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A LARGE OR SMALL ECONOMIC IMPACT ON IMPORTS?**

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**The USDA's Final Rule on Dairy Import Assessment Fees:
A Large or Small Economic Impact on Imports?**

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ABSTRACT

On March 18, 2011, the USDA Agricultural Marketing Service (AMS) published a long-awaited *Federal Register* notice (76 FR 14777) to establish a dairy import assessment as required under the 2002 and the 2008 Farm Bills. The final rule requires, as of August 1, 2011, that an assessment of 7.5 cents per hundredweight of milk, or the equivalent thereof, be imposed on imported dairy products. Based on actual dairy imports for 2010, we estimate that the assessment would generate \$3.9 million for market promotion of dairy products in the United States and abroad. But the impact of these fees on importers is likely to be very limited, ranging from 0.07% to 0.45% of average unit value (AUV), with the exception of lactose (1.07% of AUV). Under the final rule, countries which primarily export high-value dairy products with relatively low milk solids, such as European cheese producers, will pay a disproportionately low import assessment, at a likely rate of 0.16% AUV or lower. We also estimate that assessment fees are unlikely to shift demand from imports to domestically produced dairy products.

¹ This paper represents solely the views of the authors and is not meant to represent the views of the U.S. International Trade Commission or any of its commissioners. Please direct all correspondence to John Fry, Office of Industries, U.S. International Trade Commission, 500 E Street, SW, Washington, DC 20436, telephone: 202-708-4157, fax: 202-205-2384, email: john.fry@usitc.gov.

Introduction

The 1983 Dairy Production Stabilization Act (DPSA) established a program under which U.S. dairy farmers are charged an assessment, or checkoff, on all milk sold commercially.¹ Revenues from the checkoff are remitted to a Qualified State or Regional program, such as the New England Dairy Promotion Board,² or the Dairy Management Inc.(DMI),³ a nonprofit created in 1995. These entities use checkoff fees for marketing activities, including research, education, and advertising, with the aim of raising domestic and foreign consumption of U.S. dairy products. In 2010, DMI reported expenditures of \$136 million, of which \$5.3 million was budgeted to promote dairy sales overseas.⁴ Examples of DMI activities are the Fuel Up to Play 60 (FUTP60), a partnership program with the National Football League to promote dairy sales in U.S. schools; support for U.S. Dairy Export Council offices in foreign markets; and funding for research and development of dairy ingredient applications in the food and beverage industry.

The DPSA required that a checkoff of 15 cents per hundredweight be assessed of dairy farmers in the 48 contiguous States only. Producers in Hawaii, Alaska, and Puerto Rico, as well as imported dairy products, were exempt from the assessment. The 2002 Farm Bill included a provision that required dairy importers to pay an assessment equivalent to that paid by domestic producers. However, this provision was not implemented during the period covered by the 2002 Farm Bill in light of a possible conflict with U.S. obligations under the WTO agreements. Changes to the 2002 Farm Bill's dairy import assessment language in the 2008 Farm Bill resolved the possible WTO conflict, and in May 2009 the Secretary of Agriculture published a proposed amendment to the Dairy Promotion and Research Order to implement the policy. After a public comment period, the Secretary published a *Federal Register* notice in March

¹ Marketing assessments are common in U.S. agriculture. Assessments are fees collected from U.S. producers, and in many cases importers of similar goods, and used to increase consumption in the United States and selected export markets through marketing campaigns and funding research. USDA oversees how the money is spent to ensure that it is consistent with the law and USDA policy. Most of the checkoff fees for several Congressionally authorized programs are used by private nonprofits. In addition to dairy, among the Federal checkoff programs currently in effect are for beef, pork, soybeans, eggs, cotton, mushrooms, honey, peanuts, popcorn, potatoes, watermelon, cultivated blueberries, Haas avocados, and mangoes.

² USDA/AMS, Directory, April 2011. <http://www.ams.usda.gov/AMSV1.0/getfile?dDocName=STELPRDC5066009> (accessed May 11, 2011).

³ DMI is the planning and management organization funded by checkoff fees to market U.S. dairy products. It is the parent arm of the American Dairy Association, National Dairy Council, and the U.S. Dairy Export Council (USDEC). <http://www.innovatewithdairy.com/Pages/About-Us.aspx>. (accessed on April 27, 2011).

⁴ Moss, "While Warning About Fat, U.S. Pushes Cheese Sales," Nov. 6, 2010.

2011, stating that he had amended the order to require that assessments be collected on imported dairy products, starting on August 1, 2011.

The exclusion of dairy imports from the assessment in the DPSA and its later inclusion in the 2002 and 2008 Farm Bills was, and remains, a contentious issue within the dairy industry. Dairy farmers and their representatives view the exemption as unfairly putting domestic products at a disadvantage when compared to imports, while dairy importers and users see the exemption as justified because of trade policies limiting imports of dairy products (for example, cheese TRQs) and because checkoff fees are used chiefly on promoting U.S.-produced products (for example, fluid milk).

With the order now amended and information available on how the import assessment will be implemented, it is now possible to analyze the magnitude of the assessment and possible impacts on dairy trade. Specifically, the purpose of this paper is: (i) to provide a brief overview of the dairy checkoff program; (ii) to summarize the views of representative dairy groups concerning the dairy import assessment; (iii) to estimate import assessments based on trade in 2005-2010, broken down by HTS4 product, country, and ad valorem equivalents (AVE); and, (iv) to evaluate the effect of the import assessment on foreign suppliers and domestic consumers, and on future trade patterns.

Overview of the Dairy Checkoff Program

With the goal of strengthening dairy prices by raising consumption of milk and dairy products, the 1983 DPSA directed the Secretary to issue a dairy products promotion and research order.⁵ The Order established the National Dairy Promotion and Research Program (NDPRP) to be funded by a checkoff paid by farmers. This program uses checkoff fees to promote dairy demand and to expand sales of U.S. milk and dairy products in domestic and overseas markets. Dairy importers had not been subject to checkoff fees under the law.

In May 2002, the U.S. Congress passed the Farm Security and Rural Investment Act (the 2002 Farm Bill). Section 1505 of this Bill amended the NDPRP authorizing language in the DPSA to establish an assessment of 15 cents per hundredweight of milk on all dairy product imports. The law required that

⁵ Dairy Promotion Program, 7 U.S.C. 4503 (a)-(b).

the assessments be charged by Customs and Border Protection (CBP) at the time when entry documents are filed, which would then remit the assessments to the National Dairy Promotion and Research Board (Dairy Board). In addition, the 2002 Farm Bill amendments specified that importer assessments were not to be used for foreign market promotion and that the “[o]rder be implemented in a manner consistent with United States trade obligations.”⁶

However, as indicated above, the USDA did not implement the assessment requirement for imports in the 2002 Farm Bill in order to avoid a potential WTO conflict. The 2002 Farm Bill also directed the Secretary, in consultation with the U.S. Trade Representative, to ensure that the order be implemented in a manner that is consistent with U.S. international trade obligations.⁷ At the national level, the mandatory assessment applied only to producers and processors in the 48 contiguous States; producers and processors in Alaska, Hawaii, and Puerto Rico were exempt. The USTR view, with the USDA in agreement, was that the exemption of those states and Puerto Rico meant that some domestic producers would be treated more favorably than importers,⁸ in possible violation of the national treatment principle under GATT/WTO.⁹

In June 2008, Congress passed the Food, Conservation, and Energy Act, also known as the 2008 Farm Bill. The 2008 Farm Bill revised the dairy import assessment provisions in the 2002 Farm Bill in two significant ways. First, it changed the “definition” of the United States to include all 50 States, Puerto Rico, and the District of Columbia, thus making producers in these regions subject to the 15 cents per hundredweight assessment on all milk produced and marketed commercially. This change meant that an assessment could be made on imported dairy products without violating the WTO national treatment principle. Second, the 2008 Farm Bill authorized assessment and collection of a payment on imported

⁶ In addition, the 2002 Farm Bill required that the Dairy Board have the representation of importers. Initially, importers are required to be represented by two importers appointed by the Secretary. Thereafter, importer representation on the Board will be adjusted at least once every three years, if necessary, to reflect the volume of imports relative to domestic production of milk.

⁷ Dairy Promotion Program, 7 U.S.C. 4503 (d).

⁸ *Federal Register*, 76, no. 53 (March 18, 2011): 14782-14783.

⁹ National treatment is a basic principle of GATT/WTO that prohibits discrimination between imported and domestically produced goods with respect to internal taxation or other government regulations. The principle of national treatment is formulated in Article 3 of the GATT 1947.

dairy products at a rate of 7.5 cents per hundredweight of milk (or the equivalent thereof), equivalent to one-half the payment remitted from domestic dairy farmers.

On May 19, 2009, USDA published a proposed rule in the *Federal Register* to implement the dairy import assessment program, with a 30-day comment period.¹⁰ Major comments covered the use of default assessment rates,¹¹ and confidentiality of business information associated with compliance, enforcement, and recordkeeping. USDA published its final rule in the *Federal Register* on March 18, 2011,¹² amending the Dairy Order, establishing the dairy import assessment program required by the 2002 and 2008 Farm Bills, and eliminating default rates as a method of assessment. The final rule requires that, as of August 1, 2011, an assessment of 7.5 cents per hundredweight of milk (or equivalent thereof) be imposed on imported dairy products. It also requires that as of April 1, 2011, (i) two additional Dairy Board members be created (from 36 to a total of 38) to represent dairy importers; (ii) the term “United States” cover all 50 States, the District of Columbia, and Puerto Rico; and (iii) a 15 cent per hundredweight assessment on milk of dairy farmers be extended to producers in Alaska, Hawaii, and Puerto Rico.

Views of Representative Dairy Groups

The dairy import assessment has been somewhat controversial within certain segments of the U.S. dairy industry since its inclusion in the 2002 Farm Bill. Dairy manufacturers that use dairy inputs to produce further processed goods view the dairy import assessment much differently from dairy farmers and cooperatives processing milk. Representative views are summarized below.

National Milk Producers’ Federation (NMPF)

The National Milk Producers Federation (NMPF) represents U.S. dairy cooperatives and their producer members who collectively produce approximately 85 percent of the U.S. milk supply. NMPF

¹⁰ *Federal Register*, 74 (May 19, 2009): 23359.

¹¹ Default assessment rates are an alternative means of assessing dairy imports when the milk solids content is not included in an importer’s paperwork. Default assessment rates covered all 10 digit HTS subheadings for dairy products. As of March 18, 2011, when the final import assessment rule was published in the *Federal Register*, default rates were eliminated as an option for assessing such imports. Many comments submitted to AMS prior to the final rule were critical of default rates, which may have contributed to their elimination in the final rule. See, for example, CIAA letter to Whitney Rick, AMS, June 18, 2009.

¹² *Federal Register*, 76, no. 53 (March 18, 2011): 14782-14783.

first worked with Congress to include a provision in the 2002 Farm Bill to expand the promotion checkoff to imports and it again worked with Congress as it wrote the 2008 Farm Bill to ensure that the checkoff was applied in every State in the Union and Puerto Rico. In an NMPF press release, its CEO, Jerry Kozak, noted that the new dairy import assessment fee achieves a degree of fairness between domestic milk production and imports in promoting dairy consumption.¹³

International Dairy Food Association (IDFA)

The International Dairy Foods Association (IDFA) represents the Nation's dairy manufacturing and marketing industries and their suppliers, with a membership of 550 companies. IDFA is composed of three constituent organizations: the Milk Industry Foundation (MIF), the National Cheese Institute (NCI) and the International Ice Cream Association (IICA). The IDFA has expressed concerns about the impact that the new assessments on dairy imports will have on trade. IDFA notes that the United States trades dairy products with more than 150 countries, and claims that the import assessment fee has been widely opposed by U.S. trading partners.¹⁴ IDFA is concerned about how other countries will respond to this fee, and it questions why U.S. dairy farmers are willing to promote dairy imports with funds from the import assessment fee at a time when U.S. dairy imports are declining and U.S. dairy exports are growing. IDFA has also raised concerns regarding the amount of proprietary information collected for imported dairy products, relative to domestic dairy products, and the oversight of that information.¹⁵

Other Dairy Constituents

Many foreign dairy companies and multinationals that trade dairy products oppose the final rule implementing the dairy import assessment. Under an umbrella organization called the Alliance for Fair Dairy Promotion, Fonterra USA, Nestle USA, Kraft, Schreiber, IDFA, and others, submitted comments to

¹³ NMPF. "NMPF Applauds Long-Awaited Arrival of Promotion Checkoff On Dairy Imports." March 18, 2011.

¹⁴ IDFA. "IDFA CEO Expresses Concerns about Trade Implications of New Dairy Import Tax," March 18, 2011.

¹⁵ Tipton, Letter to Kimberly Coy. January 12, 2011.

USDA in June 2009, stating that dairy importers should not be required to pay the dairy assessment because the dairy checkoff program is biased toward domestic production promotion.¹⁶

Method for Calculating the Assessment

As noted, the *Federal Register* notice announcing the final rule states that the assessment rate on imported dairy products will be “7.5 cents per hundredweight of milk, *or equivalent thereof*” (emphasis added). According to the *Federal Register* notice, the assessment will be collected by CBP from the importer when entry summary documents are filed, and are based on the importer’s reported milk solids.¹⁷ Also, as noted, an alternate method of assessing dairy imports, using default rates, is no longer permitted. However, the default rates provide the best available basis for estimating assessments on dairy products, using historical data.

Under the method enacted in the final rule, the milk solids content of the product must be reported by the importer, with adequate documentation. This process essentially amounts to self-reporting by the importer. Records must be kept by the importer for two years beyond the calendar year of their applicability. For example, if an importer reports that a shipment of milk protein concentrate (HTS 0404.90.10) contained 950 kilograms of milk solids per metric ton of product, CBP would assess at a rate of \$0.01327 per kilogram.¹⁸ This rate equates to converting the \$0.075 per cwt. rate for fluid milk into a milk solids rate, assuming fluid milk contains 12.45 percent solids.

The default rates were calculated by the Agricultural Marketing Service (AMS) using various sources to provide estimates for solids content and an effective assessment rate per unit imported.¹⁹ Default rates were available for each 10-digit HTS code. The intention of the default rates was to provide a method of assessing imported dairy products if documentation was not available or not submitted. In

¹⁶ *Alliance for Fair Dairy Promotion*. “Re: National Dairy Promotion and Research Program.” June 18, 2009.

¹⁷ Milk solids content is the percent of milk solids in a dairy product. Milk solids are of 2 main types—fats and non-fat solids. Non-fat solids include milk protein, lactose, and ash.

¹⁸ *Federal Register*, 76, no. 53 (March 18, 2011): 14779.

¹⁹ USDA/AMS, *Proposed Default Import Assessment Rates for the National Dairy Promotion and Research Program*. This document also includes default milk solids percentage and volume to weight conversions used to calculate the quantity figures in this analysis.

that case, CBP would simply assess the imported product based on its weight or volume, using the appropriate rate AMS supplied.

Evaluation of the Assessment

In order to gauge the likely effects of extending the assessment to dairy imports, the authors used actual U.S. import data for 2005–10 and the AMS default rates to estimate levels of milk solid imports and assessment fees that would have been charged if the policy had been in place during that period. The purpose was not only to determine the overall assessment levels but also to break down the total by product and importing country.

On an HTS4 basis, about one-half of milk solid imports come from two products, casein and caseinates (HTS3501) and cheese (HTS0406) (table 1). Milk protein concentrates (HTS0404) are also a major source of milk solid imports. Based on milk solids, New Zealand and the EU-27 are far and away the largest dairy suppliers to the United States (table 2). But U.S. imports of dairy declined during 2005–10, and nearly the entire decline came from these two sources together with Canada, Argentina, and Australia.

Tables 3 and 4 show the U.S. imports of dairy products on a milk equivalent basis during 2010, by HTS4 number and by country. Multiplying the corresponding USDA default rates by the actual a 6-digit HTS level import values, we calculated the assessment fees that would have been paid for major categories of dairy products if the program had been in effect during 2010. Also presented are ad valorem equivalents (AVEs) of the assessment, equal to the total assessment divided by the value of imports. The results show average AVEs at 0.20 percent, ranging from 0.07 percent to 0.45 percent of average unit value, with the exception of lactose (1.07 percent). This is the equivalent of 20 cents for every \$100 of imported value—a cost to be sure, but not an extravagant one.

TABLE 1 U.S. dairy imports by HTS4, 2005–10 (1,000 hundredweight of milk equivalent)

HTS4	Product	2005	2006	2007	2008	2009	2010
401	Fluid Milk	1,023	284	500	489	394	488
402	Fluid Milk with added sweetener	3,268	3,622	4,547	4,019	4,447	2,807
403	Fluid Buttermilk, Yogurt, etc.	157	200	303	196	96	178
404	MPC and Whey	13,101	13,921	12,966	12,105	9,842	9,223
405	Butter	3,678	3,310	3,199	2,306	2,550	2,050
406	Cheese	19,095	19,296	18,393	16,172	16,171	13,828
1517	Margarine	0	0	0	0	0	0
1702	Lactose	874	927	850	1,187	1,386	1,421
1704	Confectionary- not chocolate	30	28	46	43	31	71
1806	Chocolate	10,782	9,881	9,941	7,740	5,331	4,169
1901	Food Preparations	113	184	329	707	427	704
2105	Ice Cream	163	193	203	168	186	240
2106	Other Food Preparations	6,463	9,271	8,605	3,750	5,552	2,654
2202	Beverages	57	22	17	22	37	41
3501	Casein	17,678	15,026	16,655	21,841	13,484	13,083
3502	Albumins	1,517	1,136	1,273	1,335	1,848	1,201
	Total	77,999	77,302	77,827	72,079	61,780	52,156

Source: U.S. International Trade Commission (Dataweb); U.S. Department of Agriculture, Agricultural Marketing Service, Dairy Assessment Default Rates.

TABLE 2 U.S. dairy imports by country, 2005–10 (1,000 hundredweight of milk equivalent)

Country	2005	2006	2007	2008	2009	2010
New Zealand	25,152	29,157	30,064	22,544	23,621	15,845
EU-27	20,039	16,874	16,810	21,006	15,625	15,632
Canada	15,990	14,236	13,663	10,047	6,050	5,141
Mexico	4,921	4,721	4,735	4,751	5,018	4,899
Australia	3,732	4,672	4,564	3,167	3,907	3,388
India	1,810	1,211	2,076	2,149	998	1,873
Argentina	2,049	2,177	1,479	3,459	2,386	1,299
Switzerland	936	822	885	801	743	835
Norway	947	843	974	930	917	822
Other	2,424	2,588	2,577	3,225	2,515	2,422
Total	77,999	77,302	77,827	72,079	61,780	52,156

Source: U.S. International Trade Commission (Dataweb); U.S. Department of Agriculture, Agricultural Marketing Service, Dairy Assessment Default Rates.

TABLE 3 U.S. dairy imports, estimated dairy import assessment fees collected, average unit values, and ad valorem equivalents, by HTS 4, 2010

HTS4	Product	Estimated fees collected	U.S. imports	U.S. imports	U.S. imports	Ad valorem equivalent
		<i>1,000 dollars</i>	<i>1,000 cwt milk equivalent</i>	<i>1,000 dollars</i>	<i>Dollars per cwt milk solids</i>	<i>Percent</i>
0401	Fluid Milk	37.4	488	8,396	17.21	0.45
0402	Fluid Milk w/ added sweetener	210.1	2,807	66,744	23.78	0.31
0403	Fluid Buttermilk, Yogurt, etc.	13.3	178	15,805	88.84	0.08
0404	MPC and Whey	689.4	9,223	237,616	25.76	0.29
0405	Butter	151.1	2,050	42,573	20.77	0.35
0406	Cheese	1,030.5	13,828	746,962	54.02	0.14
1702	Lactose	105.4	1,421	9,819	6.91	1.07
1704	Confectionary- not chocolate	5.5	71	3,435	48.58	0.16
1806	Chocolate	302.9	4,169	158,253	37.96	0.19
1901	Food Preparations	52.6	704	27,186	38.62	0.19
2105	Ice Cream	17.5	240	17,560	73.17	0.10
2106	Other Food Preparations	204.1	2,654	49,133	18.51	0.42
2202	Beverages	2.1	41	3,031	74.83	0.07
3501	Casein	976.2	13,083	515,086	39.37	0.19
3502	Albumins	92.8	1,201	47,287	39.36	0.20
	Total	3,890.9	52,156	1,948,889	37.37	0.20

Source: U.S. International Trade Commission (Dataweb); U.S. Department of Agriculture, Agricultural Marketing Service, Dairy Assessment Default Rates.

TABLE 4 U.S. dairy imports, estimated dairy import assessment fees collected, average unit values (AUVs), and ad valorem equivalents (AVEs), by country, 2010

Country	Estimated fees collected	U.S. imports	U.S. imports	U.S. imports	Ad valorem equivalent
	<i>1,000 dollars</i>	<i>1,000 cwt milk equivalent</i>	<i>1,000 dollars</i>	<i>Dollars per cwt</i>	<i>Percent</i>
New Zealand	1,188.4	15,845	467,269	29.49	0.25
EU-27	1,165.5	15,632	783,355	50.11	0.15
Canada	375.1	5,141	171,327	33.33	0.22
Mexico	365.3	4,899	132,047	26.95	0.28
Australia	256.2	3,388	94,843	27.99	0.27
India	136.6	1,873	76,783	40.99	0.18
Argentina	98.7	1,299	50,722	39.05	0.19
Switzerland	62.7	835	64,030	76.68	0.10
Norway	64.0	822	40,167	48.86	0.16
Chile	33.9	452	12,039	26.64	0.28
Uruguay	14.6	195	7,526	38.59	0.19
Israel	10.4	138	5,246	38.02	0.20
Total	3,890.9	52,156	1,948,889	37.37	0.20

Source: U.S. International Trade Commission (Dataweb); U.S. Department of Agriculture, Agricultural Marketing Service, Dairy Assessment Default Rates.

Because the dairy import assessment is based on the milk solids content of the imported product, and not the value, assessment fees will have less impact on importers shipping higher value goods with relatively low milk solids content (table 3). For example, cheese would be relatively less affected by the assessment than casein since it is a higher value product, despite having similar import quantities on a milk solids basis. Therefore, countries that ship lower valued products are likely to be more affected by the assessments. The United States' two largest dairy suppliers, New Zealand and the EU-27, would be affected differently. New Zealand, which sends more milk protein concentrate (MPC), would have a relatively higher assessment as compared with assessment of EU-27 and other European countries that ship more cheese and other high-value products.²⁰ The same patterns hold true for other dairy products and suppliers. Lower valued products, and countries that supply such products, will pay a relatively higher assessment on an ad valorem equivalent basis. But in every case, import assessment fees still represent a very small percentage of total value.

Table 5 provides a cross section of estimated U.S. dairy import assessment fees in 2010 across major exporting countries and imported products. Using actual U.S. imports in that year, one-half of New Zealand's assessment fees would have been collected for MPC and other products under HTS 0404; more than one-half of the fees collected from the EU-27 and almost all the fees from Norway and Switzerland would have been from cheese (HTS 0406).

Tables 6 and 7 estimate the assessment fees during 2005-2010, using historical U.S. dairy import levels and default assessment rates. The estimated dairy import assessment fees trend downward, tracking lower U.S. import volumes over the period. Over this period, roughly two-thirds of those assessments are paid by New Zealand and the EU-27, reflecting their shipments of casein, caseinates, and MPCs (NZ) and cheese (EU-27).

²⁰ In the aggregate, European cheese-exporting countries would have paid the lowest dairy assessments in 2010 as a percentage of import value, ranging from 0.10 percent for Switzerland, 0.15 percent for the EU-27, and 0.16 percent for Norway.

TABLE 5 Estimate of fees assessed using 2010 import levels, by product and country (1,000 dollars)

HTS4	Product	New Zealand	EU-27	Canada	Mexico	Australia	India	Argentina	Norway	Switzerland	Chile
0401	Fluid milk	0.3	2.7	3.9	29.2	0.9	0.0	0.0	0.0	0.0	0.0
0402	Fluid milk w/ added sweetener	19.1	28.8	0.0	109.8	10.3	0.0	0.0	0.0	0.0	27.4
0403	Fluid buttermilk, yogurt, etc.	0.0	2.5	6.2	0.3	0.0	0.0	0.0	0.0	0.0	0.0
0404	MPC and whey	566.7	4.4	112.3	0.0	0.0	3.3	0.0	0.0	0.0	0.0
0405	Butter	51.6	31.5	40.6	0.0	15.8	3.5	0.1	0.0	0.0	0.0
0406	Cheese	45.1	660.1	38.9	27.8	30.2	0.4	39.8	61.4	59.7	0.4
1702	Lactose	0.0	39.8	45.6	0.0	0.0	0.0	0.1	0.0	0.0	0.0
1704	Confectionary- not choco	0.0	5.3	0.0	0.0	0.0	0.0	0.0	0.0	0.2	0.0
1806	Chocolate	0.0	24.6	108.7	168.9	0.0	0.1	0.0	0.0	0.2	0.0
1901	Food preparations	0.0	14.3	0.0	26.5	0.0	0.1	1.1	0.0	0.0	6.0
2105	Ice cream	0.0	4.5	4.5	1.4	1.8	0.0	0.1	0.0	0.0	0.1
2106	Food preps	158.0	1.4	14.4	0.5	25.3	0.0	0.0	0.0	0.2	0.0
2202	Beverages	0.0	0.2	0.0	0.8	0.0	0.0	0.0	0.0	0.0	0.0
3501	Casein	289.9	320.4	0.0	0.0	167.0	129.2	56.3	0.0	2.5	0.0
3502	Albumins	57.7	25.0	0.0	0.0	4.9	0.0	1.3	2.6	0.0	0.0
	Total	1,188.4	1,165.5	375.1	365.3	256.2	136.6	98.7	64.0	62.7	33.9

Source: U.S. International Trade Commission (Dataweb); U.S. Department of Agriculture, Agricultural Marketing Service, Dairy Assessment Default Rates.

TABLE 6 Estimates of dairy import assessment fees, by HTS4, 2005-10 (1,000 dollars)

HTS4	Product	2005	2006	2007	2008	2009	2010
0401	Fluid Milk	78.5	22.1	38.3	36.9	30.0	37.4
0402	Fluid Milk w/ added sweetener	245.1	272.1	341.2	301.9	333.6	210.1
0403	Fluid Buttermilk, Yogurt, etc.	11.3	14.2	21.5	14.0	7.2	13.3
0404	MPC and Whey	980.3	1,041.6	970.2	904.0	735.0	689.4
0405	Butter	269.3	243.4	235.3	171.2	189.5	151.1
0406	Cheese	1,431.0	1,443.0	1,373.3	1,208.4	1,207.3	1,030.5
1702	Lactose	64.8	68.8	63.0	88.1	102.7	105.4
1704	Confectionary- not chocolate	2.3	2.2	3.6	3.3	2.4	5.5
1806	Chocolate	772.3	707.7	711.9	555.0	386.1	302.9
1901	Food Preparations	8.4	13.7	24.5	52.9	32.0	52.6
2105	Ice Cream	12.8	14.7	15.7	12.9	14.2	17.5
2106	Other Food Preparations	499.2	715.9	664.2	288.3	428.7	204.1
2202	Beverages	3.2	1.2	0.9	1.2	1.9	2.1
3501	Casein	1,304.7	1,113.6	1,232.0	1,627.5	1,001.5	976.2
3502	Albumins	117.3	87.8	98.4	103.2	142.8	92.8
	Total	5,800.4	5,761.9	5,793.9	5,368.8	4,615.0	3,890.9

Source: U.S. International Trade Commission (Dataweb); U.S. Department of Agriculture, Agricultural Marketing Service, Dairy Assessment Default Rates.

TABLE 7 Estimates of dairy import assessment fees, by country, 2005–10 (1,000 dollars)

Country	2005	2006	2007	2008	2009	2010
New Zealand	1,889.8	2,196.1	2,260.1	1,687.3	1,773.9	1,188.4
EU-27	1,490.0	1,255.1	1,250.9	1,568.3	1,164.8	1,165.5
Canada	1,161.6	1,033.3	990.0	727.3	440.9	375.1
Mexico	366.7	352.0	353.0	354.5	373.7	365.3
Australia	277.7	350.6	342.8	239.3	293.0	256.2
India	132.1	87.9	150.7	156.2	72.7	136.6
Argentina	156.7	166.3	112.8	263.9	181.8	98.7
Norway	73.7	65.8	75.7	72.5	71.6	64.0
Switzerland	70.8	62.0	66.7	60.3	56.0	62.7
Rest of World	181.3	192.9	191.2	239.1	186.5	178.5
Total	5,800.4	5,761.9	5,793.9	5,368.8	4,615.0	3,890.9

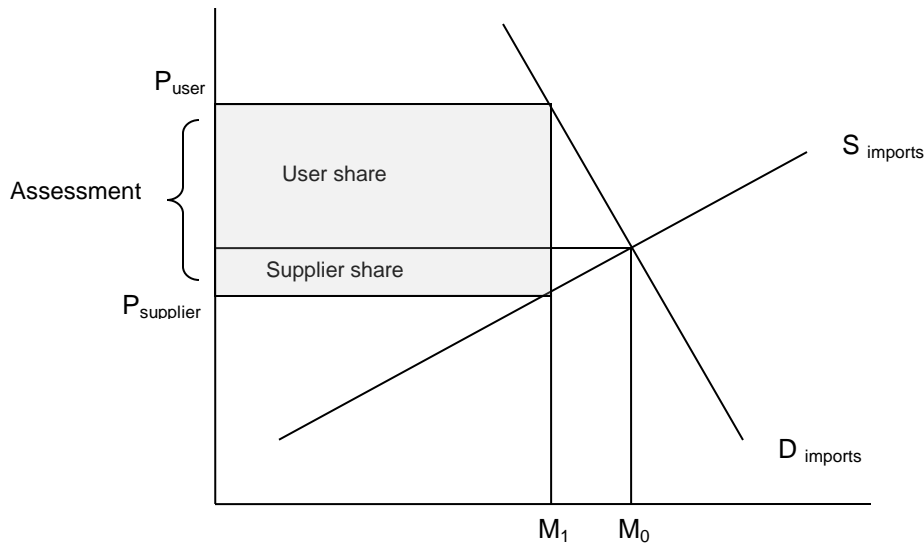
Source: U.S. International Trade Commission (Dataweb); U.S. Department of Agriculture, Agricultural Marketing Service, Dairy Assessment Default Rates.

Absorbing the Cost of the Dairy Import Assessment in the Supply Chain

Imposing the dairy import assessment raises two important questions—who will ultimately pay the cost of the assessment and what will its impact be on the demand for imported dairy products? Given that the assessment operates like a tariff on imports, a simplified economic framework for analyzing tariffs can be used for analyzing the assessment, as illustrated in figure 1. The model oversimplifies the complex marketing and supply chain of the dairy industry, but it helps illustrate the market effects of the regulation, including who bears the burden of the assessment rate. The assessment lowers the supplier price (to P_{supplier}), raises the user price (to P_{user}), and reduces the amount of imports (from M_0 to M_1). The assessment collected is represented by the shaded rectangle, which is allocated between the user and the supplier of the imported good. The more inelastic the demand (i.e., the steeper the demand curve, D_{imports}), the less the demand for imports declines, resulting in a greater financial impact of the assessment on the user. If the demand curve is infinitely inelastic, the assessment is entirely passed through to the user and not absorbed at all by the supplier.

In the aggregate, whether the supplier or the user of dairy imports absorbs the cost of the new dairy import assessment is determined largely by the price elasticity of demand. Considering the current product mix of dairy imports, we consider that imports are likely to have an inelastic demand. In that

FIGURE 1 Economic effect of dairy import assessment on demand



Source: Compiled by USITC staff.

case, assessment costs will be absorbed by final end-users rather than suppliers, and imports face some prospects for substitutability with domestic dairy products. But many dairy imports are low-cost inputs in processed goods. High-volume dairy imports, including casein, caseinates, and MPCs, are a small percentage of the overall cost of the final retail good. Additionally, certain imports are specifically tailored to production processes, and U.S. dairy companies would be reluctant to substitute them for domestically produced alternatives, as this would require costly production testing. Furthermore, cheese imports from European countries (mainly EU-27 countries, Norway, and Switzerland) are often specialty cheeses targeting high-end retail shops and specific consumer tastes. For goods such as these, small price increases are readily passed to the consumer and may not even be noticed at the checkout counter.²¹ These factors suggest a highly inelastic demand for imported dairy products, with the assessment having little impact on import demand and assessment fees affecting users more than the suppliers.

²¹ The trend toward more substitution of imported cheese by U.S. production and its impact on U.S. demand for EU specialty cheeses in the long term remains unclear. But analysts and economists continue to note both import substitution and a shift in demand for such cheeses in the large U.S. market. See for example, Dobson, "U.S. & Global Economic Outlook: What's Ahead For U.S. Dairy?" April 5, 2011; Jesse, "U.S. Dairy Trade Situation and Outlook: 2011," 2011.

Economic studies analyzing the dairy industry have demonstrated that for the most part, price elasticities of demand for dairy products in the United States are relatively inelastic.²² For example, studying the possible effects of a fat tax on the U.S. consumption of dairy products, Chouinard²³ concluded that a 10 percent tax on the fat content of dairy products has relatively little effect on the quantity of dairy products consumed. Moreover, the study's simulations suggested that such a tax would reduce average fat consumption by less than 1 percent, and a 50 percent tax on dairy fat would reduce fat consumption by only 3 percent.

Payments under the new dairy import assessment program will impact the demand for dairy imports similarly to Chouinard's fat tax, but with at least two important differences. The first is that the assessment rate is far smaller than 10 percent, severely limiting the negative effects of the tax on dairy consumption. The authors' estimates are that the import assessment will remain very small, ranging from 0.07 percent to 1.07 percent ad valorem equivalent. The second difference between an analysis of fat taxes on dairy products and the import assessment is that the new fee applies only to imports and not to all dairy products. Although dairy products produced in the United States have paid an assessment for many years, and in fact pay at double the rate of imports (15 cents per hundredweight of milk equivalent), the question is whether the imposition of a new tax on imports will shift demand toward domestic dairy products. For reasons elaborated above, the authors view this shift as unlikely to occur. Small increases in the cost of specialty cheeses are unlikely to be noticed in the final price, even if fully passed through to the consumer. For other dairy imports, U.S. food manufacturers would be reluctant to substitute specifically tailored inputs for domestically-produced alternatives. Because these inputs represent a small percentage of manufactured cost, the overall cost of the import assessment relative to the retail prices for final consumer goods is very small indeed.

Who will ultimately pay the cost of the new dairy import assessment? Based on the current product mix being imported, the final end-user (i.e, the consumer) will absorb the larger share of this cost.

²² There is recent evidence that the demand for certain dairy products has become more price elastic (See Davis, et al. *An Analysis of U.S. Household Dairy Demand*, 2010). However, in our illustration, the assumption is that products in the dairy sector are still generally price inelastic—in particular, the products which are imported into the United States.

²³ Chouinard, et al., "Fat Taxes: Big Money for Small Change," *Forum for Health Economics and Policy*, Vol. 10, no. 2 (2007).

But regardless of whether the imported products are final consumer goods or dairy inputs used in processed foods, assessments are likely to be passed through to the consumer without a noticeable impact on the demand for imported dairy products.

Conclusion

When the new USDA dairy import assessment fee goes into effect on August 1, 2011, additional funds will almost certainly be generated for the promotion of dairy products. However, assuming future trade patterns remain similar to those in 2005-10, the annual assessment fees collected from U.S. dairy imports will likely be small. If the dairy import assessment had been in effect during 2010, it would have generated about \$3.9 million for promotional activities (tables 5 and 6). For a U.S. industry that generated approximately \$100 billion in sales during 2010 and imported \$2 billion in dairy products, the generated revenues from import assessments are negligible in comparison.

Mandatory producer assessments under the Dairy Act totaled \$284.5 million in 2008, the last year for which data are available. In that year, the Dairy Board's portion of the assessment was \$95.5 million, and revenues for qualified regional and state programs totaled \$189 million.²⁴ In 2008, the import assessments would have generated approximately \$5.4 million in new revenue that year (table 6), a figure unlikely to significantly impact promotional strategies. But while the benefit to the U.S. dairy industry will be limited, the negative impact on importers, users of imported dairy inputs, and final consumers will likely be just as small.

²⁴ *USDA Report to Congress on the National Dairy Promotion and Research Program and the National Fluid Milk Processor Promotion Program*, 1.

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