



Commonwealth of Pennsylvania
Milk Marketing Board
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Official General
Order No. A-932

Posted: December 15, 2004
Effective: January 1, 2005

OVER-ORDER PREMIUM

NOW, this 15th day of December 2004, the Commonwealth of Pennsylvania, Milk Marketing Board (Board) adopts and issues this official general order pursuant to the authority conferred by the Milk Marketing Law, 31 P.S. §§ 700j-101 – 700j-1204. This order will become effective at 12:01 a.m. on January 1, 2005, and will expire at 12:00 midnight on June 30, 2005.

SECTION I

The attached findings of fact and conclusions of law are incorporated herein by this reference as though fully set forth in this order.

SECTION II

(a) In all milk marketing areas the calculation of the Class I price for milk produced, processed, and sold in Pennsylvania shall include an over-order premium of \$1.55 per hundredweight effective 12:01 a.m. on January 1, 2005, through midnight on June 30, 2005.

(b) Milk dealers shall show by line item on their monthly statements to independent producers and cooperatives the specific amount of the Pennsylvania Milk Marketing Board's over-order premium being paid.

SECTION III

All parts of Official General Order A-893 not inconsistent with this order shall continue in effect.

PENNSYLVANIA MILK MARKETING BOARD

Boyd E. Wolff, Chairman

Luke F. Brubaker, Member

Barbara A. Grumbine, Consumer Member

Date: December 15, 2004

**FINDINGS OF FACT AND CONCLUSIONS OF LAW
OVER-ORDER PREMIUM HEARING
DECEMBER 1, 2004**

FINDINGS OF FACT

1. On December 1, 2004, the Pennsylvania Milk Marketing Board (Board) convened a hearing for all milk marketing areas to receive testimony and evidence concerning the level and duration of the over-order premium.
2. Notice of the hearing was published at 34 Pennsylvania Bulletin 5458 on October 1, 2004, and was mailed to those who have requested notice of Board hearings by means of Bulletin No. 1369, dated September 23, 2004.
3. At the end of the hearing, a briefing schedule was set. Principal briefs were due on December 10, 2004, and reply briefs were due on December 13, 2004.
4. Kenneth W. Bailey, Ph. D., testified on behalf of Board Staff as an expert in dairy marketing and policy analysis. Dr. Bailey noted that 2004 had been a record year for milk prices and that Pennsylvania had begun to see some increased milk production. Dr. Bailey testified that he expected the Pennsylvania all milk price for 2004 to average \$17.45 per hundredweight and that he forecast the 2005 Pennsylvania all milk price to average \$14.77 per hundredweight. Dr. Bailey testified that his forecast for 2005 was "conservative" and less than what other economists and the USDA had forecast. Dr. Bailey made various assumptions in making his forecast: the border with Canada would remain closed to cows, fluid milk sales would be normal, cow numbers would decline in 2005 by 0.3 percent, the milk supply would grow 2 percent in 2005, and a return to normal levels of consumption for cheese and butter. Dr. Bailey offered no testimony regarding the level or duration of the over-order premium.
5. Charles Seidel, a dairy farmer from Berks County, testified on behalf of Pennsylvania State Grange. Mr. Seidel recommended that the Board set the over-order premium at \$1.55 per hundredweight. Mr. Seidel testified that the Grange felt that a higher over-order premium was justified, but nonetheless was willing to compromise and advocate the \$1.55 per hundredweight level. Mr. Seidel testified that \$1.55 was an appropriate level for the over-order premium because higher producer milk prices had been accompanied by increased production costs, hurricane victims would experience higher than normal expenses due to the unexpected need to buy additional feed to compensate for damaged crops, cows continued to leave Pennsylvania, and the market had not suffered with an over-order premium of \$1.55 per hundredweight. Mr. Seidel noted that the Grange's recommended over-order premium was in addition to the fuel adjuster to the over-order premium established by Official General Order A-927.
6. Amy Van Blarcom-Lackey testified on behalf of Pennsylvania Farm Bureau as an expert in dairy economics specifically related to matters that impact dairy prices and costs of production. Ms. Van Blarcom-Lackey recommended that the over-order premium be set

at \$1.55 per hundredweight for January 2005 through June 2005 and that the over-order premium fuel adjuster established by OGO A-927 continue as a separate entity. Ms. Van Blarcom-Lackey projected that the average price Pennsylvania producers would receive for the six month period from January 2005 through June 2005 would be \$14.36 per hundredweight (this included MILC payments and promotion assessments, but not premiums). Ms. Van Blarcom-Lackey testified that there was no reason to expect the cost of production to be significantly lower in the "near future" than the \$14.01 per hundredweight estimated by the Pennsylvania Agricultural Statistics Service (PASS) for the 12 month period ending September 30, 2004. She testified, however, that the PASS cost of production did not provide a complete picture of producers' future price needs; Ms. Van Blarcom-Lackey opined that a complete cost of production picture would include a cost for management, a cost for interest on equity, and a reasonable profit of 3.5 percent. Ms. Van Blarcom-Lackey acknowledged that the cost for management and the cost for interest on equity were economic costs, rather than actual accounting costs.

7. Ms. Van Blarcom-Lackey noted that the National Agricultural Statistics Service (NASS) Milk Production Report released on November 16, 2004, showed a 0.9 percent increase in Pennsylvania milk production in October 2004 compared to October 2003. She also noted that the NASS Milk Production Report showed that there were 1,000 more cows in Pennsylvania in October 2004 compared to October 2003. However, Ms. Blarcom-Lackey also pointed out that total cow numbers in Pennsylvania in 2003 were 10,000 less than the total cow numbers in 2002. Ms. Van Blarcom-Lackey also testified that Pennsylvania production of corn for grain and soybeans had increased over 2003, but that irregular weather conditions had resulted in somewhat irregular hay crops across the state.
8. Edward Gallagher testified as an expert in agricultural economics and dairy marketing on behalf of Dairylea Cooperative, Inc.; Dairy Farmers of America, Inc.; Land O' Lakes, Inc.; Dairy Marketing Services, LLC; the Northeast Milk Marketing Agency, and Maryland and Virginia Milk Producers' Cooperative Association, Inc. Mr. Gallagher recommended that the over-order premium be set at \$1.55 per hundredweight for January 2005 through June 2005 and that the fuel adjuster established in OGO A-927 continue separately. Mr. Gallagher testified that milk prices for the first half of 2005 were expected to average "quite a bit less than in 2004." He noted that 2004's record high milk prices, increased allocation of Posilac, and better, more abundant and less expensive feed stuffs would contribute to higher milk output and lower nationwide milk prices. Mr. Gallagher estimated that Pennsylvania farmers would receive an average blend plus MILC price of \$14.44 per hundredweight for the first six months of 2005, a decrease of \$2.29 per hundredweight for the same period in 2004.
9. Mr. Gallagher testified that Pennsylvania milk production "may be turning a corner." He noted that as of October 2004, cow numbers in Pennsylvania had increased for four consecutive months. He also noted that in October output per cow exceeded year earlier levels for the first time since July. As a result, milk production in Pennsylvania increased over year earlier levels for the first time since August 2002. Mr. Gallagher testified that with continued strong milk prices through the end of 2004, the increase in the Posilac

- allocation effective December 1, better forages, lower-priced feedstuffs, and no decrease in cow numbers, Pennsylvania producers may continue to show increased milk production for the remainder of 2004 and production growth of as much as two percent for the first half of 2005. Mr. Gallagher noted that maintaining and growing Pennsylvania's milk herd would be dependent on milk prices and dairy farmer profitability.
10. Dennis Schad testified as an expert in agricultural economics and dairy marketing on behalf of the Northeast Milk Marketing Agency (NEMMA), Dairylea Cooperative, Inc.; Dairy Farmers of America, Inc.; Land O' Lakes, Inc.; Dairy Marketing Services, LLC; and Maryland and Virginia Milk Producers' Cooperative Association, Inc.. Mr. Schad recommended that the over-order premium be set at \$1.55 per hundredweight for January 2005 through June 2005 and that the fuel adjuster established in OGO A-927 continue separately. Mr. Schad testified that dairy farmer costs of production had increased drastically between the third quarters of 2003 and 2004. Mr. Schad also testified that about 25 percent of the cost of milk production is related to feed costs and that while Pennsylvania dairy farmers enjoy an all-milk price above the national average, they also incur feed costs above national norms.
 11. Mr. Schad demonstrated the effect of Pennsylvania farmers' higher feed costs by developing a Pennsylvania milk-feed ratio. Mr. Schad noted that a milk-feed ratio above 3.0 is generally considered to be a cost-price signal to expand production, while a milk-feed ratio below 3.0 is a signal to farmers to constrict milk production. Mr. Schad testified that the national milk-feed ratio had been near or above 3.0 for much of 2004, but the Pennsylvania milk-feed ratio had gone above 3.0 only once during 2004. Mr. Schad forecast the Pennsylvania milk-feed ratio through the first six months of 2005 to be consistently below 3.0. Mr. Schad testified that the Board could do nothing to make Pennsylvania's feed costs less, but could effect the milk-feed ratio through the Board's role in setting producer prices.
 12. Mr. Schad also noted that for October 2004 PASS had reported an increase in Pennsylvania monthly milk production over year earlier levels for the first time since August 2002. However, Mr. Schad pointed out that while October 2004 production was above year earlier levels, it was 6.7 percent below October 2002 production. He also noted that during the first 10 months of 2004, Pennsylvania milk production was 3.6 percent lower than the previous year and 7.5 percent lower than 2002.
 13. Mr. Schad also testified regarding premiums in surrounding markets. According to Mr. Schad, NEMMA prices for distribution in Maryland and Delaware increased to \$1.55 per hundredweight in October when the Pennsylvania-mandated premium increased to \$1.55 per hundredweight. Mr. Schad also testified that the premium for distribution in southern New Jersey remained at \$1.20 per hundredweight. Mr. Schad testified that the Dairy Cooperative Marketing Agency (DCMA) premium for the southeastern region of the country would change effective 2005 to set the net premium in a range between \$1.45 and \$1.85 per hundredweight depending on the Class I mover; using Mr. Gallagher's Class I mover forecasts, Mr. Schad expected the DCMA premium to range from \$1.45

per hundredweight in January 2005 to \$1.57 per hundredweight by June 2005. Mr. Schad further noted that the Mideast Milk Marketing Agency gross Class I premium for December 2004 for Ohio distribution was announced at \$1.70 per hundredweight plus a \$0.06 per hundredweight fuel adjustment, with the fuel adjustment billed on all classes of milk.

14. Earl Fink testified on behalf of the Pennsylvania Association of Milk Dealers (PAMD) as an expert in milk marketing. Mr. Fink testified that the PAMD's position was that the over-order premium should be reduced, but that the PAMD could not agree on a level to which the premium should be reduced. Mr. Fink testified that the primary reason the PAMD recommended that the premium be reduced was the failure of the premiums in most surrounding markets to rise to the level of the Pennsylvania premium. Mr. Fink noted that the New Jersey premium had remained at \$1.20 per hundredweight and that Maryland "generally follows" the Pennsylvania premium. He also noted that Ohio announced premiums are above Pennsylvania's, but testified that the Ohio premiums are widely discounted to a level equal to or less than the Pennsylvania premium. Mr. Fink also testified that there were independent producers in Ohio who received a lower premium than the cooperative-announced premium. Mr. Fink testified that when Pennsylvania premiums are above those in surrounding markets, Pennsylvania dealers have to find cheaper milk in order to compete successfully with out-of-state dealers. Mr. Fink testified that that is not in the best interests of the producers or dealers.
15. The Board finds that maintaining the over-order premium at \$1.55 per hundredweight for January 2005 through June 2005 is the best response to conditions in Pennsylvania at this time. The Board also finds that the over-order premium fuel adjuster provided for in OGO A-927 shall continue independent from this over-order premium decision.

The Board found the testimony of all the witnesses to be credible, and we believe that maintaining the over-order premium at \$1.55 per hundredweight for six months plus the fuel adjuster is the proper course to take at this time. We are aware of the PAMD's concerns regarding setting the level of Pennsylvania's over-order premium at a level that will not lead to Pennsylvania dealers and retailers having to seek cheaper sources of milk; we share the PAMD's opinion that such a situation is not in the best interests of Pennsylvania dealers or producers. However, it appears to the Board that setting the Pennsylvania premium at \$1.55 per hundredweight plus the fuel adjuster for the first six months of 2005 will not result in significant market-affecting disparity between the Pennsylvania premium and premiums in surrounding markets.

The Board also continues to believe that it is important to provide an incentive for producers to remain in business in Pennsylvania and to increase production. If Pennsylvania production truly has turned a corner and is entering a period of continuing increases, the Board desires to encourage that trend. We believe that maintaining the premium at \$1.55 per hundredweight plus the fuel adjuster will do that.

CONCLUSIONS OF LAW

1. The December 1, 2004, hearing on the over-order premium was held pursuant to the authority granted to the Board in sections 801 and 803 of the Milk Marketing Law (Law), 31 P.S. §§ 700j-801 and 700j-803.
2. The hearing was held following adequate notice and all interested parties were given a reasonable opportunity to be heard.
3. All parts of Official General Order No. A-893 not inconsistent with the attached order will continue in effect.
4. In accordance with Official General Order No. A-894, milk dealers shall continue to show by line item on their monthly statements to independent producers and cooperatives the specific amount of the Pennsylvania Milk Marketing Board's over-order premium being paid.
5. In accordance with Official General Order No. A-894 (Supplemental), the over-order premium will continue to apply only to Class I milk produced, processed, and sold in Pennsylvania.
6. In adopting this order, the Board considered the entire record and concludes that the order is supported by a preponderance of credible evidence and is reasonable and appropriate under sections 801 and 803 of the Law.
7. The attached order may be amended pursuant to the procedures set out in section 801 of the Law.

PENNSYLVANIA MILK MARKETING BOARD

Boyd E. Wolff, Chairman

Luke F. Brubaker, Member

Barbara A. Grumbine, Consumer Member

Date: December 15, 2004

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