Milk Regulation in North Carolina: More Than a Lot of Bull

Consumers are wondering why the North Carolina Milk Commission can't keep milk prices down. The Commission can play an essential role in regulation — if it is reconstituted.

By Noel Allen

Photo by Paul Cooper

In 1979, milk prices on the North Carolina grocery shelf increased at twice the national inflation rate. The jump pushed North Carolina's retail milk prices higher than those in almost every other state. At the same time, however, dairy farmers here were receiving about the same wholesale price for milk as were producers in neighboring states.

Noel Allen, a Raleigh attorney, is a Public member of the Milk Commission.

I have wondered about this disparity, both as a consumer who pays more and more each month and as a representative of the "public" on the North Carolina Milk Commission. For three years, as an attorney in the Antitrust Division of the North Carolina Department of Justice, I monitored Milk Commission activities, and for the past two years, I have served as a Milk Commissioner. From both perspectives I have seen that the people who milk cows are not necessarily the people who bilk the consumers.

There are five parties to milk marketing — producers, processors, retailers, consumers, and the Milk Commission. Of these five, small producers, small processors, small retailers and consumers have suffered most from government intervention in the market place. While the Commission has received most of the blame for high prices, the large operators have reaped most of the profits. Plain old price-fixing might have caused some of the problems, but a broader, more complex set of factors has pushed North Carolina's prices so high. Close scrutiny of the role of the Commission in the milk market can begin to unravel the mystery of milk prices.

The Milk Commission administers a price guarantee system for dairy farmers — the amount processors pay the producers — to insure an adequate milk supply. The Commission does not directly fix the price milk processors (middlemen) charge retailers nor the price the retailers charge the public. Thus, the Commission controls prices only on the first step of a three-tiered system.

To assure fairness of consumer prices, we appear to face two extreme options. Retail and wholesale prices would have to be either: 1) determined by supply and demand in a truly competitive market rather than one controlled informally by processors and retailers; 2) completely regulated by a Leviathan-like Commission.

The first option — a free market for prices — can work only if the Justice Department's Antitrust Division becomes an active and aggressive participant in the milk chain, as it has on occasion in the past.

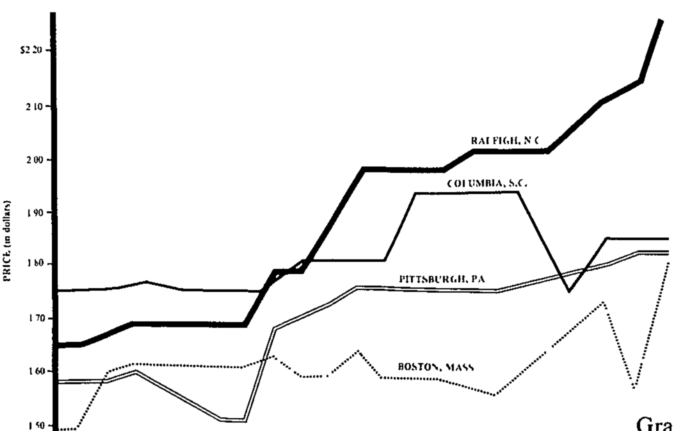
The second option — complete regulation — means unwieldly abandonment of the free market altogether, a step I philosophically oppose. Such an omnipotent Milk Commission would mean more power for government appointments and less reliance on the open market. The Commission might have to function more like the Utilities Commission, working full-time to regulate quasi-monopolies.

There may be a middle ground between abandoning the free market and losing control over the milk market to processors and retailers. The Milk Commission functions today in many ways the same as it did when it was created almost 30 years ago. Changes in Commission operations might equip this agency for regulating today's market conditions, if the Justice Department, at the same time, plays an antitrust watchdog role in the milk chain.

In the late 1940s and early 1950s, not everyone in North Carolina could get enough milk to drink; the state was consuming more than it produced. The technology of cold storage and milk processing had not developed sufficiently to insure that enough milk could come into North Carolina from other states. And when these states that were exporting milk underproduced, importing states like North Carolina suffered.

Some North Carolina leaders, including Gov. Kerr Scott (himself a dairy farmer at one time), felt that a price guarantee system for farmers could help minimize the risk of entering the high-investment dairy business. More dairy farmers would produce more milk, the lawmakers hoped, insuring an adequate supply to the consumer. By 1953, this sentiment prevailed, and the Milk Commission was established to "protect the public interest in a sufficient, regularly flowing supply of wholesome milk."

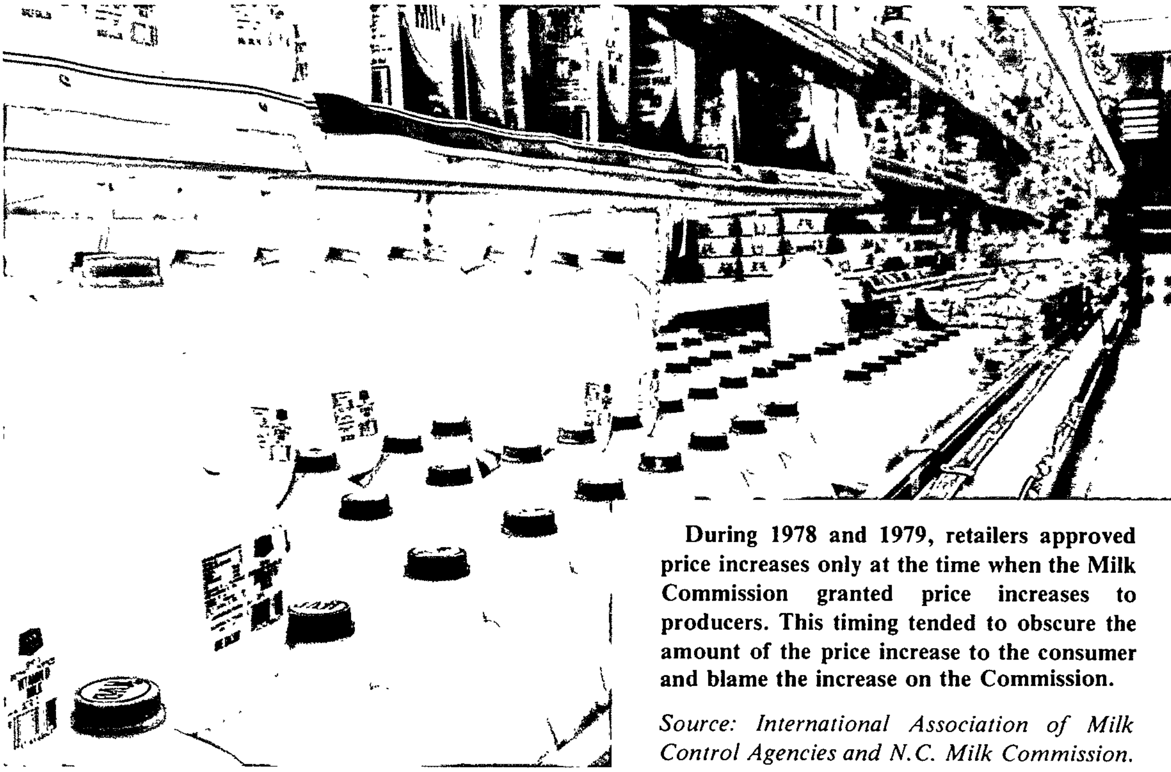
The Commission immediately established a guarantee minimum price to the dairy producer. In 1952, the year before milk regulatory laws were enacted, North Carolina farmers had produced 523 million pounds of Grade A milk, which grossed $32 million in income. Four years later, in 1956, North Carolina production had climbd to 750 million pounds of Grade A milk, a 43 percent increase in in-



RETAIL PRICE OF A GALLON OF WHOLE MILK

Source: International Association of Milk Control Agencies and Supermarket Milk Price Survey.

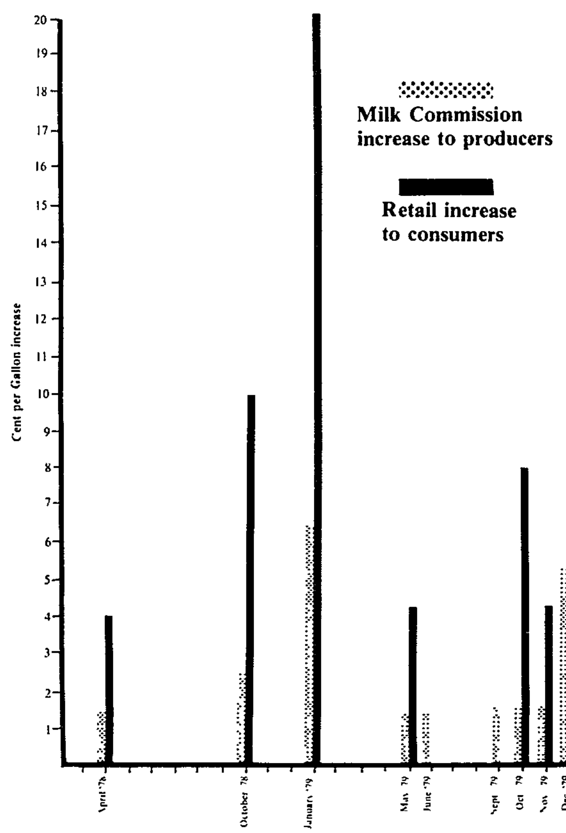
Graphs prepared by Paul Ridgeway for *N.C. Insight*



During 1978 and 1979, retailers approved price increases only at the time when the Milk Commission granted price increases to producers. This timing tended to obscure the amount of the price increase to the consumer and blame the increase on the Commission.

Source: International Association of Milk Control Agencies and N.C. Milk Commission.

COMPARATIVE PRICE INCREASES



state production. Gross income increased 38 percent to over $44 million.

The Milk Commission's purpose seemed to have been fulfilled in just four short years. No longer would anyone in North Carolina have to go without milk since the supply was now plentiful. But another transition was beginning at the same time: the number of milk producers was decreasing rather than increasing, contrary to what the legislators creating the Commission had assumed would happen. An era of consolidation was beginning. The number of Grade A milk producers in the state hit a peak of 5,137 in 1954. Today, there are only some 1,200 producers left.

One goal of the original legislation was reached — the state became a surplus producer of milk. But another function of the Commission — to help more dairy farmers survive — was not realized. The price guarantee system effectively insured more income to fewer and fewer dairy producers.

Many of the circumstances which prompted the creation of the Milk Commission in 1953, have changed dramatically. The state has become a surplus producer. Technology now allows transportation of more kinds of milk products over longer distances and accomodates longer shelf-life in the grocery.

But comparatively little has changed since 1953 regarding the basic regulatory scheme. The Commission still does not set the retail price, for example. Perhaps most importantly, the Commission has not flexed its regulatory muscle over the growing hegemony of the large producers, processors, and retailers.

The Milk Commission, since its inception, has never lacked for statutory authority. The Commission can regulate just about everything with regard to milk except the temperament of the cow. It can set the price to the consumer, to the producer, to the processor, and to other states. It can "investigate all matters pertaining to the production, processing, storage, distribution, and sale of milk." It has broad subpoena and investigatory powers and even has access to "all places where milk is processed, stored, bottled, or manufactured into food products."

But the Commission, for a variety of reasons, has not used its power to set retail prices. Whenever the Commission has come close to setting a retail price, public opposition has beaten the proposition back. But ironically, the public rarely appears at hearings on more complex matters, such as regulating the other aspects of milk marketing, which might ultimately have a greater impact on the retail price itself.

As presently established, the Commission is essentially subservient to the industry it is supposed to regulate, functioning like a trade organization at times. The industry funds its own regulation, assessing milk producers and processors three cents per 100 pounds of milk for the Commission's $400,000 annual budget. Learning the intricacies of the milk industry is difficult for the five public members of the 10-member Commission. The industry representatives, on the other hand, work in the trade full-time and have resources within the industry they represent.

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The Commission's public members have a high turnover rate. The $15.00 per diem for serving on the Commission offers no incentive for remaining on the Commission long enough to learn the complexities of milk regulation. But industry representatives develop much greater longevity on the Commission, due in part to self-interest and recognition within their industry. The Commission meets only one or two days a month. Inevitably, full-time industry employees, attorneys, and lobbyists dominate the testimony at public hearings. In the past two and one-half years, only one appearance was made in behalf of the "using and consuming public."

As now constituted, the Milk Commission regulates prices beyond the producer level (the first pricing tier) only with regard to bulk transfers and below cost sales. To curtail anticompetitive and unfair practices beyond the producer level, the Commission should depend on the powers of the Justice Department's Antitrust Division. But last year a majority of the Commission refused to request an investigation by the Antitrust Division into retail pricing.

The Attorney General has the specific duty and power to investigate potential violations of the antitrust laws (Chapter 75, N.C. General Statutes), which would include price fixing, restraints of trade, and predatory pricing. Justice Department officials feel such actions in the milk industry are virtually impossible, however. "They (the processors and retailers) can gouge all they want to, and we can't do a thing about it unless they agree to gouge together and we can prove it," says H. A. Cole, Jr., director of the antitrust division. "It's extremely difficult to prove."

But the Antitrust Division has overcome such difficulties before. In 1974, the Division, led by Deputy Attorney General Jean A. Benoy, filed a suit

Who Appoints The Commission?

The composition of the Milk Commission has varied considerably since its beginning in 1953. The changes are listed below. Since the last change in 1975, all new commission members are appointed for four-year terms, which are staggered. Commissioners can succeed themselves, and each year the Commissioners choose the chairman from among themselves. As now constituted, the Commission is appointed in this manner:

Governor (3) — two public members, one retailer;
Lieutenant Governor (2) — one public member, one producer;
Speaker of the House (2) — one public member, one processor/distributor;
Commissioner of Agriculture (3) — one public member, one processor/distributor, one producer.

Commission Membership:

1953-55 (7): 2 producers
2 distributors
1 public
1 retailer
Commissioner of Agriculture, *Ex Officio*

1955-71 (9): 2 producers
2 distributors
3 public
1 retailer
Commissioner of Agriculture, *ExOfficio*

1971-75 (7): 5 public
1 producer
1 distributor

1975-present (10): 5 public
2 producers
2 distributors
1 retailer

alleging that nine processors in North Carolina rigged bids to school systems. In a consent decree, the Defendants (all nine processors) agreed to submit copies of their bids for the school systems to the Department of Justice for review. In the year following the settlement of the case, when inflation hit 10 percent, the price of milk to public schools in the state declined by 10 percent. The Justice Department undertook this antitrust action without cooperation from the Milk Commission. More recently, after large and uniform leaps in retail milk prices, newspapers reported that the Antitrust Division was "monitoring" the situation. Within weeks, retailers dropped their prices 26 cents per gallon. Even then, however, the various retailers seemed to make the reductions at the same time and at equal rates.

A revamped Milk Commission that would function more independently could at least cooperate with aggressive Justice Department investigations. And hopefully, such a Milk Commission could address the alarming trend within the industry toward concentration. Indeed, only one-fourth the number of producers in business when the regulations were passed are still producing milk. And today, there are about 20 processors for the entire state while a generation ago practically every town of any size had its own dairy. The concentration of production into the hands of a single milk cooperative even looms as a possibility.

Photo by Paul Cooper

Today a single milk cooperative, Dairymen, Inc., controls some 40 percent of the milk production in the state. Based in Louisville, Kentucky, Dairymen has grown from a small group of farmers who pooled their milk so they could have more bargaining power with processors into a region-wide organization that now controls 70 percent of the milk production in the southeast. The fact that North Carolina does have a Milk Commission might have prevented Dairymen from controlling even more milk production here since the Commission does regulate the price paid to the producer. This guarantee minimum price, no doubt, allows some producers to compete without having to join Dairymen. But Dairymen claims that farmers can get greater utilization of their milk — having more milk classified as Class 1 milk, for example — by joining the cooperative and pooling their produce with other members.

In states that do not have milk commissions, federal regulations have been so weak as to allow virtually complete control of milk production by a single cooperative such as Dairymen. Moreover, federal antitrust laws exempt cooperatives such as Dairymen, Inc. from price fixing prohibitions.

Cooperatives like Dairymen have not limited their growing control of the milk market to the producer level. Vertical integration through the milk cycle is a growing problem with which the Milk Commission is having to cope. Last year, for example, a processor appeared before the Commission regarding milk it sought to have transported in bulk from North Carolina to Georgia. In Georgia, this processor's plants were entirely dependent upon Dairymen, Inc., for their milk. But the processor was competing with Flav-O-Rich, a processor company owned entirely by Dairymen. Dairymen was supplying Flav-O-Rich, their own processor, but apparently had stopped supplying the competing processor, an action which could corner a still larger share of the processing market. The Georgia-based milk dispute not only required the North Carolina Commission to involve itself in that individual incident. It also foreshadows what may become a similar pattern within this state as vertical integration increases.

I believe the Milk Commission can be a viable regulatory agency in preserving some pricing fairness and helping to prevent retail prices in North Carolina from topping the national index.

But a commission established nearly 30 years ago must go through some major alterations. I have suggested nine possible reforms of the Commission (see box) which can begin to address the factors now controlling our retail milk price. The wisdom of the 1953 General Assembly, it seems, has helped assure an adequate supply of milk to North Carolina. But more actions are needed to keep consumers fairly served, which was the primary goal of the legislation establishing the Milk Commission in the first place. ■

Editor's note: In proposing reforms for the Milk Commission, Mr. Allen writes as a private attorney and as a member of the Commission. His views are not necessarily those of the Center for Public Policy Research. An equally forceful call for reform might suggest a broader regulatory function for the Commission.

Suggested Reforms

1. The membership of the Commission be increased to 12 by adding two additional public members.
2. A "public staff" be carved out of the existing Commission staff to represent the using and consuming public, similar to the Public Staff of the Utilities Commission.
3. A staff attorney of the North Carolina Department of Justice should be designated to serve as a liaison between the Milk Commission and the Department of Justice. The Department of Justice could then assist in forcing fair and open competition in the marketing of milk.
4. The terms of all members of the Commission including industry representatives should be limited.
5. The producer price of milk should be made more dependent upon a rate of return factor, rather than arbitrary comparisons with other states and inflation indexes.
6. The Commission's authority to fix prices should be limited to setting minimum prices at the producer level. Authority to fix prices on the wholesale and retail levels should be repealed.
7. Industry representatives, who lobby the Commission should be required to register as lobbyists.

North Carolina Milk Commissioners

Herbert C. Hawthorne, 63, Chairman, public member. A North Carolina native, Hawthorne is a cotton broker and partner in the Statesville firm of Greer Cotton Co. He worked for the N.C. Highway Patrol (1939-45) before joining Greer Cotton in 1946. Gov. Scott appointed Hawthorne in 1971; Commissioner of Agriculture Graham reappointed him in 1976. His term expires in 1980.

Noel Allen, 32, public member. An attorney since 1973, Allen worked in the N.C. Department of Justice Antitrust Division before going into private practice in Raleigh. He has also been an English instructor, a curriculum consultant, an adjunct law professor, and a Carter for President coordinator. Appointed in 1977 by Gov. Hunt, Allen's term expires in 1981.

Inez Myles, 34, public member. A New York City native, Ms. Myles now lives in Henderson. She has been Executive Director of the N.C. Senior Citizen's Federation since 1974. She worked previously for Franklin Vance Warren Opportunities (1973-74), N.C. State Economic Opportunity Office (1970-73), National Accounting and Management Association (1969-70), and Shaw University (1968-69). Appointed by Gov. Hunt in 1977, her term expires in 1981.

Norma T. Price, 46, public member. A homemaker and active volunteer, Mrs. Price serves on the Asheville City Council. She has worked for Duke Power Company (1954-58), Transylvania County Schools (1959-60), and Argonne National Laboratories (1960-61). Appointed in 1980, by Speaker of the House Stewart, she is completing a term that expires in 1982.

Vila M. Rosenfeld, 52, public member. Chairman of the Home Economics Education Department at Eastern Carolina University at Greenville. Dr. Rosenfeld has also taught at Penn State, Kansas State, Murray State, and the Virginia secondary schools. Appointed in 1975 by Lt. Gov. Hunt and reappointed in 1979 by Lt. Gov. Jimmy Green, Rosenfeld's term expires in 1981.

Oren J. Heffner, 55, retailer. A North Carolina native, Heffner operates supermarkets in Forsyth, Davie, Davidson, and Yadkin Counties. Previously he was in the U.S. Air Force (1943-46) and worked for Heffner and Bolick Grocery (1946-51). Appointed in 1975 by Gov. Holshouser and reappointed in 1977 by Gov. Hunt, his term expires in 1981.

Russell Davenport, 70, processor/distributor. A South Carolina native now living in Fayetteville, Davenport and his family own the Sycamore Dairy. Prior to beginning work at Sycamore in 1945, Davenport worked for the N.C. State Dairy Dept. (1932-34), as an Agricultural Extension agent in Anson County (1934-39), and as a county farm agent (1939-45). Appointed in 1975 by Speaker of the House Green and reappointed by Speaker Stewart, Davenport's term expires in 1983.

William E. Younts, 59, processor/distributor. Younts is the General Manager of Long Meadow Farms of Flav-O-Rich in Durham. He earlier worked for Montgomery Dairy and served in the Army. First appointed in 1972 and reappointed by Commissioner Graham in 1976, Younts' term expires in 1980.

B. F. Nesbitt, 62, producer. A former Air Force pilot, he has been a dairy farmer since the late 1940s. He lives in Fletcher, near Asheville, where he has worked with local government issues. Appointed in 1965, Nesbitt has been reappointed several times, most recently by Commissioner Graham (1976-80 term).

David A. Smith, 42, producer. Smith is a life-long dairy farmer from Lexington. He has worked closely with Coble Dairy, as a producer and a member of the Board of Directors. He has also been Chairman of a Soil and Water Conservation District. Appointed in 1975 by Lt. Gov. Hunt, he was reappointed by Lt. Gov. Green (1978-82 term).