Non-compete agreements

By Andrew Malec, Ph.D.

Non-compete clauses are provisions in employment agreements that restrict employees from working for a competing employer for some period of time after their employment ends. From 2000 to 2008, the number of court cases involving non-competition agreements nearly doubled,[1] which has raised concern at the Federal Trade Commission ("FTC"). On January 9, 2020, the FTC held a public workshop in Washington, D.C. to assess whether it should restrict the use of non-compete clauses in employment agreements. The workshop focused on the growing use of non-compete agreements by employers across industries, whether the use of these agreements is anti-competitive, and what authority the FTC has to regulate the use of these agreements in the labor market.[2]

For the most part, panelists were in agreement that there is no legal or business justification for the use of non-compete agreements for low-wage/low-skill workers (e.g., fast food workers, dog walkers, etc.) and cited evidence that such agreements resulted in depressed wages, diminished labor mobility, and limited employee bargaining power. It should also be noted that the rate of use of non-compete agreements in states where they are unenforceable is similar to the rate of use in states where they are legal, which led panelists to state that low-wage workers are unfamiliar with state laws governing their employment agreements and/or unable to hire counsel to advise them of their rights.[3] In fact, a recent study found that banning non-competes for low-wage workers in Oregon increased hourly wages and job mobility.[4] However, it is unclear whether the FTC has the authority to address non-compete agreements through rule-making.

In contrast to the effects on low-skill/low-wage workers, panelists noted that studies also show that non-compete agreements may benefit other types of high-skilled/highly-compensated employees (e.g., CEOs and physicians). According to Lexology, economists on the panel believe that a ban on non-compete agreements would be difficult for the FTC to justify and noted that more research is necessary to determine whether the potential anti-competitive effects of non-compete agreements (e.g., stagnant wages, lack of mobility in the labor market, and limited employee bargaining power) outweigh any potential benefits (e.g., incentivizing employees to invest in training and protecting trade secrets).

While the merits of non-compete agreements are being debated at the FTC, our firm is routinely asked to assist with economic damage quantification/expert witness testimony on non-compete and trade secret litigation.

A typical litigation matter for which we are asked to assist is where a sales representative who has signed a non-compete agreement leaves his employer, joins a competitor, and competes with the prior employer. In this example, plaintiff's economic expert will often quantify plaintiff's lost profits.

We also see situations where an employee starts a business and directly competes with their current employer by utilizing misappropriated trade secrets to divert customers from their current employer to their newly formed entity. In this case, it is typical to see a plaintiff's expert compute defendant's profits to ascertain the profits that the plaintiff would have garnered had it not been for the actions of the defendant.

Litigation involving theft of confidential information is another area for which we are asked to assist. It is common to see matters where confidential information has been taken by a former employee; however, that information has not yet been utilized at the new employer. In this case, one cannot compute defendant's profits. It is also speculative to compute plaintiff's lost profit. However, it does not mean that those trade secrets do not have value. At a minimum, they are worth the cost to recreate the asset (e.g., blue print or business plan).

It is unclear what authority the FTC has in regulating non-competition agreements. In the current state, non-compete litigation is prevalent. It is also common to see litigation where there are breach of the non-competition agreement and trade secret misappropriation claims since, in many instances, it is alleged that a former employee has taken trade secret information to get a "head-start" at the new employer. While lawmakers and the FTC wrestle with the idea of restricting the use of non-compete clauses in employment agreements, there is no doubt that we can expect to see more litigation in this area.

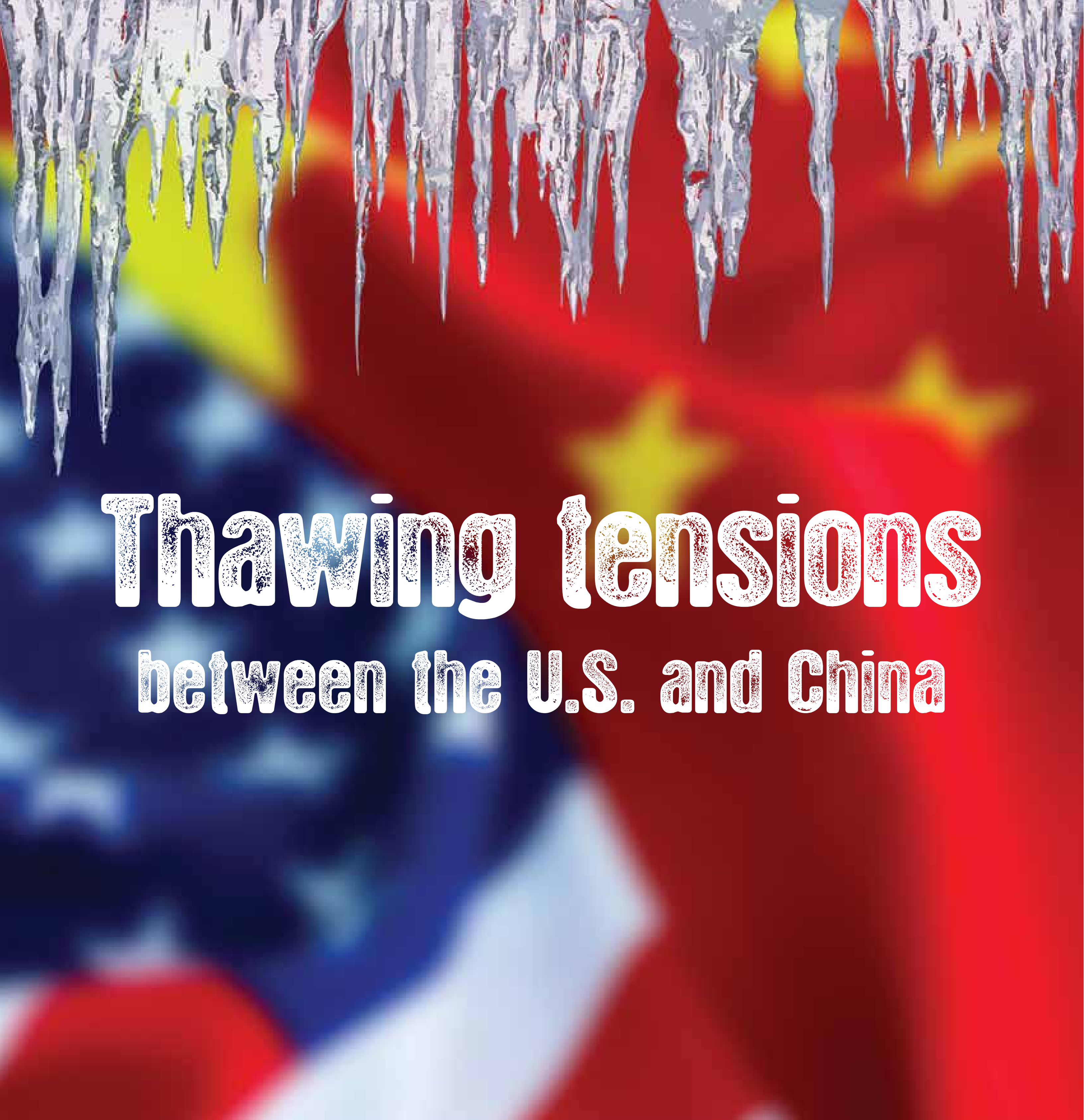
1 Starr, Evan, "The Use, Abuse, and Enforceability of Non-Compete and No-Poach Agreements," *Economic Innovation Group,* February 2019.

2 "Key Takeaways from the FTC's Noncompete Workshop," *Lexology,* January 19, 2020.

3 Ibid.

4 Lipsitz, Michael and Evan Starr, "Low Wage Workers and the Enforceability of Non-Compete Agreements" (December 9, 2019). Available at SSRN.

Andrew Malec, Ph.D. *Partner and Managing Director, is the firm's chief economist and head of O'Keefe's Intellectual Property ("IP") Practice Group. He is a recognized expert in providing economic advisory services, litigation support, and valuation opinions.*



Thawing tensions

between the U.S. and China

***Anson Smuts** CMA, CFE, CVA, Director and Senior Economist, utilizes his accounting and finance expertise in mergers and acquisitions, business valuation, intellectual property, and data analysis to identify strategies for business growth and development.*

By Anson Smuts

On January 15th, the United States and China signed a trade agreement including several commitments related to intellectual property ("IP") protection, signaling a weakening of tensions between the two countries. In addition to the commitments related to IP, China agreed to purchase $200 billion worth of U.S. goods and services over the next two years. Yet the dispute is not over. The agreement between the countries did not remove all tariffs, with President Trump stating that certain tariffs will remain until the next round of negotiations are successful – and for good reason.[1] While few can disagree with the need for an agreement between the two countries, the underlying details reveal that the origin of the dispute is far from settled.

Taking a step back, the trade dispute began in August of 2017 when the United States Trade Representative ("USTR") initiated an investigation under Section 301 of the Trade Act of 1974 into "China's laws, policies, practices, or actions that may be harming American intellectual property rights." Section 301 allows for the use of trade sanctions to protect IP rights. Subsequent to the USTR's report, tariffs were imposed upon China, which for years has been accused of demanding the transfer of IP rights from foreign firms seeking to gain access to the Chinese market. A 2015 paper by the Federal Reserve Bank of Minneapolis found that this quid pro quo policy had resulted in more than half of all technology owned by Chinese firms being obtained from foreign firms.

Estimates of the dollars lost as a result of Chinese IP practices are equally staggering. A 2011 report by the U.S. International Trade Commission estimated that total annual losses due to IP infringement in China were $48.2 billion, of which $36.6 billion represented lost sales, $11.6 billion being lost royalty or license payments. The majority of these losses related to either copyright or trademark infringement. A 2013 report by the National Bureau of Asian Research ("NBAR"), a nonprofit based in Washington DC, estimated the losses due to IP theft to be far higher, over $300 billion globally, with China allegedly being responsible for up to 70% of those losses.

The agreement struck in January 2020 contains notable wins for U.S. companies to begin addressing these issues. The agreement states "specifies improvements in trade secret protection; strengthening pharmaceutical-related Intellectual Property; granting patent term adjustments and extensions; preventing piracy and counterfeiting on e-commerce platforms; increasing transparency in geographical indications protection; preventing manufacture and export of counterfeit goods; stopping bad-faith trademarks; and increasing bilateral cooperation on Intellectual Property protection."[2] Notably, the agreement includes a requirement that China end the practice of directing its domestic companies from acquiring foreign technology, especially where such an acquisition would harm American interests. China also agreed to end any practices which would force American companies to transfer IP in joint ventures with Chinese counterparts.[3]

These requirements provide optimism that the agreement is a step in the right direction. Yet a focus upon China's behavior outside of the deal paints a less optimistic picture. Subsequent to the initiation of the trade dispute in August 2017, the USTR has released further reports detailing its findings of Chinese practices related to IP rights and protections. In March 2018, the investigation of China's policies found that promises have been made and broken before, stating: "On at least eight occasions since 2010, the Chinese government has committed not to use technology transfer as a condition for market access and to permit technology transfer decisions to be negotiated independently by businesses... The evidence adduced in this investigation establishes that China's technology transfer regime continues, notwithstanding repeated bilateral commitments and government statements."

A November 2018 update from the USTR relating to the investigation stated "China's acts, policies, and practices related to forced technology transfer in China persist" and "China shows no sign of ceasing its policy and practice of conducting and supporting cyber enabled theft and intrusions into the commercial networks of U.S. companies."

While the recent agreement between the U.S. and China is a step in the right direction, the battle is far from over. The decrease in tariffs implemented by the U.S. and the commitment by China to purchase U.S. goods and services will temporarily appease the two parties, and perhaps gestures of good faith will spur incremental improvements. However, the U.S. will eventually want to see structural change in China's treatment of IP rights and protections and China will want an end to U.S. tariffs altogether. If you're waiting for both sides to get what they want, don't hold your breath. This will be a long process to stem the tide of unfair trade practices.

[1] https://www.wsj.com/articles/u-s-china-to-sign-deal-easing-trade-tensions-11579087018

[2] https://www.natlawreview.com/article/china-makes-significant-commitments-to-improve-intellectual-property-protection

[3] https://www.nytimes.com/2020/01/14/business/economy/trump-china-trade-deal.html?searchResultPosition=2

CECL THE NEW FRONTIER

By Matthew Rizzo

Matthew Rizzo ***CPA, CVA, Director, has business valuation expertise in various types of transactions including, but not limited to mergers and acquisitions, shareholder disputes and gift tax valuations.***

The new Current Expected Credit Loss ("CECL") standards issued by the Financial Accounting Standards Board ("FASB") officially went into effect January 1, 2020 for large public financial institutions. FASB issued the new standards as a result of historically insufficient allowances for credit loss reporting. Public Business Entity non-filers will not have to implement the new CECL rules until December 15, 2020. All other financial institutions will have to comply after December 15, 2021.[1]

Three large financial institutions have reported the impact of the new CECL standards and so far, credit card divisions are the main drivers in the large increase of loss allowances.[2] The new reporting of CECL requires: (1) financial institutions to take an allowance approach as opposed to a direct write-down of the amortized cost basis, (2) a fair value floor for credit losses as opposed to credit losses exceeding total unrealized losses, and (3) allowances for full or partial reversals of previously recognized losses (rather than no immediate reversals under the old standards).[1] The new standards require a CECL account which is technically a valuation based account "measured as the difference between the financial assets' amortized cost basis and the amount expected to be collected on the financial assets (i.e., lifetime credit losses)."[1] The implications of this new standard could have a dramatic impact on financial institutions' balance sheets which could affect stock prices as price to book value is often the main metric used in valuing financial institution stocks. The CECL estimation process is still up for interpretation and will most likely vary by financial institution as no standard estimation formula exists. Each financial institution will have its own methodology that is required to be well documented and disclosed. A major addition that the CECL requires is loan losses are to be estimated over the entire life of the loan from when it is initially booked. The new standards will require a lot of forward thinking relative to each loan type and risk profile.

A looming question remains. Will these new standards incentivize financial institutions to not book loans at year end when it could conceivably book a loss (in the form of a reserve) greater than the income earned in the period? Financial institutions heavily monitor their balance sheets in order to maintain or elevate their stock prices which would certainly point to financial institutions managing their year-end portfolios with care.

Another concerning issue is what the impact of the new CECL standards will be during impending troughs or recessions in the economy where loan losses are perceivably greater than expectations. Also, will there be any penalties imposed by the SEC for large misses? CECL will be beneficial in stable economic times, but technically so were the original threshold-based standards. The real concern is whether these new standards will help stakeholders determine financial stress in these institutions. The determining factor lies in the ability of these financial institutions to estimate accurately under these new standards, which remains to be seen.

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1 https://www.federalreserve.gov/supervisionreg/topics/faq-new-accounting-standards-on-financial-instruments-credit-losses.htm

2 Biery, Mary Ellen; "Voices First look: Large SEC filers begin reporting CECL's impact." *Accounting Today,* February 3, 2020

Roles of the Financial Advisor during a Business Reorganization.

By Keith Chulumovich

Keith Chulumovich CPA, Managing Director, specializes in strategic and operational planning, business analysis and financial reporting, process improvement, turnaround/ profitability improvement initiatives, and management of operating budget and forecast planning cycles.

Aside from some of the roles listed, Financial Advisors may be engaged by creditors' committees to assist in their primary role of representing the overall interest of unsecured creditors.

O'Keefe's professionals have successfully managed and partnered with leading law firms, trustees, and receivers to develop litigation strategies and support the litigation process as an expert and the bankruptcy process as a financial advisor/Chief Restructuring Officer. In addition, we have represented numerous middle market companies to improve operational and financial performance, resolve problematic capital structures, and purchase and sell portfolio companies.

Most of us have heard the term Financial Advisor or "FA" and somewhat know what that means. For better or worse the term covers a broad range of services, duties, and responsibilities and this range of services can differ depending on the life cycle of the business involved.

When a company is doing well and needs some help getting to the next level, financial advisors are often brought in to develop long-term strategic plans, analyze pricing and profitability of products and services, provide both buy-side and sell-side acquisition due diligence, offer transitional support, and other services.

When a company is struggling and going into either an out-of-court restructuring, bankruptcy reorganization, or liquidation, the role of the financial advisor takes on a different tint. In these instances, financial advisors are deeply mired into the root causes of a troubled company's stress, looking at issues both strategically and tactically. From a strategic perspective, their task is to quickly determine the key drivers of a company, flushing out the root causes of its current distress and the feasibility, likelihood, and timing for fixing the problem(s). Tactically, turnaround advisors spend a great deal of their time managing cash and working to first stabilize and then improve operations.

Out of court, the financial advisors may act as CEO, CFO, or CRO (Chief Restructuring Officer), taking actions to stabilize the company financially. In addition to this financial stabilization, the role could include the divestiture of assets or businesses, the restructuring of old debt, securing new debt, cash flow management, process and performance improvement, coordination of vendor and creditor negotiations and communications, both internally and externally.

The role of the FA in "In Court" reorganizations is similar to those in an out of court restructuring but there are quite a few more added nuances. Prior to any chapter 11 or chapter 7 filings, an FA may be involved in either an assignment for the benefit of creditors ("ABC") as an "assignee" or a receivership (as a "receiver"). Both of these scenarios are usually governed by State jurisdictions, many of which mirror Federal Bankruptcy rules and regulations. FAs may also be trustees or hired by the trustee depending on the needs of the case.

Chapter 7 Trustee
The trustee will marshal and liquidate the assets of the business entity and then distribute the liquidation proceeds to the creditors after paying the administrative costs and other priority payments under the Bankruptcy Code. The chapter 7 trustee rarely continues to operate the business.

Assignee (ABC)
Similar to a chapter 7 trustee and responsible for liquidating the assets of the business at maximum value and distributing proceeds to creditors. Assignees are usually appointed by the principals of the debtor, typically with consent of the secured lender in order to address possibility of the assignment being disrupted by the filing of a UCC or mortgage disclosure.

Chief Restructuring Officer (CRO)
Is a senior officer of a company given broadly defined powers to renegotiate all aspects of a company's finances to deal with either an impending bankruptcy or to restructure a company following a bankruptcy filing. The roles and responsibilities of the CRO can be dictated by either the debtor, creditor, or courts. The use of experienced CROs has been increasing in popularity since the 1990s. CROs are sometimes seen as an alternative to using a trustee in bankruptcy in a reorganization bankruptcy, because the trustees may not be knowledgeable in the field of business conducted by the company.

Receiver
Is an independent professional brought in to operate and manage a business or income-producing real estate or to oversee the liquidation of the business. While the courts generally adopt the recommendation of the party seeking appointment of a receiver, the courts may choose the receiver or someone recommended by the company or other parties in interest. Receiverships, particularly general receiverships, are similar to federal bankruptcy cases in that receivers are often provided with the power to sell free and clear of liens, assume or reject executory contracts, stay creditor enforcement actions, and exercise other court supervised powers that are commonly exercised by bankruptcy trustees.

Chapter 11 Trustee
In instances where it can be shown that management is not the proper responsible party, usually because of bad faith or fraud, the court can remove the current management and bring in a chapter 11 trustee to run or liquidate the business. A chapter 11 trustee is normally a business person and is not part of the U.S. Trustee's office. The chapter 11 trustee usually has the power to hire professionals to effect the reorganization, sale or liquidation of the company. The appointment or election of a trustee occurs only in a small number of cases. Generally, the debtor, as "debtor in possession," operates the business and performs many of the functions that a trustee performs in cases under other chapters.

Small Business Trustee
This designation is associated with the newly signed Small Business Reorganization Act, effective February 19, 2020. In this role the FA as the small business trustee has a role similar to the chapter 13 trustee in a consumer bankruptcy case. They will oversee plan payments and have the authority to challenge the financial affairs of the debtor and object to the allowance of proofs of claim. The small business trustee may assist the debtor in development of a consensual plan of reorganization. The small business trustee is also authorized to operate the debtor's business if the debtor is removed as a debtor-in-possession.

Changes are coming

By Katie Montague

"The goal of the SBRA is to streamline the bankruptcy process for small businesses, reduce the number of liquidations, preserve jobs, and increase creditor recoveries."

Chapter 11 bankruptcy filings in the U.S. have remained relatively flat since 2015, which could be a sign of a thriving economy, but also could be a sign that the structure and cost of chapter 11 precludes many businesses from filing. In August of 2019, President Trump signed the Small Business Reorganization Act of 2019 (SBRA) into law, effective in February 2020. The SBRA has the potential to have a significant impact on the number of businesses filing for reorganization, designed to make it easier and more cost-friendly for small businesses with debts of not more than $2,725,625 to file under chapter 11 of the bankruptcy code. The SBRA creates a new subchapter V under chapter 11 that filers can elect to use. The goal of the SBRA is to streamline the bankruptcy process for small businesses, reduce the number of liquidations, preserve jobs, and increase creditor recoveries.

Previously, small businesses were able to file bankruptcy under chapter 11 if they had less than $2.5 million in debt. The high-cost and intricacy of the chapter 11 process, however, made it prohibitive for small businesses to file, resulting in liquidation under chapter 7 as the only option.

Under the new SBRA, some things remain unchanged. Some similarities include the filing of certain documents by the debtor, like financials and tax returns, having a plan of reorganization approved by the court, the assignment of a trustee, and payments by the debtor to the creditors.

There are also substantial differences about the bankruptcy process under the SBRA than in a traditional chapter 11 filing.

First, a small business trustee will be appointed by the U.S. Trustee in every subchapter V case. Rather than a standing or panel trustee, one will be selected from a pool of previously determined qualified small business trustees. That pool is currently being assembled and, theoretically, will include those with the financial knowhow to take on the new duties outlined under the SBRA. The trustee duties provided in the Act include assisting the debtor in developing a reorganization plan, acting as a fiduciary to creditors, appearing at status conferences, examining proofs of claims, and retaining estate funds until plan confirmation. The trustee also ensures the debtor makes timely payments required under the plan and, if the debtor fails to comply with plan requirements, the trustee can take over operations of the business.

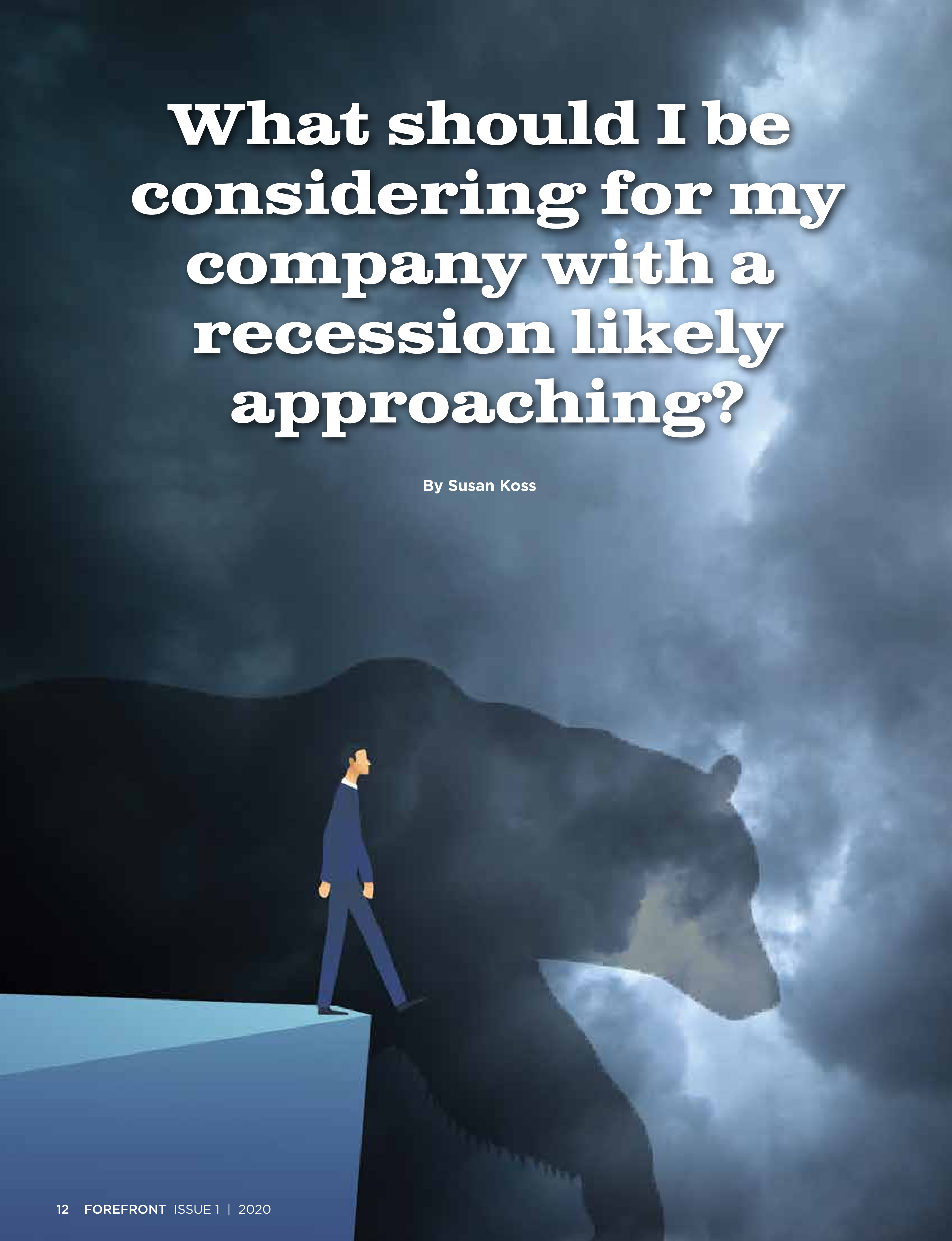
A trustee under subchapter V will act as a hybrid of what we typically think of in bankruptcy as a trustee and a financial advisor. The creation of this hybrid position and the unique set of duties awarded should help debtors navigate the complexities of filing bankruptcy in a much more efficient and cost-friendly way.

The Act also eliminates the need for creditor committees, unless one is explicitly approved in certain cases, because the trustee is supposed to act as a fiduciary to the creditors. The exclusion of an unsecured creditor committee should speed up the bankruptcy process while reducing professional fees. There are also no U.S. Trustee fees required under the SBRA. The duties outlined in the Act appear to indicate that the trustee is to act as a mediator between the debtor and creditor to formulate a confirmable plan that will be a win-win situation for all parties with lower case administration costs.

Other debtor-friendly elements of the SBRA include the allowance of administrative expenses to be paid over the life of the plan, rather than at plan confirmation date and that the plan may or may not pay unsecured claims in full. Equity holders are able to retain their interests in the business even if unsecured claims are not fully paid – a noteworthy change from chapter 11 cases, which previously required full payment to unsecured creditors for debtors to retain their ownership interests.

Chapter 11 bankruptcy was not feasible for small businesses historically. The debtor-friendly elements of the SBRA, especially a trustee to help guide a debtor through the process, should make filing for reorganization more practicable for small businesses. The goals of the SBRA will not be realized for at least three-to-five years while the first cases navigate through the entire process, but we should see in the coming months whether the new law is attractive enough to encourage small business restructurings.

***Katie Montague** CPA, CFE, Senior Associate, utilizes her financial expertise in many areas including, but not limited to turnaround & restructuring, bankruptcy, litigation support, business valuation, forensic accounting and shareholder disputes.*



What should I be considering for my company with a recession likely approaching?

By Susan Koss

Although a hotly debated area for economists, many are predicting a recession in the next 6 to 12 months given negative indicators such as the inverted yield curve[1] and a slow-down in manufacturing. With a potential recession looming, many business owners may be wondering what they should be doing to prepare for it. How can they get ahead of the curve and avoid being forced to react hastily in a crisis? Unfortunately, a sound recession business strategy isn't something one can "pull out of a hat" as soon as the economy turns. It is a comprehensive plan that includes a proactive and strategic response to the economic downturn.

According to *Harvard Business Review,* a study was conducted on U.S. public companies with greater than $50 million in annual sales during the last four economic downturns.[2] The study determined that the companies that weathered the downturns successfully tended to respond differently than unsuccessful companies in a few key areas. First, the most successful companies acted early on with the threat of an economic downturn before actual evidence of one happening. (Companies should already be in the process of preparing their recession strategy given the ongoing recession threat[3] we have been experiencing for at least the past year.) The successful companies focused on building more flexibility into their investment-planning and operations in addition to pursuing continued earnings expansion. By the time the recession was in full swing, the successful companies had reduced debt as compared to the unsuccessful companies that added more debt during this time.

The second key area is that most successful companies did not only focus on short-term issues to weather the impending economic rollercoaster, they maintained a long-term strategic perspective. Although many companies pursued operational efficiencies and improving profit margins, the most successful companies also focused on revenue growth. Prior to and during a recession, it is critical to understand that loyal customers are the primary, stable source of cash flow and organic growth. Although it is prudent to contain costs, failing to support brands or examine core customers' changing needs can threaten performance over the long-term. Companies that put customer needs under the microscope and tactically adjust strategies and product offerings are more likely than others to flourish both during and after a recession.

Another area of importance, that is often overlooked, is to review and amend the practices for ongoing management of order fulfillment, new product launches, and product discontinuation. A well designed and properly implemented product management policy will maximize margins on new products. In addition, through the use of technology, implementation of new strategies to tightly integrate the company with its customers on one end and its suppliers and/or operations on the other end can provide tremendous efficiencies. Improvements in technology, if designed and implemented properly, can also reduce risk cycle time from order to delivery, inventory levels, and costs associated with administration. Learning to understand the implications of changes in technology and how to adapt and utilize new technology can be key to attaining a competitive edge.

Management should also review the supplier base including, but not limited to, the number of suppliers, locations, terms/pricing, minimum order quantities, lead times, and level of defects. It is important to re-examine the methods and key performance indicators that are used to manage key external suppliers to mitigate supply chain risk. This type of analysis can result in more reliable, timely, and cost-effective raw material and finished product sourcing.

A critical indicator for a business' strength is its ability to perform during recessionary times. Downturns can shine a spotlight on the long-term health of a business, revealing vulnerabilities that might not have been as visible in good times. Successful companies have proven the importance of a proactive and strategic business plan to prevent vulnerabilities which can be the key to thriving rather than just surviving the next economic downturn. Many companies do not take the time to make this objective self-assessment leading to an outside stimulus to provide change when options are fewer.

***Susan Koss** CPA/ABV/CFF, CVA, Partner and Managing Director, leads the firm's Litigation Support Practice Group. She specializes in litigation support, business valuation, quality of earnings and forensic accounting.*

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1 The inverted yield curve is measured when longer-term government bond interest rates fall below short-term interest rates.

2 Kevin Laczkowski and Mihir Mysore, "What Companies Should Do To Prepare For A Recession," *Harvard Business Review,* May 9, 2019.

3 The yield curve has been inverted since March 2019.

Michigan Dairy Angst

By Stephen Weber

We're number one! In case you didn't know, our cows are the most productive in the U.S. Based on the latest report from the USDA National Agricultural Statistics Service ("NASS"), the average daily production rate for Michigan cows was 71.1 pounds per cow. The national average is 63.8. Based on our high production rate, Michigan dairy farmers should be happy, right? Unfortunately, that is not the case.

Causes of Dairy Angst

Michigan dairy farmers have faced depressing operating results for some time now. It is becoming so critical that the Michigan Agri-Business Association (MABA) had a session at their 2020 Winter Conference on recognizing the dangerous signs of depression in farmers, including dairy farmers.

The largest source of angst for Michigan dairy farmers is low prices for their milk. As you can see from the graph, over the last 4 years, Michigan dairy farmers have been receiving lower-than-average prices for their milk.

Recently, prices have experienced an uptick to slightly above the long-term real (inflation-adjusted average) milk prices. This is good news for farmers.

There are many causes for the low prices. First, consumers are switching from drinking cow's milk to alternatives such as soy and almond milk. They perceive health benefits from this change. Pain from this choice is being felt by dairy farmers across the U.S. as well as noted in the recent bankruptcy filings of Dean Foods and Borden.

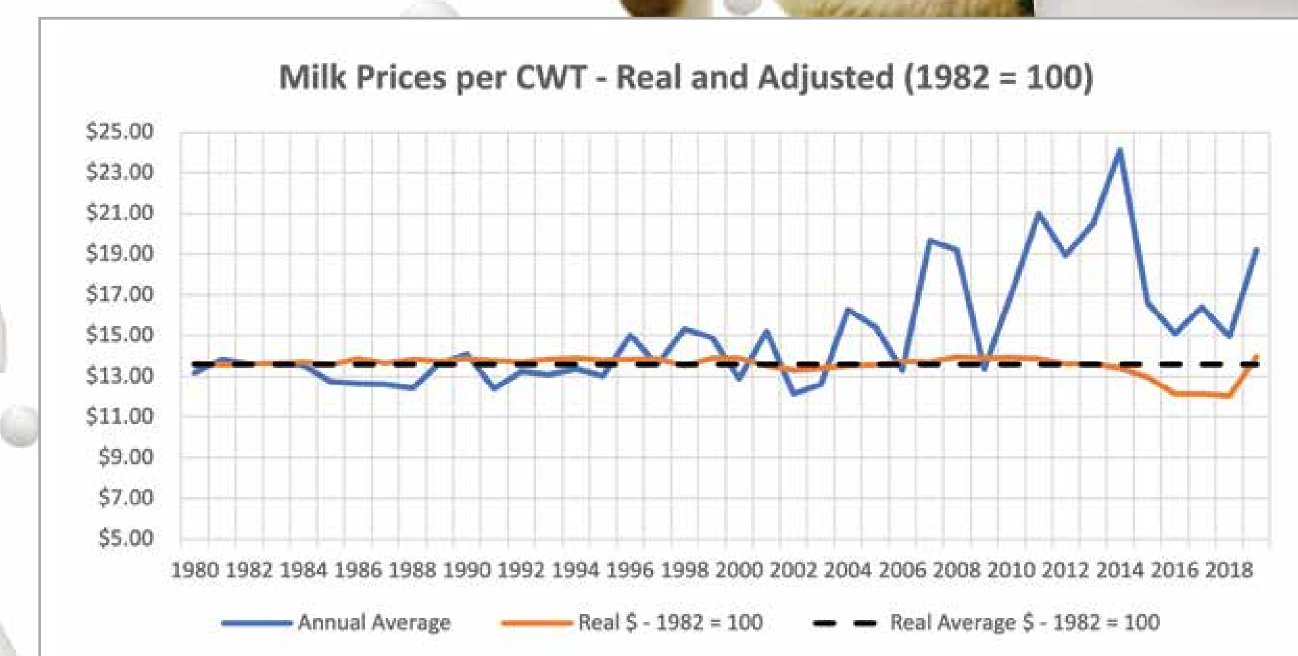
Secondly, the U.S. has been involved with trade disruption with its most significant foreign export customers: Mexico, Canada, and China. In prior years, the U.S. exported 15% of its total dairy production to foreign countries. Prior to the disruption, the U.S. supplied 75% of Mexico's cheese. Following the end of NAFTA and the implementation of other tariffs, Mexico began to import cheese from the EU. Additionally, without NAFTA in place, Canada was able to export skim-milk powder to Mexico at very favorable prices which undercut U.S. prices. Now that the USMCA is in place, we can hope that trade practices revert back to the "old normal" and Mexico returns to purchasing more economical U.S. cheese and dry skim milk.

Third, Michigan has suffered from a lack of milk processing capacity for some time. Due to our high production, a significant portion of our milk was being "exported" to other states for processing. The cost of shipping this milk out-of-state drove down the per hundredweight (CWT) price of milk from Michigan to the lowest level in the Midwest. In 2020, two new processing facilities will go online: a cheese factory in St. Johns and a milk processing facility in Greenville. This added processing capacity will significantly reduce the shipping costs and mean added revenue to Michigan dairy farmers.

Fourth, in 2019, we had horrible farming weather in Michigan. While grain prices have not increased significantly, for many farmers who plant grain, alfalfa hay, and corn silage to feed their herds, the late/small harvest has meant a significant increase in input costs. While there are supplements available for purchase to offset these nutritional losses, for farmers who lost money planting grain or hay which was not harvested, they now must shoulder the additional burden of supplement purchases to augment their herd's diet or face declining milk yields in a low-priced environment.

For 2020, we can hope that raw milk prices maintain or exceed historical real averages and return local dairy farms to positive cash flow and secure operations. However, until that happens, expect to see continued exists from the dairy market by smaller and marginal producers. The revised chapter 12 and small business bankruptcy regulations mentioned in another article in this issue may come into play for those operators.

__Stephen Weber__ CPA/CFF, CTA, Director, works with clients in the fields of turnaround management and business refinancing, litigation support, forensic and fraud evaluations, as well as performance improvement.



Source: USDA NASS data