Regarding Kansas Statute #17-1642

Kansas Statute #17-1642 provides that agricultural cooperatives chartered in Kansas may have former members who still hold equities in such cooperatives to object in writing to a merger and request their equities be returned if the merger goes through.

Dairy Farmers of America, Inc. (DFA) is an agricultural cooperative chartered in Kansas. DFA and Vermont's St. Albans Cooperative are exploring merger.

The accompanying documents detail and explain Kansas Statute $17-1642:

• A story from the current issue of The Milkweed titled, "Kansas Statute #17-1642: Ex+DFA Members May Object to Merger, Request Equity Pay-Out.

• A copy of Kansas Statute #1-1642.

• Historic articles from The Milkweed dating back to 1997, when DFA was being formed by merger of four dairy co-ops. Back then, the co-op sued former members who'd objected to the merger and scared off those claimants from pursuing return of their equities.

K.S.A. 17-1642

17-1642. Payment for interest of member objecting to merger; demand for payment; appraisal and determination of value; taxation of costs; status of member's interest; section inapplicable to certain member's interest

Currentness

(a) Except as provided in subsection (j), the association or corporation surviving or resulting from any merger or consolidation, within 10 days after the effective date of the merger or consolidation, shall notify each member or stockholder of any association or corporation of this state so merging or consolidating who objected thereto in writing and whose shares either were not entitled to vote or were not voted in favor of the merger or consolidation, and who filed such written objection with the association or corporation before the taking of the vote on the merger or consolidation, that the merger or consolidation has become effective. If any such member or stockholder, within 20 days after the date of mailing of the notice, shall demand in writing, from the association or corporation surviving or resulting from the merger or consolidation, payment of the value of the member's or stockholder's interest, the surviving or resulting association or corporation shall pay to the member or stockholder, within 30 days after the expiration of the period of 20 days, the value of the member's or stockholder's interest on the effective date of the merger or consolidation, exclusive of any element of value arising from the expectation or accomplishment of the merger or consolidation.

(b) If during a period of 30 days following the period of 20 days provided for in subsection (a), the association and any such member or stockholder fail to agree upon the value of such member's or stockholder's interest, any such member or stockholder, or the association or corporation surviving or resulting from the merger or consolidation, may demand a determination of the value of the member's or stockholder's interest by an appraiser or appraisers to be appointed by the district court, by filing a petition with the court within four months after the expiration of the thirty-day period.

(c) Upon the filing of any such petition by a member or stockholder, service of a copy shall be made upon the surviving association or corporation, which shall file with the clerk of the district court, within 10 days after such service, a duly verified list containing the names and addresses of all members or stockholders who have demanded payment for such member's or stockholder's interest and with whom agreements as to the value of such member's or stockholder's interest have not been reached by the association or corporation. If the petition is filed by the surviving association or corporation, the petition shall be accompanied by such duly verified list. The surviving association or corporation shall give notice of the time and place fixed for the hearing of such petition pursuant to subsection (c) of K.S.A. 60-303, and amendments thereto, to the members or stockholders shown upon the list at the addresses therein stated and notice shall also be given by publishing a notice at least once, at least one week before the day of the hearing, in a newspaper of general circulation in the county in which the district court is located. The court may direct such additional publication of notice as the court deems advisable. The forms of the notices by mail and by publication shall be approved by the court.

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(d) After the hearing on the petition the court shall determine the members or stockholders who have complied with the provisions of this section and become entitled to the valuation of and payment for such member's or stockholder's interest, and shall appoint an appraiser or appraisers to determine such value. The appraiser or appraisers may examine any of the books and records of the associations or corporations the stock of which such appraiser or appraisers is charged with the duty of valuing, and following an investigation, the appraiser or appraisers shall make a determination of the value of the member's or stockholder's interest. The appraiser or appraisers shall also afford a reasonable opportunity to the parties interested to submit to the appraiser or appraisers pertinent evidence on the value of the member's or stockholder's interest. The appraiser or appraisers, also, shall have the powers and authority conferred upon masters by K.S.A. 60-253, and amendments thereto.

(e) The appraiser or appraisers shall determine the value of the stock of the members or stockholders adjudged by the district court to be entitled to payment therefor and shall file a report respecting such value in the office of the clerk of the district court, and notice of the filing of such report shall be given by the petitioners to the parties in interest. Such report shall be subject to exceptions to be heard before the court both upon the law and facts. The court by decree shall determine the value of the stock of the members or stockholders entitled to payment and shall direct the payment of such value, together with interest, if any, to the members or stockholders entitled by the surviving or resulting corporation. Upon payment of the judgment by the surviving or resulting corporation, the clerk of the district court shall surrender to the surviving association or corporation the certificates of shares of stock held by the clerk pursuant to subsection (f). The decree may be enforced as other judgments of the district court may be enforced, whether such surviving or resulting association be an association of this state or of any other state.

(f) At the time of appointing the appraiser or appraisers, the court shall require the members or stockholders who hold certificated shares and who demanded payment for the shares to submit the certificates of stock to the clerk of the court, to be held by the clerk pending the appraisal proceedings. If any member or stockholder fails to comply with such direction, the court shall dismiss the proceedings as to such member or stockholder.

(g) The cost of any such appraisal, including reasonable fees and expenses of the appraiser or appraisers, but exclusive of fees of counsel or of experts retained by any party, shall be determined by the court and taxed upon the parties to such appraisal or any of them as appears to be equitable, except that the cost of giving the notice by publication and by certified mail shall be paid by the surviving association or corporation. Postjudgment interest, if any, shall be in accordance with K.S.A. 16-204, and amendments thereto, to be paid upon the value of the stock of the members or stockholders entitled thereto.

(h) Any member or stockholder who has demanded payment of the member's or stockholder's interest as herein provided shall not thereafter be entitled to vote such member's or stockholder's stock for any purpose or be entitled to the payment of dividends or other distribution on such stock, except dividends or other distributions payable to members or stockholders of record at a date which is prior to the effective date of the merger or consolidation, unless the appointment of an appraiser or appraisers shall not be applied for within the time herein provided, or the proceeding be dismissed as to such member or stockholder, or unless such member or stockholder with the written approval of the surviving association or corporation shall deliver to the association or corporation a written withdrawal of the member's or stockholder's objections to and an acceptance of the merger or consolidation, in any of which cases the right of such member or stockholder to payment for the member's or stockholder's interest shall cease.

(i) The shares of the surviving or resulting association or corporation into which the shares of such objecting members or stockholders would have been converted had they assented to the merger or consolidation shall have the status of authorized and unissued shares of the surviving or resulting association or corporation.

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(j) This section shall not be applicable to the members, stockholders or other holders of equity securities of the surviving association or corporation in any merger where the active members of the surviving association or corporation continue to be eligible to be members of the surviving association or corporation after the merger and the agreement of merger does not amend the articles of incorporation, and shall not apply to the members, stockholders or other holders of equity securities of the constituent association or corporation not surviving the merger in any merger where the active members of such constituent association or corporation are eligible to become members of the surviving association or corporation on the same terms and conditions as other similarly classified members of the surviving association or corporation.

Credits

Laws 1991, ch. 74, § 6; Laws 2000, ch. 175, § 1.

K. S. A. 17-1642, KS ST 17-1642
Statutes are current through laws enacted during the 2019 Regular Session of the Kansas Legislature effective on or before April 25, 2019.

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K. S. A. 17-1642, KS ST 17-1642
Statutes are current through laws enacted during the 2019 Regular Session of the Kansas Legislature effective on or before April 25, 2019.

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Mid-Am's Liabilities Cloud MMI's Delegates'

On September 8 or 9 in St. Louis, Milk Marketing, Inc.'s directors narrowly approved a bitterly-fought vote to join the Dairy Farmers of America merger. Immediately after the vote, on cue, MMI ceo Don Shriver escorted into the board meeting a lawyer, who, to the shock of some present, threatened MMI's directors with the warning that no one present dare speak or write anything negative about the DFA merger, because they could be personally sued!

Welcome to Dairy Farmers of Amerika.

Heil Hanman!

The narrow bottle-neck through which approval of the "mega-merger" must pass is the vote by delegates of Milk Marketing, Inc. (MMI) on Tuesday, November 25, 1997. MMI is internally divided on the merger question. Heavy-handed, one-sided, top-down information is being shoveled upon MMI members and delegates by the leadership.

Boiling the "mega-merger" issue for MMI delegates down to the bones, the single most important question becomes: what are the financial conditions of the prospective co-op partners and what contingent liabilities do they report. In the "Due Diligence" portion of the merger process, the four cooperatives have listed their contingent liabilities.

Before MMI delegates can vote rationally, they must know the contingent liabilities listed by the other three cooperatives. Without this information, they are voting with blinders on. Delegates should demand the formal listing of the contingent liabilities, prior to any delegate meeting discussion and vote. A co-op merger is a "marriage" in which the partners inherit others' assets and liabilities.

Mid-Am's potential contingent liabilities

Presuming the worst, in the case of Mid-America Dairymen, Inc. ... i.e., that the co-op might be less than truthful about its contingent liabilities, *The Milkweed* offers its own listing of Mid-Am's *possible contingent liabilities. These insights are* prepared for the purpose of helping MMI members and delegates ask better questions prior to their vote. Any correlation between these suggested liabilities and Mid-Am's actual liabilities is purely lamentable:

The Borden deal: Late this summer, Southern Foods Group (in which Mid-Am is an approximate 50% owner) acquired the dairy division of Borden. Estimated cost, after selling off nine plants in the Sunbelt: $370 million.

The Borden deal fails the "sniff test" for a couple reasons:

* The purchase price was several times higher than what dairy analysts project Borden's dairy division to have been worth. Mid-Am (or Southern Foods Group) paid at least three to four times Borden's estimated value. Industry watchers note that Borden's relatively poor performance in recent years has meant reduced maintenance and capital improvements in the dairy plants.

* Mid-Am officials ballyhooed Borden's average operating profits of around $20 million for ''95-'96. Those profits may be contrived.

--In fiscal/calendar 1994, Borden suffered operating losses and write-downs totaling $400 million! Thus, Borden's three-year, average operating results for the dairy division is NEGATIVE $120 MILLION! Former Borden employees relate that the company made fiscal '94 look as bad as possible, in order to better operating numbers for subsequent years in hopes of pawning off the business on an unsuspecting sucker.

--Even if one accepts Borden's recent, two-year operating performace as valid, the approximate $20 million profits don't cover annual interest payments on the $370 million net Borden purchase. Condition of the Borden plants is also suspect. (Mid-Am spun off the Borden purchase to Southern Foods Group--in which Mid-Am is a half-interest partner.)

Current Antitrust Investigation: Presently, the Antitrust Division of the United States Justice Department is conducting a thorough review of potential violation of a 1977 Consent Decree by Mid-Am. Since this type of investigation is conducted behind closed doors, there is no way to publicly evaluate the status of the Antitrust probe.

What potential liability is acknowledged by Mid-Am of this serious Antitrust probe in the contingent liabilities? Mid-Am's 1996 audit makes no mention of the investigation.

Southeast Dairies bankruptcy liability: In August 1996, a federal bankruptcy judge in Louisville, KY ruled that Mid-Am was liable for some $5 million in bankruptcy losses associated with the failure of Southeast Dairies. The judge found that Flav-O-Rich (a subsidiary of Dairymen, Inc.) violated a contract to supply Southeast Dairies with packaged fluid milk products, when Flav-O-Rich closed down its Louisville-area milk plant. That lost supply forced Southeast Dairies into bankruptcy.

Since Mid-Am acquired all the assets and liabilities of Dairymen, Inc. in a 1994 merger, Mid-Am is liable for this $5 million bankruptcy tab. Has Mid-Am paid off this liability? *The Milkweed's* industry sources say not. If Mid-Am carries this liability into the merger, then members of the merging co-ops will inherit this obligation.

Ex-members Lawsuit in Louisiana: In early 1994, Mid-Am merged with the Gulf Dairy Assn., a co-op based in Franklinton, Louisiana. Nearly 600 producers belonged to Gulf Dairy Assn.

At merger time, Mid-Am assumed the existing membership contracts. Those contracts stipulated that Gulf Dairy Assn. members could not be assessed more than five cents per cwt. each for co-op equity and operating losses. Mid-Am's actions virtually since day 1 have violated those contractual provisions. Mid-Am's capital retains have been one percent. And Mid-Am has stuck former Gulf Dairy Assn. members for unexplained operating losses in excess of $1.00/cwt. in worst-case months.

In 1996, three Mid-Am members from Louisiana filed suit against the co-op, seeking repayment of all capital retains and operating loss charges in excess of five cents per cwt., since the time Mid-Am merged with their former co-op. Due to health problems of the judge (and Mid-Am's laggard response), this lawsuit still festers in the early stages. The three farmers' claims are a trial balloon for similar claims of the remaining, 500+ former Gulf Dairy Assn. members. In other words, if the three farmers' claims of contract violations are upheld, then Mid-Am would be obliged to payoff all excess deducts (over 5-cents per cwt.) taken from other such individuals.

The Milkweed estimates this potential liability here of $30 to $35 million, if the farmers' claims are sustained.

Payment of retains to former members: Section 17-1642 of Kansas' state statutes specifies that merging ag cooperatives must pay back the retained funds of former members within 60 days of the vote approving merger to former members who object to the merger prior to the actual vote. (See related article, this page.)

Starting in mid-October, news that former Mid-Am (and DI) members could recover their retains by objecting in writing to the merger has swept through the dairy rumor pipeline like a fire through a petroleum refinery. There is no way to evaluate Mid-Am's potential liability here. Estimates range from $15 million to $50 million. The co-op is denying liability in this matter. Kansas statutes provide for a clear-cut path to a class action lawsuit if the co-op denies such liabilities.

Mid-Am's responses to the equity payback matter for former members has varied.

* A lawyer with the co-op told one ag journalist that DFA was a "consolidation", not a merger. (WRONG! The word "merger" in one form or another appears <u>38 times</u> in the eight-page DFA document, "Statement of Terms of the ***<u>Merger.)</u>***

* Mid-Am's membership departments tell callers that former members have no standing.

* Mid-Am representatives cite Section J of 17-1642 as excusing the co-op from paying back retains to ex-members.

Webster Hubbell "affair": In spring 1994, shortly after Webster Hubbell left the United States

Ex-Members File to Recover Retains

by Pete Hardin

On short notice, fueled by dairy's ever-active rumor mill, hundreds, if not thousands of former members of AMPI's Southern Region and Mid-America Dairymen have tried to recover their retained monies from these two merging cooperatives, using Section 17-1642 of Kansas State statutes.

Section 17-1642 of Kansas statutes specifies that <u>former</u> members of merging agricultural co-ops may recover retained earnings and equities by objecting to the merger <u>in writing</u>, **before the merger votes take place.** (AMPI Southern Region and Mid-Am delegates' merger votes were Oct. 30 and Nov. 7, respectively ... so this matter blew past before *The Milkweed* could do justice to the issue.)

If the merger passes, Kansas law specifies repayment of retains within 60 days. Section J of 17-1642 specified how co-ops may possibly avoid such payouts. If the co-op objects, a related statute in Kansas law specifies a class action lawsuit.

(*Editor's note: This one is headed for the courts.)*

Information on this potential equity pay-back went out on the "Dairy Action" Internet website. Competing milk procurers in the Southeast and Sunbelt circulated sample form letters and explanations to their producers who formerly shipped to AMPI Southern Region, Mid-Am, or predecessor co-ops (such as Dairymen, Inc.). This news spread like wildfire in the Southeast and Sunbelt, where many former members of these cooperatives can recite to within $10 the amounts of their money still held by their former cooperatives. The Louisiana Milk Producers Assn. held meetings to explain the possible opportunity to local farmers.

Mid-Am has heatedly denied the notion that the co-op should repay all retains to ex-members who went through proper channels--objecting to the merger prior to the vote. Mid-Am representatives cite Section J of 17-1642. Kansas law cites payback in a lump sum shortly after the merger. Michael Fayhee, with the law firm of McDermott, Will & Emery, told *Dairy Profit Weekly* (11/3/97) that the merger was purposefully structured to avoid that liability. Fayhee also claimed that the 10-year plan of DFA to pay back equities would priortize ex-members first!!!

Fayhee's claims are directly contradicted by a prospectus-like, eight-page DFA document titled, "Statement of Terms for the Merger." On page 7 of that document, under the "Base Capital" heading, retirement of capital accounts is prioritized in the following order:

" * estates;

" * active members whose base capital levels exceeds $1.75 per cwt., such that the excess is redeemed over a three-year period;

" * members aged 60 or above on January 1, 1998 under the redemption plans of the four participating Cooperatives, who will be grandfathered and allowed to redeem under their current retirement plan; and

" * others as determined by the Board of Directors of DFA."

It should be noted that retirement of all capital accounts is at the discretion of DFA's board of directors.

The only way Fayhee's comment that former members' equities will be retired first is accurate: **if former members are deceased!**

Fayhee implied to *Dairy Profit Weekly* that these co-ops' equities may be only worth ten cents on the dollar. The co-ops pay this guy big bucks to imply that <u>they</u>'re nearly broke!

Merger Vote by Pete Hardin

Justice Department's third-highest post in disgrace, Gary Hanman, Mid-Am's ceo, paid Hubbell some $25,000 in a Washington, D.C. hotel room. Hanman acknowledged this event in a spring '97 Mid-Am membership meeting near Cabool, MO.

(Hubbell is Bill Clinton's self-described "best friend". Hubbell resigned from the Justice Department in the midst of an investigation into charges he stole about half a million dollars from the Rose law firm of Little Rock, Arkansas. After Hubbell left Justice, he received mega-doses of consulting fees, which appear to be politically-inspired. Hubbell pled guilty to the theft charges and served 18 months in federal prison.)

Presently, Kenneth Starr's special Whitewater counsel's office is investigating Mid-Am's payment to Hubbell. There is no way of assessing any possible fines if this matter turns out adversely for Mid-Am. It's important to note that Sun Diamond, a West Coast nut and raisin co-op, was fined nearly $2 million for $5000 in illegal gratuities to former USDA Secretary Mike Espy. What will $25Gs to Webster Hubbell garner Mid-Am, by the time Kenneth Starr gets done?

(Mid-Am's directors voted to indemnify management in this matter--i.e., pay legal costs and possible fines. Did Mid-Am's board of directors approve the original payments of $25,000 to Hubbell? Where is any such approval reported in Mid-Am board minutes?)

Tuscan/Lehigh Lawsuit: Last spring, Mid-Am bought an approximate 49% interest in Tuscan/Lehigh, a pair of dairy processors located in New Jersey and Pennsylvania. The majority interests in the Tuscan/Lehigh buy were the firms' management. Purchase price has not been publicly reported.

Here's the kicker: In September, Carvel Ice Cream sued Tuscan, citing short-weighting of ice cream mix packages by Dellwood (a business acquired by Tuscan a couple years ago) that allegedly occurred from 1990 to 1997. Carvel seeks a reported $80 million in damages.

Is Mid-Am liable for a share of this lawsuit, if Carvel's claims are sustained?

(Editor's note: This matter is one of the most curious we've ever seen. For part of the 1990-1997 period, Dellwood and Carvel were owned by the same firm--Investcorp, the investment branch of the National Bank of Bahrain. Investcorp sold Tuscan Lehigh to the present owners. Then, Carvel sues Tuscan for many years of alleged short-weighting.

Long-term debt "bubble" in '99: During most of the 1990s, Mid-Am rolled over maturing long-term debts. This process started with a couple million dollars in the early '90s and swelled to $18 and $25 million in 1995 and 1996, respectively, according to Mid-Am's '94 audit.

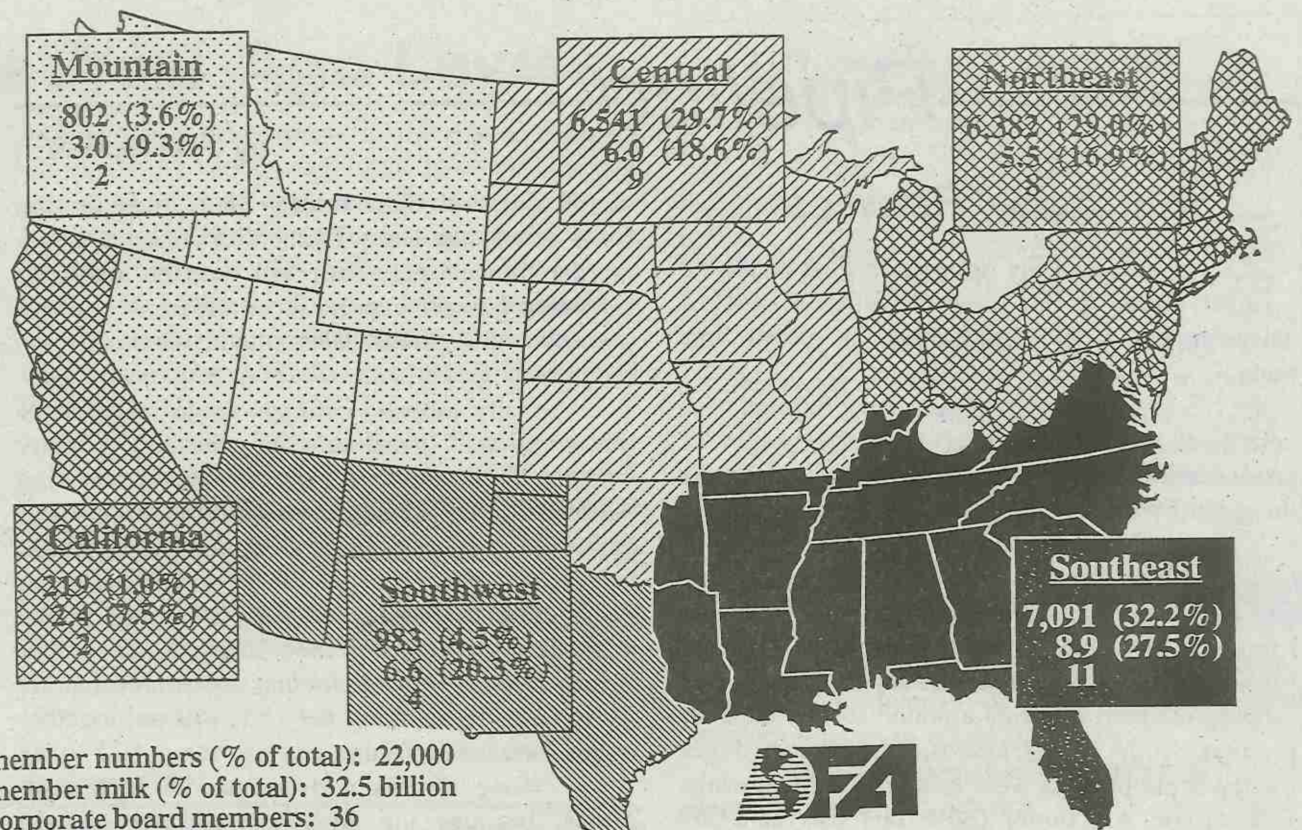
The 1996 audit shows that Mid-Am has rolled over past years' long-term obligations into a huge bubble of $43.8 million of long-term debt coming due in calendar/fiscal 1999.

If left to its own devices, how can Mid-Am pay off that bubble of long-term debt coming due in 1999? What responsible lender would countenance continued rolling-over of long-term debts?

Sum total: $___,___,___???

What is the approximate sum of known and potential contingent liabilities Mid-Am brings to the "mega-merger"? If all four co-operatives join on 1, 1998 ... Mid-Am's astounding known and suspected contingent liabilities become the onus of all DFA members.

In the opinion of the editor of *The Milkweed*, given the known and potential liabilities facing Mid-Am, if the co-op were left to its own devices, it'd either be in serious danger of financial meltdown sometime in 1999, or else members' milk checks would be severely savaged. Mid-Am's finances are a cancer which must consume increasing amounts of tissue to continue.



This map breaks down the six anticipated operating regions for Dairy Farmers of America. Figures shown, respectively, from top to bottom under each region's name are total producers, billion lbs. of member milk, and number of corporate board members. The reason for the "bullet hole" in eastern KY is because so many MMI members there hate Mid-Am (and Dairymen, Inc.) that the co-op doesn't know where to put these producers.

Next for DFA? Darigold? Dairylea? ICMPA?

Directors of the potential merging co-ops are spreading word that three additional cooperatives stand ready to join Dairy Farmers of America (DFA), as soon as feasible, after the merger start-up date of January 1, 1998.

Which co-ops would those be? Darigold, the monolith based in the Pacific Northwest, is an obvious candidate. The Independent Cooperative Milk Producers Assn. of Grand Rapids, MI, is a second possible candidate. The third rumored potential member is from the Northeast--Dairylea Co-op.

Darigold: The regional rumor mill runs red-hot, frying the monster dairy co-op of the Pacific Northwest. Darigold controls about 80% of the milk supply in its operating area. Darigold's operations are being skewed by declining milk volumes (and significant drops in milk solids) in the Pacific Northwest milk order, just as Darigold has brought back on line its Sunnyside, WA cheese plant (where capacity has just been doubled). It looks like a free-for-all as the board wrestles for control of the steering wheel after management has underperformed historically.

Hot rumor mill fodder focuses on plans being circulated by accounting-types who propose converting Darigold to a stockholder-owned company--with current equity holders likely to take a huge bath in the process. Wes Eckert, president and ceo of Darigold Farms (the co-op's consumer product division) has recently announced his abrupt retirement.

Sell-outs of 100 and 200-cow members, coupled with poor quality forages in the region, are killing farm milk volumes and solids-content. Just about everything that can go wrong at Darigold is: underperformance by the consumer products division, milk powder prices and markets, reduced manufacturing plant capacity--especially as the Sunnyside plant draws volumes from other facilities. Darigold is close to chaos.

Darigold markets a full line of consumer products under the "Darigold" label. Darigold's consumer product division has been a big-time loser. In the past year or so, Darigold has tried to sell off the consumer products division, but has not been able to correlate a buyer and a mutually-agreeable price-tag. Dean Foods looked at Darigold's consumer products, but walked away when the price tag was too steep.

Darigold's financial problems translate into dramatic, under-blend price payments to members, as well as pursuit of regional milk pricing and national policies which siphon producer resources from the milk check to the manufacturing plant. No bargain here.

ICMPA: The Independent Cooperative Marketing Producers Assn. is Michigan's second-largest dairy co-op, totaling about 650 members. ICMPA recently closed its under-utilized Kalamazoo butter-powder plant and has a balancing deal with Milk Marketing, Inc., one of the four DFA hopefuls.

ICMPA is caught in Michigan's again fractious co-op environment. The local fluid superpool is collapsing. Michigan Milk Producers Assn. (the state's biggest co-op) and ICMPA mutually distrust. ICMPA membership is being hit by producer sell-outs. Fluid processors are cherry-picking members to develop independent milk supplies--another factor *weighing on ICMPA's* membership.

At an *ad hoc* dairy producers meeting at the Rosebush sale barn on September 17, ICMPA manager Chuck Cortade publicly commented that he guessed ICMPA was going to have to join Dairy Farmers of America. It's not known if that comment represents the manager's personal opinion or official policy.

Dairylea Co-op: Based in Syracuse, NY, Dairylea is relatively secretive about financial details. Ostensibly recovering from negative net worth in the '80s, Dairylea has ventured into novel activities for a dairy co-op in recent years--livestock auctions, electricity buyers-groups, a.i., feed purchases (for large members). Dairylea's estimated membership is somewhat above 2000 members. Few others in the Northeast trust Dairylea. Dairylea's marketing programs worship big producers.

Dairylea has evolved as the personal bailiwicks of president Clyde Rutherford and ceo Rick Smith. The bewigged Rutherford holds one of dairy's all-time great egos. Word is he's been promised some fancy post to lead his troops into DFA--just like the inducement to MMI's Herman Brubaker.

Because Dairylea is so secretive about its finances, it's hard to evaluate the merits and demerits this co-op would bring to DFA.

How much would these individual co-ops bring to the merger, in terms of members and annual milk production?

Darigold: 950 producers, 5 billion lbs. of milk.
Dairylea: 2400 producers, 4.4 billion lbs. of milk
ICMPA: 700 producers, .9 billion lbs. of milk

All together, these three co-ops would add about 50% more producers and one-third more annual milk volume.

by Pete Hardin

A Structured Management Program for America's Dairy Farmers

by Dick Bylsma

America's dairy farmers are suffering through four-plus years of terrible milk prices. Falling demand for fluid milk, trade policies that impair dairy exports' volumes and prices, and rising sales of non-dairy beverages are combining to reduce overall demand for farm milk. On the positive side, cheese demand – particularly Mozzarella – remains strong and butter prices have been stable in the $2.20-$2.28/lb. range.

Meanwhile, cows with better genetics are boosting total milk production. This imbalance between supply and demand must be addressed and solved if we are to restore adequate farm milk prices.

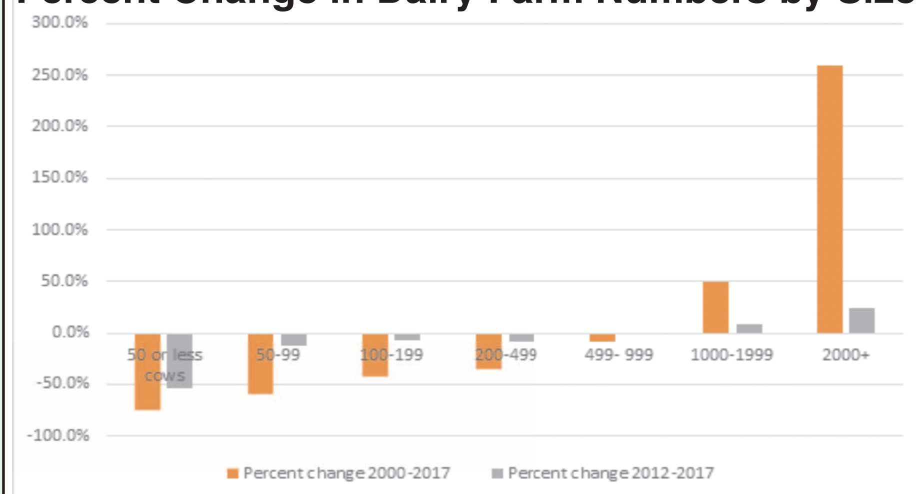
Price Is Not the Only Problem

The pricing problem is not the only concern among America's dairy farmers. We also have a "structure problem." Dairy farmers think of farm buildings when they hear the word "structure." But in the world of farm policy and economics, "structure" has a different meaning — referring to how many farms produce the nation's milk and how large each of those farms is. Looked at that way, we see America's dairy industry with a serious structure problem that worsens daily.

What is dairy's structure problem? Losing so many family-sized farms, while the number of very large farms continues growing. The numbers are shocking: The United States lost over 65,000 dairy farms that were milking less than 200 cows during 2000-2017. Meanwhile, the number of dairies with more than 2,000 cows doubled. We are stuck in what a CoBank report called a "self-perpetuating process" threatening to eliminate opportunities for family-sized farms altogether.

Won't programs that raise milk prices be enough to get America's smaller dairies off the endangered species list? Unfortunately, the answer is "no." Don't get me wrong—we at National Farmers fully support programs that balance supply and demand in ways that bring better prices. But those better prices alone won't solve the structure problem. During times of good farm milk prices and in times of terrible prices, history shows we continue to lose smaller farms and replace them with fewer, much larger operations.

This is the heart of the dilemma facing dairy policy. If you want only very large dairy farms, then programs that address price alone will achieve that result. But if you want an industry with opportunities for dairies of all sizes, you will need both a way to manage prices *and* a way to manage structure. Just to be clear, let's say it again—we need better prices for all farms, but we also need special programs aimed at the structure problem if we want smaller farms to be part of our dairy industry.



We are experiencing a massive structural shift in American dairy farming. Family-sized diaries are disappearing at shocking rates. Meanwhile, the number of very large dairies continues to grow.

Small & medium-sized dairy farms provide special benefits

When we lose small- and medium-sized dairy farms, we lose the special advantages they provide for rural economies, the environment, and food security. A recent report by Dr. Richard Levins looked into what other studies have said about the ways society benefits from family-sized dairy farms. Here are some highlights—you can read the full report at:

www.AlwaysFamilyFarms.com.

One of the reasons smaller dairies have special benefits requires little explanation or research; dispersing animals over many farms in a broad area is safer than concentrating them all in one area. A senior dairy economist with CoBank put it this way: "The largest risk with a densely concentrated milk supply is disease or natural disaster. A disease outbreak or natural disaster could quickly impact a much larger share of dairy production when it is concentrated in fewer farms."

A second, and related, benefit of smaller farms concerns the environmental impact of dairy farming. Concentrating the manure produced by, say, 100 80-cow dairies on the site of a single 8,000-cow dairy magnifies the environmental consequences of natural disasters and technical failures many times over. Furthermore, the manure from 100 80-cow dairies is often well balanced with crops grown for feed. The 8,000-cow dairy must transport manure from more distant crop farms or treat manure as a disposal problem. In the words of a 2017 report, "Livestock waste in these systems becomes an environmental pollutant rather than a recyclable resource contributing to soil health and fertility."

Community economics also favors smaller dairy farms. There is considerable evidence in the studies Dr. Levins reviewed that communities experience reduced economic vitality when they lose family-sized dairies. We must also be careful not to forget what one of those studies said: "lower numbers of cows in the area—and not simply increases in farm size—may actually represent the biggest threat to small-town agribusiness." As dairy farming becomes dominated by very few, very large, operations, the number of communities with virtually no dairies at all increases.

A Longer Term, Market-Based Policy

We need a dairy program that will wean producers from government payments and rely on market forces to manage both prices and structure. That is the intent of our "Dairy Farm Structure Management Program." Here is how the program would work: Establish a national Federal Milk Marketing Order (FMMO) with a $4.00 per cwt. price adjuster for up to one million pounds of monthly production for every dairy farm in the country.

The Federal Order system provides an established way to administer the Structure Management Program. Let's review the four goals set for the market order system:

- Insure orderly marketing of milk
- Improve income of dairy farmers
- Equalize bargaining power
- Assure an adequate supply of high quality milk

These goals make every bit as much sense today as they did when the Federal Milk Marketing Order system was created nearly 90 years ago.

The Federal Milk Marketing system uses "classified pricing" to set the price for milk. Classified pricing is a way to recognize the different values of finished dairy products made from the same milk. For example, fluid milk is priced higher than is milk going to a cheese plant. Here is the big question: If we can recognize the different values of finished products, why not recognize the different cost of the milk being produced?

A Real World Example

Now let's look at actual data for a real Federal Milk Marketing Order. I will use the Central Federal Order (Order 32) for June of 2018 as an example. In that month, the Order collected $244 million from sales of the different classes of milk products. The Order first paid farmers for components. Once that was done, $4.7 million was left to split up among farmers. This translated into a $.32 PPD for that month. All farms in the Order, if they had the same components, would have received the same price of $16.83 for their milk once the PPD was applied. (Keep in mind that this is before any adjustments cooperatives or buyers make that are outside of the FMMO system.)

When different sizes of dairies have different production costs, but we choose to pay them the same price regardless, we create the conditions for a serious structural problem like we have today. In the example we are using, the smaller dairies are pay for the privilege of milking cows while the larger dairies do well enough to stay in business and maybe even expand. **Based on the Central Federal Order June 2018 prices and the USDA's 2017 cost per size of dairy farm,** a 120-cow dairy has current margin of *negative* $2.53 per cow. At the other end of the scale, a 2,400 cow dairy has a current margin of *positive* $72.25 per cow. The larger dairies can easily underbid the smaller dairies for markets and thereby perpetuate the process of driving smaller farmers out of the picture altogether.

The situation I have described is the exact opposite in many ways of what the FMMO system was set out to do. Milk marketing is hardly orderly when we are losing so many dairy farmers in such a short period of time. The income of many dairy farmers is so low that they can't even cash flow, much less show acceptable results on a profit and loss statement. Bargaining power is anything but equalized when we have such large disparities in margins per cow. Recent years' "dumping" of milk in the Northeast and Mideast markets is clear proof of disorderly marketing conditions.

The Program Changes Things for the Better

Let's stay with the same example, but add in the Structure Management Program. We will use the exact same pool, run the exact same way, but add in the $4.00 premium for up to one million pounds produced by every dairy farmer in the Order. $4.00 per hundredweight is approximately the difference in cost the USDA shows between a small dairy operation and a very large dairy in their 2017 study. Using 2017 national estimates on herd size, I recalculated farm prices for the Central Order in June of 2018 by incorporating our proposed $4.00 for the tier one milk premium. By including our proposed change, instead of a $.32 PPD, the program gave a *negative* PPD of $1.64.

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Significantly More In Balance

This table details the impact of the proposed "Structure Management Program".

Size farm	Current Pay Price	Current Margin per Cow	Adjusted Price	Adjusted Margin per Cow
120 cows	$16.829	-$2.53	$18.869	$46.26
1000 cows	$16.829	$45.12	$16.9697	$48.33
2400cows	$16.829	$72.25	$15.7579	$47.83

- Margins based on USDA operating cost per CWT
- Using a 22800 pound cow annual average

The Structure Management Program works through the Federal Milk Marketing Order system to level the playing field among dairies of all sizes. In this example, price adjustments through the Orders balance margins in ways that provide opportunities for all dairy farmers, not just the very largest.

Dick Bylsma is the National Farmers Director of Dairy Marketing. Dick is a life-long dairy professional.

USDA's Continues Failing to Protect U.S. Organic Producers

by John Bobbe

Since February 2019, over 150,000 Metric Tonnes (over 6 million bushels) of "supposed organic corn and soybeans" have flooded U.S. markets. These shipments come from the "usual suspects" — Turkey and the countries surrounding the Black Sea. Result: U.S. organic farmers are seeing a price drop of $1.50 - $1.75 per bushel on corn.

The risk that at least some of these shipments are fraudulent is astronomical. If you can believe anything that comes out of USDA in Washington, D.C. these days, especially the National Organic Program (NOP) all these imports are legit. Not to worry, all those shipments' paperwork has been in order. Or is it?

On November 28, 2018 (as it has ever since 2016), the European Commission issued its annual memorandum "Guidelines on Official Controls on Products Originating from Ukraine, Kazakhstan, Moldova and the Russian Federation." The memorandum is effective for 2019. Much of the "organic" grain flooding U.S. markets is coming from these same countries. That EC memorandum requires rigid protocols on any shipments from those aforementioned countries.

On March 20, 2019, the Official Journal of the European Union issued a statement revoking accreditation of Control Union, a certification body based in the Netherlands. The Control Union revocation cited products, including grain, originating in the same countries as the European Commission, plus adding Turkey and United Arab Emirates.

Meanwhile here in the United States, the NOP is apparently looking the other way on "organic" grain shipments originating from these same countries.

I personally filed a formal complaint with USDA's NOP on the ship, Andalucia, which was scheduled to arrive in Moorhead, North Carolina. Subsequently, a similar complaint about the overall level of corn and soybean imports was lodged by a significant firm (based in the United States) that wants to see this import fraud mess cleaned up. The complaint noted that only half the amount of 150,000 MT of grain was shipped from the Black Sea region a year ago.

A subsequent investigation by a concerned farm group in North Carolina pointed to the USDA's NOP preventing Customs and Border Patrol (CBP) from inspecting the organic certificate and audit trail of this ship when it arrived in port. NOP reportedly gave the green light to unload the ship and asked CBP not to inspect the ship!

Since last September, I have personally reported information on suspicious ships of grain with quite specific information to USDA's NOP. But not a single ship to my knowledge was ever inspected. NOP's response in some cases was to push back as to why I suspected the shipments might be fraudulent. Control Union, the reported certifier in the Black Sea Region for many of these shipments, is still on the NOP's accredited list even though it has lost that accreditation in Europe. One has to ask, "Why"? The 2018 Farm Bill requires NOP to take action when a foreign government or agency acts on matters like revoking organic certifiers' licenses.

No secret: NOP is a weak link for enforcing organic standards on imports, when compared to Canada or the European Union. No organic farmer in the United States would ever get away with the excuse, "My paperwork is in order, no need for an annual inspection this year."

It is quite probable that NOP can't locate the Organic Farm Plans from farms supplying the grain for these shiploads and can't trace the grain back to the source. It is not reassuring that these shipments come from an area of the world where there is major civil unrest, war, massive corruption and forgery and fake "organic" documents are the name of the game. USDA's own Foreign Agricultural Service issued a report on the massive corruption in Turkish organics in 2016.

Meanwhile, protecting the organic integrity of markets for U.S. organic producers isn't much more than an NOP slogan. Producers are looking at major losses due to the flood of questionable imports from suspicious areas of the world thanks to the NOP. To date, NOP's response to my complaints and those of others questioning these shipments has been "total silence." That usually means a backroom deal has been struck to look the other way like in the past. To protect organic integrity requires real honest work, not playing paperwork and computer games with U.S. organic producers who stake their livelihood on organic integrity.

John Bobbe is the retired executive director of OFARM – a marketing agency for organic grain cooperatives.

Will USDA's AMS Blow Another $5M of "Organic" Funds?

by John Bobbe

The 2018 federal farm law again appropriated $5 million to the Agricultural Marketing Service (AMS), which includes the National Organic Program (NOP). The funds cover hiring additional staff and upgrading NOP's Organic Integrity Database (OID).

No one knowledgeable about organic agriculture's current situation will disagree that OID needs upgrading. The OID lists organic certification agencies accredited by USDA, certified organic producers and a host of other information.

In the 2014 Farm Bill under Title X, Congress appropriated $5 million to AMS for organic research and data collection. The purpose was quite vague — guised as increasing availability of organic data, generating new organic data, and hiring additional staff.

In fact, sources explain those funds were actually spent on staff and travel unrelated to organic work. A significant amount of that money was spent on a customized database, replacing an existing system primarily used for conventional agricultural and food data. Reports to this day are that hundreds of thousands of dollars are still being poured into that yet-incomplete database project, with little emphasis on organics. That evolving, new database is titled, Marketing Analysis and Reporting Systems -- acronym MARS. Over 95% of the data collected is not related to organic. To justify the project, a one-line checkbox as to whether the data is organic or other was added to a form.

However, the NOP appears to be relishing upgrading the database with the idea to help track things like organic grain imports that are shown to be fraudulent. Organic fraud, especially organic grain and vegetables, has cost U.S. organic producers hundreds of millions of dollars in losses due to depressed prices for what they sell. Organic consumers, who are paying good prices for what the USDA's organic certification process and seal are supposed to stand for, are also being defrauded.

Only in Washington, D.C. do they believe that someone sitting at a desk at USDA looking at a computer screen will substitute for boots on the ground for honestly investigating and policing to catch organic fraudsters and thus maintain organic integrity.

By playing computer games with a database, NOP is neglecting and putting off the real nuts and bolts hard work — developing the protocols to enforce the organic rules and catch those who game the system with fraudulent organic grain. Reports are NOP will only address this later in 2019, perhaps as late as November. Meanwhile, ships laden with supposedly "organic grain" keep sailing into U.S. ports. As Jenny Tucker, NOP administrator often likes to note, "The system is working, all the paperwork is in order." Ask any farmer about the currently depressed corn and other grain prices how paperwork will fix the red ink on their bottom lines.

Time will tell if the newly appropriated $5 million will be spent on organic data this time as intended, or squandered.

A Structured Management Program for America's Dairy Farmers, con't

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How did this adjustment impact prices paid to farmers of different size? The smaller farms saw a 12% increase in price while the price paid to largest farm in the pool was 6 % less. Once again, let me remind you that these results did not come from changing component values or total dollars in the pool. The only change was in the way available dollars were reallocated to level the production cost playing field among all farmers in the pool.

Here is the big change. The margins among farms of different sizes are more in balance! Both the 120-cow and 2,400-cow dairies have positive monthly margins, one at $46.26 and the other at $47.83. Notice, too, that the two margin numbers are very close to each other. That fact means farmers of all sizes now compete on the same level playing field. The bargaining imbalance that has allowed the very largest farms to drive out the smaller farms has been eliminated.

We Can Do This!

Two changes are needed before the Structure Management Program can meet its goals. First, we must eliminate what is called "depooling." Second, the Market Order System must cover all farmers in America.

Depooling occurs when a farmer is in a Federal Order, but jumps out when it is in his or her advantage to do so. The balance between, say, cheese prices and fluid milk prices, might favor a farmer staying in the pool when it goes one way, and getting out of the pool when it goes another. This loophole will have to be closed. Every farmer must play by the same rules all of the time.

The FMMO system does not currently cover every farmer in the country. If we don't fix that, farmers that don't benefit as much from the Structure Management Program can simply relocate to areas not covered by Orders. One fix: leave existing Orders alone and establish new ones for areas that are not presently covered. Another way is to establish a single national Order in which all farmers participate.

We Must Act Now

NFO recently commissioned a study of consumer preferences by the Minneapolis-based marketing group Eurofins. Ninety-three percent of consumers surveyed said it was important to support family farms. The advantages to food security, to the environment, and to rural economies that family-sized dairies provide are too valuable to lose. We need to give consumers a dairy industry that provides what they want, that is, a system that preserves and enhances the options for family dairies for generations to come.

Unfortunately, we are now on the exact opposite track. USDA projects fewer than 18,000 dairy farms by 2036. I have seen forecasts even bleaker than that. The approach we propose here can get us back on the right track and the future of one of our national treasures, the family dairy, will be secure.

No "Rabbit Out of the Hat" at Dean Foods'

by Pete Hardin

In early May, Dean Foods held its annual stockholders meeting – attendees would have been well-advised to wear black.

At that annual stockholders' gathering, and in the earnings conference call with investment analysts immediately prior, Dean Foods' management offered nothing new, no specifics on a possible purchase of the company or its subsidiaries. Earlier claims that management was pursuing "Strategic Alternatives" were left blank.

In recent weeks, Dean Foods' stock values have dropped as low as the "$1.60s" – i.e., in the $1.60 per share range. That's more than a 90% decline since early January 2017.

CEO Ralph Scozzafazza claimed incremental improvements in efficiencies were seen during 2019's first quarter. Further, he claimed that 2019's final three quarters would show continued improvement. That remains to be seen, as higher raw product costs (milk and butterfat) are clearly in the pipeline.

No talk of rumored interest by Saputo – the Canadian dairy processing giant. At this point, buyers interested in some or all of Dean Foods' assets are apparently waiting patiently on the sidelines, waiting to see what, if any, opportunities may be available in bankruptcy court.

Deam Foods' stock weathered the horrid day experienced by Wall Street on May 13 – climbing $.20/share, all the way up to $1.96.