DAILY NEWS

Yo ho ho and a little trade war

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WASHINGTON — Killing two birds with one bottle of rum, the genial ambassador from Barbados offered me both a drink and a call to arms.

“We are prepared to go to the World Trade Organization and file a complaint against the United States. This is about subsidies that go beyond subsidies and will put our people out of work,” said John Beale, a bearded former banker, holding up a bottle of Mount Gay Rum.

Mount Gay, which is made on tiny Barbados (pop.: 275,000), is the oldest rum brand and collateral damage in a low-profile, high-proof Caribbean battle. It not only pits Davids versus Goliaths but the tale’s two Goliaths against one another.

“Yes, it is all strange,” says Bill Watson, a trade expert at the libertarian Cato Institute. He thinks the U.S. is likely violating WTO rules by illegally subsidizing exports, a view shared by John Schmidt, a Chicago lawyer and top Clinton administration trade negotiator.

The strangeness concerns a de facto subsidy granted since 1917 to Puerto Rico, to correct a supposed market imbalance, and extended to the Virgin Islands in 1954. Both are U.S. territories represented by nonvoting representatives in Congress.

They are the Goliaths.

That’s because when you buy imported rum, they benefit mightily from the excise tax of $13.50 per proof gallon, which works out to $2 a bottle.

Nearly all that money is given to Puerto Rico and the Virgin Islands based on a formula linked to how much rum each territory produces relative to the other. It's essentially foreign aid to folks with sort-of American status, in theory to bolster overall development, schools and other basic needs.

It's serious money for small island economies. In recent years, Puerto Rico has been getting between $350 million and $450 million, while the Virgin Islands got $107 million in 2011 and north of $225 million last year.

Meanwhile, small rum-producing Caribbean nations such as Barbados, Guyana and Jamaica get nowhere in arguing that the rebates are unfair subsidies that help underprice their rum exports. Despite mouthing plenty of platitudes about free and fair trade, Congress doesn't give these Davids and this comparatively puny matter much thought — and keeps extending its largess every two years.

But what was a low-simmering feud turned into a full boil in 2008 with a canny move by the Virgin Islands (pop.: 110,000).

They used a big chunk of their excise tax share to lure London-based Diageo, the world's largest producer of spirits (Johnnie Walker, Smirnoff, Guinness, among others), to move its Captain Morgan spiced rum plant from Puerto Rico to a new plant on St. Croix.

Yes, Captain Morgan: a big brand with a huge following. You've seen the TV commercials and subway ads, I'm sure.

The Virgin Islands' corporate giveaway is worth nearly $3 billion over 30 years, and by guaranteeing greater production, it assured more excise taxes would return. The plant began full production last year, and the Virgin Islands' take soared.

Puerto Rico (pop.: 3.7 million) felt compelled to fight back by using a greater share of its excise revenues to support local producers, notably Bacardi and Serrales. When in Rome. . . .

Where does all this leave the rest of the small island nations who make rum, like Barbados? Watson and Schmidt believe the Caribbean nations would have a strong WTO case. "It's an export subsidy barred by the WTO," Watson says, conceding that even after winning, the Caribbean small fry would have the challenge of getting the U.S. to comply.

Donna Christian-Christensen, a Teaneck, N.J., native and the Virgin Islands' longtime congressional representative, says they've done nothing different than U.S. states that lure businesses. Rum revenues are critical, given a poor economy and the closing of a big oil refinery, and added: "I don't relish a fight with my neighbors."

She portrays Puerto Rico as a spoilsport, chagrined over not getting its traditional lion's share of the funds.

Pedro Pierluisi, her Puerto Rican counterpart in Congress, says that the commonwealth was historically scrupulous in allocating no more than 6% of its take to the rum industry. With the Diageo deal, it had to match the Virgin Islands' overtures "since there wouldn't be a level playing field if we didn't."

Pierluisi is stymied when filing bills to cap the amount funneled to their respective rum industries. The big producers lobby against him. He predicts "a race to the bottom," where the industry competes not on quality and price but on subsidies.

Meanwhile, Beale of Barbados is having no luck ginning up Capitol Hill interest in his rum dispute. Is there some Solomonic compromise to avoid a WTO fight?

Let's hope. I'd love to take the combatants out for a celebratory drink, remaining neutral by buying them each a beer.