To: John Mengel, Chief Economist, Dairy Programs, AMS/USDA
Brian Grunenfelder, Assistant Deputy Administrator, Office of Negotiations & Agreements, FAS/USDA
Gregg Young, Assistant Deputy Administrator, Office of Negotiations & Agreements, FAS/USDA
Bob Spitzer, Senior Advisor, FAS/USDA
Drew Perraut, Office of Information and Regulatory Affairs, OMB
Richard Chriss, Office of General Counsel, USTR
Roger Wentzel, Office of Agriculture, USTR

Cc: Jim Murphy, Assistant USTR for Agriculture, USTR
Tim Reif, General Counsel, USTR

Re: **Follow up to Industry Meetings on AMS' Proposed Rule for Dairy Import Assessments – *Recommendation to Exclude Non-Dairy Products from Scope of Product Coverage, including Cocoa and Chocolate Products of Chapter 18***

The attached summary is provided by the National Confectioners Association in follow up to meetings organized in late July by the Alliance for Fair Dairy Promotion with AMS, FAS, OMB and USTR on the proposed Dairy Import Assessment.

**We believe the proposed rule is too large in scope and urge AMS to exempt all non-dairy products – including cocoa and chocolate products of Chapter 18 - from the Dairy Import Assessment. In past public documents, AMS has confirmed that these intermediate chocolate products of Chapter 18 are not dairy products. *Most importantly, these intermediate products do NOT benefit from dairy promotion programs.***

NCA also strongly supports the position of the Alliance for Fair Dairy Promotion and their recommendations. Our points are summarized on the following page. Should the proposed rule move forward, our industry expects to be assessed the Dairy Import Assessment on imports of dried milk and other dairy commodities. However, we should not also be penalized for importing intermediate and semi-finished chocolate preparations of Chapter 18.

Thank you again for your time last month to allow NCA to voice our members' concerns and recommendations on the proposed rule. Please contact me or Alison Bodor, Vice President for Scientific and Regulatory Affairs, if you have any questions or would like additional information.

Sincerely,

Shawn

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Date: 24 August 2009

To: John Mengel, Chief Economist, Dairy Programs, AMS/USDA
Brian Grunenfelder, Assistant Deputy Administrator, Office of Negotiations & Agreements, FAS/USDA
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Re: **Follow up to Industry Meetings on AMS' Proposed Rule for Dairy Import Assessments –** ***Recommendation to Exclude Non-Dairy Products from Scope of Product Coverage, including Cocoa and Chocolate Products of Chapter 18***

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The attached summary is provided in follow up to meetings organized in late July by the Alliance for Fair Dairy Promotion with AMS, FAS, OMB and USTR on the proposed Dairy Import Assessment.

The National Confectioners Association represents over 450 companies that manufacture more than 90% of the chocolate and confectionery products in the United States. Our sector is comprised of both confectioners (users) and processors (suppliers) of cocoa and chocolate.

**We believe the proposed rule is too large in scope and urge AMS to exempt all non-dairy products – including cocoa and chocolate products of Chapter 18 - from the Dairy Import Assessment. In past public documents, AMS has confirmed that these intermediate chocolate products of Chapter 18 are not dairy products.** ***Most importantly, these intermediate products do NOT benefit from dairy promotion programs.***

NCA also strongly supports the position of the Alliance for Fair Dairy Promotion and their recommendations. Our points are summarized on the following page. Should the proposed rule move forward, our industry expects to be assessed the Dairy Import Assessment on imports of dried milk and other important dairy inputs. However, we should not also be penalized for importing intermediate and semi-finished chocolate preparations of Chapter 18.

Thank you again for your time last month to allow NCA to voice our members' concerns and recommendations on the proposed rule. Please contact me if you have any questions or would like additional information.

Sincerely,

Alison Bodor
Vice President, Scientific and Regulatory Affairs

NCA Recommendation**: We believe the scope of the proposed rule is too broad and recommend scaling back the scope to exclude all products *-- including cocoa and chocolate products of Chapter 18 --* that are not generally recognized as dairy products.**

**Cocoa and chocolate inputs are not dairy products.** Under the proposed rule, finished products including finished confectionery are already exempt. Semi-finished, intermediate cocoa and chocolate products of Chapter 18 should also be excluded.

Internationally and nationally, there are precedents as to what is a dairy product and what is not.

- Chocolate products of Chapter 18 are *not* "Dairy products" as specifically defined in the International Dairy Agreement[1].
- Chocolate products of Chapter 18 are *not* included in the Codex Alimentarius definitions "on the use of dairy terms in relation to foods to be offered to the consumer or for further processing"[2].
- Chocolate products of Chapter 18 are *not* listed by the World Customs Organization as what constitutes "dairy products" in Chapter 04 of the Harmonized System[3] which is incorporated into Chapter 04 of the US Harmonized Tariff Schedule.

*In each of these agreements or definitions, bulk chocolate preparations, intermediate cocoa inputs or chocolate confectionery are not included.*

Even under USDA/FAS' own Bulk Intermediate Commodity-Oriented (BICO) import aggregation categories, there is a distinct category for "dairy products" which includes sub groups of "Milk Products", "Cheese" and "Other Dairy Products"[4]. *There are no bulk chocolate preparations, intermediate cocoa inputs or chocolate confectionery included in the Dairy Products BICO groupings.* In fact, all semi-finished chocolate products and chocolate confectionery of HS codes 1806.20, 1806.31, 1806.32 and 1806.90 are defined in the BICO categories as a "Sweet Snack" under the category of "Snack Food".

**The Dairy Promotion Program offers <u>no</u> benefit to our sector.** The confectionery and chocolate sector does not and will not benefit from dairy promotion programs. If a sector's products do not benefit from the promotion programs, then that sector should not be assessed fees towards those promotion programs. Based on the default rates provided in the proposed rule, our industry would be expected to pay more than $713,000 in fees on products of Chapter 18 alone. Stated another way, Chapter 18 imports would contribute nearly 12% of the estimated $6.1 million to promote US dairy commodities our manufacturers use on a regular and recurring basis including milk powder, milk fats, butter, lactose and whey.

Nor will NCA members realize any benefit from increased demand for dairy products, and in fact will be hit <u>*twice*</u> with increased costs if cocoa and chocolate products remain on the list. First, NCA members will be assessed the import fee on semi-finished chocolate products (as well as imported milk powders and other dairy inputs) in order to promote dairy products. Then, to the extent that demand for dairy commodities increases from the promotion, dairy prices will also increase. *In effect, our members would effectively pay a tax on our own chocolate products in order to generate even higher costs to our manufacturers for US dairy inputs.*

**The Dairy Import Assessment will erode commercial efficiencies in the North American market.** More than 90% of the imports of Chapter 18 intermediate goods come from Canada and Mexico where our members have established operations to take advantage of lower costs for semi-finished chocolate goods that allow them to be more competitive in the domestic market and in foreign markets. Imposition of the dairy assessment would erode these preferences, render production at these facilities uncompetitive, undermine the economic viabilities of these manufacturing facilities, and undercut the efficiencies of highly integrated supply chains throughout the United States, Canada and Mexico. *Fair dairy promotion should not be at the expense of sectors that rely on free trade agreements to produce critical intermediate goods that support US manufacturing.*

**Proprietary information and recipe formulas should not be compromised.** Our industry has always advocated in support of strong protections for proprietary information and recipe formulas for our finished confectionery products and our members' semi-finished intermediate goods. We have worked closely with USTR and USDA to ensure foreign markets do not impose import regulations requiring access to our manufacturers' confidential recipes and formulas. We share the concern that any assessment that depends on access to recipe or formula information jeopardizes the integrity of confidential and proprietary information. *Semi-finished intermediate chocolate products of Chapter 18 should be excluded from the proposed list to ensure no outside organization may gain access to our members' proprietary commercial information.*

**Import spikes in excluded tariff lines of Chapter 18 are highly unlikely as restrictive TRQs minimize any potential savings from the Dairy Import Assessment.** Concerns that importers may shift imports to those tariff lines which are excluded from the import fee are unfounded as it would not be commercially feasible, nor provide any guarantee of reducing costs to importers. Chapter 18 chocolate products included on the proposed list are subject to three separate tariff rate quotas (TRQs): Chapter 4 Additional US Note 10, Chapter 18 Additional US Note 2, and Chapter 18 Additional US Note 3. We estimate that any shortfall in fees as a result of possible shifts in imports to excluded tariff codes of Chapter 18 would total less than $30,500, an insignificant amount compared to the millions of dollars the promotion program generates overall.[5]

- The **TRQ for Ch 4 AUSN 10** generally fills on the day it opens from all sources. However, only a minor amount imported are products of Chapter 18 (*less than 15 mt on average over the past 5 years*). Given the historic high demand for the quota and its one-day fill rate, it is highly unlikely that excluded products of Chapter 18 would significantly increase to displace other dairy products under the TRQ.
- The **TRQ for Ch 18 AUSN 2 covering products with greater than 5.5% by weight of butterfat** routinely fills (or nearly fills) for imports from Ireland and Any Country. There have been virtually zero imports from the UK, Netherlands or Australia in the past 10 years (with country-specific TRQ allocations of 3,379 mt, 45 mt and 2,000 mt, respectively). A spike in imports under these three country-specific TRQ allocations as a way to avoid paying the Dairy Import Assessment fee does not seem commercially feasible. Changes in recipes and formulations required to gain access to the unfilled 5,424 mt TRQ allocations would save roughly importers a paltry $16,000 - $22,000 total in Diary Import Assessment fees. Such a small savings in total trade seems irrelevant.
- The same logic holds true for the **TRQ for Ch18 AUSN 3 which covers chocolate crumb**. Only Ireland and UK have allocations of 1,701 mt and 422 mt, respectively. The TRQ has never filled and imports since 1995 have totaled less than 1,600 mt. Should a spike in imports occur under this TRQ, importers would generate a mere savings of $6,300 - $8,500.
- Finally, high over-quota duty rates (as great as 52.8 cents.kg + 8.5% and subject to Special Safeguards) would not justify importing products under excluded over-quota tariff codes simply to avoid paying the Dairy Import Assessment.

*In short, the circumvention argument is without merit in defending the status quo of including non-dairy products of Chapter 18 in the Dairy Import Assessment. Imports will likely not surge in excluded categories as the potential savings to importers in these very restricted TRQs would be virtually nil.*

***We urge the US Department of Agriculture to implement dairy promotion programs that do not result in US confectionery and chocolate manufacturers being disadvantaged both with increased fees on our own semi-processed products – which are not dairy products – and ensuing higher prices on essential dairy inputs. Dairy promotion program fees should exclude all non-dairy products, including cocoa and chocolate products of Chapter 18.***

## *END NOTES*

[1] Article II – Product Coverage of the *International Dairy Agreement* states "This Agreement applies to the dairy products sector. For the purpose of this Agreement, the term "dairy products" is deemed to include the following products, as defined in the Harmonized Commodity Description and Coding System ("Harmonized System") established by the Customs Co-operation Council: HS Code 04.01.10-30 Milk and cream, not concentrated nor containing added sugar or other sweetening matter; 04.02.10-99 Milk and cream, concentrated or containing added sugar or other sweetening matter; 04.03.10-90 Buttermilk, curdled milk and cream, yogurt, kephir and other fermented or acidified milk and cream, whether or not concentrated or containing added sugar or other sweetening matter or flavoured or containing added fruit or cocoa; 04.04.10-90 Whey, whether or not concentrated or containing added sugar or other sweetening matter; products consisting of natural milk constituents, whether or not containing added sugar or other sweetening matter, not elsewhere specified or included; 04.05.00 Butter and other fats and oils derived from milk; 04.06.10-90 Cheese and curd; 35.01.10 Casein".

[2] *Codex Alimentarius* Standard 206-1999, "Codex General Standard for the Use of Dairy Terms" defines a "milk product" as: "...a product obtained by any processing of milk, which may contain food additives, and other ingredients functionally necessary for the processing." Codex further defines a "composite milk product" as: "…a product of which the milk, milk products or milk constituents are an essential part in terms of quantity in the final product, as consumed provided that that constituents not derived from milk are not intended to take the place in part or in whole of any milk constituent."

[3] The *World Customs Organization's* Explanatory Notes for Chapter 04 note list "Dairy products" as: (A) Milk, i.e., full cream milk and partially or completely skimmed milk. (B) Cream. (C) Buttermilk, curdled milk and cream, yogurt, kephir and other fermented or acidified milk and cream. (D) Whey. (E) Products consisting of natural milk constituents, not elsewhere specified or included. (F) Butter and other fats and oils derived from milk; dairy spreads. (G) Cheese and curd.

[4] The *Foreign Agriculture Service's* FASonline states "These tables contain all codes which makeup the standard commodity groupings which appear on the Bulk, Intermediate, and Consumer-Oriented (BICO) reports." *Dairy Products* can be found at: www.fas.usda.gov/ustrade/ustlists/ExBICOCm.asp?QI=&type=2&code=28.
*Snack Foods* (including all products of 1806.20 – 1806.90) can be found at: www.fas.usda.gov/ustrade/USTlists/imbicocm.asp?qi=&type=2&code=61.

[5] Calculations based on available TRQ allocation amounts multiplied by the maximum default assessment as outlined by tariff code in the proposed rule. Ranges provided as dual rates per unit of product are noted as .003 and .004 for tariff lines subject to the TRQs.