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Defense-Firm Registrations with DDTC Have Doubled

The number of defense firms registered with State's Directorate of Defense Trade Controls (DDTC) surged 130% in the year after the agency amended its registration requirements and fees and the number is still growing. DDTC amended its rules in September 2008 and by the end of fiscal year 2009 on Sept. 30, 2009, registrations had jumped to 9,322 from less than 5,000, reported Lisa Studtmann, DDTC's director of compliance. Industry sources attribute some of that growth to a push that prime defense contractors, particularly aerospace and aviation firms, made to get their sub-contractors and suppliers to register.

> Of the 9,322 firms register in FY '09, 7,988 were manufacturers or exporters and 1,334 were brokers, Studtmann noted. The increase in registrations put a significant burden on the compliance office's registration and compliance division, she told an American Conference Institute program July 14.

To cope with the heavy workload, Studtmann said she has shifted the assignment for monitoring consent agreements from the registration and compliance division to the enforcement division. She said this made sense because the enforcement division is responsible for negotiating the agreements. She also moved the work of reviewing cases from the Committee on Foreign Investment in the U.S. to the research and analysis division from the registration division.

Studtmann responded to questions about DDTC's policy of requiring defense firms to consolidate all affiliate companies under one registration even when the registering company does not have direct control or ownership of the affiliate, such as a joint-venture partner. She said it's DDTC's preference to consolidate registrations so one firm has ultimate responsibility for the actions of its subsidiaries. "But if you have absolutely no control over an entity that you have been forced or asked to put on your registration, you should contact our office again and let's discuss it," she said. Studtmann also noted that some 15,000 license applications are put on hold annually because they contain the names of parties on DDTC's "watch list." Each of these so-called "hits" is reviewed by someone in her office, she said. These reviews may result in a license being denied or a requirement for the party to be removed from the application.

House Republicans Scorn GOP Leaders to Pass Tariff Bill

A majority of House Republicans rebuffed direct orders from GOP leaders to vote against the Miscellaneous Tariff Bill (H.R. 4380) July 21 and also thwarted Democratic attempts to embarrass Republicans by forcing them to reject a popular trade bill. The result was an

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overwhelming, bipartisan vote of 378-45 for passage of a measure that contains some 800 individual provisions that suspend or reduce tariffs on imports of items generally not available in the U.S. Many of these suspensions were included in previous MTB legislation and had expired at the end of 2009. The passed bill applies retroactively to Jan. 1, 2010, for those tariffs. The MTB now goes to the Senate where business representatives say it might pass before lawmakers leave for their August vacations.

> Republican leaders had urged rejection of the MTB because the proposed tariff changes had been deemed to be "earmarks," and the House Conference in March had agreed to oppose any legislation containing earmarks (see **WTTL**, May 10, page 3). Ahead of the vote, House Minority Leader John Boehner (R-Ohio) and Minority Whip Eric Cantor (R-Va.) reportedly had threatened GOP members that they would face censure by the Republican Conference, if they voted for the bill.

Democratic leaders apparently saw the chance to embarrass the Republicans and decided to bring the MTB to the House floor under a "suspension-of-the-rules" that bypassed the House Ways and Means Committee, but required a supermajority of votes to pass. If the legislation had failed, they would have been able to accuse Republicans of opposing trade and U.S. manufactures who benefit from the tariff measures. The Democratic strategy almost worked until the final vote was underway on the legislation. Republicans initially held together to follow their leaders' directions, but once 40 GOPers broke ranks and provided enough votes to assure passage of the bill, Boehner and Cantor released the rest of party to vote as they wished. In the end, 129 Republicans joined 249 Democrats in support of the bill.

The Republican Conference's stand on treating the MTB provisions as earmarks stirred a bitter dispute within GOP ranks, according to congressional sources. Boehner and Cantor were blamed for being "uncreative about how they approached the problem," one congressional source told WTTL. "They got themselves trapped by it," he added.

"I'm disappointed that I can't support this legislation," Ways and Means Ranking Member David Camp (R-Mich.) said during debate on the bill. "In my view, this bill technically does not contain earmarks in the form of limited tariff benefits," he said. Camp noted the Republican Conference decision to declare a moratorium on earmarks. "I am committed to both the letter and spirit of that moratorium and therefore will vote against the bill," he said, and he did.

"The majority is well aware of our earmark ban, and I can't help but wonder if this wasn't put on the suspension calendar after three and a half years without a vote so that it would fail and they might avoid taking the blame," Camp declared. "It's a sham and it won't work," he added. "The business community knows it, the American workers whose jobs depend on it know it, and we know it," Camp said. Rep. Kevin Brady (R-Texas) also chastised the Democrats for bringing the bill to the floor under a suspension rule . "If you are truly serious about passing this measure, why would you demand a supermajority that ensures its defeat rather than a normal majority vote that ensures its passage?" he said during the debate. "For months, we've said we cannot help the moratorium on this bill this year, and we are sincere about it. By choosing the suspension route, you have killed this bill." he argued. His prediction did not come true.

EU Appeals WTO Findings in Airbus Dispute

As expected, the European Union (EU) July 21 served notice that it is appealing much of a World Trade Organization (WTO) panel's decision in the Airbus case, alleging seven errors in the panel's interpretation and application of WTO rules (see **WTTL**, July 5, page 3). "This dispute is too important to allow the legal misinterpretations of the panel to go unchallenged," said EU Trade Commissioner Karel De Gucht in a press release. The U.S. received the EU's "lengthy notice of appeal" and is studying it, said a spokesperson for the U.S. Trade Representative's (USTR) office. The U.S. wanted the Dispute Settlement Body to adopt the report as soon as possible and a special meeting had been called for July 21. The appeal put the special meeting on ice, while the WTO Appellate Body takes up the case. The 90-day appeal process

is expected to produce another round of detailed briefs and arguments, as well as an oral hearing, which may be opened to the public. In its appeal, the EU claims the aid that EU member states gave to Airbus was not intended to give a preference to exports rather than domestic sales. The panel found that launch aid for the A380 by Germany, Spain and the United Kingdom is a prohibited export subsidy.

> The EU also disagreed with the panel's findings that all 21 instances of Airbus launch aid are subsidies because the interest rates were below market rates. The EU thinks some of the loans aren't subsidies and the panel's findings are exaggerated, an EU source said.

The EU believes compliance with the terms of the 1992 U.S.-EU agreement on civil aircraft aid should preclude a finding of subsidy, he said; referring particularly to A380 contracts. The EU will appeal the ruling where the panel based its subsidy finding on the interest rates proposed by the U.S., he said. The source said the rate the U.S. proposed was "much too high" and was based on rates venture capitalists charge. Although the rates paid by Airbus aren't public, the U.S. proposed rate was twice as high as the Airbus number, he said.

The EU will also appeal the panel's findings on infrastructure subsidies in Germany and France; the French government's capital infusion to Airbus from 1987 to 1994; the transfer of the French government's shares in Dassault to Aerospatiale in 1999; research and development grants under a general EU R&D program; the "adverse effects" on Boeing; and the U.S. claim that Boeing lost market share due to the subsidies Airbus received. The EU also claims the panel failed to make the causal link between adverse effects and the individual subsidies found. It also argues that pre-1995 subsidies should not be included in the dispute because they were given before the entry into force of the WTO subsidies agreement.

New Fight Looms over Proposal on Transfer Pricing Rules

The business community may have a new complaint to add to its litany of objections to Obama administration economic and tax polices. This time the issue is a Treasury initiative in the fiscal year 2011 budget proposal to amend international tax rules to crackdown on alleged abuses in intercompany transfer pricing practices. Along with Treasury, House Democrats are also pushing legislation (H.R. 5328) to address the problem, according to statements at a House Ways and Means Committee hearing July 22. The hearing also revealed strong opposition to such changes among Republicans.

> The government has tried to address transfer pricing several times over the last 25 years, starting with Reagan-era tax law changes, a Treasury White Paper in 1988, an amendment to Section 482 tax rules in 1994, and legislation in 2009. At issue are claims that U.S. multinationals use royalty agreements on intangible intellectual property, such as patents and copyrights, and cost-sharing arrangements with their related controlled foreign corporations (CFCs) to shift profits to low-tax countries. Testimony at the hearing also claimed companies are moving production and jobs to these low-tax countries to reduce U.S. taxes.

Treasury analysis of the issue has found that "there is evidence of substantial income shifting through transfer pricing," testified Stephen Shay, Treasury deputy assistant secretary for international tax affairs. While some estimates have put the loss of tax revenue to the U.S. at upwards of $60 billion annually, Shay cautioned against drawing conclusions from aggregated data from public sources, saying evidence has to be based on individual corporate tax returns.

The administration's proposal would "reduce inappropriate shifting of income outside the United States by clarifying the definition of intangible property, the valuation of multiple properties on an aggregate basis where that achieves a more reliable result and the valuation of intangible property taking into account the prices or profits that a controlled taxpayer could have realized through realistically available alternative transactions," Shay said. "The

administration would further attack income shifting with a new proposal on intangibles, providing that where a U.S. person transfers an intangible from the United States to a related controlled foreign corporation that is subject to a low foreign effective tax rate in circumstances that evidence excessive income shifting, then an amount equal to the excessive return will be treated as subpart F income in a separate foreign tax credit limitation basket," he said.

> The Ways and Means Committee's Ranking Member, David Camp (R-Mich.), argued that the problem isn't with transfer pricing rules but with the high corporate tax rate in the U.S., which forces companies to move production and income to lower-tax countries. "If that is the majority's real concern – the tax code pushing jobs overseas – then I would suggest we focus on the real problem, which is the corporate tax rate," Camp said.

Lawmakers Press for Action against Transshipment Hubs

House members raised concerns at a July 22 hearing about the diversion of controlled U.S. goods through transshipment countries such as the United Arab Emirates, Malaysia, China and nations in Central Asia and vowed to pass new legislation to deal with the problem. Members of the Foreign Affairs Committee's subcommittee on terrorism, nonproliferation and trade tried to elicit details from State and Commerce witnesses on the transshipment problems through those countries, but the officials said they could only answer those questions in a classified, closed-door meeting that was to be held with the lawmakers after the public hearing.

> Deputy Assistant Secretary of State Vann Van Diepen and Bureau of Industry and Security (BIS) Assistant Secretary Kevin Wolf dodged questions on how the administration intends to implement Title III of the recently enacted Iran Sanctions Act. The section requires the Director of National Intelligence to prepare a report within the next 180 days identifying countries that allow the diversion of controlled goods and technology. Based on that report, the president is required to designate countries of diversion concern and for BIS to impose export licensing requirements on these countries. The law, however, has several waiver provisions that would allow the president to put off these designations.

Committee members were particularly concerned about diversion activities in the UAE. Van Diepen noted that the UAE has adopted an export control law but is still staffing up the office that will oversee the law and drafting implementation regulations. "It is very clear to us that the UAE government at the highest levels and broadly throughout the agencies understand the importance of nonproliferation and dealing with proliferation problems through effective action," he told the committee. The UAE "has taken very important steps, not just by passing legislation, but in terms of stopping specific shipments and shutting down companies dealing with specific individuals," he stated. They are "taking important concrete steps in a tangible way that are having an impact on the problem," he asserted.

* * * Briefs * * *

EXPORT ENFORCEMENT: MTI Corporation of Richmond, Calif., will pay $20,000 fine in agreement with BIS to settle single charge of exporting bench-top muffle furnace, classified as EAR99, to Indian laboratory on BIS Entity List. Firm will pay $5,000 now and $3,000 in monthly payments until January 2011.

KORUS FTA: House Democrats apparently aren't satisfied talking with USTR officials about Korean FTA, and 109 of them sent letter to President Obama July 22 asking to meet with him directly to discuss their objections to the deal (see **WTTL**, July 19, page 2). They told president they oppose deal because of provisions on financial services, investment, labor, autos, beef and textiles.

FCPA: SEC attorneys and Bobby Benton, vice president for Western Hemisphere for Pride International, Inc., Houston-based offshore drilling company, told Houston U.S. District Court June 10 that Benton has agreed to enter consent agreement to settle civil suit charging him with violating FCPA for his role in bribery of officials in Venezuela and Mexico and violation of FCPA records and reporting requirements.