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UNITED STATES DEPARTMENT OF AGRICULTURE
BEFORE THE SECRETARY OF THE UNITED STATES
DEPARTMENT OF AGRICULTURE
AGRICULTURE AND MARKETING SERVICE

Docket No. AO-14-A74, ET AL.
DA-06-01

National Public Hearing
January 24 - 27, 2006
Alexandria, Virginia

In Re:

The Matter of Proposed Amendments
To Tentative Marketing Agreements
And Orders

Brief submitted on behalf of
O-AT-KA Milk Products Cooperative, Inc. and
Upstate Farms Cooperative, Inc.
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Inc.

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\$1.9 Million Pricing Trap Due To Outdated Cost Data

O-AT-KA is owned by three dairy cooperatives. To the extent that its costs cannot be recovered due to outdated cost data in the make allowance, the dairy farm families that are members of these cooperatives are being hurt unfairly.

The inherent problems that arise from using outdated cost data were explained by the witness for O-AT-KA, Craig Alexander. Based on 20 years of experience in the dairy industry “in a variety of capacities involved with dairy economics, market analysis, regulatory impact of State and Federal orders, and bulk milk and dairy commodity sales” (V. III, at 174), Mr. Alexander explained how product formulas use “processing or ‘make’ allowances” to “determine the benchmark minimum market value of milk to produce butter and nonfat dry milk for Class IV uses and cheese for Class III uses” (V. III, at 178).

Mr. Alexander emphasized the need to keep such make allowances up to date. Otherwise, as costs increase, the manufacturers’ efforts to recoup their costs by increasing the prices of manufactured products “is no solution as these increases are captured by the NASS surveys and fed back into pricing formulas with no cost

recovery to the producers and balancing plants.” As a result, “the producers who have to shoulder the responsibility for balancing the market, investing in plants that make cheese, nonfat dry milk and butter, are not compensated fairly as compared to other producers in the market.” (V. III, at 178).

Therefore, balancing plants such as O-AT-KA “are indeed trapped into outdated fixed make allowances that need immediate updating.” (V. III, at 178). **Mr. Alexander quantified just how deep this unfair pricing trap for Western New York’s dairy farm families was in 2005: \$1.9 million!**

O-AT-KA Supports Proposal #1

For the reasons given in Mr. Alexander’s testimony (V. III, at 181-186), “O-AT-KA supports the application of the CDFA and RCBS data as detailed in Mr. Wellington’s testimony” (V. III, at 181).

A key consideration is that the updated make allowance should use “the medium cost group of nonfat dry milk plants in the California survey” (V. III, at 182). “The medium group for California is more representative of similar plants in Federal Orders” (V. III, at 182). “[I]t is the butter-powder plants that are doing relatively more of the balancing” (V. III, at 183). Therefore, such Federal Order butter-powder plants “will have higher than average costs compared to large plants producing the same commodities in heavy manufacturing areas such as California with less variation in supply” (V. III, at 183).

Furthermore, despite Mr. Yale’s protestations that such balancing costs should not be dealt with nationally, the Department ruled as recently as January 2005 that such balancing costs should be dealt with in the make allowances for Class III and IV (V. III, at 183-185, quoting the Department’s final decision from the Northeast Pooling Provisions hearing at Federal Register: Vol 70, No. 19).

O-AT-KA Supports Including 2005 Energy Costs

In general, this hearing’s decision will be based on 2004 cost data because more recent cost data is difficult, if not impossible, to obtain. However, with respect to energy costs, cost data for 2005 is both readily available and highly material to the unfair price trap in which manufacturing plants, including O-AT-KA, find themselves. Furthermore, considering how volatile energy costs are, there is merit to the indexing of energy costs as advocated by National Milk (V. III, at 186-188).

O-AT-KA Supports Re-Opening the Hearing

At the hearing, National Milk sought to introduce testimony by Dr. Roger Cryan regarding how best to implement the Department's decision in this hearing. In particular, National Milk wanted the status quo make allowances to continue with respect to Class I and Class II. However, in response to a motion by some of the participants in the hearing, those portions of National Milk's testimony could not be entered into the record.

For the reasons stated by Dr. Cryan, Marvin Beshore and me at the hearing (Vol. IV, at 43-61) and in our post hearing briefs, Upstate Farms and O-AT-KA respectfully submit that this ruling by the Administrative Law Judge should be reversed.

The resulting re-opening of this emergency hearing would not, and should not, open the door to consideration of a number of "decoupling proposals." Such "decoupling proposals" should await the non-emergency hearing into make allowances that is contemplated by many of the parties to this hearing as soon as Cornell completes collecting the data and analysis that is needed for a full review of such pricing issues.

Instead, the re-opened hearing should be limited to the merits of leaving the status quo make allowance in effect when calculating Class I and/or Class II prices while permitting an emergency updated make allowance to take effect when calculating Class III and IV prices. It is necessary and desirable that the Department take such testimony and evidence into consideration when determining how best to implement its decision.

Emergency Conditions Exist

In any case, it is urgent that the Department move ahead on an emergency basis.

As detailed by several witnesses, including Mr. Alexander (V. III, at 176-177), 12 plants have closed in the Northeast since January 2004. Five of these plants were balancing plants. And even the closing of other plants adversely impacts the ability of the milk shed to balance supplies.

In addition, the unfair burden on dairy farm families, including those whose cooperatives own O-AT-KA, mounts month by month. The resulting disorderly marketing conditions are not theoretical; in the Northeast, they are already happening. As Mr. Alexander explained:

We have found that increased milk in our market and decreased alternatives for handling milk are placing increased pressure to make these commodities. We see milk volumes continuing to increase this winter, and already available capacity is being stretched to the limit. We are extremely concerned about our ability to process milk while sustaining increased losses. . . . [Indeed, i]f left to run its course, unchanged make allowances will undercut the very ability of the federal order program to preserve minimum pricing for milk. Minimum class pricing will be undermined, disorderly conditions will increase as uneconomic milk movements and alternative sales under class will be sought out to avoid processing losses or simply because plants have closed and there is no home. (V. III, at 188-189).

During cross-examination, Mr. Alexander stressed that emergency conditions will worsen as the flush builds this Spring. “[A]lready we are seeing increased milk volumes coming into the plant, and I think that’s reflecting overall in the milk shed (V. III, at 201). One major problem “is the decline in plant capacity that we talked about and Mr. Wellington explained” (V. III, at 201). There are also “increases in production on the farm and farm expansion[s], more milk per cow, etc.” (V. III, at 202). Therefore, milk “volumes are increasing and we are seeing, perhaps, even an earlier spring flush than normal . . . [that] we expect . . . to continue on through the spring” (V. III, at 202).

Conclusions

Upstate Farms shares the views expressed herein by O-AT-KA. Furthermore, Upstate Farms and O-AT-KA continue to support Proposal #1 and the request by National Milk and ADCNE to re-open the hearing to determine what effect, if any, this emergency decision regarding Class III and IV make allowances should have on Class I and II prices.

Respectfully submitted,

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