NMPF MAKE ALLOWANCE TESTIMONY

United States Department of Agriculture
Before The Secretary of Agriculture

Hearing beginning August 23, 2023

Testimony Presented By:

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FarmFirst Dairy Cooperative Testimony in Support of National Milk Producers Federation (NMPF) Proposal 7 on Increasing Make Allowances.

My name is Jeff Lyon. This testimony is presented in support of **Proposal 7: Increase in make allowances in the component price formulas to the following levels:**

Butter	**$.21 per pound**
Nonfat dry milk	**$.21 per pound**
Cheese	**$.24 per pound**
Dry whey	**$.23 per pound**

Background & Experience

This testimony is presented on behalf of FarmFirst Dairy Cooperative (FarmFirst) which is a long-time member of NMPF. My time in the dairy industry covers more than 30 years working directly for dairy farmers.

As General Manager for FarmFirst, I have the overall responsibility for all our divisions and departments. With respect to our milk marketing division, Family Dairies USA, I am involved with setting the monthly milk price, pooling/de-pooling decisions, and federal order issues. I represent the cooperative in dairy policy discussions individually, through NMPF, and the Midwest Dairy Coalition. I am a member of the Central Milk Producers Cooperative board of directors.

I got my start working on dairy policy issues in July 1985 as an agriculture legislative assistant for former Wisconsin Congressman Steve Gunderson in his Washington DC office. Mr. Gunderson was the ranking member on the Dairy subcommittee, and I worked on the 1985 Farm Bill, which included the whole herd buyout program and increasing Class I price differentials.

In the spring of 1986 through March 1988, I served as assistant director for the National Commission on Dairy Policy, a federal commission created by Congress in the 1985 Farm Bill to evaluate US dairy policy. The report was submitted to Congress.

For 22 years I worked for the Wisconsin Farm Bureau Federation. In my first four years and last seven years with Farm Bureau, I coordinated the national affairs program and also lobbied on state legislative and regulatory issues. I was the lead staff person for our Dairy Advisory Committee. I lobbied on dairy issues in Washington DC individually, with the Farm Bureau president, the board of directors, and young farmers. I prepared testimony for my president and a farmer member for a federal order hearing in the early 1990s. For the other 11 years, I led the member relations division and was responsible for coordinating the organization's membership procurement and retention efforts. While not involved daily in dairy policy I had a thorough understanding of our position on dairy issues.

Before joining FarmFirst, I served seven years as the Deputy Secretary at the Wisconsin Department of Agriculture, Trade, and Consumer Protection. At DATCP, my primary responsibilities included the implementation of policy and rules affecting DATCP, assisting in the management of 600 plus employees, programs, and operations and representing DATCP in relations with other persons, foreign delegations, and stakeholders including the legislature and the Governor.

FarmFirst has been a member NMPF since 2013, when three Wisconsin based cooperatives merged to form FarmFirst. I have served on the NMPF's Board of Directors for six years. I have also been a member of NMPF's Economic Policy Committee for six years. I have been a member of NMPF's Federal Order Task Force which for almost two years has studied, evaluated, and proposed the NMPF proposals being heard at this national Federal Order hearing. I would like to thank the Secretary of Agriculture for holding this national hearing to consider NMPF proposals. FarmFirst believes the adoption of NMPF's proposals will benefit the entire dairy industry.

FarmFirst Dairy Cooperative

FarmFirst has nearly 2,600 dairy farmer members in seven Upper Midwestern states, which include Illinois, Indiana, Iowa, Michigan, Minnesota, South Dakota, and Wisconsin. Their milk is pooled under Federal Orders, 30, 32 and 33. We are a diverse cooperative that provides milk test verification services, markets milk, and owns a milk testing laboratory.

We provide milk test verification services for our members that ship their milk to proprietary milk processors, which is the vast majority of our 2,600 members. Our members ship milk to 52 processors that are predominantly cheese plants. These plants range from some of the largest to the smallest in the Upper Midwest.

Our membership includes all sizes of dairy farms - small, medium, and large with the largest concentration of our members in Wisconsin. Our members and their farms are critical to the local economy and infrastructure in their communities with their purchases of products and services including but not limited to banking, equipment dealers, veterinarians, and feed and fertilizer dealers.

Through our milk marketing division, Family Dairies USA, we sell nearly 600 million pounds of milk annually to 20 to 25 milk proprietary processors of products in all four Classes of milk on behalf of our 135 Family Dairies USA patrons. FarmFirst markets all of its milk in Federal Milk Marketing Order 30.

We advocate for our members on policy issues based on positions adopted by delegates at our annual meeting. Our 10-person board of directors, all of which are dairy farmers, and staff are responsible for advancing member positions on issues. FarmFirst represents nearly 7.7 billion pounds of milk production annually. In 2022, Hoard's Dairymen ranked FarmFirst as the seventh largest cooperative with respect to milk volume and the second largest cooperative with respect to the number of members in the US.

FarmFirst does not own or operate a processing facility to convert milk into a finished product. However, FarmFirst has an intake/reload facility that allows us to store milk for short periods of time to balance the milk going to processors, keeping milk fresh until delivery.

Challenges:

FarmFirst sells milk through negotiated annual supply agreements with our buyers and through "spot" loads that are sold to plants that we do not have a supply agreement with. Our milk buyers pay a premium (a negotiated amount above the Class III price) which we are able to return to our patron members. In exchange, our buyers are guaranteed a regular supply of high-quality milk when they need it. We also work with our buyers on a weekly basis and adjust our milk deliveries based on the demand from their customers. We also source organic, A2A2 milk, and grass-fed milk for our milk buyers when requested.

Our customers rely on FarmFirst to handle milk in excess of their needs annually, seasonally, monthly, weekly, or daily basis. These balancing serves are costly for FarmFirst member owners.

Since FarmFirst does not operate a processing facility, my testimony will address the effect that current make allowances have had on my members and why FarmFirst supports the NMPF proposal. Over the last few years, FarmFirst has experienced a significant decrease in the premiums we have received for our milk due in large part to outdated make allowances.

Current make allowances have compressed margins at processing plants, which in turn have been passed on to producers in the form of lower premiums so processing plants can manage their margins. Make allowances need to be updated in the long-term interest of processor reinvestment in their plants.

In situations as we are in right now with an oversupply of milk makes the situation worse for producers. Milk gets dumped or is sold well below the Class price.

From January 2020 through July 2023, we experienced a 24 percent decrease in the average negotiated premium paid per pound of milk, which resulted in approximately $2.7 million or about $0.16 cents per hundredweight on average that we were not able to pay our Family Dairies USA producers. The $2.7 million does not include milk sold under the Class III price.

For our members that FarmFirst provides milk test verification services, I do not have the manufacturing cost data for the proprietary plants, which is considered confidential information, but the situation is similar with negative Producer Price Differentials (PPD) and the prices received by members.

Manufacturing costs or “make allowances” are an integral part of the determining milk prices and Product Price Formulas (PPF) do not work as intended when make allowances are set below the actual cost of commodity manufacturing.

As the NMPF stated in their petition, “Under Federal Order Reform, Product Price Formulas (PPF) replaced the previous direct survey of prices paid for manufacturing milk. PPFs moved the process of establishing the basis for Federal Order pricing up the marketing chain one step to survey unregulated buying and selling of wholesale, spot, commodity style, dairy products. Those dairy product prices became the foundation, working backward via economic formulas, to determine the minimum price of milk used to make those commodity dairy products. Adjusting their prices by subtracting the non-milk costs of manufacturing these products and applying appropriate yield factors determines an implied value for the components of milk used to produce them. Having accurate and updated plant processing costs, or “make allowances,” and appropriate product yield factors are critical for this indirect method of determining milk prices, which is a principal function of the Federal Order Program. Yet a regular and systematic method of ensuring that these critical PPFs remain accurate, and current has not been established.”

There is no question that manufacturing costs have increased since they were last updated in 2008. During our deliberations on the NMPF Federal Order Task Force, members were concerned that the while the 2018 Make Allowance Study commissioned by USDA and done by University of Wisconsin-Madison dairy economist Dr. Mark Stephenson provided valuable information on manufacturing costs there were inconsistencies in his methodology compared to previous make allowance surveys, due in large part to the voluntary nature of the survey that disincentivized those plants with a less of a cost increase to respond to the survey.

Proposal:

The NMPF proposal makes modest increases to make allowances to partially alleviate problems that have led to the disorderly marketing of milk. The NMPF proposal balances producer and processor interests. It is generally understood that increasing the make allowances will have a negative effect on producer prices, at least in the short term.

Due to the lack of agreed upon comprehensive, industry-wide data on costs, yields and plant volumes and the impact on producer margins, it is imperative that make allowances only be increased to the levels being proposed by NMPF. Larger increases in make allowances that are being proposed by other organizations would only compound the problem and would narrow margins even further to levels that would negatively impact the profitability of producers, thus jeopardize milk production needed for future dairy demands.

The impact of even modest increases in make allowances will be an additional negative on producer margins when one considers the low projected milk price for the remainder of 2023 into 2024 and already narrow margins due to high feed costs, and increased labor, fuel, and equipment costs.

A perfect example of the tight margins being experienced by producers are the payments received by producers since 2018 through the Dairy Margin Coverage Program (DMC), the safety net program that was included in the 2018 Farm Bill. The DMC program is a voluntary risk management program for dairy producers that offers protection to dairy producers when the difference between the all-milk price and the average feed price (the margin) falls below a certain dollar amount selected by the producer. The DMC offsets some of the costs being incurred by producers but not all.

Year	Total Numbers of Farmers Enrolled	Percentage of Farmers with Production History Enrolled	Total Payment
2019	23,394	73.45%	$451,645,929
2020	13,506	45.11%	$233,991,933
2021	19,079	69.17%	$1,187,176,978
2022	17,973	71.33%	$83,739,531
2023 *	16,996	73.41%	$610,588,174

*Through 8/15/2023

With respect to processors, make allowances were never intended to guarantee processors a profit on the products they produce but to determine a value for the components of milk.

While not part of this national hearing, the NMPF is actively pursuing legislative authority and funding for USDA to conduct regular, mandatory, auditable plant processing cost studies to use to update make allowances. If this can be accomplished, the dairy industry will be able to use accurate and more reliable information in updating make allowances.

Summary:

In closing, the industry did not get into the make allowance situation overnight and USDA should not expect to get out of this situation entirely on the backs of producers. The modest increases to make allowances included within the NMPF proposal is a good first step to balance the interests of both producers and processors. More importantly, when USDA is given the authorization and funding to conduct mandatory cost surveys as NMPF is also proposing, this will ensure necessary make allowance modifications will be made in the future.

This will also ensure such make allowance changes are conducted on a regular basis. Once USDA's releases their mandatory plant cost results, then the industry can decide whether to petition for a hearing. This enables the industry to go through the normal hearing process which includes changes being voted on by dairy farmers since Federal Milk Marketing Orders are a program for dairy farmers. Going through this formal process ensures markets will be corrected, which results in market stability and orderly marketing.