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Expert: Rum war could be WTO case

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A new front opening in the Caribbean rum war could land the U.S. in hot water with the World Trade Organization.

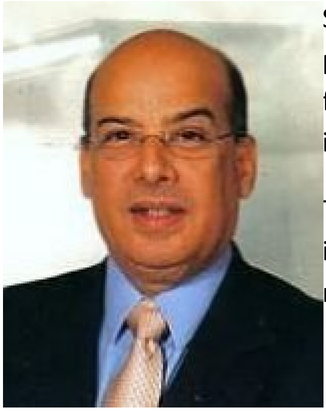
That is the warning from Sir Ronald Sanders, a former Caribbean representative to the WTO, in a recent op-ed piece titled “Caribbean Rum Facing Threat in U.S.”

Rum-producing countries of the Caribbean Community and Common Market (CARICOM) have launched a lobbying campaign to get the U.S. government to cut back on subsidies to its rum producers in Puerto Rico and the U.S. Virgin Islands is putting the industry of other nations at a serious disadvantage.

Caricom officials were scheduled to meet with U.S. Trade Representative Ron Kirk in Washington, D.C. this month to complain about the incentives, but Sanders said they may have to take the U.S. to arbitration at the WTO “ unless diplomatic efforts settle a looming problem before it concretizes.”

At stake is rum production in several CARICOM countries together with the foreign exchange earnings and employment that it generates.

The federal government returns most of the $13.50 excise tax it collects on every proof gallon of rum sold in the U.S. to Puerto Rico and the U.S. Virgin Islands, based on the amount of rum produced by each territory.



Sanders argues that the federal rum rebate program itself is not the main problem. Rather, it is how the USVI and Puerto Rico are increasingly funneling the funds to private rum producers through sweetened local incentives.

The bulk of that money had gone to support investments in infrastructure, health and education, with smaller portions going to market local rums.

“Now, these two U.S. affiliates are taking advantage of U.S. government refunds to them, of excise taxes on rum, to subsidize vastly increased rum production and marketing in their territories,” Sanders said. “The huge increase in rum exports to the U.S. mainland, at a subsidized cost, would squeeze-out CARICOM rums; and subsidized marketing would make it virtually impossible to compete.”

The incentives duel between the two territories was sparked when Diageo decided to move production of its Captain Morgan rum from Ponce to St. Croix, after landing huge incentives from the USVI government, which basically split the rum-rebate revenue between the government and the liquor producer. The USVI also entered into a similar deal with Fortune Brands, which produces Cruzan rum in St. Croix.

In response, Puerto Rico passed basic incentives worth 46 percent of the rum-rebate revenue generated from branded-rum sales and 25 percent from bulk-rum sales, which is rum produced for third parties. At stake in the rum fight are hundreds of millions of dollars in federal rum-rebate funds and hundreds of local jobs.

Last month, the USVI sweetened its deal with Cruzan to keep the company on a competitive footing with Puerto Rico-based producers after local incentives kicked in.

Puerto Rico government officials have complained that the excessive subsidies granted by the USVI to rum producers could endanger the whole rum rebate program. Resident Commissioner Pedro Pierluisi has filed legislation to cap the amount of rum rebate revenue that could be used to subsidize rum production, but the measure has languished in Congress.

Sanders notes that the USVI “ is desperate to create opportunities for employment and economic growth,” especially in the wake of the surprise shutdown of the huge Hovensa oil refinery on St. Croix earlier this year.

The Diageo deal alone will add 20 million proof-gallons of rum production capacity in the region – more than 50 percent of the current U.S. market, according to Sanders.

Moreover, known and reported subsidies to other producers in the USVI and Puerto Rico are resulting in additional new capacity for existing facilities.

“The enlarged production from this new capacity will affect not only the US market, but other world markets as well, since the U.S. cannot absorb all the rum that can be produced at these new or expanded subsidized facilities,” Sanders said.

The U.S., if does not cap the use of rum rebate funds for marketing and capacity building, could be in violation of WTO rules in three ways, he said.

Failure on that front lead to the “collapse” of the CARICOM rum industries, he warned.

“Rum-producing CARICOM governments would have little option but to file for a dispute settlement with the U.S. at the WTO,” Sanders said. “But, the WTO process would a long and costly exercise for all the governments concerned.”

Sanders said that highlights the inadequacy and unfairness of the WTO remedies for developing countries when its rules are violated by rich nations.

“But, that is another issue,” he said, adding that “the record of the U.S. at the WTO in relation to the interests of small CARICOM countries – on bananas and internet gaming – has been harmful.”

He sought to tie the rum issue to the position of the U.S. in the Caribbean.

“There is a clear need for renewed and improved relations between the U.S. and CARICOM countries particularly in economic matters that improve the areas and levels of aid and investment,” Sanders said.

A U.S. failure to take action on CARICOM’s rum concerns could leave a sour taste in the mouths of neighbors of the USVI and Puerto Rico, he said.

“If they fail to do this, relations between the U.S. and CARICOM will sour with the Caribbean, once again, feeling let down,” Sanders concluded.