From: Lauren Becker [mailto:lbecker@dtbassociates.com]
Sent: Wednesday, December 30, 2009 3:46 PM
To: ATR-Agricultural Workshops
Cc: KEwing@steptoe.com; jkozak@nmpf.org; Kevin Brosch; Tom Balmer; Jim Tillison
Subject: NMPF Workshop Comments

Dear Sir or Madam:

Attached please find a cover letter and comments on the Workshops to Explore Competition and Regulatory Issues in the Agriculture Industry from the National Milk Producers Federation. Two hard copies will follow by mail.

Thank you,
Lauren Becker

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December 30, 2009

Dear Attorney Holder and Secretary Vilsack:

Enclosed please find comments on the Workshops to Explore Competition and Regulatory Issues in the Agriculture Industry from the National Milk Producers Federation.

Sincerely,

Kevin J. Brosch, Esq.
Counsel to National Milk Producers Federation

Before the U.S. Departments of Justice and Agriculture

In the matter of

Workshops to Explore Competition and Regulatory Issues in the Agricultural Industry

Comments of the National Milk Producers Federation

Introduction

The National Milk Producers Federation (NMPF) hereby provides its comments in anticipation of the workshops to be held jointly by the U.S. Departments of Justice and Agriculture in 2010 to explore competition and regulatory issues in the agricultural industry. Founded in 1916, NMPF is a national association representing the interests of approximately 40,000 of America's dairy farmers through their participation in thirty local, regional or national dairy cooperatives. These 40,000 dairy farmers produce more than sixty percent of America's milk. NMPF serves as the voice for these dairy producers on national policy issues.

NMPF requests the opportunity to participate in the workshop on the Dairy Industry that will be held on June 7, 2010 in Madison, Wisconsin. NMPF believes that any discussion of competition and regulatory issues affecting the dairy industry must take into account, first and foremost, the interests and concerns of dairy farmers themselves. NMPF requests that its President, Mr. Jerry Kozak, be

permitted to participate and to present the views of the association and its membership.

Background –Structure of the Dairy Producer Sector

Dairy production continues to represent one of the best opportunities for farms of all sizes throughout the United States, but especially for the small and medium-sized family farm. Although the number of dairy farms has decreased substantially over the past twenty years, there remain approximately 57,000 licensed dairy farms in the United States, and there are dairy producers in every State of the Union.

Dairy farming, like other sectors of agricultural production, has been under constant pressure towards consolidation because of the dynamics of the modern economy. Just twenty years ago, there were approximately 150,000 dairy farms in the United States; today there are fewer than half that many. Nonetheless, dairy farming, unlike some other areas of animal agriculture – *e.g.*, poultry or egg production – remains a business in which the small and medium independent farm can participate. Despite the significant reduction in the number of dairy farms over the past two decades, the average dairy herd in the United States is still quite moderate -- approximately 138 cows. Dairy farms can, of course, vary greatly in size, and the size of dairy farms is often a reflection of the region of the country. Farms in the older and more traditional dairy production areas in the Northeast and Midwest – *e.g.*, Vermont, New York, Pennsylvania, Michigan, Wisconsin and Minnesota – tend to be smaller than dairy farms in western States where dairy

production has emerged over the past half century – *e.g.*, California, Arizona, Idaho and New Mexico.

Both U.S. domestic demand for dairy products and the size of the U.S. dairy herd have remained fairly constant over recent years. The U.S. domestic market for dairy products is very mature and there has been only small annual growth in overall demand. However, the U.S. dairy production sector is highly innovative, and as such, increases in productivity (*e.g.*, output per cow) have generally outpaced increases in demand. Over recent years, productivity has grown about two percent per annum, while domestic demand for dairy products has grown on average about one percent. The size of the national herd has been fairly stable, between 9.1 and 9.3 million cows. Increases in productivity, as well as other economic factors, have led to increased exports of U.S. dairy products. By 2008, the United States exported approximately eleven percent of its dairy production; however, when the worldwide recession hit in 2009, U.S. dairy exports shrunk to only five percent of production, This collapse of export markets for our dairy products has been the principal cause of extreme economic distress that has been felt across the country in the dairy production sector during the past year as volumes formerly exported remained in the domestic market, driving down average prices.

The Role and Importance of Dairy Cooperatives

The majority of dairy farmers in the United States – approximately 70% – are members of dairy cooperatives formed and operated in a manner consistent with the Capper-Volstead Act. USDA reported in a recently published study that there

were 155 dairy cooperatives operating in this country in 2007, and cooperatives were present in all regions of the United States.[1] Cooperatives accounted for 82.6% of all milk marketed in the United States.[2]

Of those 155 cooperatives, 45 had processing or manufacturing plants and another twelve had milk receiving facilities; 98 were very small marketing cooperatives that had no processing, manufacturing or receiving facilities.[3]

The majority of cooperatives with manufacturing or processing facilities are members of NMPF. Although several NMPF member cooperatives are now national in scope and membership, the majority of NMPF member cooperatives and of all dairy cooperatives are small or regional in scope and composition. For example, NMPF members include cooperatives such as St. Albans Cooperative Creamery in Vermont, Upstate Niagara Cooperative, Inc. in New York, Foremost Farms USA in the Upper Midwest, and Tillamook County Creamery Association in Oregon. A list of dairy cooperatives currently operating in the United States is attached hereto as Exhibit 1.

The cooperative system has been the hallmark of U.S. dairy production since the middle of the 19th Century. As USDA's succinct history of dairy cooperatives

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[1] K. Charles Ling, USDA Rural Development, Marketing Operations of Dairy Cooperatives, 2007, Research Report 218 (July 2009) (hereinafter referred to as "Ling Study"), available at http://www.rurdev.usda.gov/rbs/pub/Rd218.pdf. In June 2009, USDA reported online that its 2008 survey found 147 cooperatives. *See* USDA Rural Development Service, Cooperative Programs National Data, Table 1 (June 2009), available at http://www.rurdev.usda.gov/rbs/coops/table08.xls.

[2] Ling Study, p. 4.

[3] *Id.*, at pp. 1 & 3.

outlines, cooperatives arose and developed in response to fundamental economic realities of dairy production, including the rise and dramatic increase of urbanization, the development of rail and highway freight transportation, the imbalance between thousands of dairy farmers and the very small numbers of middle-man dealers, and the need for dairy farmers to work together to solve a problem unique to the dairy sector – "balancing" seasonally varying supply with unrelated changes in demand.[4] These economic realities continue today.

While cooperatives perform many functions for their farmer members, one of the most important is the function of "balancing" – *i.e.*, collecting excess raw milk and manufacturing storable products such as cheese, butter or milk powder during periods of flush production when the market will not absorb all of the available fluid milk.[5] As the USDA history notes:

> Milk is unique among farm commodities. It is highly perishable, produced and "harvested" on a daily basis, and moved from farm to market every other day, if not every day. The volume of milk produced varies seasonally and daily for biological reasons. This variation is not coordinated with changes in demand, which also vary from day to day and from season to season. The task of balancing, or coordinating, the amount of milk supplied to the volume of milk demanding, is thus problematic.[6]

Because dairy production goes through high and low cycles during the year, production will at times exceed demand and it is crucial to the economic health of

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[4] USDA Rural Development, Cooperatives in the Dairy Industry, Cooperative Information Report 1, Section 16, pp. 4-8 (rev. ed. Sept. 2005), available at http://www.rurdev.usda.gov/rbs/pub/cir116.pdf.

[5] Cooperatives not owning manufacturing facilities assist in the balancing function by assembling and facilitating the movement of excess milk to such facilities.

[6] *Id.* at p. 3.

the industry that, during flush periods, excess fluid milk be manufactured into these storable products. "Balancing" is thus essential for the economic health of all dairy farmers. Yet proprietary dairy manufacturers, focused on processing and marketing dairy products, have historically been reluctant to purchase more raw milk than immediately needed for their own purposes. [7] By taking on the "balancing" function, cooperatives serve an essential role in advancing the economic health of dairy farmers. And it is important to note that, by converting excess raw milk to a storable product, this balancing function benefits not only a cooperative's own dairy producer members, but also non-member dairy farmers operating in the same markets.

A second critical benefit of the cooperative system is that it enables a large number of dairy producers to band together to market their production jointly. This collective marketing permits not only the many small and moderate sized farmers, but also the very largest dairy producers, the opportunity to remain in business and to compete successfully in an ever more concentrated economic environment. These joint marketing activities include a wide range of often capital-intensive and costly activities, including collecting raw milk, testing of nutrient components and other requirements, transportation to and from manufacturing facilities, marketing to and negotiating with purchasers and resellers, and, by some cooperatives, manufacturing and distribution of consumer products. The vast majority of individual dairy farmers could not afford the capital investment required to process

[7] *Id.* at p. 8.

their own milk on the farm and market and distribute the processed products to the consuming public. Moreover, most dairy farmers – and particularly those located in the more remote rural areas of the United States – do not have the means to economically transport their individual production to market.

In other words, most individual dairy farmers – even the largest – simply do not have the market presence or leverage on their own to supply the many services that are essential to marketing dairy products in today's increasingly urban and suburban channels of commerce. The cooperative system permits individual dairy farmers to work together to take advantage of economies of scale in the collection, processing and transportation of milk to market. The cooperative system has become even more important to dairy farmers as our national population has become increasingly more urbanized and food distribution and retailing have become increasingly concentrated. Stated simply, the cooperative system is what enables the independent dairy farm to survive today.

Importance of Capper-Volstead

The Capper-Volstead Act has played a critical role in maintaining a broad and diverse dairy producer sector. One of the most important – perhaps the most important – factor in maintaining competition in the dairy sector has been the availability of the Capper-Volstead Act exemption allowing farmers to remain independent, while still taking cooperative action without fear of challenge under the antitrust laws. The laws of economics dictate that as any industry matures over time, there will be greater concentration as competitors take advantage of

economies of scale in producing and delivering products to market. The very innovative dairy farming sector has embraced technological and other developments to create such scale economies, contributing to the overall decline in absolute numbers of individual dairy producers over the past century. As a practical matter, however, such innovations will not be enough to enable individual dairy farms to survive and compete if they were forced to do so on their own. To reach the kinds of scale required to justify the large capital investments needed to stand on their own, most dairy farms would have to give up their independence and control by entering contractual and economic relationships found in certain other agricultural sectors (*e.g.*, poultry and eggs) or by completely dissolving into a corporate amalgam. The cooperative structure allows individual family farm operations to continue to exist by permitting farmers to prepare and jointly market their products without giving up economic and practical control of their farms.

While the Capper-Volstead exemption fosters competition in the dairy sector by protecting a structure that allows thousands of individual farmers to operate and compete, it has also advances several other important economic and social policies of the United States. The Capper-Volstead exemption fosters small business in the dairy sector, helps to maintain economically viable rural communities, and helps to maintain healthy dairy industries, not only in the traditional producing regions of the Northeast and Upper Midwest where farms are of smaller sizes, but also in western regions where the cooperative infrastructure provides for the assembly of a milk supply from typically larger, and often more isolated, farms.

Concentration

As discussed above, U.S. dairy production remains a diverse enterprise with approximately 57,000 licensed dairy farms nationally. While there has been notable concentration in the dairy production sector over the past twenty years, today there are still tens of thousands of individual, family-owned dairy farms in the United States. Moreover, there is great diversity in the way in which dairy producers participate in the market. The majority of dairy farmers still participate through their membership in local or regional cooperatives; a lesser but still substantial number of farmers are members of cooperatives that are national in scope. Nearly thirty percent of all dairy farmers are independent producers (*i.e.*, they are not members of any dairy cooperative).[8]

The dairy cooperative sector also remains diverse and not significantly concentrated. As noted above, USDA's annual survey of cooperatives found 155 dairy cooperatives in 2007. These handled a wide range of production volumes – from less than 100 million pounds to over 6 billion pounds[9] – and involved a wide range of different kinds of dairy product marketing activities.[10] The study also revealed significant changes in the distribution of cooperative size and range of

[8] As noted above, even dairy producers that do not join cooperatives implicitly rely upon the "balancing" services provided by the cooperative(s) operating in their local area to avoid economically devastating milk-price reductions in annual "flush" seasons of excess raw milk production.

[9] Ling Study, at p. 10, table 9.

[10] *Id.* at p. 3, table 2.

operating activities as compared to 2002. [11] Yet overall the share of milk handled by cooperatives relative to the whole dairy industry remained steady, as did the shares of milk handled by the four, eight, and twenty largest dairy cooperatives, respectively, compared both to total U.S. volume and to cooperative volume.[12]

Moreover, the dairy producer and dairy cooperative sectors play only a secondary role in manufacturing dairy products for the consumer market. Only about one-third of the milk produced by farmers who are members of dairy cooperatives is processed in plants owned and controlled by those cooperatives. Farmer-owned cooperatives enjoy only a small share of consumer sales for dairy products, with proprietary dairy manufacturers dominating those sales. Only eleven cooperative plants manufacture ice cream, and only that same number manufacture cultured dairy products. Cooperatives market only seven percent of the fluid milk sold in the United States, only four percent of the ice cream, only ten percent of the yogurt and only 14 percent of the sour cream.[13]

In contrast to the situation of consumer products, cooperative plants predominate when it comes to producing products required to "balance" the

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[11] Changes in the numbers of cooperatives in various size categories suggest movement both "up" and "down" the size chart in Table 9 of the study. *Id.*, at p. 10. Similarly, changes in types of marketed products in table 2 suggest dynamic adjustments by various dairy cooperatives during the same period. *Id.* at p. 3.

[12] *Id.* at p. 10, table 10.

[13] *Id*, at p. 7.

market. Cooperative manufacturing accounts for 71% of the butter manufactured in the United States and 96% of the dry milk products.[14]

Thus, when it comes to most consumer products, the majority of dairy processing in this country is done by proprietary companies, and this sector has become increasingly concentrated. Similarly, only a very small portion of the milk and dairy products sold at retail in this country is sold by dairy farmers or their cooperatives through retail outlets they own or control. Most dairy products are sold at retail in large chain stores, and increasingly food retail has become concentrated at both a national and regional levels.

There is a significant gap between prices that dairy farmers receive for their milk and the prices that consumers pay for milk and other dairy products at the retail level. In recent years, farmers have received a smaller and smaller percentage of the consumer dollars paid for dairy products. Increasingly, the lion's share of consumer spending on dairy products is captured at the processing or retail levels of the food chain.

By contrast, there is far less diversity and much more concentration in the dairy processing and food retail sectors. Increased concentration in the dairy processing and food retail sectors are issues that could be of concern in terms of both fair returns for dairy farmers and of fair prices for consumers. There is ample competition at the production level in the dairy industry. Federal antitrust and

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[14] *Id.* at pp. 5 & 6.

regulatory policies should be directed at insuring that there is also ample competition downstream in the processing and retail sectors.

Vertical Integration

Although NMPF has concerns about the levels of concentration in proprietary manufacturing and retail marketing and distribution sectors, NMPF believes that the current vertical structure of the dairy industry as a whole is broadly consistent with a healthy competitive environment. There is currently only limited overlap among the producer, processing, and retail sectors. As of 2007, fewer than one third of dairy cooperatives processed milk products other than fluid milk.[15] Some 63% of all milk handled by dairy cooperatives was sold in raw form for further processing and resale in fluid or other forms of products.[16] Dairy cooperatives marketed only 7.4% of packaged fluid milk products and 26% of all natural cheeses produced in the United States.[17] NMPF opposes increased vertical integration in the dairy industry to the extent that now exists in the poultry and egg industries – where independent producers have disappeared and where farmers have been relegated to being "contract growers" for large national or multinational companies. This should not be allowed to be repeated in the dairy sector.

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[15] USDA Rural Development Service, Cooperative Programs, Marketing Operations of Dairy Cooperatives-Historical Summaries, Table 1 (June 8, 2009) (29%), available at http://www.rurdev.usda.gov/rbs/coops/dairy.htm.

[16] *Id.* at Table 4; *see also* Ling Study, at p. 4, table 4.

[17] Ling Study, at 8, table 8. Due to the special role of cooperatives in balancing their members' seasonally varying milk production, cooperatives produced some 93% of dry milk products, 42% of dry whey products, and 71% of butter produced in the United States. *Id.*

Marketplace Transparency

NMPF favors maximum marketplace transparency so that competition can exist fairly and rationally at all levels of the food production and distribution chain, and so that government regulation can operate in a manner consistent with market forces. Unfortunately, there are very few sufficiently-traded markets for dairy products in the United States. NMPF has long contended that the collection and publication of market information regarding dairy products is a regulatory function that the U.S. Department of Agriculture can and should undertake. NMPF supported the enactment of provisions in the Dairy Market Enhancement Act of 2000 to require mandatory inventory reporting as a means of developing greater marketplace transparency. NMPF has offered to work with USDA towards effective implementation of that congressional mandate and has consistently urged USDA to make marketplace transparency in the dairy sector a top priority.[18]

Conclusion

NMPF welcomes the opportunity to comment on these issues of antitrust in the dairy sector. The unique characteristics of the dairy farmer's product – its extreme perishability and biologically-driven seasonality – have combined with economic realities to create the need for dairy producers to join together into cooperatives. Dairy cooperatives continue to provide the critical "balancing" and joint marketing activities upon which all dairy farmers rely – whether small or large,

[18] *See* Letter dated December 4, 2009 from Jerry Kozak, President, National Milk Producers Federation to Honorable Tom Vilsack, Secretary of Agriculture.

and whether members of a cooperative or not. The antitrust exemption of the Capper-Volstead Act has long created the legal basis for this hallmark of the dairy industry and must be maintained for the dairy cooperative system to help preserve opportunities for independent dairy farms in this country. Given the increased concentration that has occurred in the processing and retail sectors, the dairy cooperative structure will be more important to dairy farmers than ever in the future.

Finally, NMPF looks forward to elaborating on these comments at the June 7, 2010 workshop in Madison, Wisconsin, as the voice of the nation's dairy cooperatives and their 40,000 dairy farmer members.