



Maryland & Virginia
Milk Producers Cooperative Association, Inc.

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July 13, 2005

Hearing Clerk
United States Department of Agriculture
STOP 9200 – Room 1083
1400 Independence Avenue, SW
Washington, DC 20250-9200

Reference: Milk in the Appalachian and Southeast Marketing Areas, Docket No. AO-388-A15 and AO-366-A44;DA-03-11

Please find attached to this email our comments on the referenced order merger recommended decision.

If you have any questions, please do not hesitate to contact me at 703-742-6800.

Sincerely,

Jay S. Bryant
Treasurer and General Manager

JSB/jbs

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Milk in the Appalachian and Southeast Marketing Areas

Docket No. AO-388-A15 and AO-366-A44; DA-03-11

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**Comments on Partial Recommended Decision, and
Request for Expedited Final Decision**

These comments are filed on behalf of Maryland & Virginia Milk Producers Cooperative Association, Inc., hereinafter referred to as "MD & VA".

The comments filed here by MD & VA provide partial comment on certain areas of interest in the Partial Recommended Decision on the Appalachian and Southeast Federal Milk Marketing Orders (the Decision). Comments and Exceptions on other areas in the Decision on proposals not adopted will be filed at a later date. No statement in these comments regarding supports of an amendment to the individual Appalachian and Southeast Orders should be construed as a lessening of the support by MD & VA for the consolidation of the two orders into a single Federal Order marketing area.

MD & VA supports all of the provisions which were adopted for amendment in the Decision. These provisions include recognition of the worsening milk deficit condition in the southeastern United States and the embracing of increased Transportation Credit Balancing Fund assessments; the need to expand the marketing area to ensure orderly marketing in the Commonwealth of Virginia, inclusion of Market Administrator discretion in the setting of producer milk percentages and producer qualification for Transportation Credits; and the elimination of the ability to simultaneously pool milk on a Federal Milk Marketing Order and a state order that provides for marketwide pooling. MD & VA finds especially laudable the increase in Transportation Credit balancing Fund assessments.

Comments on Transportation Credit Balancing Fund Assessments

History has demonstrated that the current maximum rates of \$0.065 per hundredweight of Class I producer milk in the Appalachian Order and \$0.07 per hundredweight in the Southeast Order are insufficient to cover the Transportation Credits which have been claimed. As cited in the Decision (FR 29424), the Southeast Order market administrator has prorated payments every year 2001 to 2003. Although not cited in the Decision, the hearing record shows that the Appalachian Order market administrator prorated Transportation Credit payments in December 2003. We note that both the Appalachian Order market administrator and the Southeast Order market administrator prorated payments from the respective Transportation Credit Balancing Funds during substantial portions of the 2004 payout period. There is no indication in the

hearing record that milk production in the southeast will begin to increase any time soon; in fact, data in the hearing record suggest just the opposite. At the same time, record evidence shows increases in Class I sales, and a projected continuation of this trend. Thus, the record suggests that the shortages of funds in the Transportation Credit Balancing Funds will not correct themselves by decreases in the volume of supplemental milk needed to supply the Class I needs of the southeast. Increases in the assessments for the Transportation Credit Balancing Funds are necessary to correct these shortages.

The distance milk moves to supply the Class I needs of the southeast has increased as the milkshed has expanded with decreased production inside the southeast (FR 29424). More miles milk moves means more dollars needed to pay transportation costs. The insufficiency in the Transportation Credit Balancing Fund assessments has worsened, and has created increased burdens on the marketers of raw milk to find other ways to help cover the costs associated with the transport of this milk. Increasing the Transportation Credit Balancing Fund assessments rightfully returns a portion of the cost of supplying Class I milk to the southeast on the consumers of Class I, rather than the suppliers of the raw milk.

The record is replete with information on impacts to handler equity which arise when the Transportation Credit Balancing Funds are insufficiently funded. Reducing the shortages in the Transportation Credit Balancing Funds will lessen some of these inequities.

The need for the Transportation Credit Balancing Funds in the Appalachian and Southeast Orders is well settled. The importation of supplemental bulk milk to the southeast is necessary for supplying the Class I needs of the market (FR 29411). The need for continuing the existence of the Transportation Credit Balancing Funds, and the proposed increases in Transportation Credit Balancing Fund assessments are founded in fact, and are appropriate.

Comments on Transportation Credit Balancing Fund Provisions

MD & VA supports the provisions as proposed to be amended in the Decision allowing market administrator discretion in setting the percentage production standard for a producer to be eligible for such producer's milk to receive Transportation Credit Balancing Fund payments.

Both the current Appalachian and Southeast Orders provide that an out-of-the-marketing-area producer may be considered a supplier of supplemental milk to the market and thus eligible for such producer's milk to receive a Transportation Credit Balancing Fund payment if the producer was not a producer during more than two months in the February through May period, and not more than 50 percent of the milk of the dairy farmer was received as producer milk during those two months.

A proposal was heard at the Hearing regarding the spring months referenced in this section, and comments on that issue will be made at a later date.

MD & VA supports in general greater market administrator discretion in setting limits and minimum performance standards in Federal Orders. Order provisions which provide defined minimum or maximum levels of performance or set limits on certain activities need to permit

flexibility to allow proper response to the ebb and flow of milk and milk products. The local market administrator is in the unique position to evaluate general marketing conditions, changes in supply and demand for milk, changes in sources and destinations of milk, as well as the impact in changes in milk production due to the biologic nature of production, or to structural changes which can influence milk and dairy product consumption. Overly rigid provisions in these areas can cause inefficiencies in the marketing of milk, disorderly marketing, or uneconomic movements of milk.

Defining under the Order what milk is “supplemental milk” by limiting the portion of milk pooled from a dairy farmer in the spring months is a prime example of an Order provision which needs flexibility. As the milkshed for the southeast continues to change, and in particular expand, the 50% standard referenced above may not always be appropriate. Unexpected declines in milk production in the spring months may signal the need for additional shipments of milk into the Order areas over the historic levels. Such an occurrence may be temporary in nature and worthy of only transitory adjustment. In such a case it is highly desirable for the market administrator to have discretionary authority to adjust the delivery standard. The market administrator can make such a determination much more quickly than a change can be made through the formal rules process, and thus temporary changes can be implemented when needed, and provisions returned to the stated measure if appropriate at the end of any such temporary condition. The requirement that prior to making any change in the provision a market administrator must seek views, data and argument from the industry assures openness in decision-making, inclusiveness, and fairness.

Comments on Expansion of the Appalachian Order Marketing Area

MD & VA supports the Decision’s recommendation that certain heretofore unregulated areas in the Commonwealth of Virginia be included in a Federal Order marketing area. Producer and handler equity will be enhanced, orderly marketing will be advanced, and marketing efficiencies will accrue from the inclusion of the proposed 25 additional counties and 14 additional independent cities in the Appalachian Order marketing area (hereinafter referred to as the Virginia Expanded Area).

As cited in the Decision (FR 29410) three fluid milk distributing plants are located in the Virginia Expanded Area. Two of the plants are currently Appalachian Order pool distributing plants, and one plant alternates between regulation on the Northeast Federal Milk Marketing Order (No. 1001) and partially regulated status.

Of the three plants located in the Virginia Expanded Area, only the National Dairy Holdings plant located at Roanoke, Virginia did not express any existing problem associated with the size of the Federal Order Marketing area.

The Kroger Company plant at Lynchburg, Virginia, an Appalachian Order pool distributing plant, has limited the expansion of its sales area in order to preserve its regulatory status as a pool distributing plant on the Appalachian Order (FR 29422). A regulatory process which limits a handler’s ability to operate its business in the most efficient and cost effective manner must be scrutinized. As cited in the Decision, this situation has placed the plant in a

position of undue hardship. Dairy farmers who supply the Kroger plant with raw milk have been concerned about the impact on producer blend prices if the plant failed to qualify as a pool plant. Expansion of the marketing area will allow the plant to operate more efficiently, will perpetuate its regulatory status as a pool plant, and eliminate the disorder which could occur if the plant's regulatory status changed.

Further, with regard to the Kroger Company plant at Lynchburg, Virginia, perpetuating its regulation on the Appalachian Order would allow the plant to remain competitive in procuring its supply of raw milk, as the plant is in competition for supplies with other plants pooled on the Appalachian Order.

The Dean Foods plant located at Mt. Crawford, Virginia has likewise been plagued with issues related to the size of the Federal order marketing area. This plant has alternated regulatory status between being a Northeast Order pool distributing plant, and a partially regulated distributing plant. As cited in the Decision (FR 29423), a recurring change in the regulatory status of a plant, either between Federal Orders, or in and out of Federal regulation, is disorderly. Inclusion of the Virginia Expanded Area in the marketing area would allow this plant to be continuously pooled on the Appalachian Order, removing the disorder associated with changes in regulation.

As cited in the Decision (FR 29423) the Mt. Crawford plant would be in a more competitive position to procure its supply of raw milk, inasmuch as it the plant is in competition for supplies with other plants pooled on the Appalachian Order. In addition, the blend price to producers delivering to the Mt. Crawford, Virginia plant would be stabilized, and uncertainty regarding the blend price producers would receive would be diminished somewhat.

Other issues arise when plants are in competition and the regulatory status of one plant is constantly changing. Because of blend price differences, over order price implications can occur, causing handler inequity in actual Class I cost. In addition, partially regulated plants can be perceived to have a Class I price advantage when only a portion of the Class I use in the plant is priced in a regulated market. Fully regulating for the long term all of the plants in the Virginia Expanded area under the Appalachian Order will correct these actual and perceived inequities, and bring order and stability to the area.

Record testimony and the Decision (FR 29422) indicate at most a small potential impact on the Virginia State Milk Commission and Virginia Base-holder producers. Any likely impact on such producers is expected to be positive, owing from an increased regulated blend price at the Mt. Crawford, Virginia plant, and removing the possibility of lowered regulated blend prices were the Lynchburg, Virginia plant to become regulated in an Order other than the Appalachian Order.

The expansion of the Appalachian Order marketing area into 25 additional counties and 14 additional independent cities in Commonwealth of Virginia was not opposed by any party, either at the hearing or on brief.

Comments on Amending the Producer Milk Definition

MD & VA supports amending the Appalachian and Southeast Federal Orders to exclude as Producer Milk any milk from a dairy farmer that shares simultaneously in the revenues of a state operated marketwide pool. We note that the record indicates that the Virginia State Milk Commission does not operate a producer revenue pool, and as such, as indicated in the Decision (FR 29427) and in the record, Virginia Base-holder producers (and by reference Virginia Milk Commission Base milk) would not be precluded from pooling on either the Appalachian or Southeast Orders as a result of this proposed amendment. MD & VA repeats their position that any provision regarding the limiting of pooling milk from a dairy farmer that shares simultaneously in the revenues of a state-operated marketwide pool must not pertain to Virginia Base-holder producers.

3.2.2 The market disorder, unfair competitive advantages, and absolute inequity which comes of milk being pooled simultaneously on multiple Orders, be they Federal Orders or state Orders, is unqualified. For all the reasons cited in the Decision, the ability to “double dip” should be eliminated.

As cited in the Decision (FR 29426), Federal Orders have for many years disallowed the same milk from being pooled simultaneously on multiple Federal Orders. The right for handlers to pool milk by diversion must be structured such that the diverted milk is associated as a reserve supply for the Order on which pooled. While milk in a particular geographic area may be available for balancing the supply and serving as a reserve supply for more than one Federal Order marketing area, the same hundredweight of milk cannot be used simultaneously by more than one plant. Just as milk can't be in two places at the same time, it shouldn't be pooled two places at one time. The milk must be associated with one area or the other, or neither area, but not both areas simultaneously.

The same conditions must apply for milk associated with a state operated marketwide pool and a Federal Order pool as exist for two Federal Order pools. The ability for milk to be simultaneously pooled on a state-operated marketwide pool and a Federal Order pool violates the premises set out on why milk may be pooled in the first place. Milk may serve one market only at a time, and thus must not be allowed to be pooled on multiple pools at one time.

Recommended and Final Decisions in other Orders rightfully installed the prohibition against simultaneously pooling on multiple Orders. The Appalachian and Southeast Orders should be amended likewise.

Need for Expedited Action

A number of the amendments as proposed in the Partial Recommended Decision should be installed on an accelerated schedule. MD & VA hereby requests that an Expedited Final Decision be issued without delay after the close of the time period for filing written exceptions. MD & VA requests that the following issues be dealt with in such an Expedited Final Decision: increases to the Transportation Credit Balancing Fund assessments, and expansion of the Appalachian Order marketing area into 25 additional counties and 14 additional independent

cities in Commonwealth of Virginia, for the reasons set out below. Additionally, the inclusion of market administrator discretion in setting the percentage production standard for a producer to be eligible for such producer's milk to receive Transportation Credit Balancing Fund payments should be incorporated in an Expedited Final Decision if it is anticipated that a typical Final Decision on this issue cannot be made effective prior to February 2006.

Need for Expedited Decision Regarding Transportation Credit Balancing Fund Assessments

The increases proposed in the Partial Recommended Decision to the Transportation Credit Balancing Fund assessments for the Appalachian and Southeast orders should be made effective on an expedited basis.

According to market administrator statistics introduced at the hearing, for the year 2003 the monthly average Class I producer milk in the Appalachian Order was approximately 370.2 million pounds, and the monthly average Class I producer milk in the Southeast Order was approximately 385.8 million pounds, together representing approximately 756 million pounds of Class I producer milk per month. Using the Decision's recommended increase of three cents per hundredweight of Class I producer milk in the Transportation Credit Balancing Funds assessments; this represents a monthly increase in assessments in excess of \$225,000.00, or an annual increase of more than \$2.7 million for the two Orders combined. These funds are not inconsequential to the marketers of raw milk in the southeast, and every month that implementation of the increases to the Transportation Credit Balancing Fund assessments is delayed results in greater losses by those marketers of raw milk.

The hearing record and the Decision are clear as to the cause and results of insufficient funding of the Transportation Credit Balancing Funds. Postponement in implementation only serves to exacerbate the identified problems. Continued expected declines in milk production in the region only point to the critical need for quick action on this amendment.

Only modest opposition was received from handlers or dairy farmers to the proposed increases in Transportation Credit Balancing Fund assessments (FR 29424). Class I handlers in large part did not oppose increases in Transportation Credit Balancing Fund assessments due to their recognition of the increasing costs of servicing the Class I needs of the southeast, and the need for those market service cost to be borne by the consumers of Class I milk, not the raw milk suppliers. Opposition from one minority dairy farmer group focused on the desire to see funds equivalent to the amount which would be raised from increases in the Transportation Credit Balancing Fund assessments dedicated to encouraging milk production in the southeast. MD & VA wholeheartedly supports initiatives to increase milk production in the critically deficit southeast, but we are doubtful of the existence of legal authority for the Federal Order program to engage in such an endeavor. Absent such a possibility under the Federal Order program, one of the best alternative is increases in regulated Class I costs. Increasing the Transportation Credit Balancing Fund assessments does just that.

Need for Expedited Decision Regarding Expansion of the Marketing Area

The expansion of the Appalachian Order marketing area as proposed in the Partial Recommended Decision should be made effective on an expedited basis.

Class I and blend price inequities are not issues that can stand long before creating severe disorder in milk markets. Such is the case in the portion of Virginia which the Decision proposes to include in the Appalachian Order marketing area. Market disorder of the magnitude described in the Decision must be eliminated quickly or producer and handler confidence in the Federal Order program will erode.

The disorderly marketing conditions which have given rise to the need for the marketing area expansion will not subside until the amendment is accomplished and is effective.

In addition to the market disorder described in the decision, other logistical and operational issues will be addressed by the expansion of the marketing area. Handlers have altered sales patterns, held off sales expansions, and made other operational changes to preserve their regulatory status as fully regulated plants. These kinds of operational inefficiencies and burdens at the plant level must not be continued any longer than absolutely necessary. Expansion of the marketing area at the earliest possible date will allow these handlers to operate their businesses in a more cost effective and efficient manner. Delay in implementation of the Decision's recommendation for expansion of the marketing area is not warranted, and in fact delay is detrimental to the plant operators and to the dairy farmer suppliers to those plants.

Summary

MD & VA supports the all of the amendments to the Appalachian and Southeast Federal Milk Marketing Order as included in the Partial Recommended Decision. Each of the proposed amendments will enhance handler and producer equity, reduce disorderly marketing, and will promote the orderly flow of milk and milk products in the marketplace.

Further, MD & VA supports the issuance of an Expedited Final Decision on the proposed increases to the Transportation Credit Balancing Fund assessments, and expansion of the Appalachian Order marketing area into 25 additional counties and 14 additional independent cities in Commonwealth of Virginia.

MD & VA thanks you for the opportunity to make these comments, and looks forward to a quick Decision implementing the needed amendments to the Appalachian and Southeast Federal Milk Marketing Orders.