BEFORE THE UNITED STATES DEPARTMENT OF AGRICULTURE
AGRICULTURAL MARKETING SERVICE

In the Matter of	:	
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MILK IN THE NORTHEAST AND	:	**Docket Nos.: AO-14-869 et al;**
OTHER MARKETING AREAS	:	**DA-00-03**

COMMENTS AND EXCEPTIONS TO THE TENTATIVE FINAL RULE SUBMITTED ON BEHALF OF THE ASSOCIATION OF DAIRY COOPERATIVES IN THE NORTHEAST

I. Introduction.

This comments and exceptions are submitted on behalf of the Association of Dairy Cooperatives in the Northeast ("ADCNE").[1] The Association consists of the following member dairy cooperatives: Agri-Mark, Inc.; Dairy Farmers of America; Dairylea Cooperative Inc.; Land O'Lakes, Inc.; Maryland and Virginia Milk Producers Cooperative Association, Inc.; O-AT-KA Cooperative; St. Albans Cooperative Creamery, Inc.; and Upstate Farms Cooperative, Inc. The members of ADCNE market in excess of 65 percent of the milk in Order 1, the federal order regulating the marketing of milk in the Northeast marketing area. Order 1, in turn, represents more than 20 percent of the milk in the Federal Milk Marketing Order system. Each of the ADCNE member cooperatives are Capper-Volstead qualified cooperatives recognized to represent their members in federal milk market orders.

ADCNE members have a diverse set of operations and, consequently, a diverse set of

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[1] Individual ADCNE members have separately stated positions with respect to certain issues in this proceeding upon which the Association has taken no position in these comments.

individual interests. Agri-Mark, Inc., a northeastern cooperative, markets milk to third-party buyers and operates a butter powder plant as well as two cheese plants, through its Cabot Cheese subsidiary. Dairylea Cooperative Inc. primarily markets milk to third parties, but is also a member of O-AT-KA, which owns and operates a butter powder plant. Dairylea is also a member and a joint venture partner in Deitrich's Milk Products, LLC, which has butter powder plants at Middlebury Center and Reading, Pennsylvania. Dairy Farmers of America, in the Northeast markets to third parties and is a joint venture partner in Deitrich's Milk products, LLC. Land O'Lakes operates a butter powder plant at Mt. Holly, Pennsylvania, and markets to third parties. Maryland and Virginia Milk Producers Association, like Land O'Lakes, markets to third parties and operates a butter powder plant at Laurel, Maryland. O-AT-KA is a cooperative of three cooperatives, Upstate, Niagara and Dairylea, and it owns and operates a butter powder plant at Batavia, New York. St. Albans Cooperative Creamery markets to third parties and also operates a condensing and drying plant. Upstate Farms is a cooperative in western New York which owns and operates fluid bottling plants and is a part owner in O-AT-KA system. Upstate Farms also markets milk to third parties.

The positions advanced in these comments and exceptions represent the consensus of the positions of these dairy farmer cooperatives and do not necessarily represent the narrow economic interest of each organization. In reaching and advancing consensus positions in this proceeding, ADCNE has attempted to balance the interests of their dairy farmer members as producers and of the cooperatives' operations as both marketers of milk to third parties and manufacturers of all classes of dairy products.[2]

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[2] These comments and exceptions are submitted subject to the right to supplement the filing if the comment period is extended. ADCNE requested an extension of time for filing these comments in view of the injunction issued by the US District Court on January 31, which in

II. ADCNE Supports the Refusal to Adopt Proposals 30 and 31 or Any Other Proposals Which Would Change the Differentials for Class II or I Prices or the "Higher of" Mover for Calculating Class I Prices.

ADCNE commends the Department's analysis and reasoning in rejecting Proposals 30, 31, or any modifications to those proposals which would change the basis for calculating Class I and Class II prices or Class I and Class II differentials. There are three reasons why these proposals should not be adopted. First, the proposals were beyond the scope of the Congressional mandate for the hearing. As the Notice of Hearing (Exhibit 1) stated: "The purpose of the hearing is to receive evidence with respect to the economic and marketing conditions which relate to reconsideration of the Class III and Class IV milk pricing formulas included in the final rule for the consolidation and reform of federal milk orders. The mandate from Congress via the Consolidated Appropriations Act 2000 (P.L. 106-113, 115 Stat. 1501), requires the Secretary of Agriculture to conduct a formal rule-making proceeding to reconsider the Class III and Class IV milk pricing formulas included in the final rule for the consolidation and reform of federal milk orders and to implement any changes until January 1, 2001." Neither Proposal 30 (which proposed to change the Class I differentials) nor Proposal 31 (which would

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effect changed the tentative rule subject to comment, and also in view of the Department's precipitous retraction of the extension of time granted on Friday, February 2. Both of these circumstances make a modest extension of 14 days, as ADCNE requested, both reasonable and helpful to the rulemaking process. The apparent reluctance to grant the additional few days is beyond the comprehension of these parties. It would appear that only a narrow special interest is being served when virtually all rulemaking dockets acted on within the lame duck period of the past administration are extended generally for 60 days, while a comment period, not a rule, cannot be extended for 14 days in view of a court injunction.

change the Class II differential) were proposals which addressed reconsideration of the Class III or Class IV price formulas. Consequently, those proposals were correctly rejected.

Secondly, even if the proposals were properly within the scope of the Hearing Notice, they should not be adopted because they were not fully debated. The industry rightfully approached this Hearing as one mandated to reconsider Class III and Class IV prices. For that reason, there was minimal consideration given to the practicalities or ramifications of the changes in Class I and Class II differentials proposed in Proposals 30 and 31. Each of these proposals could have very substantial impacts on producers in all markets. It should be sufficient to note that the Class I differential structure has been the subject of many days of federal order hearings; many days of congressional hearings and debates; and substantial federal court litigation. To tinker with the resulting statutorily-mandated system without a focused hearing process would have been quite inappropriate.

Finally, the Hearing Record on the proposals, such as it is, did not support adoption of the proposals. The revised Proposal 30, advocated by the Family Dairies USA, would result in substantial reductions in dairy farmer income throughout the federal order system. There was and is nothing in the evidence presented by the proponents of Proposal 30 or elsewhere in the hearing record which supports these revenue reductions to dairy farmers.[3] Furthermore, the proposal presented in testimony at the hearing — to change the formulation of the base price for Class I differentials — was plainly not in the hearing notice and, consequently, hearing participants were not able to fully evaluate its impact, as Mr. Hollon testified. (Tr. 1545-1546). Because of both these procedural and substantive defects, the proposal should not be adopted and

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[3] In fact, the period of the hearings is the period of some of the lowest prices generated by the federal order program in twenty years.

the tentative final decision should be affirmed.

Proposal 31 was also not supported by the record. All of the evidence of record suggested that the current 70¢ differential between Class II and Class IV was and is an appropriate recognition of the additional value of the Class II soft manufactured products and it does not provide any artificial or inappropriate incentive for substitution of Class IV ingredients for Class II ingredients. See, e.g., Exhibit 45. Furthermore, it is not clear how Proposal 31 could be implemented: presumably, it would require the maintenance in the order of two sets of order language which calculate Class II prices on both a "before" and "after" basis. This would be highly impractical, if it were even possible, and is in no way justified by the hearing record.

On the basis of the foregoing, ADCNE commends the Department for the decision not to adopt Proposals 30 and 31.

III. ADCNE Supports the Product Prices, and Adjustments Thereto, Adopted in the Tentative Final Decicion for Use in the Class III and Class IV Price Formulas.

ADCNE supports the product prices and adjustments to those prices adopted in the tentative final decision for use in the Class III and Class IV formulas. Specifically we support the decisions: (1) To continue the use of NASS-collected prices, rather than CME prices; (2) To refuse to include 640 lb. block prices in the cheese prices collected; (3) To maintain the 3 cent add-on to barrel prices when averaging barrel and block prices; and (4) To adjust the barrel cheese prices to 38% moisture. We will discuss each of these proposed changes in turn.

A. NASS Survey Prices Should Continue To Be Used in Class III and Class IV Price Formulas.

Several proposals in the hearing notice suggest using Chicago Mercantile Exchange ("CME") prices rather than USDA National Agricultural Statistics Service ("NASS") prices in

Class III and Class IV price formulas. USDA correctly, in our view, adopted NASS prices for the tentative final rule. That action has been enhanced and reinforced by the subsequent legislation which will greatly strengthen the reliability, completeness, and integrity of the NASS price series. The NASS prices for dairy products used to formulate Class III and IV minimum milk prices are the correct prices to use, as the Department has concluded.

B. 640-Pound Blocks of Cheddar Cheese Should Not Be Included in the NASS Survey.

The Department correctly refused to adopt Proposal 12 which would include 640 lb. blocks of cheddar cheese in prices used to establish Class III milk prices. The record established and USDA concluded that there is an insufficient basis of arms-length trading in this cheese variety to make it a part of the market-price for cheese discovered via the NASS survey. The record revealed a lack of sufficient reporters of 640s to make it a viable part of the NASS survey. (Tr. 54-55) That confirmed the National Cheese Exchange experience where trading was disbanded for lack of interest after a short experiment. As the decision noted, much of the trade in 640s tends to involve customer-specified characteristics which would make such transactions unsuitable for a price series. (Tr. 1575). The market in 640 pound blocks of cheddar cheese does not involve sufficient buyers and sellers in arms-length transactions to provide good data to establish the Class III price for producer milk in all federal milk orders.[4]

C. The Department Correctly Found That Three Cents Should Continue to Be Added to the Moisture-adjusted Barrel Cheese Price to Make it Comparable to Block

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[4] If 640 prices were to be collected and used in the NASS series, another adjustment to the average price, similar to the adjustment for averaging barrels and 40 lb. blocks, would need to be determined. Obviously, the cost of manufacturing and packaging a 640-lb. block of cheese is something less than that for 16 separate packages of 40 lb. cheese blocks. Consequently, the 640 lb. block price would need to be adjusted appropriately if it were to be averaged with 40 lb. block prices for the purpose of pricing producer milk. When 640s traded on the National Cheese Exchange, they tended to trade at a price between the price of blocks and barrels.

Chese Prices.

ADCNE commends the Department for the decision not to adopt the NCI/IDFA proposal to reduce the price adjustment for barrel cheese from 3¢ to 1¢ (thereby reducing the Class III milk price by 15¢-20¢ per hundred-weight). The proposal was not supported by the record and was premised upon the demonstrably incorrect proposition that: "This 3¢ really consists of two components [cost of manufacture and a moisture adjustment]" (Yonkers, Tr. 309). In fact, the 3¢ does not reflect a moisture adjustment factor at all because it is representative of the historical difference in market value of barrel cheese versus block cheese after adjustments for moisture. As the tentative decision concluded, the historical record of barrel and block prices validates that spread which should be retained.

C. The Department Correctly Concluded that the Moisture-adjustment to Barrel Cheese Prices should be to 38% to Make Those Prices Comparable to Block Chese Prices.

The Department correctly concluded that barrel prices should be adjusted to 38% moisture, rather than 39%, for averaging with block cheddar prices. The only evidence of record concerning the average moisture of block cheese is that it is 38% moisture. Consequently, that is the correct moisture level to which barrel prices should be adjusted. The barrel cheese moisture level is collected by NASS when collecting barrel price data. That figure will now be enhanced in reliability by the legislation giving NASS additional tools to enable it to collect and publish universal, accurate and reliable cheese prices. To convert barrel prices to 39% moisture, for price discovery purposes, when block cheese is known to average 38% moisture is nothing more than a cheap-shot price reducing gimmick for the benefit of cheese manufacturers. The component price formulas, including the make allowances, are carefully crafted to avoid erring on the high side of producer prices in many respects, particularly in areas where precision is not possible.

Where precision is possible, and cheese prices can be precisely adjusted to the known comparable moisture, there is no reason that a price series, if it is to have some integrity should not use the correct moisture figure. The Department's decision correctly, and properly, did just that and ADCNE commends the Department for that decision.

IV. ADCNE Comments upon the Make Allowances Adopted for Class III and IV.

In determining the appropriate make allowances for Class III and Class IV prices, ADCNE suggested that the Department should use all credible, reliable information available to it and we believe the Department did so and commend the decision in that regard. We wish to comment in only two respects with respect to make allowance issues. First, we highly commend the Department's refusal to consider the NCI survey data. That survey did not meet minimum acceptable standards for reliable information in a federal administrative, on-the-record rulemaking held pursuant to 5 U.S.C. §§ 556-57. We argued, and continue to believe, that relying upon such data would seriously demean the importance of sworn, first-hand, subject-to-cross-examination testimony which is the touchstone for these hearing records.[5] The Department's decision preserves the importance of the record in these hearings for the future and is an important ruling which should be reaffirmed in the final decision.

ADCNE supported the use of the California state cost study information also. While, unfortunately, there was not a witness available at the hearing to discuss the California information, it remains an audited, state-agency-compiled study which has inherent indicia of

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[5] The NCI/IDFA survey data was not admissible evidence because it was not of the "sort upon which responsible persons are accustomed to rely," (7 C.F.R. § 900.8 (D) (1)) and would not constitute substantial evidence such as is required for agency action pursuant to the Administrative Procedure Act (5 U.S.C. § 706 (2) (E)). See, e.g., Carter-Wallace, Inc., v. Gardner, 417 F.2d 1086 (4th Cir. 1969)(In an administrative hearing, summary exhibit of pharmacy costs and inventories was not admissible where witness was not familiar with underlying data and supporting documents were not available for use in cross-examination).

reliability. However, we do wish to note some concern with respect to the use which the Department made of the California cheese manufacturing figures for administrative overhead. Although it was not explained in great detail in the decision, the Department utilized the California figures for plant and administrative overhead and added them to the RBCS figures presented by Dr. Ling to reach the final cheese make allowance of $.165 per pound. This was more than one cent per pound greater than the weighted average make allowance, using both the RBCS and California data, as calculated by Ed Coughlin for the National Milk Producers Federation and supported by ADCNE. The difference was the inclusion of 1.9 cents per pound for general and administrative expense from one of the California publications. Without any testimony about the California numbers, or data from any other source with which to compare the number, it is impossible to either commend or critique the figure with precision. We would note, however, that the allowance given would provide the newest, largest, and most efficient cheese plants (with daily intakes of 3 to 5 million pounds) with annual "G & A" allowances[6] of $2 million to $3.5 million dollars; allowances which are certainly generous, to say the least. It would surely be preferable to have some basis in testimony in the record on which to base that sort of expense level before building it into plant costs, at the expense of minimum producer prices.

V. The Class III Price Formula in the District Court Order of January 31 Should Be Continued in the Final Rule.

ADCNE supports the continuation of the "status quo" formulation of protein and butterfat prices in Class III, as adjusted by the factors adopted in the Tentative decision and supported

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[6] This cost is in addition to other categories of indirect expense including return on investment.

above in these comments. We are satisfied that that system of determining protein values for Class III is the best option on this hearing record.

VI. Conclusion.

ADCNE recognizes that the Department was confronted with many complex issues in this proceeding, and was required to labor under a Congressionally imposed time frame for the decision. ADCNE finds much to be commended in the decision and files these comments to note its support for the Department's recommendations in the respects stated herein. On the basis of the foregoing, ADCNE respectively requests that the Secretary adopt a final decision consistent with these comments.

Respectfully submitted,

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