



US Department of Agriculture  
Dairy Industry Advisory Committee

Final Report

1 February 2010

2  
3 **Recommendations for Public Policy to Improve Dairy Farm Profitability and**  
4 **Reduce Milk Price Volatility**

5  
6 **Forward**

7 The United States Department of Agriculture (USDA) established the Dairy Industry Advisory  
8 Committee (Committee) in August 2009, under the rules of the Federal Advisory Committee Act  
9 (FACA), and Secretary Tom Vilsack appointed 17 members to serve on the Committee on January 6,  
10 2010. The Committee charter is “to review the issues of: 1) farm milk price volatility and 2) dairy farmer  
11 profitability. The Committee will provide suggestions and ideas to the Secretary on how USDA can best  
12 address these issues to meet the dairy industry’s needs.” The Charter further explains, “the exchange of  
13 views and information between industry representatives and USDA should result in improved  
14 understanding of the impact of USDA programs on the dairy industry and contribute to those programs’  
15 effective and efficient administration.”

16 The Committee Bylaws state that “Members will be selected from a cross section of the dairy  
17 industry representing: producers and producer organizations, processors and processor organizations,  
18 handlers, academia, retailers, consumers, and state agencies involved in organic and non-organic dairy at  
19 the local, regional, national and international levels.” Individuals serving on the Dairy Industry Advisory  
20 Committee are as follows<sup>1</sup>:

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<sup>1</sup> All members except Dr. Novakovic are considered under FACA to be serving as Representative Members and are appointed to obtain the perspectives of public sector stakeholders. Dr. Novakovic serves as a Special Government Employee under appointment by Secretary Vilsack.



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1  
2

<b>Members</b>	<b>Affiliation</b>
Paul Bourbeau	Paboco Farms, Inc., Vermont
Jay Bryant	Maryland and Virginia Milk Producers Cooperative Association, Virginia
Erick Coolidge	Le-Ma-Ra Farm, Pennsylvania
Timothy Den Dulk	Den Dulk Dairy Farm, LLC, Michigan
Debora Erb	Springvale Farms & Landaff Creamery, LLC, New Hampshire
James Goodman	Northwood Farm, Wisconsin
James Krahn	Oregon Dairy Farmers Association, Oregon
Edward Maltby	Northeast Organic Dairy Producers Alliance, Massachusetts
Andrew Novakovic	Cornell University, New York
Randy Romanski (replacing Rodney Nilsestuen, dec. July 2010)	Department of Agriculture, Trade and Consumer Protection, Wisconsin (formerly)
Robert Schupper	Ahold USA Retail, Pennsylvania
Manuel (Ray) Souza	Mel-Delin Dairy, California
Patricia Stroup	Nestle USA, California
Sue Taylor	Leprino Foods Company, Inc., Colorado
Edward Welch	Associated Milk Producers Inc., Minnesota
James (Ricky) Williams	Williams Dairy & Williams Dairy Trucking, Inc., Georgia
Robert Wills	Cedar Grove Cheese Inc., Wisconsin



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1 **Executive Summary**

2 The federal government has a number of programs in place to intervene when dairy prices fall to  
3 low levels. For example, the Dairy Product Price Support Program (DPPSP) is designed to prevent  
4 wholesale and farm prices from falling below a certain level. The Milk Income Loss Contract (MILC) is  
5 designed similarly to the countercyclical payments used for many other agricultural crops and provides a  
6 cash income supplement to partially offset the impact of low milk prices.

7 During 2009, MILC income supplements were triggered from February through November 2009.  
8 Just short of \$1 billion was spent on MILC in the two fiscal years from October 2008 to September 2010.  
9 The Agricultural Appropriations bill for FY2010 provided an additional \$290 million as direct payments  
10 to farmers through the Dairy Economic Loss Assistance Payment (DELAP) Program. These direct  
11 payments to farmers were far and away the most significant and costly of the existing program activities  
12 in the last two years.

13 Surplus butter and nonfat dry milk were sold to the government, at supported price levels, under  
14 the DPPSP as well. The magnitude of DPPSP sales was quite small. In fiscal year 2009, government  
15 purchases as a percentage of all commercial disappearance was 0.03% on a milkfat basis and 1.7% for  
16 nonfat solids. The FY2010 special Agricultural Appropriation also provided \$60 million for the purchase  
17 of cheese to be used in domestic food assistance programs. Of this total, \$43 million was spent in  
18 FY2010. In that year, the purchases enabled by the special appropriation amounted to about 0.3% of total  
19 cheese production. For fiscal year 2009, \$230 million was spent to acquire surplus dairy products under  
20 the DPPSP. While these government purchases and expenditures were helpful, they were not large  
21 enough to mitigate the drop in commercial sales.

22 In addition to these core dairy programs, the government made \$108.6 million in direct loans to  
23 dairy farmers through the Farm Loan Program (FLP), loan guarantees, concessions and options for  
24 restructuring, rescheduling or deferring payments on existing FLP loans. The Dairy Export Incentive  
25 Program (DEIP) was activated after several years of dormancy. Existing programs were implemented and  
26 even augmented in 2009 and 2010 but even those efforts did not prevent 2009 from being the worst year  
27 for dairy farm profitability in decades.



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1           The DIAC makes 23 recommendations that are listed in the table at the end of the summary.  
2       Recommendations are grouped thematically but the order in which they appear has no intended  
3       connotation about their importance. The first set of recommendations relate to existing programs. These  
4       are recommendations that do not require Congressional action.

5           The Committee finds that existing Federal programs and legislation had a limited impact on  
6       mitigating the massive impact of recent market events. Some laws provide no flexibility to the Secretary  
7       of Agriculture, while others allow some or even considerable discretion. When a proposed action has or is  
8       likely to have an impact on government expenditures, even programs that offer discretion to the Secretary  
9       cannot be used without approval of the Office of Management and Budget (OMB). Meanwhile, Federal  
10      Milk Marketing Orders (FMMOs) are designed for longer-term regulation of markets and are not readily  
11      amenable to mitigating shorter-term price events.

12          Considering existing programs alone, if the Secretary can identify funding sources, he can use the  
13      Dairy Product Price Support Program (DPPSP) and one or more food assistance programs to stimulate  
14      demand and lift prices. In this report, the Dairy Industry Advisory Committee suggests guidelines for  
15      using these programs.

16          Allocating part of the U.S. government's budget to dairy programs necessarily involves tradeoffs  
17      with other programs. The Committee suggests that using objective measures of sector hardship can reduce  
18      political pressures in the allocation process. The Committee recommends that the Secretary implement  
19      trigger levels based on the difference between average milk prices and a new measure of feed costs. The  
20      Secretary can then objectively determine when dairy farmers face extreme hardship by examining  
21      whether the difference between revenues and costs fall below specific trigger levels. Extreme hardship  
22      would justify shifting governmental resources from other uses. Within this framework, the first trigger  
23      would indicate use of a food assistance program to increase demand for dairy products. At the second  
24      trigger, the DPPSP purchase prices may be raised. The committee recommends applying these responses  
25      cautiously.

26          The Dairy Industry Advisory Committee also recommends that the Secretary of Agriculture review  
27      existing program administration to examine its impact on exacerbating price volatility or delaying the  
28      government's response to dairy farmers' economic distress. For example, there are some delays in using



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1 the DPPSP because of extra grading and other requirements and slower payment than is typical with  
2 commercial accounts. Testimony before the Committee indicated that, despite significant improvements  
3 in the Order amendment process, the FMMO program is difficult to change and could still be improved.  
4 Moreover, the FMMO milk pricing formulas may be transferring volatility in narrow subsectors of the  
5 dairy market into wider milk prices. A number of appropriate changes in administration of these programs  
6 are within the current authority of the Secretary.

7 The Committee has also reviewed and considered alternative actions that would require new  
8 legislation or regulation. In so doing, it was guided by the charge from the Secretary to focus attention on  
9 dairy farm profitability and milk price volatility. Thus, the second set of recommendations relates to  
10 actions that primarily address issues of milk price protection, stabilization or regulation. In a sense they  
11 approach the problems of milk price volatility from the perspective of can this be prevented or reduced.  
12 The third set take the perspective that, if price volatility cannot be avoided, what can be done to reduce its  
13 impacts on the industry. This section is referred to as income protection or stabilization. The fourth and  
14 last section combines a variety of recommendations that seek to improve dairy farm profitability or  
15 enhance the development of dairy markets, using strategies different from price or income stabilization.

16 It should also be noted that, while there was widespread Committee support for most of these  
17 recommendations, some recommendations were harder to reconcile across the entire group. Indications of  
18 support among Committee members are listed with each recommendation as a vote tally.

19 This report has three main sections. In the first, the justification for existing and new dairy policy is  
20 reviewed, with an emphasis on the Committee's charge to focus on dairy farm profitability and milk price  
21 volatility. In the second section, existing programs, laws and authorities are discussed. Lastly, proposals  
22 and recommendations for modifications to existing programs or the creation of new programs are  
23 reviewed and discussed.



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NUMBER	RECOMMENDATION	PAGE
<b>EXISTING PROGRAMS AND AUTHORITIES</b>		
1	DEVELOP A SYSTEM THAT PROVIDES AN ACCURATE ASSESSMENT OF DAIRY FARM PROFITABILITY IN THE DAIRY INDUSTRY. USDA should develop a data gathering and reporting system that expresses farm profitability in the dairy industry using an index to provide an impartial overview of the general level of profitability at the farm level based on the milk price-feed cost margin. <i>12 in favor, 5 opposed, 0 abstaining</i>	21
2	REVIEW FEDERAL MILK MARKETING ORDERS. The Secretary of Agriculture should appoint a committee to review implications of Federal Milk Marketing Orders, including, but not limited to, end-product pricing's impact on milk price volatility and impact of classified pricing and pooling on processing investment, competition and dairy product innovation. <i>17 in favor, 0 opposed, 0 abstaining</i>	33
3	SIMPLIFY AND IMPROVE RISK MANAGEMENT PRODUCTS FOR DAIRY FARMERS. Continue to simplify and improve Livestock Gross Margin-Dairy and overhaul Adjusted Gross Revenue-Lite in order to make them more accessible and easier for dairy farmers to use and adapt Livestock Risk Protection for use by dairy farmers. Expand risk management education. <i>17 in favor, 0 opposed, 0 abstaining</i>	38
4	USE OF USDA FARM LOAN PROGRAMS. The Secretary should work with the FSA in Washington and all State FSA Executive Directors and State Committee members, particularly those in States with significant numbers of dairy operations, to promote efficient and effective use of the FLP for dairy farmers. We especially encourage the use of the Guaranteed Loan Program with existing commercial lenders. Apparently, some States leverage the Farm Loan Programs more effectively than others. We recommend that the federal FSA examine any disparities and develop strategies to share best practices across regions. <i>17 in favor, 0 opposed, 0 abstaining</i>	50
5	EMERGENCY INTERVENTIONS. The Secretary should develop a system of triggers and actions to guide his choices for special and emergency interventions, using existing programs. <i>17 in favor, 0 opposed, 0 abstaining</i>	55
<b>PRICE PROTECTION, STABILIZATION AND REGULATION</b>		
6	BEST USE OF FUNDS: Explore elimination of the dairy product price support program and the dairy export incentive program and use budget savings to enhance the safety net for producers. <i>16 in favor, 0 opposed, 1 abstaining</i>	57
7	STRONGLY CONSIDER THE ELIMINATION OF END PRODUCT PRICING. Explore alternative measures to the current end product pricing system, such as competitive pricing and mandatory price reporting. <i>17 in favor, 0 opposed, 0 abstaining</i>	60



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NUMBER	RECOMMENDATION	PAGE
8	COLLECT AND PUBLISH PRICE DATA. Collect and publish data on alternative measures of a competitive pay price, considering but not limited to the proposals of the National Milk Producer Federation and Maine Dairy Industry Association. <i>15 in favor, 2 opposed, 0 abstaining</i>	60
9	ADOPT A GROWTH MANAGEMENT PROGRAM. The federal government should adopt a growth management program that allows new producers to enter and allows producers to expand production. <i>9 in favor, 8 opposed, 0 abstaining</i>	61
<b>INCOME PROTECTION AND STABILIZATION</b>		
10	ESTABLISH RISK MANAGEMENT MARGIN LINES OF CREDIT. USDA should develop a credit mechanism (direct lending or credit guarantee) for first buyers of milk (cooperative or proprietary) to cover the margin deposits required on contracts for risk management between first buyers and producers of raw milk. <i>17 in favor, 0 opposed, 0 abstaining</i>	65
11	MODIFY MILK INCOME LOSS CONTRACT PROGRAM AND PROVIDE A MARGIN INSURANCE OPTION using funds from the elimination of the DPPSP and DEIP. Continue MILC, with a production cap based on available funds, with two important modifications: (1) use an all-milk income/feed cost margin trigger, and (2) provide an insurance program for production excluded by the cap to provide protection for larger producers. <i>15 in favor, 2 opposed, 0 abstaining</i>	68
12	ADOPT TAX-DEFERRED FARM SAVINGS ACCOUNTS. Federal tax law should be amended to allow dairy farm operators to create special tax-deferred savings accounts. These accounts should not be subject to matching government contributions and should not have a limit on dollars deferred per year. To be eligible, contributions must remain in the account for a minimum of six months; the account-holder can withdraw their funds at their own discretion thereafter. Payment of income taxes on contributions and interest would occur in the tax year in which the funds are withdrawn. <i>17 in favor, 0 opposed, 0 abstaining</i>	71
<b>PROFITABILITY AND MARKET IMPROVEMENT</b>		
13	SUPPORT COMPETITIVE MARKET STRUCTURES. USDA, through its regulatory authority and in cooperation with FTC and DOJ, should continue to monitor and support competitive marketing structures throughout the supply and marketing chain of the dairy industry. <i>17 in favor, 0 opposed, 0 abstaining</i>	74



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<b>NUMBER</b>	<b>RECOMMENDATION</b>	<b>PAGE</b>
14	<p>MAINTAIN AND EXPAND PROGRAMS FOR EXPORT MARKET DEVELOPMENT. Continue and expand programs like the Market Access Program and the Foreign Market Development Program.</p> <p><i>17 in favor, 0 opposed, 0 abstaining</i></p>	76
15	<p>SUPPORT REDUCTION OF SOMATIC CELL COUNT STANDARD. Recommend that the Secretary of Agriculture support the adoption of a maximum somatic cell count of Grade A milk in the amount of 400,000 cells per milliliter at the farm level at the Interstate Milk Shippers Conference. The implementation should occur over a period of time not to exceed 48 months.</p> <p><i>17 in favor, 0 opposed, 0 abstaining</i></p>	79
16	<p>ENHANCED FLUID MILK SOLIDS STANDARDS. Encourage the Secretary to explore the impacts of California-type fortification standards for U.S. beverage milk.</p> <p><i>17 in favor, 0 opposed, 0 abstaining</i></p>	81
17	<p>RESTRICT USE OF DAIRY DESCRIPTORS ON PRODUCT LABELS. Recommend that USDA support restriction of dairy descriptors, including terms such as milk, cheese, yogurt, butter, for use on products made from milk.</p> <p><i>17 in favor, 0 opposed, 0 abstaining</i></p>	84
18	<p>SUPPORT FOR VALUE-ADDED DAIRY. The Secretary of Agriculture should support programs that enhance value-added market development for dairy farms and dairy products. Opportunities include, but are not limited to, the development of educational training programs and technical assistance for farms, inspectors, and regulatory personnel to accommodate unique value-added dairy farm operations. A study should be made to examine the impact of user fees on value-added dairy product operations.</p> <p><i>15 in favor, 0 opposed, 2 abstaining</i></p>	86
19	<p>PROVIDE INCENTIVE PAYMENTS FOR ENVIRONMENTAL PRACTICES. The Secretary of Agriculture should increase the amount of money available for incentive payments to dairy farmers for environmental practices that address social, economic and environmental benefits to dairy farm communities.</p> <p><i>16 in favor, 1 opposed, 0 abstaining</i></p>	88
20	<p>CONTINUE THE EQIP AND GRANT PROGRAMS. Continue the EQIP program and give dairy farmers preference in grant programs for implementation of energy audits, infrastructure development for value-added processing and distribution facilities, construction of facilities to meet food safety regulations and farmland protection, and to allow beginning farmer loans for farm transfers between generations.</p> <p><i>15 in favor, 1 opposed, 1 abstaining</i></p>	89
21	<p>PHASE OUT ETHANOL SUBSIDIES. Support the rapid phase out of the blender's credit and tariff on imported ethanol.</p> <p><i>16 in favor, 1 opposed, 0 abstaining</i></p>	91
22	<p>DAIRY HERD HEALTH. Create a program to rapidly eradicate TB and Johnes from the U.S. dairy herd</p> <p><i>17 in favor, 0 opposed, 0 abstaining</i></p>	93



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NUMBER	RECOMMENDATION	PAGE
23	DAIRY LABOR. The Secretary of Agriculture should use his influence with other agencies and Congress to provide a legal means for dairy farms to employ year-around long-term immigrant labor. Provide assurance that existing farm laborers have the opportunity to obtain permanent resident status. <i>13 in favor, 1 opposed, 3 abstaining</i>	98

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2 **Signed:**

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_____	_____
Paul Bourbeau	Randy Romanski
_____	_____
Jay Bryant	Robert Schupper
_____	_____
Erick Coolidge	Manuel (Ray) Souza
_____	_____
Timothy Den Dulk	Patricia Stroup
_____	_____
Debora Erb	Sue Taylor
_____	_____
James Goodman	Edward Welch
_____	_____
James Krahn	James (Ricky) Williams
_____	_____
Edward Maltby	Robert Wills
_____	_____
Andrew Novakovic	



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1 **Introduction**

2 With the ink barely dry on the 2008 Farm Bill, the U.S. economy descended into the worst  
3 recession since the Great Depression of the 1930s. The dairy industry suffered a combination of  
4 recession-driven demand effects and more sector-specific supply effects. Dairy exports, which had been a  
5 primary contributor to dairy farm prosperity in 2007 and 2008, collapsed as global demand declined.  
6 Domestic demand, especially in foodservice, also shrank as consumers trimmed household budgets. On  
7 the supply side, feed costs, the single largest expense of milk production, hit record highs. This created  
8 the worst margin squeeze since the early 1970s and pushed most dairy farm businesses into the red,  
9 eliminating years of growth in dairy farm balance sheets. Although net income for dairy farmers  
10 improved in 2010, weakened balance sheets leave farmers vulnerable to any near-term negative margins.

11 This report reviews current and possible new federal laws and programs intended to assist dairy  
12 farmers, and it discusses their potential application and impacts in various market environments. Milk  
13 and dairy product markets begin with industries that provide products and services to dairy farmers and  
14 end with consumers of traditional dairy products and other products containing significant dairy  
15 ingredients. This report will attempt to highlight significant implications and considerations along the  
16 entirety of the supply chain, but its orientation is defined by the Secretary's charge to focus on the twin  
17 issues of milk price volatility and dairy farm profitability.

18 **Milk Price Volatility**

19 A Working Definition of Price Volatility

20 Since the collapse of prices in 2009, it is common to hear milk prices described as "volatile". The  
21 image this connotes is negative, but beyond that it is not a well-defined concept. Prices can be considered  
22 to have three fundamental dynamic characteristics: certainty, stability and adequacy.

23 Certainty means that a future price is predictable. The more confident a prediction is, in amount  
24 and distance, the greater the price certainty. Certainty can be measured by the difference between the  
25 future price one expects at a future time and the actual price that is realized.

26 Stability refers to how much price changes over time. This involves the frequency and size of  
27 change. A price that never changes is stable and predictable, but otherwise the two concepts are



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1 independent. For example, a highly seasonal price pattern might be quite predictable while still being  
2 “unstable.” Stability can be measured statistically in several ways, involving either amplitude or  
3 frequency. Adequacy is a more subjective assessment, but it concerns whether a price returns positive net  
4 revenue to the seller.

5 With this in mind, the Committee used the following description of volatility to consider and  
6 evaluate policy solutions to the problem of volatility:

7 *Prices that are volatile over time are unpredictable, unstable, and at least occasionally*  
8 *inadequate.*

9 This, of course, does not preclude the possibility of prices being very advantageous to a seller at other  
10 times.

11 Causes of Price Volatility in the Dairy Sector

12 Before the Agricultural Act of 1949 established the Dairy Price Support Program (DPSP), farm  
13 milk prices exhibited a high degree of instability. The relative spread from high to low was generally as  
14 great or greater than the dispersion in milk prices known today. The frequency was quite different as the  
15 earlier fluctuations were entirely seasonal, whereas today one or more cyclical components overwhelm a  
16 seasonal component. This instability had its effects, but these fluctuations were primarily seasonal and  
17 generally predictable.

18 From 1950 to 1989, milk price variability was considerably dampened compared to the first half of  
19 the 20th century. During the 1970s, the primary price mover was inflation, which affected the entire U.S.  
20 economy. To offset surpluses generated by aggressive support price policies of the late 1970s, from 1981  
21 to 1990, dairy markets were affected by a variety of significant government programs, including large  
22 product purchases and two new, temporary supply management programs. Beginning in 1983, the support  
23 price for milk used in manufacturing was gradually reduced from over \$13.00 per cwt. to under \$10.00,  
24 where it has more or less remained. At this low level of support, government purchases have been  
25 infrequent. While there clearly were price issues in the 1970s and 1980s, volatility, as defined in this  
26 report, would probably not be the word used to describe them.

27 Since 1990, the farm milk price has become highly variable and unpredictable. The causes of this  
28 increased volatility are debatable but likely involve policy or regulatory issues and economic factors. As a



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1 policy matter, the reduction of the federal support price for milk during the 1980s may have revealed an  
2 underlying susceptibility to volatility.

3 Price volatility in the last decade also corresponds to significant changes in administration of  
4 federal dairy programs. The base price for Federal Milk Marketing Order formulas was changed from a  
5 competitive pay price survey of prices paid to a subset of dairy farmers by otherwise unregulated plants  
6 (the Minnesota-Wisconsin [M-W] price and then the so-called Basic Formula Price [BFP]) to class prices  
7 derived from the wholesale prices of four dairy commodities (product price formulas or end product  
8 pricing). This change had the effect of directly tying farm price volatility to the volatility of wholesale  
9 prices for dairy commodities, which had always been more volatile than the previous competitive pay  
10 price series for milk. The switch to a product formula price occurred in 2000.

11 Another significant policy event that seems to have changed dairy markets was the conclusion of  
12 the Uruguay Round negotiations under the General Agreement on Tariffs and Trade, now referred to as  
13 the World Trade Organization (WTO). In the United States, the Uruguay Round Agreements Act was  
14 passed in 1994. Under the Agreement on Agriculture (AoA), the U.S. and other developed countries  
15 agreed to provide access to its dairy markets by foreign competitors equal to about five percent of total  
16 U.S. sales with relatively low levels of tariff protection (this roughly doubled U.S. imports from about 2.5  
17 percent to five percent of sales). Above this level, the U.S. replaced its strict import quota system with a  
18 tariff-based system that generally provides a high degree of protection for most dairy commodities but  
19 greater access to value added products, such as European-style cheeses. In exchange for increasing access  
20 to foreign marketers, the U.S. dairy industry gained greater access to foreign markets. Increased trade  
21 subjected U.S. dairy markets to the effects of changes in world supply and demand conditions, including  
22 weather, political shocks and foreign food safety issues. This increased trade opportunity may also have  
23 contributed to increased price instability.

24 The somewhat unusual position of the U.S. among world dairy product traders may be a  
25 compounding factor. The US is among the largest producers of milk and milk products in the world. Its  
26 cost structure puts it in the rather unusual position of being either a potential net importer or net exporter.  
27 U.S. buyers tend to import high-value cheeses and other specialized products and sell low-value  
28 commodities, especially dry powders. As such, the U.S. has tended to be a net importer on a dollar value  
29 basis since the Uruguay Round agreement, but on a milk equivalent basis it has often been a net exporter.



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1 This has been increasingly true in the last several years. Periods of net export have been the result of a  
2 combination of factors, including strong world demand, weak supplies by more consistent exporters, and  
3 favorable exchange rates. While the U.S. is hardly unique in being susceptible to swings in world  
4 markets, its vacillation between being a net importer or net exporter is unusual and perhaps puts it in a  
5 more volatile position.

6 Another policy element that may contribute to persistence in dairy farming and milk production,  
7 despite economic stress on farms, is the pooling of returns under federal and state milk marketing orders.  
8 Marketwide pools, which have been the norm for milk pricing for the last century or so, represent a  
9 system of average pricing whereby processors pay a much different price for milk than the individual  
10 price that farmers receive. This is because processors pay minimum regulated classified prices based on  
11 their product sector, whereas dairy farmers receive a weighted average of the various classified prices,  
12 regardless of the products that are made from their own milk. While useful in ensuring that farmers do not  
13 destructively compete<sup>2</sup> with one another for the highest valued market, pooling mutes price signals that  
14 would otherwise discourage production from individual producers or suppliers facing a down market or  
15 subsector.

16 Although not a matter of public policy per se, a related element is that the vast majority of the milk  
17 marketed in the U.S. is marketed via cooperatives, and the cooperative business model has long been to  
18 accept responsibility to market whatever volume of milk a producer chooses or is able to produce.<sup>3</sup> In  
19 periods of stress, when markets are long, there is essentially no marketing risk for a producer, in the sense  
20 that every pound of milk produced will be purchased. Cooperatives cannot simultaneously agree to

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<sup>2</sup> "Destructive" competition is a term used historically to describe competition between dairy farmers for high priced markets or buyers that results in lower average prices for all farmers. Competition between buyers and sellers can be difficult but it is generally considered to be "constructive" provided the competitive conditions are fair and balanced.

<sup>3</sup> Of course there are exceptions to this general rule. A few cooperatives have long operated a "closed membership", to control growth by restricting entry. In recent years, it has become more common for cooperatives to institute short or longer term restrictions on individual farm growth, especially when the cooperative is processing its member's milk directly.



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1 market every pound of milk and guarantee a favorable price. Prices must be able to adjust to clear the  
2 market. Pooling, combined with the essentially unlimited cooperative guarantee to purchase all milk  
3 produced, is likely to exacerbate price volatility because those practices tend to delay production  
4 adjustments when prices are low. When the Dairy Price Support Program was more aggressively used, it  
5 essentially guaranteed a government outlet for surplus dairy commodities and many cooperatives invested  
6 in producing these sorts of products, especially nonfat dry milk and butter (which also happen to be  
7 highly tradable products in world markets). This also helps to explain the relatively open-ended  
8 purchasing agreements cooperatives have had with their members. This marketing and pricing system  
9 has been in place for about a century; so modern price volatility cannot be blamed on pooling and market  
10 security, but those two elements likely do confound the ability of the marketplace to react to volatility  
11 caused by other factors.

12 In terms of the internal economics of the sector, dairy analysts have described dairy markets as  
13 having low price elasticities of supply and demand for farm level milk, and inelastic price elasticity of  
14 demand for many dairy products throughout the market chain. While analysts debate the degree of  
15 elasticity, most agree that short-term elasticities are small. As such, small relative changes in quantities  
16 are associated with relatively large changes in price. This has always been true for dairy markets, and  
17 some have argued that it is less true today. Regardless, the reduction in price support exposes the industry  
18 to this kind of volatility more now than when the DPSP was more important in establishing market prices.  
19 Product formula pricing may further aggravate the volatility enhancing aspects of product supply and  
20 demand inelasticities. Because this form of pricing regulates the margin between the four dairy  
21 commodity output prices and the minimum price that processors of those products must pay for milk,  
22 manufacturers have much less margin risk as long as they produce those specific commodities or a  
23 product whose price is highly correlated with one of them.

24 One reason for the low degree of milk supply elasticity is that dairy farming is a production activity  
25 that is characterized by a high degree of asset fixity. An operating farm will endure a great deal of short  
26 term stress (negative cash flow) as long as the operator believes that the farm will be profitable in the long  
27 term and sufficient credit or reserves exist to get through the negative period. Moreover, the generally  
28 high degree of fixed costs and the fact that cows are not machines that can be simply turned off means  
29 that it generally makes sense in the short term to produce at full capacity. Thus, in periods of low or



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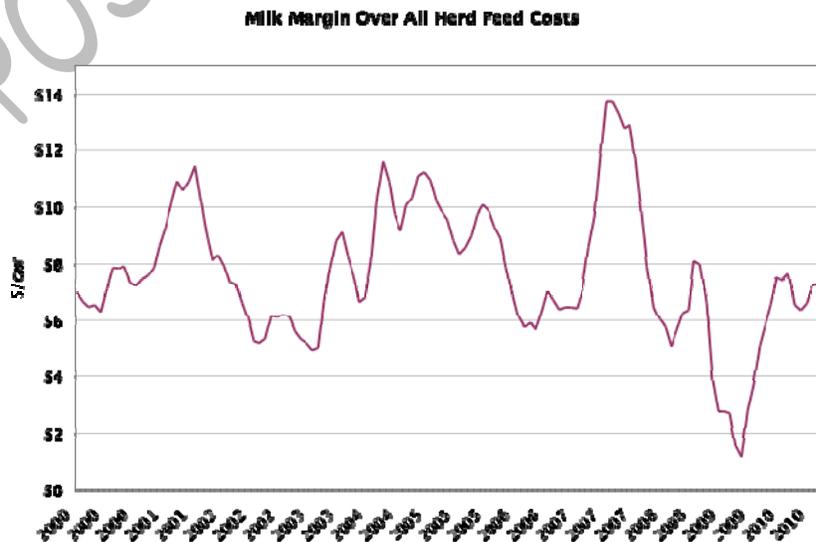
1 negative margins, farmers will continue to produce until they decide to discontinue their business or their  
2 access to credit is eliminated.

3 **Dairy Farm Profitability**

4 In addition to swings in milk price, dairy farmers have experienced significant changes in prices of  
5 feeds and other production inputs. Feed is the single largest milk production cost component (40-50  
6 percent). Thus, dairy farmers are especially sensitive to the prices of purchased feeds or to the prices of  
7 inputs used in homegrown feed production. Key feedstuffs include corn, soybean meal, and alfalfa hay.  
8 Other important production inputs are energy and labor and—for those who grow their own feed—fuel,  
9 fertilizer and seed.

10 From Fall 2006 through Summer 2008, the price of corn increased from about \$2.00 to about \$5.50  
11 per bushel. The increase in soybean prices was equally dramatic. Among the causes of feed price  
12 increases, expanded bio-fuel production created a large and new demand for corn and contributed to the  
13 price increase for soybeans and other crops. Weather and international grain demand also contributed to  
14 high feed costs.

15 Milk prices were moving to a cyclical low in 2006. As a result of the high feed costs that in turn led  
16 to decreased milk supply, the  
17 price of milk rose from a low of  
18 \$11.70 per cwt. in July 2006 to a  
19 high of \$21.90 in November  
20 2007—the all time record high  
21 for the nominal price of milk. By  
22 the end of 2008 and through  
23 2009, the farm profitability  
24 equation had again turned against  
25 dairy farmers. Although corn  
26 prices and other input costs  
27 softened from their highs, milk  
28 prices fell even more. The





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1 problem in 2009 was not just the low price of milk, which was no lower than the levels of the previous  
2 two cycles. The problem was extremely low to negative margins. In many months, the milk check barely  
3 covered the cost of feed. This is illustrated in the accompanying chart<sup>4</sup>

4 Clearly, the low point in milk margin over feed costs (\$/cwt) during 2009 is far lower than the  
5 previous troughs in 2006 and 2002 although milk prices were approximately the same in the three years.  
6 The distinction between prices and margins is important. Prices influence margins and financial  
7 outcomes, but output price alone does not determine farmers' well-being. Most dairy and other  
8 agricultural support programs are based on or triggered by an output price, such as milk price. The  
9 usefulness of that simple approach has been seriously challenged by the events of the last two years and is  
10 a concern looking forward.

11 The experience of 2009 has sensitized industry members and analysts that a milk price that looks  
12 good, or even high, by purely historical comparisons can easily be inadequate when input prices are high.  
13 This has caused much attention to be focused on alternative measures of profitability in dairy farming.  
14 The need for this is attenuated by a general feeling that grain prices have likely shifted to a new average  
15 level and that recent "highs" may prove to represent a new "normal."

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<sup>4</sup> This chart uses a margin methodology developed by the National Milk Producer's Federation in its Foundation for the Future proposal combined with USDA price data. There are several ways to measure margins or other indicators of the relationship between the price of milk and the prices or costs of feed, or farm returns more generally. The methodology proposed by NMPF is reasonable; however, in using it in this paper, the Committee does not imply a formal endorsement of their methodology.



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1 Measures of Profitability

2 *Recommendation 1:*

3 *DEVELOP A SYSTEM THAT PROVIDES AN ACCURATE ASSESSMENT OF DAIRY*  
4 *FARM PROFITABILITY. A data gathering and reporting system should be developed that*  
5 *expresses farm profitability in the dairy industry using an index to provide an impartial*  
6 *overview of the general level of profitability at the farm level based on the milk price-feed*  
7 *cost margin.*

8 There is no single best way to describe or measure dairy farm profitability. Various concepts are  
9 used, and each can lead to rather different perspectives on "profitability" of dairy farmers.

10 Two observations reveal a basic conundrum about the apparently simple concept of profitability. In  
11 1975, USDA estimates that 443,610 "operations" reported having milk cows and total milk production  
12 that year was 115,398 million pounds. In 2009, USDA estimates that there were 65,000 operations having  
13 dairy cows and annual production was 189,320 million pounds. Thus, the number of operations declined  
14 85% while production increased 64%.

15 It is tempting to use the data on number of dairy operations as evidence that there must be a long-  
16 term problem with dairy farm profitability. Even from year to year, it is common to describe poor  
17 profitability across the sector as the cause for dairy farms going out of business. On the other hand, if one  
18 looks at the growth in milk production, it is just as logical to say that dairy farming must have been  
19 profitable to support that level of growth over so many years.

20 Data on farm numbers and prices are simple facts about the U.S. dairy sector. Interpreting these  
21 facts and translating their meaning for questions like "are dairy farms profitable" or "is dairy farm  
22 profitability a long term problem" is less straightforward. Perhaps the simplest conclusion that can be  
23 made from these data is the following: Farm milk prices have not kept pace with consumer price  
24 inflation<sup>5</sup>, but apparently the lower rate of increase in farm milk prices has been adequate to support an

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<sup>5</sup> The US average price paid for all milk went from \$8.78 in 1975 to \$12.83 in 2009. Given the instability of prices in both periods, as opposed to the steady trend in milk production and the number of farms, a



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1 impressive long-term increase in milk production. However, it is equally clear that many farm operators  
2 have found the increase in price to be "inadequate". The decline in numbers of farm operations that milk  
3 cows is testimony that these farmers have found better places to invest their equity, labor and  
4 management skills and/or that farmers reached normal retirement decisions and those farms were  
5 consolidated rather than passed on as is to a new generation. By the same token, the increase in milk  
6 production means that there is a group of farmers who have found profits to be sufficient to justify  
7 continuing and even expanding.

8 If nothing else, this simple exercise reveals the difficulty in using averages to explain the complex  
9 economic factors and outcomes related to dairy farming.

10 Whether looking at an average or results for a specific farm, another question is how one ought to  
11 measure profitability. Operators will logically use different criteria to measure profit depending on their  
12 goals, size, business structure, location, etc. High prices do not ensure high farm level profitability, and  
13 prices that are more modest do not condemn farms to a lack of profitability. It is the relationship between  
14 cash revenue and cash costs that keeps farms in business in the short term (liquidity), and measures such  
15 as the return on equity or net farm income that define the long-term profitability of the farm operation.  
16 There are many different production practices and, as with many small businesses, plenty of  
17 entrepreneurial initiative and innovation that make a single standard for farm profitability difficult to  
18 define. Some farms may be unprofitable in the long term, even though they have positive cash flow from  
19 most years to the next. Other farm families may be eligible for public assistance for health insurance and  
20 food stamps but still see dairy farming as the best place to invest their equity and labor. In assessing dairy  
21 farm profitability, lenders will use criteria based on their standard loan practice and current government

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better indication of trend is to consider the average prices in the early 1970s vs. the late 2000s. These values are approximately \$8 per cwt. and \$15, respectively. This is an increase of 88%. Over those same time periods, the Consumer Price Index for all goods increased from about 50 to 196, according to the Bureau of Labor Statistics. If the average farm price had increased by the same percentage, it would have been over \$31 in the 21<sup>st</sup> Century. The "nominal" price of milk increased 88% but the "real" price decreased over 50%.



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1 regulations. The USDA and other Federal agencies may choose different criteria (for example, USDA  
2 Rural Development uses tangible net-worth).

3 In response to the economic crisis experienced by much of the agricultural sector in the early  
4 1980s, the American Bankers Association decided that there was a need to standardize how farm financial  
5 performance is measured. This ultimately led to the creation of an independent organization called the  
6 Farm Financial Standards Council. The FFSC is a voluntary, not for profit organization that seeks "to  
7 create and promote uniformity and integrity in financial reporting and analysis for agricultural producers."  
8 It currently endorses 21 specific measures of financial performance. Different groups of measures are  
9 deemed to be alternative and useful indications of liquidity, solvency, profitability, repayment capacity,  
10 and financial efficiency. A description of each is provided in Appendix A.

11 In considering the concept of dairy farm profitability, the status of dairy farm profitability  
12 currently, and alternative ways to assist farmers in improving profitability, the Committee discussed  
13 numerous aspects of these questions. While we recognized that it is very appealing to have one "best"  
14 measure that could be used to gauge farm profitability over time or to guide public policy actions, in the  
15 end we concluded that no single measure is "best" for all purposes. Some measures are appealing because  
16 they can be calculated or estimated without a lot of data. They are simple. Other measures are more  
17 appealing conceptually, but they are complex and difficult to calculate.

18 Recognizing that there are appropriate times and applications for different measures, we conclude  
19 that a margin measure, such as the average (per cwt) net return from the sale of milk less the cost of  
20 purchasing feed to produce 100 pounds of milk – the milk margin over feed costs – is a simple but useful  
21 measure of short term financial performance of dairy farm businesses.<sup>6</sup> The milk margin over feed cost

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<sup>6</sup> USDA has reported a ratio of the all milk price to an index of feed prices for decades. The milk-feed price ratio is the pounds of 16% protein mixed dairy feed equal in value to 1 pound of whole milk. The higher the ratio, the more feed a dairy producer could buy with proceeds from the sale of a pound of milk. Reported monthly by USDA, feed prices used in the ratio are based on current U.S. prices received for corn, soybeans and alfalfa hay. The milk: feed price ratio has been a familiar and easy tool for indicating net returns to dairying: however some recent research has highlighted that in times of great volatility this measurement is not accurate (Understanding the milk-to-feed price ratio as a proxy for dairy farm profitability: CA Wolf October 2010, Journal of Dairy Science.). While conceptually related, a composite



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1 does not account for other production cost components, such as labor, energy, depreciation, capital,  
2 veterinary services, and nutritional supplements. These costs vary greatly across individual operations,  
3 either by region or the structure of the farm business. These other costs are probably not as volatile as  
4 feed costs; hence, the milk margin over feed cost remains a fairly reasonable short-term indicator of farm  
5 financial performance. However, individual producers will need to take into account their own  
6 circumstances when evaluating how well this simple national measure represents their financial status.

7 Later in the report, we recommend the use of milk margin over feed costs for policy purposes, but  
8 in so doing, it should be understood that we do not think it is the "best" measure of profitability. As a type  
9 of cash flow measure, it falls in the financial category FFSC describes as a measure of liquidity.

10 Alternatively, net farm income (NFI) is an appealing measurement of profitability and can be especially  
11 useful in comparing the profitability of different dairy farms. Return on equity (ROE), another measure of  
12 profitability endorsed by FFSC, is a helpful measurement when comparing profitability in dairy to other  
13 agricultural or even non-agricultural businesses.

14 The Status of Dairy Farm Profitability

15 The impact on business equity and liquidity for farmers in 2009 was at an unprecedented level that  
16 will need many months, if not years, of higher net returns to remedy. Those dairy farms that are under  
17 most pressure are farms that:

- 18 • Must purchase feed
- 19 • Have highly leveraged assets
- 20 • Rely heavily on cash flow from the farm business for household income

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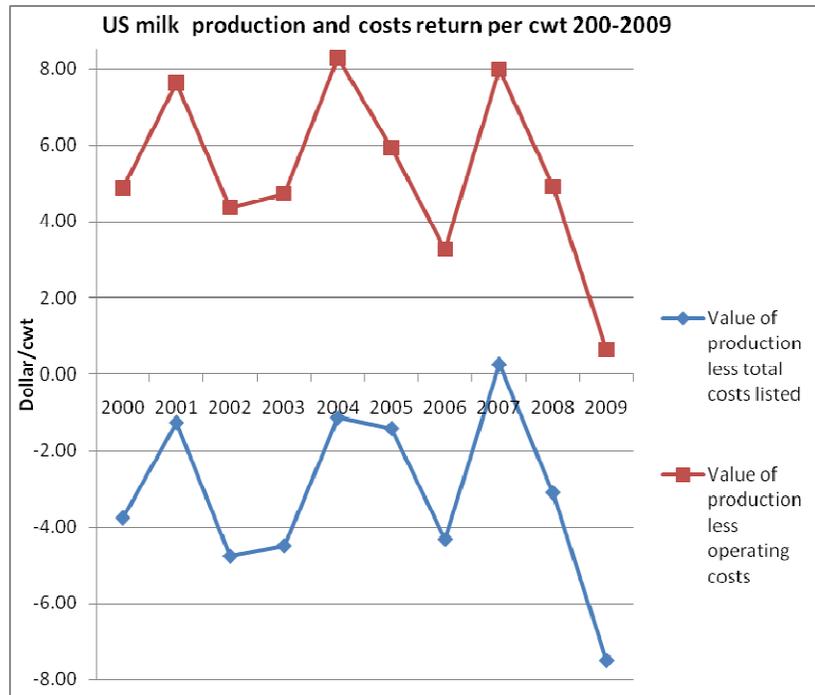
index of prices of feed is not the same as the average cost of the same feeds used to produce 100 pounds of milk. The first is simply a ratio of prices; the second results in a margin per cwt of milk produced.



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1 Economists at USDA-ERS estimate costs of production on dairy farms across the US<sup>7</sup>. Their  
 2 reports estimate operating and total costs of production and various returns per hundredweight (cwt),  
 3 including hired labor, general  
 4 farm overhead, taxes, insurance,  
 5 and non-cash items. From these  
 6 basic data and estimates, it is  
 7 possible to calculate measures of  
 8 profitability like Net Farm  
 9 Income or Return on Equity.  
 10 The accompanying chart uses  
 11 this data source to illustrate net  
 12 returns over total and operating  
 13 costs. It clearly shows the  
 14 collapse in 2009.



15 The dairy industry is very  
 16 diverse in production practices,  
 17 location, capital investment, overhead costs, and expectations. Estimated averages certainly do not  
 18 describe every farm situation, some of which are much worse, some much better, and many of which  
 19 follow a somewhat different pattern over time. Nevertheless, these estimates bear witness to the severe  
 20 economic challenge experienced across the dairy sector in 2009. Perhaps even more importantly for long-  
 21 term policy, the chart also indicates that dairy farms experience a considerable amount of margin  
 22 volatility.

### 23 Current Legislative and Regulatory Authorities<sup>8</sup>

<sup>7</sup> USDA ERS: Recent Costs and Returns, United States and ERS Farm Resource Regions, New Format and Regions.

<sup>8</sup> A tabular summary of the objectives and legislative authorities for major dairy programs is provided in Appendix B.



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1 Dairy programs are legal authorizations or mandates specified by Congress and implemented as  
2 regulations by the USDA or another executive agency of the federal government. Some of these programs  
3 exist under permanent law while others are temporary. Temporary programs may exist for many years,  
4 but periodically Congress needs to reaffirm them. The so-called Farm Bill is an “omnibus” legislation that  
5 mostly codifies changes to laws and programs that exist in other statutes. Therefore, it is usually a bill of  
6 amendments to existing law. Underlying laws, such as the Agricultural Adjustment Act of 1933, the  
7 Agricultural Marketing Agreement Act of 1937, and the Agricultural Act of 1949, contain the original  
8 authorizations for basic dairy programs. This chapter of the report focuses on existing laws and programs  
9 and attempts to offer the Secretary guidance in how the existing programs might best be used in those  
10 cases where the Secretary has some discretion and flexibility. It is also an objective to better inform the  
11 dairy community about existing laws and the opportunities and limits that the Secretary faces in working  
12 within existing statutes and regulations.

13 Congress has latitude in how strongly it directs an action of the Executive Branch. In many cases, a  
14 law authorizes USDA or another agency to do something, but it does not require or even enable that  
15 action. For example, under the old parity-based Dairy Price Support Program (DPSP), USDA could  
16 announce a support price for milk that was no less than 75 percent of the parity price but no more than 90  
17 percent. Thus, USDA was authorized to choose within a range. Sometimes USDA is permitted to do  
18 nothing at all. For example, USDA is not required to implement a Federal Milk Marketing Order, either  
19 by the instruction of Congress or at the request of farmers. The Secretary has the authority to deny a  
20 request for a new Order or even suspend or discontinue an existing Order. Lastly, Congress may give the  
21 Secretary authority to act but not provide necessary funding, so, as a result, the policy is not implemented.

22 Current programs have direct effects on milk prices, dairy product sales, farm incomes, and other  
23 direct aspects of dairy profitability and volatility. Many programs exist outside of USDA authority that  
24 affect dairy markets, including tax policy, public borrowing, transportation, energy, environment, labor  
25 policy, and food regulations. The primary focus in this report will be on dairy-specific programs that  
26 could reasonably impact farm level dairy markets. Where a recommendation is made for an action not  
27 under the direct purview of the Secretary of Agriculture, the Committee encourages the Secretary to exert  
28 influence and resources are at his disposal to encourage the appropriate agency or agencies to adopt the  
29 recommended action. Where there are specific recommendations related to the operation of an existing



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1 program (as opposed to creating new legislation to modify an existing program), that recommendation is  
2 made at the beginning of each program section. A concluding recommendation is offered that spans  
3 several programs.

4 The Committee offers its recommendations with awareness that the President's Office of  
5 Management and Budget (OMB) may constrain executive discretion and, therefore, policy  
6 implementations. The Committee also acknowledges the risk of undesired and/or unanticipated  
7 consequences of any policy choice. Individually and collectively, members of the Committee assessed  
8 the consequences of each recommendation along the dairy supply chain.

9 The Office of Management and Budget

10 The Secretary of Agriculture can only initiate and operate programs 1) which he is authorized to  
11 administer and 2) which have a well-defined mandatory or discretionary source of funding. If a program  
12 is mandatory, Congress provides authority to spend whatever money is required to achieve the purposes  
13 of that act. If the program is discretionary, Congress may or may not provide funding to support the  
14 program. When funding is limited, which is often, the Office of Management and Budget plays a crucial  
15 role in determining which programs may be implemented.

16 OMB implements and enforces Presidential policy government-wide through “budget development  
17 and execution, agency management, coordination and review of all significant Federal regulations by  
18 executive agencies, review and clearance of all agency communications with Congress, and executive  
19 orders and Presidential memoranda.” ([http://www.whitehouse.gov/omb/organization\\_mission/](http://www.whitehouse.gov/omb/organization_mission/))

20 OMB has significant influence on the spending ability of any federal agency, including USDA.  
21 When Congress provides a clear mandate and sufficient funding to conduct a program, OMB's primary  
22 concern is the efficient execution of the required program. However, when an authorized program is  
23 unfunded or underfunded, the Secretary must work with OMB to determine where funding might be  
24 available or even whether any such funding can be found. Inasmuch as OMB reports to the President,  
25 OMB's priorities, both programmatically and from the standpoint of financial stewardship, are driven by  
26 the President's overarching priorities. In periods when budgets are tight, OMB tows a hard line on  
27 discretionary spending. Even when budgets have some room, OMB will and must evaluate tradeoffs when  
28 an Executive agency, like USDA, makes a request.



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1 Comments on Possible Unintended Consequences

2 One of the challenges in any public policy is that few choices make everyone better off. Instead,  
3 policies involve tradeoffs. In the dairy sector, tradeoffs exist among producers and among dairy  
4 processors, retailers, consumers, taxpayers, and alternate agricultural and food sectors. Because of this,  
5 we recognize, for example, that policies that are good for some dairy farmers may not be good for all  
6 dairy farmers. This is evident in the ongoing public debates related to varying farm size, business models  
7 and regions of the U.S.

8 While we have not been charged to address business or individual issues that derive primarily  
9 beyond the farm sector, we cannot look at farm level policy solutions without considering their possible  
10 downstream effects over time.

11 We also recognize that the Secretary has a responsibility to balance and represent a public interest  
12 in the administration of USDA programs and acknowledge that achieving that balance is a difficult task.  
13 The purpose of the policies discussed here is to counter extreme market conditions, but not to eliminate  
14 fundamental market functions.

15 **The Dairy Product Price Support Program**

16 *Recommendation Note:*

17 *At the conclusion of the chapter on existing laws and programs, we offer a recommendation*  
18 *that relates to the Secretary's use of the DPPSP. We also make a recommendation*  
19 *concerning legislative changes that impact the DPPSP.*

20 The Dairy Price Support Program (DPSP) was authorized under the Agricultural Act of 1949 and  
21 has been reauthorized by subsequent Farm Bills. The Act gave the Secretary of Agriculture discretion to  
22 establish a support price that would cover 75-90 percent of "parity" (a measure of farmers' purchasing  
23 power in comparison to a base period in the early 20<sup>th</sup> century). In 1981, Congress suspended the  
24 requirement that the Secretary establish support prices within that range and, in 2008, the parity language  
25 was deleted.

26 The 2008 Food Conservation and Energy Act (FCEA or "Farm Bill") also altered the purchase  
27 price targets, replacing a "support price" for milk with "purchase prices" for commodity cheddar cheese,



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1 butter and nonfat dry milk. This altered program was titled the Dairy Product Price Support Program  
2 (DPPSP). Purchase prices, specified in law by FCEA or announced by USDA prior to 2008, did not  
3 change significantly and are listed in the following table.

4 Dairy product manufacturers initiate the process of moving surplus product off the market to  
5 government storage. USDA is obliged to buy any and all quantities of eligible product offered at the  
6 announced purchase prices. Typically, any such product so acquired will either be sold back into  
7 commercial markets at the statutory sellback price or will be made available for use in an international  
8 food assistance program (for example, under Sec. 416(b) or one of the domestic programs, such as  
9 TEFAP or School Lunch).

Price	Before FCEA 08	After FCEA 08
Support Price for Milk Used in Manufacturing, average fat test (per cwt)	\$9.90	not specified
Purchase Price for Cheddar Cheese, blocks (per pound)	\$1.1314	\$1.13
Purchase Price for Cheddar Cheese, barrels (per pound)	\$1.1014	\$1.10
Purchase Price for Butter (per pounds)	\$1.05	\$1.05
Purchase Price for Nonfat Dry Milk (per pound)	\$0.80	\$0.80

10

11 To the extent that manufacturers take advantage of this guaranteed price, wholesale market prices  
12 should not fall below the government offer price, or at least not by very much. In practice, sellers show  
13 some reluctance to sell cheese and butter to the government. USDA issues standards for product  
14 purchases that do not match the standards required by commercial buyers and payment terms are outside  
15 of industry norms. Many manufacturers refer to a "cost of selling" to the federal government, with  
16 estimates of that cost in the neighborhood of 3-5¢ per pound of product. In January 2009 wholesale



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1 cheddar cheese prices were six to seven cents per pound less than the USDA purchase price for three  
2 weeks without generating sales to the CCC. As an approximation, a one-cent per pound change in the  
3 price of cheese equates to about a change of about 10 cents per cwt of milk. USDA should make program  
4 changes that minimize reluctance to participate.

5 The USDA purchase prices assure manufacturers of listed commodities that they will have a  
6 market for those products at those prices. Also, market prices of these products are the foundation for  
7 class prices in Federal Milk Marketing Orders (and to a large extent for the California Stabilization and  
8 Marketing Plan for Market Milk), so the effect of government purchases is widespread. Some analysts  
9 suggest that dairy price supports have resulted in too many resources being directed toward production of  
10 the targeted commodities compared to other products that might have better or broader commercial  
11 market opportunities. If this causes a distortion that leads to inefficient allocation of resources in dairy  
12 markets, returns to farmers will eventually be reduced.

13 Although Congress specified a fixed support price for milk from 1981 to 2008, when it passed the  
14 FCEA it changed specifications of commodity support prices from “shall be” to “shall be no less than.”  
15 In so doing, the Act created authority for the Secretary to announce higher purchase prices than those  
16 specified in the bill. However, this authority was not accompanied with an appropriation that would make  
17 it easy to exercise that authority.

18 USDA used this discretionary authority to increase the purchase prices for cheddar cheese and  
19 nonfat dry milk in August, September and October 2009. Compared to the purchase prices listed in the  
20 table above, the Secretary increased the purchase price of cheddar cheese by 18 cents per pound (16  
21 percent) and nonfat dry milk by 12 cents per pound (15 percent). This action resulted in little dairy  
22 support program purchases of NDM by the CCC, as product prices increased over the same period. In  
23 November 2009, support prices for cheddar cheese and nonfat dry milk under the DPPSP reverted to the  
24 levels specified in the FCEA. The Secretary’s authority to make changes in the DPPSP support prices is  
25 limited by available funding as detailed in the previous discussion regarding the Office of Management  
26 and Budget.

27 **Milk Income Loss Contract**



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*Recommendation Note:*

*In the chapter on alternative laws and programs, we offer a recommendation concerning legislative changes that impact the MILC.*

The Milk Income Loss Contract (MILC) is a form of countercyclical income support that draws some elements from the structure of the (discontinued) Northeast Dairy Compact and the ongoing countercyclical price (CCP) subsidies established for program crops (food and feed grains, etc.) in the Farm Security Act of 2002.

The Northeast Dairy Compact was a Congressionally sanctioned agreement between the six New England states to coordinate a minimum price for Class I milk marketed in their jurisdiction. When Congressional approval for this multi-state Compact expired, the calculation methodology was adapted to a countercyclical income subsidy that would apply to all dairy farmers in the contiguous United States. As such, there are three key variables that determine payments to farmers: the price trigger, the payment rate, and the marketings payment limit.

Following the methodology of the Northeast Dairy Compact, the Northeast Federal Milk Marketing Order, Boston city zone Class I price serves as the price trigger. When the actual Boston Class I price falls below \$16.94, the MILC program becomes active. In the 2008 FCEA, Congress modified the trigger price to include an automatic adjustment for changes in the prices farmers pay for certain feeds used in a dairy ration. USDA's National Agricultural Statistics Service calculates the national dairy ration cost each month. When the monthly ration cost exceeds \$7.35 per cwt, the trigger price is increased by 45 percent of the difference between the ration-cost trigger and the estimated actual U.S. average cost. For example, if the dairy ration cost is estimated to be 10 percent above \$7.35 per cwt, the milk payment trigger rises 4.5 percent (or \$16.94 times 1.045 = \$17.70). The FCEA increases the automatic feed adjustment trigger cost from \$7.35 to \$9.50 per cwt beginning on September 1, 2012.

A payment rate was originally set at 45 percent of the difference between the announced monthly price and the trigger, approximately the same percentage as the Class I utilization in the Northeast Federal Milk Marketing Order. The FCEA reduces the MILC payment rate from 45 to 34 percent of the difference between the announced monthly price and the trigger price beginning on September 1, 2012. There have



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1    been other periods when the payment rate has varied. These changes are made by Congress as a way to  
2    achieve budget targets, not because of conceptual or philosophical changes about the program.

3           Lastly, the MILC has limitation on how much an individual farm operator can receive. The concept  
4    of a payment limit is derived from countercyclical payment programs for other agricultural crops and was  
5    not used in the old Compact. For major program crops, the CCP and other subsidies are generally limited  
6    by a maximum dollar amount. In the case of the MILC, the payment is limited by the number of pounds  
7    of milk on which a subsidy payment can be received. Like the dollar limit, the quantitative limit has two  
8    objectives. First, it limits government exposure to budget costs. Second, it targets limited budget dollars  
9    to provide greater assistance to smaller scale farmers, which Congress has generally favored in the form  
10   of payment limitations and income eligibility rules for other agricultural programs.

11           Currently, dairy producers are eligible to receive payments on up to 2.985 million pounds per fiscal  
12   year. At the national average production per cow, this equates to a farm size of about 150 cows. Producers  
13   whose marketings exceed the cap can choose the month for which they want to start receiving payments.  
14   Marketings prior to that month don't count toward the limit even if the MILC program is active. From that  
15   month, they receive payments for all months in which the program is active until they reach their limit.  
16   The calculation starts over at the beginning of a new marketing year. This means that smaller farmers will  
17   receive a greater proportional benefit relative to their gross income than will a very large farm.

18           Many large-scale producers for which the eligible volume represents a very small portion of their  
19   total production or gross income have criticized the program as being unfair to them. Also, many  
20   producers and analysts believe that the price of milk remains at lower levels for longer periods when  
21   MILC payments are triggered. The extent to which this occurs is debated. Regardless, payments and their  
22   volume limitations are the basis for both political support and criticism of the program.

23           The MILC program is administered by the Farm Service Agency of the U.S. Department of  
24   Agriculture and is a mandatory program over which USDA has no discretionary authority. USDA does  
25   promulgate rules to interpret and enforce the program as authorized by Congress. These rules define  
26   requirements for eligibility and compliance, but they do not alter the fundamental parameters specified in  
27   legislation.

28   **Federal Milk Marketing Orders**



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1 *Recommendation 2:*

2 *REVIEW FEDERAL MILK MARKETING ORDERS. The Secretary of Agriculture should*  
3 *appoint a committee to review implications of Federal Milk Marketing Orders, including,*  
4 *but not limited to, end-product pricing's impact on milk price volatility and impact of*  
5 *classified pricing and pooling on processing investment, competition and dairy product*  
6 *innovation.*

7  
8 *Recommendation Note:*

9 *Although FMMOs provide some valuable services to the dairy sector, their use of end-*  
10 *product pricing and pooling raise concerns. The Committee feels that these are critical*  
11 *issues for addressing our charge, but that we have not been given sufficient resources or*  
12 *time to fully evaluate market order administration within the current legislative context and*  
13 *make more specific recommendations. Some important changes may require Congress to*  
14 *act. In the chapter on alternative laws and programs, we offer a recommendation*  
15 *concerning legislative changes that impact Federal Milk Marketing Orders.*

16  
17 Federal Milk Marketing Orders (FMMOs) are the oldest U.S. dairy industry specific programs.  
18 Milk marketing cooperatives used classified pricing and pooling over 30 years before passage of enabling  
19 federal and state legislation, beginning in the 1930s. Over time, most state laws gave way to the federal  
20 law due to states' inability to price or regulate milk in interstate trade. However, several states continue to  
21 have some form of milk price regulation, including California, New York, Pennsylvania, Virginia, Maine,  
22 Montana, Nevada, and North Dakota.

23 Fluid (beverage) milk processors are automatically subject to the requirements of a FMMO.  
24 Manufacturers of other dairy products are not automatically regulated. Instead, in order to share in Class I  
25 (beverage) milk price premiums, manufacturers of other products are required to demonstrate their  
26 capacity to supply milk to the fluid milk market. The specific performance or pool qualification  
27 requirements vary across orders, ranging from quite easy to very difficult. By defining eligibility to  
28 participate in the Order, these performance requirements may make it more costly for ineligible



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1 companies to purchase milk in the area affected by the Order. The USDA should be vigilant to assure that  
2 criteria for participation are justified and not exploited by some groups of farmers to avoid sharing market  
3 premiums with others.

4 Marketing orders are complex regulatory instruments. Many comprehensive descriptions are  
5 available to interested readers. Rather than focusing on the mechanics of the orders, the Committee  
6 wishes to highlight several aspects of market order operation that are related to its charge.

7 The AMAA of 1937 authorizes but does not mandate Federal Orders. Orders are initiated and  
8 amended through producer requests followed by formal hearings, briefings, recommended decisions,  
9 public comments, a farmer vote, and, ultimately, final decisions by USDA. Changes in an order are  
10 approved by an affirmative vote of two-thirds of the dairy farmers whose prices would be subject to the  
11 order. Farmers may only vote for or against the entire order, they cannot vote on specific provisions of the  
12 order. If a vote fails, the order ceases to exist. The logic behind the all or nothing vote hinges on two  
13 aspects of the law. First, the AMAA requires the Secretary to craft orders that are “in the public interest,”  
14 meaning the Secretary has to balance the objectives and concerns of farmers with those of the rest of the  
15 supply chain down to consumers. Second, only a farmer whose price is or would be affected by an Order  
16 are allowed to vote on its provisions. If they could choose only those favorable to them, the Secretary  
17 could not ensure that the public interest was balanced. Today, Federal Milk Marketing Orders cover about  
18 two-thirds of the U.S. milk supply. Most of the rest of the nation's milk supply is regulated under a state  
19 plan, which is generally similar in operation to a federal order.<sup>9</sup>

20 The Committee agrees that Federal Orders play a valuable role in oversight of compliance issues  
21 such as accuracy of weights, milk component testing, contract enforcement, auditing, and in data  
22 gathering and publication of statistics vital to market transparency.

23 The current structure of the FMMO system uses "product formula" or "end product" pricing based  
24 on National Agricultural Statistics Service (NASS) dairy commodity survey prices to determine minimum

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<sup>9</sup> California represents about 22% of US marketings. The amount of state regulated milk in the next two largest states, Pennsylvania and New York, represents less the 2% of US marketings.



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1 classified prices for milk. Under end-product pricing formulas, Chicago Mercantile Exchange (CME) spot  
2 prices for cheese and butter have a large influence on milk prices, even though they are not used directly  
3 in the formulas. Processors typically use CME prices for basic price discovery and as a reference to  
4 reduce their margin risk. Many cheese makers establish selling prices tied directly to the CME spot price  
5 in a given week. Thus, the prices paid to marketers of milk by plants and reported to NASS tend to be  
6 highly correlated with CME prices. The spot (CME) commodity markets trade very little product relative  
7 to the total volumes manufactured and sometimes exhibit large and unexpected swings in price. An  
8 aggravated price movement in a specific dairy commodity on the CME will likely be transmitted to  
9 farmers as increased farm milk price volatility. There is a concern in the dairy community that the CME  
10 markets are subject to manipulation by a small group of traders, although CME and the Commodity  
11 Futures Trading Commission, which have federal oversight responsibility, do not find evidence of  
12 frequent or routine illegal manipulation of those market mechanisms. The structure of spot cash markets  
13 themselves lend to volatility as they serve only as a market of marginal production and may not be  
14 representative of the value of all product.

15 Some other fundamental aspects of classified pricing and pooling may hamper dairy farmers'  
16 ability to innovate and create unintended incentives for farmers and processors. Milk prices paid by  
17 processors of commodities referenced in classified prices tie relatively closely to their finished product  
18 prices. Manufacturers of other dairy products face additional risk as their prices and costs deviate from  
19 those of the referenced commodities. The reduced margin uncertainty for manufacturers of the basic  
20 commodities makes those commodities relatively low-risk investments. This distortion discourages dairy  
21 product innovation, reduces market efficiency, and therefore lowers money available for farmers.

22 Similarly, improvements in dairy processing technology and changes in consumer preferences may  
23 render some of the original justifications for classified pricing and/or pooling obsolete. In the mid-20<sup>th</sup>  
24 Century, the percentage of Federal Order milk used to make fluid milk products was in the range of 60-65  
25 percent. In the 21<sup>st</sup> Century, Class I utilization has been in the neighborhood of 40 percent. Developments  
26 in milk transportation and storage ability, long-term declines in per capita beverage milk consumption and  
27 increases in cheese consumption, establishment of extremely large farmer-owned cooperatives,  
28 development of protein filtration technology, the increasing use of dairy products for ingredient usage in  
29 other foods, the emerging product preferences of both domestic and global dairy consumers and a host of



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1 other factors necessitate a strategic look at the future role of Federal Orders, especially in its role in price  
2 setting and pooling.

3 While the Federal Orders have many functions in the dairy industry, the underlying structure, as  
4 well as the rulemaking required, means that the Federal Order system is not a viable vehicle for USDA to  
5 assist dairy farmers during periods of stress. At best, FMMOs provide long term, consistent regulation of  
6 price, not short-term price stabilization. However, the Committee recommends further work by USDA,  
7 this Committee, or some other commission focused on analyzing the operations of the FMMO program,  
8 including end-product pricing's impact on milk price volatility and impact of classified end-product  
9 pricing and pooling on processing investment, dairy product innovation and competition.

10 **Dairy Export Incentive Program**

11 *Recommendation Note:*

12 *The committee has no specific recommendations concerning the current operation of the*  
13 *DEIP. However, given its limited value in the current global dairy trade climate, we suggest*  
14 *using DEIP funds more effectively for other programs in Recommendation 12. In the chapter*  
15 *on alternative actions, we do make broader recommendations related to dairy export*  
16 *programs and activities.*

17 The Dairy Export Incentive Program (DEIP) helps exporters of U.S. dairy products make sales to  
18 foreign buyers when U.S. prices exceed prevailing world prices for targeted dairy products and  
19 destinations. As part of its World Trade Organization (WTO) commitments resulting from the Uruguay  
20 Round Agreement on Agriculture, annual export subsidy ceilings are set for each commodity. These  
21 define maximum quantities and maximum budgetary expenditures, which are charged against the United  
22 States' constrained subsidies under the WTO agreement. Private companies, not the U.S. government,  
23 make all sales under the DEIP.

24 USDA issues two types of bonus invitations: those inviting exporters to compete for a bonus and  
25 those inviting exporters to apply for an announced bonus. When USDA issues an invitation for offers,  
26 agricultural exporters negotiate a sales contract with prospective buyers in eligible countries. The sale  
27 may be contingent on USDA's approval of a bonus. Each prospective exporter submits requests to USDA



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1 suggesting a bonus that would allow sales to take place at the agreed price. USDA chooses which bonuses  
2 to award.

3 Under an announced bonus, requests meeting all program requirements are accepted in the order  
4 submitted. USDA has the right to reject any or all bids.

5 Once USDA accepts a bonus request, the exporter and USDA's Commodity Credit Corporation  
6 (CCC) enter into an agreement. The bonus is paid to the U.S. exporter in cash. The CCC determines the  
7 bonus payment by multiplying the bonus specified in the agreement by the net quantity of the commodity  
8 exported. Once an exporter furnishes USDA with evidence that the specified commodity has been  
9 exported to the target destination under the terms of the agreement, the exporter receives the bonus.

10 To be consistent with WTO agreements, USDA has limited the use DEIP to instances when 1) U.S.  
11 prices are above prices in international markets and 2) the claim that we are countervailing other  
12 countries' subsidies is plausible. In recent years, U.S. and "world" dairy commodity prices have been  
13 closely aligned or the U.S. price has been below prices in competing countries; hence, the economic and  
14 legal justification for an export subsidy has been weak. Moreover, the European Union (EU) has reduced  
15 its dairy export subsidies as part of its agricultural policy, diminishing arguments that the U.S. is  
16 offsetting other countries' subsidies. The EU did resume export subsidies following price-supporting  
17 actions it took during 2009, but the EU maintains its longer-term commitment to dismantling dairy  
18 industry support programs.

19 In addition to DEIP, other Foreign Agricultural Service (FAS) programs are intended to enable or  
20 assist U.S. agricultural and food exports. These range from export promotion activities (such as trade  
21 shows, tours and visits) to programs that facilitate commercial transactions. Many agricultural businesses  
22 use export credit guarantees for commercial financing of U.S. agricultural exports.

23 Use of DEIP or other export assistance as a countercyclical measure to reduce dairy price volatility  
24 is limited by the requirements that U.S. prices be above world prices and/or the existence of evidence that  
25 other countries are providing export subsidies. However, it is sensible to exhaust all possible DEIP  
26 options before taking more extreme measures, such as raising support prices. We believe this is well  
27 understood within USDA.



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1 **Risk Management Programs**

2 *Recommendation 3:*

3 ***SIMPLIFY AND IMPROVE RISK MANAGEMENT PRODUCTS FOR DAIRY FARMERS.***

4 *Continue to simplify and improve Livestock Gross Margin-Dairy and overhaul Adjusted*  
5 *Gross Revenue-Lite in order to make them more accessible and easier for dairy farmers to*  
6 *use and adapt Livestock Risk Protection for use by dairy farmers. Expand risk management*  
7 *education.*

8 Dairy farmers may use public or private programs to manage risk. Farmers, without government  
9 assistance, can hedge milk or input prices using futures and options contracts on traded exchanges. In  
10 addition, depending on location, some farmers can forward contract milk with dairy cooperatives and  
11 other buyers. This choice is not available to farmers in California because forward contracting  
12 mechanisms do not exist within its state-regulated milk pricing system. Farmers also can forward contract  
13 some inputs, mainly feed, with suppliers.

14 There are some concerns that limit the use of risk management tools. Futures contracts may be  
15 “lumpy,” offered in unit sizes that are not easy for small producers to use on their own. Also, some  
16 hedging tools require “margin,” a posting of earnest money to cover the financial exposure of hedged  
17 positions. These margin requirements are designed to make sure that those with positions in the futures  
18 market can perform (settle up) under their contract terms. Margin requirements can tie up a significant  
19 amount of cash in a dairy operation.

20 USDA’s RMA offers two risk management tools. One is designed specifically for dairy farmers  
21 and is called Livestock Gross Margin - Dairy (LGM-Dairy). Another is a program available for any type  
22 of farm called Adjusted Gross Revenue Lite (AGR-Lite).

23 **Livestock Gross Margin (LGM) Dairy**

24 LGM-Dairy, introduced in 2007, is a bundled hedging tool that provides protection to dairy  
25 producers for the difference between feed costs and milk prices. Rather than having to hedge milk prices  
26 and feed prices separately, LGM-Dairy establishes a floor on gross margins (milk price minus feed costs)  
27 and pays an indemnity if the margin falls below the established floor. The farmer chooses how much of



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1 his or her milk to cover and the month of the coverage. Premiums are based on expected milk revenue and  
2 expected feed costs that are calculated using futures market prices on Class III milk, corn and soybean  
3 meal at the time the insurance is purchased. While any given farmer's milk revenue or feed costs will not  
4 equal the futures prices on the Chicago Mercantile Exchange (CME), his or her margin changes are  
5 expected to correlate closely enough to CME price movements to make the tool useful for reducing risk.

6 Unlike futures contracts, LGM-Dairy does not require a minimum amount of milk. Producers may  
7 sign up for this program monthly and may choose to cover up to ten months of production at a time.  
8 Farmers may not purchase insurance for margins on more than 24 million pounds of milk over that  
9 period.

10 RMA announced changes on October 26, 2010, designed to make LGM-Dairy user-friendlier.<sup>10</sup>  
11 For policies sold after December 17, 2010, premiums are due at the end of the coverage period rather than  
12 at the beginning. This allows the premium to be deducted from the indemnity. Higher deductible levels  
13 are also now offered. The maximum deductible level increased from \$1.50/cwt. to \$2.00. With this  
14 change, producers are better able to cover a minimum gross margin, which is comparative to catastrophic  
15 coverage. Allowable feed ranges have also been changed to better customize feed rations for an individual  
16 producer. Importantly, a subsidy has also been added for producers purchasing multiple months of LGM-  
17 Dairy insurance. The level of the subsidy is based upon deductible level selected, ranging from 18% for a  
18 \$0 deductible to 50% for a \$2 deductible<sup>11</sup>. These changes should encourage additional participation in  
19 the program, but it is too early to assess the impact.

20 Adjusted Gross Revenue Lite (AGR Lite)

21 In 1998, RMA developed a new insurance product intended for all farmers and based on adjusted  
22 gross income (AGI) as reported on Schedule F (Profit or Loss from Farming, IRS Form 1040) of the farm  
23 business' tax form. The program combines protection from production losses related to natural causes

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<sup>10</sup>USDA - RMA. "Improvements to the Livestock Gross Margin for Dairy Cattle Insurance Plan." October 26, 2010. RMA Program Announcement.

<sup>11</sup> RMA Fact Sheet "[Livestock Gross Margin Insurance - - Dairy Cattle](#)" November 2010



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1 with output price declines or input price increases related to market fluctuations. That product became  
2 quite complex and was difficult to use, so AGR-Lite was developed in 2002 to provide a simpler tool that  
3 would have the same goal.

4 Any farmer can use AGR-Lite and the revenue protection applies to the whole farm, not one  
5 product. Premiums are lower for farmers who sell more products because their expected total margin risk  
6 is reduced by that diversity.

7 Participation rules are not conducive to dairy production. No more than 35 percent of farm income  
8 can come from animals or animal products. Milk marketings are limited to 1.6 million pounds annually.  
9 The program only calculates costs of feed that is purchased, not feed that is grown. Total farm liability  
10 cannot exceed \$1 million and gross income must be below \$2,051,282.

11 Farmers select the coverage percentage of their total AGI and the percentage of the difference that  
12 they can receive if their actual AGI is less than the selected income coverage level. The maximum income  
13 coverage is based on each producer's average AGI over the previous five years.

14 Use and Participation in LGM-Dairy and AGR-Lite

15 Although they are similar, the LGM-Dairy and AGR-Lite approaches to income protection differ  
16 beyond the fact that one is tailored to dairy and the other is designed for small, diversified farming  
17 operations. LGM-Dairy works on the basis of a price spread, the difference between the price of milk and  
18 the cost of feed expressed relative to an amount of milk produced. The resulting margin is expressed in  
19 \$/cwt. AGR-Lite is based on the concept of income less production expenses, where both vary with the  
20 amount of milk produced (and other agricultural sales) and the amount of feed (and other production  
21 inputs) purchased. The result is net farm income in total dollars.

22 Few dairy farmers have participated in either program. Costs, size limits, market conditions,  
23 program design, and targets explain the lack of participation.

24 This Committee recommends an examination and overhaul of these programs to make them easier  
25 for dairy farmers to use. Current feedback from the farm community is that these programs are much too  
26 complicated and involve too much paperwork and that the cost of the program is not justified by its likely  
27 return.



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1           USDA has recently implemented several changes to LGM-Dairy. We believe these are important  
2 and useful. We encourage USDA to monitor the impact of these changes on usage by dairy farmers and  
3 continue to adjust the program accordingly.

4           RMA has sponsored a number of educational programs for dairy farmers. Cooperative Extension  
5 in many States, State agencies, cooperatives, and private industry have also repeatedly developed  
6 educational programs related to hedging, specific tools like LGM-Dairy or price risk management more  
7 broadly. Despite these considerable efforts, dairy farmers have yet to embrace these tools. Some of the  
8 reason for this is due to limitations in the tools and some is due to general lack of familiarity with risk  
9 management. We believe that there remains a need for broad and general education on price and income  
10 risk management strategies and tactics for dairy farm businesses. Volatility in the dairy industry is still a  
11 relatively new experience (less than 20 years) for many farmers, and the range of strategies and tools  
12 available is even more recent, with some tools still unknown or being developed. It is understandable that  
13 farmers are unsure of whether or how to manage their own risk. USDA risk management programs could  
14 provide a valuable tool to dairy farmers simply by providing or facilitating that education, regardless of  
15 the actual risk management tools used.

16 **CCC Charter Act, Section 5**

17           The Commodity Credit Corporation (CCC) was created in 1933 to handle commercial transactions  
18 that involve agricultural commodities. It is the business vehicle through which various programs  
19 stabilize, support, and protect farm income and prices. CCC also facilitates the movement of surplus or  
20 other agricultural commodities to various government and non-governmental outlets.

21           The Commodity Credit Corporation Charter Act of 1948 establishes the general purpose of the  
22 CCC and its operating rules and authorities. Section 5 of the Act, excerpted below, grants authorities to  
23 acquire and disburse agricultural commodities.

24           *SEC. 5. [15 U.S.C. 714]*

25           *SPECIFIC POWERS. —In the fulfillment of its purposes and in carrying out its annual*  
26 *budget programs submitted to and approved by the Congress pursuant to Chapter 91 of*  
27 *Title 31, the Corporation is authorized to use its general powers only to —*

28           *(a) Support the prices of agricultural commodities (other than tobacco) through loans,*  
29 *purchases, payments, and other operations.*



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1           **(b) Make available materials and facilities required in connection with the production**  
2           **and marketing of agricultural commodities (other than tobacco).**

3           **(c) Procure agricultural commodities (other than tobacco) for sale to other Government**  
4           **agencies, foreign governments, and domestic, foreign, or international relief or**  
5           **rehabilitation agencies, and to meet domestic requirements.**

6           **(d) Remove and dispose of or aid in the removal or disposition of surplus agricultural**  
7           **commodities (other than tobacco).**

8           **(e) Increase the domestic consumption of agricultural commodities (other than tobacco)**  
9           **by expanding or aiding in the expansion of domestic markets or by developing or aiding**  
10           **in the development of new and additional markets, marketing facilities, and uses for such**  
11           **commodities.**

12           **(f) Export or cause to be exported, or aid in the development of foreign markets for,**  
13           **agricultural commodities (other than tobacco) (including fish and fish products, without**  
14           **regard to whether such fish are harvested in aquacultural operations).**

15           **(g) Carry out conservation or environmental programs authorized by law.**

16           **Carry out such other operations as the Congress may specifically authorize or provide**  
17           **for.**

18           **In the Corporation's purchasing and selling operations with respect to agricultural**  
19           **commodities (other than tobacco) (except sales to other Government agencies), and in**  
20           **the warehousing, transporting, processing, or handling of agricultural commodities**  
21           **(other than tobacco), the Corporation shall, to the maximum extent practicable consistent**  
22           **with the fulfillment of the Corporations purposes and the effective and efficient conduct**  
23           **of its business, utilize the usual and customary channels, facilities, and arrangements of**  
24           **trade and commerce (including, at the option of the Corporation, the use of private sector**  
25           **entities).**

26  
27           This Section of the legislation defines a number of things that the CCC may do; however, this  
28           permission is different from what is actually possible or required. These general authorities enable the  
29           Secretary of Agriculture to implement the procurement and sale of dairy products under the DPPSP and  
30           various other programs related to domestic and international food assistance.<sup>12</sup>

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<sup>12</sup> The CCC is managed by a Board of Directors, subject to the general supervision and direction of the Secretary of Agriculture, who is an ex-officio director and chairperson of the Board.



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1           If no specific program requires the Secretary to procure and/or distribute dairy or other  
2 commodities, he could use the provisions of this Charter to do so if and only if there is a source of funds  
3 authorized by the Office of Management and Budget. Many of the programs that use the CCC as a  
4 procurement conduit are described in the next two sections.

5 **Domestic Food Assistance Programs**

6 *Recommendation Note:*

7 *At the conclusion of the chapter on existing laws and programs, we offer a recommendation*  
8 *that relates to the Secretary's use of domestic food assistance programs.*

9           The majority of the USDA budget, about two-thirds, is devoted to food and nutrition programs.  
10 These programs are generally administered through the Food and Nutrition Service and include the  
11 following:<sup>13</sup>

- 12           1. Supplemental Nutrition Assistance Program (SNAP, formerly Food Stamps)
- 13           2. Special Supplemental Nutrition Programs for Women, Infants, and Children (WIC)
- 14           3. School Meals
  - 15               a. National School Lunch
  - 16               b. Fresh Fruit and Vegetable Program
  - 17               c. School Breakfast Program
  - 18               d. Special Milk Program
  - 19               e. Team Nutrition
- 20           4. Summer Food Service Program
- 21           5. Child and Adult Care Food Program
- 22           6. Food Assistance for Disaster Relief

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<sup>13</sup> For more information: (<http://www.fns.usda.gov/fns/>)



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1       7. Food Distribution

- 2           a. Schools/Child Nutrition Commodity Programs (CNP)
- 3           b. Food Distribution Program on Indian Reservations
- 4           c. Nutrition Services Incentive Programs (NSIP)
- 5           d. The Commodity Supplemental Food Program (CSFP)
- 6           e. The Emergency Food Assistance Program (TEFAP)

7           Only the Special Milk Program is exclusive to dairy products, but many of these programs have  
8 played a significant role in increasing the availability and use of dairy products among children and the  
9 needy. The Special Milk Program provides cash subsidies to schools for milk they serve to children not  
10 covered under the School Lunch and similar programs.

11           The overwhelming majority of public schools, and many private ones, participate in the National  
12 School Lunch Program, while a significant and growing number also offer the School Breakfast Program.  
13 Milk is the only product required to be offered with each school meal, and school milk accounts for  
14 approximately 6% of all fluid milk consumption in the United States.

15           USDA provides grants to States, which in turn deliver WIC program benefits to pregnant and  
16 lactating women, infants and young children. Historically, WIC has had a strong emphasis on providing  
17 milk and other nutritious dairy products to these people.

18           TEFAP was originally started during the early 1980s when surpluses under the DPSP became  
19 burdensome. The success of the Temporary Emergency Food Assistance Program led to the creation of  
20 The Emergency Food Assistance Program. Today, TEFAP is the primary vehicle for distributing  
21 commodity foods to States that, in turn, distribute food to Food Banks and similar local food distribution  
22 agencies.

23           Each of these programs can be a vehicle for the use and distribution of dairy foods. However,  
24 several factors limit their effectiveness as a short-term response to a dairy surplus. First, these programs  
25 are budgeted. Increased dairy purchases would displace purchases of other food products. USDA may  
26 shift funding among various commodities, but many non-dairy foods have legitimate claims on available  
27 funds.



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1 Second, these programs require planning, implementation, and execution. Programs that coordinate  
2 with state-run activities are subject to the timing, planning and discretion of the receiving state or school  
3 district. Programs in which USDA works directly with an agency typically involve a spending and  
4 utilization plan of that agency. Schools, in particular, plan their budgets and menus early in their fiscal  
5 cycles. Once in place, these plans are not often changed.

6 Third, the amount of dairy products that can be used and provided to these programs on a timely  
7 basis is limited. For example, storage space and refrigerator capacity to minimize spoilage are limited. In  
8 addition, because dairy processors must continue to service existing customers or risk losing their  
9 customer base, they cannot divert unlimited quantities to food assistance outlets on a sporadic basis.

10 Finally, increased use of dairy products in food assistance programs may substitute for commercial  
11 sales if recipients substitute the additional dairy products that they receive for dairy products that they  
12 would normally purchase through commercial channels. If this occurs, total utilization of dairy products  
13 does not increase and dairy producers don't benefit.

14 Congress can create funding and programs to respond to something like the dairy crisis of 2009,  
15 but once funding for food and nutrition programs are established the Secretary cannot easily alter the plan  
16 or find additional funding to support one specific agricultural or food sector.

**17 International Food Assistance Programs**

18 Several programs provide food to needy people in low-income countries on an ongoing basis or to  
19 provide emergency assistance in times of natural or other specific disaster. These include:

- 20 A. Food for Peace
- 21 B. McGovern-Dole
- 22 C. Food for Progress
- 23 D. Section 416(b)

24 Food for Peace (FPA, often called P.L. 480) was authorized under the Agricultural Trade  
25 Development and Assistance Act of 1954. At first considered a temporary response to mitigate  
26 agricultural surpluses, this program has evolved to become a pillar of U.S. food assistance and is  
27 considered a core program by advocates for low-income countries. The FPA has three titles, each with a



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1 specific objective and providing assistance to countries at a particular level of economic development.  
2 Title I is administered by USDA. Titles II and III are administered by the U.S. Agency for International  
3 Development (USAID). USAID is an independent federal agency that operates under the supervision of  
4 the Secretary of State. FPA, Title I—Trade and Development Assistance, provides for government-to-  
5 government sales of U.S. agricultural commodities to developing countries.<sup>14</sup> Agreements under the Title  
6 I credit program may provide for repayment terms of up to 30 years with a grace period of up to five  
7 years. Title I also allows for grant programs, which have outnumbered loans in recent years. Depending  
8 on the agreement, commodities provided under the program may be sold in the recipient country and the  
9 proceeds used to support agricultural, economic or infrastructure development projects there.

10 Since fiscal year 2006, new funding has not been requested because demand for food assistance  
11 using credit financing has fallen or grant programs have been a more appropriate tool.

12 FPA, Title II—Emergency and Private Assistance, provides for the donation of U.S. agricultural  
13 commodities to meet emergency and non-emergency food needs in other countries.

14 FPA, Title III—Food for Development, provides for government-to-government grants to support  
15 long-term growth in the least developed countries. Donated commodities are sold in the recipient country,  
16 and the revenue generated is used to support economic development programs. In recent years, this title  
17 has been inactive.

18 Although the Secretary of Agriculture is responsible for Title I uses of agricultural commodities, he  
19 needs funding in order to act. In recent years, advocates for international food assistance have urged  
20 Congress to provide direct cash subsidies that would allow foreign governments or approved agencies in  
21 foreign countries to buy food wherever they can find it most cheaply. While this approach enables the  
22 most total food assistance per dollar spent, it may not provide much support for U.S. agriculture.

23 The McGovern-Dole International Food for Education and Child Nutrition Program helps promote  
24 education, child development, and food security for some of the world's poorest children. It provides for  
25 donations of U.S. agricultural products, as well as financial and technical assistance, for school feeding

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<sup>14</sup> For more information: (<http://www.fas.usda.gov/excredits/FoodAid/pl480/pl480.asp> )



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1 and maternal and child nutrition projects in low-income countries. The Foreign Agricultural Service of  
2 USDA administers this program, authorized by the Farm Security and Rural Investment Act of 2002.

3 Commodities are donated through agreements with private organizations, cooperatives,  
4 intergovernmental organizations and foreign governments. Commodities may be donated for direct  
5 feeding or, in limited situations, for local sale to generate proceeds to support school feeding and nutrition  
6 projects.

7 Under the Food for Progress Act of 1985, agricultural commodities are provided to developing  
8 countries and emerging democracies that are committed to introducing and expanding free enterprise in  
9 the agricultural sector. Commodities are currently donated to foreign governments, private voluntary  
10 organizations, nonprofit organizations, cooperatives, or intergovernmental organizations.

11 The implementing organizations request commodities and USDA buys those commodities from the  
12 U.S. market. USDA donates the commodities to the implementing organizations and pays for the freight  
13 to move the commodity to the recipient country.

14 Section 416(b) of the Agricultural Act of 1949, as amended, provides for overseas donations of  
15 surplus commodities acquired by the CCC. Donations are not permitted to reduce the amounts of  
16 commodities that are traditionally donated to U.S. domestic feeding programs or agencies or disrupt  
17 normal commercial sales.

18 Availability of commodities under Section 416(b) depends on CCC inventories and acquisitions.  
19 Programming varies from year to year. The commodities are made available for donation through  
20 agreements with foreign governments, private voluntary organizations (PVOs), cooperatives, and  
21 intergovernmental organizations. Depending on the agreement, the commodities donated under Section  
22 416(b) may be sold in the recipient country and the proceeds used to support agricultural, economic, or  
23 infrastructure development programs.

24 The Section 416(b) program is currently not active, as there are no CCC-owned commodities  
25 available at this time.

26 The assortment of foreign food export programs provides opportunities for the U.S. government to  
27 increase use of dairy products. However, that authority is tempered by budgetary constraints and by



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1 concerns that the dispositions not be disruptive to recipient country economies or of world trade in dairy  
2 products.

3 **Section 32, Public Law 74-320**

4 In 1935, as part of its response to the hardship for agriculture during the Great Depression,  
5 Congress created a permanent authority to give USDA money from U.S. customs receipts (tariffs) to  
6 support farmers whose products were not otherwise covered or protected by more specific commodity  
7 policy. The Secretary has discretion in how to use Section 32 funds. The following is from a  
8 Congressional Research Service report written in 2006:

9 *Section 32 of the act of August 24, 1935, authorizes a permanent appropriation equal to*  
10 *30% of annual U.S. customs receipts (P.L. 74-320 as amended; 7 U.S.C. 612c). This*  
11 *money was first available to assist Depression-era producers of non-price-supported*  
12 *commodities. Section 32 funds, along with up to \$500 million in any unobligated prior*  
13 *year funds, are to be used for (1) encouraging the export of farm products through*  
14 *producer payments or other means; (2) encouraging the domestic consumption of farm*  
15 *products by diverting surpluses from normal channels or increasing their use by low*  
16 *income groups; and (3) reestablishing farmers' purchasing power. The Secretary of*  
17 *Agriculture has considerable discretion in deciding how to achieve these broad*  
18 *objectives.*

19 *.....Today [viz. 2006], most of this appropriation (now approximately \$6.5 billion yearly)*  
20 *is transferred to the U.S. Department of Agriculture (USDA) account that funds child*  
21 *nutrition programs. Other Section 32 funds are used by USDA to purchase meats,*  
22 *poultry, fruits, vegetables, and fish, which are diverted mainly to school lunch and other*  
23 *domestic food programs. Several times in recent years, the Secretary of Agriculture also*  
24 *has drawn substantial amounts from Section 32 to pay for special farm disaster relief.*  
25 *This has added to the debate over how much flexibility the Secretary should have over*  
26 *use of the reserve, and whether the disaster aid has or could come at the expense of the*  
27 *other Section 32 activities.*

28 *Excerpted from:*  
29 *Farm and Food Support Under USDA's Section 32 Program,*  
30 *by Geoffrey S. Becker; Specialist in Agricultural Policy; Resources, Science, and Industry Division;*  
31 *Congressional Resource Service; RS20235; 28 November 2006.*

32 Because the DPSP was defined to broadly assist the dairy sector, Section 32 funds could not be  
33 used to purchase or distribute dairy products. With the evolution of the DPSP into the DPPSP in 2008, an  
34 argument could be made that government support has now been legally limited to commodity packaged  
35 butter, nonfat dry milk and cheddar cheese. Under this interpretation, Section 32 funds could support  
36 other dairy products, such as mozzarella cheese, fluid milk, or whey protein concentrate.



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1 Section 32 does not create a program; it creates a source of funds. Thus, this money could be used  
2 in conjunction with existing programs that are designed for domestic food assistance, international  
3 exports or food aid. The legislative language “reestablishing farmer’s purchasing power” suggests an even  
4 broader authority to, for example, compensate producers for losses caused by low prices. However, it is  
5 unclear whether Section 32 funds could legally be used to benefit the dairy sector since, even with the  
6 change in the DPSP, other programs, such as MILC, are specifically designed for dairy. Moreover, USDA  
7 in fact uses other authorities to purchase dairy products for the same uses as Sec. 32 commodities.

8 **Farm Loan Programs**

9 *Recommendation 4:*

10 *USE OF USDA FARM LOAN PROGRAMS. The Secretary should work with the Farm*  
11 *Service Agency in Washington and all State Farm Service Agency Executive Directors and*  
12 *State Committee members, particularly those in States with significant numbers of dairy*  
13 *operations, to promote efficient and effective use of the Farm Loan Program for dairy*  
14 *farmers. We especially encourage the use of the Guaranteed Loan Program with existing*  
15 *commercial lenders.*

16 *Apparently, some States leverage the Farm Loan Programs more effectively than others. We*  
17 *recommend that the federal FSA examine any disparities and develop strategies to share*  
18 *best practices across regions.*

19 USDA’s farm loan program operates under the authority of the Consolidated Farm and Rural  
20 Development Act (7 U.S.C. 1936) and is administered by USDA’s Farm Service Agency (FSA). FSA  
21 makes direct and guaranteed farm ownership and operating loans to qualified and eligible farmers and  
22 ranchers who cannot obtain commercial credit from a bank, Farm Credit System institution, or other  
23 lender. It also issues emergency loans in situations where farmers have been adversely impacted by severe  
24 weather conditions. FSA loans can be used to purchase land, livestock, equipment, feed, seed, and  
25 supplies. Loans can also be used to construct buildings or make farm improvements. FSA employs farm  
26 loan officers who originate and service Direct Farm Ownership and Operating Loans. FSA works with  
27 banks and Farm Credit System institutions, providing guarantees on loans originated and serviced by  
28 those commercial lenders.



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1 In fiscal year (FY) 2010, \$6.115 billion was appropriated for the FLP. As of September 3, 2010,  
2 the FLP had 33,541 loans in its national portfolio for a total of \$4.913 billion. The maximum principal  
3 amount per borrower in direct loans is \$300,000. The maximum total principal amount for direct loans  
4 plus loan guarantees is \$1,119,000. This amount is adjusted annually based on inflation.

5 The top five states in FY 2009/10 in terms of number of new loan applications are listed below.  
6 New direct and guarantee loan volumes for the first eleven months of the fiscal year are in parenthesis.

- |    |              |                 |
|----|--------------|-----------------|
| 7  | 1. Wisconsin | (\$419 million) |
| 8  | 2. Minnesota | (\$309 million) |
| 9  | 3. Iowa      | (\$286 million) |
| 10 | 4. Texas     | (\$220 million) |
| 11 | 5. Nebraska  | (\$235 million) |

12 Wisconsin FSA FLP Example

13 As Wisconsin is the largest customer of the FLP, with by far the majority of its loans procured by  
14 dairy producers, we provide here a closer look at Wisconsin's successful use of the program.

15 The Wisconsin FSA FLP portfolio crossed the \$1 billion threshold in early 2010. As of August 31,  
16 2010, it held 4,956 loans for a total of \$1.24 billion. Of these, 62 percent were direct loans and 38 percent  
17 were loan guarantees. Approximately 90 percent of FLP borrowers in Wisconsin are dairy producers.

18 The FSA FLP has, for many years, been an important source of credit for Wisconsin dairy  
19 producers. Wisconsin FSA FLP has historically been one of the top three among all states in both the  
20 number and the dollar volume of loans. FSA FLP has loan program managers assigned to cover every  
21 county in the state. They do an excellent job of outreach to farmers. They partner with many other entities  
22 that can help them more effectively serve farmers including the Wisconsin Department of Agriculture,  
23 Trade and Consumer Protection, Wisconsin Technical College System, University of Wisconsin School  
24 for Beginning Dairy and Livestock Farmers, and others. FSA has developed strong working relationships  
25 with commercial agricultural lenders to broaden the scope of its loan guarantee and interest assistance  
26 programs. In short, there are few agricultural borrowers or lenders in Wisconsin that are not aware of the  
27 FSA FLP.



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1 As commercial agricultural credit became more difficult to obtain in 2009, the importance of the  
2 Wisconsin FSA FLP became even more pronounced. Lenders pointed many borrowers towards the FLP,  
3 and FLP loan volume in the state increased dramatically.

4 There are some key reasons that the FSA FLP works well in Wisconsin:

5 Wisconsin FLP has a high level of participation in the Preferred Lender Program (PLP), which  
6 allows experienced agricultural lenders to quickly obtain USDA Loan Guarantees with a minimal amount  
7 of paperwork. Subsequent review by State FSA FLP staff allows the private lender to conduct their  
8 business with minimal disruption of their normal operating procedures. FSA FLP monitors the aggregate  
9 performance of each lender rather than each individual loan application. Lenders with strong records of  
10 success maintain PLP status; those with higher losses are more closely scrutinized. (Many states have  
11 struggled to implement these loan guarantee processes.)

12 Wisconsin FSA FLP views itself as a partner with private agricultural lenders, and the lenders look  
13 at FSA FLP in that way as well. In many cases, the private lender has part of the financing package and  
14 FSA has part of the financing package. It is not an “either, or” situation.

15 Wisconsin FSA FLP contracts out to the private sector for many services such as real estate and  
16 chattel appraisals that assist their loan officers, which allows them to focus on the duties that only they  
17 can do. In the past, FSA FLP loan officers would have done these tasks. By contracting out for these  
18 services, FSA FLP has freed up its loan officers to serve new loan applicants and service their existing  
19 loan portfolios. This has allowed Wisconsin FSA FLP to be a national leader in loan-making, while  
20 keeping delinquencies and losses among the lowest in the nation. Wisconsin FSA FLP has centralized its  
21 loan liquidation process in the State office, which also frees up field loan staff to make and service more  
22 loans.

23 Despite maintaining a large loan portfolio with borrowers who were unable to obtain commercial  
24 credit, Wisconsin FSA FLP has experienced relatively low delinquency rates. In FY 2009/10,  
25 approximately 1.93 percent of the direct loan portfolio and 0.88 percent of the guaranteed loan portfolio  
26 was delinquent. By commercial lending standards, these delinquency rates are relatively low, particularly  
27 considering the poor economic conditions in the dairy industry during the period.



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1 On a national level, Secretary Vilsack issued a letter at the height of the 2009 dairy crisis to all of  
2 FSA's dairy producer-borrowers informing them of the loan servicing options available to alleviate  
3 financial stress. These options included lifting milk check assignments to allow money to flow through  
4 for family living and operating expenses, deferring principal and interest payments, lowering payments  
5 through rescheduling or re-amortizing of debt, and other options. Many FLP borrowers contacted their  
6 loan managers to take advantage of the relief that was available.

7 All State FLPs could extend the scope of their Guaranteed Loan Programs by building effective  
8 Preferred Lender Programs (PLP). PLPs make it much easier for commercial lenders to use FLP  
9 Guarantees. PLPs make more efficient use of State FLP staff time by minimizing the loan processing  
10 involved in each guarantee. The definition of a "family farm" for purposes of extending credit under the  
11 Farm Loan Program (FLP) should be interpreted consistently in all states. Approximately 95 percent of  
12 the dairy operations in the United States are milking fewer than 500 cows. Most of those would meet the  
13 FLP definition of a family farm and would find the FLP to be a very beneficial source of credit during  
14 times when access to commercial credit is limited.

15 Dairy industry stakeholders across the country should take the initiative to learn more about the  
16 federal loan programs available to producers and other agriculture-related businesses in their states. In  
17 addition to the FSA FLP, other federal agencies such as USDA Rural Development and the Small  
18 Business Administration have loan programs that may be helpful to dairy producers.

19 When it works well, the FLP can be critically important to our nation's dairy producers, especially  
20 when economic conditions make commercial credit difficult to obtain. The remarkably low default rate  
21 experienced in the FLP shows that funds invested in the program will be used wisely and will recirculate  
22 to provide help to even more farmers. We appreciate the Secretary's and Congress' work in providing  
23 additional funds for the FLP during the 2009 dairy crisis. We encourage the Secretary to also provide  
24 adequate staffing for the FLP. State FSA Executive Directors should be given the discretionary authority  
25 to temporarily re-assign county-level staff from commodity programs to the FLP during times of high  
26 loan demand. FSA Executive Directors should also be given the ability to temporarily hire assistance,  
27 such as experienced, retired commercial agricultural lenders to provide support to FLP staff during  
28 periods of strong demand. To achieve maximum efficiency of FSA staff, USDA could encourage State



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1 FSA offices to consider contracting out to the private sector for items like real estate and chattel  
2 appraisals.

3 **Market News, Research, and Promotion Programs**

4 *Recommendation Notes:*

5 *In the section on alternative price protection programs, we offer additional*  
6 *recommendations that relate to the creation of new public information related to dairy*  
7 *markets and dairy sector performance.*

8 Numerous federal programs support dairy market development, day-to-day dairy business  
9 decisions, and the ability of dairy businesses to plan. They do so by providing information on milk and  
10 dairy product prices, market conditions, and market outlook. Such programs include the Agricultural  
11 Marketing Service (AMS) Dairy Market News; various data serials published by NASS, ERS and FAS;  
12 special analytical reports by ERS; and the USDA World Agriculture Supply Demand Estimates  
13 (WASDE). USDA also operates programs for market and business development, and AMS participates in  
14 the oversight of the National Dairy Promotion and Research Board.

15 These programs typically provide valuable information for buyers and sellers in dairy markets.  
16 While valuable for both long-term profitability of the dairy industry and beneficial to ensure the smooth  
17 functioning of markets and as a resource for sound business decisions, the programs are not constructed  
18 or intended for direct short-term assistance.

19 There has been considerable discussion in recent months and years about two dimensions of market  
20 reports – mandatory reporting and electronic submission of data.

21 Although individual plant farm pay price reporting is required under FMMOs, these data are  
22 collected for purposes of enforcing price regulation, not to provided general market reports of prices.  
23 Most surveys of prices by NASS, AMS, ERS or other agencies are conducted on a purely voluntary basis.  
24 Some surveys are done with very formal attention to statistical survey techniques and some are very  
25 informal. Mandatory price reporting seeks to compel dairy businesses to report their price transactions so  
26 that the reliability of the marketwide results is ensured. In a sense, this becomes a census rather than a  
27 statistical sample. The confidentiality of individual business records would be protected.



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1 Electronic reporting of data is a tactical issue, but it is encouraged to facilitate the collection,  
2 dissemination and use of market price data.

3 Congress passed two laws related to mandatory price reporting. One was imbedded in the 2008  
4 Farm Bill. Last Fall, the Mandatory Price Reporting Act of 2010 was passed, which extends and expands  
5 the price reporting requirements under the previous legislation. It includes mandatory weekly electronic  
6 reporting for dairy products. As a result, USDA's Dairy Product Mandatory Reporting Program: (1)  
7 requires persons engaged in manufacturing dairy products to report certain information including the  
8 price, quantity, and moisture content where applicable, of dairy products sold by the manufacturer; and  
9 (2) requires persons storing dairy products to report information on the quantity of dairy products stored.  
10 The National Agricultural Statistics Service (NASS) collects such information for the program. The  
11 Agricultural Marketing Service (AMS) has implemented a plan to verify the price information submitted  
12 by dairy product manufacturing plants to NASS. Any manufacturer that processes and markets less than  
13 1 million pounds of dairy products per year is exempt from the price reporting requirements.

14 **Recommendation for the Use of Existing Programs in Times of Severe Economic Distress**

15 *Recommendation 5:*

16 *EMERGENCY INTERVENTIONS. The Secretary should develop a system of triggers and*  
17 *actions to guide his choices for special and emergency interventions, using existing*  
18 *programs.*

19 Barring legislative changes, the programs which permit the Secretary some flexibility in their  
20 application as emergency measures in times of critically low farm margins are the DPPSP and one or  
21 more food assistance programs. If the Secretary can identify sources of funding, he could stimulate or  
22 supplement commercial demand and thereby lift prices via either of these approaches.

23 We strongly suggest using food assistance programs first and resorting to increasing DPPSP  
24 purchase price levels only under severe stress, as the Secretary did in 2009. Movements of the DPPSP  
25 purchase prices can disrupt commodity financial markets, as well as U.S. export markets, and thereby  
26 impact the financial positions of farmers and others who have chosen to mitigate risk through those



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1 markets. It would not be helpful to undermine the use of risk management tools because price support  
2 interventions were unpredictable.

3 When dairy farm margins, as measured by the new margin measurement (cf. recommendation 1),  
4 decrease to the first trigger level, the Committee recommends that the Secretary guide food assistance  
5 purchases toward additional dairy products. This would temporarily create new demand for dairy  
6 products, which would exert upward pressure on dairy product prices and, therefore, farm level milk  
7 prices. The Secretary should ensure that government purchased dairy foods donations do not significantly  
8 displace commercial sales. Therefore, dairy foods should be provided to people who would not otherwise  
9 purchase them or would purchase a lesser amount.

10 If dairy farm margin levels decrease to the second trigger level, the Secretary would have  
11 justification to increase the purchase prices under the DPPSP to levels that provide more revenue for dairy  
12 farmers.

13 Although the triggers provide a justification and a guide, the Secretary should maintain discretion  
14 as to whether to implement these measures. He should determine that market conditions are a result of  
15 extraordinary shocks rather than predictable cyclical price swings. Keep in mind that this  
16 recommendation is made in the context of existing programs, one of which is MILC. The feed cost  
17 adjusted MILC payment may or may not trigger in the same months as the margin trigger. This would be  
18 one of the elements for which the Secretary would need to account in determining the need for an  
19 extraordinary response.

20 USDA should also develop standards that assure that the measures do not significantly or  
21 unavoidably harm export markets or commercial channels. When the margin measurement methodology  
22 has been determined, appropriate margin trigger level(s) identified, and any corresponding DPPSP price  
23 level increases that might occur at those trigger levels set, USDA should publish those details. That way,  
24 potential future government interventions, such as increases in the DPPSP, can be considered and  
25 included in dairy farmers' personal milk marketing and business decisions. Uncertainty related to  
26 government intervention may tend to discourage farmers from protecting their own margin risk because  
27 of varying expectations about timing or impacts of government interventions.



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1 **The Secretary should apply both of these approaches judiciously and rarely. If these approaches**  
2 **are used too frequently, they lose their effectiveness. We encourage the Secretary to work with**  
3 **OMB in developing the rationale for emergency interventions before such actions become**  
4 **necessary, based on market conditions. We do not intend to indicate that this Committee supports**  
5 **continuation of the DPPSP. We merely intend to provide a framework around which the**  
6 **Secretary's existing authority should be applied. Concluding Comments About Existing Programs**

7 Numerous programs can be used to benefit dairy farmers and the dairy sector in times of stress.  
8 This includes programs to directly support prices or farm incomes and programs that more indirectly  
9 affect the demand for dairy products and thereby strengthen markets and prices.

10 In theory, all of these programs could be extremely helpful in times of economic stress, but in  
11 practice, most are not well suited to unanticipated stress and quick responses to emergency conditions. In  
12 many cases, the Secretary of Agriculture has no authority to change a program or operate it outside of a  
13 very narrow range of legislatively defined parameters. In some cases, the law grants the Secretary some  
14 discretion in defining a program's parameters, but when the Secretary's decisions have an impact on  
15 government expenditures, he or she must get approval from the President's Office of Management and  
16 Budget. Obtaining permission to use discretionary authority for agricultural programs in general and  
17 dairy in particular can prove difficult.

18 **New Programs, Legislation and Regulation**

19 Programs to Stabilize and Regulate Milk Prices

20 *Dairy Product Price Support Program and Dairy Export Incentive Program*

21 *Recommendation 6:*

22 *BEST USE OF FUNDS: Explore elimination of the Dairy Product Price Support Program*  
23 *and the Dairy Export Incentive Program and use budget savings to enhance the safety net*  
24 *for producers.*

25 The DPPSP and DEIP programs were discussed in detail in the previous section on current  
26 authorities. The consensus of the DIAC is that there are circumstances when the Secretary should  
27 seriously consider using the tools at his disposal, but that the industry would be better served with some



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1 new tools. While these programs have some merit and should be used until alternatives are in place, the  
2 committee believes that their effectiveness has become limited and that the budgetary resources tied up in  
3 them could be better used for other programs.

4 The member's perspectives on each of these programs is not unanimous but there is a widespread  
5 belief that both programs have problems.

6 In recommendation 14, we express our strong endorsement of programs to help develop U.S.  
7 export markets. To some extent, DEIP can play that role; however, the implementation of the program has  
8 generally fallen short of the goals its supporters desired. In the current global dairy economic climate, the  
9 ability to use DEIP within WTO parameters is severely limited, as discussed in the introductory section.  
10 There are also arguments from a marketing perspective against an ongoing policy of export subsidies as  
11 well. In sum, we believe DEIP is not the best use of scarce federal resources, even though we do support  
12 federal involvement in export market development.

13 Earlier in the report we described the evolution and current status of the DPPSP. Again, opinions  
14 on the merits of this program are diverse. They range from a belief that the program could play a helpful  
15 and positive role in protecting farm prices to a very strong belief that the program is ultimately more  
16 disruptive than helpful - that it creates perverse incentives in the investment of processing facilities and  
17 the amounts of alternative products produced, even when the program is inactive.

18 Alternative, safety net type programs will be more fully discussed in the section on price  
19 stabilization programs. Recommendation 11 concerns a particular approach and specifically refers to  
20 replacing DPPSP and DEIP. Our more general recommendation here is to suggest that if Congress can  
21 come up with a better safety net program for dairy farmers, we would support ending the DPPSP and  
22 DEIP to provide budget for an alternative program that better protected dairy profitability.

23 *Federal Milk Marketing Orders*

24 Federal Milk Marketing Orders, as they currently exist, were discussed in an earlier section of  
25 this report. We have recommended (#2) that "The Secretary of Agriculture should appoint a committee to  
26 review implications of Federal Milk Marketing Orders, including, but not limited to, end-product  
27 pricing's impact on milk price volatility and impact of classified pricing and pooling on processing  
28 investment, competition and dairy product innovation."



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1 Congress authorized the creation of a Congressional “commission” to review Federal Milk  
2 Marketing Orders in the 2008 Food, Conservation and Energy Act (Farm Bill). Although it was  
3 subsequently decided to not pursue this commission, our experience leads us to better appreciate the need  
4 for a focused effort, involving people who are deeply familiar with the intricacies of this complex  
5 regulation.

6 Testimony received by the DIAC and our own personal experiences suggest that there are  
7 advantages and disadvantages to classified pricing and pooling, which are the fundamental tools of  
8 FMMOs. Similarly, there are positives and negatives in the specific implementation of these tools that  
9 currently exist in FMMOs. For example, classified pricing may be a helpful way to establish prices for  
10 milk, but setting class prices by a formula tied to wholesale prices of basic dairy commodities might not  
11 be the best approach.

*Recommendation 7:*

***STRONGLY CONSIDER THE ELIMINATION OF END PRODUCT PRICING. Explore alternative measures to the current end product pricing system, such as competitive pricing and mandatory price reporting.***

16 This recommendation goes beyond recommendation 2, which calls for a broad review, by more  
17 firmly stating our skepticism of the merits of the current use of wholesale prices of four dairy  
18 commodities to establish the minimum prices paid for milk under FMMOs. Testimony spoke to the need  
19 for a new system of price discovery in FMMOs or even more generally. Determining the best alternative  
20 approach to end-product classified pricing is beyond the ability of our committee effort. However, for the  
21 reasons outlined in the introductory section on Federal Milk Marketing Orders, we believe eliminating  
22 end-product pricing has merit and deserves particular review and attention. The objective should be to  
23 simplify the dairy price regulation and use a system in which all participants would have a high degree of  
24 trust and confidence.



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*Recommendation 8:*

*COLLECT AND PUBLISH PRICE DATA. USDA should collect and publish data on alternative measures of a competitive pay price, considering but not limited to the proposals of the National Milk Producer Federation and Maine Dairy Industry Association.*

We have also previously discussed ongoing and new efforts at price and market news reporting. A new system of weekly, electronic reporting will be implemented in the coming months. We applaud this effort and encourage USDA and industry members to use it and evaluate its usefulness over the coming year.

Beyond the current plan to survey dairy product prices, we encourage USDA to collect and report data on actual milk prices paid by dairy processors. Such information would assist members of the dairy industry in better understanding the possible consequences of switching to a competitive pay price approach in establishing FMMO minimum class prices.

*Growth Management*

*Recommendation 9:*

*ADOPT A GROWTH MANAGEMENT PROGRAM. The federal government should adopt a growth management program that allows new producers to enter and allows producers to expand production.*

Proposals have been made in the last year to authorize a new federal program that would create new and targeted incentives to control production growth in periods of economic distress on dairy farms. The DIAC is not prepared to endorse a specific plan; however, we agree that a primary challenge in taming milk price volatility is to better coordinate milk marketings with milk usage over time. We do not agree on whether this should be a public or a private endeavor.

In evaluating specific proposals and considering the concept in general, we recognize advantages and disadvantages to a new government program of this type. While a simple majority of the committee supports a new federal program, as a group we recognize that there are different perspectives on the merits of such a plan. Indeed, the members of the committee reflect the diversity of perspective and opinion within the industry. Some people are opposed to the concept altogether. Even supporters of the concept within the Committee disagree on a specific plan or implementation. In the remainder of this



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1 section, we will briefly highlight aspects of these programs that are appealing to us but also discuss  
2 cautions about this approach.

3 *Merits of Growth Management Plans*

4 The most compelling justification for a federal program to help the dairy industry better align milk  
5 production growth with growth in demand is that experience has amply demonstrated that when supply  
6 and demand are not aligned in the short run milk prices can rise or fall dramatically. Hence, if we could  
7 anticipate long markets, we could avoid or minimize the resulting drop in prices.

8 Other countries and regions have had government-regulated production controls. At their most  
9 extreme, such programs include very sophisticated and elaborate programs that establish marketing  
10 quotas on each farm, require quota to market milk, and include stiff and prohibitive penalties for bringing  
11 more milk to market. The EU is in the process of phasing out their quota program. Canada continues to  
12 use a supply management system for milk. Historically, European and Canadian producers have enjoyed  
13 relatively high farm milk prices and stable returns to dairy farming. The U.S. implemented a form of  
14 supply management in 1984-85 with its Milk Diversion Program (MDP). Under the MDP, dairy farmers  
15 were offered payments for reducing milk marketing from 5-30% relative to a base period. The MDP  
16 resulted in higher prices while it was in effect.

17 Historically, European and Canadian producers have enjoyed relatively high farm milk prices and  
18 stable returns to dairy farming. The MDP resulted in sharply higher prices while it was in effect. It is  
19 undeniable that a range of programs of this type can be effective in stabilizing milk prices to farmers  
20 and/or either preventing milk prices from falling precipitously or bringing them back up if they do.

21 The limited US experience with short-term programs of this type and the international experience  
22 with longer-term programs provide lessons that have impacted current policy discussions. A reflection of  
23 this is that proponents of a new, US version of this type of program prefer to refer to it as "growth"  
24 management, rather than the historically common label of "supply" management. This change in name  
25 reflects meaningful intentions about what kind of intervention is sought.

26 Even with the promise of significantly higher prices, few US dairy farmers desire a heavy-handed  
27 public program involving quotas and strict controls on how much milk they market. By the same token,  
28 short-term programs like the old MDP or its successor the Dairy Termination Program (buyout), while



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1 effective when they were actively engaged, failed to have long-term benefits. Thus, a new growth  
2 management program is sought that would operate as a safety net during times of economic distress. It  
3 would have longevity in the sense that it would be available as an ongoing tool, but it would only be  
4 activated when economic conditions warranted intervention to protect farmers from disastrously low  
5 prices. The disincentives created by this program would be real and potent, but they would not be in  
6 place to prevent long term growth or to create new up front costs for new entrants or when farms change  
7 hands.

8 Industry advocacy groups have put several growth management plans forth in recent months.  
9 Although there are important differences in the leading proposals, they all strive to tame milk price  
10 volatility in general and avoid or mitigate especially low milk prices. In this sense, they are intended to be  
11 a safety net. At the same time, all proponents have made it clear that their intention is not to stifle or  
12 discourage long-term investment in the dairy sector. For example, they wish to avoid the accumulation of  
13 value that occurs within strict quota systems, where the right to sell milk may take on very high values.  
14 The new plans allow for natural, long-term production growth, in line with the underlying growth in  
15 domestic and world demand. They try to provide for the natural exit of existing producers and enable new  
16 producers to enter the industry. A healthy exit and entrance is considered necessary to maintain a viable  
17 dairy structure. These plans aim to have little impact on import and export activity; be national and  
18 mandatory; and reduce the cost of government dairy programs in general.

19 Analyses presented to the Committee suggest that a Growth Management Plan could be effective  
20 in reducing milk price volatility and do so at a government cost that is less, perhaps much less, than the  
21 cost of current programs. Dr. Scott Brown of the Food and Agricultural Policy Research Institute at the  
22 University of Missouri and Drs. Charles Nicholson and Mark Stephenson (of The California Polytechnic  
23 State University-San Luis Obispo and the University of Wisconsin, respectively) presented analyses of  
24 these plans to the DIAC. These analyses are part of the public record. They analyzed the National Milk  
25 Producers Federation "Foundation for the Future" plan as a collective package, including the replacement  
26 of price supports and MILC with margin insurance in combination with the Dairy Market Stabilization  
27 Plan. The Costa/Sanders Plan, named after its Congressional sponsors in 2010, adds a growth  
28 management program to existing programs, including the DPPSP and MILC and was also analyzed. As



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1 currently constructed, these programs would not have a significant effect on longer-term dairy farm  
2 returns, as measured by net farm operating income.<sup>15</sup>

3 *Concerns About a Mandatory, National Growth Management Plan*

4 Although there is general agreement that it is essential to align milk marketings with commercial  
5 market needs, how this is accomplished is something about which Committee and industry members more  
6 generally debate. For some, it is simply the case that a federally mandated effort to intervene in the  
7 individual production decisions of a farm business is unappealing or unacceptable in any case.

8 Other critics have concerns that a federal program would be very difficult to run efficiently and  
9 effectively. In this case, the concern is not categorical or based on principle; rather it is practical. Part of  
10 this concern is about the ability of USDA to monitor and enforce individual farm marketings. Other

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<sup>15</sup> Then Pennsylvania Senators Arlen Specter and Robert Casey in the 111th Congress introduced another plan that includes a supply or growth management component. This approach would establish a minimum price for milk used in manufacturing classes based on the average national cost of producing milk. The Class I price would be determined more or less as it currently is.

The act permits supply management in two phases: Under the first phase, if the Secretary of Agriculture determines that there would be overproduction of milk in 2011, he could reduce the value of milk on up to 5 percent of every producer's production. This reduction would be one half of the value of milk used in manufacturing classes. If the corresponding class price were \$20 per cwt, then the reduced price would be \$10 per cwt on up to 5 percent of the farm's milk production.

Under the provisions of the second phase, if the Secretary feels too much milk is going to be produced, he can then put an additional penalty on any producer who produced more milk than the previous year. The Secretary would have full authority to establish a (reduced) value on this extra milk.

This bill was introduced in the Senate in August 2009 and immediately referred to the Senate Committee on Agriculture, Nutrition and Forestry, as is common practice. It has failed to receive sufficient support to move further. Despite the clear indication that there is insufficient political support to move this legislation, linking regulated milk prices to a (full economic) cost of production has passionate support among a group of dairy farmers, even if it requires the Secretary to implement a special program to limit excess production. Although the form of this "inventory management" program is not elaborated, the limited description is consistent with the more recent proposals for "growth management".



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1 concerns are around the ability of any specific formula, trigger or committee to accurately predict the  
2 timing of intervention and the ensuing negative consequences of wrong timing or magnitude.

3 Other concerns relate to potential disruptions in commercial markets, either domestically or abroad.  
4 A fundamental characteristic of any growth management plan is that it would activate or bite more deeply  
5 when milk prices are low or heading down. It is precisely at such moments when the U.S. has enjoyed  
6 significant export opportunities. Thus, it is possible, perhaps even likely, that we would close the door on  
7 our opportunity to grow new markets in foreign countries.

8 The possibility for disruptions in domestic markets also exists. The MDP was intended to be a  
9 national program. It provided the same incentives to reduce marketings everywhere in the US, and it had  
10 no constraints on who could partake in the program. As it turned out, participation in the Southeast was  
11 high because those producers, with their production system, found it easier to make temporary and limited  
12 cutbacks in production than was true in the Upper Midwest and the Northeast. This resulted in a greater  
13 reduction in Southeastern milk marketings, a region that is chronically short of milk. Southeastern  
14 cooperatives incurred considerable additional expense to bring northern milk to the South so that they  
15 could fill out their contractual obligations to Southern processors.

16 Within the Committee there was general agreement that a program should be national in scope, but  
17 different members raised different concerns about cutting marketings on a regional or product sector  
18 basis. Their concern is that the kind of regional effect that occurred in the 1980s programs could happen  
19 with a new program. In addition to the regional effect, some members expressed concern that developing  
20 and high value markets could face an artificial shortage under a growth management plan. In their  
21 opinion, shorting such a market channel would not make sense in either the long or short term, regardless  
22 of any “average” benefit.

23 Thus, these combined concerns are sufficient to cause a significant minority of members to  
24 withhold their support for a federal growth management plan.

25 Programs to Protect and Stabilize Farm Incomes

26 *Price and Income Risk Management*

27 As discussed in the section on existing programs and recommendation 3, USDA’s Risk  
28 Management Agency (RMA) offers two risk management tools that are designed to help dairy farmers.



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1 Private markets had earlier developed more conventional price hedging tools, either on milk price alone  
2 or with input prices. We do not endorse one practice over another, but we make a recommendation that  
3 we believe will enhance the usability of conventional hedging tools.

4 *Recommendation 10: ESTABLISH RISK MANAGEMENT MARGIN LINES OF CREDIT.*  
5 *USDA should develop a credit mechanism (direct lending or credit guarantee) for first*  
6 *buyers of milk (cooperative or proprietary) to cover the margin deposits required on*  
7 *contracts for risk management between first buyers and producers of raw milk.*

8 Direct price hedging and several other risk management tools, like LGM-Dairy, depend on futures  
9 markets. In contrast with other segments of agriculture in which robust futures markets have existed for  
10 decades, futures instruments in the dairy industry have largely been limited to the period since cash-  
11 settled dairy futures were introduced in 1997. Several factors, including lack of historical experience,  
12 minimum contract sizes that exceed some individual farm's production, complexity, and margin  
13 requirements limit direct participation by farms in futures market risk management activities.

14 In many markets, suppliers do not take direct hedging positions. Instead, a buyer will offer a  
15 forward price contract and use futures markets tools to protect their price risk. One reason why this can be  
16 appealing and sensible is that one buyer is able to combine the positions of many sellers. They have the  
17 advantage of that volume to develop expertise and methods to make complex decisions and complicated  
18 transactions more easily than a single seller such as a single dairy farmer. Additionally, the risk  
19 management activity of the producers can be directly incorporated into producer payments, eliminating  
20 the need for producers to track separate futures contract settlements.

21 A specific example relates to "margin calls." In the context of futures markets, "margin" is the  
22 amount of money that must be on deposit by both buyers and sellers of futures contracts to ensure  
23 performance of the terms of the contract. It is one of several mechanisms that the exchanges use to  
24 address the credit risk that might otherwise exist across anonymous counterparties. Initial margin is  
25 required upon initiation of a buy or sell position, and further margin may be required over the lifetime of a  
26 futures position when the price of the futures contracts held by a party is unfavorable to the current  
27 futures market prices. Maintenance margin is the minimum equity that must be maintained for each  
28 contract in a customer's account subsequent to the deposit of the initial margin. Minimum initial and



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1 maintenance margins are set by the exchange for each market but individual brokerage firms may require  
2 margin deposits at higher levels than the exchange minimums.<sup>16</sup>

3 A party's margin account is adjusted daily based upon the difference in the value of the futures  
4 contracts being held and the daily settlement price, a process that is referred to as "mark to market." For  
5 example, if a dairy farmer sold a Class III milk future contract for \$15 and the daily settlement price for  
6 that contract is \$18, she would have been required to wire transfer some portion of the \$3 difference to  
7 her broker in order to maintain the minimum maintenance margin account. If, in contrast, the daily  
8 settlement price for that contract is \$12, she would have been credited the difference in her margin  
9 account. The requests from the brokerage firm to a customer to bring margin deposits up to a required  
10 minimum level are referred to as margin calls.

11 Margin calls are obstacles to direct dairy producer hedging because of the logistical challenge of  
12 having to monitor their positions daily and arrange for a transfer of funds to their broker daily when they  
13 have sold futures at a price below the current price in an upwardly moving market. The logistical and  
14 emotional stress of responding to margin calls is sufficient to keep many producers from managing their  
15 milk price risk directly. Additionally, margin requirements can involve a substantial amount of money,  
16 day to day. The financing of margin deposits can be a considerable expense and a deterrent to using the  
17 hedging tool, even when it ultimately works to the seller's advantage.

18 Programs offered by milk buyers, both cooperative and proprietary, that overcome the obstacles to  
19 risk management are essential to increasing the usefulness of risk management tools for producers. Such  
20 programs have been available for many decades to grain and oilseed producers in the form of cash  
21 forward contracts offered by country elevators. However, the ability for many entities to offer dairy  
22 producers these programs that facilitate producer risk management could be constrained by margin call  
23 encroachment on credit capacities. Even having only half of their producers manage price or margin risk  
24 on half of their milk could generate millions of dollars in potential margin calls per day for some  
25 cooperatives. This working capital may be out of reach for some, even though the margin costs are not

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<sup>16</sup> Plourd, Phil. From Price Taker to Price Maker. Coffee, Sugar & Cocoa Exchange, 1997. Pp. 115-122.



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1 true operating costs of the cooperative or proprietary buyer of milk. Rather, the margin account value  
2 (plus or minus) is reflected in the milk price paid to the producers who contracted for the forward price or  
3 margin. As a result, the risk associated with default on the debt associated with the margin calls is  
4 minimal.

5 In such circumstances, facilitating financial tools can have a powerful effect on the ability of a  
6 company to develop and use risk management tools. It is in this vein that the Committee recommends that  
7 USDA, through its existing credit programs, develop new financial products that would make it easier to  
8 finance margin calls and thereby enhance the usability of hedging tools.

9 The Committee recommends that USDA establish a credit mechanism to facilitate risk  
10 management margin lines of credit to first buyers (cooperative or proprietary) of milk. These lines of  
11 credit should be available through the direct lending or credit guarantee program. Funds that could be  
12 borrowed against the line of credit would be restricted to funds required to cover margin calls associated  
13 with bona fide risk management activity documented by contracts between the first buyers and producers  
14 of raw milk.

15 This recommendation should not be taken as an endorsement of simple price hedging as a risk  
16 management tool above all others. This recommendation is intended to improve the usefulness of an  
17 existing tool. It does not preclude the development or improvement of other tools that might be used  
18 instead of or in addition to price hedging.

19 *Modified MILC and Margin Insurance*

20 *Recommendation 11:*

21 *MODIFY MILK INCOME LOSS CONTRACT PROGRAM AND PROVIDE A MARGIN*  
22 *INSURANCE OPTION using funds from the elimination of the DPPSP and DEIP. Continue*  
23 *MILC, with a production cap based on available funds, with two important modifications:*  
24 *(1) use an all-milk income/feed cost margin trigger, and (2) provide an insurance program*  
25 *for production excluded by the cap to provide protection for larger producers.*

26 Rapid input price inflation following World War II led to low net returns to dairy farmers even as  
27 milk prices were increasing as well. The adoption of the Dairy Price Support Program as part of



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1 permanent law in the Agricultural Act of 1949 was a strong Congressional endorsement of the merits of  
2 some kind of "safety net" protection for dairy farmers against extreme economic distress. As discussed  
3 elsewhere, the current DPPSP is no longer structured to provide much help to dairy farmers and the  
4 primary safety net tool has become MILC. The committee believes that some kind of federal safety net  
5 continues to be warranted. As is true of the industry at large, different members have different  
6 preferences for specific forms or types of safety net programs. For some, the growth management concept  
7 is more appealing or believed to be more effective. Some favor a safety net only under economic  
8 conditions that are extreme and largely unpredictable, such as occurred in 2009, but perhaps not in the  
9 case of the cyclical downturns in 2002-03 and 2006. Some are ready to trade all existing safety net  
10 programs for new programs based on an insurance-type program calibrated around milk margins over  
11 feed costs. To the extent there is a debate, it should be noted that the debate is not about the concept of a  
12 safety net, but rather on what form is most effective or fair.

13 In considering existing programs, in particular MILC, and new proposals, such as the NMPF Dairy  
14 Producer Margin Protection Program (DPMPP), many members of the Committee were intrigued by the  
15 possibility of combining these two approaches. Ultimately the recommendation that mustered the greatest  
16 support in the committee was to retain the basic framework of the MILC program but amend the trigger  
17 and add on a margin insurance type program for milk marketed in excess of the payment cap.

18 Every farmer would prefer that the monthly market price of milk be at a level that results in a fair  
19 and adequate net return. This has not been the reality of milk markets for many years. In the absence of  
20 that condition, MILC has significantly helped a lot of farmers during challenging times. Although the  
21 payment limitation constrains benefits for larger farms, 76 percent of herds nationally have fewer than  
22 100 cows; another 13% have between 100 and 200 milking cows cap.<sup>17</sup> Thus, some 80% of all US farms  
23 are eligible to receive the full countercyclical payment on all their milk sales.<sup>18</sup> Farm sizes are not  
24 distributed the same across all states, but producers in every state have received benefits from MILC.

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<sup>17</sup> [http://www.nass.usda.gov/QuickStats/Create\\_Federal\\_All.jsp](http://www.nass.usda.gov/QuickStats/Create_Federal_All.jsp)

<sup>18</sup> The cap becomes operable at ranges of 130-180 cows depending on production levels.



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1 Farmers in Wisconsin received an average of \$13,300 per herd; in New York the average is \$13,400; in  
2 California it is \$47,000; and in Georgia the average dairy farm received \$26,470.<sup>19</sup>

3 MILC has significantly helped farmers during challenging times. Although the payment limitation  
4 constrains benefits for larger farms, 76 percent of herds nationally have fewer than 100 cows; another  
5 13% have between 100 and 200 milking cows.<sup>20</sup> Thus, about 80% of all U.S. farms are eligible to receive  
6 the full countercyclical payment on all their milk sales.<sup>21</sup> Farm sizes are not distributed the same across all  
7 states, but producers in every state have received benefits from MILC. Farmers in Wisconsin received an  
8 average of \$13,300 per herd; in New York the average is \$13,400; in California it is \$47,000; and in  
9 Georgia the average dairy farm received \$26,470.<sup>22</sup>

10 In the discussion of dairy farm profitability and in conjunction with recommendation 1, we have  
11 previously stated the merits of using the simple milk margin over feed cost measure instead of focusing  
12 on the price of milk alone. We have also recognized that this financial measurement is not without some  
13 limitations. Nevertheless, it is our conclusion that it makes sense to use one measure as the action signal  
14 for any safety net program. Hence, we recommend that a milk margin over feed cost trigger replace the  
15 feed cost adjusted Boston Class I price trigger that is currently used for MILC. There should be some  
16 examination of which feed prices to use and how to most quickly distribute funds to farmers.

17 While we believe modifications to the existing MILC program or its implementation would  
18 improve it, we recognize that this does not address the concerns of the largest dairy farmers for whom  
19 MILC provides little assistance and may even make their situation worse by prolonging periods of low  
20 milk prices. To address this concern, we recommend a supplemental margin protection plan that would  
21 offer all producers the opportunity to protect their margin on volumes of milk marketed in excess of the  
22 payment cap for MILC. The nature of this plan and how it would work is based on the modified MILC

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<sup>19</sup> Calculated from data on MILC payments by state and number of farms by state from USDA.

<sup>20</sup> [http://www.nass.usda.gov/QuickStats/Create\\_Federal\\_All.jsp](http://www.nass.usda.gov/QuickStats/Create_Federal_All.jsp)

<sup>21</sup> The cap becomes operable at ranges of 130-180 cows depending on productivity levels.

<sup>22</sup> Calculated from data on MILC payments by state and number of farms by state from USDA.



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1 plan. The same payment trigger would apply. If the actual national average margin in a month fell below  
2 the specified payment trigger, a MILC payment program would automatically activate. The margin  
3 insurance supplement would allow dairy farmers who want to receive coverage on larger volumes of milk  
4 to obtain that coverage by paying a modest premium. Similarly, the program could offer higher margin  
5 protection levels for any farmer, large or small, by setting a higher payment trigger for a premium charge.

6 This supplemental “buy-up” insurance tier would include a federal subsidy for buying additional  
7 margin coverage protection. The subsidy amount would be based upon a sliding scale. As higher coverage  
8 levels are elected, producers will get a lower subsidy on the cost of the margin protection.

9 Countercyclical payment programs, of any type, must contend with the desire to protect dairy  
10 farmers from severe market events versus the desirability of allowing markets to work and send  
11 appropriate price signals when supply is long relative to demand. This is a difficult balancing act, and  
12 there will be different perspectives on when that balance is disturbed too much in one direction or the  
13 other. It is also likely that a federal program of countercyclical payment will undermine the incentive to  
14 use private risk management tools. This is evident in the case of other agricultural crops.

15 The Committee does not have a specific recommendation for the magnitude of the MILC margin  
16 trigger or the parameters of a supplemental margin protection program. We assume that the types of  
17 parameters desired and the level of protection that the government can afford to offer will be subject to  
18 active public debate. We believe that government savings from the elimination of the DPPSP and DEIP  
19 programs should be used to fund the MILC program and subsidize the premiums for supplemental margin  
20 insurance at a level consistent with an economic safety net goal.



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1 *Farm Savings Accounts*

2 *Recommendation 12:*

3 *ADOPT TAX-DEFERRED FARM SAVINGS ACCOUNTS. Federal tax law should be*  
4 *amended to allow dairy farm operators to create special tax-deferred savings accounts.*  
5 *These accounts should not be subject to matching government contributions and should not*  
6 *have a limit on dollars deferred per year. To be eligible, contributions must remain in the*  
7 *account for a minimum of six months; the account-holders can withdraw funds at their own*  
8 *discretion thereafter. Payment of income taxes on contributions and interest would occur in*  
9 *the tax year in which the funds are withdrawn.*

10 Tax-deferred farm savings accounts are one of several tools that should be in the dairy farm  
11 toolbox to assist in the private management of volatility in prices and farm returns. Farm savings  
12 accounts are a vehicle, somewhat like a retirement investment account, that farmers can use to defer  
13 taxable income. A retirement account is designed to transfer taxable income from years of high earned  
14 income before retirement to years of low earned income after retirement. The farm savings account  
15 concept is to transfer taxable income from highly profitable years to years of low or negative taxable  
16 returns. Like a retirement savings account, a special qualified account would be established but the  
17 management of the funds within the account would be entirely at the discretion of the owner.

18 The concept of a tax-deferred farm savings accounts was explored as an alternative to traditional  
19 crop programs during the development of the 2002 Farm Bill. They were ultimately rejected in favor of  
20 the more familiar programs. There are important differences between those older proposals for crops and  
21 what is proposed here, although the basic concepts are the same. One key difference is that the earlier  
22 proposals included government incentives in the form of matching funds. This was patterned after the  
23 subsidies to inspire the use of crop insurance. In contrast, the Committee believes that tax-deferred  
24 savings accounts have merit as a margin management tool by themselves. While we do not doubt that a  
25 government match would encourage use of the accounts, we do not recommend using scarce government  
26 funds for this purpose.

27 Another very important difference is that previous proposals, and also a similar program in Canada,  
28 were burdened with many restrictions on how money could be deposited to and withdrawn from a savings



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1 account. In contrast, this Committee recommends that the only limitations would be that deposits could  
2 only be made on amounts of taxable income reported on Schedule F of the IRS 1040 form. So, farmers  
3 have to have taxable farm income to save. They cannot create a farm "loss" by depositing more money in  
4 a farm savings account than the farm earned in taxable net income. Likewise, withdrawals would be  
5 reported as a farm earning on Schedule F in the year they are withdrawn. We recommend that a period of  
6 six months must lapse before a deposit can be withdrawn.

7 In transferring taxable farm income across years, this program is intended to mitigate cash flow  
8 volatility, both for the individual participant and for the industry as a whole. Analysis presented to the  
9 Committee by Nicholson and Stephenson determined that the impact of a version of Farm Savings  
10 Accounts on milk price volatility is "comparable to the reduction observed for other proposed programs  
11 such as Costa Sanders, Marginal Milk Pricing or Foundation for the Future."<sup>23</sup>

12 A Farm Savings Account helps producers manage income risk, but it does not shield them from  
13 risk or eliminate the risk. It only works if a producer is able to operate at a level where average returns  
14 over many years are adequate, and it only makes sense if specific returns in any given year are highly  
15 variable relative to that adequate average return. If these conditions are true, then any farm, regardless of  
16 size or location, could take advantage of a farm savings account.

17 The Committee recognizes that a farm savings account would generally not be used in the current  
18 environment. It works best in moving taxable income from a high margin year to a low margin year. The  
19 dairy cycle will eventually move farm incomes up, but that does not characterize 2010 and probably will  
20 not occur in 2011. However, we would strongly suggest that now is precisely the right time to begin to  
21 develop this program so that it can be available in the next up phase of the dairy cycle.

22 In addition to assisting producers through periods of financial stress by creating a cash reserve,  
23 farm savings accounts may well have the benefit of reducing capital costs on farms. Most farmers are  
24 highly motivated to avoid income taxes. They do so in two basic ways. In years of relatively high

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<sup>23</sup> Nicholson, Charles and Mark Stephenson; Initial Analysis of the Impacts of a farm Savings Account Program on Price Volatility, Preliminary Analysis, September 17, 2010.



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1 profitability, they take advantage of farm cash accounting and purchase consumable inputs, like feed and  
2 fertilizer, and investment inputs, like equipment or cattle, to report as expenses in higher income years,  
3 assuming that this will balance out in the coming year, when they actually will begin using the inputs.  
4 This is not an effective strategy unless the second year has significantly lower returns than the first year,  
5 especially for investment inputs. A farm savings account does not require a profitable year to be followed  
6 by an unprofitable year.

7 The second common farm business strategy is to borrow operating capital in years of low net  
8 returns. This replaces operating cash with borrowed cash to maintain necessary cash flow balance. The  
9 alternative of balancing cash flow in a low year by drawing on cash reserves saves the cost of borrowing.  
10 Credit costs can also be an issue in the profitable year. If a farmer buys an investment input to declare as a  
11 cash expense in the high year, he is generally still left with some portion of capital being financed. Thus,  
12 farmers incur an ongoing intermediate or long-term interest expense in the good year and a short-term  
13 interest expense in the bad year. The farm savings account, once it is established, would earn farmers an  
14 interest return. This is a sharp contrast to the cost of credit incurred with current tax management  
15 practices.

16 One particular form of this strategy that bears noting is the level of investment in farm expansion  
17 and other production enhancing capital projects that are made with the objective of avoiding tax liabilities  
18 under current tax law. If farm savings accounts reduced or eliminated current incentives to reduce tax-  
19 avoidance driven farm expansion it may reduce the production surge that often contributes to a deeper  
20 down cycle after profitable years.

21 The Committee recommends amending federal tax laws to provide for farm savings accounts that  
22 contain the following provisions:

- 23 1) No limits on the dollars deferred per year, except that the deposit may not exceed the taxable farm  
24 income on Schedule F, excluding the deposit.
- 25 2) No government match on farm deposits.
- 26 3) Deposited money must remain in the account a minimum of six months but otherwise withdrawal  
27 in amount and timing is allowed at the account-holder's discretion thereafter.



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- 1           4) Withdrawals from the account are taxable as Schedule F income whether they derive from the  
2           original principal or from earnings on the account.

3           The rules proposed above would provide a tool that benefits dairy producers through the  
4           development of a tax deferral mechanism that could result in reserve capital to address margin down turns  
5           or negative cash flow. Because dairy farmers already largely reduce their tax liability through forward  
6           purchases or expansion, this proposal should have minimal impact on tax collections.

7           Programs to Improve Profitability and Dairy Markets

8           *Recommendation 13:*

9           *SUPPORT COMPETITIVE MARKET STRUCTURES: USDA, through its regulatory*  
10          *authority and in cooperation with FTC and DOJ, should continue to monitor and support*  
11          *competitive marketing structures throughout the supply and marketing chain of the dairy*  
12          *industry.*

13          Market power, whether deriving from monopolistic power, product differentiation or collusion,  
14          conveys the opportunity to control supply and raise price. Traditional industrial organization theory  
15          connects, although it does not require, market power and market concentration. Dairy markets are  
16          increasingly dominated by one or a few firms, and concentration has been increasing at all levels of the  
17          market chain. Many farmers have fewer potential buyers for their milk, and in some areas only one is  
18          common (Senate Hearing, 2003 Serial No. J-108-51).<sup>24</sup> Some processors of dairy products have  
19          significant market share in their product categories. One company accounts for 30% of fluid milk sales  
20          across the U.S.<sup>25</sup> and in some areas that same company has 70% of the local market.<sup>26</sup> A few firms also  
21          increasingly dominate distribution and retail channels and almost half (46%) of the retail sector is

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<sup>24</sup> Senate hearing, 2003 (October 30). Monopsony issues in agriculture: buying power of processors in our nation's agricultural markets hearing before the committee on the judiciary United States Senate One Hundred Eighth Congress First Session. Serial No. J-108-51

<sup>25</sup> Feedstuffs 1/19/04)

<sup>26</sup> Senate Hearing, 2003 Serial No. J-108-51, p.5



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1 comprised of five companies<sup>27</sup>. By the same token, processors themselves can also face few potential  
2 suppliers of milk. The US Department of Justice is studying issues of market power in food markets.  
3 Dairy is one of the markets receiving close attention.

4 A variety of concerns have been raised in public testimony and comments made to the committee.  
5 These include:

- 6 • A declining farm share of the retail expenditures on dairy products
- 7 • The short term relationship between price changes at the retail or wholesale levels and the  
8 farm price of milk
- 9 • The health or fairness of competition in wholesale level markets
- 10 • The implications of the competitive structure of the industry for dairy farm prices and  
11 marketing options
- 12 • The importance of the Chicago Mercantile Exchange as a primary de facto price discovery  
13 tool for the dairy sector and its appropriateness for that purpose

14 A number of studies have been done on various aspects of these questions and regulatory agencies  
15 such as the Commodity Futures Trading Commission and the Department of Justice Antitrust Division,  
16 have formally and informally explored these general questions and specific activities. Research is  
17 ongoing but to date the various studies have not provided either a solution or a firm conclusion to resolve  
18 these concerns. Regulatory and legal efforts have resulted in some specific mitigating actions, but no  
19 evidence of widespread market failure has been determined or revealed.

20 The Committee recommends that the Secretary continue to monitor and support competitive  
21 market structures throughout the dairy value chain and consider potential impacts on healthy competition  
22 when developing and implementing regulatory programs.

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<sup>27</sup> Progressive Grocer's Super 50 (5/1/04)



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1 *Export Markets*

2 *Recommendation 14:*

3 ***MAINTAIN AND EXPAND PROGRAMS FOR EXPORT MARKET DEVELOPMENT.***

4 *Programs like the Market Access Program and the Foreign Market Development Program*  
5 *should be continued and expanded.*

6 Ample evidence has been presented to the Committee that the U.S. is uniquely positioned to take  
7 advantage of export opportunities. The transition to becoming a consistent supplier of value-added dairy  
8 products should provide more consistent and resilient export volumes, thereby reducing the incremental  
9 price volatility currently contributed by our volatile export volumes. The Committee recommends that  
10 USDA maintain and even expand its trade export development capacity to take advantage of new export  
11 opportunities for dairy products and increase exports of value-added dairy products.

12 Several USDA programs, including the Market Access Program (MAP) and the Foreign Market  
13 Development Program (FMDP) administered by the Foreign Agricultural Service fund activities that  
14 introduce U.S.-produced dairy products to key export markets and are important components of the  
15 budgets of organizations like the U.S. Dairy Export Council.

16 Recently, the National Commission on Fiscal Responsibility and Reform released its findings<sup>28</sup> on  
17 areas reconciling the budget deficit through policy and fiscal reform. Spending suggestions covered a  
18 range of Federal Agencies and programs. Changes to agricultural programs included spending reductions  
19 for MAP. This recommendation is in direct conflict with the Administration's goal of doubling exports  
20 2015. Programs like MAP implement the Administration's goal by facilitating export enhancement. MAP  
21 is a sound investment in US agriculture's global competitiveness and results in increased U.S. exports.  
22 Considering new export goals and the benefit to the U.S. dairy industry, MAP funding should be  
23 maintained.

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<sup>28</sup> The National Commission on Fiscal Responsibility. "[The Moment of Truth](#)." December 2010. White House Release.



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1           The export market has been especially important to the U.S. dairy industry price recovery in 2010.  
2           During the first nine months of 2010, U.S. exports were equivalent to 43 percent of the total nonfat dry  
3           milk/skim milk powder (NDM/SMP) produced, 65 percent of the whey proteins, 65 percent of the  
4           lactose, four percent of the cheese, and eight percent of the butter produced in the US.

5           A review of the price relationship between the domestic and international markets and import /  
6           export data substantiates the interplay between U.S. and international dairy prices. Prior to the  
7           implementation of the WTO reforms in the mid-1990s, U.S. exports were minimal. The implementation  
8           of the WTO Agreement on Agriculture, combined with ongoing reforms to the EU Common Agricultural  
9           Policy, resulted in reduced export subsidies from the E.U. Increased animal protein demand in  
10          developing countries and the convergence of U.S. and international prices over the last decade has  
11          resulted in increasing U.S. exports and an improved balance of dairy trade. In fact, international prices  
12          have exceeded U.S. prices for long periods since 2005.

13          WTO negotiations to further liberalize trade may have important consequences for the dairy sector.  
14          The impact of WTO tariff commitments and the funds required to pay damages if the U.S. were to  
15          increase its tariff barriers beyond agreed levels makes isolation of the domestic market unlikely and  
16          untenable. Additionally, a protectionist approach that isolates the U.S. markets and significantly raises  
17          prices would reduce or eliminate the greatest growth opportunities for the U.S. dairy industry.

18          Global demand for dairy products is increasingly driven by income growth and changing diets in  
19          developing countries. That has opened up new opportunities for dairy product exports and also increased  
20          the correlation between farm-gate prices in different countries. We live in a market economy and ninety-  
21          six percent of the world's population, live, purchase and consume products outside of the United  
22          States. During the Committee discussions it was stressed that the dairy industry has become increasingly  
23          globalized and complex, there is higher volatility in output and input prices, and new sources of demand  
24          growth (exports, functional nutrients, pharmaceutical products) are emerging.

25          The Committee recognizes it must use caution when using existing econometric models to predict  
26          world demand. Because export demand is so new to the U.S., existing models may over simplify and  
27          underestimate the situation, making predicting demand and supply challenging. However, in general  
28          terms, the potential for an expanding market for international trade is based on the projection that the



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1 number of middle-class consumers in emerging markets is projected to triple by 2030, reaching one  
2 billion in that year. These consumers will demand more animal proteins for their diets, including dairy  
3 products. For example: China has 20 percent of the world's population and growing per capita income.  
4 Its dairy product consumption is expected to increase by about 10 percent annually in the coming years.  
5 Dairy product consumption is also expected to grow by 4 to 9 percent annually in Southeast Asia,  
6 depending upon the country. Mexico, Algeria and Saudi Arabia have recorded increases in dairy product  
7 consumption and are open to dairy imports. Mexico, in particular, will continue to represent a growing  
8 market for U.S. dairy exports. The opportunity for sales to these countries exists now as they start to  
9 invest in their own dairy infrastructure. The U.S. dairy industry needs to be proactive in competing for  
10 these markets with product they want. The world market can become a dependable growth sector for U.S.  
11 dairy whether supply is in surplus or deficit. The US can be a player in the world market if it reacts to  
12 world trends rather than expecting the world market to be tailored to U.S. current manufacturing capacity.

13 Expanding existing market access and opening new markets under future trade agreements will  
14 significantly boost U.S. agricultural export sales. However, the industry's current role as largely a residual  
15 supplier of bulk commodities is leading to increased volatility in the U.S. market. The U.S. needs to be  
16 proactive in marketing more profitable value-added product as well as bulk commodities on the world  
17 market.

18 *Farm Milk Quality*

19 *Recommendation 15:*

20 *LOWER SOMATIC CELL COUNT LIMIT FOR GRADE A MILK. We recommend that the*  
21 *Secretary of Agriculture support the adoption of a maximum somatic cell count of Grade A*  
22 *milk in the amount of 400,000 cells per milliliter at the farm level at the Interstate Milk*  
23 *Shippers Conference. The implementation should occur over a period of time not to exceed*  
24 *48 months.*

25 The quantity of somatic cells in milk is one of the primary indicators of milk quality. Elevated  
26 somatic cell counts (SCC) are indicative of mastitis, or the inflammation of the udder, which may or may



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1 not be accompanied by clinical signs of inflammation.<sup>29</sup> Annual losses in net milk income per cow for  
 2 subclinical mastitis are estimated at \$200 per year. For every clinical case of mastitis in a herd, there are  
 3 likely 15-40 cases of subclinical mastitis and these cases may be responsible for up to 70% of production  
 4 losses associated with mastitis. The typical production losses associated with different levels of SCC in  
 5 the milk are illustrated in the accompanying table. Every dollar invested in a mastitis control program  
 6 will return \$15-20 in production, premiums, and reduced death and culling.<sup>30</sup>

Bulk tank SCC	Percent infected quarters in herd	Percent production loss
200,000	6	0
500,000	16	6
750,000	25	12
1,000,000	32	18
1,500,000	48	29

7  
8  
9  
10  
11  
12 This basic biology is well understood; however, science alone cannot provide a discrete answer to  
 13 the optimal somatic cell count standard. High SCC is an indication of a herd health issue, but levels that  
 14 may indicate that a production management response is appropriate are not an indication that there is a  
 15 food safety issue. In fact, we are confident that current standards provide ample consumer protection and  
 16 that Grade A dairy products are safe. Nevertheless, there are many improvements to quality that are  
 17 worthwhile even though they don't relate to food safety. In addition to productivity lost at the farm level,  
 18 high SCC levels also have negative impacts on dairy processing, especially lowering cheese yields.

19 The Food and Drug Administration through the Pasteurized Milk Ordinance (PMO) oversees the  
 20 U.S. somatic cell count (SCC) standard. The National Conference on Interstate Milk Shipments (NCIMS)  
 21 is held every two years and its members debate proposed changes to the PMO. The National Milk

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<sup>29</sup> Clinical mastitis is those infections that are typically accompanied by the observable signs of inflammation: redness, swelling, heat and pain, and abnormal milk. Subclinical mastitis is infections that result in high somatic cell counts, but the udder and the milk appear normal.

<sup>30</sup> Dr Linda Tikofsky: Quality Milk Production Services, Cornell University



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1 Producers Federation (NMPF) proposes lowering the SCC standard to 600,000 cells per ml effective Jan.  
2 1, 2012; 500,000 cells per ml by Jan. 1, 2013; and 400,000 cells per ml by Jan. 1, 2014.<sup>31</sup> This resolution  
3 is expected to be presented at the NCIMS in April 2011. If passed, the NCIMS will recommend to FDA  
4 to lower the SCC standard contained in the PMO.

5 The European Union (EU) has declared that all farm milk used in U.S. exports to their member  
6 countries must be held to the same SCC standard as domestic EU dairy producers. The EU standard is  
7 currently 400,000 cells per ml at the farm level.

8 The Committee believes that lowering the U.S. SCC standard would increase access to European  
9 markets, encourage producers to remove inferior animals, improve on farm management practices, and  
10 increase the quality of U.S. milk. This may enable the U.S. to be more competitive in other markets as  
11 well. However, the move to a stricter SCC standard should be done carefully and in phases so as to not  
12 inhibit U.S. price competitiveness or place greater strain on dairy producers and those agencies that support  
13 them.

14 The committee cautions that the regulatory change for Grade 'A' milk should be carefully  
15 implemented by the FDA because the E.U. SCC standard is quite different than the current U.S. SCC  
16 standard. If U.S. standards are changed to mirror the E.U. standards, the U.S. should use similar testing  
17 mechanisms so unnecessary burdens are not placed on U.S. producers or regulatory agencies. The shift of  
18 focus to farm level SCC counts is a dramatic change from using the commingled silo or tanker for testing  
19 for regulatory purposes. Also, the current U.S. method of SCC sampling for purposes of regulation is  
20 one-point-in-time versus the E.U.'s three-month rolling geometric mean. It should also be noted that the  
21 E.U. makes exceptions to this standard for products such as raw aged cheese and for certain countries  
22 such as Romania, which is exempt.

23 The U.S. dairy industry should be able to adapt if the regulations are implemented carefully.  
24 Dairy producers have already demonstrated their ability to adapt in response to stricter SCC standards

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31 It should be noted that their proposal gives some discretion for seasonally dependent events.  
<http://nmpf.org/latest-news/news-dairy-coops/articles/eu-somatic-cell-count-standard-still-unresolved>



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1 when the regulated SCC standard was reduced from 1,500,000 cells per ml to 1,000,000 cells per ml in  
2 the 1970s and from 1,000,000 cells per ml to the current 750,000 cells per ml around 1990.

3 *Dairy Product Quality – Enhanced Fluid Milk Solids Standards*

4 *Recommendation 16:*

5 *ENHANCED FLUID MILK SOLIDS STANDARDS: The Secretary should explore the*  
6 *impacts of California-type fortification standards for U.S. beverage milk.*

7 Milk contains water, nonfat solids and butterfat. The nonfat milk solids are composed of proteins,  
8 lactose and minerals. The percentage content of any cow's milk varies by breed of cow, season, diet and  
9 region. Nationally, the average annual composition of milk is 8.72 percent nonfat solids and 3.67 percent  
10 butterfat, with the remainder being water.

11 The FDA establishes minimum standards for fluid milk products. States can also establish  
12 standards for fluid milk marketed within the State. The minimum standard for nonfat solids for the  
13 majority of the country is 8.25% for fluid milk at the retail level. Since 1962 fluid milk marketed in  
14 California has to meet different standards. The current standard is 8.7% for whole milk, 10% for reduced  
15 fat (2% fat) milk, 11% for low fat (1% fat) milk and 9% nonfat solids in skim milk. There are several  
16 fortified fluid milk products commercially available in other states. These products have been developed  
17 by companies who are using conventional market mechanisms to differentiate products and segment  
18 consumer preferences. These products come in a wide variety of forms and may involve fortification  
19 techniques and ingredients quite different from the standardized California products.

20 Over the last 20 years there have been numerous studies of the effects of imposing California fluid  
21 milk standards across the US<sup>32</sup>. At the request of the US Congressional Dairy Farm Caucus, the  
22 University of Missouri's Food and Agricultural Policy Research Institute wrote a report to consider the  
23 potential effects of mandating California fluid milk standards on a national level (FAPRI study).

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<sup>32</sup> Salathe and Price, Outlaw et. al., Boynton



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1           The study indicated that fortifying the nation's milk to California standards would remove an  
2 additional 350 million pounds of nonfat solids per year. That would quickly drive nonfat dry milk prices  
3 higher and increase average farm milk prices by 27 cents per hundredweight during the first year. Those  
4 price increases would then slip to 17 cents in the second year and narrow to 9 cents by the seventh year,  
5 the study said, as farmers increase milk production in response to the higher prices and consumer demand  
6 decreases because of higher milk prices. The study estimated that the cost of the additional milk solids  
7 alone would increase the retail price of a gallon of milk by about 17 cents. The study did not have a  
8 current estimate of other processing costs that might increase because of fortification.

9           Although the FAPRI study mirrors previous studies, it notes, "The market situation is very  
10 different today than when those studies were conducted." One key difference is that the U.S. dairy sector  
11 has now become a major exporter of skim milk solids. Past studies were done when there were large  
12 government stocks of nonfat dry milk, and adding more solids to milk was thought to be a way to reduce  
13 that surplus. Today, the effect of fortification would reduce exports, the study said, as fewer nonfat solids  
14 become available. Because a majority of the Committee were not comfortable that current studies  
15 illustrate a long-term benefit to dairy farmers, the committee supports further investigation of the areas  
16 that the FAPRI report did not cover. Some of these questions could be:

17           1. How will consumers respond?

18           FAPRI shows that retail milk prices will likely rise under California fluid standards and the  
19 consumers later responds to higher prices. There is insufficient data to assess the effect of higher prices  
20 and whether consumers may substitute other products. Advocates of the California products argue that  
21 they are better because lower fat products retain more of the "mouth feel" of the whole milk product.  
22 They contend that U.S. consumers would prefer fortified products and that milk sales would increase.  
23 However, higher standards in California have not resulted in increased volume sales. Critics raise  
24 concerns that the different taste and mouth feel of fortified milks could alienate milk drinkers accustomed  
25 to unfortified milks. The committee recommends more study of the impact on consumer purchases.

26           In addition, will there be regional consumer price differentials that may lead consumers to consider  
27 substitutes if the differentials are too high? The issue of increased cost and what percentage is passed on  
28 to the consumer or absorbed by the manufacturer/retailer is an important issue that will need to be  
29 investigated and assessed.



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1           2. What is the availability of nonfat solids and how will this impact trade?

2           There have not been excess solids in recent years, and under conditions of significant milk exports,  
3 there is unlikely to be excess solids. There is potential for encouraging further imports of MPC from New  
4 Zealand and other places if U.S. solids are not readily available and price competitive. The change in  
5 standards would likely frustrate organic producers, as organic NDM powder is in short supply.

6           3. What are the regional disparities?

7           The FAPRI study also showed that price benefits to dairy farmers were regional, with farmers in  
8 heavy nonfat dried milk (NDM) producing states, such as California, benefitting while dairymen in large  
9 cheese-producing states, such as Wisconsin and Minnesota, actually seeing milk price decreases over  
10 time. Increased milk production and potentially reduced consumption would drive cheese and butter  
11 prices lower, according to the analysis. The Secretary should also consider any potential impact on  
12 producer prices should DPPSP be terminated.

13           4. How will this influence fluid processors?

14           The committee realizes that the FAPRI report on fluid milk fortification does not consider the  
15 potential additional cost of equipment that may be required to fortify milk and associated operating  
16 expenses. Some processors would have additional capital costs for storage tanks and blending or other  
17 equipment. Those manufacturers already set up to handle the increased storage may well have a  
18 competitive advantage while others experience conversion costs. In most cases, smaller scale processors  
19 would have to use dry milk powder. As dry milk powder oxidizes over time, some modification of storage  
20 conditions for dry materials might be required. This could leave smaller plants more vulnerable to  
21 procurement factors. Given recommendation 13 to maintain competitive market structures, we would also  
22 want to see analysis of the potential impact on bottler consolidation because of these higher costs.

23           Our recommendation to explore the impacts of California-type fortification standards for US  
24 beverage milk recognizes the many differences of opinion within the dairy industry and the lack of  
25 conclusive evidence in existing studies. The committee recommendation keeps this as an option among  
26 various ideas that are part of a national solution. We are hopeful that the new standards would increase  
27 the farmer pay price and could have benefits for consumption of fluid milk, but we acknowledge that  
28 there isn't enough information available to adopt new standards at this time.



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1 *Dairy Product Quality – Dairy Product Labeling*

2 *Recommendation 17:*

3 *RESTRICT USE OF DAIRY DESCRIPTORS ON PRODUCT LABELS. We recommend that*  
4 *USDA support restriction of dairy descriptors, including terms such as milk, cheese, yogurt,*  
5 *butter, for use on products made from milk.*

6 Product innovation has occurred throughout the food sector. Many dairy products are no longer  
7 limited to strictly defined standards of identities, and many new novel products have been introduced to  
8 the market. At the same time, some non-dairy products have associated themselves by connotation or  
9 direct reference with the positive image of dairy products. This has the potential to lead to consumer  
10 confusion about the composition of such products. Dairy products have beneficial combinations of  
11 nutrients not found in other products. Advertising and food container labels should be accurate and  
12 truthful so consumers are properly informed of product contents and are not misled. Making informed  
13 food choices would improve nutrition and increase overall health.

14 The Committee is concerned that misleading food product names or labels are having a detrimental  
15 impact on dairy product sales. Some products are currently being marketed that mimic traditional dairy  
16 products and are labeled using milk or dairy terms.<sup>33</sup> For example, there are a number of beverage  
17 products that use the word "milk" in their brand name or product name, yet these products do not meet the  
18 standard of identity for milk. Sometimes these products are positioned in stores to directly compete with  
19 conventional fluid milk or other dairy products. The committee supports healthy competition and  
20 consumer choice, but consumers must have access to accurate information and not be misinformed or  
21 confused when making their choices.

22 The committee feels that milk and dairy products utilizing added protein or calcium in their  
23 production should, ideally, use natural milk ingredients in the fortification process. It was noted however,  
24 that this requirement could only be applied to dairy products with a FDA Standard of Identity. Accurate

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<sup>33</sup> The committee's concern extends to subtle misspellings that may suggest milk content or equivalence, e.g. Kreme or Cheez.



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1 dairy product descriptions and formulations that comply with legal FDA definitions and production  
2 practices can only make it easier for the consumer to purchase products that are not misrepresented.

3 Our recommendation is not intended to stymie innovation or prevent dairy product manufacturers  
4 from using ingredients that are and have been customarily added to dairy products, such as flavorings,  
5 seasoning, vitamins, and similar functional ingredients. These inclusions are common for dairy products  
6 and add to the dairy product experience. Our concerns lie in subtle or blatant portrayals of non-dairy  
7 foods or ingredients as being the same as milk and dairy products.

8 The Committee recommends that the Secretary of Agriculture support restrictions on dairy  
9 descriptors that will help preserve the integrity of milk's nutritious and wholesome image. Eliminating  
10 confusion over product identity and content will likely favor and protect demand for milk and dairy  
11 products. Truthful and accurate food labels can also contribute to improving consumer health and helping  
12 them to make accurate and educated choices.

13 *Dairy Management Practices and Production Costs – Value-Added Dairy Operations*

14 *Recommendation 18:*

15 *SUPPORT FOR VALUE-ADDED DAIRY. We recommend that the Secretary of Agriculture*  
16 *support programs that enhance value-added market development for dairy farms and dairy*  
17 *products. Opportunities should be explored including, but not limited to, the development of*  
18 *educational training programs and technical assistance for farmers, inspectors, and*  
19 *regulatory personnel to accommodate unique value-added dairy farm operations. A study*  
20 *should be made to examine the impact of user fees on value-added dairy product operations.*

21 Opportunities exist for dairy farms to increase their profitability and sustainability by the marketing  
22 of value-added dairy products. Indeed, in the last five years, the number of farms in the United States has  
23 grown 4 percent and the operators of those farms have become more diverse, according to results of the  
24 2007 Census of Agriculture. The latest census figures show a continuation in the trend towards more very



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1 small and very large farms and fewer mid-sized operations. Many of these smaller farmers are either  
2 beginning farmers<sup>34</sup> and/or second career farmers.

3 Local and regional food systems are the fastest growing areas in agriculture.<sup>35</sup> The value-added  
4 marketing of dairy products by small to medium sized operations to take advantage of this developing  
5 trend can either be achieved within a wholesale market (for example organic certification) or by direct  
6 marketing using on-farm processing or joint ventures for manufacturing and marketing of dairy products.

7 The changing face of agriculture is attracting entrepreneurs who see the value in directly marketing  
8 dairy products, and they are bringing new expertise to the industry and new approaches to dairy farming  
9 that appeal to many consumers.

10 At the same time, some dairies that are struggling to remain in business. The loss of small to mid-  
11 size conventional dairy operations is well documented. An opportunity to capitalize on location  
12 advantages and leverage involvement in their local community by marketing value-added dairy products  
13 may allow vulnerable farm businesses to continue. In many communities, this is seen as also having  
14 associated benefits to the preservation of the economic and social infrastructure of the rural community.

15 Direct marketing of fluid and manufactured dairy products involves new and considerable costs for  
16 a farm-based business. The high capital cost of manufacturing equipment, challenges to establishing a  
17 customer base and, in some circumstance, regulation can inhibit the growth of on farm value-added  
18 enterprises and provide high barriers to innovation and profitability for dairy farms that want to maximize  
19 their location or product by selling direct to the consumers. Adding disproportionate expenses to farms  
20 and food producers that already depend on slim margins will reduce opportunity and create barriers to  
21 entry for producers of all scales. Overextended regulations undermine private and voluntary systems of  
22 training and continuous improvement, and undermine any sense of “shared responsibility” among all

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<sup>34</sup> USDA’s definition of a farm encompasses a large number of different farming operations, and the beginning farmer definition is, likewise, broad. USDA’s current definition of a beginning farm is one operated by a farmer who has operated a farm or ranch for 10 years or less.

<sup>35</sup> Agriculture Secretary Vilsack Launches Showcase on 'Know Your Farmer, Know Your Food' Website Online Resource will Expand National Dialogue About Economic Opportunity for Producers -8/30/2010



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1 food-system players, ultimately harming the public the regulations purport to protect. Establishment and  
2 enforcement of baseline standards, especially in areas of greatest known risk, is an important  
3 responsibility of government. All dairy manufacturing is regulated in some form by municipality, county,  
4 state and/or federal regulations that are continually evolving to meet new areas of risk. Federal, state and  
5 local agencies need to work together in a consistent fashion to tailor enforcement that is appropriate and  
6 effective in light of local and regional realities, reinforcing a multi-stakeholder process of continuous  
7 improvement. The Committee recommends that the Secretary actively support the development of  
8 educational training programs and technical assistance for farms, inspectors, and regulatory personnel to  
9 accommodate and nurture unique, value-added dairy farm operations.

10 *Dairy Management Practices and Production Costs – Environmental Practices*

11 *Recommendation 19:*

12 *PROVIDE INCENTIVE PAYMENTS FOR ENVIRONMENTAL PRACTICES. The Secretary*  
13 *of Agriculture should increase the amount of money available for incentive payments to*  
14 *dairy farmers for environmental practices that address social, economic and environmental*  
15 *benefits to dairy farm communities.*

16 For the dairy industry, sustainability isn't new. Innovation and efficiencies in milk production,  
17 processing, packaging and transportation have all contributed to its ability to do more with less, to be  
18 profitable and to provide wholesome dairy products to feed a growing population. Environmental  
19 practices, from recycling water and manure to crop technologies that improve the soil and prevent  
20 erosion, have all contributed to dairy's dramatic increase in productivity. And, "in an era of dwindling  
21 natural resources and a growing population that cares deeply about the health and environmental impact  
22 of the products they buy, the dairy industry is committed to doing more with less."<sup>36</sup> In order to do more  
23 with less, existing resources will need to be managed more effectively, with new technologies created,  
24 developed and adopted. Society will need to commit more of its resources to this process as well,  
25 leveraging the contributions of dairy.

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<sup>36</sup> Jerry Kozak, CEO NMPF, U. S. Sustainability Commitment Progress Report



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1 Dairy has taken a leadership position in determining its carbon foot print and partnered with USDA  
2 in many environmental areas. Anaerobic digesters can reduce green house gas emissions, as can feed  
3 inputs. Other examples include initiatives around practices like nutrient management, with protection of  
4 both surface and ground water. The industry itself cannot be expected to assume all the burden of the  
5 societal benefits. The dairy industry provides a number of indirect benefits that are hard to quantify; from  
6 jobs to leadership in communities; from environmental impact reduction to improved wildlife habitat;  
7 from the aesthetic value of a working landscape to social values.

8 The Committee encourages the Secretary to recognize the impact of dairy farmers as stewards of  
9 environmentally stable rural land, job creators and economic drivers of rural economies. The Secretary  
10 should increase the amount of Federal environmental funds, especially those funds not traditionally  
11 targeted for dairy operations, which can directly assist dairy farms with environmental challenges. The  
12 Committee recommends that the Secretary give preference to dairy farms in different policy and program  
13 venues to address environmental challenges that directly affect farm profitability and also address the  
14 social and economic effects of dairy farm on the rural community, while providing a nationwide supply of  
15 milk.

16 *Promoting Dairy Farm Development – EQIP and Other Grants*

17 *Recommendation 20:*

18 *CONTINUE THE EQIP AND GRANT PROGRAMS. The EQIP program should be*  
19 *continued, and dairy farmers should be given preference in grant programs for*  
20 *implementation of energy audits, infrastructure development for value-added processing and*  
21 *distribution facilities, construction of facilities to meet food safety regulations and farmland*  
22 *protection, and to allow beginning farmer loans for farm transfers between generations.*

23 With increasing state, county and federal conservation regulation and enforcement, the costs of  
24 meeting these regulations and the time dealing with regulators who lack experience with farm operations  
25 will increase. The Environmental Quality Incentives Program (EQIP) is one program that can assist the  
26 individual dairy farmer in meeting increasing regulation. EQIP was approved in 1996 by amending the  
27 Food Security Act of 1985 (Farm Bill), reauthorized in the Farm Security and Rural Investment Act of  
28 2002 and again reauthorized in the Food, Conservation and Energy Act of 2008 (FCEA or “Farm Bill”).



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1 EQIP offers financial and technical help to assist eligible producers install or implement conservation  
2 practices on eligible agricultural land. The five EQIP national priorities are very applicable to the  
3 environmental challenges that the dairy industry experiences.<sup>37</sup> EQIP offers contracts that provide  
4 financial assistance to help develop conservation plans and implement conservation practices. EQIP may  
5 provide payments up to 75 percent of the estimated incurred costs and loss of income of certain  
6 conservation practices and conservation activity plans.

7 The USDA Rural Development Agency's Rural Energy for America Program Grants/Energy Audit  
8 and Renewable Energy Development Assist (REAP/EA/REDA) provides grant money for energy audits  
9 and renewable energy development to organizations that help agricultural producers and rural small  
10 businesses reduce energy costs and consumption. USDA should continue to harness programs like REAP  
11 to promote the use of manure digesters to create energy generation in rural America.

12 As the number of dairy farms in any one area decrease there is a corresponding decrease in the  
13 economic viability and profitability for service providers. As these service providers disappear, there is  
14 an increased overhead for maintenance, repair and other input service costs, plus the availability of  
15 production advisors. In order to re-establish that infrastructure to meet the changing needs of farmers the  
16 USDA Rural Development Value-Added Producer Grants (VAPG) can be used for both capital and  
17 planning activities and for working capital to market value-added agricultural products and for farm-  
18 based renewable energy. Eligible applicants are independent producers, farmer and rancher cooperatives,  
19 agricultural producer groups, and majority-controlled producer-based business ventures.

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<sup>37</sup> Reductions of nonpoint source pollution, such as nutrients, sediment, pesticides, or excess salinity in impaired watersheds consistent with Total Daily Maximum Loads (TMDLs), where available; the reduction of surface and groundwater contamination; and reduction of contamination from agricultural point sources, such as concentrated animal feeding operations (CAFOs); conservation of ground and surface water resources; reduction of emissions, such as particulate matter, nitrogen oxides (NOX), volatile organic compounds, and ozone precursors and depleters that contribute to air quality impairment violations of National Ambient Air Quality Standards; reduction in soil erosion and sedimentation from unacceptable levels on agricultural land and promotion of at-risk species habitat conservation.



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1 In a previous section, the merits of FSA loan programs have been addressed. These programs can  
2 have a profound affect on helping the development of dairy farming systems, of many types and varieties.

3 The consolidation of dairy processors, distribution, warehousing and retailers has created an  
4 opportunity for entrepreneurs, including dairy farmers, to diversify and bring unique or innovative dairy  
5 products to the market. Programs that provide grant money and technical assistance to assist the  
6 establishment of valued-added dairy processing benefit the individual farmer or group of farmers and also  
7 expand choices for consumers.

8 The Committee recognizes that this recommendation is intended to impact the 2012 Farm Bill and  
9 will be subject to tight budgetary constraints, congressional budget rules, a smaller CBO baseline, budget  
10 reconciliation, and a looming Federal budget deficit. The intent of this recommendation is to provide  
11 ongoing support to dairy operations to face the challenges and demands of dairy farming in the 21<sup>st</sup>  
12 century. The Committee recommends that EQIP and other environmental programs be fully funded in the  
13 2012 Farm Bill. The Secretary should support the funding and implementation of these and other  
14 programs that will provide cost share or full cost grants to enable dairy farmers to increase innovation in  
15 marketing of dairy products; improve dairy farm production methods; enable dairy farmers to make  
16 capital investments in their operations in anticipation of regulatory changes; and provide ongoing support  
17 to dairy farm operations.

18 *Dairy Management Practices and Production Costs – Corn Based Ethanol Subsidies*

19 *Recommendation 21:*

20 *PHASE OUT ETHANOL SUBSIDIES. We support the rapid phase out of the blender's*  
21 *credit and tariff on imported ethanol.*

22 The Volumetric Ethanol Excise Tax Credit (“VEETC”), also known as the “blender’s credit”, is the  
23 primary federal tax incentive to produce ethanol. The tax credit, which was created by the American Jobs  
24 Creation Act of 2004, provides blenders and marketers of fuel with a federal tax credit of 45¢ on each  
25 gallon of ethanol blended with their gasoline. The Energy Independence and Security Act of 2007  
26 mandated nine billion gallons of renewable fuels be used in 2008 and 36 billion gallons of renewable  
27 fuels to be used annually by 2022. Of the total, 21 billion gallons must come from advanced biofuels and  
28 from sources such as cellulose (i.e., corn stalks, wood chips, switchgrass, etc.) and sugarcane. The Act



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1 requires 12.6 billion gallons of conventional ethanol (or about 4.5 billion bushels of corn) be used in 2011  
2 and 15 billion gallons (5.357 billion bushels) by 2015. Ethanol blenders receive a 45¢ per gallon tax  
3 credit on all ethanol blended through 2015 and a 10¢ gallon tax credit on the first 15 million gallons of  
4 ethanol made by companies that produce less than 60 million gallons per year. The tax credit of 54¢ per  
5 gallon is applied to all ethanol blended in the U.S. and a registered blender is the only individual in the  
6 supply chain that is eligible for this credit, which can only be taken once. This credit is now refundable  
7 quarterly, and all funds are paid out of the General Fund of the federal budget.

8 In December 2010 the credit and tariff were renewed for one year by Congress. That extension was  
9 opposed by many environmentalists and by other industries that use corn, including livestock producers.  
10 Among the opponents' arguments was that because there are federal quotas in place for minimum use of  
11 ethanol, the subsidy would not increase the volume sold. The proponents of the credit and tariff disagreed.  
12 Opponents of the credit and subsidy argue that the dramatic increases in the prices of corn and soybean  
13 meal that we are currently experiencing are a direct result of our current ethanol policy, which forces  
14 demand adjustments in the livestock sector rather than in the sector (blended gasoline) that can more  
15 easily adjust.<sup>38</sup> Ethanol mandates, demand subsidies, and import barriers reduce the ability of world feed  
16 markets to cope with unexpected supply disruptions by forcing most of the adjustment to take place in the  
17 livestock industry rather than in the ethanol industry.

18 Although farmers have some ability to adjust their purchases of inputs in response to the margin  
19 squeeze generated by higher feed prices, their response is limited by the implications for production and  
20 the health of their herds. Moreover, although there are a variety of feedstuffs available to farmers, there  
21 are a finite amount of feed inputs possible in a balanced ration. Moreover, many of these alternative feeds  
22 have prices correlated with the basic feed inputs of corn or soybeans.

23 The renewal of the blender's credit and tariff for ethanol together with the renewable fuels mandate  
24 follows a policy that created a new use for one quarter of the corn crop. Corn production has increased  
25 dramatically in recent years, but, by and large, surge in demand has absorbed all the increase and market

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<sup>38</sup> Impact on Ethanol, Corn, and Livestock from Imminent U.S. Ethanol Policy Decisions by Bruce A. Babcock, Center for Agricultural and Rural Development or Iowa State University.



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1 prices still rise. This increased use of corn and the subsequent increase in price for all feed inputs has an  
2 undeniable effect on dairy profitability. A continuation of the decrease in the milk price-feed cost margin  
3 for dairy farmers, despite higher milk prices, will result in a major devaluation of all dairy-related assets  
4 including cows, equipment and facilities, aggravating the precarious economic situation in which all dairy  
5 farmers found themselves in 2009 and 2010.

6 High feed costs have contributed to the economic volatility and unprofitability that has beset dairy  
7 farmers since 2008 and over the long term, higher corn prices will have to be reflected in higher consumer  
8 prices for meat and dairy products. Increased feed costs will affect the ability of U.S. dairy farmers to  
9 compete on the world market, which has many low cost production competitors.

10 While the committee recognizes the benefits of ethanol production to corn growers and their rural  
11 communities, it also recognizes its negative impact on dairy and livestock producers and their  
12 communities. We recommend that the Secretary support phasing out the blender's credit and tariff on  
13 imported ethanol and allow market forces to determine the desirability of using corn for ethanol and/or  
14 imported ethanol.<sup>39</sup>

15 *Dairy Herd Health Programs*

16 *Recommendation 22:*

17 *DAIRY HERD HEALTH: Adequately fund and implement programs to rapidly eradicate TB*  
18 *and Johnes from the U.S. dairy herd.*

19 Programs to promote the eradication and control of Bovine tuberculosis and Johne's disease need  
20 to be adequately funded, regularly updated and supported by ongoing research. Education and outreach  
21 with continued producer involvement is vital to controlling both these diseases, which directly affect the  
22 health of dairy cows and the profitability of dairy farmers. Adequately funded testing and long-term  
23 research is needed to assist in disease control and to highlight areas of opportunity in the programs to

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<sup>39</sup> Keep in mind that this recommendation does not address the Renewable Fuel Standard requirement and its significant impact on requiring the use of ethanol blends in gasoline. As long as there is an effective RFS, the use of corn for ethanol will not be purely market driven.



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1 regulate, monitor and control these diseases. Investment in programs that can monitor and eradicate  
2 bovine TB and Johne's disease will create a healthier livestock industry and more profitable dairy farms.

3 Bovine Tuberculosis<sup>40</sup>

4 Since 1917 the prevalence rate of tuberculosis in U.S. cattle herds dropped from 5 percent to less  
5 than 0.001 percent.<sup>41</sup> In developed countries, eradication programs have reduced or eliminated  
6 tuberculosis in cattle, and human disease is now rare; however, reservoirs in wildlife can make complete  
7 eradication difficult.

8 In 1917, under pressure from medical, veterinary, and animal industry lobbies, Congress passed a  
9 \$1 million appropriations bill initiating the State-Federal Cooperative Bovine Tuberculosis Eradication  
10 Program which is administrated by the U.S. Department of Agriculture's (USDA) Animal and Plant  
11 Health Inspection Service (APHIS), State animal health agencies, and U.S. livestock producers. These  
12 Uniform Methods and Rules (UMR) are the minimum standards adopted and approved by the Deputy  
13 Administrator, Veterinary Services (VS), Animal and Plant Health Inspection Service (APHIS), on

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<sup>40</sup> Bovine TB is a chronic bacterial disease of cattle that occasionally affects other species of mammals. This disease is a significant zoonosis that can spread to humans, typically by the inhalation of aerosols or the ingestion of unpasteurized milk.

In developed countries, eradication programs have reduced or eliminated tuberculosis in cattle, and human disease is now rare; however, reservoirs in wildlife can make complete eradication difficult. Tuberculosis is usually a chronic debilitating disease in cattle, but it can occasionally be acute and rapidly progressive.

Bovine tuberculosis can be controlled by test-and-slaughter or test-and-segregation methods. Affected herds are re-tested periodically to eliminate cattle that may shed the organism; the tuberculin test is generally used. Infected herds are usually quarantined, and animals that have been in contact with reactors are traced. Only test-and-slaughter techniques are guaranteed to eradicate tuberculosis from domesticated animals. Once eradication is nearly complete, slaughter surveillance, with tracing of infected animals, may be a more efficient use of resources. Sanitation and disinfection may reduce the spread of the agent within the herd. Once the most prevalent infectious disease of cattle and swine in the United States, bovine TB caused more losses among U.S. farm animals in the early part of this century than all other infectious diseases combined.

<sup>41</sup> USDA APHIS: A New Approach for Managing Bovine Tuberculosis: Veterinary Services' Proposed Action Plan



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1 January 21, 1999. They were established for the maintenance of tuberculosis-free accredited herds of  
2 cattle, captive cervids, bison and goats, and the maintenance of State status in the U.S. Department of  
3 Agriculture's tuberculosis eradication program. These minimum standards do not preclude the adoption  
4 of more stringent standards by any state, status zone within a State, or region containing multiple states.

5 The TB eradication program has successfully reduced the incidence of the disease in U.S. cattle,  
6 but there continues to be a low incidence of TB as evidenced by newly identified infected herds over the  
7 past several years. In order to have a more concerted effort to achieve the end goal of complete  
8 eradication of bovine TB from the U.S. cattle herd, with no recursions, it has become evident that  
9 USDA's program needs to be updated, and the antiquated testing methodologies and surveillance tools  
10 improved. The current APHIS program was designed around the absence of TB and the Uniform Methods  
11 and Rules (UMR) are outdated using invalid assumptions. The USDA issued a concept paper in  
12 December 2009, *A New Approach for Managing Bovine Tuberculosis: Veterinary Services' Proposed*  
13 *Action Plan*, to improve the control and eradication of TB. The National Milk Producers Federation  
14 provided comments<sup>42</sup> on that paper on behalf of dairy farmers and they can be summarized under the  
15 following points:

16 • **Mitigate Disease Introduction:** Efforts to fully eradicate TB in the US are compounded by  
17 several known or suspected routes of exposure which require further regulatory enhancements to  
18 minimize these risks including Mexican imported feeder cattle, Mexican imported event cattle, Canadian  
19 imported cattle, wildlife reservoirs and employee transmission.

20 • **Enhance Diagnostics and Surveillance & Traceability:** Diagnostic, surveillance and  
21 traceability capabilities have not kept pace with the changing needs of the TB eradication program.  
22 Current diagnostics are no longer adequate for the low-level incidence of TB the U.S. now has. The  
23 success of both the TB and brucellosis eradication programs has led to a decline in the use of permanent  
24 identification for breeding cattle.

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<sup>42</sup> <http://www.nmpf.org/files/file/NMPF-TB-comments-12-04-09.pdf>



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1           • **Manage TB Affected Animals & Herds:** Enhancement of the management tools available for  
2 producers who have a TB-infected animal identified to their premises is required to advance the TB  
3 eradication program.

4           • **Modernize Regulatory Framework:** An effective TB eradication program requires modernizing  
5 the regulatory framework.

6 Johne's Disease<sup>43</sup>

7           The National Animal Health Monitoring Systems (NAHMS) study, Dairy 2007<sup>44</sup>, showed that 68.1  
8 percent of US dairy operations are infected with the bacterium (MAP) which causes Johne's disease (JD).  
9 Dairy 2007 also suggests that at least one out of every four US dairy operations may have a relatively

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<sup>43</sup> Johne's disease is primarily a health problem for ruminant animals and occurs most frequently in cattle herds. The bacterium *Mycobacterium avium paratuberculosis* (MAP) causes Johne's disease. It represents a significant production problem for dairy farmers. It is particularly common in dairy cattle not because they are more susceptible to it, but because they are more frequently exposed to the MAP organism. There are only two clinical signs of Johne's disease: rapid weight loss and diarrhea. Because the signs of Johne's disease are similar to those for several other diseases, laboratory tests are needed to confirm a diagnosis. If a case of Johne's disease occurs, it is very likely that other infected animals (who may still appear healthy) are in the herd. This infection is contagious, which means it can spread from one animal to another.

Currently there is some public health concern about Johne's disease. There is a small amount of somewhat contradictory evidence that links the causal organism of Johne's disease to a disease of humans called Crohn's disease. This evidence suggests that *Mycobacterium paratuberculosis* shed in the milk from dairy cattle may cause Crohn's disease in humans. Some researchers believe MAP is the cause of Crohn's disease for at least a subset of patients. The majority of gastroenterologists, however, do not; they believe that MAP, if found in this subset of patients, is simply a by-stander amongst the many other organisms that are found in a malfunctioning gastrointestinal tract. No connection has been shown between contact with animals with Johne's disease, dairy product consumption and Crohn's disease. This aspect of MAP is a complex and controversial area of scientific investigation. Pasteurization, a commonly required process in any approved dairy foods processing facility, kills the bacteria. With pasteurization, it does not represent a food safety problem for humans.

<sup>44</sup> NAHMS Study: Johne's Disease on U.S. Dairies, 1991-2007



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1 high percentage of Johne's-infected cows in their herds. Lost productivity due to Johne's disease is  
2 estimated to cost the US dairy industry \$200 million to \$250 million annually.

3 Johne's disease is a difficult problem for livestock owners because clinical symptoms of the disease  
4 may not occur until two to five years after infection has taken place. After infection, but before clinical  
5 symptoms are apparent, the infected animal is likely to be contagious. There is currently no treatment for  
6 Johne's disease. General recommendations are to cull infected animals. There is no preventive vaccine  
7 available to combat infection. The vaccine that is currently available simply minimizes clinical signs and  
8 shedding of the organism. It does not prevent new infections.

9 The Uniform Program Standards for the Voluntary Bovine Johne's Disease Control Program  
10 (VBJDCP) has been developed by the National Johne's Disease Working Group, the Johne's disease  
11 committee of the United States Animal Health Association, State Veterinarians, industry representatives,  
12 and the USDA's Animal and Plant Health Inspection Service (APHIS) Veterinary Services (VS) to  
13 provide national standards for the control of Johne's disease. This is a voluntary program and the only  
14 Federal regulation related to JD is that cattle, sheep, goats, and other domestic animals that are positive to  
15 an official test for JD may generally be moved across state lines only to a recognized slaughtering  
16 establishment or to an approved livestock facility for sale to such an establishment.<sup>45</sup> The VBJDCP  
17 consists of three basic elements: 1) Education—to inform producers about the cost of JD and to provide  
18 information about management strategies to prevent, control, and eliminate the disease; 2) Management—  
19 to work with producers to establish good management strategies on their farms; and 3) Herd testing and  
20 classification—to demonstrate the level of risk of JD on the farm.

21 The committee agrees that programs to promote the eradication and control of Johne's disease and  
22 Bovine tuberculosis need to be adequately funded, regularly updated and supported by ongoing research.  
23 Education and outreach, with ongoing producer involvement, is vital to controlling both these diseases,  
24 which directly affect the health of dairy cows and the profitability of dairy farmers. Investment in  
25 programs that can monitor and eradicate bovine TB and Johne's disease will create a healthier livestock  
26 industry, more profitable dairy farms and a cleaner environment.

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<sup>45</sup> Title 9, *Code of Federal Regulations* (9 CFR), part 80



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1 Dairy Labor

2 *Recommendation 23:*

3 *DAIRY LABOR: The Secretary of Agriculture should use his influence with other agencies*  
4 *and Congress to provide a legal means for dairy farms to employ year-around long-term*  
5 *immigrant labor. Provide assurance that existing farm laborers have the opportunity to*  
6 *obtain permanent resident status.*

7 Immigrant labor plays a very important role in contributing to the success of America's dairy  
8 industry; a large percentage of the hired workers on dairy farms are immigrants. This is true for a great  
9 number of dairy farmers across this country, large and small. Dairy farming, particularly the care and  
10 milking of cows, is labor intensive. As production methods have become more sophisticated, sourcing  
11 qualified and committed farm labor has become an increasing challenge.

12 A 2009 report by researchers at Texas A&M provide considerable insight into the nature of hired  
13 labor on dairy farms.<sup>46</sup> The following discussion relies heavily on this report for descriptive information.

14 A growing source of farm labor has come from immigrants, whether under government plans or  
15 from those immigrants who are otherwise able to work legally in the US.<sup>47</sup> Despite compliance with Form  
16 I-9 protocol, the employment of many of these employees remains under a cloud. Uncertainty about  
17 immigration reform has been an issue with many dairies that have previously used qualified and  
18 motivated immigrant labor.<sup>48</sup>

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<sup>46</sup> "Dairy Farms employed an estimated 138,000 full-time equivalent workers in 2008: 41%, or 57,000 of those were estimated of foreign origin, primarily from Mexico" The Economic Impacts of Immigration on US Dairy Farms, June 2009, National Milk Producers Federation (NMPF) and Texas A&M.

<sup>47</sup> Farm Labor Shortages and Immigration Policy - Linda Levine, Specialist in Labor Economics, Congressional Research Office, November 9, 2009

<sup>48</sup> "Vermont dairy farms count on illegal immigrants" By Wilson Ring, AP Staff Writer, May 13, 2009, <http://www.immigrationworksusa.org/uploaded/file/051309Vermontdairyfarmscountonillegalimmigrants.pdf>



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1 In the Texas A&M study, dairies reported that the average number of hired workers per dairy farm rose  
2 from 5.0 in 2006 to 5.6 in 2008, with most of the growth in full-time employees. In 2008, four workers  
3 per farm were reported to be full-time. Approximately 47 percent of all farms surveyed reported the use  
4 of immigrant labor.

5 Respondents to the 2008 Texas A&M AgriLife Research survey reported that they paid their  
6 workers \$506 in average weekly wages, while most also reported providing at least one non-wage benefit  
7 to employees, such as paid vacation, housing, and/or insurance. Those non-wage benefits brought average  
8 dairy workers salaries in 2008 to \$31,521, significantly higher than salaries in the landscaping, ranching,  
9 and fast food sectors, which employ similar proportions of immigrant workers. Texas AgriLife Research  
10 estimated that if federal labor and immigrant policies were to result in the loss of just half of the 57,000  
11 foreign-born dairy workers, an additional 66,000 workers would also be lost, due to the closure of some  
12 dairy farms, and the resulting multiplier effect of fewer jobs in grain and fertilizer production and sales,  
13 veterinary services, milk hauling, and related agricultural service jobs. This would produce an economic  
14 loss of \$11 billion.

15 There are many issues and tensions linked to immigration policy. The committee does not seek to  
16 address all those issues. Rather, in the midst of major immigration reform, the special relationship of  
17 dairy and immigrant labor should be considered. Specifically, dairy producers need a program that  
18 provides dairy farm employment opportunities for foreign guest workers in sufficient quantities for year  
19 round employment and eliminates questions regarding the legal status of these employees or the  
20 employer. Current guest worker programs, as well as provisions for seasonal agricultural labor, do not  
21 work for dairy operations. Dairy farming is a year-round enterprise, with workers' primary roles in  
22 working with cows and calves. Consistent and expert animal care only comes from hands-on experience  
23 over time, a time period longer than just a few months.

24 In order to preserve a continued supply of fresh milk in the United States within the current  
25 economic and demographic conditions, the issues surrounding immigrant labor for dairy farmers needs to  
26 be resolved. Large numbers of dairy farms in most, if not every, state are dependent on immigrant labor.  
27 Enforcement only, without a workable program for agriculture, will severely impact the dairy industry.  
28 The Committee shares the concerns of all Americans about protecting the United States, and it is not  
29 willing to sacrifice security. However, failing to provide for orderly flows of greatly needed workers will



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1 create enormous economic consequences for our industry and do very little to enhance our border  
2 protection. A dairy worker visa program (or modification of the current H-2A visa program) that allows  
3 for terms up to three years for dairy workers with the ability to renew those visas is needed. The program  
4 should also be respectful of those who take the opportunity to work in this country and allow for the  
5 opportunity for permanent residency or citizenship if desired.

6 The DIAC committee recognizes that the Secretary does not have any authority over immigration,  
7 but in his role as a member of the Cabinet and his relations with Congress he should urge those who do  
8 have jurisdiction to meet this need of the dairy industry.

9 **Summary and Conclusions**

10 Dairy farm operations have an impact on their rural communities far beyond providing high  
11 quality, nutritious products. Dairy farms are job creators and tend to be a strong investor in their local  
12 community both with vendor purchases and long-term social commitment. The multiplier effect on the  
13 economy, reduction of the tax burden on local economies, the maintenance of open space and many other  
14 positive secondary effects of dairy farming are important contributions made by a vibrant and healthy  
15 dairy sector. The Secretary has frequently stated that we must be aware of the needs of all dairy farmers,  
16 of all structures and business models and in all locations. Dairy farmers themselves would be the first to  
17 also add that a healthy and vibrant dairy foods processing and marketing sector is essential to their own  
18 prosperity and also add a variety of economic and social benefits where they exist.

19 Many studies have shown the impact of dairy farms on local economies. One common theme in all  
20 of them is the multiplier effect of the dairy industry.<sup>49</sup> Dairy farming is a capital-intensive industry with  
21 many direct, indirect and induced effects. Dairy farms and milk processors directly affect the economy  
22 by employing farmers, milkers, truck drivers and workers at processing plants. The dairy industry also  
23 indirectly affects local economies through the purchases of inputs and services required to keep the

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<sup>49</sup> The Community Value of a Dairy Farm: September 8, 2009 N. Alan Bair, Director of Dairy Industry Relations, The Pennsylvania State University



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1 industry operating. By creating and maintaining employment, the spending of salaries and wages by  
2 workers employed in the dairy industry helps support the economy.

3 Beyond their direct economic effects, dairy farms have other community benefits. They are often  
4 regarded as stewards to the countryside who provide conservation and land preservation benefits for all.  
5 The disappearance of working farms and the subsequent dilapidation of the land and buildings have a  
6 significant negative effect on the rural economy and community and may add costs to the State or local  
7 government for the maintenance of land. Beyond its historical role in land stewardship, many new  
8 methods are becoming technically and economically available to provide new environmental benefits,  
9 including the possibility of harnessing methane from animal wastes to generate energy as well as manage  
10 environmental risks related to manure handling.

11 It is also increasingly imperative to world food security that the US protects and preserves its  
12 working farmland. In return, farms will continue to benefit from producing products for the US and  
13 international marketplaces. Farms of all sizes and business models are welcome and have a place in  
14 ensuring a strong, diverse dairy industry.

15 A myriad of complex issues face dairy farmers as they prepare their businesses to compete in a  
16 growing global economy. Relatively new business challenges such as increased feed prices, more volatile  
17 milk prices, changing consumer diets, a global economy, and new production and processing technologies  
18 have challenged the industry to develop new, adaptive strategies.

19 The Committee presents analyses of many of these issues and highlights their importance. It offers  
20 a number of recommendations for how USDA, and others, can assist in that development and provide  
21 tools for dairy farmers to help their farm businesses survive and thrive in the coming years. We encourage  
22 USDA and the industry to continue its dialogue and implement those strategies that provide a long-term,  
23 fundamentally sound dairy business climate.



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1 **Appendix A - Farm Financial Performance Measures**

2 In January 1989 a “Farm Financial Standards Task Force” was created with the mandate to develop  
3 and publish standardized Financial Guidelines for Agricultural Producers. The Farm Financial Standards  
4 Task Force was incorporated in March 1993, as a “Nebraska non-profit corporation” and on November  
5 12, 1994, the corporate name was changed to Farm Financial Standards Council to reflect more  
6 appropriately a permanent organization.

7 The FFSC accepts as one of its core missions to: "present standardized definitions and methods for  
8 calculating financial measures which may be used in the measurement of financial position and financial  
9 performance of agricultural producers." Currently, 21 measures are endorsed by the FFSC.

10 Farm Financial Standards Council

11 <http://www.ffsc.org/index.htm>

12 Liquidity

13 **Current Ratio:** Calculated as (total current farm assets) / (total current farm liabilities). This measure of  
14 liquidity reflects the extent to which current farm assets, if sold tomorrow, would pay off current farm  
15 liabilities.

16 **Working Capital:** Calculated as (total current farm assets) – (total current farm liabilities). This measure  
17 represents the short-term operating capital available from within the business.

18 **Working Capital to Gross Income:** Measures operating capital available against the size of the  
19 business.

20 Solvency

21 **Debt-to-Asset Ratio:** Calculated as (total farm liabilities) / (total farm assets). This represents the bank’s  
22 share of your business. A higher ratio is an indicator of greater financial risk and lower borrowing  
23 capacity.

24 **Equity-to-Asset Ratio:** Calculated as (farm net worth) / total farm assets). This measure of solvency  
25 compares farm equity to total farm assets.

26 **Debt-to-Equity Ratio:** Calculated as (total farm liabilities) / farm net worth. This measure compares the  
27 bank’s ownership to your ownership of the business.

28 Profitability

29 **Rate of Return on Assets:** Calculated as [(net farm income) + (farm interest) – (value of operator labor  
30 and management)] / (average value of farm assets). This measure represents the average “interest”  
31 rate being earned on all investments in the business (your investment and that of your creditors).

32 **Rate of Return on Equity:** Calculated as [(net farm income) – (value of operator labor and  
33 management)] / (average farm net worth). This measure represents the “interest” rate being earned by



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1 your investment in the farm. This return can be compared to the return on your investments if equity  
2 were invested somewhere else, outside the business.

3 **Operating Profit Margin:** Calculated as  $(\text{return on farm assets}) / (\text{value of farm production})$ , where  
4 return on farm assets equals  $(\text{net farm income from operation}) + (\text{farm interest expense}) - (\text{opportunity}$   
5  $\text{return to labor and management})$ . This measure of profitability shows the operating efficiency of the  
6 business. Low expenses relative to the value of farm production result in a healthy operating profit  
7 margin.

8 **Net Farm Income:** Calculated as  $(\text{gross cash farm revenue}) - (\text{total cash farm expense}) + (\text{inventory}$   
9  $\text{changes}) + (\text{depreciation and other capital adjustments, including gains/losses from the sale of capital}$   
10  $\text{assets})$ . This measure represents profitability or the farm's return to labor, management and equity.

11 **EBITDA:** Earnings before interest, taxes, depreciation, and amortization—measurement shows the  
12 earnings of the business that are available for debt repayment.

### 13 Repayment Capacity

14 **Term Debt Coverage Ratio:** Calculated as  $[(\text{net farm operating income}) + (\text{net nonfarm income}) +$   
15  $(\text{depreciation}) + (\text{scheduled interest on term debt and capital leases}) - (\text{family living and taxes paid})] /$   
16  $(\text{scheduled principal and interest payments on term debt and capital leases})$ . This measure of  
17 repayment capacity tells whether the business produced enough cash to cover all intermediate and  
18 long-term debt payments.

19 **Capital Replacement Margin:** Calculated as the value of  $(\text{net farm income}) + (\text{net nonfarm income}) +$   
20  $(\text{depreciation} - (\text{family living expenses, taxes paid, scheduled payments on term debt}))$ . This measure  
21 describes the amount of money left over after all operating expenses, taxes, family living cost, and  
22 scheduled debt payments have been made.

23 **Capital Debt Repayment Capacity:** Measurement of all sources of income that could be used to pay  
24 debt (both farm and non-farm sources of income.)

25 **Replacement Margin:** Enables borrowers and lenders to evaluate the ability of the operation to generate  
26 funds necessary to repay debts with maturity dates longer than one year and to replace assets.

27 **Replacement Margin Coverage Ratio:** To show if enough income was generated to cover term debt  
28 payments and the cash contribution for new equipment.

### 29 Financial Efficiency

30 **Asset Turnover Rate:** Calculated as  $(\text{gross farm revenue}) / (\text{average farm assets})$ . This measures the  
31 efficiency of using capital. A high level of production in proportion to the level of capital investment  
32 yields a high (or efficient) asset turnover rate.

33 **Operating Expense Ratio:** Calculated as the value of  $[(\text{total farm operating expenses}) - (\text{depreciation}) -$   
34  $(\text{farm interest})] / (\text{gross farm revenue})$ . This measure reflects the proportion of farm revenues used to  
35 pay operating expenses, not including principal or interest.

36 **Interest Expense Ratio:** Calculated as  $(\text{farm interest}) / (\text{gross farm revenue})$ . This measure of financial  
37 efficiency shows how much of gross farm revenue is used to pay for borrowed capital.

38 **Depreciation Expense Ratio:** Calculated as  $(\text{depreciation and other capital adjustments}) / (\text{gross farm}$   
39  $\text{revenue})$ . This measure indicates what proportion of farm revenue is needed to maintain the capital  
40 used by your business.

41 **Net Farm Income from Operations Ratio:** Calculated as  $(\text{net farm income from operations}) / (\text{gross}$   
42  $\text{farm revenue})$ . This measure of financial efficiency compares profit to gross farm revenue. It shows



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- 1 how much is left after all farm expenses, except for the return to unpaid operator and family labor,
- 2 management and capital, are paid.

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**1 Appendix B – Summary**

**Summary of Dairy Product Price Support Program (DPPSP)**

**Objectives:**

Price Support - prevent farm price of milk from falling below a target level by purchasing dairy commodities specified by Congress at specified minimum prices. The underlying objective is variously described as to create greater price stability or to enhance farm prices and income.  
Minimize impact on commercial sales when disposing of government stocks

**Methods:**

USDA/CCC offers to purchase butter, cheese, and nonfat dry milk, according to established specifications, at the announced purchase prices.  
If this price is appealing to manufacturers of those commodities, compared to prevailing or expected market prices, the manufacturer initiates a “response” to USDA’s “invitation.”  
CCC takes ownership of the product and is expected to dispose of the product in a manner that recognizes its value as a food product but which does not undermine the commercial market for similar products. This may include domestic and international food assistance, use in government programs and facilities, use in animal feeds, and the like.  
If a product is offered for sale in commercial channels, its price must equal or exceed the established Sellback Price. Sellback Prices are currently 110% of purchase prices.

**Legal Authority:**

Agricultural Act of 1949 (as amended)

**Administering Agency:**

U.S. Department of Agriculture - Farm Services Agency  
Farm Programs - Price Support Division  
Commodity Operations - Commodity Credit Corporation



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Summary of the Milk Income Loss Contract (MILC)
<p><b>Objectives:</b> Income Support - augment dairy farmer income when milk prices are low</p>
<p><b>Methods:</b> Provide a countercyclical payment to qualified dairy farmers when the Class I price announced for the Boston city zone of the Northeast Federal Milk Marketing Order falls below a legislatively specified value. In addition to setting the benchmark or target price, the law also specifies a percentage of the difference between the target price and the announced price. The payment rate is based on that percentage. Total payments are limited to a specified amount of milk marketings (pounds of milk sold) per farm. In each marketing year, qualified dairy farmers must elect the month in which they are first eligible to begin receiving a monthly MILC supplement. Payments are made in each consecutive month in which a payment is due until the annual limit on marketings is reached.</p>
<p><b>Legal Authority:</b> Food, Conservation and Energy Act of 2008 (FCEA). The MILC was first authorized under the Farm Security Act of 2002 (FSA). But, its legislative origin traces to emergency market transition assistance authorized under the Agriculture, Rural Development, Food and Drug Administration, and Related Agencies Appropriations Act, 2000 (H.R.1906).</p>
<p><b>Administering Agency:</b> U.S. Department of Agriculture - Farm Services Agency Farm Programs - Price Support Division</p>

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**Summary of Federal Milk Marketing Orders (FMMO)**

**Objectives:**

- Orderly marketing (not specifically defined)
- Adequate supplies of milk for fluid purposes

**Methods:**

- Classification of producer milk according to the product in which it is used and minimum pricing of milk according to class
- Pooling the values paid by processors for each class of milk to return a common “pool” price to all producers, regardless of the actual destination of their milk
- Auditing to ensure and enforce compliance by regulated handlers

**Legal Authority:**

- Agricultural Marketing Agreement Act of 1937 (as amended)

**Administering Agency:**

- U.S. Department of Agriculture - Agricultural Marketing Service - Dairy Programs

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Summary of the Dairy Export Incentive Program (DEIP)

Objectives:

- Increase sales of US dairy products in foreign markets, particularly to offset export subsidies from other countries
- Encourage dairy product marketers to export

Methods:

- Provide cash subsidies to dairy product exporters by supplementing privately negotiated export prices.

Legal Authority:

- Created under the Dairy Production Stabilization Act of 1983 and initiated in May 1985. Reauthorized under the Agriculture, Conservation, and Trade Act of 1990, the Uruguay Round Agreements Act of 1995, and the Federal Agriculture Improvement and Reform Act of 1996.

Administering Agency:

- U.S. Department of Agriculture - Foreign Agricultural Service

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