IDFA
International Dairy Foods Association
Milk Industry Foundation
National Cheese Institute
International Ice Cream Association

EXHIBIT
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SUPPLEMENTAL TESTIMONY OF INTERNATIONAL DAIRY FOODS ASSOCIATION
JULY 2007 FEDERAL MILK ORDER HEARINGS
DOCKET NO. AO–14–A77, et al.; DA–07–02

IDFA earlier in this hearing testified in opposition to proposal 20, but at that time no proponent witnesses had yet testified, and we indicated that we might provide additional testimony after we had heard from the proponents. Nothing in the proponent testimony that was subsequently presented in Indianapolis changes IDFA's opposition.

As noted in my previous testimony, without an adequate level of make allowance, a manufacturing plant cannot continue to operate long term, as it will have insufficient funds available to pay the vital costs necessary for operating the plant. For that reason, increased costs must lead to an increased make allowance.

Proposal 20 requires the same procedure to determine changes in cost of manufacturing as are currently utilized by USDA in deciding to change a make allowance. However, instead of using the results of that determination to change the make allowance and allow the minimum farm milk price to change so that processing and marketing costs are reflected in regulated minimum prices, proposal 20 would leave the make allowance unchanged. It would simply identify the amount of the cost increase and require handlers to try to negotiate with their customers in an effort to recover these increased costs in the form of a surcharge added to the wholesale dairy price. If this "let's hope it works" effort fails, the processor and others like it are doomed to returns inadequate to cover their costs, given that the minimum milk prices to farmers they will continue to be obligated to make will not have been changed whatsoever.

The proponent witness cited what he claimed were several examples of surcharges like the ones he envisions being attempted by manufacturers to effectuate proposal 20. However, two of those examples are regulated charges that all regulated processors must pay (the MilkPEP check off assessment and the Pennsylvania Milk Marketing Board over order prices), so no one can avoid having to bear them. And, the third example was DairyAmerica's attempt to implement an energy surcharge on nonfat dry milk prices. But during re-direct, the witness noted that even such a large U.S. supplier of nonfat dry milk was only a small player in international markets. Certainly, it would be improbable if not impossible for such a small international player to change long established terms of trade by introducing a new surcharge based simply on USDA's determination that costs of processing in the U.S. allowed for such a surcharge.

One of the fatal flaws in proposal 20 is that processors regulated by Federal orders face competition from not only unregulated areas and even unregulated milk in Federal order marketing areas, but also from states like California which has its own milk price regulations and is unlikely to change its longstanding practice of changing (increasing) make allowances in response to changes to costs of processing. Therefore, the examples to which the proponents point do not apply to the situation their proposal would create. Handlers purchasing milk from non-federally regulated suppliers would have lower (or no) minimum milk price obligations to farmers, and would have a substantial cost advantage over federally regulated handlers. Federally regulated handlers would not find it possible simply to insist that their customers pay a surcharge. Their customers would instead go to suppliers who would be more than happy to meet their needs without the increased price.

One obvious alternative for a customer would be to purchase off of the CME. Proponent's witness implies that this obvious choice should be ignored because long standing prices relationships between the CME and actual transaction prices can be altered quite easily. IDFA is of the opinion that this might sound good in theory, but in practice would be an utter failure.

Take the hypothetical example used during cross examination of the proponent's witness, where the current market situation yields a CME price of $1.40 for cheddar cheese and USDA has determined that the costs of processing have increased by 3 cents per pound of cheese. If an example processor has a long standing practice of pricing cheese to a customer at exactly the CME price, proposal 20 requires that handler now seek to charge that customer the CME price plus 3 cents per pound. How much common sense can it take to see that the customer, who in the past has had the option of paying $1.40 either to the CME or to the cheese processor and chosen to buy from the cheese processor, now is faced with the alternative of paying the cheese processor $1.43 or buying on the CME for $1.40. The choice is no longer revenue neutral; rather, continuing to purchase cheese from the cheese processor would cost the customer 3 cents more than the going CME market price.

Clearly, increasing the established price relationship with the CME is not as simple in the real world as the proponent's witness wants USDA to believe. Furthermore, this hypothetical buyer has more options available to a customer than the CME, like plants not regulated by Federal orders in California and other areas of the country.