UNITED STATES DEPARTMENT OF AGRICULTURE

BEFORE THE SECRETARY OF AGRICULTURE

AGRICULTURAL MARKETING SERVICES

POST HEARING BRIEF OF AGRI-MARK, INC.

April 1, 2024

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I. Introduction

This post-hearing brief is submitted on behalf of Agri-Mark, Inc. a dairy cooperative owned by nearly 500 dairy farm families in New England and New York. Our members are pooled in Federal Order 1. Our cooperative has been marketing milk for dairy farmers since 1916 and has headquarters in Andover, Massachusetts and in Waitsfield, Vermont. Our farm families supply more than 3.2 billion pounds of milk annually that we use to make our award-winning Cabot and McCadam branded cheeses, dairy products, and ingredients. Agri-Mark operates three cheese manufacturing facilities in Cabot, Vermont; Middlebury, Vermont, and Chateauguay, New York. All three are pooled supply plants. At our Middlebury, Vermont facility we also produce valuable whey proteins that are marketed around the world. Agri-Mark operates a butter-powder facility in West Springfield, Massachusetts that is a non-pooled supply plant. Lastly, Agri-Mark supplies fresh fluid milk to the region's largest dairy processors.

A. Memberships

As a farmer-owned cooperative with ownership of manufacturing facilities, Agri-Mark's interests are diverse, and aligned with many of the voices heard during the hearing. Agri-Mark maintains membership in several of the associations that participated in the recent Federal Milk Marketing Order (FMMO) Hearing, including the National Milk Producers Federation (NMPF), the International Dairy Foods Association (IDFA) and the Wisconsin Cheesemakers Association (WCMA). Additionally, Agri-Mark holds memberships with two state Farm Bureaus and many of our member-owners are members of Farm Bureau in the seven states where our farmers reside. As such, Agri-Mark and its members took an active role in the development of the proposals submitted at the hearing, both directly and indirectly.

B. Position Background

Agri-Mark participated directly in NMPF's Task Force focused on FMMO modernization. The Task Force was made up of experts from 15 other dairy cooperatives who spent nearly two years researching, reaching consensus, and developing an FMMO modernization proposal. At the hearing, Agri-Mark testified in support of all aspects of the comprehensive NMPF FMMO modernization proposal, on five separate occasions.

C. Focus of Brief

Agri-Mark submits this brief to highlight the importance and stress the urgent need to update make allowances in the Class III and IV formula factors. Our focus on make allowances is not intended to discount the significance of the other aspects of the hearing, which are valuable to our farmer-owners. Yet, it is critical that our farmers' decades-long investment in manufacturing assets be protected by increasing FMMO make allowances in the Class III and IV formulas to levels that are reflective of current costs of manufacturing.

Today's outdated make allowances are creating financial losses at Agri-Mark, which are being passed on to our member-owners as re-blends in their milk checks. Because these losses are not felt equally across cooperatives, outdated make allowances have created disorderly marketing conditions within our milkshed and marketplace. Agri-Mark's ability to compete in Federal Order 1 is significantly and negatively impacted due to this effect. (Exhibit-NMPF-70, page 2), (Exhibit-NMPF-20, page 2)

D. Urgency

Current make allowances are extremely out of date, and the industry needs an interim fix. The record shows there is broad industry agreement to develop a better process of data acquisition in the future. However, we cannot wait for Congress to mandate audited make allowance surveys. The sense of urgency is widespread, but particularly crucial to cooperatives with Class III and Class IV manufacturing assets. These cooperatives, including Agri-Mark, struggle to maintain profitability while paying members minimum announced milk prices. These cooperative members face financial burdens beyond those without manufacturing assets. A make allowance update is required to return to orderly markets. We must not let our aspirations for perfection get in the way of progress.

II. Make Allowance

FMMOs are intended to meet several objectives, including promoting orderly milk marketing. Through end-product pricing, raw milk prices are determined via a series of economic formulas. If any aspect of those economic formulas is not reflective of the marketplace, the resulting calculated prices will be unsuitable, and disorderly marketing may occur. Make allowances are a critical component of our current end-product pricing system and represent the cost of manufacturing raw milk into commodity products. They are the prime example of outdated formulas in the Federal Order prices causing disorder. While make allowances have remained fixed for sixteen years, actual manufacturing costs have risen. The result of today's outdated make allowances is a Federal Order system that is not deriving minimum prices. Instead, these prices are overvalued and sending the wrong market signals. If we are to continue to utilize end-product pricing to establish minimum Federal Order prices, make allowances must accurately reflect today's manufacturing costs. (Exhibit-NMPF-20, page 2)

A. Outdated Make Allowances Wreak Havoc on Orderly Markets

When make allowances are set too low, and FMMO minimum prices are overvalued, commodity manufacturers with no ability to increase prices struggle to pay these prices. The devastation requires those impacted to adopt individual solutions to mitigate financial loss and avoid risk of failure. These solutions may include lack of investment including delayed maintenance, investing in non-commodity products, reducing over-order premiums or additional de-pooling, or in the case of manufacturing cooperatives, passing along losses to member-owners in the form of re-blends.

Focusing specifically on cooperatives, these individual solutions may work in the short-term, but in the long-term they place burdens on manufacturing cooperatives, while benefiting those without ownership of Class III and IV assets. This experience is well documented in the record, including in NMPF's testimony on Proposal 7.

> *"When Federal Order make allowances are established at levels below the costs of producing commodity dairy products, farmers whose cooperatives own and operate balancing plants end up absorbing costs that other market participants do not experience but benefit from the orderly marketing system enabled by the cooperatives operating milk balancing plants. As cooperatives pass the marketwide service-related balancing losses to their members via reduced pay prices, producers shipping to cooperatives and other handlers that do not operate balancing plants do*

> *not experience these lower pay prices.* ***This unfairly penalizes dairy cooperative members who invest in plant and marketing systems to support orderly marketing."*** (Exhibit-NMPF-12, pages 6-7)

These "unfairly penalized" dairy cooperative members experience this market disorder when receiving re-blends that spread the cooperative's losses to its members, while those who do not own manufacturing assets reap the benefits. The record shows multiple accounts from cooperatives experiencing this type of disorder in the marketplace.

Agri-Mark is one of those cooperatives. Agri-Mark's Chairman James "Cricket" Jacquier, states in his testimony (Exhibit-NMPF-70, page 2) that *"today's inadequate make allowances have created a reality in which* ***some farmers are already receiving reduced pay prices compared to their neighbors****. This inequity goes directly against the fundamentals of the FMMO by creating disorderly markets."*. On page 2 of his testimony, Mr. Jacquier goes on to say:

> *"…today's outdated make allowances have forced solutions within our cooperative. The increase in costs has been transferred to members via lower returns and pay prices adjustments. It is hard to watch as we've been backed into a corner, having to make decisions that impact our members.* ***When these impacts are different than our neighbors, our competitiveness within the milkshed becomes tarnished****. We must update make allowances at the FMMO level. This will alleviate the mismatched pressure placed on cooperatives, thereby helping to return to the orderly markets FMMOs were intended to protect."* (Exhibit-NMPF-70, page 2)

The record shows that this experience is widespread throughout the Orders. Northwest Dairy Association's testimony states that:

> *"Additionally, and not unlike other cooperatives across the United States, we have needed to implement a producer paycheck deduction to help balance the books for these continued cost challenges. The continued challenges to pay our members the Federal Order Minimum price and to show a profit to reinvest in our plants as well as position manufacturing plants and balancing plants near milk supply sources casts a dark shadow over the cooperative in the eyes of our membership and puts strain on member's financials. However, our membership and board understand the value to reinvest into these facilities for the next generation, but it has put our cooperative at a significantly higher level of financial risk and strain."* (Exhibit-NMPF-19, page 2)

Land O'Lakes states in their testimony that:

> *"It is clear that commodity manufacturing plants, especially those that are tasked with balancing milk supply and demand, struggle to make a profit since the effect of undervalued make allowances is to overvalue milk prices. This leads to a lack of investment in manufacturing capacity. At the same time,* ***losses on existing plants are shouldered by producers that have made the decision to invest in commodity processing assets, creating inequitable pay prices for those producers****, which has been established in past decisions as a form of disorderly marketing.* ***The costs of maintaining the market balancing facilities must be borne by the market, not only by the owners of the facilities****."* (Exhibit-NMPF-14, pages 9-10)

Lastly, Maryland and Virginia Milk Producers Cooperative testified to the following:

> "… we believe cooperatives like ours, who made the necessary investments in manufacturing plants and who provide a valuable balancing service to the marketplace, are over-burdened when the Federal Order make allowances don't properly reflect the cost of converting raw milk

to storable commodities. Consequently, we believe that cooperatives like ours won't continue to make further investments in manufacturing either to upgrade current facilities or invest in new technologies without some cost adjustment. As a result, the whole marketplace will suffer without an increase." (Exhibit NMPF-23, pages 4-5)

B. Areas of Agreement: There is a problem.

National Milk Producer's Federation (NMPF), International Dairy Foods Association (IDFA), Wisconsin Cheese Makers Association (WCMA) and American Farm Bureau Federation (AFBF) have all agreed that costs of manufacturing have increased, disorderly marketing is occurring and a change to the make allowances is critical. All four associations agree that the negative consequences of not updating make allowances put the success of the dairy industry at risk.

C. Areas of Agreement: Future Process

The four associations also conclude that today's current mechanism of collecting the data necessary to show USDA that a change in make allowances is warranted, is not sustainable for the future. The three agree that a new mechanism is necessary. This mechanism is to give USDA the authority to conduct mandatory and auditable cost of processing surveys every 2 years.

Agri-Mark supports NMPF, IDFA and AFBF's joint legislative effort to provide USDA with the authority to conduct mandatory and auditable costs of processing surveys every two years. Granting USDA this authority legislatively will provide a robust, accurate and timely source of processing cost data for the industry to evaluate on a consistent basis. Hearing requests can be made if the survey data suggests make allowances may be unrepresentative of actual processing costs.

In the absence of this data, maintaining accurate FMMO pricing is a challenge. With widespread industry support for this effort, we are confident that this authority will be granted. Having published and audited processing cost data derived from mandatory surveys, will position the industry to make more educated recommendations on make allowances in the years to come. Further, this will assist USDA in future data-driven decisions, giving confidence to not only USDA, but to the industry and farmers, that Federal Order prices are based on sound science and reflective of reality.

D. Areas of Disagreement: Level

The record shows ample testimony and data supporting the undeniable trend that costs of manufacturing have undoubtedly increased since the last update in 2008. However, the record shows differences in opinion as to what the level of that increase should be.

a. IDFA/WCMA

Proposals 8 and 9 from IDFA and WCMA utilize data from two separate sources to derive their recommended values. Their proposals are a weighted average of these two data sources.

The first source is Dr. Mark Stephenson's 2022 Cost of Processing survey. Dr. Stephenson has a long history of conducting cost of processing surveys for the industry and USDA. Dr. Stephenson's work was the basis of the last two make allowance increases. The 2023 survey had the largest participation of any of his surveys, with half of participants being cooperatives. Agri-Mark was one of those participants.

The second source of cost of processing data came from a regression analysis conducted by Dr. Bill Shiek of the Dairy Institute of California. The analysis utilized data from the California Department of Food & Agriculture (CDFA) cost of processing surveys from 2003-2016, which was an audited source of state-level data. CDFA data has also informed USDA decisions in past make allowance hearings.

The average of the two data sources, plus an additional $0.0015 for marketing costs, form the basis of the IDFA/WCMA proposals. Proposals 8 and 9 show an average increase in make allowances from 2008 to 2022 of 56% (62% for butter, 42% for cheese, 62% for nonfat dry milk, and 59% for dry whey). In recognition of the substantial increase and the subsequent shock these increases would send to dairy farmers, Proposals 8 and 9 implement their 2022 cost values over the course of four years. Year 1 would cover half of those increases (equivalent to an average 28% increase), and the remaining half would be split over the following three years. (Exhibit-IDFA-6)

b. NMPF

NMPF's Proposal 7 makes modest increases to the make allowances within the component price formulas as follows:

- Butterfat From $0.1715 to $0.21 per pound of butter.
- Nonfat Solids From $0.1678 to $0.21 per pound of nonfat dry milk.
- Protein From $0.2003 to $0.24 per pound of cheddar cheese.
- Other Solids From $0.1991 to $0.23 per pound of dry whey.

Admittedly, NMPF's proposal only partially addresses the increase in manufacturing costs many of its cooperatives have incurred over the last sixteen years. Instead, NMPF's proposal is "directionally correct" (Exhibit-NMPF-12, page 7). The proposal is an interim solution, intended to recognize the imperfect data available, provide some financial relief to manufactures, all while ensuring a reasonable producer impact. Proposal 7 coincides with the industry's legislative efforts to conduct future cost of processing studies.

Several cooperatives, including Agri-Mark, supported Proposal 7. They did so with acknowledgement that from a pure manufacturing perspective, NMPF's proposed make allowances are not adequate and will not cover the full increase in costs of processing their cooperatives have incurred since 2008. Cooperatives must always balance the needs of their business with the needs of their owners. Manufacturing cooperatives in particular walk a fine line between the financial needs of their manufacturing assets and their member pay prices, and must review both needs in tandem.

c. Cooperative Reports

Several cooperatives testified on the record to their own cooperative's cost increases. The record shows differences in these levels, but again the trend is crystal clear: costs of processing have increased since the last update in 2008.

- Agri-Mark, Inc. reported that the cost of processing across our four plants increased on average 20 percent since 2008. Agri-Mark cited investments to improve efficiencies, but noted increases in cost categories that are market-driven and outside the plants control. Increases were found across all cost categories, with notable increases in the cost of insurance, manufacturing labor and benefits, and repair and maintenance. On a weighted average Class III basis, Agri-Mark saw cost of processing increase 23 percent. On a Class IV basis, the cost of processing increased 17 percent. Agri-Mark noted that the Class IV increases were muted by the West Springfield butter/powder plant shifting from historically being a balancing plant, to running at full capacity in the recent years when milk has been in surplus. (Exhibit-NMPF-20, page 3)
- Land O'Lakes compared their own 2022 category data to those categories in the 2007 Stephenson cost survey. They testified to a 50 percent increase in processing labor and 33 percent increase in utilities costs associated with butter manufacturing costs. For nonfat dry milk manufacturing costs, the increase in processing labor was 38 percent and increase in utilities

costs were 36 percent. Additionally, all other categories for butter and nonfat production increased 112 percent. (Exhibit-NMPF-14, page 3)

- Ellsworth Cooperative Creamery testified that total costs to make barrel cheese have gone up \$0.064 per pound in 16 years (Exhibit-NMPF-15, page 3), while total costs to produce dry whey went up \$0.054 per pound (Exhibit-NMPF-15, page 5). Ellsworth stated support for NMPF's proposal as a starting point.
- Northwest Dairy Association supported NMPF's proposal as being "directionally correct with increased cost to operation of our manufacturing and balancing plants" (Exhibit-NMPF-19, page 1), and reported between 2008 and 2022, their 2022 data showed manufacturing cost increases of over 80 percent. (Exhibit-NMPF-19, page 2)
- Associated Milk Producers, Inc. (AMPI) testified that their cost of manufacturing for cheese was up 47 percent in 2022 as compared to 2008. (Exhibit-IDFA-25, page 4) AMPI listed orderly markets as the need for make allowance increases. In addition, AMPI stated "It also puts the regulated milk costs in greater alignment with the prices paid by the many unregulated competitors we compete against for product sales every day." (Exhibit-IDFA-25, page 5)
- Maryland and Virginia Milk Producers Cooperative testified to a 64 percent increase in their costs to process nonfat dry milk over the last twelve years, and stated that "Because this increased cost cannot be captured in the sale of a commodity product to the marketplace, the only option we have is to place that cost recapture burden as a "market adjustment" on our members' monthly milk statements, which requires that our members absorb the impact of this cost increase…"(Exhibit-NMPF-23, page 4)

E. Plenty of Data

While there is disagreement to what level USDA should set the make allowances at, this variation is not a new phenomenon in Federal Order hearings. The record shows that the data offered in the 2023-2024 hearing is consistent with data USDA has used in past Federal Order decisions, including voluntary cost of processing surveys, mandatory CDFA cost of processing surveys, and most importantly individual manufacturer cost data. The record also shows that USDA has been presented with an abundance of evidence to support the trend that manufacturing costs have increased dramatically. The data may be imperfect, but there is plenty of it to support the trend and warrant a USDA decision.

F. Areas of Disagreement: Urgency

As with the level of the make allowance, there also exists a continuum of opinions on the urgency of implementation of make allowances. However, the record shows that there is a clear winner in this debate, with three of the four major associations (NMPF, IDFA and WCMA) in support of immediate action.

AFBF disagrees and contends that we should make no increases to the make allowances until future and more precise data is available. They conclude that any update to the make allowances must be based on mandatory and audited cost data. AFBF provides no data supporting their reasons for a delay. (Exhibit-AFBF-3, page 4)

While there is widespread industry agreement that a mandatory and audited USDA cost survey is the best and most sustainable option in the future, the urgency of make allowances is of critical importance for the sake of orderly marketing. The consequences of inaction are too great. (Exhibit-IDFA-25, page 5), (Exhibit-NMPF-18, page 2)

We cannot let manufacturing cooperatives and their member-owners continue to face today's unequal financial burdens. A make allowance increase is required to return to orderly markets. We must not get bogged down with aspirations for perfection, in today's imperfect data world. We strive for perfection in the future, but today, we must prioritize progress.

III. Summary

In summary, when it comes to updating the make allowances, the record shows disagreement over the level and urgency by which USDA should make their determination. While the record may not have the perfect data set, it shows an abundance of testimony supporting the trend of increasing manufacturing costs since 2008. The record also shows substantial evidence of inadequate make allowances wreaking havoc on orderly markets. Make allowances must be increased without delayed implementation to restore this order.

The industry agrees and is working together towards a legislative fix to grant USDA the authority to conduct mandatory, auditable plant processing cost studies every two years. It is our goal that this future data source will support the industry in calling for future hearings and give USDA confidence in the data to support future decision making. In the meantime, an interim fix is vital.

Agri-Mark members have invested in their cooperative and manufacturing capacity for over 100 years. We look forward to continuing this legacy and require updated make allowances to do so. We thank USDA for the opportunity to provide a post-hearing brief. We request that USDA's decision on make allowance increases recognize the urgency of the disorder in the marketplace and be implemented as fast as possible.

Respectfully submitted,

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CERTIFICATE OF SERVICE

Milk in the Northeast and Other Marketing Areas
Docket No.: 23-J-0067

Having personal knowledge of the foregoing, I declare under penalty of perjury that the information herein is true and correct, and this is to certify that a copy of the POST HEARING BRIEF OF AGRI-MARK, INC. has been furnished and was served by electronic mail upon the following parties on April 3, 2024 by the following:

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