CIAB Testimony

My name is Thomas Facer and I am here today to testify in favor of the proposed amendment to the Federal Marketing Order for Tart Cherries. I represent New York State as the lone representative. I have served on the CIAB since its inception either as a board member or alternate board member and have served as Treasurer and currently serve as Chairman.

There is only one stated purposes for the Cherry Marketing Order as published in the Federal Record, which is to increase the value of cherries to growers. The current manner in which diversion credits generated from the on farm destruction of cherries by growers are accounted for does not support the stated purpose of the Marketing Order. Tart cherry crop production has historically been variable due to weather conditions which has lead to highly variable grower pricing and marketing conditions. When the Marketing Order was initially developed and promulgated the economic theory supporting the improvement in grower returns was to control the supply of cherry products marketed into the domestic tart cherry market. By controlling the supply available to the market each year, supply would be stabilized and grower return would be stabilized. The handlers of the tart cherry crop were regulated by restricting the sales a handler could market into the domestic market to the percentage of 'Free' tonnage established by a formula for the entire industry based on crop size, carry over inventory and prior 3 year average industry domestic sales. The handlers had the burden of proof to provide documentation that the 'restricted' volume of cherries a handler handled (handle) was kept out of the domestic market. The primary supply control mechanism used allowed handlers to place product into a 50 million pound reserve inventory to be used during years of low crop production to stabilize supply. These reserve inventories would be released during low crop years and replenished in high crop years, thus stabilizing supply and grower pricing. The marketing order also allowed handlers to obtain 'credits' towards their restriction volume for exporting products outside of North America and to apply for diversion 'credits' for new products or new markets up to 5 million pounds per season, industry wide. The final method allowed to satisfy regulation requirements was for growers to destroy cherries in the orchard and obtain 'grower diversion credits'. Handlers needed to obtain these credits to use to satisfy regulation. The Marketing Order was presented to the industry with several examples showing a stabilization of grower pricing of approximately $.25 per pound and in large crop years a regulation percentage of 25%; the industry adopted the Marketing Order by a significant margin of both growers and handlers.

Since the initial adoption of the order there have been several modifications to 'improve' the order both by formal and informal rule making. Over that same time there

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have been many changes in the consumption patterns of cherry consumers. Unfortunately, since the promulgation of the Marketing Order, regulation has in many years been much higher than the 25% expected and grower returns in those years has been much less than the $.25 anticipated. There are many reasons for the increased regulation percentage that are not relevant to the discussion of this amendment. However, as the regulation percentage increases the use of orchard diversion is discouraged rather than encouraged as originally intended. All regulation of the Marketing Order is at the handler level and handlers have been required to include all orchard diversion certificates received from growers as part of their handle. To this total handle the regulation percentage is assessed. The best way to understand this is to look at an example of what happens as an individual handler utilizes orchard diversion certificates to satisfy regulation requirements. In this example the handler has domestic customers that purchase on an annual basis cherry products that require 10 million pounds of raw cherries to produce. The handler has no export business and has 1 million pounds of qualifying new product activity. The products the handler produces have a shelf life of 18 months. The handler plans to participate in the 50 million pound primary reserve but does not want to participate in the secondary reserve. As you can see in the example, as the crop size increases, the regulation increases and the quantity of grower diversion certificates required for the handler to satisfy regulation requirements increases disproportionate to the regulation increase. Growers will not destroy fruit in the orchards when other processors will accept the fruit, and as a result growers require payment for this destruction. Handlers who have excess export or new product credits also sell those credits to handlers who need them. In this example with a 200 million pound crop (below national consumption) the regulation percentage is 20%. But the handler cannot sell 1.0 million pounds equivalent of its production to customers that expect the product unless the handler covers the regulation requirement in some other manner. With a crop less than national consumption it is not reasonable to destroy cherries in the orchard but if that was the only option the handler had they would be required to destroy 1.2 million pounds to 'free up' 1. million pounds of product. As the crop gets larger in the example the quantity of grower diversions needed rises much quicker than the shortfall in sales opportunity. When the crop reaches 300 million pounds plus the 50 million pound carryover in the example the quantity of grower diversions required to satisfy the 4.4 million pound regulation requirement grows to 9.4 million pounds.

As an example, one of the handlers I work with had the following experience in 2009. The 2009 crop was large and there was carryover from 2008 that resulted in a 68% regulation, leaving only 32% available to sell to their customers. The handler required some growers they deal with to destroy a portion of their fruit in the orchard which they paid the grower $.05 per pound for the fruit destroyed. The grower was paid $.15 per pound for the portion of the crop that was harvested and delivered. The

growers the handler deals with did not have enough fruit to meet the handler's sales need plus destroy the amount of fruit necessary to meet the regulation. This forced the handler to purchase excess credits from other handlers and purchase cherry products they do not market to place into reserve. They were successful in a sealed bid offer to purchase credits for $.20 per pound and were unsuccessful in all attempts less than $.20. If the stated purpose of the Marketing Order is to improve cherry grower returns I suggest this example points out there is a problem with the system.

The proposed amendment addresses the current inequity in the utilization of grower diversion credits by allowing the handler to utilize them on an equal basis with other diversion activities. This will remove the current disincentive to destroy fruit when the regulation requirements are very high due to large crops and/or excessive free carryover from prior years. The entire industry will realize a slightly higher regulation percentage with the amendment but the quantity of tonnage available to be marketed will be the same as it is without the amendment change. Undoubtedly handlers who typically generate excess diversion certificates will oppose the amendment change; I argue the windfall they have realized under the current method of handling grower diversion does not fit the purpose of the marketing order.

With this change I suggest grower returns will improve as was first envisioned with the original implementation of the marketing order. In years when crop size is small to large there is unlikely a need to destroy fruit in the orchard, that does not change with this amendment. However, when there is a very large supply, crop size and/or carryover, some handlers will offer much higher payments to growers to destroy fruit than has been experienced to date with the marketing order for the reasons I have already stated. These payments for destruction will entice growers to destroy more fruit than has been destroyed in the past. In the past the fruit that will now be destroyed was in the secondary reserve pool, this excessive reserve inventory cost the industry carrying costs plus in most cases frozen storage costs plus some market value depression on the free market. These expenses will be saved and market prices will be a bit less depressed, both will lead to higher grower returns. Over time production must be in line with consumption, the industry cannot produce more than is consumed. The change this amendment makes to the marketing order will aid in bringing the production/consumption closer to balance over time and allow growers to realize increased returns.

Current Structure

	#'s	#'s	#'s
National Regulated Crop + Free Carryover Of 50M	200	275	350
InOrchard Destruction	0	10	20
Regulation % (Assuming non regulated areas 10M)	20%	42%	54%
Handler processed #'s	10	10	10
Handler available to sell	8.0	5.8	4.6
Handler's Customer needs			
Domestic	9	9	9
'New' Products	1	1	1
Total			
Shortfall Due to Regulation	1.0	3.2	4.4
Options to satisfy regulation			
Purchase product to place in primary reserve	0.1	0.1	0.1
Grower diversion certificates (Grower Owned)	1.2	5.3	9.4
Purchase Export Credits (Handler owned)	1.0	3.1	4.3
Purchase excess NP Credits (Handler owned)	1.0	3.1	4.3

Amended Structure

	#'s	#'s	#'s
National Regulated Crop + Free Carryover Of 50M	200	275	350
In Orchard Destruction	0	10	30
Regulation % (Assuming non regulated areas 10M)	20%	44%	58%
Handler processed #'s	10	10	10
Handler available to sell	8.0	5.6	4.2
Handler's Customer needs			
Domestic	9	9	9
'New' Products	1	1	1
Total			
Shortfall Due to Regulation	1.0	3.4	4.8
Options to satisfy regulation			
Purchase product to place in primary reserve	0.1	0.1	0.1
Grower diversion certificates (Grower Owned)	1.0	3.3	4.7
Purchase Export Credits (Handler owned)	1.0	3.3	4.7
Purchase excess NP Credits (Handler owned)	1.0	3.3	4.7