



HOUSE COMMITTEE ON AGRICULTURE



Ranking Member Collin Peterson

Detailed Summary: The Dairy Security Act of 2011

Nearly three years ago the dairy industry was devastated by the combination of declining milk prices and escalating input costs. The dairy safety net did not work in 2009 and it won't work if similar events occur now.

The Dairy Security Act of 2011 will provide producers with a base level of margin security, give producers new flexibility to employ additional risk management strategies and create stability and inspire growth in the dairy industry while saving taxpayer dollars.

Creating a Stronger Safety Net

Dairy Producer Margin Protection and Dairy Market Stabilization Programs

Dairy producers will have the option to sign up for the basic margin program, helping them to better manage risk by addressing the gap between milk prices and feed costs. Producers that sign up for the margin program would then automatically be enrolled in the stabilization program which will alert producers when additional production may affect their overall margins.

The Dairy Producer Margin Protection Program will provide producers with options to best protect their margins, offering security they have not had in the past. The basic margin program would provide a floor for producer margins by providing a government funded catastrophic loss safety net for all producers. Producers may also elect to purchase additional coverage under a supplemental margin protection program.

The program calculates a producer's margin based on the difference between the all-milk price and the average feed cost. Each participating producer will have a milk production base – the highest annual milk production from the three years prior to implementation. This milk base will be fixed for the 5-year duration of the basic margin protection program. Under the supplemental margin program, producers will have the option to increase the coverage amount throughout the program's duration.

The Dairy Market Stabilization Program will help prevent extreme margin volatility for dairy producers by sending producers strong and timely market signals that do not currently exist. Those signals alert producers when additional milk production entering the market may have significant consequences on their overall margins. This program also takes into account the importance of export markets, allowing the industry to continue meeting increased worldwide demand.

The stabilization program is designed to act swiftly and infrequently to address brief market imbalances.

- When the actual national margin is below \$6.00 for two consecutive months, producers will receive payment for 98% of their base milk marketings and be subject to a maximum reduction in payment equal of 6% of current milk marketings.

- When the actual national margin is below \$5.00 for two consecutive months, producers will receive payment for 97% of their base milk marketings and be subject to a maximum reduction in payment equal of 7% of current milk marketings.
- When the actual national margin goes below \$4.00 in a single month, producers will receive payment for 96% of their base milk marketings subject to a maximum reduction in payment equal of 8% of current milk marketings.

USDA would be authorized to periodically conduct audits to ensure compliance with the program.

Under the proposal, a producer board will be appointed by the Secretary of Agriculture with the authority to purchase products through commercial sources for donation to food banks and other appropriate sources, as well as to conduct other activities that expand consumption and build demand for dairy products without duplicating activities by the dairy check-off.

Revising Federal Milk Marketing Order Pricing

The Federal Milk Marketing Orders provide substantial benefits to dairy farmers and milk processors by ensuring the equitable sharing of revenues generated by bottled milk sales, providing milk market information and auditing how milk is used in plants to ensure a level playing field among processors. However, in today's global marketplace milk pricing is too complex and results in unintended consequences.

The Dairy Security Act of 2011 simplifies the basic pricing system through a formal hearing process conducted by USDA. The proposal would change the way milk used to manufacture cheese (Class III) is priced, from a complicated end-product formula to a more market-oriented competitive pricing system. Milk used in the manufacturing of cheese is the single largest use of milk in the United States.

The legislation also directs the Secretary of Agriculture to hold hearings on eliminating the complicated end-product pricing formulas to determine minimum milk prices for the different classes of milk. The make allowances and yield factors built into these price formulas have become a major source of debate and division within the dairy producer and processor communities. Critics maintain that end-product pricing creates winners and losers in the marketplace and that requiring a minimum price puts dairy product manufacturers at a competitive disadvantage with areas not regulated by federal orders.

The bill directs the Secretary to replace end-product pricing formulas for Class III milk with a competitive milk pricing system through a hearing process. Cheese manufacturers will compete for a milk supply. A competitive price not only fairly compensates producers based on local supply and demand; it also reduces price volatility, encourages product innovation and allows manufacturers to compete domestically and internationally.

Replacing Current Programs

Current dairy programs are not addressing the realities of today's dairy industry, such as rising input costs and a growing export market. The Dairy Security Act of 2011 will eliminate the outdated programs outlined below.

The Dairy Product Price Support Program (DPPSP) was developed in 1949 to encourage milk production in the United States. It allows the government to purchase dairy products off the market and store them for future sale or use. However, the dairy industry looked drastically different in 1949 than it does today. Today, the export

market is a major driver of demand growth for U.S. dairy products and a key component of stronger milk prices. In this environment, interrupting the flow of U.S. dairy products to export markets by temporarily diverting those products to the government is detrimental to maintaining export markets.

The Milk Income Loss Contract Program (MILC) compensates dairy producers when domestic milk prices fall below a specified level. Today, the program pays producers 45 percent of the difference between the actual Class I base price and \$16.94, as adjusted by the dairy feed ration adjustment, and covers only 2.9 million pounds of a producer's milk per fiscal year. As witnessed in 2009, when prices are high but margins are low MILC does not provide an adequate safety net to producers. With increasing feed costs and shrinking margins, producers need a stronger safety net than these current programs can provide.

The Dairy Export Incentive Program (DEIP) pays cash bonuses to exporters, allowing them to sell certain U.S. dairy products at prices lower than the exporter's costs of acquiring them. USDA has not utilized this program and, in today's market, this program is outdated.

Summary

The current environment in the dairy sector is becoming very similar to what we saw leading up to the 2009 collapse. The dairy industry cannot wait for another crisis for Congress to do something to fix the broken dairy safety net. The Dairy Security Act of 2011 will provide a more effective, yet lower cost, safety net for dairy producers, a simplified milk marketing system for processors and an abundant and safe food supply for consumers.