accounting Standard 2(12) is not exclusive; it states that “The allocation may be based, *for example*, on the relative sales value of each product...” In other words, it does not suggest that this is the *only* methodology. Thus, it is not

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correct to say that use of “relative sales value” to allocate raw material cost is mandatory. New Process appears to argue instead that use of “relative sales value” is the only *rational* method for allocating raw material costs in this case.

13. 2. An essential part of New Process’s argument is that the method that SECOFI chose to follow was irrational and necessarily created distorted costs – and that the only way to avoid these irrational distortions was to follow the “relative sales value” method in International Accounting Standard 2(12).

14. SECOFI states the contrary. SECOFI explains that it rejected the relative sales value allocation methodology because (1) it results in a change in manufacturing cost whenever there is a change in relative sales values; (2) it implies that two grades of products made from the same material (prime sheet) would have different production cost; and (3) it is inconsistent with New Process’ proposed methodology for allocating labor costs, which is based on sales volume (quantity) rather than value.<sup>6</sup>

15. SECOFI asserts that since both prime and secondary steel use the exact same materials, the materials costs for both are identical. (Again, scrap is by SECOFI’s analysis a by-product of prime and secondary steel production and thus no net costs can be assigned directly to

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<sup>6</sup> Remand Results, para. 41.

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it.)<sup>7</sup> SECOFI's methodology<sup>8</sup> essentially allocates raw material costs between prime and secondary products by the relative sales quantity of the two products, after adjusting for the recovery value of the scrap steel. This methodology results in the use of the same unit raw material costs for both prime and secondary grade steel. SECOFI believes this method is rational.

16. The analysis of whether either method is rational – the New Process method or the SECOFI method – must take into account the information New Process submitted and the data available to SECOFI.

17. New Process stated that its raw materials consisted of unprocessed prime coils and unprocessed secondary coils. New Process said it was able to produce an unspecified quantity of secondary finished product from its prime raw material, and an unspecified quantity of prime finished product from its secondary raw material (and vice versa).<sup>9</sup> If New Process had data on the proportion of prime raw material it used to make secondary finished products (and vice versa), it does not appear that New Process submitted this data to SECOFI. Had New Process done so, it is possible that SECOFI would have had some other basis to determine raw material costs, such as the proportions of prime and secondary raw materials used to produce,

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<sup>7</sup> Remand Results, para. 42.

<sup>8</sup> Remand Results, paras. 44-50.

<sup>9</sup> See New Process Submission, at 5-7.

**NON CONFIDENTIAL**

respectively, the prime and secondary finished products. Apparently, SECOFI did not have the ability to do this based on the information available to it, and New Process does not now contend that SECOFI should have done this.

18. Equally, SECOFI does not claim that New Process failed to provide necessary information on raw material costs, or that SECOFI was required to determine raw material costs based on “best information available.” Instead, SECOFI argues that (1) that the “relative sale value” method proposed by New Process was not rational; and (2) that only SECOFI’s method was a rational and appropriate method.

19. **3.** The central question is whether SECOFI’S used a lawful and rational method in view of the limited information available. The issue is not whether New Process’ methodology is more rational, or whether this panel, if deciding the issue *de novo*, would follow New Process’, SECOFI’s or some other methodology.

20. SECOFI’s methodology for allocating materials costs does not appear to be inconsistent with any provision of law, nor with Article 2(II) of the Regulations Against Unfair Trade Practices in International Commerce. That regulation simply provides:

“The cost of production shall be calculated based on the sum of the costs, both fixed and variable, of materials and fabrication, in the course of normal commercial operations, in the country of origin, to which is added a reasonable amount for administrative expenses and other general expenses.”



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21. Article 22 of that regulation also states: “In any event, generally accepted accounting principles shall be followed.”

22. New Process appears to claim that SECOFI has not followed generally accepted accounting principles (“GAAP”) in allocating raw material costs. In its strongest argument, New Process argues that SECOFI’s method does not follow GAAP, because the method is not one that any business would follow:

As demonstrated below, the Investigating Authority method makes it appear irrational to sell secondary material under any circumstances, since the costs the Investigating Authority allocates to secondary products will always exceed the revenues that can be obtained. This result is wholly inconsistent with GAAP. . . . [N]o one in the market uses cost allocation methods that attribute prime costs to secondary products.

New Process, Challenge to the Determination on Remand, p. 9.

23. We agree with New Process that if no business would use a particular cost allocation method, that method would not be consistent with GAAP. An accounting method must reflect business reality. Businesses pay accountants to develop accounting methods that are useful for the business or for the financial community. If no business would use a particular method to keep track of its costs in a particular circumstance, the method, by definition, cannot be “generally accepted” in that circumstance.

**NON CONFIDENTIAL**

24. Our problem is that New Process has not supported its argument with evidence in the administrative record. It has not presented evidence sufficient to prove that no business would use SECOFI's method. Although it has provided an "example" of the Investigating Authority's approach, the example depends on a hypothetical price for secondary coils. There is no evidence that New Process's sample price (or value) for secondary coils is representative – or that prices in the United States, or export prices during other periods of time, are not at higher levels (or that SECOFI's method would not produce a profit at higher price levels). It may well be that during the (limited) period of investigation, market conditions were such that it was impossible to sell secondary coils at a price above cost, and the fact that all or most sales were made below cost does not in itself demonstrate that the accounting methodology was faulty, particularly with a cyclical product such as steel. In summary, New Process has not supported its argument with evidence.

25. We also note that SECOFI's method is not precluded by GAAP. While International Accounting Standard 2(12) suggests as an example that "relative sales value" be used where two products are jointly produced, the only requirement is that the costs be "allocated between the products on a *rational and consistent basis*." (Emphasis supplied.) New Process does not disagree that SECOFI's method was applied on a "consistent basis." As we have noted, New Process has not given the panel sufficient evidence to support its argument that SECOFI's

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method is not “rational” because no business would follow it.

26. We must affirm SECOFI’s methodology unless it lacks legal foundation, is in violation of the law, erroneously weighs the facts, or exceeds SECOFI’s discretion, thus violating Federal Fiscal Code Article 238. Based on the evidence in the administrative record, SECOFI’s method of allocating raw material cost has not been shown by New Process to violate GAAP, or Articles Article 2 or 22 of the Regulations Against Unfair Trade Practices in International Commerce. We also note that SECOFI’s methodology has been used in at least one U.S. Department of Commerce case, *Circular Welded Steel Non-Alloy Steel Pipe from the Republic of Korea*.<sup>10</sup> There, the U.S. Department of Commerce allocated equal manufacturing costs to both “prime” and “second-grade” pipe, in that instance at the request of the foreign exporters (respondents). The respondents had claimed that “they expend the same material, capital, labor and overhead for both grades of pipe and therefore costs should be allocated in such a manner.” While the facts were somewhat different, the end result was similar to the allocation methodology used by SECOFI in this instance. We cite this U.S. determination not as precedent, but simply as a further indication that, in the absence of evidence to support New Process’s argument, SECOFI’s allocation of raw material costs is not automatically irrational or in violation of Federal Fiscal Code Article 238. Accordingly, SECOFI’s methodology of allocating raw material costs is affirmed.

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<sup>10</sup> 57 Fed. Reg. 42,942 (1992).

**B. Other Cost Allocations**

27. 1. New Process asked SECOFI to allocate hand labor costs between coated and non-coated products based on production volume (quantity) of coated and non-coated products, and then on the basis of coils versus sheets. This was based on the conclusion that different work is required to produce differing products, and that the hand labor effort will vary with production volume for each product category.<sup>11</sup> SECOFI accepted this methodology generally but rejected New Process' "relative labor cost associated with each process," apparently because New Process did not provide sufficient information as to the sources or the methodology which demonstrate that the hand labor costs for the two products are different.<sup>12</sup> Thus, for example, SECOFI notes that the New Process' labor cost data as provided to SECOFI could be interpreted in at least four different ways.<sup>13</sup> SECOFI also suggests that had New Process' methodology been used, the dumping margins for the products under investigation would have been increased.<sup>14</sup>

28. New Process objects that SECOFI at no time asked for additional information or clarification, or sought to verify the information presented, and thus asserts that SECOFI was

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<sup>11</sup> New Process Submission, at 18.

<sup>12</sup> Remand Results, para. 53.

<sup>13</sup> SECOFI Submission, at 29.

<sup>14</sup> SECOFI Submission, at 30.

**NON CONFIDENTIAL**

obligated to accept the information submitted at face value.<sup>15</sup> We also note that this issue has an unusual administrative context. As described in the panel's decision of September 27, 1996, SECOFI did not advise New Process of any deficiency in New Process's responses to the questionnaire. SECOFI did not conduct a verification of New Process's data and, thus, there was no verification visit or report from which New Process could learn of any problem. Nor did SECOFI conduct a disclosure conference to advise New Process of any questions or to seek any clarification. Ordinarily, it is a goal of administrative procedure for all issues to be disclosed, discussed and resolved by the administrative agency conducting the proceeding. Here, this goal was not achieved.

29. The failure of SECOFI to seek clarification of New Process' earlier submissions, and instead to reject their methodology in part for lack of clarity, is troubling. There appears to be no persuasive reason why SECOFI, reviewing New Process' submissions in response to this panel's decision of September 27, 1996, could not have asked New Process for clarification of its methodology.<sup>16</sup> Such practice would "help to ensure that its calculations are based on accurate

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<sup>15</sup> New Process Submission, at 22.

<sup>16</sup> The panel notes that the U.S. Department of Commerce routinely issues "deficiency letters" after it has reviewed submissions of respondents in antidumping cases, in which it seeks (and routinely receives) clarification of those portions of the submissions which are unclear or incomplete. However, while Commerce "may request any person to submit factual information at any time during a proceeding," it is not required to do so. 19 C.F.R. §353.31(b)(i).

**NON CONFIDENTIAL**

and complete data”.<sup>17</sup> The panel also notes that NAFTA requires that the parties in an antidumping proceeding in Mexico must be afforded an opportunity “to present facts and arguments in support of their positions prior to any final determination, to the extent time permits...”<sup>18</sup> There is no evidence in this proceeding that SECOFI has sought to comply with the letter or spirit of this requirement, which of course applies to investigations initiated after January 1, 1994.

30. As this Panel noted in its September 27, 1996 decision, several provisions of law applicable to anti-dumping investigations in Mexico give foreign exporters a legal interest in presenting evidence and in having that evidence considered. *See generally* this Panel’s decision dated September 27, 1996, paragraphs 93 through 97. We also noted that international treaties like the General Agreement on Tariffs and Trade (GATT) are considered a part of internal law in Mexico and applicable to anti-dumping investigations. This includes Part I of the Agreement on Implementation of Article VI of the General Agreement on Tariffs and Trade (“1979 GATT Anti-Dumping Code”). Article 6, Paragraph 7 of the 1979 GATT Anti-Dumping Code requires that “all parties shall have a full opportunity for the defense of their interests”.

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<sup>17</sup> Crystal and Solid Polystyrene from the United States, Case No. MEX-94-1904-03 (1996), at 42.

<sup>18</sup> NAFTA, Annex 1904.15(f).

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31. We believe that in the circumstances of this case, where SECOFI had a question about the data submitted by a foreign exporter, it would appear to have been an easy matter for SECOFI to seek a clarification from New Process. SECOFI has not mentioned any unusual burden in doing so. In these circumstances, a failure to seek clarification did not give New Process “a full opportunity for the defense of their interests” within the meaning of Article 6, Paragraph 7 of the GATT Anti-Dumping Code. For that reason, it was illegal under Article 238(III) of the Federal Fiscal Code.

32. New Process did not specifically mention Article 238(III) in its Challenge to the Determination on Remand. However, it clearly mentioned the procedural error by SECOFI and the Panel treats this mention as a reference to Article 238(III). On remand, SECOFI is required to give New Process an opportunity to provide additional information and to make clarifications regarding its proposed calculations of hand labor cost, indirect manufacturing cost, overhead expense, profit and credit, and then to make a new calculation of those items taking into account any new information or clarifications that New Process provides.

33. 2. With regard to indirect manufacturing expenses, SECOFI followed essentially the same approach as with allocation of manufacturing costs, rejecting New Process’ relative sales value methodology. Our discussion of that issue thus controls indirect manufacturing expenses as well.

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34. **3.** With regard to New Process' methodology for determining overhead expenses and profits, and credit expenses, SECOFI asserted that New Process had failed to adequately explain its calculations or methodology.<sup>19</sup> Therefore, it ignored this data and calculated these expenses directly from New Process financial statements, as "best information available." Once again, it allocated such expenses to primary and secondary steel, but not directly to scrap, for reasons articulated earlier. Here again, the critical issue is whether SECOFI had an obligation to request additional information or clarification from New Process under the applicable law and regulations; the panel again finds that SECOFI had such an obligation and did not meet it in the circumstances of this case.

**C. Exclusion of Certain Products**

35. New Process also contends that certain New Process products should be excluded from the dumping calculations because they are not included in A-D of para. 128 of the definitive resolution of August 2, 1994.<sup>20</sup> New Process contends that contrary to the Remand Results, which state SECOFI "has excluded only those products that are not similar to those of national manufacture," SECOFI did not in fact do so.<sup>21</sup> SECOFI admits that notwithstanding the

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<sup>19</sup> Remand Results, paras. 59, 67.

<sup>20</sup> New Process Submission, at 28.

<sup>21</sup> See Remand Results, para. 64.



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statement in the Remand Results, it did not in fact exclude any such products. Once again, it blames the “impossibility” of making such exclusions on New Process; SECOFI asserts that the product descriptions submitted by New Process did not permit SECOFI to determine, on the basis of ultimate use of the product, that they should be excluded because they were not similar to those produced domestically.<sup>22</sup> Once again, SECOFI’s practice of failing to seek clarifying information did not give New Process “a full opportunity for the defense of their interests” within the meaning of Article 6, Paragraph 7 of the GATT Anti-Dumping Code. For that reason, it was illegal under Article 238(III) of the Federal Fiscal Code.

**D. Additional New Process Concerns**

36. In its confidential submission, New Process has raised “Additional New Process Concerns.” [

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<sup>22</sup> SECOFI Submission, at 39.

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**IV. INLAND STEEL COMPANY**

37. Inland correctly notes that SECOFI, in deciding to impose a new and higher duty on New Process (67.07 percent in place of 38.22 percent), effectively raised Inland's rate as well, since Inland is now subject to the highest New Process rate as "best information available."<sup>23</sup> (SECOFI decided, consistent with its normal administrative practice, to impose the highest dumping margin assigned to any party upon Inland, because Inland refused to permit a verification of the information that Inland had submitted to SECOFI in response to the initial request for information.<sup>24</sup>) Inland simply requests that, in the event this panel takes action which causes New Process' rate to be lowered, that the panel direct that this new, lower rate be applied to Inland as the new "best information available" rate.<sup>25</sup> Because the panel is taking action which might cause

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<sup>23</sup> Inland Steel Submission of May 23, 1997.

<sup>24</sup> Remand Results, paras. 31-32.

<sup>25</sup> Inland Submission (pages un-numbered).

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SECOFI to change New Process' rate, Inland's request is granted to the extent of our requiring SECOFI, in the second remand, to determine a new "best information rate" for Inland based on the recomputed dumping margin for New Process.

**V. ORDER OF THE PANEL**

For the reasons expressed above, the panel affirms SECOFI's Remand Results of April 30, 1997, with respect to the allocation of raw material costs of New Process. The Panel also orders that, on a second remand to be completed within 120 days of the date of this opinion and order, SECOFI do each of the following:

1. Fully inform New Process of all missing information and of all needed clarifications regarding proposed calculations of hand labor cost, overhead expense, profit and credit expense for New Process, and regarding product exclusions for New Process;

2. Give New Process an opportunity to provide additional information and to make clarifications regarding proposed calculations of hand labor cost, overhead expense, profit and credit expense, and regarding product exclusions;

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3. Based on the above, make new dumping calculations for New Process and for Inland.

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Issued on September 15, 1997  
Signed in the original by:

September 15, 1997.  
Date

Gustavo Vega Cánovas, Chairman  
Gustavo Vega Cánovas, Chairman

September 15, 1997.  
Date

Eduardo Magallón Gómez  
Eduardo Magallón Gómez

September 12, 1997.  
Date

Michael D. Sandler  
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September 12, 1997.  
Date

José Luis Soberanes Fernández  
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