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**BRIEF FOR THE FEDERAL TRADE
COMMISSION AS AMICUS CURIAE**

Preliminary Statement

On October 20, 1986, the Federal Trade Commission ("Commission") moved for leave to file a brief amicus curiae in this proceeding. The motion was granted on November 20, 1986. The Commission is a federal agency charged with enforcing, inter alia, Section 5 of the Federal Trade Commission Act, which prohibits "unfair methods of competition in or affecting commerce." (15 U.S.C. § 45(a)). In fulfilling its mandate, the Commission seeks to ensure that sound and consistent economic principles are applied to issues affecting competition. Accordingly, it offers this brief to aid the Court in reviewing certain findings made by the Department of Commerce in this case.

In June 1985 Micron Technology, Inc. ("Micron") filed a petition alleging that imports from Japan of 64K dynamic random access memory components ("64K DRAMs") were being dumped and that these dumped imports materially injured the United States DRAM industry. The petition alleged that in a "mature stage of production" the total manufacturing cost of the Japanese firms was at least \$1.25 per unit (Pet. at 15)¹ and that Japanese firms had sold 64K DRAMs in Japan at approximately \$2.30 per unit as recently as October 1984 (id. at 11). Micron further alleged that Japanese firms lowered their prices in Japan to \$.90 (id. at 11-12) following Micron's price reduction in October 1984.

¹ Motorola, Inc. agreed that the cost to produce and market 64K DRAMs is about \$1-\$1.25 (testimony of Steve Sparks at ITC hearing July 15, 1985, Transcript (Tr.) at 24).

Japanese home prices allegedly continued to decline through May 1985 (id. at 12).

After investigating sales of 64K DRAMs for the period January 1 through June 30, 1985, the Department of Commerce ("Department") found that some home sales by Japanese firms were at prices below the Japanese "cost of production," with both depreciation and historic research and development ("R&D") expenditures included as part of the total "cost of production." 64K Dynamic Random Access Memory Components (64K DRAM's) from Japan, 51 Fed. Reg. 15943, 15944 (April 29, 1986) ("64K DRAMs"). For some of these sales, the Department therefore decided to use a "constructed value" (an approximation of the actual average total cost of production), rather than market prices in Japan, as the benchmark against which to compare Japanese prices in the United States. The Department found dumping margins ranging from 12 to 35 percent (id. at 15954). The International Trade Commission ("ITC") then found, by a 4-2 vote, that the United States DRAM industry was materially injured by Japanese imports. 64K Dynamic Random Access Memory Components from Japan (Final), ITC No. 1862 (June 1986).

Oki Electric Industry Co., Ltd. ("Oki") seeks review of the Department's findings and has raised many issues concerning the Department's constructed value calculations. In this brief the Commission addresses only the threshold question raised by Oki: whether the Department incorrectly ignored actual prices in Japan when it used a constructed value.

The Commission maintains that, consistent with the purpose of the antidumping law to preserve for United States consumers the benefits of fair competition, Congress intended the Department to use a constructed value for an imported product only if home sale prices for that product deviated from normal business practice. The record in this case shows that in early 1985 two factors may have led DRAM producers to price in Japan below average total cost: (1) replacement of 64K DRAMs by 256K DRAMs; and (2) an unanticipated "slowdown" in the DRAM industry. We suggest that in pricing in response to these factors, the Japanese producers may have followed "normal business practice." In choosing to use a constructed value for 64K DRAMs, the Department ignored these factors and made no finding as to whether the Japanese prices of Japanese DRAM producers deviated from normal business practice. Accordingly, this Court should reverse and remand to the Department for further findings respecting the propriety of employing a constructed value.

QUESTION PRESENTED

Whether the Department erred in not making findings regarding normal business practice before using a constructed value for 64K DRAMs.

ARGUMENT

- I. **THE ANTIDUMPING LAW REQUIRES THE DEPARTMENT TO DETERMINE NORMAL BUSINESS PRACTICE BEFORE USING CONSTRUCTED VALUES, AND IT FAILED TO DO SO.**

The antidumping law was intended to secure the benefits of free and fair competition for American consumers. This law is one of several Congressional responses to "unfair practices" in

foreign commerce.² The legislative history of the antidumping law applicable to this proceeding (19 U.S.C. §§ 1673 et seq.) confirms that the current law's purpose and intent are in all material respects the same as the Antidumping Act of 1921 (S. Rep. No. 249, 96th Cong., 1st Sess. (1979) at 61,107; H.R. Rep. No. 317, 96th Cong., 1st Sess. (1979) at 59). The 1921 Act's legislative history discloses that its goal was not to interfere with the importation of fairly traded imports, but rather to deal with predatory sales by foreigners. The law's purpose was to

protect our industries and labor against a now common species of commercial warfare of dumping goods on our markets at less than cost or home value if necessary until our industries are destroyed, whereupon the dumping ceases and prices are raised at above [sic] former levels to recoup dumping losses. By this process while temporarily cheaper prices are had our industries are destroyed after which we more than repay in the exaction of higher prices. [H.R. Rep. No. 1, 67th Cong., 1st Sess. (1921) at 23-24].

² Other responses include passage of the first countervailing duty law in 1890, 26 Stat. 584 (1890); and enactment of the Antidumping Law of 1916, 15 U.S.C. §§ 71 et seq., shortly after the 1914 passage of both the Clayton Act, 15 U.S.C. § 12 et seq., and the Federal Trade Commission Act, 15 U.S.C. § 41 et seq. The purpose of this antidumping law was to place foreign firms selling in the United States in the same position "with reference to unfair competition" as domestic firms. H.R. Rep. No. 922, 64th Cong., 1st Sess. (1916) at 9-10. Samuel J. Graham, an Assistant Attorney General in President Wilson's administration, described the 1916 antidumping provision as follows:

Any anti-dumping provision is not a matter of taxation, or, strictly speaking, tariff. . . . Its purpose should be to prevent unfair competition. Just as we have said to our own people by the Clayton act that they should not indulge in unfair competition, so we propose to say the same to the foreigner. [Letter to The New York Times (July 4, 1916) at 10].

Congress recently reaffirmed the proposition that the anti-dumping law is designed to provide United States consumers with the benefits of fair competition. In discussing the Trade Reform Act of 1974, which enacted the current statutory provision on constructed value, the Senate Finance Committee stated:

This [1921 Antidumping] Act is not a 'protectionist' statute designed to bar or restrict U.S. imports; rather, it is a statute designed to free U.S. imports from unfair price discrimination practices [3] . . . [T]he Antidumping Act does not proscribe transactions which involve selling an imported product at a price which is not lower than that needed to make the product competitive in the U.S. market, even though the price of the imported product is lower than its home market price. Such so-called 'technical dumping' is not anticompetitive, hence, not unfair; it is procompetitive in effect. [S. Rep. No. 1298, 93d Cong., 2d Sess. (1974) ("S.Rep. No. 1298") at 179 [(emphasis added)].

Consistent with the policy of preserving the benefits of fair competition, Congress has striven to ensure that American consumers obtain imported goods at the lowest prices established by free market forces. Thus a product ordinarily may not be deemed to have been "dumped" unless (allowing for transport costs and tariffs) its American price is below its "foreign market value." That value is determined by the product's price in its

³ This sentence was cited with approval by Senator Danforth in the debates on the Trade Agreements Act of 1979. Cong. Rec. S10317 (daily ed. July 23, 1979). Senator Danforth also said that dumped imports are not in the best interest of the United States consumer, since "the long run impact is likely to be higher prices and greater profits for the foreign producers once the domestic competition has been crippled." Id. Senator Heinz, in the same debates, said that the antidumping and countervailing duty provisions are aimed at countries that do not rely on "free market principles and . . . on competition and the law of comparative advantage as arbiters of the marketplace." Cong. Rec. S10306 (daily ed. July 23, 1979).

home market when sold in "usual commercial quantities and in the ordinary course of trade" or, if it has insignificant sales in its home market, by its sales price in third countries (19 U.S.C. §§ 1673, 1677a, 1677b; 19 CFR § 353.1).

Assuming the sales of a product are made in "usual commercial quantities and in the ordinary course of trade" in the home market, the Department is required to accept the home sales price of the product as its foreign value unless it determines that home sales have been made at "less than the cost of production . . . over an extended period of time and in substantial quantities and . . . not at prices which permit recovery of all costs within a reasonable period of time in the normal course of trade." (19 U.S.C. § 1677b(b) (emphasis added)).

The legislative history of the antidumping laws makes clear that constructed values are to be applied only in limited circumstances and not merely because significant home sales have been made at prices below production costs:⁴

⁴ Congress noted that costs as measured by accountants might not reflect true economic costs and indicated that the Department should use economic costs when deciding whether to use constructed value. Congress therefore directed the Department to "employ accounting principles generally accepted in the home market of the country of exportation if [the Department] is satisfied that such principles reasonably reflect the variable and fixed costs of producing the merchandise" (H.R. Rep. No. 571, 93d Cong., 1st Sess. (1973) at 71).

Because of the difficulty in assaying true economic costs, the use of home market sales is preferable to the use of constructed value. Smith-Corona Group v. United States, 713 F.2d 1568, 1576 n. 20 (Fed. Cir. 1983), cert. denied, 465 U.S. 1022 (1984). As this case indicates, the calculation of constructed value is fraught with difficult issues such as the proper rate of depreciation, allocation of costs common to several products, and the appropriate rate of return on investment. None of these issues needed to be addressed by the Department unless it first (FT. CONT'D)

These standards would not require the disregarding of below-cost sales in every instance, for under normal business practice in both foreign countries and the United States, it is frequently necessary to sell obsolete or end-of-model year merchandise at less than cost. Similarly, certain products, such as commercial aircraft, typically require large research and development costs which could not reasonably be recovered in the first year or two of sales. Thus, infrequent sales at less than cost, or sales at prices which will permit recovery of all costs based upon anticipated sales volume over a reasonable period of time would not be disregarded. However, the practice of systematically selling at prices which will not permit recovery of all costs would be covered by this amendment and such sales would accordingly be disregarded. [S. Rep. No. 1298 at 173 (emphasis added)].

Thus, home market sales of 64K DRAMs at a low price when a new model DRAM is replacing it would not justify development of a constructed value. Similarly, home market sales of a current product at below total cost when demand growth for the product has failed to meet expectations would not justify development of a constructed value. Congress intended that the Department would resort to a constructed value only if the foreign firms' home market prices deviated from "normal business practice."

Congressional intent notwithstanding, in this case the Department has made no finding respecting normal Japanese business practice for 64K DRAMs. In rejecting Oki's argument that below cost home market sales merely responded to competitive conditions in Japan, the Department stated only that "consistent

determined that the price in Japan of 64K DRAMs did not cover "the cost of producing the merchandise" and did not "permit recovery of all costs within a reasonable period of time in the normal course of trade." The Department never made this finding.

with our standard practice, [the Department has] disregarded below-cost sales where they constituted more than 10 percent of total home market sales . . . over the six month period of investigation."⁵

The Department's failure to determine the "normal business practice" for the specific industry conflicts with its statutory obligation to make such findings, and that fact alone would justify reversal of its decision. E.g., Burlington Truck Lines, Inc. v. United States, 371 U.S. 156, 167-68 (1962); see Southwest Florida Winter Vegetable Growers Association v. United States, 584 F. Supp. 10, 15-16 (C.I.T. 1984) (in finding no dumping, the

⁵ The Department's entire response was as follows:

Not only did the petition allege below-cost sales in the home market and provide substantial support for this allegation, but the Department's review, based on verified submissions of the respondents, has concluded that the petition was correct in its assertions. While the anti-dumping law does embody a strong preference for the use of actual home market sales data, it also directs that home market sales that are below cost of production may not be used to establish foreign market value where they: (1) Have been made over an extended period which permit[s] recovery of all costs within a reasonable period of time in the normal course of trade. Section 773(b), and 19 CFR 353.7.

Consistent with our standard practice, we disregarded below-cost sales where they constituted more than 10 percent of total home market sales of such or similar merchandise over the six month period of investigation. We used above-cost home market sales for purposes of making our fair value comparisons, where they accounted for more than 10 percent of home market sales. Where less than 10 percent of the home market sales were above cost, we determined that such sales were insufficient to form an adequate basis for determination of foreign market value. In such situations, the Department used constructed value to determine foreign market value, in accordance with the Act, the regulations and the legislative history (Section 773(b), 19 CFR 353.7 and S. Rep. No. 96-249, 98th Cong., 1st Sess. 95-96 (1979)). 64K DRAMS at 15948.

Department properly did not disregard sales by Mexicans that were as much as 50 percent below the cost of production -- even though such sales accounted for up to 50 percent of all sales -- because this was normal business practice permitting full cost recovery by Mexican growers of winter vegetables).⁶

Moreover, as we demonstrate below, application of accepted economic principles to the available record evidence strongly suggests that had the Department acted as the law requires, to determine "normal business practice," it might have concluded that application of a constructed value to this case was unwarranted. A remand of this proceeding would permit that issue to be definitively resolved.

II. PRICING OF 64K DRAMS BELOW THE AVERAGE TOTAL COST OF PRODUCTION IN THE JAPANESE MARKET MAY HAVE BEEN NORMAL BUSINESS PRACTICE.

In the absence of subsidies (which are not at issue here), there are two mutually exclusive reasons why firms may sell products at less than the average total cost of production. Either the selling firm is engaged in predatory practices, or the producer is temporarily selling below average total cost as a matter of normal business practice. In the present proceeding, although there is a general allegation of predation in Micron's

⁶ See also Welded Stainless Steel Pipe and Tubing From Japan, 43 Fed. Reg. 17439, 17440 (April 24, 1978) and Carbon Steel Plate from Japan, 43 Fed. Reg. 12780, 12782 (March 27, 1978) (in finding dumping, Department of the Treasury recognized the four-year business cycle of the Japanese steel industry as the appropriate period over which to determine whether all costs had been recovered).

petition, the Department made no finding respecting predation.⁷ The record suggests that sales below total cost in Japan in early 1985 were consistent with normal competitive business practices.

A. Normal Business Practice May Dictate Below Cost Sales of Obsolete Model DRAMS.

The Department found, as Micron had alleged, that the production of 64K DRAMS was "at a mature stage" by 1985. 64K DRAMS at 15944. Clearly, it is possible for a mature model DRAM to be sold in a competitive market at a price below average total cost (see Paul A. Samuelson and William D. Nordhaus, Economics at 478-480 (12th ed. 1985)).⁸ DRAM shipments follow a product life

⁷ Successful predation requires the satisfaction of several stringent market conditions. Robert H. Bork, The Antitrust Paradox: A Policy at War with Itself (1978) at 144. The Supreme Court recently noted "a consensus among commentators that predatory pricing schemes are rarely tried, and even more rarely successful." Matsushita Electric Industrial Co., Ltd., et al. v. Zenith Radio Corp., et al., 106 S. Ct. 1348, 1357-1358 (1986). The Court observed:

[T]he success of such schemes is inherently uncertain. . . . Moreover, it is not enough simply to achieve monopoly power, as monopoly pricing may breed quick entry by new competitors eager to share in the excess profits. The success of any predatory scheme depends on maintaining monopoly power for long enough both to recoup the predator's losses and to harvest some additional gain. [(id. at 1357) (emphasis in original)].

⁸ The existence of "sales below total costs" at any point in time does not necessarily evidence abnormal business behavior (Samuelson and Nordhaus, supra, at 478-480). Some expenditures must be incurred prior to the actual production and sale of 64K DRAMS. As a result, producers will base their development and investment decisions on the anticipated price of such DRAMS, with the expectation that, on average over the life of the 64K DRAM generation, price will at least equal average total cost. A firm with accurate expectations in a competitive market will recover all its costs over the long run (id. at 480). However, a compe- (FT. CONT'D)

cycle characterized by initial growth, succeeded by a plateau, which is followed by a decline in unit volume.⁹

This cycle has been repeated as the advance of technology has led to successive products or "generations" of DRAMs.¹⁰ Each new DRAM generation provides approximately four times as much memory capacity as its predecessor in (roughly) the same amount of space. As the Department observed, purchasers find the increased capacity of new generations desirable.¹¹ Indeed, purchasers have previously substituted the 4K DRAM for the 1K DRAM; the 16K DRAM for the 4K DRAM; and so on. Firms that begin the production of any particular DRAM generation are aware that, at

titive firm may not cover average total costs during some time periods if the product is being replaced by a superior product, or more generally if the firm's expectations turn out to be wrong.

⁹ Prehearing Brief of Oki Electric before the U.S. Department of Commerce, March 6, 1986 at Annex 1. ITA Public Investigation File A-588-505. Additionally, trade press reports at the beginning of 1985 noted a substantial reduction in the expected lives of 64K DRAMs and above. In particular, the life of the 64K DRAM generation, introduced in 1980, was estimated to be four years. See, for example, "Premature Erosion of DRAM Prices Changing Economics of Memory Market," Electronic News (April 1, 1985) at 1, 27-28; 64K Dynamic Random Access Memory Components from Japan (Final), ITC No. 1862 (June 1986) at A-3. Therefore, as Micron alleged, and the Department found, by the beginning of 1985, the 64K DRAM generation was at a mature stage (and hence probably nearing the end of its economic life).

¹⁰ 64K Dynamic Random Access Memory Components from Japan (Preliminary), ITC No. 1735 (August 1985) at A-2.

¹¹ Department of Commerce Memorandum Supporting Notice of Investigation of 256K and above DRAMs. Appendix at 1-2. ITA Public Investigation File A-588-505. See Dynamic Random Access Memory Semiconductors of 256 Kilobits and Above from Japan; Initiation of Antidumping Investigation, 50 Fed. Reg. 51450 (December 17, 1985).

some undetermined point in the future, a new superior DRAM generation is likely to emerge.

Observing the generational shift in both DRAM capacity and end-use designs, the ITC has found the pricing of successive generations of DRAMs to be interrelated.¹² Specifically, the rate at which substitution occurs depends upon the difference in the market prices of new and old DRAMs. As the price difference narrows (for example, as the ratio of 64K DRAM price to 16K DRAM price falls), it becomes profitable for more and more DRAM users to switch to the emerging generation. Indeed, the Department has indicated that, as a "rule of thumb . . . large scale displacement by a new generation product occurs once the price ratio [between the new generation and the old] is 5:1." (Department of Commerce memorandum, supra at App. at 2).

The availability of a new DRAM generation will therefore diminish both the demand for, and price of, the preceding generation. As output of the new generation rises and its price falls, the decline in demand for the preceding generation will accelerate. Nonetheless, firms will continue to produce the preceding generation in the short-run (i.e., before such firms can reconfigure their plants for production of the new generation) as long as prices suffice to cover average variable production cost (Samuelson and Nordhaus, supra at 479). Thus, the observation that a current DRAM generation in the process of replacement is

¹² Dynamic Random Access Memory Semiconductors of 256 Kilobits and Above From Japan (Preliminary), ITC No. 1803 (January 1986) at 11.

being sold at prices below average total cost is consistent with competitive behavior and normal business practice.

When the Department made constructed value calculations for 64K DRAMs from Japan (January 1, 1985 through June 30, 1985), the 64K DRAM had indeed reached the point at which its replacement by the 256K DRAM was accelerating. The ITC staff, in its review of the domestic United States market, reported that 64K DRAMs "are now in the process of being superseded by 256K DRAMs."¹³ During 1985, the 256K DRAM accounted for the majority of United States DRAM consumption measured in terms of memory capacity,¹⁴ even though it had been produced commercially only since 1983.¹⁵

In Japan, as in the United States, it is possible that the advent of 256K DRAMs reduced the competitive price at which 64K DRAMs could be sold.¹⁶ The decline in price of 64K DRAMs to a level below average total cost is consistent with the competitive substitution of 256K for 64K DRAMs and the fact that, in the

¹³ 64K Dynamic Random Access Memory Components From Japan (Preliminary), ITC No. 1735 (August 1985) at A-2.

¹⁴ Data compiled by the U.S. International Trade Commission, 64K Dynamic Random Access Memory Components From Japan (Final), ITC No. 1862 (June 1986) at b-2. In finding that the domestic "like product" for the imported 64K DRAM was all DRAMs, the ITC observed, "[p]urchasers of DRAMs are essentially buying memory capacity." id. at 8

¹⁵ Dynamic Random Access Memory Semiconductors of 256 Kilobits And Above From Japan (Preliminary), ITC No. 1803 (January 1986) at A-13.

¹⁶ "With customer inventories bulging and 256K capacity coming on-stream, OEMs [original equipment manufacturers] are reported to be demanding further price concessions from the memory suppliers." "64K RAM Orders Scrubbed as OEMs Pressure Prices," Electronic News (January 14, 1985) at 1 as reproduced in Letter to Secretary of Commerce on behalf of Hitachi, Ltd. (October 28, 1985), ITA Public Investigation File A-588-505 at Exhibit A.

short run, competitive price is determined by demand and variable cost conditions (Samuelson and Nordhaus, supra at 478).

B. Normal Business Practice May Justify Below Cost Sales When Total Demand for DRAMs Fails to Meet Expectations.

The ITC also found that United States consumption of all DRAMs did not increase in 1985 "as had been anticipated." 64K Dynamic Random Access Memory Components from Japan (Final), supra, at 15. Total United States consumption of DRAMs, measured on the basis of bits of memory, rose by only 34 percent in 1985, as compared to an increase of 93 percent between 1983 and 1984 (id. at b-2). As a Motorola official told the Department, "the users of dynamic RAMs were starting to see a reduction in demand in August, about 1984. This became more obvious by the fourth quarter." (Testimony of Steve Sparks on March 10, 1986, Tr. at 75.) Micron told the ITC in July 1985 "There is no doubt that the entire semiconductor and computer industry has suffered a downturn in the last six months" (Testimony of Joseph Parkinson on July 15, 1985, Tr. at 14).

Pricing below average total cost may represent normal business practice in a competitive industry during periods in which demand fails to meet producer expectations (Samuelson and Nordhaus, supra at 478). The observation that, at a particular point in the course of trade, a price is not sufficient to recoup average total cost is therefore not evidence of abnormal business behavior because, in periods of slack demand, competitive prices will not cover average total cost. Because many of the costs of developing, designing, and installing plants to produce DRAM

chips were incurred in the past, these expenses do not determine current prices (Samuelson and Nordhaus, supra at 479).

C. The Department's Failure to Make Essential Findings Requires Remand.

The record may thus support a finding that Japanese producers, in pricing 64K DRAMs below total cost, acted pursuant to normal business practice in response to market conditions. The Department, however, failed to make any finding regarding the state of the market or normal business practice. Rather, it simply invoked its "standard practice" and "disregard[ed] below-cost sales where they constituted more than 10 percent of total home market sales of such or similar merchandise over the six month period of investigation." 64K DRAMs at 15948. This approach wholly fails to consider conditions pertinent to the market, and is inconsistent with the statutory mandate that home market sales may be disregarded, and constructed values applied, only if (among other conditions) goods are sold at prices that do not "permit recovery of all costs within a reasonable period of time in the normal course of trade" (19 U.S.C. § 1677b(b)).

CONCLUSION

For the foregoing reasons, this proceeding should be remanded to the Department of Commerce so that it may reconsider whether it properly rejected otherwise relevant home market sales and computed a constructed value for 64K DRAMs.

Respectfully submitted,

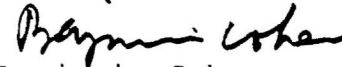
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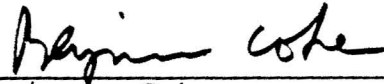
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