

UNITED STATES DEPARTMENT OF AGRICULTURE
AGRICULTURAL MARKETING SERVICE

IN RE:	)	
	)	
MILK IN THE NORTHEAST AND	)	
OTHER MARKETING AREAS;	)	Docket Nos
PROPOSED AMENDMENTS TO	)	AO-14-A74, et al.;
TENTATIVE MARKETING	)	DA-06-01
AGREEMENTS AND ORDERS	)	

**LEPRINO FOODS COMPANY’S BRIEF AND PROPOSED FINDINGS AND
CONCLUSIONS IN REGARDS TO PROPOSALS TO AMEND THE CLASS III AND
CLASS IV MILK PRICE FORMULA MANUFACTURING ALLOWANCES.**

INTRODUCTION AND SUMMARY

Pending before the United States Department of Agriculture (“Department”) are proposed amendments to the Class III and Class IV milk price formula manufacturing allowances applicable to all Federal Milk Marketing Orders (“Orders”). The hearing on these matters was held January 24 - 27, 2006, in Alexandria, Virginia and September 14 – 15, 2006 in Strongsville, Ohio (“Hearing”). The reconvened portion of the Hearing, held September 14 – 15, was to accept into evidence data on plant manufacturing costs compiled by Cornell University and other pertinent data specifically addressing plant manufacturing costs that is publicly available. Leprino Foods Company (“Leprino”) previously submitted a post-hearing brief based upon the evidence at the January portion of the Hearing. Leprino is submitting this brief to supplement the earlier brief based upon the additional record evidence from the September portion of the Hearing.

Evidence presented at the Hearing supports the following conclusions:

1. The make allowance for cheese should be set no lower than 20.77 cents per pound of cheese.
2. The make allowance for dry whey should be set no lower than 20.32 cents per pound of dry whey.

The following is further elaboration on the record evidence supporting these conclusions:

Cornell Cost Study

The cost study results presented by Dr. Mark Stephenson of Cornell University should be used as the beginning reference point for setting the make allowances for cheddar cheese and whey manufacturing. Dr. Stephenson's cost study was conducted using the same methodology as the cost studies that have been conducted by the California Department of Foods and Agriculture ("CDFA") for many years. This methodology was developed by CDFA for the purpose of providing ongoing manufacturing cost data that is used as a point of reference in making policy decisions regarding the appropriate make allowances in the milk price formulas in the state of California. The allocation procedures for multi-product plants are clearly defined and evenly applied.

The consistent methodology used in the completion of the Cornell cost study and the thorough review of data by Dr. Stephenson results in a superior cost study to the data presented by Dr. Charles Ling of the Cooperative Marketing Services Division of Rural Development within USDA at the January Hearing. Dr. Ling's data was derived from a benchmarking study of cooperative-owned plants. This study lacks representation of proprietary plants. Additionally, given its purpose as a benchmarking study, Dr. Ling's data was not generated using clearly defined and consistent allocation procedures. Although Dr. Ling's study was based upon plants that primarily produce cheddar cheese, some volumes of other cheeses were included in the cheddar cost data [Exhibit

18, page 4, footnotes 1 and 2]. The costs for these other cheeses were not allocated to those cheeses; rather, they remained in the cost study for cheddar cheese.

The Cornell cost study updated to 2005 energy costs and modified to include a marketing allowance of 0.15 cents per pound supports the following:

1. The make allowance for cheddar cheese should be set no lower than 20.77 cents per pound of cheese. Dr. Stephenson articulated very clearly that the population estimate of 20.28 cents more accurately represents the weighted average cost of cheddar plants outside of California than does the sample-weighted average of 16.38 cents. This is due to the stratified sampling methodology that was used to identify survey plants. Given the skewing of this sampling methodology to over-represent large plants, the data must be reweighted by the size distribution of plants across the entire industry. Dr. Stephenson's population estimate does just that.

The data included in Dr. Stephenson's study covered twelve-month periods as far back as 2004. Over this extended period, energy costs have been very volatile. Dr. Stephenson estimates that impact of restating the energy costs from the survey period to 2005 rates would be an increase in the cheddar cost of 0.34 cents. This adjustment to update the cost data to a more current time period should be considered in setting the make allowance.

And finally, the costs covered by Dr. Stephenson's study are confined to the cost of processing and do not include a cost to market the product. The 0.15 cent per pound marketing cost allowance adopted as part of the current make allowance and supported in the January portion of the Hearing should also be incorporated in the make allowance set as a result of this Hearing.

Therefore, the make allowance for cheddar cheese should be set no lower than 20.77 cents (20.28 + 0.34 + 0.15) per pound of cheese.

2. The make allowance for dry whey should be set no lower than 20.32 cents per pound of dry whey. The methodology used to establish the 20.32 cent minimum make allowance is similar to the methodology outlined above for cheddar cheese. Specifically, it is the 19.41 cents from Dr. Stephenson's cost study updated by 0.76 cents to bring the energy costs to 2005 levels. Additionally, a 0.15 cent marketing cost is added.

However, the Department should consider setting the make allowance for whey higher than 20.32 cents. Dr. Stephenson's study for whey is likely skewed by the stratified sampling technique in the same way as his cheddar data is. He expressed a desire to make a population adjustment but was stymied from doing so by a lack of plant size data representative of the whey plant population in the United States. This lack of data with which to statistically correct for the sampling technique, however, does not preclude the Department from making the policy judgment that would naturally flow from the fact that the sample weighted average under represents the weighted average costs of the population of whey plants outside of California. The Department should set the whey make allowance higher than the 20.32 cents that is justified based upon the sample weighted average.

Conclusion

The need for relief by manufacturers operating under the Orders is even more urgent today than it was in January. The extended period over which the industry has continued to pay milk prices based upon costs from the late nineties has led to mounting stress. The fixed relationship between finished product prices and the Class III and IV formula milk prices limits the marketplace's ability to adjust for these changes. Consequently, the long-term viability of manufacturers is being threatened by the shortfall between the make allowances in the current Class III and IV formulas and current costs.

The Hearing record from January and September is replete with evidence that manufacturing costs have increased significantly since the time period of the cost surveys used to establish the current make allowances. Leprino urges the Department to update the make allowances on an emergency basis so that the manufacturing plant capacity necessary to sustain orderly marketing conditions is not further jeopardized.

Respectfully submitted,

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