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Boeing Takes Trade Law Abuse To A Whole New Level

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Deep within the bowels of the U.S. Commerce Department's mammoth headquarters in Washington, D.C., in a cloistered parcel of nondescript offices, toil a couple dozen analysts, accountants, and lawyers, who consider themselves the last line of defense for U.S. industries facing the "ravages of unfair trade." In case there was any doubt about their commitment to mission, these guardian angels recently changed their agency's name from the relatively innocuous "Import Administration" to the baton-wielding "Enforcement and Compliance." With its flimsy allegations of unfair trade on the part of Canadian aircraft manufacturer Bombardier, the Boeing Company hopes to exploit Enforcement and Compliance's singularity of purpose to protect its monopolist's perch.

The antidumping law is purported to exist to protect American companies and their workers from the effects of foreign competitors selling their products in the United States at "unfairly low" prices. Why competition—encouraged as it is in all forms of domestic commerce—suddenly becomes a scourge when foreigners are offering the lower prices is a question without a coherent answer. Under the law, "relief" in the form of antidumping duties is available if the domestic industry can demonstrate that it is materially injured or threatened with material injury by reason of those unfairly low-priced imports.

Contrary to the myth that antidumping is about leveling the playing field and protecting U.S. companies and workers from predatory foreign firms, the law has become a commercial weapon used by U.S. companies against other U.S. companies. Antidumping has become a convenient channel through which domestic firms can saddle their competition (both foreign and domestic) with higher costs and their customers with fewer alternative sources, while giving themselves

room to raise their own prices, reap higher profits, and—in the case of Boeing—reinforce their market power.

In a year that has featured a record number of U.S. trade remedy case initiations (43 antidumping cases and 20 countervailing duty cases through September 5), Boeing's dumping complaint against Bombardier is far and away the most audacious. It takes misappropriation of the antidumping law to a whole new level.

Boeing—never one to abstain from taxpayer largesse—claims that it is threatened with material injury because of sales of 109-seat aircraft by Bombardier to Delta Airlines, which have not happened and will not happen until mid-2018 at the earliest. Moreover, the aircraft in question are of a class that Boeing not only doesn't produce, but is technically incapable of producing for several years because all of its production capacity is committed to a backlog of orders for its larger aircraft. In fact, Boeing voluntarily withdrew from this market in 2006 in order to shift its focus to producing larger aircraft—the 126-seat 737-700 and the 138-seat 737 MAX 7—which has been keeping Boeing in the black.

Delta (and other carriers) requires aircraft of different sizes and seating capacities so that it can serve both high demand and low demand routes cost-efficiently. Boeing's larger planes are not economically viable substitutes for Delta because using them risks flying with empty seats, which means higher costs per seat, lower returns for shareholders, and increased ticket prices.

By filing these cases, Boeing is effectively asking the government to misappropriate the antidumping law by finding that it is threatened with material injury by reason of sales that have never taken place, of a product that Boeing stopped producing more than a decade ago, all because Boeing might decide someday that it wants to reenter that market. Otherwise, Boeing is simply asking the government to enhance its monopoly power by forcing the airlines to buy aircraft that are uneconomical to fly. Neither explanation helps Boeing's image.

Dumping is defined as the sale of a product in a foreign market at a lower price than the price obtained by the same producer in his home market. Dumping is measured by comparing a foreign producer's U.S. and home market prices over a specific period of time. For each comparison (sometimes there are thousands or tens of thousands of sales, other times just a few), the difference between the net U.S. price and the net home market price is considered the unit margin of dumping. A positive dumping margin results when the U.S. price is lower than the home market price and a negative dumping margin results when the U.S. price exceeds the home market price. The antidumping duty ultimately imposed is, in theory, equal to the weighted average dumping margin calculated for all U.S. sales expressed as a percentage of U.S. sales value.

But that straightforward-sounding exercise of comparing prices and calculating dumping margins is rife with subjective interference and methodological sleights of hand. The administering agency maintains considerable discretion when it comes to determining the existence of dumping, and estimating its magnitude. Which sales should be included in calculating average prices? What product models should be collapsed together and treated as a single product for purposes of calculating average prices? What expenses should be subtracted from gross prices

before net prices are compared between markets? What constitutes the date of sale? How should company-wide costs be allocated to the subject merchandise?

When the purpose of the antidumping law's administering agency is to "safeguard and enhance the competitive strength of U.S. industries against unfair trade through the enforcement of U.S. antidumping duty (AD) and countervailing duty (CVD) trade laws," one cannot be faulted for raising questions about objectivity. But when fulfilling that mission requires (1) "conduct[ing] AD/CVD investigations and administrative reviews to determine if imports are being sold at less than fair value or benefitting from unfair subsidization" and, AT THE SAME TIME (2) "counseling U.S. industries on how to petition the U.S. government to seek relief from injurious and unfairly traded imports," it is no longer in dispute that the process lacks objectivity.

That conclusion is supported by the hundreds of U.S. court rulings that have found the Commerce Department (Enforcement and Compliance) acting illegally or otherwise beyond it authority. Citing findings from an older Cato study, in the 18-month period between January 2004 and June 2005, the U.S. Court of International Trade (CIT) remanded 19 cases to the Commerce Department with instructions to revisit its decisions or recalculate figures. In 14 of those 19 cases, the resulting dumping margins were lower after the remand instructions were followed, suggesting a higher incidence of exercising discretion to the detriment of the importing interests.

If the Commerce Department finds dumping in the Boeing case, the lawyers representing Bombardier, Canada, Delta Airlines, and the other carriers would likely appeal the case to the CIT, which will have a field day identifying administrative abuses. For starters, there are no U.S. sales to assess. Bombardier and Delta entered into a purchase agreement last year, with no fixed dates of sale. Historically, the Commerce Department has rejected purchase agreement date as the date of sale because in many cases—as would be expected in this case as it involves sales of big ticket items—the terms of sale (quantity, price, product modifications, delivery terms, after-sale services) can change significantly after the purchase agreement date. Offering a set price for a delivery in 2 or 3 years of a product that costs tens of millions of dollars to produce, occasions mid-production design changes, and contains components whose costs fluctuate with commodity prices is a highly risky proposition. Accordingly, Bombardier (and Boeing, for that matter) doesn't do it. Bombardier doesn't register sales in its accounting records until the aircraft is delivered and an invoice is cut.

Nevertheless, Enforcement and Compliance appears to be going forward with a dumping analysis based on sales made between April 1, 2016 and March 31, 2017. An objective observer would conclude that since there were no sales of subject merchandise in the United States during that period, there was obviously no dumping during that period. But Enforcement and Compliance appears to be planning to treat the purchase agreement date as the date of sale, and the preliminary terms established there—price, quantity, etc.—as the actual sales terms.

To complicate matters further, there are no production costs recorded on Bombardier's books during the period of investigation for any of the aircraft in the Delta purchase agreement. Many of the aircraft won't be produced for several years, so it will be years before the costs are accurately recorded in the company's books. Enforcement and Compliance hasn't provided any

guidance as to how Bombardier should attempt to conform with its reporting requirements, but seems to be suggesting that it will consider the costs incurred during the one-year period of investigation to produce those airplanes on the purchase agreement that have been produced.

Of course, as Boeing's lawyers and the cost accountants at Enforcement and Compliance know full well, unit production costs of high-fixed-cost products and other products that benefit from learning curve effects, are always higher-than-average in the early production phases, and decrease as output rises. The unit costs that Bombardier would report for the first few of the 75 aircraft on the purchase agreement would be much higher than the average unit cost of the 75th. Boeing's CEO, in a statement to shareholders, even boasted about unit cost reductions of 30 percent on the 80thBoeing 787 produced and 40 percent on the 240th.

In order to account for these learning curve effects and to avoid skewing profit reporting and projections, companies are permitted, under Generally Accepted Accounting Principles, to adjust these costs by incurring them at stages that match them more realistically to revenues. Indeed, Boeing spreads it costs out across the life of its aircraft programs so as not to mislead investors or potential investors. Yet, Boeing seems to be okay with Enforcement and Compliance's decision to disallow this approach so that it can generate high dumping margins for Bombardier.

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Production costs, of course, are relevant to antidumping determinations because if there are no sales in the home market made in the ordinary course of trade, the U.S. price is compared to a

cost-based estimate of what the price should be in the home market. When a company reports higher costs, it is more likely that its home market sales will be made at prices below the cost of production and eliminated for being outside the ordinary course of trade. As a result, that higher cost, increased by an estimate of what the profit should be, acts as the benchmark to which the U.S. price is compared when calculating the dumping margin.

Keep your eye on developments in this case, the preliminary results of which are due from Commerce in the next couple of weeks. It provides an excellent example of how subjectively and capriciously the antidumping law is administered and it could be the next most explosive issue threatening U.S.-Canada trade relations.