AGRICULTURAL MARKETING SERVICE
USDA

RE: MILK IN THE NORTHEAST AND
OTHER MARKETING AREAS

{AO-14-A74, et al.; DA-06-01

COMMENTS AND EXCEPTIONS TO THE TENTATIVE FINAL DECISION

SUBMITTED BY

LACTALIS AMERICAN GROUP

January 18, 2007

Hearing Clerk
Stop 9200-Room 1031
US Department of Agriculture
1400 Independence Ave. SW
Washington, DC 20250-9200S

These comments and exceptions are being filed by Lactalis American Group, Inc. (Lactalis), a cheese making company with three milk manufacturing plants purchasing milk regulated by the Federal Milk Marketing Order system.

We were extremely disappointed with the referenced Tentative Decision. In fact we found the Decision to be insulting to the cheese plants in this country that purchase milk regulated by the Order system.

A Lactalis representative testified at the Hearing in January that costs of making cheese in a New York plant had increased 14 percent from 1998 to 2005, even after expanding the plant to improve efficiencies, and based on existing conditions at that time expected even greater increases in 2006. Other cheese plant representatives testified in much the same manner. In fact there was no credible testimony that refuted the statements regarding the significant increased manufacturing costs since the manufacturing allowance was made a part of the federal order pricing system

The Secretary decided, even with the overwhelming testimony regarding the need to increase the make allowance and to do so quickly, to delay the hearing until further evidence was available from a study to be done by Cornell University.

The Cornell researcher testified that in his opinion, the correct cost of making a pound of cheese based on his study, adjusting the results to obtain a weighted average cost, was \$0.2028. That finding was consistent with testimony received in the January hearing and was also consistent with the CDFA and RCBS information entered into the record.
It was extremely disheartening to read the Tentative Decision which raised the cheese make allowance by less then two percent when considering all the evidence that costs had increased by a much greater percentage in the time since the original factors had been implemented.

While we understand that milk prices to dairy farmers have not been exceedingly high, we also understand that milk prices are a function of supply and demand. Should the resulting prices from a reasonable manufacturing allowance be below the price that will result in an adequate supply of milk, the milk prices will increase rapidly as seen in 2004 when the class III milk price exceeded \$20 at one point.

Milk producers will be the beneficiaries of higher milk prices if supply/demand conditions warrant higher prices. In fact, based on the current international dairy situation, milk producers are pretty well assured of significantly higher milk prices this year as compared to prices in 2006. Due to the circularity of the milk pricing formula, butter/powder and cheese plants do not benefit by improved supply/demand conditions.

Based on current Order provisions, cheese plants have little opportunity to improve their profitability by raising prices to their customers. Doing so only increases the cost of their raw material necessary to make the cheese. Regulation is putting cheese manufacturers at a competitive disadvantage to cheese manufacturers obtaining milk not covered by federal order pricing. A large portion of cheese made in the U.S. today is made in areas not covered by federal order regulation. Cheese plants in those areas have lower milk costs as they have adjusted (in some cases through state regulation) their milk prices to reflect the higher manufacturing costs experienced in recent years.

Everyone understands that the Department, in nearly all cases, cannot move quickly to deal with changing conditions. That fact should mean that order regulations should be as un-intrusive as possible and allow the industry more latitude to deal with those quick changing market conditions. In addition, cheese manufacturers understand they cannot run cheese plants without milk and in many cases pay well over the minimum federal order class price to assure themselves an adequate supply. The manufacturing allowance should reflect a ***minimum*** price and let the market determine the ***effective*** price.

Lactalis American Group, Inc. hereby requests that the Secretary reconsider the proposed make allowance for cheese and follow the recommendations of the Cornell study to use a $0.2028 make allowance factor for cheese.

Federal order regulations should not be designed to put plants purchasing milk regulated by the federal order system at a disadvantage to those purchasing non-regulated or state regulated milk. Using the proposed make allowance of only $0.1682 will seriously jeopardize the financial health of the cheese making industry in much of the country and will ultimately be more detrimental to milk producers if they are unable to continue to operate due to inadequate returns.

Respectfully,

Rodney K. Carlson
Corporate Director: Milk Procurement
Lactalis American Group, Inc.