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NO TIME TO CRY OVER SPILT MILK: THE EFFECT OF THE EUROPEAN MILK QUOTA REPEAL ON AMERICAN DAIRY FARMERS

Tyler R. Smith†

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I. INTRODUCTION

March 31, 2015, marked the expiration date on the three-decade old milk quota across the European continent. Dairy farmers throughout Europe threw out the caps on their production of milk that had long since spoiled their maximum production abilities. Today the removal of the milk quota is allowing European countries to bolster milk exports to the far reaches of the globe. Asian markets have been flooded by the new outpouring of European dairy. European dairy farmers are reaping the benefits of the milk quota repeal. For American dairies, however, the milk has been spilled at their expense. American dairy exports have seen a drastic decline in the past year.¹ This trend will only continue if certain measures are not taken by American legislators and the President. Furthermore, these changes must be expedited because the American dairy industry is painfully aware that there is no time to cry over spilt milk.

The quota had been put in place by the former European Economic

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1. Alan Levitt, *U.S. Dairy Exports End Five-Year Growth Streak*, U.S. DAIRY EXPORT COUNSEL (Feb. 5, 2016), <http://blog.usdec.org/usdairyexporter/u.s.-dairy-exports-end-five-year-growth-streak> [hereinafter Levitt, *Growth Streak*].

Community in 1984, which placed a limit on the production of dairy products for all European Union members.² The quota, which functioned by taxing any dairy production that exceeded a maximum limit, expired in March of 2015.³ The ramifications of the removal of this cap has had, and will continue to have, a significant impact on farmers in the EU.⁴ However, the impact is not to be restrained to solely the European continent. The worldwide dairy industry is bracing itself for a further surge in European dairy production that will affect both domestic and international milk imports and exports.⁵ Dairy farmers in every corner of the globe will be affected by the repeal of this quota.⁶

The European Union repealed one of the most impactful pieces of legislation currently affecting worldwide agricultural production.⁷ Today, milk is one of the most valued products in the European agriculture market.⁸ Most member states of the European Union have a substantial dairy industry.⁹ The surge in European exports, coupled with a decline in milk demand, has caused American dairy exports to plummet.¹⁰ That being said, American dairy farmers have overtly attempted to increase both domestic dairy production and international dairy

2. Commission Regulation 1371/84, 1984 O.J. (No.132/11) (EC) [hereinafter Commission Regulation 1371/84].

3. *Id.*; INST. FOR PROSPECTIVE TECH. STUDIES, EUROPEAN COMM'N, ECONOMIC IMPACT OF THE ABOLITION OF THE MILK QUOTA REGIME 10 (2009), http://ec.europa.eu/agriculture/analysis/external/milkquota/full_report_en.pdf.

4. Alan Levitt, *Growing European Milk Production Weighing on Markets*, U.S. DAIRY EXPORT COUNCIL (Dec. 22, 2015), <http://blog.usdec.org/usdairyexporter/growing-european-milk-production-weighing-on-markets> [hereinafter Levitt, *Weighing on Markets*]; ECONOMIC IMPACT OF THE ABOLITION OF THE MILK QUOTA REGIME, *supra* note 3, at 10-16; Simon Coveney, *Dairy Sector Readies for Milk Quota Overhaul*, IRISH EXAMINER (Apr. 1, 2014), <http://www.irishexaminer.com/viewpoints/analysis/dairy-sector-readies-for-milk-quota-overhaul-263834.html>; Mark Astley, *Milk Quota Abolition will Create North European 'Production Belt'*, DAIRY REPORTER (Mar. 18, 2014), <http://www.dairyreporter.com/Markets/Milk-quota-abolition-will-create-North-European-production-belt>.

5. See Astley, *supra* note 4; INFORMA ECON., INC., AN INTERNATIONAL COMPARISON OF MILK SUPPLY CONTROL PROGRAMS AND THEIR IMPACTS 8-13 (2010), http://future.aae.wisc.edu/publications/Informa_Supply_Control_Impacts_0910.pdf.

6. Arjun Kharpal, *Why Europe is Crying Over Spilled Milk*, CNBC (Oct. 2, 2013), <http://www.cnbc.com/id/101080564#>.

7. *Id.*

8. *Milk and Milk Products*, EUROPEAN COMM'N, http://ec.europa.eu/agriculture/milk/index_en.htm (last visited Aug. 20, 2016).

9. ECONOMIC IMPACT OF THE ABOLITION OF THE MILK QUOTA REGIME, *supra* note 3, at 1.

10. Levitt, *Growth Streak*, *supra* note 1.

exports, most notably in China.¹¹ If American dairy farmers are to maintain relevance in the global dairy market, much less accomplish their goals of increased exports, they are going to need help from lawmakers in Washington.¹²

Part of this self-examination will include a hard critique of subsidy and taxing programs currently affecting American dairy farmers.¹³ Furthermore, the extent of regulations, particularly federal, need to be compared to their European counterparts.¹⁴ Finally, there is significant room to enhance international trade agreements to adapt and preemptively prepare for increased international trade competition.¹⁵ The author believes the Trans-Pacific Partnership (TPP) trade agreement would prove to be crucial for American dairies.

This analysis will not focus primarily on the merits of quota systems or regulations abroad. Rather, it will concern the current American policies and goals in the dairy industry and how they interact with the current European Quota System. This will be followed by an examination of what can be expected from the repeal of the quota system and potential concerns for American dairy farmers. Finally, the actions American legislators and dairy producers can take to adapt and proactively attack these problems will be addressed—namely, how pursuing the TPP is a necessary step to ameliorate the declining exports for American dairy farmer

II. THE EUROPEAN QUOTA SYSTEM

A. History of the Quota System

In 1984, the European Economic Community (EEC), presently known as the European Union (EU), passed the Dairy Produce Quota Regulations.¹⁶ The new regulation was introduced to the European Community's Common Agricultural Policy (CAP).¹⁷ Since its inception in 1962, CAP has served as the umbrella

11. See Andrew Martin, *America's Got Milk and China Wants It*, BLOOMBERG BUSINESSWEEK (June 5, 2014, 4:04 PM), <http://www.businessweek.com/articles/2014-06-05/china-wants-americas-milk-and-u-dot-s-dot-dairy-exports-benefit>.

12. *Export Profile*, 24 U.S. Dairy Export Council, no. 3, Sept. 2014, at 1, 4, <http://usdec.files.cms-plus.com/PDFs/ExportProfileSept2014.pdf>.

13. See *Policy*, USDA, <http://www.ers.usda.gov/topics/animal-products/dairy/policy.aspx> (last visited Aug. 20, 2016).

14. See *id.*

15. See *Dairy Export Incentive Program (DEIP)*, USDA, <http://apps.fas.usda.gov/excredits/deip/deip-new.asp> (last visited Aug. 20, 2016); see e.g., Uruguay Round Trade Agreements, 19 U.S.C.S. §§ 3501-3624 (2016).

16. See Commission Regulation 1371/84, *supra* note 2.

17. *The Common Agricultural Policy After 2013*, EUROPEAN COMMISSION, <http://ec.europa.eu/agriculture/cap-post-2013/> (last visited Aug. 20, 2016); EUROPEAN

agency that carries out legislative policies for agriculture in Europe.¹⁸ This program serves as the legislative organization for regulations such as subsidies and quota systems for the European Union.¹⁹

The Dairy Produce Quota Regulations, which included a milk quota system, provided a method for capping milk production throughout Europe.²⁰ The members of the EEC at the time of the regulation's passage included: Belgium, Denmark, France, West Germany, Greece, Ireland, Italy, Luxembourg, Netherlands, and the United Kingdom.²¹ This group of western European nations made up one of the world's largest producers of dairy products.²² Although the regulation was set to expire in 1989, it had been renewed several times.²³ All members of the European Union abide by the Milk Quota system.²⁴

Those pushing for the milk quota system in Europe were addressing the growing milk surplus problem in Europe. During the 1970s, milk production considerably exceeded milk consumption.²⁵ Despite attempts to find alternative uses for the milk surplus, such as livestock feed, humanitarian aid, and increased exports, the milk production surplus continued to grow during the early 1980s.²⁶ The surplus was costing the CAP program well over 3 billion pounds in 1983.²⁷ This would be about a 9 billion pound expenditure if calculated for inflation.²⁸ This cost was incurred to purchase excess milk from dairy producers and

COMMISSION, OVERVIEW OF CAP REFORM 2014-2020 at 2 (2013), http://ec.europa.eu/agriculture/policy-perspectives/policy-briefs/05_en.pdf [hereinafter OVERVIEW OF CAP REFORM].

18. *The Early Years: Establishment of the CAP*, EUROPEAN COMMISSION, http://ec.europa.eu/agriculture/cap-history/early-years/index_en.htm (last updated Aug. 20, 2016).

19. See OVERVIEW OF CAP REFORM, *supra* note 17.

20. Commission Regulation 1371/84, *supra* note 2.

21. See Alice Cunha, *The European Economic Community's Third Enlargement*, 12 Miami-Fla. Eur. Ctr. of Excellence, no. 6, June 2012, at 7, http://aei.pitt.edu/43444/1/Cunha_EEC_3rd_Enlargement.pdf.

22. See ECONOMIC IMPACT OF THE ABOLITION OF THE MILK QUOTA REGIME, *supra* note 3, at 10.

23. Council Regulation (EC) Amending Regulation (EEC) No. 3950/92.

24. See ECONOMIC IMPACT OF THE ABOLITION OF THE MILK QUOTA REGIME, *supra* note 3, at 10.

25. *Id.*

26. 454 Parl Deb HL (5th ser.) (1984) col. 1757-87 (UK), <http://hansard.millbanksystems.com/lords/1984/jul/20/dairy-produce-quotas-regulations-1984> [hereinafter 454 Parl Deb HL].

27. *Id.*

28. See *Purchasing Power of British Pounds from 1270 to Present*, MEASURING WORTH, <http://www.measuringworth.com/ppoweruk/> (last visited Aug. 20, 2016).

government programs. The burden to stock butter and skimmed milk powder fell largely on the public sector.²⁹

The EEC member states found two possible solutions to their dilemma: enforce drastic price cuts or introduce a quota system.³⁰ Finding the price cuts would have needed to be extraordinary to have any effect on milk consumption, so the EEC elected to institute a milk quota system.³¹

The actual quota system involved a system of caps and levies. Each member state was given a quota that was based off their historical milk production in 1981.³² The EEC and CAP program placed a proportional limit on each member state that included the total metric tons of milk each nation could produce. For example, Ireland, a state with a traditionally large dairy industry had a cap of 245,000 metric tons.³³ Meanwhile, Luxembourg had a significantly smaller cap of 25,000 metric tons.³⁴ Each member state was allowed to produce and sell milk up to their specified cap without penalty.³⁵

Until recently, when the milk quota was abolished, the quota system was implemented under two different methods on the individual state level. The first was a wholesale quota for the delivery of milk to approved milk purchasers or dairies.³⁶ The second, a direct sales quota, was a quota on the sale of milk products directly to the public consumers.³⁷ Each member state would then break down individual quotas for every producer within the state.³⁸ It was the responsibility of each member state to ensure that their production remains under the specified quota level.³⁹

Still, the inevitability of exceeding this cap existed. Overproduction in any

29. ECONOMIC IMPACT OF THE ABOLITION OF THE MILK QUOTA REGIME, *supra* note 3, at 10.

30. 454 Parl Deb HL, *supra* note 26.

31. *Id.*

32. Commission Regulation 1371/84, *supra* note 2, at art. 4.

33. *Id.*

34. *Id.* at art. 1.

35. *Id.*

36. Rural Payments Agency, *How the Milk Quota Scheme Works*, GOV.UK, <https://www.gov.uk/how-the-milk-quota-scheme-works> (Guidance withdrawn on May 12, 2016) (last visited Mar. 5, 2016).

37. *Id.*

38. European Commission Press Release IP/10/1454, Milk: Three Member States Face Levies Worth € 19 Million for Exceeding Milk Quota (Oct. 29, 2010), http://europa.eu/rapid/press-release_IP-10-1454_en.htm; ECONOMIC IMPACT OF THE ABOLITION OF THE MILK QUOTA REGIME, *supra* note 3, at 10.

39. Rural Payments Agency, *supra* note 36.

of the member states resulted in a surplus levy or “superlevy” on the state.⁴⁰ Recently, that levy amounted to 27.83 euros for every 100kg of overproduction.⁴¹ This amounted to heavy fees for even minimal overproduction of milk. In the 2009-2010 quota period, the EU fined Denmark, the Netherlands, and Cyprus 19 million euros for exceeding milk production quotas.⁴² Actual dairy farmers usually incurred the penalty costs.

B. Domestic Effect of the Quota System

The quota system was initially introduced to limit public spending in the European dairy sector, standardize milk production, and stabilize milk prices.⁴³ It then underwent several extensions.⁴⁴ The system evolved from a policy used to control milk production, into an entirely different market altogether.⁴⁵ Prior to the repeal, member states were willing to trade and sell milk quotas through exchanges.⁴⁶ These exchanges occurred at the private and national level.⁴⁷ With these exchanges, farmers that produced less than their approved amount of milk were able to sell to other farmers that would likely exceed their limit.⁴⁸ Governments of the member states created agencies to help farmers fully understand the value of their quotas when they were looking to buy or sell the right to produce milk.⁴⁹ The quota system created an entirely new market; not a market for milk but rather a market for the right to produce it.⁵⁰

Although the quota system did see some success in stabilizing the milk market, it is now abolished.⁵¹ There were several reasons for the abolition of the

40. European Commission Press Release IP/10/1454, *supra* note 38.

41. Commission Regulation 1371/84, *supra* note 2, at art. 1.

42. European Commission Press Release IP/10/1454, *supra* note 38.

43. ECONOMIC IMPACT OF THE ABOLITION OF THE MILK QUOTA REGIME, *supra* note 3, at 1.

44. Council Regulation (EC) Amending Regulation (EEC) No. 3950/92; ECONOMIC IMPACT OF THE ABOLITION OF THE MILK QUOTA REGIME, *supra* note 3, at 10.

45. ECONOMIC IMPACT OF THE ABOLITION OF THE MILK QUOTA REGIME, *supra* note 3, at 11.

46. *Id.*; Rural Payments Agency, *supra* note 36.

47. ECONOMIC IMPACT OF THE ABOLITION OF THE MILK QUOTA REGIME, *supra* note 3, at 11.

48. *Id.*; Rural Payments Agency, *supra* note 36.

49. See generally HM Revenue & Customs, *Other Issues: Valuing Milk Quotas*, GOV.UK, <http://www.hmrc.gov.uk/manuals/ihmanual/IHTM24251.htm> (last visited Aug. 15, 2016).

50. ECONOMIC IMPACT OF THE ABOLITION OF THE MILK QUOTA REGIME, *supra* note 3, at 11.

51. *Id.* at 1.

system, including: the system raised the price of milk; it corrupted free market principles; it was grossly inefficient and difficult to administer for governments; and it was generally unfair to both farmers and certain member states.⁵²

General economic principles show that quotas, even quotas on a much smaller scale than the Dairy Produce Regulations in Europe, force a price increase on the products being limited in production.⁵³ Quotas restrict the production or quantity of a product that can be produced or sold.⁵⁴ If the market determined demand for the product exceeds the amount that can be produced, demand will exceed supply.⁵⁵ When supply cannot meet demand, price will be increased in order to decrease demand.⁵⁶

Higher EU milk prices are most likely detrimental to the European continent as a whole. Consumers are forced to pay higher prices for milk and the farmers are not able to sell the same quantity.⁵⁷ Also, the European Union is competing with other states throughout the globe for dairy exports.⁵⁸ If they are forced to have a higher milk price than their global competitors, they will miss opportunities for additional exports and potentially rely more heavily on imports.⁵⁹

Since some member states can competitively produce more milk than their respective quotas allow, the quota system effectively distorted the market and that state's opportunities.⁶⁰ For example, Italy had been consistently penalized for overproduction of milk.⁶¹ There were several reasons for their failure to stay within the quota system, but the most obvious was that overproduction was competitively advantageous for them.⁶²

On the individual or private level, farmers with the most rights to produce

52. *Milk Quota*, REFORM THE CAP <http://www.reformthecap.eu/issues/policy-instruments/milk-quota> (last visited Aug. 20, 2016).

53. INFORMA ECON., INC., *supra* note 5, at 8-9; *Milk Quota*, *supra* note 52.

54. Commission Regulation 1371/84, *supra* note 2; *Milk Quota*, *supra* note 52.

55. See Milton Friedman, *The Kennedy Round*, NEWSWEEK, July 17, 1967, at 80, <http://0055d26.netsolhost.com/friedman/pdfs/newsweek/NW.07.17.1967.pdf>; *Milk Quota*, *supra* note 52.

56. See Friedman, *supra* note 55; *Milk Quota*, *supra* note 52.

57. See ECONOMIC IMPACT OF THE ABOLITION OF THE MILK QUOTA REGIME, *supra* note 3, at 12; see also *Milk Quota*, *supra* note 52.

58. See Astley, *supra* note 4; see also *Milk Quota*, *supra* note 52.

59. ECONOMIC IMPACT OF THE ABOLITION OF THE MILK QUOTA REGIME, *supra* note 3, at 6; *Milk Quota*, *supra* note 52.

60. *Milk Quota*, *supra* note 52.

61. European Commission Press Release IP/10/1454, *supra* note 38; *Milk Quota*, *supra* note 52.

62. *Milk Quota*, *supra* note 52.

milk, not the farmer with the best capabilities, had a market advantage.⁶³ If a farmer possessed fewer production rights than he was capable of producing, the farmer was at a severe disadvantage.⁶⁴ He would have sacrificed potential profits for further production or been forced to purchase additional quota rights from another farmer.⁶⁵ Finally, farmers that possessed greater production rights than they were capable to produce were able to sell their additional production rights to other farmers.⁶⁶ They were essentially rewarded for selling a product they put little effort in creating.⁶⁷ This situation created a vast market distortion that severely harmed certain individual farmers.

The quota system created a costly burden for governments that consumed a vast amount of public resources.⁶⁸ Each member state was responsible for making sure the state, as a whole, stayed under the allotted limit for production.⁶⁹ With this said, each member state had some freedom with regard to ensuring that production did not exceed the quota limit within their state.⁷⁰ They were able to administer their own quota system to farmers by providing licenses to produce milk on the individual level or by purchasing excess milk from the farmers to stay below the quota limit.⁷¹ Regardless of the method chosen, arguably, the state's resources were burdened as the expertise required to undertake such a daunting task was complex.⁷²

The second effective alternative mentioned above required the member state to purchase excess milk production.⁷³ The obvious costs for the government to purchase the excess milk were only exacerbated by the remedial costs that followed.⁷⁴ In the end, this method defeated the original purpose of the quota system, which was to remove the burden on the public sector to find a use and pay

63. *See id.*

64. *See* ROEL JONGENEEL ET AL., WAGENINGEN UNIV. & RESEARCH CTR., EVALUATION OF CAP MEASURES APPLIED TO THE DAIRY SECTOR 8-11 (2011), http://ec.europa.eu/agriculture/eval/reports/dairy/fulltext_en.pdf.

65. *See id.* at 73.

66. *Id.*

67. *See id.*

68. European Commission Press Release IP/10/1454, *supra* note 38; JONGENEEL, *supra* note 64.

69. Commission Regulation 1371/84, *supra* note 2.

70. *See* Rural Payments Agency, *supra* note 36.

71. *See id.*

72. *See generally* JONGENEEL ET AL., *supra* note 64, at 8-9 (showing a table of necessary considerations for this evaluation).

73. *Milk Quota*, *supra* note 52.

74. *See* Rural Payments Agency, *supra* note 36.

for excess production of milk.⁷⁵

Perhaps the most glaring drawback to the quota system concerned its overall fairness, for both farmers and member states.⁷⁶ As mentioned previously, the quota system was based on set limits of production, which varied by member state.⁷⁷ These limits were not arbitrary and were calculated by measuring historical production levels.⁷⁸ For certain member states, this method of setting the quota was sometimes a death knell to potential increases in production.⁷⁹ Member states, most notably the Netherlands, could have potentially surpassed the U.K. in milk production, well over a decade ago, as they had the resources and economic capability to do so.⁸⁰ However, the quota held them behind their fellow EU member in production.⁸¹

Additionally, growing member states also had no incentive to increase their domestic capabilities. States, such as the Czech Republic, were attempting to increase GDP in all industries but were handcuffed by the quota system.⁸² If the state or other private entities wanted to invest in the dairy industry, they would have been limited by the previously set quota. What investor would have wanted to invest in an industry that would have been penalized for being too successful?

This inequality in production was ultimately passed down to the farmers. Just as the economic inefficiencies of the quota system ultimately hurt the farmer, the inequalities also crippled their potential to be successful. A farmer in the Netherlands would not have the same opportunities as a farmer in the U.K., despite being governed by the same pertinent legislative body.⁸³ Even if a particular Dutch farmer was smarter, more frugal, and more driven than her British counterpart, she

75. 454 Parl Deb HL, *supra* note 26; *Milk Quota*, *supra* note 52.

76. *Milk Quota*, *supra* note 52.

77. JONGENEEL ET AL., *supra* note 64, at 72.

78. *Id.*

79. *See Milk Quota*, *supra* note 52.

80. Compare Katrien van't Hooft, *History of NL Dairy Farming*, DUTCH FARM EXPERIENCE, <http://www.dutchfarmexperience.com/history-nl-dairy-farming/> (last visited Aug. 20, 2016) (showing a fourteen fold increase in average milk production in Netherlands in 2007), with ECONOMIC IMPACT OF THE ABOLITION OF THE MILK QUOTA REGIME, *supra* note 3, at 3.

81. ECONOMIC IMPACT OF THE ABOLITION OF THE MILK QUOTA REGIME, *supra* note 3, at 6.

82. *See generally Czech Business Economic Facts*, AM. FRIENDS OF THE CZECH REPUBLIC, <http://www.afocr.org/economic-facts> (last visited Aug. 20, 2016) (connecting the Czech Republic's GDP with trade regulation by the EU and growth needed in agricultural exports to EU and diversifying their economy).

83. Rural Payments Agency, *supra* note 36; ECONOMIC IMPACT OF THE ABOLITION OF THE MILK QUOTA REGIME, *supra* note 3, at 11.

would simply be unable to compete on the same level if she had a more restricted cap on her production.

The quota system had its obvious drawbacks. The legislators within the European Economic Commission took note of these shortcomings and took action to solve the problems by repealing the quota system.

III. THE U.S. DAIRY INDUSTRY

A. History of U.S. Dairy Regulation

American legislators have taken two approaches towards regulating the dairy industry.⁸⁴ The first is domestic legislation, which includes providing subsidies to dairy farmers.⁸⁵ The second is creating international free trade agreements that provide an avenue to export greater quantities of milk across the globe.⁸⁶

Initially, both federal and state legislation mirrored a quota system during the Great Depression.⁸⁷ In 1932, Wisconsin passed an act that set minimum and maximum prices of milk.⁸⁸ The federal government would purchase determined amounts of dairy products in order to aid in the control of volatile milk prices.⁸⁹ These actions were largely ineffective as controlling the price of milk addressed only a symptom of the mass economic problem.⁹⁰ Additionally, the federal government was not capable of effectively controlling the quantity of milk in the national market.⁹¹

The idea of government intervention in the dairy industry took a turn after the Great Depression.⁹² The Agricultural Act of 1949 introduced a system of subsidies for farmers throughout America.⁹³ The underlying objectives of supporting farmers through government intervention is largely intact today.⁹⁴ The

84. See Daniel A. Sumner & Joseph V. Balagtas, *United States Agricultural Systems: An Overview of U.S. Dairy Policy*, in *ENCYCLOPEDIA OF DAIRY SCIENCES 2* (H. Roginski, J. Fuquay & P. Fox eds., Elsevier Science Ltd. 2002).

85. See *id.*

86. See *id.*

87. *Id.* at 1.

88. ERIC M. ERBA & ANDREW M. NOVAKOVIC, CORNELL UNIV., E.B. 95-05, *THE EVOLUTION OF MILK PRICING AND GOVERNMENT INTERVENTION IN DAIRY MARKETS 8* (1995), <http://dairy.wisc.edu/pubPod/pubs/EB9505.pdf>.

89. Sumner & Balagtas, *supra* note 84, at 6.

90. *Id.* at 7.

91. *Id.* at 3-6.

92. ERBA & NOVAKOVIC, *supra* note 88, at 1.

93. *Id.* at 10.

94. *Id.* at 16.

Agricultural Act of 1949 allowed the USDA to purchase dairy products at agency-determined prices.⁹⁵ The agency prices would be determined in relation to the market price at the time.⁹⁶

The subsidy served as a safety net for the farmers that work in an unpredictable milk industry.⁹⁷ While consumer demand for dairy maintains a relatively consistent level, many other factors can potentially cripple a farmer's livelihood without a subsidy.⁹⁸ Storms, droughts, unseasonable freezes, falling crop prices, and rising cattle feed prices can significantly raise or lower the production and eventual price of milk on the market.⁹⁹ Should milk prices fall too low, dairy farmers would not be able to turn the profit necessary to undertake expensive operations.¹⁰⁰ The farmers could be wholly unable to continue operations without the subsidy.¹⁰¹

During the 1990s, the federal government maintained a sizeable subsidy for dairy farmers but did slightly cut back subsidies for milk products.¹⁰² The trend of cutting back subsidies persisted from 1995 to 2000.¹⁰³ In general, relative to other agricultural industries, milk products receive lower subsidies.¹⁰⁴ Today, there is continued discussion on shifting from subsidies, to more of an emergency fund type program.¹⁰⁵

The Milk Income Loss Contract program (MILC) served as an additional subsidy program.¹⁰⁶ The program allows for the direct government compensation to dairy farmers when milk prices fall below a specified level.¹⁰⁷ This subsidy was

95. *Id.* at 10.

96. *Id.*

97. *See id.* at 8-9.

98. *Id.* at 10-16.

99. *See id.* at 15.

100. *Id.* at 6.

101. *Id.* at 9.

102. Sumner & Balagtas, *supra* note 84, at 2-3.

103. *Id.* at 3.

104. *Id.* at 2 (stating, "the U.S. government continues to provide small amounts of direct financial subsidy for U.S. exporters of dairy products.").

105. *See generally* USDA, ECONOMIC EFFECTS OF U.S. DAIRY POLICY AND ALTERNATIVE APPROACHES TO MILK PRICING (2004), <http://www.usda.gov/documents/NewsReleases/dairyreport1.pdf> [hereinafter DAIRY POLICY AND ALTERNATIVE APPROACHES].

106. FARM SERV. AGENCY, USDA, 2014 FARM BILL FACT SHEET: MILK INCOME LOSS CONTRACT PROGRAM 1 (2014), http://www.fsa.usda.gov/Internet/FSA_File/milc_2014.pdf [hereinafter MILK INCOME].

107. *Id.*

administered on a regional basis throughout the country.¹⁰⁸

The MILC program was eventually replaced by the Margin Protection Program.¹⁰⁹ The Margin Protection Program serves as more of an insurance policy for downturns in milk profits.¹¹⁰ It focuses on the quantity of milk being sold, rather than the price of dairy.¹¹¹ The program covers all catastrophic events.¹¹² Additionally, farmers can purchase government backed “coverage” for declining milk sales total.¹¹³

The Margin Protection Program is coupled with the Dairy Product Donation Program, which works similarly to the old MILC program.¹¹⁴ During times of nationally low levels of dairy production, the federal government is authorized to award subsidies to the affected farmers.¹¹⁵ While the MILC program of direct subsidies was technically phased out, its underlying methods remain intact.¹¹⁶ Farmers purchase insurance for guaranteed subsidies and understand that a complete failure cannot occur under these new programs.¹¹⁷ Dairy farmers are still covered by a substantial safety net.¹¹⁸ These programs are valid through 2018 and are administered through the Farm Service Agency.¹¹⁹

The USDA claims that the effect their dairy programs have on farmers is modest.¹²⁰ However, they do admit that the effect of the subsidies on the economy and farmers is hard to calculate.¹²¹ The federal government has had substantial intervention in dairy programs for the better part of the past century.¹²² It is difficult to predict the effect of the federal government’s withdrawal from the dairy

108. *Id.*

109. *Dairy Margin Protection Program*, USDA, <http://www.fsa.usda.gov/programs-and-services/Dairy-MPP/index> (last visited Aug. 20, 2016).

110. *See* FARM SERV. AGENCY, USDA, 2014 FARM BILL FACT SHEET: MARGIN PROTECTION PROGRAM FOR DAIRY 2 (2014), http://www.fsa.usda.gov/Internet/FSA_File/mpp_dairy.pdf [hereinafter MARGIN PROTECTION].

111. *Id.*

112. *Id.*

113. *Id.*

114. *Id.* at 1.

115. *See id.* at 3.

116. *See* MILK INCOME, *supra* note 106, at 1; *see also* MARGIN PROTECTION, *supra* note 110, at 1.

117. *See* MARGIN PROTECTION, *supra* note 110, at 1.

118. *See* MILK INCOME, *supra* note 106, at 1.

119. MARGIN PROTECTION, *supra* note 110, at 1.

120. DAIRY POLICY AND ALTERNATIVE APPROACHES, *supra* note 105, at 84-85.

121. *See id.* at 5.

122. *Id.*

industry.¹²³

The USDA estimates that the subsidies currently raise the price of milk by only about 1 percent.¹²⁴ However, this number is calculated during times of relatively stable dairy output when subsidies are relied upon less by farmers.¹²⁵ Past years, where the subsidies have been relied on in greater amounts, have resulted in disproportionately higher milk prices.¹²⁶ In future years, when more subsidies are required, a similar escalation in milk prices can be expected.¹²⁷

Others argue that the subsidies have a far greater effect on the global economy, in addition to American dairy farmers.¹²⁸ Farmers have expressed concerns that the Margin Protection Program could face similar problems that were seen in the European quota system.¹²⁹ The Margin Program bases subsidies and coverage on a farmer's past production history to determine future output.¹³⁰ American farmers argue that the government is trying to predict the output of various farmers.¹³¹

This could lead farmers to potentially fear producing too great of a quantity in good years because of the information they would provide the FSA. The FSA could then overestimate the farmer's capabilities and consequently be unwilling to provide a subsidy cushion for certain years. What may be viewed as a good year by the FSA could, in reality, be a poor performance output for a farmer given their production capabilities. At present, the hybrid insurance-subsidy structure is here for the foreseeable future.¹³² While its drawbacks are well documented, the safeguards it provides dairy farmers are undoubtedly beneficial to some.¹³³

American lawmakers have also taken action to promote the sale of American milk abroad.¹³⁴ International trade agreements have been distinctly beneficial for

123. *Id.*

124. *Id.*

125. *See id.* at 6.

126. *Id.*

127. *See id.*

128. Jason Stein, *Wisconsin Dairy Farmers Could be Hurt by Change in Subsidy Program*, MILWAUKEE J. SENTINEL (July 15, 2012), <http://www.jsonline.com/news/statepolitics/wisconsin-dairy-farmers-could-be-hurt-by-change-in-subsidy-program-ed63rgj-162536416.html>.

129. *Id.*

130. *See* MARGIN PROTECTION, *supra* note 110, at 1.

131. Stein, *supra* note 128.

132. *See* MILK INCOME, *supra* note 106, at 1; MARGIN PROTECTION, *supra* note 110, at 1.

133. *See* DAIRY POLICY AND ALTERNATIVE APPROACHES, *supra* note 105, at 84.

134. Jaime Castaneda, *Trade Agreements Deliver for the U.S. Dairy Industry*, CHEESE MARKET NEWS, <http://www.cheesemarketnews.com/guestcolumn/2014/10oct14.html> (last

several parties.¹³⁵ Two particular trade agreements have brought significant gains to the American dairy industry.¹³⁶ The North American Free Trade Agreement (NAFTA) and the Uruguay Round of the World Trade Agreement (WTO) have aided in reducing barriers to dairy imports and exports.¹³⁷

NAFTA came in to effect in America in 1994.¹³⁸ NAFTA has greatly benefitted the trade of products within the countries of Mexico, the United States, and Canada.¹³⁹ NAFTA has targeted three main problem areas of dairy trade that has created greater opportunities for dairy farmers in the North American continent.¹⁴⁰ NAFTA has substantially reduced trade barriers among the countries in market access, sanitation requirements, and rules of origin.¹⁴¹

Mexico and the U.S. have been particularly active in increasing market equality between the countries.¹⁴² This includes decreasing the aforementioned subsidies in both countries.¹⁴³ Furthermore, it thoroughly depletes the tariffs on exports while severely restricting import quotas in both countries.¹⁴⁴ "Because Canada excluded its dairy sector from the NAFTA, provisions would affect dairy trade only between the U.S. and Mexico."¹⁴⁵

NAFTA has proven to be a successful venture for dairy exporters.¹⁴⁶ As a first step in large-scale international trade agreements, dairy exports thoroughly increased, which resulted in higher gains for dairy farmers.¹⁴⁷ Only one year after the signing of the agreement, U.S. Dairy exports to Mexico increased over six times to \$6.7 billion.¹⁴⁸ NAFTA was and is ultimately beneficial for American dairy farmers.¹⁴⁹

visited Aug. 20, 2016).

135. *Id.*

136. *Id.*

137. *Id.*

138. *NAFTA*, NAFTANOW.ORG, <http://www.naftanow.org> (last visited Aug. 20, 2016).

139. Castaneda, *supra* note 134; JOE OUTLAW ET AL., DAIRY MKTS & POLICY: ISSUES & OPTIONS, P-14, NAFTA AND THE U.S. DAIRY INDUSTRY 1 (1994), <http://dairy.wisc.edu/pubPod/pubs/P14.pdf>.

140. *See* OUTLAW ET AL., *supra* note 139, at 1.

141. *Id.*

142. *See id.*

143. *Id.*

144. *See id.* at 1-2.

145. *Id.*

146. Castaneda, *supra* note 134.

147. *Id.*

148. *Id.*

149. *Id.*

The WTO expanded free trade agreements across several more borders; the agreements totaled at 123 contracting parties.¹⁵⁰ The WTO has extended the successes of NAFTA to several countries.¹⁵¹ Dairy farmers have noticed an intense increase in exports to South America as a result of the agreement. Overall, the free trade agreements have significantly benefited the American dairy farmer and the American economy as a whole.¹⁵²

What should be noted is that conflict between international free trade and domestic subsidies are apparent. Countries are unwilling to enter into free trade with farmers who are subsidized by a federal government.¹⁵³ One reason is because subsidized milk inherently carries an artificially higher price.¹⁵⁴ A Mexican dairy farmer cannot compete on an even playing field with an American farmer receiving subsidies.¹⁵⁵ The costs of selling milk at a higher price are initially handed to the importing consumer. However, this will naturally decrease demand and effectively bring the costs back to the exporting country and their dairy farmers.

More free trade opportunities have been sought by American lawmakers.¹⁵⁶ Lawmakers have significantly torn down trade barriers throughout the western hemisphere.¹⁵⁷ However, Asia and the Oceanic States still have significant barriers to trade with the United States.¹⁵⁸ What is potentially more alarming is the fact that nations like China and Australia are consistently entering into new trade agreements.¹⁵⁹

In one case, Australia signed a free trade agreement with China, which bodes

150. *The Uruguay Round*, WORLD TRADE ORG., http://www.wto.org/english/thewto_e/whatis_e/tif_e/fact5_e.htm (last visited Aug. 20, 2016).

151. Peter Bondarenko, *North American Free Trade Agreement (NAFTA)*, ENCYCLOPEDIA BRITANNICA, <https://www.britannica.com/event/North-American-Free-Trade-Agreement> (last visited Aug. 20, 2016).

152. Castaneda, *supra* note 134.

153. OUTLAW ET AL., *supra* note 139, at 2.

154. *Id.*

155. *Id.*

156. *See id.* at 6.

157. *See id.* at 1.

158. *See generally* U.S. Dairy Export Council, *Second-half Slump Tempers 2014 Dairy Export Records*, DAILY HERD MGMT. (Feb. 5, 2015, 5:07 PM), <http://www.dairyherd.com/news/second-half-slump-tempers-2014-dairy-export-records>.

159. *Murray Goulburn looks to milk China free trade agreement*, THE AUSTRALIAN BUS. REV. (Nov. 27, 2014, 3:28 PM), <http://www.theaustralian.com.au/business/news/murray-goulburn-looks-to-milk-china-free-trade-agreement/news-story/a03c9ba7fa710a78d63e882f91846ab7> [hereinafter *Murray Goulburn*].

well for Australia's dairy exports.¹⁶⁰ Leading Australian dairy exporters expect to increase investment in exporting operations by over \$500 million in the next three years in order to accommodate the new demand for milk.¹⁶¹ This is a direct result of the new trade agreement.¹⁶² As mentioned, the U.S. is looking to increase exports to China.¹⁶³ There is significant demand for dairy in this area, which the U.S. could capitalize on.¹⁶⁴ However, neighboring states such as Australia, Russia, and Europe may swallow up these opportunities if the U.S. fails to act quick enough.¹⁶⁵

In conclusion, American lawmakers currently utilize domestic legislation such as subsidies and insurance programs to support American dairy farmers.¹⁶⁶ Additionally, the use of international free trade agreements has bolstered net exports and profits for farmers.¹⁶⁷ These actions are often in conflict with one another as true "free trade" necessitates the repeal of domestic subsidies.¹⁶⁸

B. U.S. Dairy Exports

As stated, the U.S. has consistently sought to export milk and dairy products at a greater level.¹⁶⁹ However, the past year could not have been worse for U.S. dairy exports. Total export sales were down twenty-six percent in 2015.¹⁷⁰ This marked the first decrease in exports in over five years. Furthermore, the U.S. lost considerable market share amongst the world dairy market. In 2015, the exported volume of dairy as a percentage of total production was down 15.3 percent from 2014.¹⁷¹

There are multiple reasons for the decline in U.S. exports of dairy. The global demand for milk, particularly in Asia, has declined.¹⁷² Also, Russia issued an embargo on all dairy products coming from Europe.¹⁷³ However, the repeal of the

160. *Id.*

161. *Id.*

162. *Id.*

163. *See generally* Martin, *supra* note 11.

164. *Id.*

165. *Murray Goulburn, supra* note 159.

166. *See generally* MILK INCOME, *supra* note 106; MARGIN PROTECTION, *supra* note 110.

167. *Castaneda, supra* note 134.

168. *Id.*

169. *See* U.S. Dairy Export Council, *supra* note 158.

170. *Levitt, Growth Streak, supra* note 1.

171. *Id.*

172. *Id.*

173. *Id.*

milk quota in Europe is assuredly responsible for the decrease in U.S. exports.¹⁷⁴ While U.S. exports drastically decreased in the past year, European exports actually increased.¹⁷⁵ Additionally, there does not appear to be any immediate signs of reversing this trend.¹⁷⁶

IV. THE GLOBAL DAIRY MARKET

A. Effect of the Quota Repeal

Just before the repeal of the EU milk quota went into effect, the U.S. Dairy Export Council published a lengthy report predicting the possible ramifications of the repeal.¹⁷⁷ The Export Council, a “non-profit, independent membership organization that represents the global trade interests of U.S. dairy producers, proprietary processors and cooperatives, ingredient suppliers and export traders,” is one of the leading authorities on American dairy export data and prognostication.¹⁷⁸

In the fall of 2014, they predicted that American dairy exporters “should not get overly distracted by” the changes that result from the repeal of the milk quotas.¹⁷⁹ They added that “[t]he U.S. dairy industry remains well poised to continue the impressive growth seen in the last decade or so.”¹⁸⁰ To be fair, this prediction was tempered with a qualifier stating “without a major, and currently unforeseen, downturn in the world’s economic performance in the next few years” demand will exceed supply for milk in foreign markets.¹⁸¹

The effect of the repeal of the EU milk quota was far greater than even the foremost experts could have anticipated. American exports have drastically declined while their European counterparts are increasing their export volume and

174. *Id.*

175. See Alan Levitt, *Still No Story To Suggest Market Lift*, U.S. DAIRY EXPORT COUNCIL (Jan. 14, 2016), <http://www.usdec.org/research-and-data/market-information/market-commentary-archives/market-commentary/market-commentary-01-14-16> [hereinafter Levitt, *Market Lift*].

176. *Id.*

177. See U.S. DAIRY EXPORT COUNCIL, EUROPEAN UNION: THE IMPACT OF THE REMOVAL OF MILK QUOTAS IN 2015 (Fall 2014) [hereinafter MILK QUOTAS IN 2015].

178. *About Us*, U.S. DAIRY EXPORT COUNCIL, <http://www.usdec.org/about-us> (last visited Aug. 20, 2016).

179. MILK QUOTAS IN 2015, *supra* note 177, at 67.

180. *Id.*

181. *Id.* at 66.

sales.¹⁸² Americans lost significant market share in Asia and Africa.¹⁸³ That market share has been devoured by the newly bolstered European production.¹⁸⁴ In conclusion, the repeal of the European milk quota regime has directly affected American exporters.

B. American Answer to the Repeal

American lawmakers are not without options in attempting to help American dairy farmers through what could be a potential significant downturn in U.S. exports of milk.¹⁸⁵ The best option for legislators is to decrease subsidies on the domestic level and increase free trade agreements on the international level.

The first step in helping American farmers could potentially be to roll back milk subsidies to a bare minimum insurance policy. At first glance this may seem counterintuitive, but it should ultimately enhance the profitability of the American dairy farmer. It should help increase domestic demand, allow for greater free trade with other nations, and ultimately increase net exports. While some may be reluctant to relinquish the safety net supporting American dairy farmers, this step can aid in the long run.

Currently the U.S. has a hybrid insurance and subsidy program for American Dairy farmers through the Margin Protection Program.¹⁸⁶ The MPP was yet another step in rolling back subsidies.¹⁸⁷ American legislators can continue to reduce the subsidies to a full insurance style program. Truthfully, American dairy farmers are far less reliant on these subsidies relative to their fellow farmers in other agricultural industries.¹⁸⁸

Reducing the subsidies should reduce the price of dairy in America. With lower prices, the domestic demand for American milk should increase. The dairy subsidy is present regardless of the demand or supply of milk.¹⁸⁹ It follows that an increased demand for milk would come with no extra effort to produce more milk. However, it is entirely possible that an increased demand could occur and dairy farmers could increase production, and eventually their overall profitability.

Next, a downgrade of subsidies and the federally funded insurance programs

182. Levitt, *Growth Streak*, *supra* note 1.

183. *Id.*

184. *Id.*

185. *Id.*

186. MARGIN PROTECTION, *supra* note 110, at 1.

187. *See id.*

188. *See generally* OUTLAW ET AL., *supra* note 139.

189. *See* MARGIN PROTECTION, *supra* note 110, at 1 (stating the MPP “is a voluntary risk management program for dairy producers”).

should create opportunities for greater free trade. As previously noted, domestic subsidies have been a roadblock in securing full free-trade agreements. With regards to NAFTA, Mexico is often unwilling to increase trade of certain commodities that are supported by subsidies.¹⁹⁰ Both nations have heated disagreements over the Canadian government's involvement throughout their agricultural industry.¹⁹¹ The bottom line is that nations are unwilling to trade with other nations that are subsidizing items.¹⁹² In order to even enter the conversation for new trade agreements, American lawmakers must be willing to reduce federal support for dairy farmers.¹⁹³

As exemplified by NAFTA, increased free trade agreements should naturally lead to increased exports. As more and more nations become willing to trade with America, dairy exporters should be able to send their milk product to additional markets. The potential millions that could demand milk could result in greatly increased profits for American dairy farmers.

A rollback of subsidies would most likely be a necessary step in accomplishing the second action American lawmakers can enact in aiding American dairy farmers, actively seeking additional trade agreements. Recently, Australia's largest dairy company signed a massive dairy trade agreement with China.¹⁹⁴ Australia has recognized the need for greater free trade agreements with other nations.¹⁹⁵ The benefits for both nations are likely to be significant for consumer and farmer alike.¹⁹⁶

The U.S. has already taken note of this success as they have actively sought to mimic the Australians. The U.S. Congress is currently considering the Trade Promotion Authority legislation.¹⁹⁷ This Act should greatly increase free trade agreements in crucial regions for American exports. Most notably this act would pave the way for the Trans-Pacific Partnership (TPP).

The TPP is yet another free trade agreement that would bring greater free

190. *See generally* OUTLAW ET AL., *supra* note 139, at 1.

191. *See generally id.*

192. *See generally id.*

193. *See generally id.*

194. *See Murray Goulburn, supra* note 159.

195. *See id.*

196. *See id.*

197. Aaron Forbes & Julia Lawless, *Hatch Calls on Senate to Pass Bipartisan Trade Promotion Authority that Give Congress and the American People a Voice on Trade*, U.S. SENATE COMMITTEE ON FIN. (May 18, 2015), <http://www.finance.senate.gov/chairmans-news/hatch-calls-on-senate-to-pass-bipartisan-trade-promotion-authority-that-gives-congress-and-the-american-people-a-voice-on-trade>.

trade to nine participating countries.¹⁹⁸ These countries, such as Canada, the United States, Peru, Chile, Australia, New Zealand, and Singapore, would create a web of free trade throughout the Pacific Ocean.¹⁹⁹ Prominent exporters of dairy such as the United States and Australia would be able to ship milk products to Singapore and Peru without the traditional barriers of tariffs.²⁰⁰ Furthermore, the trade agreement would require each member to undergo “robust market liberalization.”²⁰¹ This means that each member will have to roll back subsidies and other government intervention domestically.

America has had a historically different approach towards government intervention in the dairy industry than their European counterparts. In many respects, the European quota system was flawed as it stunted milk production and impeded the success of European dairy farmers. However, the European Union is making wholesale changes to their intervention. These changes have drastically impacted the global milk market.

America must be able to manage the EU milk quota repeal with some changes of its own. The best option is to remove barriers such as subsidies and overbroad insurance programs to support its free trade efforts. Productive international trade relationships with partner countries will be necessary to remain a global power in the dairy market. It is important to maintain this status for the sake of American dairy farmers.

198. OUTLINES OF TPP, U. S. TRADE REP. (2011), <https://ustr.gov/tpp/outlines-of-TPP>.

199. *Id.*

200. *See id.*

201. *Id.*