# Washington Tariff & Trade Letter®

A Weekly Report for Business Executives on U.S. Trade Policies, Negotiations, Legislation, Export Controls and Trade Laws

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## STATE REQUIRES "DUE DILIGENCE" AS PART OF $2.5 MILLION SETTLEMENT

In a consent agreement with EDO Corporation of New York, State's Directorate of Defense Trade Controls (DDTC) has required the company to make export compliance reviews part of its future "due diligence" investigations for mergers and acquisitions. The consent agreement, which requires payment of a $2.5 million civil fine, involves activities at Condor Systems, a California firm that EDO acquired in July 2002 following Condor's filing for Chapter 11 bankruptcy protection. EDO's deal with State was reached late in 2003 but only recently unearthed.

> DDTC agreed to allow EDO to apply $750,000 of the fine toward a remedial compliance program, including credit for $175,000 already spent. In addition, DDTC required EDO to establish a position for a Special Compliance Officer (SCO) and to adopt a series of measures to assure compliance with the Arms Export Control Act (AECA) and the International Traffic in Arms Regulations (ITAR). The deal also includes specific reporting and auditing requirements.

"Respondent acknowledges the need to include export compliance in its due diligence reviews in merger and acquisition activities and to ensure that all new employees involved in AECA/ITAR-regulated activities hired as a result of such acquisitions are trained and instructed regarding the requirements of the Act and the Regulations and respondent's compliance policies and procedures," stated the agreement, which was signed in November 2003.

The settlement with State was in addition to a $1 million fine Condor paid as part of a February 2003 plea agreement with the U.S. Attorney for San Francisco. Condor pled guilty to two violations of 18 USC 1001 for making false statements to State in an export license application for a signal processing system sold to the Swedish military. The plea followed a Federal Grand Jury investigation into the firm's dealings with Sweden and Korea dating back to 1995 and its disclosure of technology for systems it had developed for the U.S. Navy and was restricted from disclosing without Navy approval. [**Editor's Note**: Copy of consent agreement and charging letter to EDO will be sent to WTTL subscribers on request.]

## EXPORT LAWYERS QUESTIONS DRAFT BIS "SAFE-HARBOR" PLAN

Trade attorneys who have reviewed an advance draft of the Bureau of Industry and Security's (BIS) proposal for establishing a new "safe harbor" rule to give legal immunity to firms that adequately apply "red flag" screens to potential customers are raising red flags of their own. The trade bar reportedly is concerned that the rule could become a de facto export licensing requirement and a way for export enforcement officers to collect intelligence on foreign end


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users. In January, BIS began to discus its plans for the safe harbor rule and to collect informal comments on the idea from the exporting community (see **WTTL**, Jan. 5, page 1). It also issued a stealth notice in the March 15 Federal Register asking for comments on the safe harbor concept and the work needed to use this mechanism but without any details.

> According to a copy of the safe-harbor draft obtained by WTTL, BIS wants to amend the definition of "knowledge" in Section 772.1 of the Export Administration Regulations (EAR) to include a "reasonable person" standard. It also wants to amend the Red Flags provision of the rules to increase the number questions to answer to 23 from 12. The draft, however, doesn't include those additional flags.

In addition, the agency plans to establish a mechanism for firms to submit a report to BIS to reveal that their screening process uncovered a red flag but that the concerns raised were appropriately resolved. If BIS does not respond to that notice in a specific number of days, the current draft says 45 days, than the exporter "may proceed with the transaction with the understanding that BIS concurs in the party's assessment that any red flags have been successfully resolved and that the party qualifies for the safe harbor," the advance draft declares.

The draft explicitly states that submitting a safe-harbor report "would not be mandatory." But attorneys argue that licensing rules that require disclosure of inconsistent information about consignees might require the submission of such information for other licenses. They also say they are worried that reporting could become a condition added to licenses. While the draft doesn't provide details on what has to be submitted in a report, it says exporters can show "through contemporaneous documentation that they took certain specific steps" to determine that they don't have knowledge that the export is going to a prohibited end use or user.

The Federal Register notice asking for comments on the safe-harbor idea says BIS expects only 100 respondents to participate in the program, but it does not indicate how many reports it expects to receive. It estimates these reports should take only one to four hours to prepare. Given that some large firms screen thousands of exports a year and get numerous red flag reports that are subsequently resolved, BIS could be overwhelmed by reports from exporters who want to ensure they've gotten safe-harbor treatment for their red-flag determinations.

## CANADA SEEKS WTO CONSULTATIONS ON LUMBER REVIEWS

Just as a World Trade Organization (WTO) dispute-settlement panel was issuing a final report on one aspect of the U.S.-Canada dispute over softwood lumber, Ottawa was opening a new complaint against the International Trade Administration's (ITA) handling of administrative reviews in the case and its alleged failure to issue individual countervailing duty (CVD) rates for Canadian producers. Canada has asked the U.S. for consultations, which is usually the prelude to a formal request for another panel to review the charges.

> Canada complains that ITA promised to expedite the establishment of individual CVD rates for Canadian lumber producers last year. Of the 109 Canadian producers that asked for expedited CVD orders, 52 were given individual rates and 27 are still waiting for a decision, Ottawa contends. More troubling to Canada is a recent ITC decision to conduct individual administrative reviews for only 11 producers, leaving over 280 companies that asked for individual rates subject to the generally higher "all other" CVD rate.

A WTO panel April 13 issued its previously leaked final decision on Canada's challenge of ITA's antidumping decision on softwood lumber. The panel upheld Commerce on almost all of its methods and decisions in finding dumping against imports, but on a split 2-1 decision, it said ITA violated WTO rules in the way it applied the policy of "zeroing" dumping averages from different exporters (see **WTTL**, March 15, page 3). Both the U.S. and Canada are expected to appeal the decision to the WTO Appellate Body over different parts of the opinion. The zeroing dispute is now proceeding on several paths, with five WTO members, led by the

European Union (EU), seeking a separate panel ruling against the ITA practice. The EU, which lost a different Appellate Body ruling, *EC Bed Linen*, on zeroing, wants the WTO to enforce the same policy against the U.S. The dissenting panelist in the lumber ruling said he supported the U.S. policy despite the *Bed Linen* decision because the Body reached a decision it didn't need to address. The Appellate Body's opinion "is *obiter dicta*, as Article 2.4 was not part of a claim before the Appellate Body," wrote panelist Gerhard Hannes Welge of Germany.

> Meanwhile, pressure is mounting again for a bilateral deal to settle the lumber dispute. A NAFTA binational panel's ruling on the International Trade Commission (ITC) remand determination on threat of injury in the case was postponed to April 30. Before then, Canadian Prime Minister Paul Martin will be in Washington April 29-30 for talks with President Bush and key U.S. Cabinet members. Canadian Trade Minister Jim Peterson is coming to D.C. April 19-20.

Sources speculate that they will push for an agreement before the NAFTA panel ruling comes out. But lumber producers in Quebec, Ontario and Alberta wrote to Peterson April 16 to renew their opposition to the deal proposed by the U.S. in December.

## COMMERCE MOVING TEXTILE STAFF TO IMPORT ADMINISTRATION OFFICE

With the Multifiber Arrangement (MFA) coming to an end Dec. 31 and hence the job of negotiating and managing textile and apparel quotas ending, Commerce will move the Office of Textiles and Apparel from under the assistant secretary for trade development to under the assistant secretary for import administration. In their new home, the textile and apparel staff will help handle the avalanche of textile antidumping and countervailing duty cases and China anti-surge cases that are expected to be filed when the global quota system ends.

> As the MFA's demise approaches, textile and apparel industries around the world have stepped up their effort to get the WTO to revisit the decision to terminate the system at the end of the year. At last count, 31 trade associations have signed a draft letter to WTO Director General Supachai asking him to convene an emergency meeting of WTO members before July 1 to get the body to agree on extending the MFA termination date to Dec. 31, 2007.

Sources in Geneva say Supachi has not yet received the so-called Istanbul Declaration from the associations. One source said the director general probably will reject the proposal because the WTO is an organization of governments and doesn't respond to requests from industry groups. More important, trade officials at the WTO consider the end of the MFA and opening of free trade in textiles and apparel among the most important accomplishments of the Uruguay Round. In addition, one source noted, the exporting countries that now complain about China's expected capture of a large share of world trade in textiles after Jan. 1, 2005, were the nations that pushed for the end of the quota system.

## WTO APPELLATE BOBY RECOMMENDS PROCEDURAL CHANGES

Members of the WTO Appellate Body (AB) have proposed changing the way countries file and amend appeals of dispute-settlement body rulings in order to give parties better notice of the issues under review. The proposed changes in the Appellate Body's Working Procedures, which were submitted to the chairman of the WTO Dispute-Settlement Body April 8, represent experience the Body has acquired over the eight years since the Uruguay Round Agreement established the process for reviewing panel opinions.

"Notices of Appeal sometimes do not disclose very clearly what is appealed," the AB members noted. They suggested changing the procedures to state more specifically what is required in a notice. The goal would not be to make the process more burdensome, but to encourage consistency from the outset of the appeal and to afford members the "full opportunity to exercise

their rights of defense," they said. Another proposal would require countries that file "other appeals" in a case to give formal notice of their participation. Lack of formal notice can create confusion about the scope of an appeal, they said. In addition, the AB wants to revise the process for amending appeals. While maintaining the appeal notice as the key document defining the scope of a case, the members said they "wish to avoid confusion that may arise when an appellant seeks to file different documents elaborating on or adding to its Notice of Appeal."

## USTR SHUFFLES STAFF, SPLITS UP ASIA TO CREATE CHINA OFFICE

U.S. Trade Representative (USTR) Robert Zoellick April 13 announced a shift of titles and responsibilities for his office, including the establishment of new offices to deal with China, pharmaceuticals and capacity building. The changes were part of funding approved for the USTR's office in the 2004 budget appropriations act enacted in January. All the new positions will report to Deputy USTR Josette Shiner.

> Zoellick has split the USTR office handling Asian affairs, naming Charles Freeman to be acting assistant USTR (AUSTR) for China Affairs and head of the staff responsible for China, Taiwan, Hong Kong, Macau and Mongolia. AUSTR for Asia Wendy Cutler will now focus on Japan, Korea and APEC. Mary Ryckman will take new post of AUSTR for Trade Capacity Building. Veteran USTRer Ralph Ives will add the title of AUSTR for Pharmaceutical Policy to his post as AUSTR for Southeast Asia and Pacific Affairs.

## IRAQ IMPOSES LICENSING REQUIREMENTS ON SCRAP EXPORTS

As American alloy metal producers petition BIS to restrict exports of scrap metals from the U.S., the Minister of Trade in Iraq has imposed export licensing requirements on exports of scrap from Iraq. The new Iraq system, which goes into place April 30, will require scrap dealers to be licensed by the ministry and to pay a license fee of 50,000 Iraqi dinars or about $35 per ton for scrap exports. The restrictions on Iraqi scrap exports came as the Coalition Provisional Authority announced that Iraq Customs was created April 1 and is now imposing a 5% "reconstruction levy" on all imports except a large selection of exempted goods, including food, medicine, medical devices, humanitarian aid and goods valued under 500,000 dinars.

> The short-supply petitions were filed with BIS April 7 by the Copper and Brass Fabricators Council and the Non-Ferrous Founders Society. The associations want BIS to establish a monitoring system and impose a 380,139 metric ton export quota on scrap copper and scrap copper-alloy (see **WTTL**, Dec. 15, page 4).

* * * BRIEFS * * *

COMMERCE: Senate April 8 confirmed Rhonda Newman Keenum to be assistant secretary and director general of U.S./Foreign Commercial Service. She comes from Edelman Worldwide PR firm. In 2000 she worked for National Republican Committee.

CHINA SURROGATE: CIT Judge Timothy Stanceu April 9 rejected (Slip Op. 04-33) ITA's use of data from Indian Reserve Bank and Indian Import Statistics instead of company-specific data in calculating surrogate costs in antidumping case against pipe fittings from China. Judge remanded case back to ITA to explain why it departed from normal practice in determining surrogate values and why it chose to use alternative information (see **WTTL**, April 12, page 2).

TRADE FIGURES: Manufactured goods exports in February were up 12.3% to $65 billion, Census reported April 14. Services exports, which are now being tracked as measure for offshoring in services sector, rose 10.2 % to record $27.3 billion. Goods imports gained 10.5% to record $112.3 billion, as services imports, which some consider offshoring, increased 12.3% to record $22.2 billion.

FOOD IMPORTS: FDA in April 14 Federal Register reopen record on its advance notice requirements for food imports to propose aligning reporting time frames with Customs advance notice rules.