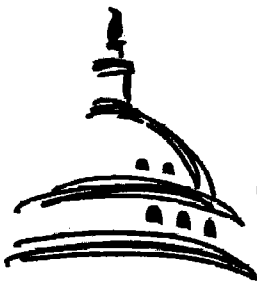


# CRS Report for Congress

## Sugar Policy and the 2008 Farm Bill

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**Congressional  
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# Sugar Policy and the 2008 Farm Bill

## Summary

Congress reauthorized the sugar program with some changes in the Food, Conservation, and Energy Act of 2008 (P.L. 110-246, the 2008 farm bill). It is designed to guarantee the price received by sugar crop growers and processors and intended to operate at “no cost” to the U.S. Treasury. To accomplish this, the U.S. Department of Agriculture (USDA) limits the amount of sugar that processors can sell domestically under “marketing allotments” and restricts imports. At the same time, USDA seeks to ensure that supplies of sugar are adequate to meet domestic demand. “No cost” is achieved if USDA applies these tools in a way that maintains market prices above minimum price support levels. Should prices fall, processors who take out loans have the right to hand over as payment sugar that had earlier been pledged as collateral. Such a step results in program costs.

Effective January 1, 2008, sugar imports from Mexico no longer are restricted under the rules of the North American Free Trade Agreement. Additional imports are allowed entry under other free trade agreements. Both the Congressional Budget Office (CBO) and USDA had projected that, if the sugar program were to continue without change, additional imports would bring prices down below support levels and make it attractive for processors to default on price support loans. With loan defaults representing a cost, USDA would not be able to operate a no-cost program.

To address any U.S. sugar surplus caused by imports, the farm bill conference agreement mandates a sugar-for-ethanol program. USDA is now required to purchase as much U.S.-produced sugar as necessary to maintain market prices above support levels, to be sold to bioenergy producers for processing into ethanol. Funding is open-ended for this program. Other provisions increase the minimum guaranteed prices for raw sugar and refined beet sugar by 4% to 5%, mandate an 85% market share for the U.S. sugar production sector, and remove certain discretionary authority that USDA exercises to administer import quotas. Though CBO scores some savings with the ethanol program, sugar program provisions are projected to cost about \$650 million over five years and just over \$1.2 billion over 10 years.

The final sugar provisions reflect the proposals presented to the House and Senate Agriculture Committees by producers of sugar beets and sugarcane and the processors of these crops. They favored continuing the structure of the current sugar price support program but sought changes to enhance their position in the U.S. marketplace. Their sugar-for-ethanol provisions ensure that the prospect of imports adding to U.S. sugar supplies under any future trade agreements will not undermine the program’s price guarantee and the sugar industry’s market share. Food and beverage manufacturers that use sugar oppose the new program’s provisions, arguing that costs to consumers will increase and that new requirements will restrict the flow of sugar for food use in the domestic market. The Bush Administration opposed these provisions, with the President identifying them as one reason why he vetoed the farm bill.

This report will be updated to reflect key developments.

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For more information, please see the following CRS product:

CRS Report RL33541, *Background on Sugar Policy Issues*, by Remy Jurenas.

# Sugar Policy and the 2008 Farm Bill

## Recent Developments

On June 24, 2008, the State of Florida struck a tentative deal to purchase U.S. Sugar Corporation for \$1.75 billion and turn its sugarcane acreage into water reservoirs. The aim is to facilitate water flow from Lake Okeechobee as part of an environmental project to restore the Everglades. This company accounts for about 9% of U.S. sugar production, and is one of three sugar processing firms in Florida. Under the deal, the company will operate for at least another six years, before its facilities and land are acquired by the state. While this development will have no impact on how the new sugar program provisions are administered, it can be expected to affect the outlook for what other affected sugar interests and policy makers seek in future U.S. sugar policy when Congress considers the next farm bill.

On June 20, spokesmen for the American Sugar Alliance (which represents producers of sugar crops and firms that process them) in an interview welcomed provisions in the enacted 2008 farm bill that create the sugar-to-ethanol program. They pointed out that this “new market-balancing mechanism” will be used only when imports oversupply the U.S. market, and in particular would help address the uncertainty of sugar imports from Mexico.<sup>1</sup>

On June 18, the House and the Senate overrode President Bush’s second veto of the 2008 farm bill (H.R. 6124). With these steps, this bill, which authorizes sugar program provisions and the new sugar-to-ethanol program for five years, became law (P.L. 110-246). Program provisions will take effect on October 1, 2008.

On May 15, the Sugar Policy Alliance (a coalition of food and beverage manufacturers that use sugar, and public interest, consumer, and taxpayer groups) stated that lawmakers “missed an opportunity to reform U.S. sugar policy” in passing the farm bill conference report. It noted that the loan rate increases will lead to surplus production (the problem the new program is intended to solve); that the 85% market share guaranteed for U.S. growers “will potentially violate U.S. trade obligations” and undermine the U.S. Department of Agriculture’s (USDA’s) ability to manage the program effectively; and that the sugar-for-ethanol program will be a “costly new measure [that] requires the government to give away taxpayer dollars.”<sup>2</sup>

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<sup>1</sup> Bureau of National Affairs, *International Trade Daily*, “Sugar Industry Officials Welcome Farm Bill Provisions,” June 23, 2008.

<sup>2</sup> Sugar Policy Alliance, “Farm Bill Jeopardizes American Industries, Workers and Consumers, U.S. Sugar Policy Falls Short,” May 15, 2008, at [<http://sweetenerusers.org/051508.pdf>].

## Overview of Sugar Program

The sugar program is designed to guarantee the minimum price received by growers of sugarcane and sugar beets, and by the firms (raw sugar mills and beet refiners) that process these crops into sugar. To accomplish this, the USDA limits the amount of sugar that processors can sell domestically under “marketing allotments” and restricts imports. USDA is required to operate the sugar program on a “no-cost” basis. This means USDA must regulate the U.S. sugar supply using allotments, import quotas, and related authorities so that domestic market prices do not fall below guaranteed minimum price levels. These are set out in law as specified loan rates, which serve as the basis from which USDA derives effective support levels. If the market price is below the support level when a sugar price support loan comes due, its “non-recourse” feature means a processor can exercise the legal right to forfeit, or hand over, sugar offered to USDA as collateral for the loan in fulfillment of its repayment obligation. This report focuses on the issues raised by the sugar program provisions in the House and Senate farm bills and floor amendments.

See **Appendix A** for a side-by-side comparison of the sugar provisions in the enacted 2008 farm bill with previous law and the House and Senate farm bill provisions. For background information, see CRS Report RL33541, *Background on Sugar Policy Issues*.

## Issues in Farm Bill Debate

Consideration of future U.S. sugar policy in debating the 2008 farm bill revolved primarily around four issues. These were raising the level of minimum price guarantees to be made available to processors, how to use two tools to manage U.S. sugar supply, authorizing any sugar surplus to be used as a feedstock for ethanol, and accounting for projected program costs. Though industrial users of sugar in food and beverage products initially explored converting the sugar program to operate similar to the programs in place for the major grains, oilseeds and cotton, this policy option did not receive further attention.

### Level of Sugar Price Support

USDA is required to extend price support loans to sugar processors that meet certain conditions on passing program benefits to the farmers that supply them with sugar beets or sugarcane. These loans are made at statutorily set loan rates,<sup>3</sup> and account for most of the effective support level made available to producers and processors. USDA is required to use its other tools to protect this price guarantee.<sup>4</sup>

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<sup>3</sup> For sugar, the loan rate is the price per pound at which the Commodity Credit Corporation (CCC) — USDA’s financing arm — extends nonrecourse loans to processors. This short term financing at below market interest rates enables processors to hold their commodities for later sale.

<sup>4</sup> The loan rates alone do not serve as the intended price guarantee, or floor price, for sugar.  
(continued...)

Loan rates for raw cane sugar have not changed since 1985; for refined beet sugar, since 1992. These minimum prices have guaranteed producers of sugar crops and the processors that convert these crops into sugar, a price that since the early 1980s has ranged from two to four times the price of sugar traded in the world marketplace.

The farm bill conference agreement would increase sugar loan rates by 4% to 5% by 2011. Conferees split the difference between the House- and Senate-proposed rate increases and adopted the Senate approach that proposed to increase rates in stages each year. The loan rate for raw cane sugar would rise in quarter-cent increments from the current 18.0¢ per pound to 18.75¢/lb., beginning with the 2009 sugarcane crop. The refined beet sugar loan rate would similarly increase in stages, from the current 22.9¢ per pound to 24.1¢/lb in FY2011.<sup>5</sup>

Growers and processors had initially sought a one cent increase in the raw cane sugar loan rate (with a corresponding increase in the refined beet sugar rate), and had acknowledged their satisfaction with receiving half of their request in the House-passed farm bill. They argued that the increase in the loan rate is needed to cover increased production costs, particularly energy inputs. Sugar users countered that the House-proposed higher loan rates would increase costs to taxpayers by an additional \$100 million annually. They also noted that while the bill's ethanol provisions (see "Sugar for Ethanol" below) "are supposedly designed to deal with surpluses," the loan rate increase "can only encourage *higher* surplus production."<sup>6</sup> The Bush Administration, in its statement of administration policy on the House and Senate farm bills, opposed the increase in the loan rates for sugar.

## Controlling Sugar Supply to Protect Sugar Prices

The sugar program uses two tools — import quotas and marketing allotments — to ensure that producers and processors receive price support benefits. By regulating the amount of foreign sugar allowed to enter and the quantity of sugar that processors can sell, USDA can for the most part keep market prices above effective support levels, meet the no-cost objective, and ensure that domestic sugar demand is met. If successful, the likelihood that USDA acquires sugar due to loan forfeitures is remote.

**Import Quotas.** The United States must import sugar to cover demand that the U.S. sugar production sector cannot supply. However, USDA restricts the quantity of foreign sugar allowed to enter for refining and/or sale to manufacturers

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<sup>4</sup> (...continued)

In practice, USDA sets marketing allotments and import quota levels in order to support raw cane sugar and refined beet sugar at slightly higher price levels. Each price level takes into account the loan rate, interest paid on a price support loan, transportation costs (for raw sugar), certain marketing costs (for beet sugar), and discounts. These are frequently referred to as "loan forfeiture levels" or the level of "effective" price support.

<sup>5</sup> The loan rate for refined beet sugar would reflect the requirement that it be set each year equal to 128.5% of that year's raw cane sugar's loan rate, beginning in 2009.

<sup>6</sup> Letter to Members of Congress, from food and beverage companies and trade associations, and public interest groups, July 13, 2007.

for domestic food and beverage use. Quotas are used to ensure that the quantity that enters does not depress the domestic market price to below support levels. Quota amounts are laid out in U.S. market access commitments made under World Trade Organization (WTO) rules and under bilateral free trade agreements (FTAs).

The sugar program authorized by the 2002 farm bill accommodated, or made room for, imports of up to 1.532 million tons each year. This import level is one of the four factors that USDA has used to establish the national sugar allotment (called the “overall allotment quantity”), and reflected U.S. trade commitments under two trade agreements in effect when the 2002 program was authorized (**Table 1**).

**Table 1. Annual U.S. Sugar Import Commitments  
When the 2002 Farm Bill Was Enacted**

	<i>short tons</i>
World Trade Organization Quota (minimum)	1,256,000
North American Free Trade Agreement (NAFTA) — Mexico Quota (maximum) <sup>a</sup>	276,000
<b>Total</b>	<b>1,532,000</b>

a. Applied only through the end of calendar year 2007.

Since January 1, 2008, however, U.S. sugar imports from Mexico are no longer restricted. Under NAFTA, Mexico no longer faces any tariff or quantitative limit on the amount of sugar exported to the U.S. market. With this opening, though, imports could fluctuate from year to year for various reasons. First, the amount of Mexican sugar exported to the U.S. market will depend largely upon the extent that U.S. exports of historically cheaper high-fructose corn syrup (HFCS) displace Mexican consumption of Mexican-produced sugar. Surplus Mexican sugar, in turn, would likely move north to the United States.<sup>7</sup> Second, Mexico’s sugar output, though trending upward, does vary from year to year, depending upon weather and growing conditions. Mexican government policy also is to hold three months worth of sugar stocks in reserve and to allow sugar imports when needed to meet demand and lower prices.<sup>8</sup> Third, Mexican sugar prices in recent years have for the most part been higher than U.S. sugar prices. To the extent that this occurs, the incentive for a Mexican sugar mill to export sugar north in search of a better price is reduced. Fourth, U.S. buyers’ concerns about the quality of Mexican sugar may limit the amount that actually flows north in the next few years.

<sup>7</sup> However, the recent increase in U.S. HFCS prices due to the higher cost of corn — its main input — may reduce its competitiveness against Mexican-priced sugar. To the extent this price difference narrows, the incentive for Mexican bottlers of soft drinks to shift to HFCS is lowered.

<sup>8</sup> U.S. sugar processors also will be free to export sugar to Mexico to take advantage of the occasional higher prices there.

Also, the United States has committed under other existing and pending bilateral FTAs to allow for additional sugar imports.<sup>9</sup> Such imports in 2013, the fifth year of the sugar program authorized by the 2008 farm bill, could total from about 420,000 tons to 1.215 million tons *above* existing WTO and NAFTA/Mexico trade commitments. The wide range reflects two varying assumptions made to estimate by how much HFCS use in Mexico might displace sugar consumption in Mexico and create a surplus available for export to the U.S. market.

**Legislation.** The sugar program provisions in the farm bill conference report do not directly address the issue of additional sugar imports. Instead, a new sugar-for-ethanol program is authorized to handle the price-related impact of such imports (Section 9001 in the energy title; see “Sugar for Ethanol” and “Program Costs” below). However, other provisions prescribe how USDA must now administer import quotas. To cover shortfalls (because of hurricanes or other disastrous events) in what domestic sugar processors can sell under allotments, USDA is directed to ensure that most imports enter in the form of raw cane sugar rather than refined sugar. While historically most permitted imports have entered in raw form, USDA allowed large quantities of refined sugar to enter after the late 2005 hurricanes significantly affected the ability of cane refineries in Louisiana and Florida to process raw sugar. This policy change is intended to ensure that cane refineries (which process raw sugar into refined sugar) can more fully use their operating capacity. Unlike five years ago when the Congress considered the last farm bill, most cane refineries are now a key part of vertically integrated operations owned by raw sugar processors and/or sugarcane producers. Also, limiting the entry of refined sugar enhances the position of the domestic beet sector to increase their sales of refined sugar.

Conferees, though, did not adopt provisions found only in the House-passed bill that would have directed USDA to regulate when and how much raw cane sugar imports are allowed to be shipped to U.S. cane refineries. While USDA announced shipping patterns in FY2003-FY2005, the impact of the hurricanes led to a decision not to follow this long-standing practice in FY2006-FY2008. USDA justified removing these restrictions because of “changes occurring over time in the domestic marketing of cane sugar.” The House-proposed provisions could be viewed as intending to increase the transaction costs for countries that export larger amounts of sugar to the U.S. market and giving a slight competitive edge to domestic processors with respect to buyers. Food and beverage firms opposed “micro-managing” the timing of imports, noting that the application of such rules will limit the ability of cane refiners to efficiently use their processing capacity and could lead to serious shortfalls at times in the amount of sugar supplied to the market.<sup>10</sup> In commenting on the House bill, the Bush Administration expressed concern over requiring shipping patterns for quota sugar imports. Also, several countries eligible to ship sugar to the U.S. market expressed concern that the proposed regulation of the flow of imports would run counter to U.S. trade commitments. Because of the concern

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<sup>9</sup> Most of the sugar access provisions in the Dominican Republic-Central American FTA (DR-CAFTA) already are in effect. Congress has yet to consider the FTAs with Panama and Colombia, which would grant additional access for their sugar to the U.S. market.

<sup>10</sup> Letter to Members of Congress, July 13, 2007.

expressed that prescribing how sugar import shipping patterns should be administered would open up the United States to challenges by sugar exporting countries in the WTO, these provisions were dropped in conference.<sup>11</sup>

**Marketing Allotments.** In the 2002 farm bill, the domestic production sector accepted mandatory limits on the amount of sugar that processors can sell — known as marketing allotments — in return for the assurance of price protection. It viewed allotments as a way to try to capture any growth in U.S. sugar demand, and assumed that the then-U.S. sugar import quota commitments would continue without change (see “Import Quotas” above). The statute, however, stipulated that if (1) USDA estimates imports will be above 1.532 million short tons, and (2) that such imports would lead USDA to reduce the amount of domestic sugar that U.S. processors can sell, then USDA must suspend marketing allotments. Suspending allotments because of additional imports raises the prospect of downward pressure on market prices if most U.S. sugar demand is already met. If the additional imports were to cause the price to fall below support levels, forfeitures would occur and USDA would be unable to meet the no-cost requirement. Including the allotment suspension provision was designed to ensure that USDA not lose control over managing U.S. sugar supplies for fear of the consequences that could be unleashed (i.e., demonstrate its inability to implement congressional policy).

**Legislation.** Implementation of the 2002 farm bill’s marketing allotment authority resulted in the U.S. sugar production sector’s share of domestic food consumption ranging from a low of 73% in FY2006 to a high of 89% in FY2004. Concerned that their market share would decline as sugar imports increase under various trade agreements (see “Import Quotas” above), sugar producers and processors decided to pursue a different approach, which farm bill conferees adopted. It guarantees that the domestic production sector always benefits from a minimum 85% share of the U.S. sugar-for-food market. USDA would be required to announce an “overall allotment quantity” — the amount of sugar that all processors combined can sell — that represents at least 85% of estimated sugar consumption. This is intended to address the sector’s objective that imports not displace the ability of U.S. sugar processors to sell more of their output in each successive year, to the extent that U.S. demand for sugar grows.

## Sugar for Ethanol

**Background.** Sugar producers and processors have had an ongoing interest in exploring the potential for using sugar crops and processed sugar as a feedstock to produce ethanol (a gasoline additive). In the 2002-2003 period, they encouraged USDA to explore selling forfeited sugar stocks to corn-based ethanol processors. A few ethanol producers experimented by adding sugar to speed up the ethanol fermentation process, but the results appear to have been disappointing.

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<sup>11</sup> The World Trade Organization administers trade dispute settle procedures whereby a country can file a case against another alleging that the latter operates a program or policy that runs counter to WTO rules. In this context, the prospect arose that a sugar exporting country might allege that the proposed shipping patterns provision were discriminatory or trade distorting.

