

Testimony of Mr. Dalton Yancey

Representing

The Members of the
Florida Sugar Cane League,
Rio Grande Valley Sugar Growers, and
Hawaii Sugar Farmers

Before the

Farm Service Agency

United States Department of Agriculture

Regarding the Consideration of

The Granting of Cane Sugar Marketing Allotments

To New Entrants

For the 2003 and Subsequent Crops

January 29, 2003

INTRODUCTION

My name is Dalton Yancey. I am pleased to present this testimony on behalf of the members of the Florida Sugar Cane League, the Rio Grande Valley Sugar Growers, and the Hawaii Sugar Farmers, regarding the implications of the granting of cane sugar marketing allotments to new entrants will have on the above named interests. My contact information is appended to the end of this testimony for your information.

We are pleased that the Department of Agriculture has convened this hearing today to review the pending application of the Arizona Sugar Factory, L.L.C. (Arizona Sugar) for new entrant allotments. We strongly believe that this hearing to review the issues surrounding the application is very timely, and we thank you for convening it.

We believe that the application submitted by Arizona Sugar is so premature that it must be denied at this time. The noticed application raises a host of issues about how the Department will consider and address the many factual and competitive issues raised by this application. Material changes to the application that were requested by the applicant as recently as last week underscore the prematurity of this application.

Because this is the first such application to be made, we urge the Department to carefully establish an equitable process for addressing such issues not only with regard to this application, but with regard to any number of additional applications that may be made in the future for cane allocations and allotments.

BACKGROUND

When Congress passed and the President signed the Farm Security and Rural Investment Act of 2002, the sugar marketing allotment provisions of the Agricultural Adjustment Act of 1938 were amended to provide for “new entrant” processors to obtain processing allotments. Congress wisely provided that these new entrant allotments may only be granted under narrowly specified circumstances.

First, the legislation seeks to assure that any new entrants are viable companies that are processing sugarcane and that can demonstrate a real world ability to produce and market sufficient raw cane sugar to fulfill the allocation.

In the case of sugarcane, the law requires that the Secretary of Agriculture shall take into consideration any adverse effects that the provision of the allocation or allotment may have on existing cane processors and producers.

These adverse effects must be carefully considered and weighed before the Secretary grants an initial allocation to any new entrant processor or an initial allotment to a new entrant State.

THE PENDING APPLICATION SHOULD BE DENIED

At the present time we are opposed to the granting of allotment in the State of California to the Arizona Sugar Factory, L.L.C. (Arizona Sugar) as originally noticed in the Federal Register. We are also opposed to the granting of allotment to Arizona Sugar in the State of Arizona, as we understand to be the applicant's latest desire. It is our understanding that the applicant has requested an allotment of 10,000 short tons raw value (STRV) for crop year 2003, with that allotment expanding to 50,000 STRV by crop year 2005.

Our understanding of the status of the applicant is that as of today there is no sugarcane processing facility owned and operated by Arizona Sugar, either in California or in Arizona. There has been no demonstration that the applicant has a certain, existing supply of sugarcane to supply the as yet non-existent processing facility. There has been no demonstration of the applicant's ability to market the cane sugar that this venture may produce, with all that entails.

Based on the facts, as they are known to us, we believe that by any objective analysis this venture presently fails every test contemplated by Congress and the Department in the authorizing statute and the implementing regulations. We will address some of these tests later in our testimony.

There has been some discussion of deferring a decision on the Arizona Sugar application until a later date, but in the mean time granting the applicant a "provisional" allotment for crop year 2003. Presumably some subsequent review by the Department, prior to the beginning of crop year 2003, would be made to determine whether the applicant meets the appropriate statutory and regulatory requirements.

We are strongly opposed to such a course of action. The administrative invention of a "provisional" allotment is not authorized in or contemplated by the implementing statute. In addition, without a subsequent, duplicative hearing on the application, this course of action will deprive other interested industry participants of the due process envisioned in the statute. Commercially, the granting of a provisional allotment will announce that the government intends to take allotment away from existing cane processors and grant it to a speculative business venture. The adverse effects that such a policy will impose on viable, existing cane processors and producers will be manifold, and are addressed in some detail below.

SETTING AN EQUITABLE PROCEDURAL PRECEDENT

We oppose the granting of some sort of "provisional allocation" to the applicant – or to any applicant – based on the expectation that the statutory tests for a new entrant may be met at some later date. We do not believe that this is consistent with the statute. Such a course of action will harm existing sugar producers and processors for the speculative enrichment of possible new entrants.

Perhaps more importantly, we are very concerned with the precedent that will be set by the granting of a “provisional allocation”. The granting of a “provisional allocation” may appear to be an administrative convenience in the case of a single processor application. However, when viewed through the prism of the precedent that it sets, it will have serious and far-reaching adverse consequences.

ADVERSE IMPACTS ON EXISTING PRODUCERS

It must be recognized that the allocation of allotments is a zero sum game. The granting of any new allotment, even to an immature or speculative new venture, by definition reduces the allotment available to existing sugarcane processors and producers that are mature, on-going business concerns.

If several applicants were to be granted “provisional allocations” it will create great uncertainty and instability in the market for sugar in the United States. Preventing such uncertainty and instability was one of the primary reasons that Congress enacted marketing allotments for sugar in the 2002 farm bill.

Business Uncertainty and Market Disruptions.

The uncertainty created by the granting of “provisional allocations” could lead to disruptions in every facet of the business of existing sugar processors, from the security of their lines of credit from lenders all the way down to the jobs of their workers in the fields and on the production line. In addition, great uncertainty will be cast upon the planting intentions and preparations of sugarcane growers. This uncertainty and caution will affect the sales of the many input suppliers that depend on the business of sugarcane growers to remain solvent. Jobs could be threatened at every step of the supply chain, from input suppliers to sugarcane growing operations, to sugarcane processors, to marketers and food manufacturers.

These disruptions should not be imposed on this array of individuals and concerns in order to satisfy an applicant’s desire to have a “provisional allocation” locked up *before* the applicant has proven that it meets the requisite tests as a sugarcane processor under the law.

The uncertainty created by “provisional allocations” will create obvious difficulties for the nation’s sugarcane growers and processors in planning their crop plantings, processing capacities, and marketing plans for the “provisional” 2003 crop year. It will not be known which, if any, applicants fulfill the statutory requirements to receive their allocations until days before the crop year begins (but well after planting, with harvest fast approaching). Consequently, the potential allotment amounts for existing allotment holders will be an unknown (and subject to further reduction) until the last possible moment.

The injection of this kind of administrative volatility into the production, supply, and marketing of sugar is unwarranted.

A more subtle, but no less damaging effect of the granting of “provisional allocations” is the serious implication for the availability of financing for existing sugarcane producers and processors. As administrative volatility is increased surrounding the allotment allocation process, lenders will likely view their lending risk as increasing as well. Thus, the ability of existing producers and processors to maintain production financing will be diluted in favor of speculative ventures that are granted “provisional allocations”. This is likely to damage the interests of the agricultural lending community as well as sugarcane producers and processors.

The granting of “provisional allocations” will garner similar negative effects for the ability of sugarcane processors to fulfill sales contracts for their products. In order to avoid the possibility of having to unwind contracts due to uncertain and possibly declining allotment allocations, existing processors will likely respond by forward contracting less sugar. This will lead to increased volatility and reduced certainty in the supply and pricing of sugar commercially. These effects will likely manifest themselves in increased supply and price volatility in the food manufacturing and consumer sectors.

We believe that when the allocation of allotment is contemplated to speculative or immature ventures, or on a “provisional” basis, the many adverse impacts on mature, on-going concerns dictate a decision against the granting of such allocations.

Circumvention of Due Process.

In addition, the granting of any provisional allocation is likely to circumvent the carefully considered process for the open public consideration of the facts surrounding an application for allotments by the Department and the industry.

The Arizona Sugar application before us today is a good example of this problem. There are no facts on which to conclude that the applicant meets any of the legal requirements to be a viable processor. If the applicant were to be granted a “provisional allocation” following this hearing, the statutory requirement for a hearing regarding the facts on which the allocation was granted will not have been satisfied. That requirement can hardly be satisfied if the only fact surrounding the issue of whether or not the applicant is a qualified “processor” is the fact that the processor does not yet exist.

Under this circumstance, the only way to fulfill the hearing requirement is to hold a second hearing on the facts of the applicant’s status as an eligible processor. Presumably, this second hearing would need to take place some time *after* the processor arguably achieves “eligible” status but *before* the allotment is actually granted. For example, if an initial hearing and the granting of a provisional allocation now means that there cannot or will not practically be another hearing on the Arizona Sugar application to determine whether the applicant factually fulfills the necessary requirements, then we believe that today’s hearing will have been premature. The statutory hearing requirement will have been rendered useless and other interested industry participants will have been disenfranchised.

WHAT FACTORS SHOULD BE CONSIDERED IN DETERMINING WHETHER A “PRODUCER” IS LEGITIMATE?

In the public announcement regarding this hearing, USDA suggested that it might be helpful if we addressed the issue as to what the evidence of legitimacy should be for an applicant seeking an allocation of allotment. In other words, what does it take to be a processor, a marketer, and a producer of sugar?

We believe that a good starting point for this discussion is the definitions for these terms used in the Department’s implementing regulations (7 CFR 1435.2). These regulations define a “sugarcane processor” to mean

“...a person who commercially produces sugar, directly or indirectly, from sugarcane, has a viable processing facility, and a supply of sugarcane for the applicable allotment year.”

All of the terms in this definition assume that the processor currently “*produces sugar*”, “*has a viable processing facility*”, and “*has a supply of sugarcane*”. Neither the statute nor the regulations contemplate that an allotment may be granted to an applicant that merely *plans* to produce sugar, *seeks to construct* a viable processing facility, or *may have* a supply of sugarcane.

It is also worth noting that the definition lays out a conjunctive test. All three requirements must be met before an applicant can meet the test as a sugarcane processor.

In sum, we believe that before an applicant can be considered a producer eligible for the granting of allotment, the applicant must show that they have the land, water, labor, management skill and capacity to grow a crop of sugarcane; the processing capacity, capital investment, labor, and skill to operate a processing facility; and the marketing expertise and capacity to profitably market the sugar on a competitive basis.

We urge that any applicant for an allocation also meet the many regulatory requirements a processor must meet to be eligible for the sugar loan program. These requirements act as evidence of a processor’s viability, and include:

- A sugarcane processor is eligible for loans only if it has agreed to all of the terms and conditions in the applicable USDA loan application, and has executed a note and security agreement, and storage agreement with the Commodity Credit Corporation (7 CFR 1435.102(b)).
- All sugar pledged as collateral must be derived from that of eligible producers, processed and owned by the eligible

processor, stored in a CCC-approved warehouse, and meet minimum quality requirements (7 CFR 1435.102(c) and (d)).

- A processor receiving a loan must meet the minimum grower payment requirements for the crop year (7 CFR 1435.104).
- The processor must certify to CCC that the processor intends to share its allocation among its producers fairly and equitably, and in a manner reflecting each producer's production history (7 CFR 1435.310).

Similarly, the regulations define the term "ability to market" to mean

"the estimated quantity of sugar, raw value, as CCC determines, that *will be produced* in the cane State or by the sugarcane processor, as appropriate, during the applicable crop year." (*emphasis added*).

Like the definition of "processor", the "ability to market" definition requires the Commodity Credit Corporation to estimate the quantity of sugar that "*will be produced*" by the processor. In the context of an application for an allocation of sugar marketing allotment, this definition does not allow room for conjecture that a completely speculative processing venture meets the "ability to market" requirement. Only a concrete factual showing that the processor will with certainty be producing sugar sufficient to fulfill an allocation of marketing allotment will meet this definitional test.

The definition of the term "market" in the regulations provides further guidance as to the requirements that a processor must meet to be eligible for an allotment allocation. The term "market" is defined to mean

"the transfer of title associated with the sale or other disposition of sugar in United States commerce, including the forfeiture of sugar loan collateral under [the loan program], and for any integrated processor and refiner, the movement of raw cane sugar into the refining process. Marketings do not include sales for nondomestic or nonhuman use, or sales of sugar to enable another processor to fulfill an allocation established for such processor."

This definition makes clear that to be eligible a processor's ability to market must be measured by actual sales and transfers of title of loan-eligible sugar produced by the processor. Sales or other dispositions of sugar that are ineligible for the loan program do not constitute marketings for purposes of the marketing allotments. Thus, a processor must meet the requirements of the sugar loan program, in addition to other requirements, before being considered for an allotment allocation.

In addition, the loan program regulations define the term "eligible producer" as owners of the crop both at the time of harvest and the time of delivery to the processor. Producers determined to be ineligible as a result of regulations governing highly erodible land and

wetland conservation, crop insurance, or controlled substance violations are not eligible under the sugar program (7 CFR 1435.102(a)).

OTHER REGULATORY ISSUES

The rule published by the Department of Agriculture to implement the sugar loan and allotment programs was published as a final rule on August 26, 2002. This rule was not subjected to the public comment process during or after its consideration. As such, we would like to take this opportunity to raise for consideration a few related issues regarding the implementation and administration of the flexible marketing allotments for sugar.

Reallocation of cane sugar State allotments.

We are very concerned that the Department has not reassigned the deficit cane sugar allotment allocations among the cane sugar States. Estimates vary, but it is likely that upwards of 100,000 tons of deficit (unused) cane sugar allotment exists in at least 2 cane growing States. At the same time, approximately 200,000 tons of raw cane sugar remain blocked from the market because sugar supply in their State(s) exceeds the available allotment.

The preamble to the sugar program implementing regulations points out that the “2002 Act instructs CCC to periodically determine whether a processor has more allocation than sugar supply and then reassign the deficit according to a very specific hierarchy.” We agree that both the statute and the implementing regulations require this periodic review and reassignments.

However, we are concerned that the Department has administratively determined to delay the reassignment of cane sugar allocations unnecessarily. Again, the preamble to the sugar implementing regulations provides that

“...CCC can limit these sales [of allocations] by reducing the allocation of the processor buying over-allocation sugar. CCC will permit these transactions until May 1 of each crop year, which is expected to leave enough time in the crop year to permit CCC to reassign the unused allocation. ... These sales are not permitted between cane processors in different States.”

The prevention of the reassignment of unused cane allocation to other cane States until May 1 of each crop year has been imposed administratively. It is not contemplated or required by the statute. In the current market situation for cane sugar, the imposition of this trigger date threatens to lead to further increases in the Overall Allotment Quantity for sugar marketing allotments and even to an increase in the amount of sugar imported into the United States under the Tariff Rate Quota for sugar.

We are strongly of the opinion that it is not appropriate to manage the sugar program in a manner that authorizes an increase in the imports of foreign sugar into the United States while U.S. sugar producers sit on warehouses filled with U.S. sugar that can be marketed within the program's Overall Allotment Quantity (OAQ).

We urge the Department to review this issue in light of the unique circumstances facing the industry, and to reassign the cane sugar deficits as soon as possible. In order to prevent the substitution of foreign sugar for U.S. sugar that can be marketed under the OAQ, these reassignments must be made well before the end of March 2003.

Allocation of the Talisman processing facility allocation.

We are disappointed that to date the Department has not distributed the allocation for the Talisman processing facility as required by the statute and implementing regulations. The statute requires that the Talisman allocation be distributed among Florida sugarcane processors according to the agreements between the cane processors and the Secretary of the Interior dated March 25, and March 26, 1999. The agreements between the Florida industry and the Department of Interior all reference lands to be transferred or exchanged between the parties; thus the Talisman allotment should be divided in accordance with how the Talisman lands were so allocated in the agreements referred to. The land exchange documents do not reference the crops grown on the lands so referenced, and any attempt to divide the base Talisman allotment based upon where sugar grown on the former Talisman lands is currently being processed would have no statutory or legal basis.

We urge the Department to revisit this issue as soon as possible and to conform the Florida processor allocations to the statutory requirement. Conforming these allocations to the law will immediately release additional supplies of "blocked" sugar to the market.

"New entrants" cannot remain "new" indefinitely.

Upon reviewing the regulations, we are concerned with the apparent presumption in the regulations that new entrant processors and new entrant States are somehow granted permanent status as "new" entrants. This treatment is not consistent with the authorizing statute.

For example, the statute defines a "mainland State" as any State other than an "offshore" sugarcane-producing State (section 359a(1)). This contrasts with the regulation's de facto definition of a new entrant State as any State other than Hawaii, Puerto Rico, Florida, Louisiana, or Texas. This definitional difference is a serious departure from the statute with potentially serious adverse consequences for existing sugar producers.

The statute contemplates that following the crop year for which a State is granted an initial allocation of allotment, the State will no longer be considered a "new entrant" eligible for unlimited allotment allocations. Once the State becomes a sugarcane-

producing State within the mainland of the United States, it shall be treated as a “mainland State”, consistent with the statute’s definitions.

In addition, allowing a “new entrant State” to maintain its “new” status indefinitely runs contrary to common sense, and will allow an endless string of new entrant processors to petition the Department for allocations of allotment in the State. As the regulations are drafted, the Department could transfer unlimited amounts of allotment from the three mainland States named in the regulations (not the statute) to even a single “new entrant” State. Such a wholesale, unlimited transfer of allotment from existing cane-producing States to new entrants is not consistent with or contemplated by the statute.

The ramifications of the regulations’ definitional departure from the statute are very far-reaching, and potentially very damaging to existing cane sugar producers. We urge the Department to review this issue carefully, and to make the amendments necessary to bring the regulations into conformity with the governing statute.

Thank you again for convening this important hearing. I am available to answer any questions that you may have.

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