

The

New Look • New Size

Milkweed



Dairy's best information and insights

Issue No. 345, April 2008

--Huge Losses Totaled \$109,277,000 in '07

DFA (Enron of the Dairy Industry): "10 Years and Crumbling"

by Pete Hardin

Small wonder that copies of the 2007 financial audit were impossible to find at the March 17-18 annual meeting of Dairy Farmers of America in Kansas City, Missouri. (DFA is the nation's largest milk producers' cooperative).

The theme at DFA's 10th annual meeting was, "10 Years and Building." More accurately, the theme should have been: "10 Years and Crumbling." DFA's audit reported huge financial losses and the shocking financial condition of its biggest subsidiary – National Dairy Holdings (NDH). NDH lost \$134.2 million in 2007. That figure does not include another \$25 million infused by DFA at the end of the third quarter to cover a loan default by NDH.

DFA reported net losses of \$109 million dollars for its fiscal year ending December 31, 2007. That's the biggest financial loss ever reported by any U.S. dairy cooperative. That figure was a net of nearly \$144.8 million in losses written off during fiscal 2007. The difference between the \$144.8 million in write-downs and the \$109 million net loss was buffered by profits from other DFA internal operations. Spread over DFA's 10,587 dairy farmer members, the 2007 loss equals just over \$10,000 per member farmer.

Those losses constitute DFA's first-ever financial loss during its decade. Not to worry! DFA CEO/President Rick (alias, "Tricky Rick") Smith and Board Chairman Tom Camerlo presented happy faces in their "Letter to Our Members" accompanying the audit. Smith and Camerlo claimed that DFA's internal businesses "had a strong year – in fact our best ever." Smith and Camerlo further proclaimed that "... DFA's financial outlook has never been better."

It's hard to see how DFA's internal businesses "had a strong year" when NDH lost \$63.5 million just in the fourth quarter, after DFA was forced to put NDH's catastrophe financials on to DFA's books.

Can DFA recover from the "Hanman Years"

DFA management is now sorting through its collection of subsidiaries and joint ventures at a time of tremendous financial pressure, both within

the dairy industry and in general.

DFA was formed in late 1997 by merger of four dairy cooperatives. Gary Hanman, then CEO/president of Mid-America Dairymen (DFA's predecessor), engineered the merger and ran DFA as his own creation for the first eight years.

Three of the four original co-ops merged into DFA were in very weak financially: Mid-Am, AMPI Southern Region, and Western Dairymen's Cooperative, Inc. To pull in the fourth co-op – Milk Marketing, Inc. (which had solid equities) – a deal was cut to make MMI's egocentric president Herman Brubaker DFA's first board chairman. But DFA has been all about the stumpy Hanman and his trademark red suspenders. No head of a major dairy entity molded the organization to his tastes like Hanman did for DFA. Under Hanman, DFA became a "cult" directed by and feeding Hanman's coercive personality.

Hanman built DFA into an ill-fitting empire, using questionable mergers and forced acquisitions. Those that didn't succumb to the charms were dragged in against their will. DFA's "yes, yes" boards were filled with Hanman's hand-picked and custom-fertilized "mushroom directors."

DFA remains "Hanman's Baby," even though Hanman was finally shepherded into retirement in December 2005. In summer 2005, Rick Smith had warned DFA's board that Hanman had to go if the co-op were to survive financially. Sorting through Hanman's money-losing collection of businesses and dealings is now "Tricky Rick's" baby. (Rumor mill: Hanman still goes to work at DFA's headquarters in Kansas City about three days a week.

DFA's \$109 million loss in 2007 symbolizes the start of the great task of "taking apart" the Hanman era. The total of \$144.8 million in reported write-downs is just the initial reckoning for costs associated with many years of DFA's manic growth propelled by neither reason nor business sense. Joint comments by Smith and Camerlo in the 2007 DFA audit stated that the losses were due to "non-recurring write downs." YES, *those* specific losses won't reoccur. But more severe write-downs from other subsidiaries' losses loom, unless DFA can reverse NDH's \$134.2 million tide of red ink last year.

'07 audit confusing – changes in '06 numbers

Normally, a financial audit provides a comparison of the most recent financial year to the previous year. In the case of DFA's 2007 audit, there were so many unexplained changes in the data from the prior year (2006) that, instead of comparing "apples to apples," analyzing DFA's 2007 finances versus 2006's results is more like comparing an apple to some form of vegetable. Example: DFA backdated some \$25.7 million of write-downs for plant closings that occurred in 2007 against 2006's financial results. BUT ... DFA never restated the bottom line of 2006's net earnings (\$34.377 million) in its 2007 audit. How can the co-op write off another \$25.7 million against a prior fiscal year and still report the *same* bottom line as one year ago? Enron-style accounting, that's how!

More analysis of DFA/NDH finances on pages 4-5