

January 1996

AGRICULTURAL MARKETING

U.S. Cotton Market Before and After Import Assessments



**Resources, Community, and
Economic Development Division**

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Congressional Recipients

As authorized by the Cotton Research and Promotion Act Amendments of 1990, the cotton research and promotion program was extended to include assessments on imported cotton. This program, commonly known as the cotton check-off program,¹ has collected assessments on domestic cotton since 1967. The program's activities are intended to strengthen cotton's competitive position in relation to synthetic fibers and maintain and expand domestic and foreign markets for U.S. cotton. The Cotton Board, composed of producers and importers, is responsible for the check-off program and develops research and promotion plans and related budgets. The Cotton Board contracts with a single organization, Cotton Incorporated, to implement the check-off program. The U.S. Department of Agriculture's (USDA) Agricultural Marketing Service (AMS) is responsible for ensuring that the program complies with its authorizing legislation.

The 1990 act required that we analyze (1) the growth in the U.S. market for cotton and cotton products, particularly following the imposition of assessments on imports; (2) the extent to which import restrictions, such as quotas, on cotton and cotton products have permitted or prevented importers from benefiting from any such growth in the U.S. market; and (3) the relevant U.S. international trade obligations and the compliance of the assessment on imported cotton and cotton products with these obligations. The act also required that we report on the administration of the cotton check-off program for imports.

Results in Brief

The U.S. market for raw cotton and cotton products grew at about the same rate—about 6.6 percent annually—before and after the imposition of the assessment on imports in 1992. Industry experts believe that it is unlikely that the cotton import assessment has had any measurable effect on the growth rate because the assessment is a relatively minor cost for imported cotton products—about one-half cent for a man's cotton shirt, for example, or a total of about \$14 million annually on imported cotton products valued at \$19 billion.²

¹The term "check-off" refers to the way that the promotion and research programs are funded: A small amount is deducted from the revenues that producers and/or other members of an industry receive from the sale of their products.

²Almost all U.S. imports of cotton are textile and apparel cotton products, not raw cotton.

Since 1984, quotas and tariffs have not prevented imported cotton products from sharing in the growth in the U.S. market. The volume of imported cotton products has increased even faster than the U.S. consumption of cotton, expanding from 1.5 billion pounds in 1984 to about 3.8 billion pounds in 1994, an average annual increase of about 10 percent. Imported cotton products accounted for almost half of the domestic consumption in 1994.

The assessment on imported cotton products complies with U.S. trade obligations, according to the Assistant U.S. Trade Representative for Agricultural and Commodity Policy, Office of the U.S. Trade Representative (USTR), and officials from the Foreign Agricultural Service's Tobacco, Cotton, and Seed Division in USDA. These officials told us that U.S. trade obligations are based on the principle of treating imported products in the same manner as comparable domestic products are treated—the principle of “national treatment.” The cotton import assessment is in accord with this principle because the assessment imposed on imports is the same as the assessment imposed on like domestic products and because importers have benefited from the check-off program at least as much as domestic producers, as measured by the increasing import share of the U.S. market.

USDA has established the administrative framework outlined in the 1990 act for assessing cotton imports. Among other things, USDA held a referendum of producers and importers on whether to assess imports, set an assessment rate for cotton imports that is equivalent to the rate charged domestic producers, and established collection procedures with the U.S. Customs Service (Customs).

While USDA has put in place the administrative framework for assessing cotton imports, two major issues remain unresolved. First, importers are paying assessments on the U.S. cotton content of imported cotton products, even though provisions in the 1990 act allow for an exemption because the assessments have already been paid by U.S. producers. To receive an exemption from the assessment, USDA requires importers to document the presence of U.S. cotton in imported products. Importers generally do not find it cost-effective to provide this information. Consequently, we estimate that importers are paying import assessments of about \$2.1 million annually on cotton products containing U.S. cotton on which assessments have already been paid. Second, producers and importers disagree on the broader management and oversight functions of the Cotton Board. Overall, importers believe that the Cotton Board does

not adequately oversee the activities of Cotton Incorporated, the industry organization that operates the check-off program. Producers, on the other hand, believe that the program is successful as currently managed and does not require significant changes.

Background

During the 1960s, in an effort to address the decline in demand for cotton brought on by competition from synthetic fibers, cotton industry organizations proposed legislation to create a federally authorized, industry-funded program aimed at expanding consumers' demand for cotton. Subsequently, the Cotton Research and Promotion Act of 1966 authorized the creation of the Cotton Board and charged it with increasing cotton's share of the textile and apparel market through a research and promotion program.³

The 1966 act gives the Cotton Board the primary responsibility for administering the cotton check-off program, including developing program plans and budgets. The act also directs the Cotton Board to contract with an organization, governed by cotton producers, to carry out its research and promotion activities. Since 1967, that organization has been a nonprofit corporation called Cotton Incorporated.

From 1967 to 1991, all domestic producers had to pay cotton assessments. However, the act allowed producers who were not in favor of supporting the program to request a refund. In the late 1980s, about one-third of the assessments collected were refunded. In November 1990, the Congress enacted the Cotton Research and Promotion Act Amendments of 1990, which was included under title XIX, subtitle G, of the Food, Agriculture, Conservation, and Trade Act of 1990 (known as the 1990 Farm Bill). These amendments authorized two fundamental changes in the funding procedures for the cotton check-off program: (1) the imposition of assessments on imported cotton and cotton-containing products and (2) the elimination of refunds. To become effective, however, these revisions had to be approved in a referendum by at least half of the domestic producers and importers voting. About 60 percent of those voting approved these revisions in July 1991. In effect, the approved changes made the program mandatory for both domestic producers and importers.

³Two GAO reports provide information on U.S. agricultural research and promotion programs, including the cotton program: Agricultural Marketing: Federally Authorized Commodity Research and Promotion Programs (GAO/RCED-94-63, Dec. 29, 1993) and Agricultural Marketing: Comparative Analysis of U.S. and Foreign Promotion and Research Programs (GAO/RCED-95-171, Apr. 28, 1995).

After the final regulation was issued and other administrative procedures were completed, import assessments on cotton products began to be collected on July 31, 1992. The assessments are collected by Customs and remitted to the Cotton Board through AMS on a monthly basis.

Domestic producers pay an assessment when they sell their raw cotton. The current cotton assessment is a fixed rate of \$1 per 500-pound-bale plus 0.5 percent of the market value. Based on a market value of 60 cents per pound, the total assessment per pound of raw cotton is about one-half cent. Importers pay an assessment on the raw cotton equivalent of imported textiles and apparel. To calculate the assessment rate for imported cotton products, USDA has established procedures for estimating the amount of raw cotton used to manufacture about 700 different cotton products. (See app. I for examples of how AMS calculates rates for an imported cotton product.)

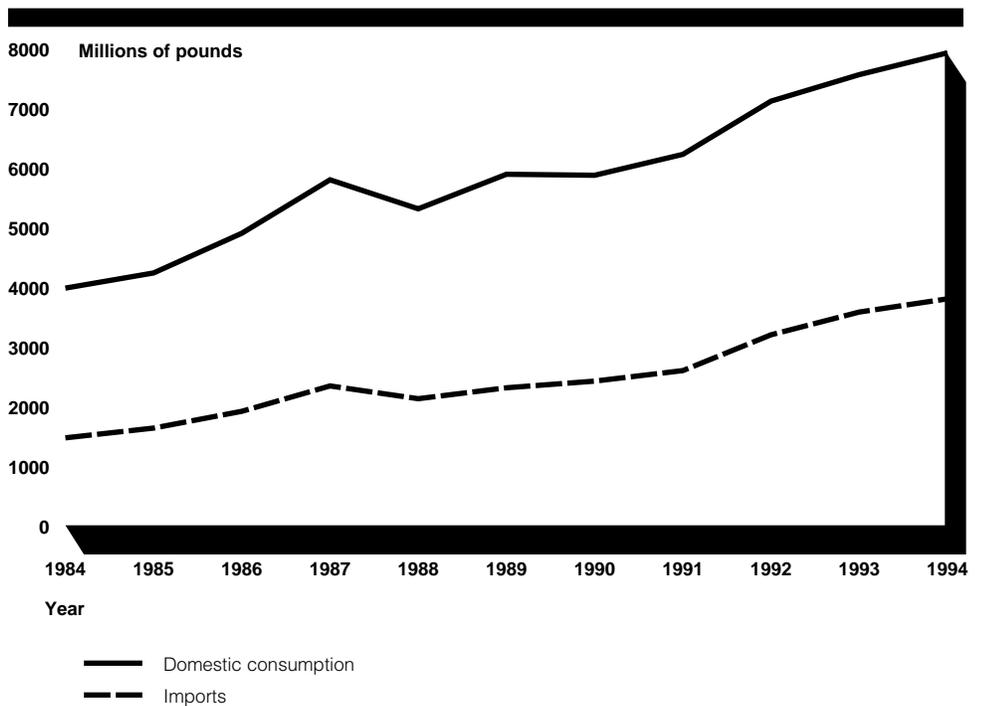
Because the check-off program is federally authorized, the Secretary of Agriculture and AMS have certain oversight responsibilities. The Secretary must approve the Cotton Board's recommended program plans and budgets before they can become effective. AMS' responsibilities include (1) developing regulations to implement the check-off program, in consultation with the cotton industry, and (2) ensuring compliance with the authorizing legislation and AMS' orders and regulations. Generally, the act and AMS' regulations specify allowable activities, such as the type of promotion or research activities, the level and collection of assessments, the composition of the Board, and the types of allowable expenditures. To ensure compliance, AMS reviews the Board's budgets and projects to, for example, prevent the Board from engaging in prohibited activities, such as lobbying. However, AMS' oversight role does not include reviewing the program's effectiveness. AMS is reimbursed by the Cotton Board for its oversight costs.

The assessment on cotton imports and the elimination of refunds have contributed, in large part, to the substantial growth in the Cotton Board's check-off revenues since 1990. In 1990, the Cotton Board received check-off revenues from producers of about \$27.6 million after refunds. In fiscal year 1994, the Cotton Board's check-off assessment revenues totaled about \$56.8 million—\$43.2 million, or 76 percent, from domestic producers and \$13.6 million, or 24 percent, from importers.

U.S. Cotton Consumption Has Continued to Increase After Imposition of the Assessment

The imposition of the cotton import assessment has not prevented increases in the U.S. consumption of cotton. Between 1984 and 1991, the U.S. consumption of raw cotton and cotton products grew from 4 billion pounds to 6.2 billion pounds, an average annual growth rate of 6.6 percent. Following the imposition of the cotton import assessment in 1992, the U.S. market continued to grow at about the same rate through June 1995. The U.S. consumption of cotton may exceed 8 billion pounds in 1995. (See fig. 1.)

Figure 1: U.S. Domestic Consumption and Imports of Cotton and Cotton Products, 1984-94 (in Millions of Pounds of Raw Cotton Equivalent)



Source: GAO's analysis of data published by USDA's Economic Research Service.

Government and other experts knowledgeable about the U.S. textile and apparel industry⁴ agreed that the imposition of the cotton import assessment beginning in July 1992 has had no significant impact on the

⁴These industry experts included USDA's Chief Economist and the president of the Cotton Board. We also spoke with staff from the International Cotton Advisory Committee, the Department of Commerce's Office of Textiles and Apparel, the U.S. International Trade Commission, and USDA's Economic Research Service.

long-term growth in U.S. consumption of domestic cotton. They pointed out that the relatively small size of the cotton import assessment—about one-half cent per pound of raw cotton equivalent—is likely to have little effect on retail prices.

According to these experts, the primary factor explaining the growth in cotton consumption since 1984 is consumers' increasing preference for cotton apparel—per capita consumption increased from 17 pounds to 30 pounds between 1984 and 1994. They also said that technological developments, such as wrinkle-resistant cotton fabric and different denim finishes, have further enhanced consumers' preference for cotton apparel.

In addition, these experts said that the cotton check-off program has contributed to consumers' preference for cotton, although they could not cite any study measuring the extent of the program's contribution. According to USDA's Chief Economist, a positive correlation generally exists between increased promotion and increased sales of a particular product. However, he also said that researchers measuring this positive correlation have found that it can vary from small to large, depending on the product, the time period involved, and other factors.

Quotas and Tariffs Have Not Prevented Importers From Sharing in the Growth of U.S. Cotton Consumption

As discussed in the conference report on the 1990 Farm Bill,⁵ some lawmakers were concerned that while importers would be contributing to the check-off program on an equal footing with domestic producers, they would be denied equivalent access to the U.S. cotton market because of tariffs and quotas. According to the USTR, in 1992 the United States maintained quotas for about 67 percent of imported cotton products.

Despite these concerns, quotas and tariffs have not prevented cotton imports from sharing in the growth in the U.S. market. Cotton imports have grown even faster than U.S. consumption, increasing from 1.5 billion pounds in 1984 to about 3.8 billion pounds in 1994, an average annual growth rate of about 10 percent. In addition, imported cotton products accounted for 48 percent of U.S. cotton consumption in 1994, up from 37 percent in 1984. Industry experts attribute the growth in these imports primarily to the growing U.S. market for cotton products and lower-priced apparel manufactured in developing countries with low wages. These experts also pointed out that in the absence of quotas and tariffs, cotton imports would probably have increased at an even higher rate, although they could not say by how much.

⁵H.R. Conf. Rep. No. 916, 101st Cong., 2nd Sess., 1155-1156 (1990).

The experts cited several reasons for the increase in cotton imports, even with quotas. First, not all countries are subject to U.S. quotas. Second, countries subject to these quotas vary in the amount of their quota, and the United States has generally agreed to annual increases in the quotas. Third, not all countries fill their quotas. And fourth, when countries do fill their quotas, U.S. retailers and major textile and apparel exporters have become adept at finding alternative sources of supply in countries that have not filled their quotas. The experts also pointed out that current bilateral quotas negotiated under the Multi-fiber Arrangement will be phased out over 10 years under the Uruguay Round agreement, negotiated under the General Agreement on Tariffs and Trade (GATT).⁶

Similarly, as a result of the Uruguay Round agreement, the United States has agreed to slightly reduce textile and apparel tariffs to an average of 15 percent over 10 years. However, experts note that tariffs—currently an average of 17 percent of the value of imported apparel—have not prevented cotton imports from increasing even faster than domestic consumption. This increase has occurred because imported apparel apparently has a substantial cost advantage over domestic apparel.

USDA and the USTR Believe That the Cotton Import Assessment Complies With U.S. Trade Obligations

According to USTR's Assistant U.S. Trade Representative for Agricultural and Commodity Policy and officials from the Foreign Agricultural Service's Tobacco, Cotton, and Seed Division in USDA, the assessment on cotton imports complies with the requirements of U.S. trade agreements. The primary guiding principle of these agreements for imports is that of "national treatment," which is established in the GATT, Article III, National Treatment on Internal Taxation and Regulation. This principle holds that imports (1) shall not be subject to internal charges that are higher than those applied to like domestic products and (2) shall be treated, under national laws and regulations, as favorably as like domestic products.

According to USDA documents and our discussions with officials from the Foreign Agricultural Service and the USTR, the implications of the cotton import assessment were discussed during USDA's rule-making process for cotton imports in 1991 and during GATT negotiations during 1992. Officials concluded that the cotton import assessment complies with the principle of national treatment because the assessment imposed on importers is the same as the assessment imposed on domestic cotton producers and the assessment is mandatory for both importers and producers. Furthermore,

⁶The Arrangement Regarding International Trade in Textiles, known as the Multi-fiber Arrangement, has governed world trade in textiles and apparel since 1974. The Multi-fiber Arrangement allows signatories to place quantitative limits, or quotas, on most imports of textiles and apparel.

importers have shared in the growth of U.S. cotton consumption as much as domestic producers, as measured by the increasing import share of the U.S. market.

During 1991 and 1992, some major importers and foreign countries objected to the U.S. imposition of the check-off assessment on cotton imports. They contended that such an assessment is a nontariff trade barrier, which is contrary to the GATT's overall objective of reducing trade barriers and liberalizing trade. Some importers also questioned whether they received benefits from the program comparable to those received by domestic producers. However, the USTR and USDA officials said that they were not aware of any country that had filed a formal challenge to the import assessment with the USTR or the World Trade Organization, the arbiter of international trade disputes. Some experts we talked with suggested that challenges may not have been filed because the amount of money involved is insignificant compared with the value of the trade taking place. Import assessments collected in 1994 totaled about \$14 million, compared with an estimated value of \$19 billion for cotton imports.

USDA and USTR officials also told us that they are not concerned about the possibility that other countries could impose check-off assessments on U.S. exports. They pointed out that check-off programs expand market demand within a country, which can increase U.S. exports to that country. Therefore, as long as countries impose such assessments in line with the principle of national treatment, such assessments could have long-term benefits for U.S. exporters.

Administrative Issues Are Unresolved

USDA has put in place the necessary framework for administering the cotton check-off program as it relates to assessing imports. However, two significant administrative issues concerning the assessment on imported cotton are unresolved. First, importers are paying assessments on products containing U.S. cotton for which assessments have already been paid. To get an exemption from this assessment, importers must document the U.S. cotton content of imported products, as USDA requires. However, because importers find it difficult to provide such documentation, they rarely use this exemption. Second, importers and producers on the Cotton Board disagree over whether the Board has adequately carried out its responsibility to oversee the activities of Cotton Incorporated.

USDA Has Established an Administrative Framework for Assessing Imported Cotton Products

USDA has carried out the activities specified in the 1990 legislation to assess imported cotton products. For example, USDA held a referendum on whether to assess imports and eliminate refunds of assessments. A majority of producers and importers who voted approved assessing imports and eliminating the refund provision. Working with Customs, USDA established procedures for calculating, collecting, and remitting assessments on imported cotton products. USDA also established equivalent assessment rates for imported cotton products; issued relevant orders and regulations governing the program's operations; established procedures for exempting imports containing U.S. cotton; and provided for the representation of cotton importers on the Cotton Board.

Appendix II contains detailed information on the administrative requirements for imports set forth in the 1990 amendments and on the actions taken by USDA to implement them.⁷

Procedures for Obtaining Exemption From Assessments on U.S. Cotton in Imported Products Are Difficult to Comply With

The 1990 act required USDA to establish procedures to ensure that the domestic cotton used in imported products has been subject only to the one assessment provided for by law and that the assessment has not been paid twice—once when the raw U.S. cotton was sold and again when the same cotton was used in imported textiles and apparel. In response to the statute, USDA and the Cotton Board have developed procedures under which importers can be exempted from the assessment if they can document the domestic cotton content of the articles they import.

However, generally cotton importers cannot readily obtain the information needed to document the amount of U.S. cotton in imported products because U.S. cotton is not easily identifiable in imported products. For example, foreign mills may import U.S. cotton and combine it with cotton from other countries to produce cotton products. These products may then be shipped to factories and mixed with other cotton textiles before the final product is exported to the United States.

⁷In December 1995, USDA's Office of Inspector General issued a report on AMS' and the Cotton Board's administration of the cotton research and promotion program (Audit Report No. 01099-1-At, Dec. 7, 1995). The report stated that AMS and the Cotton Board generally performed their responsibilities in accordance with the Cotton Research and Promotion Act and Order. The Office of Inspector General also reported that the import assessments collected by Customs differed each month from the amounts paid to AMS and transmitted to the Cotton Board. For a 2-year period, reported collections exceeded payments to AMS and the Cotton Board by about \$500,000. The Office of Inspector General recommended that AMS work with Customs to develop procedures for reconciling and resolving monthly differences between the collections reported and the collections paid to AMS and the Cotton Board.

With this complicated flow of cotton products, importers generally cannot document at a reasonable cost which products contain U.S. cotton. Importers, who are primarily retailers, note that the country of origin of the raw cotton contained in their products has generally not been of interest to them and therefore they do not collect such information. Consequently, some importers are paying more in assessments than they should. Using USDA's Economic Research Service data on the U.S. cotton content in imported cotton products, we estimated that importers are paying import assessments of about \$2.1 million annually on cotton products containing U.S. cotton, which should be exempt from the assessment.⁸

USDA considered alternatives to use in place of requiring documentation during the rule-making process but decided that they were either inequitable or not practicable. One alternative proposed was an across-the-board reduction in the import assessment rate. USDA believes this alternative disproportionately benefits countries that manufacture cotton products with little U.S. cotton. The other alternative was to adjust the import assessment rate for each country on the basis of the estimated amount of U.S. cotton used in manufacturing cotton products exported to the United States. Customs believes that maintaining different assessment rates for each exporting country is not administratively practicable. Recognizing that the current approach results in double assessments on U.S. cotton, the Cotton Board is exploring the possibility of identifying which foreign mills use mostly U.S. cotton as a way to help learn which imported products contain significant amounts of U.S. cotton.

Importers and Producers Disagree Over the Cotton Board's Oversight Role

While producers are generally satisfied with the Cotton Board's efforts to oversee Cotton Incorporated, importers are more critical. In fact, one importer who was a member of the Board's executive committee resigned from the Board in February 1995, charging that its oversight was inadequate. Importers we spoke with contend that the Cotton Board has relinquished its fundamental oversight responsibility and left important management decisions to Cotton Incorporated. However, by statute, importers are excluded from Cotton Incorporated's board of directors, thereby leaving importers' interests unrepresented.

⁸The Economic Research Service estimated in 1993 that the U.S. cotton content in imported cotton textiles and apparel totaled about 968 million pounds out of total cotton imports of about 3.6 billion pounds. About 42 percent of the 968 million pounds of U.S. cotton was contained in textiles and apparel assembled in Mexico and Caribbean countries. These assembled cotton products from Mexico and the Caribbean are apparently easily identified as containing U.S. cotton; the other 58 percent of the U.S. cotton was contained in textiles and apparel imported from other countries that cannot be easily identified, according to importers.

More specifically, importers argue that the Cotton Board's current procedures for approving Cotton Incorporated's proposed budget amount to "rubber stamping." They contend that budget submissions do not contain sufficient detail for adequate review. For example, they cite an event that came to their attention only by accident—an annual, one-night public relations event costing an estimated \$370,000, which was not identified in the 1995 budget. Importers questioned whether the budget contains other such unidentified items that the Cotton Board should be aware of.

Furthermore, these importers said that the Cotton Board's meetings to review the budget are not conducive to raising "tough-minded, business-oriented" questions about the budget. They attributed this situation, in part, to the fact that the members of both Cotton Incorporated's board of directors and the Cotton Board are producers nominated by the same state associations. Therefore, producers on both boards know each other. Also, over the course of a few years, former members of Cotton Incorporated's board of directors may serve on the Cotton Board and vice versa. Equally important, the expertise and experience needed to carry out the cotton check-off program reside primarily with the staff of Cotton Incorporated. For these reasons, the Cotton Board is inclined to accept the plans and budgets submitted and approved by Cotton Incorporated.

Producers we spoke with are generally satisfied with the Cotton Board's oversight and do not see the need to "micromanage" the check-off program, which they believe has had a clear record of success. However, producers also recognize that the Board's oversight could be strengthened. Therefore, as suggested by the importers, the Cotton Board has agreed to have an outside contractor conduct an overall evaluation of the program. The Board has also agreed to hold a 1-day meeting to begin developing a long-term plan that sets out goals and priorities to guide Cotton Incorporated's activities. While importers are willing to participate in these efforts, they still believe that producers have not addressed the need for the Cotton Board to play a more assertive role in carrying out its oversight responsibility. In addition to an improved planning process, importers would like to see the Board develop a budget process that allows more time and opportunity to ask in-depth questions about budget expenditures.

These differences between producers and importers could make it difficult to achieve the confidence in and support for the program that the Congress has recognized as essential to the continued operation of

check-off programs. With reference to all such programs under which imports are assessed, in section 1999S(a) of the 1990 Farm Bill, the Congress found that:

“(6) the producers and importers that pay assessments to support the programs must have confidence in, and strongly support, the checkoff programs if these programs are to continue to succeed; and

“(7) the checkoff programs cannot operate efficiently and effectively, nor can producer confidence and support for these programs be maintained, unless the boards and councils faithfully and diligently perform the functions assigned to them under the authorizing legislation.”

Because the cotton check-off program is industry-funded and -operated, AMS has found it to be more effective for the industry than for AMS to assume primary responsibility for deciding how to strengthen the Cotton Board’s oversight role. AMS officials said that they have consciously decided to focus on guiding rather than prescribing the efforts of the Cotton Board to strengthen its oversight. For example, AMS program officials met with the Cotton Board and Cotton Incorporated to discuss the need for more useful and detailed budget information. This approach resulted in an improved budget report for fiscal year 1995. In addition, consistent with its approach of guiding the industry’s efforts, AMS, in October 1995, called for a meeting of the Cotton Board, including staff and representatives of producers and importers, to help resolve the conflict between importers and producers. AMS envisions this meeting, which may be held in early 1996 at the start of the annual budget process, as an opportunity to chart a course of action to better integrate importers into the check-off program.

Even if the Cotton Board exerts more oversight, finding common ground between the producers and importers will be difficult. The major importers are large retailers who do extensive brand-name advertising and see little benefit from the research and promotion program’s generic advertising. Importers generally did not want to participate in the program—61 percent of the importers voting in the 1991 referendum opposed the assessment on cotton imports. Also, importers, who are outnumbered 5 to 1 on the Cotton Board and are not represented at all on Cotton Incorporated’s board of directors, find it difficult to influence the program’s direction.

Nevertheless, importers told us that they are willing to work with producers to develop an efficient and effective cotton program. However, importers also told us that they would have more influence over the program's direction and their interests would be better served if they were represented on the board of directors of Cotton Incorporated. AMS officials, producers, the president of the Cotton Board, and the president of Cotton Incorporated told us that they would have no objection to having importers on Cotton Incorporated's board of directors, but they noted that the authorizing legislation would have to be revised to allow this representation.

Conclusions

The cotton check-off program's promotion efforts have probably contributed to cotton's growth in the U.S. market. In addition, the U.S. consumption of cotton and the import share of the U.S. cotton market continued to increase following the imposition of the assessment on imported textiles and apparel. The value of this assessment—about one-half cent for a man's cotton shirt—is not likely to slow consumer demand for cotton. Furthermore, this assessment is in accordance with U.S. international trade agreements, according to USDA and USTR officials.

While USDA has established an administrative framework for assessing imported cotton, two major issues raised by importers have yet to be resolved. The first of these issues—double payments on assessments—may be addressed to some extent by current efforts to identify foreign mills that use a significant amount of U.S. cotton. The second issue, however, is more difficult to resolve—the extent of the Cotton Board's oversight over Cotton Incorporated. While the Cotton Board and AMS are taking steps to address this issue, these efforts do not deal with importers' lack of representation on Cotton Incorporated's board of directors. Neither producers nor AMS officials object to including importers on Cotton Incorporated's board of directors. However, the legislation authorizing the program must be amended to allow such representation. But even if this issue is resolved, developing a cooperative working relationship between producers and importers will be difficult, given their fundamentally different perspectives on the program.

Objectives, Scope, and Methodology

To conduct this review, we analyzed data from USDA's Economic Research Service on U.S. cotton consumption and imports of textiles and apparel for 1984-95. We discussed the results of our analysis and related issues with knowledgeable officials, including USDA's Chief Economist and the

president of the Cotton Board. We also spoke with staff from the International Cotton Advisory Committee, the Department of Commerce's Office of Textiles and Apparel, and the U.S. International Trade Commission. We discussed U.S. international trade obligations with staff of USDA's Foreign Agricultural Service and the USTR. Furthermore, we reviewed the relevant legislation and USDA's orders and regulations pertaining to the cotton check-off program and other relevant documents and studies.

To provide information on the administration of the cotton check-off program for imports, we discussed the program's administration and related issues with officials of USDA's Agricultural Marketing Service and Customs. We also discussed the program's administration with the president, the chairman, and the treasurer of the Cotton Board; the president of Cotton Incorporated and the chairman of its board of directors; and representatives of importers on the Cotton Board. We reviewed relevant legislation, regulations, orders, the memorandum of understanding between USDA and Customs, and studies of the cotton check-off program. We also discussed various legal issues with USDA's Assistant General Counsel for Marketing.

We performed our work between July 1995 and December 1995 in accordance with generally accepted government auditing standards.

Agency Comments and Our Evaluation

We provided copies of a draft of this report to AMS for its review and comment. We met with AMS' Cotton Division officials, including the Director, Deputy Director, and Chief of the Research and Promotion Staff. These officials generally agreed with the information discussed and provided some clarifying comments that we have incorporated into the report where appropriate.

As agreed with your offices, unless the contents of this report are publicly announced earlier, we plan no further distribution of this report until 7 days from the date of this letter. At that time, we will send copies of this report to the Secretary of Agriculture and other interested parties. Copies will also be made available to others upon request.

Please contact me at (202) 512-5138 if you or your staff have any questions. Major contributors to this report are listed in appendix III.

A handwritten signature in black ink that reads "Robert A. Robinson". The signature is written in a cursive style with a large, stylized initial "R".

Robert A. Robinson
Director, Food and
Agriculture Issues

List of Recipients

The Honorable Richard G. Lugar
Chairman

The Honorable Patrick J. Leahy
Ranking Minority Member
Committee on Agriculture,
Nutrition, and Forestry
United States Senate

The Honorable William V. Roth, Jr.
Chairman

The Honorable Daniel Patrick Moynihan
Ranking Minority Member
Committee on Finance
United States Senate

The Honorable Pat Roberts
Chairman

The Honorable E (Kika) de la Garza
Ranking Minority Member
Committee on Agriculture
House of Representatives

The Honorable Bill Archer
Chairman

The Honorable Sam Gibbons
Ranking Minority Member
Committee on Ways and Means
House of Representatives

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Abbreviations

AMS	Agricultural Marketing Service
ERS	Economic Research Service
GATT	General Agreement on Tariffs and Trade
HTS	harmonized tariff schedule
USDA	U.S. Department of Agriculture
USTR	U.S. Trade Representative

Examples of Calculations of Cotton Import Assessments

This appendix contains two examples of how (1) the import cotton assessment is calculated (including the conversion from pounds to kilograms) and (2) an assessment on a sample cotton import shipment is calculated.

Calculation of the Total Assessment on Imported Cotton Products

The per-kilogram assessment represents the sum of the assessment and the supplemental assessment. An example of how the assessment is calculated follows:

- One bale = 500 pounds
- One kilogram = 2.2046 pounds
- One pound = 0.453597 kilograms

The \$1-per-bale assessment is converted to kilograms:

- A 500-pound bale = 226.8 kilograms (500 x 0.453597)
- The \$1-per-bale assessment = \$0.002000 per pound (1/500) or \$0.004409 per kilogram (1/226.8)

The supplemental assessment of 5/10 of 1 percent of the value of the cotton is converted to kilograms:

- Average price received = \$0.683 per pound or \$1.5057 per kilogram (0.683 x 2.2046)
- 5/10 of 1 percent of the average price in kilograms = \$0.007529 per kilogram (1.5057 x 0.005)

The two assessments are added to obtain the total assessment per kilogram:

\$1-per-bale assessment	\$0.004409
Supplemental assessment	\$0.007529
Total assessment per kilogram	\$0.011938

Calculation of the
Assessment on a
Shipment of Imported
Cotton

Men's cotton knit pullover (116 dozen or 1,392 shirts)
HTS (harmonized tariff schedule) number 6110.20.2065

Total value of shipment = \$13,325
Tariff at 20.3 percent = \$2,705 ($\$13,325 \times 0.203$)
Cotton check-off assessment = \$10.14

The cotton check-off assessment is calculated as follows:

Weight of shipment = 734 kilograms
Conversion factor = 1.1574 (applied to determine the raw
cotton fiber content of the shipment)
Total assessment per kilogram = \$0.011938

$734 \times 1.1574 = 849.5316$ kilograms
 $849.5316 \times \$0.011938 = \10.14

Source: Based on information obtained from a Customs entry document provided to GAO by an import broker serving the John F. Kennedy Airport port of entry.

USDA Actions to Implement the Administrative Framework Outlined in the 1990 Amendments

The Cotton Research and Promotion Act Amendments of 1990 set forth administrative implementing procedures for the U.S. Department of Agriculture (USDA) to extend the research and promotion program to cotton imports. Table II.1 lists these procedures and the actions USDA took to implement them.

Table II.1: Administrative Requirements in the Legislation and USDA Action

Administrative requirement in the Cotton Research and Promotion Act Amendments of 1990	USDA's administrative action
Implementing referendum	
<p>Section 1993 (2) —The Secretary of Agriculture shall, within a period not to exceed 8 months after the date of enactment of the act, conduct a referendum among cotton producers and persons that are cotton importers to ascertain if a majority of those voting approve the proposed amendment to the order.</p>	<p>USDA held an implementing referendum during July 17-26, 1991. The proposed amendment was approved by a majority (60 percent) of the importers and producers voting in the referendum. Results were announced in a nationally distributed press release on August 2, 1991.</p>
Assessment on imported cotton products	
<p>Section 1992 (3) — If the proposed amendment of the order implementing the Cotton Research and Promotion Act Amendments of 1990 is approved in the referendum, each importer shall pay assessments on imported cotton products.</p>	<p>USDA's final rule was published in the Federal Register (57 FR 29181) on July 1, 1992. The rule provided for Customs to collect assessments on cotton and cotton products imported into the United States on or after July 31, 1992.</p>
Termination of refunds to producers	
<p>Section 1996 (2) —The right of a producer to demand a refund shall terminate if the proposed amendment of the order implementing the Cotton Research and Promotion Act Amendments of 1990 is approved in the referendum. Such right shall terminate 30 days after the date the Secretary of Agriculture announces the results of such referendum if such amendment is approved. Such right shall be reinstated if the amendment should be disapproved in any subsequent referendum.</p>	<p>The actual elimination of assessment refunds to cotton producers became effective on September 1, 1991, 30 days after USDA announced the results of the July 1991 referendum.</p>

(continued)

**Appendix II
USDA Actions to Implement the
Administrative Framework Outlined in the
1990 Amendments**

**Administrative requirement in the Cotton Research and
Promotion Act Amendments of 1990**

USDA's administrative action

Importers' representation on the Cotton Board

Section 1992 (2)(B)—An appropriate number of representatives, as determined by the Secretary of Agriculture, of importers of cotton on which assessments are paid, will serve on the Cotton Board. The importers' representatives shall be appointed by the Secretary of Agriculture after consultation with organizations representing importers, as determined by the Secretary.

USDA's final rule amending the regulations for Cotton Board membership was published in the Federal Register (56 FR 65929) on December 20, 1991. The rule provided for an initial representation on the Cotton Board of four importers. In addition, the rule stated that additional importer members could be added to the Cotton Board after consultation by the Secretary with importer organizations and after consideration of the average annual volume of imported cotton that would be subject to assessment for 5 preceding years.

In June 1995, four organizations represented importers: (1) United States Association of Importers of Textiles and Apparel, (2) United States Apparel Industry Council, (3) American Association of Exporters and Importers, and (4) American Import Shippers Association.

Import assessment rate comparable to domestic producer rate

Section 1992 (3)—The rate of assessment on imports of cotton shall be determined in the same manner as the rate of assessment per bale of cotton handled, and the value to be placed on cotton imports for the purpose of determining the assessment on such imports shall be established by the Secretary of Agriculture in a fair and equitable manner.

USDA's final rule, published in the Federal Register (57 FR 29181) on July 1, 1992, established a rate of assessment for imported cotton and cotton products that is the same, on a raw-cotton-equivalent basis, as the rate imposed on domestically produced cotton.

De minimis amount not subject to assessment

Section 1997 (1)(B)—Imported cotton shall not be assessed for any entry having a weight or value less than any de minimis figure as established by regulations. The de minimis figure that is established should minimize the burden in administering the import assessment but still provide for the maximum participation of imports of cotton in the assessment provisions of the act.

Section 1205.510 (b)(3) of USDA's final rule established a de minimis value of \$220.99 per line item on Customs entry documentation. Any line item entry in which the value of the cotton contained therein is less than \$220.99 is not subject to the assessment.

Procedures to ensure cotton content of imported products is not subject to more than one assessment

Section 1992 (3)—The Secretary shall establish procedures to ensure that the upland cotton content of imported products is not subject to more than one assessment.

Section 1205.510 (b)(5) and (9) of USDA's final rule (FR 29181, July 1, 1992) automatically exempts textile articles assembled abroad in whole or in part of fabricated components, produced in the United States and articles imported into the United States after being exported from the United States for alterations or repairs.

Section 1205.510 (b)(6) of USDA's final rule allows imported cotton and cotton products, which contain U.S.-produced cotton or cotton other than upland cotton, to be exempted by the Cotton Board.

Section 1205.520 of USDA's final rule allows each importer of cotton or cotton-containing products to obtain a reimbursement on that portion of the assessment that was collected on cotton produced in the United States or cotton other than upland cotton.

(continued)

Appendix II
USDA Actions to Implement the
Administrative Framework Outlined in the
1990 Amendments

Administrative requirement in the Cotton Research and Promotion Act Amendments of 1990

USDA's administrative action

Reimbursement of federal agencies' costs

Section 1992 (3)—The order shall provide for reimbursing the Secretary of Agriculture for up to \$300,000 in expenses incurred in connection with any referendum, and for up to 5 employee years in administrative costs after an order or amendment thereto has been issued and made effective. The order shall also include a provision for reimbursing any agency in the federal government that assists in administering the import provisions of the order for a reasonable amount of the expenses incurred by that agency.

In 1993, USDA billed the Cotton Board for about \$128,000 in reimbursable costs (which included first year start-up costs of almost \$45,000) associated with collecting import assessments on cotton products. In November 1995, Customs reported costs of about \$56,000 for fiscal years 1994 and 1995.

Required reports from USDA and Customs

Section 1998—Not later than 1 year after imported cotton products are subject to assessment, (1) the Secretary of Agriculture was required to prepare a report concerning the implementation and enforcement of the cotton check-off program and any problems that may have arisen in the implementation and enforcement as it relates to imports and (2) the Customs Service was required to prepare a report concerning its role in the implementation and enforcement as it relates to imports.

In August 1993, USDA submitted its report to the Congress.

Customs officials were not able to determine whether the agency had prepared such a report.

USDA 5-year review of import program

Section 1993 (2)—After the implementing referendum is held, the Secretary of Agriculture will conduct a review once every 5 years to ascertain whether another referendum is needed to determine whether producers and importers favor continuation of the amendment provided for in the Cotton Research and Promotion Act Amendments of 1990. The Secretary is required to make a public announcement of the results of the review within 60 days after each fifth anniversary date of the referendum.

Results of Secretary of Agriculture's review are scheduled to be announced by September 1996.

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