



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

FOR-75



**Statement on behalf of the Milk Industry Foundation
and the
International Ice Cream Association
before the
U.S.D.A. Task Force on Federal Order Reform**

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**Presented by:
Gary A. Corbett
Vice President, Governmental and Dairy Industry Relations
Dean Foods Company**

Mr. Chairman:

Thank you for the opportunity to appear before the task force today. I am Gary Corbett, V.P., Governmental & Dairy Industry Relations, Dean Foods Company. My statement today is on behalf of the Milk Industry Foundation (MIF) and the International Ice Cream Association (IICA).

Our associations have been working for several months to develop recommendations for this process. A first step in any analysis is to define what is to be accomplished. Determining objectives and/or criteria is necessary. The associations suggest the following objectives and/or criteria for use by USDA.

Basic Objectives and/or Criteria to Guide the Process

Any proposed changes to the Federal Order (F.O.) system by USDA should be evaluated against the following;

- Does it result in simplified and reduced regulations?
- Does it result in regulations which are less intrusive in milk marketing?
- Does it allow markets to play a greater role in pricing milk and dairy products?
- Is it consistent with international trade agreement provisions?
- Does it assure domestic consumers an adequate supply of milk at economically justified market competitive and reasonable prices?
- Does it reflect market based economic models?
- Is it consistent with general marketing conditions which would exist without the regulations?
- Does it provide for orderly marketing?
- Does it create an incentive for milk to flow to its highest valued, best use?
- Does it insure equitable treatment of producers, handlers and consumers?
- Does it standardize classification throughout the country and among various dairy ingredients and components?

Today I will address only the issue of basic Formula Prices. However, other issues such as Federal order consolidations, multiple basing points, multiple component pricing and the linkage of Class I prices to manufacturing prices or the basic formula price are equally important.

The associations strongly urge this and other USDA task forces addressing these additional issues to coordinate their actions and deliberations in order to arrive at the best possible milk order reform package.

Basic Formula Price

With regard to the basic formula price, the associations would like to offer two alternatives for consideration -- one that maintains the classified pricing structure and, the other, which would provide no BFP, but would pool Class I differentials.

Suggestion #1: For thirty years, the industry has debated the reliability of the basic mover of class prices known as the Minnesota-Wisconsin (M-W) price and its temporary replacement, the Basic Formula Price (BFP). The M-W price was established in 1961, when Minnesota and Wisconsin produced a significant volume of grade B milk and was viewed as the surplus milk production region. Over the past thirty-five years, supply and demand conditions in the Upper Midwest have changed. Plant capacity exceeds milk production and has resulted in a premium structure for milk used in manufacturing. USDA's survey of mailbox prices indicates that prices paid to producers in Chicago and Upper Midwest federal orders are above the Order blend prices and are some of the highest market prices in the United States.

Additionally, the upper Midwest is no longer the primary source of milk for manufacturing. Milk production has increased significantly and rapidly in many areas of the West, including Texas, New Mexico, Arizona, California, Idaho and Washington. Milk is available in the entire Western area at considerably lower prices and in more abundant supplies than in the Upper Midwest. Fluid utilization is low in these areas, leaving nearly 2/3 of the milk available for manufacturing.

California's State order provides for significantly lower Class prices for butter, powder and cheese than similar Class prices required to be paid in surrounding and nearby Federal Milk Marketing Order areas. This disparity, to a very large extent, led to the adoption of Class III-A pricing under Federal Milk Marketing Orders.

The associations support the harmonization of manufacturing milk prices, if a BFP is to be used. It appears that about the only way Federal and State order harmonized manufacturing milk prices can be achieved is to adopt a BFP reflecting milk values for manufacturing in the West, and adjust it for transportation cost to the Midwest.

Under the FAIR Act, California can come under the Federal Order system or elect to remain a separate State Order. If it comes under the Federal Order system, it's Class prices will surely be reconciled with other Federal Order BFP's. If the Federal Order BFP is significantly higher than that set by California, it is unlikely the California Federal Order would pass the Federal Order referendum, and would therefore remain subject to State pricing.

Additionally, if California's cheese, butter and powder manufacturing milk prices were increased to the current BFP levels, there would be fewer plants willing to purchase the milk at those prices and, if the higher prices prevailed, milk production in California would likely increase even more rapidly.

In consideration of these and other factors, the associations recommend consideration be given to using a basic formula price (if one is to be used at all), which reflects the value of milk used for manufacturing in the Western states.

The associations are analyzing several alternative formulas and urge USDA to undertake an evaluation of these alternatives as well:

1. Using a weighted average of the California 4A and 4B pricing formula.
2. Using the California 4A and 4B prices as separate classes.
3. Using Western butter, powder, and cheese prices in another product formula.
4. Developing a Western States based competitive pay price series.

The Western States based BFP should be adjusted for transportation costs to the Midwest. This would result in a higher BFP in the Midwest than that set in the West.

In addition to these suggestions, the associations urge that in any event, the BFP formula should not result in BFP prices which would exceed those resulting from the current formula and also there should be no multiple or regional make allowances.

Consistent with several of the criteria set forth earlier in these comments, the associations urge that consideration be given to using only two classes of milk -- Class I (basically the same as now) and Class II (everything not included in Class I). MIF and IICA believe that the two-class system is desirable if a BFP is retained. This would eliminate Class III--A pricing which is opposed by the associations. The associations oppose the addition of an export class of milk which would make milk available outside the U.S. at prices below those charged for internal use.

Suggestion #2: The associations also urge consideration be given to eliminating all manufacturing milk classes and pooling only Class I differentials. Under this proposition, we believe actual dairy farmer pay prices would likely be unchanged because all processors and manufacturers would compete for available milk supplies and therefore, the basic competitive price would be equal to, or exceed, what would otherwise be a BFP. In addition to the basic competitive price, all producers under the order would receive the same full price enhancing benefits of the pooled Class I differentials. Manufacturers and processors of manufactured products would pay a basic competitive price but they would not pool the money for these products. Class I users would also pay a basic competitive price which would not be pooled, but, in addition, Class I users would pay the appropriate Class I differential into the pool to be distributed to all producers under the order based on the total amount of milk pooled.

This would eliminate the debates, arguments and continuous challenges to the appropriateness of the BFP. It would also mitigate some of the regional disparities and challenges.

MIF and IICA urge USDA to consider these suggestions. The associations are proceeding to analyze them more carefully and would appreciate USDA's help in this analysis.

Thank you. I would be happy to answer any questions.