September 26, 2006

Hearing Clerk
Stop 9200- Room 1031
United States Department of Agriculture
1400 Independence Avenue, SW
Washington, D. C. 20250-9200

Dear Hearing Clerk:

The undersigned Board of Directors of Family Dairies USA, a multi-purpose USDA qualified cooperative, is submitting this brief regarding recent proposals to amend Class III and Class IV manufacturing milk price allowances. The brief is submitted on behalf of the 3500 dairy farmer members who milk cows in 7 upper Middle Western states and who own this cooperative. Our members contend that dairy producers and dairy manufacturers should be considered by the Secretary to be equal stakeholders and to be afforded equal consideration in matters affecting the production side of this great industry.

At the outset, let us make it clear that our member stakeholders were not party to the request by the UDIA et. al. along with certain members of Congress to pressure USDA to "adopt immediately, on an interim basis, updated make allowances" based on evidence presented at the previous January make allowance hearing. We applaud the Secretary for seeking additional information in the Cornell Study before making a rush to decision in this matter.

Our members' reluctance to support this call for an immediate increase in manufacturing cost allowances for Class III and IV is not due to our failure to empathize with some manufacturers who are seeing their operating margins squeezed by accelerating energy costs. Our members fully understand margin squeeze because their own dairy farm's bottom lines are being impacted negatively by the same energy cost increases.

In fact, early in 2005 (well before the original Agri Mark Emergency Hearing request) the Family Dairies USA Board and management on behalf of its producer members contacted leading Federal Order 30 officials regarding the possibility of requesting an emergency Federal Order hearing that could address the problems of rising energy costs that dairy farmers are facing – something along the lines of a fuel adjustment or energy allowance administered with, or through, the Federal Order System. The Order officials considered the request and were sympathetic, but advised the Board Chairman, personally, there was no authority under the Federal Order System rules to address producer cost of production or pricing problems. These facts were read into the January record by our cooperative representative.

Such authority is obviously afforded manufacturers under FMMO rules as evidenced by the request for, and the subsequent holding of, this emergency make allowance hearing. Furthermore, our members acknowledge that current FMMO rules do allow the Secretary to enact the proposed make allowance upward adjustments if the evidence and data in the record are sufficient to support such a proposal. Such make allowance adjustments could afford most dairy manufacturers a cost of production guarantee, and in some cases, certain manufacturers could be afforded actual windfall profits especially if the allowance were too generous.

Unfortunately, all economists agree such adjustments would lower Class III and Class IV prices and these proposals would require the money needed to pay for these adjustments to come right out of our and other US dairy producers' already shrunken milk checks. The negative impact on dairy farmer income would be in excess of 300 million dollars the first year.

So, unfortunately, the hit to our producer members' milk checks and to their bottom lines puts them in an adversarial position to their processor friends. As stated above, a great deal of the problem lies in the lack of asymmetry in the way FMMO rules deal with the cost of production protection afforded processors and not afforded farmers.

All of the above puts the Secretary in a very difficult position as he prepares to issue the final rule in this matter. It would be the greatest of ironies if a government agency decision would solve the problems of the processor stakeholders at the expense of producer stakeholders especially if costs were not justified. The Secretary must do due diligence as he reviews the evidence and data submitted.

As producers we have expertise when examining producer energy and cost of production pricing problem data, but when we review the hearing record, we know we lack the expertise to fully debate the legitimacy of the arguments put forward. We did note that even the Cornell Study relied almost exclusively on data submitted voluntarily by processors and was not audited data. In fact, none of the cost analysis presented at the January hearing outside of government stats were audited which just enforces our call for due diligence.

It should also be noted that once an upward adjustment is made, it becomes practically permanent. Even though it does not seem to appear in the record, the secretary might note that one of the key energy manufacturing costs, natural gas, according to the EIA has dropped from a high in 2005 of 14 cents per cmf to 7.4 cents per cmf at the beginning of 2006, and as this was written on September 21, 2006, the price of this important energy source closed at 4.74 cents per cmf. It would be a travesty to lock in what could be a windfall profit for certain large efficient manufacturers at the expense of our hard pressed family farmers if the cost data upon which the decision was made was not representative of the real costs when the decision is finally granted.

Our frustrations are summarized well as we quote the last two paragraphs of a summary written by Professor Ed Jesse and Brian Gould of the University of Wisconsin concerning this subject that we submitted as attachments to the brief in our January testimony shown below:

"Unless offset by higher product prices, correcting the flaws in product price formulas that we have noted would result in a lower Class III price. This raises the question of whether changes would inequitably alter the sharing of revenues between dairy farmers and cheesemakers. Put more likely, farmers can argue-quite legitimately-that since they receive no assurances of profitable milk prices under federal orders, why should cheesemakers be treated any differently.

In response, we note that fixed cheesemakers margins may be fine if they assure reasonable profitability, promote efficiency and productivity growth, and encourage competition for cheese milk at prices above the federal order minimum. On the other hand, fixed margins can be a serious problem if they consistently yield sub-par returns and cause disinvestment in cheesemaking. Farmers and cheesemakers are partners-both must be profitable over the long run to sustain a healthy dairy industry."

Thank you for hearing our considerations!

Respectfully submitted,

Peter Kleiman, President	Stewart Huber, Vice President
Walter Lueder, Secretary-Treasurer	Allen Blommel, Director
Delores Fagle, Director	Sharon Laubscher, Director
Jan Morrow, Director	George Ramsden, Director