International Dairy Foods Association
Milk Industry Foundation
National Cheese Institute
International Ice Cream Association

June 7, 2002

Hon. Philip M. Crane
Chairman
Subcommittee on Trade
Committee on Ways and Means
US House of Representatives
Washington, DC 20515

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SUBJECT: HR 1786 -- Comments in Opposition to a Bill Increasing Tariffs on Imports of Casein, Caseinates and Milk Protein Concentrate

Dear Mr. Chairman:

These comments respond to the Subcommittee's request of May 3, 2002, for written comments on certain miscellaneous trade and tariff bills. The International Dairy Foods Association (IDFA) wishes to express its strong opposition, on behalf of dairy processors and manufacturers, to HR 1786, a bill that would raise tariffs and impose tariff-rate quotas on imports of casein, caseinates, and milk protein concentrates.

The International Dairy Foods Association (IDFA) is an industry trade association based in Washington, DC whose members include approximately 600 companies involved in the processing, manufacturing, marketing or distribution of dairy foods. Products of IDFA member companies include beverage milk, dairy-based dips and dressings, yogurt, creams, cheeses, ice cream and novelties. Reflecting the diversity and openness of the U.S. dairy foods industry, IDFA member companies range from small, family-owned businesses to large, multinational corporations and are located throughout the United States.

IDFA supports open and competitive markets, in the United States as well as abroad, and accordingly supports trade-liberalizing initiatives and opposes trade protectionism. The bill HR 1786 would *increase* tariff barriers to the U.S. market for milk protein concentrate and casein, thereby increasing costs to U.S. users of these dairy products. With no U.S. industry producing these products, available supply would decrease and costs to consumers increase.

We wish to note that historically the Trade Subcommittee has approved tariff *suspension or elimination* bills for imports that do not have a competing domestic industry. In the case of HR

1786, the legislation moves in exactly the *opposite direction* – it would *increase tariffs* for imports that do not currently have a competing domestic industry. In addition, HR 1786 would violate existing U.S. international obligations under trade agreements, including the World Trade Organization (WTO) agreements. IDFA therefore strongly opposes the legislation and urges the Subcommittee to take no further action on this or similar legislation.

<u>What are these products?</u>

The bill HR 1786 would affect two general categories of products – milk protein concentrate (MPC) and casein (including caseinates, a further processed form of casein). Both MPC and casein are value-added milk products that have been processed, typically with the use of filtration technology, to remove certain constituents naturally occurring in milk (such as lactose, water, and minerals). The technology used in the manufacturing process allows the manufacturer to produce a product with customized protein levels. Different forms of MPC therefore vary in their protein level ranging from 40% protein by weight to 90% protein by weight. Caseins are more highly processed forms of milk proteins with protein levels in excess of 90%. The level of milk protein is typically an identifying characteristic of MPC and casein, affecting its use as well as price.

Both MPC and casein offer technical and functional characteristics that are needed in particular applications. The nutritional benefits of the high level of protein is a major factor in many purchasers' decisions. Consistency of that protein level is often also critical. Other technical factors include viscosity, important for a thicker or creamier texture. These traits make MPC and casein valuable for a broad range of food as well as non-food products. Food uses include, for example, baby food, bakery products, non-dairy creamer, frozen desserts, cheese products, meal replacers, breakfast foods, soups, processed meat, and high protein bars and beverages and other nutritional foods. Non-food uses range from animal feed to dietary supplements, medical products, cosmetics and industrial uses.

Although the technology for manufacturing MPC and casein has been available to U.S. companies for many years, no domestic industry has developed for the production of either MPC or casein. The primary reason for the lack of a U.S. industry has been the operation of the U.S. dairy price support program, which acts as an economic disincentive to manufacture more expensive, value-added milk products as opposed to a commodity product such as nonfat dry milk (which has a guaranteed customer in the U.S. government at the price support level).

Consequently imports are the only available source of supply for these dairy ingredients.[1] New Zealand is the largest supplier of U.S. imports of MPC as well as casein. Other foreign suppliers include Ireland, the Netherlands, Australia, France, Hungary, and Denmark, among others. The total value of U.S. imports from all sources in 2001 was $626 million.

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[1] The largest dairy company in New Zealand recently announced a joint venture with a U.S. dairy cooperative to begin manufacture of MPC in the United States, however, commercial production has not yet started.

The proposed legislation (HR 1786)

HR 1786 would significantly restrict the cost and availability of MPC and casein in the U.S. market by imposing new tariff-rate quotas on imports and substantially increasing the applicable tariff on over-quota imports.

No tariff-rate quota currently exists for any of these products, which are classified in two different chapters, and various subheadings, of the U.S. Harmonized Tariff Schedule. MPC with at least 40% but not more than 90% protein is classified under either 0404.90.10, while MPC with at least 90% casein is classified under 3501.10.10. Casein is classified under 3501.10.50, and caseinate is classified under 3501.90.60. Under current U.S. law, a tariff of $0.0037 per kilogram (the equivalent of 0.17 cent per pound) is currently applied, at the WTO-bound rate, for all these tariff lines. No quota applies.

The pending bill would establish elaborate new tariff-rate quotas for most of the imports of MPC and casein. The existing duty rate would apply to only a small portion of existing trade -- about a third of the MPC actually imported in 2000, or half of the MPC imported last year. Any additional imports of MPC above the quota level of 15,818,000 kilograms would be subject to a very high over-quota duty of $1.56 per kilogram (equivalent to 71 cents per pound). If these specific rates are converted to an ad-valorem equivalent, the over-quota duty rate would have been 54% in 2000 and 44% in 2001 -- a substantial tariff barrier.

For casein, the legislation would have a similar effect. The existing duty would apply to only 45% of the volume imported in 2001 and 51% of the volume imported in 2002. The proposed over-quota tariff of $2.16 per kilogram (equivalent to $0.98 per pound) would be assessed on up to 55% of the casein imported in 2001 and 49% of the volume imported in 2002. On an ad-valorem equivalent basis, the over-quota tariff would have been 53% in 2000 and 45% in 2001.

The effects of raising tariffs to roughly 50% on the majority of MPC and casein imported into this country would be quite adverse. Costs to users and consumers would increase dramatically, and import supply would contract. At the same time, there is no domestic industry supplying these products. Food manufacturers and medical supply companies would find themselves in the undesirable position of choosing between passing through the rise in prices to consumers, discontinuing production, or moving production outside the United States to remain competitive with their foreign competitors.

Displacement and substitutability

Proponents of the legislation assert that imports of these products are displacing domestic sales of nonfat dry milk. The truth is, however, that nonfat dry milk is simply not an acceptable substitute for casein or milk protein concentrate in many uses. Casein and MPC provide both nutritionally and functionally superior attributes to nonfat dry milk -- higher levels of protein, consistency of protein content levels, superior viscosity, and removal of select milk components that are not desired in the particular end product. The removal of lactose is a particularly signficant distinction, as many of the end-use products are manufactured to be lactose-free so as to reach consumers who are lactose-intolerant. Nonfat dry milk, which contains lactose, cannot be used at all for these products. Nonfat dry milk is not a true substitute for MPC or casein, and therefore imports of MPC and casein are not displacing sales of nonfat dry milk. They are different products, with different uses and values.

Trade agreement violations and trade policy implications

The bill HR 1786 would also have adverse trade policy consequences. The bill's new tariff-rate quota restrictions and increased over-quota tariffs abrogate the United States' trade agreement obligations, by exceeding existing tariff bindings as well as violating WTO procedural rules. Despite the bill's inclusion of purported "compensation authority" language, the United States has no WTO right to unilaterally increase tariffs, as the bill would do. WTO rules spell out a process for consultation and negotiation of trade compensation, which are ignored by the legislation's provisions. Increases in tariff rates for MPC and casein above the bound rates, which are the same as currently applied rates, would violate WTO bindings. Adversely affected foreign supplier countries would have a right to retaliate against the United States for these WTO violations, and undoubtedly would do so. In addition to the economic effects of retaliation against U.S. exports, the U.S. would suffer in its credibility to negotiate reduced trade barriers in foreign markets, as it is trying to do in the WTO, FTAA, and various bilateral negotiations.

Existing U.S. tariff rates for MPC and casein are already at their WTO-bound ceilings. No tariff-rate quota previously existed on these products. Moreover, no absolute quota existed on these products at the conclusion of the Uruguay Round negotiations, that might have justified conversion at that time to tariff-rate quotas. Tariff treatment of other dairy products, such as nonfat dry milk, differs because they were subject to Section 22 quotas at the time of the Uruguay Round negotiations and therefore today have tariff-rate quotas. That is simply not the case for MPC or casein.

Proponents of the legislation assert that imports of MPC and/or casein are being subsidized by foreign governments and offer this as an additional justification for tariff-rate quota restrictions. However, as the Subcommittee is aware, U.S. trade remedy laws already exist for countering the injurious effects of foreign subsidies. The proper avenue of relief for allegations of unfair trade practices is through the use of U.S. trade remedy laws, not legislated tariff increases.

In sum, there are many reasons to reject HR 1786. It is trade protectionism with no corresponding domestic industry to protect; anti-consumer; a violation of WTO agreements; and damaging to the credibility of the United States at a critical time for current trade negotiations. We urge the Subcommittee to reject this legislation, and not allow it to move forward in the legislative process.

Thank you for the opportunity to share our views with the Subcommittee. With best regards,

E. Linwood Tipton
President and CEO
International Dairy Foods Association