BEFORE THE UNITED STATES DEPARTMENT

OF AGRICULTURE

AGRICULTURAL MARKETING SERVICE

IN RE:	:	7 CFR Part 1000
Milk in the New England and	:	
Other Marketing Areas	:	Docket No. 23-J-0067
	:	AMS-DA-23-0043

POST-HEARING BRIEF FOR

DAIRY COOPERATIVE MARKETING ASSOCIATION, INC. ("DCMA")

John A. St. Peter, Esq.

Dempsey Law Firm, LLP

Counsel to DCMA

10 Forest Avenue, Suite 200

Fond du Lac, WI 54935

jsp@dempseylaw.com

This National Federal Milk Marketing Order Hearing was called to receive evidence on several proposals to amend the formulae for computing various of the Class Prices under 7 CFR §1000 for all eleven of the current Federal Milk Marketing Orders.

Dairy Cooperative Marketing Association, Inc. (DCMA), a Capper-Volstead Marketing Agency in Common, offers comments and findings and conclusions in favor or Proposal 13, as listed in the Hearing Notice. Proposal 13 seeks to amend the base Class I skim milk price computation in all Federal Milk Marketing Orders. Specifically, the proposal seeks to replace the simple average of the Class III and Class IV Advanced Skim Milk pricing factors with the "higher-of" the two factors, and to remove the additional $0.74 per hundredweight monthly add-on to the "average-of" result. Simply put, Proposal 13 seeks to return the computation of the Advanced Skim Milk Price, commonly referred to as the Class I mover, to the formula existing and used under the Federal Orders for the period of January 2000 through April 2019.

All of DCMA's nine Members are themselves, Capper-Volstead Cooperatives, each qualified to market milk of their dairy farmer members on Federal Milk Marketing Orders. DCMA operates across the southeast region of the U.S., the geographic region most associated with the Appalachian, Florida, and Southeast Federal Milk Marketing Order marketing areas. The Members of DCMA are:

Appalachian Dairy Farmer Cooperative, Inc. Crouse, North Carolina

Cobblestone Milk Cooperative, Inc., Chatham, Virginia

Cooperative Milk Producers, Inc., Blackstone, Virginia

Dairy Farmers of America, Inc., Kansas City, Kansas

LANCO-Pennland Quality Milk Producers, Inc., Hagerstown, Maryland

Lone Star Milk Producers, Inc., Wichita Falls, Texas

Maryland & Virginia Milk Producers Cooperative Association, Inc., Herndon, Virginia

Select Milk Producers, Inc., Artesia, New Mexico

Southeast Milk, Inc., Belleview, Florida

DCMA supports Proposal 13 as listed in the Hearing Notice, the return of the computation of the Advanced Class I skim milk price to the "higher-of" the Class III advanced skim milk price, or the Class IV advanced skim milk price. The current "average-of" the Class III advanced skim milk price and the Class IV advanced skim milk prices, plus the fixed differential of $0.74 per hundredweight of skim milk, has not only resulted in numerous negative unintended consequences, it has failed in achieving its perceived or anticipated positive intended consequences.

I. 2018-2019 RATIONALE FOR CHANGING CLASS I MOVER

Industry participants from both the fluid milk processor industry subsector and the dairy farmer producer subsector came together in 2018-2019 to discuss and develop a plan to aid processors of Class I products in hedging their raw milk price risk on packaged Class I products. Processors had stated that hedging their Class I price risk under the then in-place "higher-of" the Class III advanced skim milk price, or the Class IV advanced skim milk price, for determining the advanced skim milk price portion of the Class I base price was difficult since Class I price hedging required positions in the both the Class III and Class IV markets simultaneously. In addition to processors' desire to manage their raw product price risk, it was argued that the process of hedging could promote retail price stability, which theoretically should slow the persistent declines in Class I per capita consumption in the U.S., on the belief that hedging by processors could yield more stable retail prices, and this stability in retail prices should spur fluid milk consumption. These were worthy purposes.

Chief from the dairy farmer side in this negotiation process was the need for Class I revenue neutrality over time. Dairy farmers were willing to accept a plan that made hedging for Class I processors easier, even recognizing that an "average-of" computational process could, in some months, yield a Class I price lower than the "higher-of." The fixed $0.74 per hundredweight add-on to the "average-of" computation was derived from the historical relationship of the "higher-of" to the "average-of" and was installed to create the price neutrality sought by dairy farmers, and thus a bargain was struck. Certainly dairy farmers are also supportive of any reasonable pricing process or formula that would be positive to Class I sales, but not if that pricing change lowered their Class I prices over time. **(Vitaliano Statement, Exhibit NMPF – 30, Hearing Exhibit 229, page 5 of 13.)**

II. THE REALITY VERSUS THE INTENDED CONSEQUENCES

Neither of the anticipated benefits to processors nor the promised benefits to the industry in general from the conversion from the "higher-of" computation to the "average-of" computation for Class I prices has been realized.

First, the Hearing Record provides no data which suggests, certainly on the great majority of Class I packaged fluid products – High Temperature Short Time (HTST) processed milk, that there is much Class I hedging occurring at all, and no evidence that the use of hedging Class I price risk is more prevalent now then prior to the installation of the "average-of" process. In fact, the predominance of testimony demonstrated that traditional HTST jug milk is sold by the processor to the wholesaler/retailer on what can best be described as a "tolling" basis – that is at the Federal Order announced Class I prices for a month plus a contracted margin over the Classified raw milk cost. The margin over Class I raw product cost is typically fixed over the life of the fluid milk sales contract. Consequently, since the revenue on packaged milk sales flowing back to the processor from the wholesaler/retailer moves in lock-step with the monthly changes in the Federal Milk Marketing Order announced Class I prices, there *is no* price risk to the Class I processor. No price risk means no need to hedge. The need to hedge Class I price risk on a predominance of Class I fluid milk products did not exist when the "average-of" plan was developed, and no new need to hedge Class I price risk has arisen since the adoption of the "average-of" because the primary pricing convention between processors and their wholesale and/or retail customers has not changed. Consequently, the quantity and portion of Class I milk being hedged against Class I price movement is *de minimis* at best, and certainly does not justify the multiple negative consequences wrought from the "average-of" formula.

Second, no data was introduced at the Hearing supporting the contention that Class I milk product consumption trends have changed, either reversing toward the positive or diving more negatively since the installation of the "average-of" Class I pricing system. Social and life-style factors drive fluid milk consumption trends, not a perceived retail price volatility.

Providing Class I processors of the predominance of Class I packaged fluid milk products a pricing method to easily hedge their future price risk is not currently needed in the industry, if it ever was, because the processors of most of the Class I packaged products are not facing substantive price risk. Consumer choices in the retail dairy aisle are not being made exclusively on whether fluid milk prices have risen or fallen over the last month.

III. THE REALITY OF UNINTENDED CONSEQUENCES

A. The current Class I mover has resulted in millions of dollars in losses of producer income.

As mentioned, the dairy farmer side of the Class I pricing system negotiations with processors of Class I products valued, first and foremost, Class I price neutrality over time, and the formula for determining an "average-of" Class I price mover was constructed to provide that neutrality. To be blunt, the "average-of" formula for determining Class I prices has not been *neutral* to dairy farmers, it has been baneful.

NMPF Exhibit 30A, Hearing Exhibit Number 230, shows the extent to which the "average-of" system has been anything but price neutral to dairy farmers. For the period of May 2019, the first month the "average-of" system was effective, through July 2023, the impact of the "average-of" price computation has resulted in total Federal Order pool values decreasing more than $940 million, an average loss in Class I skim milk prices of $0.57 per hundredweight versus the skim milk price that would have been in place had the "higher-of" process remained in effect. Revenue neutral? The opposite.

When computing the impact of the "average-of" mover system on producer blend prices, the problem hits home for dairy farmers even more. Across the eleven Federal Orders, for the May 2019 through July 2023 period, the Federal Order blend prices fell $0.15 per hundredweight versus what would have existed had the "higher-of" process remained in place. Revenue neutral? Again, the opposite.

The "average-of" Class I base skim milk price computation system has failed miserably in meeting its stated objective to provide dairy farmers with Class I revenue that matches, over time, the Class I pooled revenue that would have been generated under the "higher-of" Class I pricing method. If that failure were not bad enough on its own, it is particularly stinging that the genesis of this whole plan – increased use of Class I price risk hedging, hasn't materialized in any meaningful way.

B. <u>The adverse impact of the blend price across the southeast is more than double the impact in the country as a whole</u>.

The southeast region, for this purpose the Appalachian, Florida and Southeast Order marketing areas, have been particularly hard hit from the impact of the "average-of" mover. Due to the southeast Orders' high Class I use percentages, the negative impact of the "average-of" on the southeast Federal Orders' uniform prices has been greater than the blend price impact to all of the Federal Orders in total. For the May 2019 through July 2023 period, the Federal Order weighted average impact of the "average-of" versus the "higher-of" in the Appalachian Order Number 1005 was a blend price reduction of $0.39 per hundredweight, a blend price reduction of $0.42 per hundredweight in the Florida Order Number 1006, and a blend price loss of $0.37 per hundredweight for the Southeast Order Number 1007. These blend price impacts across the southeast are more than double the impact in the country as a whole.

The resultant Federal Order blend price impairments from the "average-of" Class I mover computation in the southeast Federal Orders creates a double peril – blend prices decline more than the U.S. average in the highest milk production-cost region of the country, and also reduces the blend price gradient between the milk-deficit southeast and the reserve supply Federal Orders to the north and west of the southeast that provide the critical supplemental milk to the southeast. This blend price gradient dynamic is demonstrated abundantly by **<u>Exhibit NMPF-112D, Hearing Exhibit Number 496</u>**.

Although **<u>Exhibit Number 496</u>** refers to Proposal 20's impact on the reserve supply regions to the southeast blend price gradient deterioration, the math works the same for Proposal 13 as it does for Proposal 20. Any national across-the-board decrease in Class I prices will reduce the blend prices in Federal Orders 1005, 1006, and 1007 more per hundredweight than the rest of the country, owing to the southeast's higher Class I utilization percentages. The math is simple, the results are devastating.

Nationwide revenue neutrality for the "average-of" versus the "higher-of" Class I pricing processes has failed, and the impact on producer milk checks resulting from the change in the Class I price computation method is not felt uniformly across the country, with the southeast suffering the most, in two very important ways.

IV. PROPOSED ALTERNATIVE MOVER COMPUTATION PROPOSALS ARE NOT THE ANSWER

Hearing Proposals 14 and 15 each propose something of a hybrid of the "average-of" and the "higher-of Class I mover computation. Although they recognize that the current "average-of" mover computation fails in its stated objective of revenue neutrality to dairy farmers, they attempt to push the search for national revenue neutrality out across multiple months, even multiple years, by way of various methods of over-time Class I value true-ups. While theoretically these proposals seek to solve revenue neutrality absent in the current "average-of" computation, Proposals 14 and 15 will continue the "average-of" failure to transmit Class I revenue into the Federal Order pools in a timely manner, perpetuating the problems of creating increased incidences of negative Producer Price Differentials (PPD) and the problem that always follows negative PPDs: depooling. And depooling increases marketing disorder, which is inconsistent with the Federal Order reform justification underlying the "higher-of" mover change.

Throughout the Hearing process, the testimony given, the exhibits offered and received, and all the back and forth between the numerous lawyers and witnesses, a central truth has emerged. The only Class I Base Skim Milk Price computation that provides all of the positive attributes and achieves all of the objectives of the "higher-of" Class I Base Skim Milk Price computation is "higher-of" process. Any substitute for the "higher-of" is a grossly inferior substitute.

V. CONCLUSIONS

The installation in the Federal Milk Marketing Orders of the current Class I Base Skim Milk Price formula using the average of the Class III advanced skim milk price and the Class IV advanced skim milk price, plus a $0.74 per hundredweight fixed adjuster, was a grand experiment. The experiment had high designs, high aspirations, and high hopes. It has also failed at a very high level.

There is an axiom in economics that any lasting change in technology or a change in an operational process is by definition an improvement in the technology or process, because if the change doesn't prove beneficial, you can always return to the previous process that did, in fact, work. It is time for the Federal Order Program to recognize the failure of the "average-of" process, and make the proper correction, a return to the "higher-of", the process that worked.

The current Class I mover computation has reduced pool revenues by millions of dollars, and with that reduction, caused dairy farmer blend prices to suffer, and while significant everywhere, the suffering is not uniformly felt across the country. Lower blend prices inherently lead to lower Producer Price Differentials and lower Producer Price Differentials lead to de-pooling and the market disorder and uneconomic movements of milk follow depooling. Reducing Class I prices is a recipe for market failure, no matter what the system or process that reduces them, and disincentivizes the delivery of milk to Class I. The testimony from the witness from Crystal Creamery made it plain that negative Producer Price Differentials send the signal for dairy farmers to deliver milk to manufacturing Class usages, not to Class I.

> Q: [Vulin] "And so once that PPD crosses the threshold of $0, once it's down in the negative range, what does that mean for a supplier who chooses to supply a Class I processor versus a Class III processor who can depool? "
>
> A. [Schuelke] "There is now no incentive to supply milk to a Class I plant. If you were equidistant from a Class I plant and a manufacturing plant, you would now have no incentive to supply the Class I plant."
>
> **(Hearing Transcript Page 11259, Lines 10 through 17, January 19, 2024)**

The current Average-of Class I mover computation system has failed the industry nationwide, but has particularly failed the southeast. Any pricing system under the Federal Orders that makes it more difficult to supply milk to deficit regions thereby undermining the purposes and requirements of the Agricultural Marketing Agreement Act. Retaining the "average-of," or installing any Class I price mover mechanism that is something other than the "higher-of", threatens the supply of milk to Class I, and thus must be rejected.

The Secretary must apply pricing provisions in the Federal Milk Marketing Orders that encourage milk to be made available to, and in fact supply milk to, Class I markets. The "higher-of" mover does exactly that, unlike the current Class I price formula and any other offered substitute process. Thus Proposal 13 must be adopted in the most expeditious manner available to the Secretary.

The Members of Dairy Cooperative Marketing Association, Inc. support Proposal as included in the Hearing Notice, and urge the Secretary's adoption of the Proposal as soon as practicable. Proposal 13 will correct the unintended and unanticipated defects in the current Federal Order language, thereby restoring the intended functionality of the Class I mover. Finally, the price divergences and extensive depooling found in the record will be appropriately limited.

Submitted March 5,

John A. t. Peter, Esq.
Counsel to Dairy Cooperative Marketing Association, Inc.
Dempsey Law Firm, LLP
Forest Avenue, Suite
Fond du Lac, WI 54935
jsp@dempseylaw.com

DEMPSEY LAW
WWW.DEMPSEYLAW.COM

10 FOREST AVENUE, SUITE 200
FOND DU LAC, WI 54935
920.922.0470 TEL
920.235.2011 FAX

WRITER'S DIRECT
920.922.0470 EXT. 404
JSP@DEMPSEYLAW.COM

DEMPSEY LAW

March 25, 2024

VIA U.S. MAIL AND EMAIL: SM.OHA.HEARINGCLERKS@USDA.GOV
Hearing Clerk
United States Department of Agriculture
STOP 9203 - Room 1031
1400 Independence Avenue SW
Washington, DC 20250

RE: Post-Hearing Brief of Dairy Cooperative Marketing Association, Inc. re: National Milk Marketing Order Pricing Formula I Hearing

Greetings:

Enclosed is the post-hearing brief filed on behalf of DCMA in the above hearing matter.

Thank you.

Sincerely,

DEMPSEY LAW FIRM, LLP

John A. St. Peter

Enclosure
JSP/jaw

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 FOR DAIRY COOPERATIVE MARKETING ASSOCIATION, INC. ("DCMA") WITH LETTER has been furnished and was served by electronic mail upon the following parties on March 25, 2024 by the following:

USDA (OGC)
Brian Hill, OGC
Brian.Hill1@usda.gov
Michelle McMurtray, OGC
Michelle.McMurtray@usda.gov
Donna Erwin, OGC
Donna.Erwin@usda.gov
Carla Wagner, OGC
Carla.Wagner@usda.gov

USDA (AMS) Dairy Programs
Dana H. Coale, Deputy Administrator
Dana.Coale@usda.gov
Erin Taylor, Director Order Formulation and Enforcement Division
Erin.Taylor@usda.gov

AMS - FMMO Hearing
FMMOHearing@usda.gov

USDA (OSEC)
Katharine Ferguson
Katharine.Ferguson@usda.gov

Lucas S. Sjostrom, Executive Director
Minnesota Milk Producers Association
P.O. Box 65
Brooten, MN 56316
E-mail: lucas@mnmilk.org

Mike Stranz, Vice President of Advocacy
National Farmers Union
20 F Street NW, Suite 300
Washington, DC 20001
E-mail: mstranz@nfudc.org

Erick Metzger, General Manager
National All-Jersey, Inc.
6486 East Main Street
Reynoldsburg, OH 43068
E-mail: emetzger@usjersey.com

Peter Vitaliano
National Milk Producers Federation
2107 Wilson Blvd., Suite 600
Arlington, VA 22201
E-mail: pvitaliano@nmpf.org

Counsel for National All-Jersey, Inc.
John H. Vetne
E-mail: johnvetne@gmail.com

Wendy M. Yoviene
Baker, Donelson, Berman, Caldwell, & Berkowitz PC
901 K Street, NW, Suite 900
Washington, DC 20001
E-mail: wyoviene@bakerdonelson.com

Counsel for National Milk Producers Federation
Stoel Rives LLP
101 S. Capitol Blvd., Suite 1900
Boise, ID 83702
Bradley R. Prowant
E-mail: bradley.prowant@stoel.com
Nicole C. Hancock
E-mail: nicole.hancock@stoel.com

Mike Brown, Chief Economist
International Dairy Foods Association
1250 H Street, NW, Suite 900
Washington, DC 20005
E-mail: mbrown@idfa.org

Counsel for International Dairy Foods Association
Steven J. Rosenbaum
Covington & Burling LLP
1201 Pennsylvania Avenue, NW
Washington, DC 20004
E-mail: srosenbaum@cov.com

Counsel to Dairy Cooperative Marketing Association, Inc.
John A. St. Peter
Dempsey Law Firm, LLP
10 Forest Avenue, Suite 200
Fond du Lac, WI 54935
E-mail: jsp@dempseylaw.com

American Farm Bureau Federation
600 Maryland Avenue SW, Suite 1000W
Washington, DC 20024
Sam Kieffer
E-mail: sk@fb.org
Roger Cryan
E-mail: rogerc@fb.org
Danny Munch
E-mail: dmunch@fb.org
Erin M. Anthony
E-mail: erin@fb.org
Mike Tomko
E-mail: miket@fb.org

Mark Lamers
Lamers Dairy, Inc.
N410 Speel School Rd.
Appleton, WI 54915
E-mail: mark.lamers@lamersdairyinc.com

Counsel for Select Milk Producers, Inc.
Ryan K. Miltner
The Miltner Law Firm, LLC
100 North Main Street
P.O. Box 477
New Knoxville, OH 45871
E-mail: ryan@miltnerlawfirm.com
ryan@miltner-reed.com

Counsel for Milk Innovations Group
Davis Wright Tremaine LLP
920 Fifth Avenue, Suite 3300
Seattle, WA 98104
Charles M. English, Jr.
E-mail: chipenglish@dwt.com
Ashley L. Vulin
E-mail: ashleyvulin@dwt.com
Grace Bulger
E-mail: gracebulger@dwt.com

Marin Bozic
Edge Dairy Farmer Coop
E-mail: marin@bozic.io

CERTIFICATE OF SERVICE (cont'd)
Milk in the Northeast and Other Marketing Areas
Docket No.: 23-J-0067

Daniel Smith
E-mail: dsmith@gmavt.net
dsmith@dairycompact.org

Jim Sleper
Sleper Consulting, LLC
E-mail: sleperjp@gmail.com

Respectfully Submitted

WANDA MOSBY

Digitally signed by WANDA MOSBY
Date: 2024.03.25 13:32:42 -04'00'

Wanda Mosby, Legal Assistant
USDA/Office of Administrative Law Judges
Hearing Clerk's Office, Room 1031-S
1400 Independence Ave., SW
Washington, DC 20250-9203