



EXHIBIT # _____

**Testimony of
Robert D. Wellington of Agri-Mark Dairy Cooperative
In Support of Proposals 1 and 2
At Federal Order Hearing
(Docket No. AO-14-A77, et al.; DA-07-02)
February 26, 2007 in Strongsville, Ohio**

My name is Robert D. Wellington. I serve as Senior Vice President of Economics, Communications and Legislative Affairs for Agri-Mark Dairy Cooperative. I have served in that capacity, along with being their economist, since 1989. Prior to that I worked eleven years as an economist and the chief of research and market information with the former New York-New Jersey Milk Market Administrator's Office. I have a Bachelor's and a Master's degrees in agricultural economics from Rutgers University, where I also taught.

Agri-Mark is a Capper-Volstead Cooperative with approximately 1400 member-owners whose farms produce milk throughout the six New England States and New York State. Agri-Mark owns and operates a cheese plant in Middlebury, Vermont, another in Chateaugay, New York, a cheese and other dairy products plant in Cabot, Vermont and a butter-powder plant in West Springfield, Massachusetts.

PROPOSAL #1

The intent of proposal #1 is to provide an update to the make allowances determined in the hearing held in January and September of 2006. Agri-Mark and other proponents have already submitted comments relative to the interim final decision and we ask that the hearing record and all comments relative to that hearing become part of this record.

I will not re-iterate my testimony and comments submitted at that hearing but any updating of make allowances proposed under this proposal #1 are intended to update what ever make allowances are finally determined as a result of that hearing.

USDA Agricultural Marketing Service (AMS)'s preliminary economic analysis of Class III and Class IV prices conducted by its Office of the Chief Economist did a very good job relative to the initial intent of Proposal #1 and we appreciate their efforts.

While we would like also to include updated data from the Cornell study, the limited time and schedule of Professor Mark Stephenson does not allow us to have that additional information for this hearing. I did consider the option of providing individual plant information from Agri-Mark and others, but we believe that USDA has made it clear that it will only consider cost information from surveys such as Cornell and CDFA.

New data is available from CDFA and Proposal #1, as correctly interpreted in USDA economic analysis, is to amend make allowances to reflect that new manufacturing cost information. This new data is for calendar year 2005.

Scenario A in the USDA analysis shows that such a CDFA update would increase butter, NFDM and cheese make allowances by \$.0014, \$.0092 and \$.0029 cents per pound respectively. This analysis use volume weights updated to 2006 data also. The impact of this initial change on producer prices under proposal #1 is extremely small.

As stated by USDA in its economic analysis report, "Incorporation of the most recent CDFA cost data and 2006 weighting results in small variations from baseline forecasts. Slight decreases in protein and nonfat solids prices lower the skim price across all classes. This results in an average \$0.01 per cwt. decrease in the Federal order blend price. Dairy product prices increase slightly. There is no change in the average all-milk price over the nine-year period."(page 7)

The dry whey make allowance method used in the interim final decision did not use CDFA data. Agri-Mark and others disagree with that part of the decision. If USDA decides to include the CDFA dry whey costs in the final-final decision as we believe they should do, we propose that the 2005 CDFA skim whey powder manufacturing costs at \$0.2851 should be used in that calculation.

Table 4 of USDA's economic analysis (page 8) shows the methodology for Scenario A involving Proposal #1. This table clearly shows the dramatically lower Cornell make allowance costs compared to CDFA costs. Keep in mind that the CDFA study uses audited information as well as more current information. We also have concerns about applying the Cornell survey costs across the entire national volume of dairy products manufactured. Professor Stephenson clearly showed that the cheese costs selected by USDA to be used in the interim final decision are not the average costs incurred by the population; the costs chosen by USDA were heavily and disproportionately weighted in favor of large, low costs cheese plants.

Agri-Mark continues to support the changes proposed in our comments to the interim final decision. However if those changes are not enacted, then the following procedure should be used to amend the interim decision: use the product volumes in the individual surveys, NOT the national product volumes, to weight the CDFA and Cornell information. Table 1 contains the results for such a procedure for all four dairy products.

The resulting proposed make allowances for cheese is \$0.1765 per pound, for butter it is \$0.1336 per pound, for NFDM it is \$0.1636 and for whey powder it is \$0.2075.

TABLE 1: WEIGHTED AVERAGE MAKE ALLOWANCE COSTS OF MOST RECENT CORNELL AND CDFA STUDIES

	SURVEY VOLUME (pounds)	SURVEY PRICE (per pound)	WEIGHTED AVG PRICE (per pound)
CHEESE			
CDFA	826,583,500	\$0.1914	\$0.1765
CORNELL	963,576,672	\$0.1638	
BUTTER			
CDFA	396,627,948	\$0.1408	\$0.1336
CORNELL	125,602,044	\$0.1108	
NFDM			
CDFA (med)	253,123,854	\$0.1872	\$0.1636
CORNELL	280,535,487	\$0.1423	
WHEY PDR			
CDFA	97,953,043	\$0.2851	\$0.2075
CORNELL	568,735,884	\$0.1941	

PROPOSAL #2

This proposal seeks to have USDA use an annual manufacturing cost survey of U.S. cheese, whey powder, butter and nonfat dry milk plants to automatically update the manufacturing allowance for those products used in Class III and IV component prices.

Federal Orders currently use a weekly NASS survey of hundreds of plants to automatically update dairy commodity prices since these prices change within a very small time frame. However manufacturing inputs such as energy, chemicals, labor also can change within a relatively short time frame and this needs to be reflected in the Orders.

The Cornell plant survey should be used as the basic methodology to update annual manufacturing allowances on a similar basis. This would allow Class III and IV prices to reflect regularly updated plant costs without the need for lengthy, untimely and controversial hearings and decisions.

We propose that Market Administrator audit personnel oversee the survey and select the sample plants as well as collect, audit and assemble the cost information. A random, stratified sample of plants should be drawn each year and the results applied across the entire population of plants.

The same methodology should be used in each survey each year. Any change in the methodology would have to be done via the hearing process.

We initially propose several criteria to be applied across the survey results to set the applicable make allowance.

1. The plant cost allowance would be set at a level that would allow a minimum of 80% of the milk volume used by plants in the entire Class III and IV manufacturing plant population to cover their costs.
2. In addition, the national cost allowance should be set at a level that would allow a minimum of 25% percentage of the producer milk volume used by Class III and IV manufacturing plants in any specific Federal Order pooling at least 4 billion pounds of milk annually, to cover their costs. According to 2006 Federal Order data shown in Table 2, this provision would involve plants in the following Federal Orders: Northeast, Mideast, Upper Midwest, Central, Southwest and Pacific Northwest.
3. The final make allowance should use the higher of either criteria 1 or 2. This will act as a safeguard to assure that no large milk manufacturing region with have all their manufacturing plants unable to cover their costs.

TABLE 2: UTILIZATION OF PRODUCER MILK IN CLASS III AND CLASS IV PRODUCTS, BY FEDERAL ORDER, 2006

ORDER	CLASS III	CLASS IV	TOTAL
	(million pounds of producer milk)		
Northeast	5,075	2,584	7,659
Appalachian	334	758	1,092
Southeast	1,659	691	2,350
Florida	101	154	255
Mideast	6,435	1,230	7,665
Upper Midwest	20,119	728	20,847
Central	6,194	1,566	7,760
Southwest	4,172	1,740	5,912
Arizona	1,171	652	1,823
Pacific Northwest	2,078	2,771	4,849
TOTAL	47,338	12,873	60,211

In Professor Stephenson's testimony at the hearing in this location on September 14, 2006, he calculated a weighted average cheese manufacturing cost estimate for the population of commercial cheddar cheese plants he had information for. That weighted average estimate of the population was \$0.2028 per pound. He stated that that value would cover about 82% of the volume of cheddar cheese made in the country and the processing costs of about 33 percent of the plants.

Even through a make cost allowance set to cover 80% of the milk volume would cover fewer than 33 percent of the cheese plants, Agri-Mark believes it would be a fair rate to set. We

propose that the same 80% rate we used for all four dairy products under make allowance consideration.

During Dr. Stephenson's cross examination, he mentioned that the weighted value of the cheese plant sample, namely (\$0.1638 per pound) would likely not cover the manufacturing costs for any cheese plant in the Northeast. This was of great concern for producers and handlers in the region since more than five billion pounds of producer milk were used to manufacture cheese in 2006. That milk volume is down substantially from just a few short years ago and further declines would create severe disorderly marketing conditions for the region.

The second criteria involves using a make allowance that assures that at least 25% of the manufacturing milk in any Federal Order with more than 4 billion pounds of combined Class III and IV use annually not be used by plants that are in a loss position, struggling with minimum pricing. This provides for at least a billion pounds of plant capacity in those Orders. If USDA used the weighted average estimate of the plant population instead of the sample as we propose at the 80% level, I believe it would be unlikely that this second criteria would set the national make allowance under all Orders on a regular basis.

The Dairy Division-AMS of USDA originally worked with Dr. Stephenson on his plant cost survey prior to any hearing announcement. I believe that they also provided some funding for his efforts. In my conversations with Dr. Stephenson in 2005 both at his office and when he was meeting with Agri-Mark plant staff and cost accountants in preparation for providing our plant information, he mentioned that his intent was to create a working plant cost methodology for likely regular use by USDA or some regulatory agency. Agri-Mark believes that the basic methodology is now available and experienced audit staff at the Market Administrators' offices have the expertise to conduct Dr. Stephenson's model on an annual basis.

Thank you for consideration of these two proposals. Agri-Mark has also submitted three additional proposals numbered 10, 11 and 14 in the hearing notice. In the interest of keeping this hearing record as organized as possible, we will testify on those proposals as they are reached in sequence.