IMPERIAL SUGAR COMPANY

TESTIMONY OF

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RE: IMPLEMENTATION OF THE SUGAR TITLE OF THE FARM SECURITY AND RURAL INVESTMENT ACT OF 2002

BEFORE THE SENATE COMMITTEE ON AGRICULTURE, NUTRITION & FORESTRY

May 10, 2005

My name is Robert A. Peiser. I am the President and CEO of Imperial Sugar Company which is headquartered in Sugar Land, Texas and operates two major cane refineries located in Savannah, Georgia and Gramercy, Louisiana. I am pleased to offer this testimony to the Committee on behalf of Imperial's 809 employees because the subject matter affects those employees very substantially every day of their working lives.

From the outset, let me say clearly and unambiguously that the US sugar program provides valuable benefits for the domestic industry and provides a more stable structure under which to conduct business than would be the case without the program. Benefits accrue to many parties, not just the domestic growers, and some level of protection from unlimited imports from the world market seems prudent. This said, there are several issues that face the independent cane refiner sector that may not be well handled by the current policy and need the Committee's attention, most notably issues relating to raw cane sugar availability and relative support prices. My testimony addresses these and other concerns below.

I. Overview of Domestic Sugar Industry in a Changing World Market: Key Issues

Independent Cane Refiners Have a Unique Role: Traditionally, the Committee has been very familiar with the positions expressed by the grower segment of the sugar industry and the sugar users, including manufacturers of food products who use large volumes of refined sugar in their products that they provide to the wholesale trade and to the retail consuming public. Cane refiners sit between those two entities in the industry and provide a critical and necessary service to both. We are the market for the sugar growers' raw sugar, and in turn the sugar users are our customers for the refined sugar products we make. While occupying a low profile compared to the attention focused on the growers and sugar users, cane refiners serve a necessary and critical role in the domestic sugar industry when viewed broadly; without cane refiners there simply is no domestic sugar industry as we know it today. And as you set public policy in this area, the domestic sugar program needs to recognize the critical role and contributions of cane refiners or the program is destined to fail.

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Imperial is an independent refiner—meaning that we do not grow the raw cane sugar or sugar beets that we refine. Other than Imperial, and a couple of relatively small processing facilities, the rest of the domestic sugar industry has become partially or fully vertically integrated, as for-profit or cooperative sugar growers purchased previously independent refining and processing assets. As a result, the vertically integrated grower-refiners supply themselves with the raw cane sugar or sugar beets grown by their integrated affiliates. In contrast, Imperial totally depends on our ability to purchase raw cane sugar from unaffiliated third parties, which include both US and foreign growers.

Independent cane refiners like Imperial provide a critically important relief valve for periods of short supply in the domestic marketplace. We are able to acquire raw sugar from foreign sources and convert it into refined products packed and delivered in a form acceptable to US buyers during periods of domestic crop shortfalls. As critical as this market function is, the Committee should observe that over the last two decades US sugar policy has unintentionally, but nonetheless effectively, undercut the independent cane refining sector. Specifically, domestic sugar policy has encouraged the expansion of domestic crops at the expense of imports. The ensuing decline in import supply from the mid 1980s to the present time has caused the closure of 15 cane refineries, leaving only eight remaining today.

The cost of this very real adverse impact of US sugar policy has been significant. The many now-closed refineries provided high paying jobs with benefits to urban markets, especially in coastal cities such a Brooklyn, Boston and Philadelphia. While the goal of the policy has been to protect domestic growers to a reasonable degree, the unanticipated result of that policy has been that those benefits to growers have come at the expense of cane refiners. Imperial believes that the Agriculture Committee should be highly concerned with preserving US cane refining jobs—especially so when the jobs in jeopardy are in the ***independent*** cane refining sector which provides strong competition to the integrated refiners who make their money either as growers, refiners or both.

The disruptions in the market for sugar in the Fall of 2005 caused by the temporary closure of the Domino facility in Chalmette after Hurricane Katrina illustrate that the relief valve provided by cane sugar refiners is currently in a finely balanced state and that even a temporary reduction in cane refiner capacity may lead to periods of shortage and higher than normal pricing. Imported refined sugar can help to temper this situation, but differences in quality, packaging and transport of these foreign supplies limit the ability of many buyers to utilize these products on a short term basis. Domestic cane refiners provide the quickest source of additional sugar of the quality and form demanded by US buyers. It is our considered opinion that current and future policy should seek to preserve the vital function of the domestic cane refining sector in the US sugar industry and ensure that programs are administered in a manner that allows cane refiners to operate at levels of economic capacity utilization and with competitive profitability.

Imperial's Operations in Savannah, GA and Gramercy, LA: Imperial views itself as an important element of the agriculture industry in this country. Imperial's two cane refineries produce approximately 14 percent of the nation's refined sugar needs and we provide a full range of refined sugar products to the retail, food service and industrial markets.

Our largest facility—the cane refinery located in the port of Savannah, GA, which represents about 60 percent of our entire production capacity—has historically refined large volumes of US-grown raw sugar, particularly from Florida growers. But as the Florida industry has vertically integrated over the last several years and expanded refining capacity locally there, Imperial has lost nearly all previous access to that traditional source of raw sugar. **We are now confronted with the reality that in 2006 and for the indefinite future, our Savannah refinery is almost wholly dependent upon foreign raw sugar for its operations.**

The Savannah refinery is one of the largest and most efficient in the nation. By itself, the Savannah refinery represents about 9 percent of the nation's sugar refining capacity. Its loss or even a decline in productivity would have significant adverse impacts on the price and supply dynamics of the US sugar market. We directly employ about 374 people at Savannah, and there are many more jobs in the Savannah economy dependent upon the vitality of our refinery, including local small businesses, stevedores, dockworkers, truck drivers and many others in the service industry either serving that facility or the approximately 60 ships that each year bring raw sugar to our plant, or delivering our refined product to our customers.

Imperial buys all the US grown raw cane sugar we can. In fact, in normal years, almost 100 percent of the raw cane sugar that we refine at our Gramercy facility is grown by US farmers. We are proud of our long-term association with our domestic growers and given their importance to the Gramercy refinery we have a strong interest in having a financially stable and vibrant domestic sugar producing community. No one should accuse Imperial of being anti-US grower. As some of the Louisiana growers who currently supply our plant are considering their own vertical integration our attention is again focused on obtaining an alternate supply source to support that facility and its 279 employees. We do not oppose the right of growers to invest in the business and vertically integrate.

We do object to the restrictions of the policy (marketing allotments and import limitations) that make it difficult or impossible for an independent refiner to obtain replacement supplies and compete on a level playing field. As imports are limited by quotas and domestic supplies are limited by marketing allotments for the cane and beet sectors, it is possible for vertical integration to occur with the knowledge that after the integration the current domestic sugar program will starve non-vertically integrated competitors (i.e. independent refiners) of supply which could lead to the closure of other cane refineries. This is a serious disadvantage and to the extent that this part of the US sugar program aids and abets such a dynamic it should be changed. In the last three years we have seen the closure of over 1 million tons of refining capacity for what appears to be such raw sugar access related issues. We at Imperial must stabilize our supply against this contingency and will be taking action to acquire sugar from offshore sources, but we are very concerned that the program may limit our ability to adequately complete this important task.

Lessons of CAFTA Must Be Appreciated: Given our now nearly total dependency on foreign raw sugar at Savannah, Imperial's support for CAFTA last year was understandable as a part of our search for sufficient reliable sources of raw sugar. We hasten to note our deep appreciation for the skillful and judicious manner in which the Members of this Committee, under the leadership of Chairman Chambliss, negotiated a series of commitments from USDA that lead to the enactment of CAFTA last summer. The additional 110,000 tons of sugar which CAFTA permits to enter the US is insignificant relative to the total size of the US sugar market in general—representing about 1 percent of the over 10 million ton market. The addition of that incremental supply to the marketplace is important to Imperial's ability to maintain Savannah's operations, fully serve our customers, and continue full employment for our direct employees at the refinery, as well as the many jobs dependent on us in the port of Savannah and the broader local economy.

The Administration has announced it is negotiating additional FTA's with other nations, many of whom would desire access to the US sugar market. Imperial remains supportive of additional access of raw sugar to the US marketplace. **Imperial would also support an increase in available supply from domestic raw cane sugar producers that would result in additional supply to our facilities.** The ability to increase available domestic supply is hamstrung by the overall cane sector allotment levels provided in the current sugar policy. Imperial would support an increase in the cane share of the overall allotment quantity to facilitate our access to more domestic cane production.

The Committee should further observe that during the CAFTA debate Imperial and other supporters of CAFTA reliably estimated that in FY-06 the US sugar market needed at least an additional 700,000 tons of sugar beyond the current 1.250 million ton WTO-mandated minimum level of imports to meet projected market needs. All observers now acknowledge those estimates proved completely correct. As such, the 110,000 tons from CAFTA fades to insignificance in the real world we actually have experienced in 2006. I raise this CAFTA experience because it illustrates very vividly the Committee's obligation while reviewing the state of the current Farm Bill's sugar program to carefully separate fact from rhetoric if we are going to seriously consider proposals for what to do in the upcoming Farm Bill reauthorization debate. Time has long passed where we can afford to allow public policy in this area to be premised on misperceptions and outdated caricatures of the world which do not correspond to the economic reality of the increasingly integrated international sugar market.

II. The 2002 Farm Bill's Sugar Program: What Works? What Does Not Work?

We view the essential mission of today's hearing to illustrate what works and what does not work in the sugar program established by the 2002 Farm Bill. We applaud the Committee in its effort to fully explore these questions before entertaining proposals with regard to what changes may be appropriate or may be needed in the next Farm Bill reauthorization.

A. What does work in the current USDA sugar program:

USDA Professionals: The first thing that must be said about what is good about the current sugar program is the enormously talented and dedicated professionals administering that program. Whatever you might says about the wisdom of any particular provision of the program they were handed by the 2002 Farm Bill, the USDA's personnel has performed admirably and effectively under a virtual constant crisis scenario to use all the tools Congress gave them to make that program work for the range of interested parties and the public interest in general. The USDA has done a great job in working through a difficult maze of political and market problems in dealing with the sugar program. They have struggled, especially in the past year, to rise to unprecedented challenges caused by natural disasters, changing international treaties and evolving market forces to effectuate Congress's intent to adequately supply the US market without net cost to the US taxpayer. This Committee ought to know the near heroic lengths to which the USDA sugar program professionals have gone to meet these challenges. Imperial certainly appreciates their work as do many others in our sugar sector.

Programmatic Elements: As for specific programmatic elements that appear to be working, there are several which we would bring to your attention:

- **Marketing Allotments**: We conclude that marketing allotments have generally worked in controlling domestic over-production although it comes at a high administrative cost. This is not to say that these marketing allotments work for cane refiners however (indeed, we also include them in our discussion of problem areas below). In fact, they often frustrate our access to supplies of sugar on an efficient basis, forcing us to jump through many hoops that would not exist in a market free of such supply controls. Our observation also is that administering the marketing allotment provisions entails very substantial dedication of USDA's personnel resources. Perhaps this is not surprising in that the marketing allotments are inherently an artificially imposed deviation from the efficiency of the unregulated market place where producers would make their own decisions as to how much to plant and sell.

- **Re-Export Program**: The re-export program remains a bright spot in sugar policy. With the re-export program, cane refiners can secure incremental business and we obtain the flexibility of sourcing non-quota sugar that allows us to solve many short term supply issues that would otherwise require regulatory solutions. We applaud the USDA for flexibly administering this program. In the current year the USDA has allowed an extension of the time allowed between importation of raw sugar and the subsequent re-export of refined products. We urge the Department to make this change permanent and to consider an increase in the size of the licenses granted to refiners. The Department has been working for some time on an updating of the regulations surrounding this program and we urge Department to complete this project and promulgate revised rules.

- **Removal of Shipping Pattern Restrictions**: When quotas were large and domestic crops traded freely (before vertical integration) quota arrivals from the largest shippers were limited so that offshore sugar would not flood the market and prevent the local crop from being marketed at harvest. Last year, the USDA wisely removed shipping patterns from the administration of the quota and we urge them to make this a permanent practice. This would allow offshore sugars to flow to the US in enough quantity to satisfy the demands of independent refiners who do not have domestic production early in the year. The majority of the foreign suppliers in the current quota have crop cycles that generate shipments to the US from December onwards, so we need to remove limits from those who can ship during the first 3 or 4 months of the crop year in order to ensure adequacy of supply in that busy, multi-month holiday season (the period leading up to and including Halloween, Thanksgiving and Christmas).

- **Organic Sugar**: We thank the USDA for aggressively expanding the access to the US for organic sugars. This market is growing at a very rapid rate and it is important for all in the sugar industry to support access to our markets for these sugars to ensure that demands are met. US sugar policy must encourage the market responsiveness of the domestic sugar program to the growing consumer demand for the slate of organically grown sugar products, ***none of which are grown in this country.***

B. What is not working (or not working well enough):

There are several important provisions of the sugar program that are not working or not working well enough—perhaps because they are either ill-conceived conceptually or because they are not efficient tools to deal with realities in the market place.

- **Support Prices**: The difference between the raw sugar support and the white sugar support is too narrow to allow independent processors to survive with current energy prices. Refining raw cane sugar is an energy intensive business and the rising cost of natural gas, coal, fuel oil and electricity have dramatically increased the conversion costs facing the industry over the last several years. The difference between the white sugar support price and the raw sugar support price embodied in the price support loan program is no longer wide enough to allow profitable operation of refineries when both markets are at the support level. This differential needs to be widened in future legislation if cane refiners are to survive at the low end of the sugar cycle.

- **Marketing Allotments**: Current TRQ imports plus imports from Mexico and FTA's will likely threaten the allocation import trigger at 1.532 million tons and this may have to be revised in order to preserve marketing allotments. As marketing allotments are a useful (although flawed) policy tool, the Committee should consider removing or raising this limitation in the next legislation.

- **TRQ Imports**: The current Tariff Rate Quota (TRQ) allocation among the world's nations is archaic and hinders refiners from developing an efficient and flexible supply chain with preferred high quality raw sugar suppliers. The base period for determining the country allocations of the US quota was in the late 1970s and early 1980s. This was a period of extremely high sugar prices and the list of suppliers that created the current allocation was distorted as a result. Since that time some of the quota holders have ceased being net exporters, some no longer produce sugar, and others do not have production large enough to satisfy increased demands from the US without importing for their local markets. We ask the Committee to urge our trade negotiators to work diligently to change the allocations of sugar applicable to the quota to a more market responsive system that would allow refiners to source sugar more flexibly from suppliers of high quality raw sugar and to respond to changes in production and export status of quota holding nations.

- **Timing of Announcement of TRQ Each Year**: As the quota can always be presumed to be at least the minimum, it does no harm to make an early announcement of at least the minimum quota. The administrative process has many time consuming components involving the USDA setting a base quota, USTR issuing country allocations and issuing CQE's, and notification of the Certifying Authorities in the quota holding nations. Starting this series of events earlier would jump start a process that often delays the earliest potential arrivals of offshore sugar to the US market. This matters because with so much vertical integration now domestic crops do not flow immediately to market, but are held for shipment throughout the year and those sugars are not available to independent refiners like Imperial. It puts us in the position of being held hostage. Elimination of shipping patterns is also critical in this regard.

- **Import Limitations in General**: The confluence of marketing allocations and TRQ controls in the current program basically allow domestic processors to capture all of the demand increase in the US market. While some FTA's now allow for small growth over time, **the sugar program should allow imports to grow or shrink each year at the same rate as estimated demand increases or decreases.**

- **Information Gathering in a NAFTA environment**: With the prospect of a unified North American market for sugar soon upon us, we at Imperial are concerned about the lack of good publicly available information from Mexican sources about the supply and demand for sugar and sweetener within Mexico. The USDA does an outstanding job of collecting information and disseminating it in the US, but we lack similar information from Mexico. We urge the development of a structured exchange of information, coordinated by the USDA, that would disseminate information from Mexico to the interested public in the US.

Conclusion: On behalf of all our Imperial Sugar Company employees, we thank the Committee for allowing us the opportunity to provide our views on the state of the US sugar program. While this hearing is intended to serve an oversight function as to what is the current status of that program, we look forward to a future opportunity to share our views on what might constitute valuable changes in the US sugar program that should be included in the next Farm Bill in order to make the domestic sugar program serve America's interests even more efficiently and more productively. As is evident from our testimony today, Imperial supports revising the current sugar program in the next Farm bill to address the concerns we have raised. We do not support simply extending the current program without addressing these serious problems since their adverse impact will only increase if not addressed. We look forward to working cooperatively with the growers, processors, refiners and users who make up the domestic sugar industry to come to an agreement on policies that will create a healthy, profitable industry for all interested parties.