Statement Edward W. Gallagher
for the Proponents of Proposals 1, 2, 7 and 9

Dairy Farmers of America, Inc., Michigan Milk Producers Association, Dairylea Cooperative Inc. and the National Farmers Organization together are the proponents of proposals 1, 2, 7 and 9.

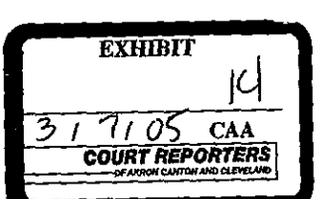
Dairy Farmers of America (DFA) is a member owned Capper Volstead cooperative of 13,500 farms producing milk in 49 states. DFA pools milk on 9 of the 10 Federal Milk Marketing Orders, including the Mideast Federal Order.

Michigan Milk Producers Association (MMPA) is a member owned Capper Volstead cooperative of 1,350 farms producing milk in 4 states. MMPA pools milk on the Mideast Federal Order.

Dairylea Cooperative (Dairylea) is a member owned Capper Volstead cooperative of 2,400 farms producing milk in seven states. Dairylea member milk is pooled in 3 of the 10 Federal Milk Marketing Orders, including the Mideast Federal Order.

National Farmers Organization (NFO) is a member owned Capper Volstead association marketing milk for more than 1,500 farms producing milk in 18 states. NFO pools milk on 6 of the 10 Federal Milk Marketing Orders including the Mideast Federal Order.

The proponents are strong supporters of Federal Milk Marketing Orders. In as much, we are advancing a number of proposals to correct certain marketing issues



that have developed and that are undermining the integrity of the Mideast Federal Order and creating disorderly marketing conditions. These issues need immediate attention and action. The central issues of this hearing are to provide for more orderly marketing by adjusting certain performance qualification criteria for sharing in the market wide pool proceeds of the Order and recognizing that the cost of serving the Class I market should be borne in a greater way by all producers who share in the Order's revenues. Failure to address these issues will be detrimental to all the members of our cooperatives both in their day-to-day dairy farm enterprises and the investments they have made in milk processing businesses.

Summary of Proposals for This Hearing

DFA, MMPA, Dairylea and NFO advance a series of proposals for the Mideast Federal Order to address the present day dynamics surrounding the pooling of milk under Order 33. These issues are quite similar to those that have been or are being addressed in a number of other Federal Milk Marketing Orders. DFA has made and supported similar proposals in other Orders and together with MMPA provided proposals and supporting evidence at the 2001 Mideast Order hearing on pooling and performance standards (AO-168-A68). DFA and Dairylea have advanced similar proposals at the 2002 Northeast Order hearing (AO-14-A70). The supporters of Proposals 1, 2, 7, and 9 consider market conditions that now exist in Order 33 to be disorderly and these proposals are offered as remedy. Please note that DFA, MMPA, Dairylea and NFO also are supporters of proposal 10, dealing with producer-handlers. We appreciate that this proposal has been removed from this proceeding to be heard at a later date.

Proposal 1 will incorporate language into Order 33 that will eliminate the possibility of simultaneously pooling the same milk both in a Federal Milk Marketing Order

and a State Milk Marketing Order with a marketwide pool. Please note that Order 33 does not presently have the language recently incorporated in other Orders - that establishes this safeguard. Testimony will be presented, and official notice taken of prior hearing records, in an effort to incorporate that concept and language into Order 33.

Proposal 2 deals with pool performance standards. Its goal is to better define those producers who are consistently providing service to the Class I market and thus should share in the blended Class I market returns. Michigan Milk will present its own modification to this proposal.

Proposal 7 deals with the issue known as "de-pooling". Its goal is to mitigate the incidence of, and blend price impact of, the practice of depooling. This proposal seeks to create economic consequences on handlers for choosing to have some of their milk "opt out" of the pool. DFA, MMPA, Dairylea and NFO depool milk when economically advantageous to our members and logistically feasible. However, we think this practice is detrimental to the Order system and to dairy farmers and wish it stopped or curbed. During Federal Order Reform, the Secretary of Agriculture recognized depooling as an Order issue when he incorporated changes to the data used in and the timing of announcements for Class I pricing. These changes were intended to limit price inversions which contribute to depooling. Also hearings have been held in other markets to address this same issue.

Proposal 9 would establish a "transportation pool", funded by blend price revenues, to offset a portion of the cost to transport milk to pool distributing plants, for Class I use.

We will present two witnesses, Mr. Rasch and myself to deal with the specifics of our proposal and the technical workings of the language we propose. We will also present several dairy farmers who will address the current operation of Order 33 affects them as individual producers.

Proposal 1 – Dual Pooling

Proposal 1, when adopted, will eliminate the potential for milk to be simultaneously pooled on Order 33 and a state marketing order with marketwide pooling. This is a disorderly marketing practice which has now been prohibited in other orders where it has occurred or could occur. We request that official notice be taken of the following Decisions of the Secretary:

- 68 Fed. Reg. 37674 (June 24, 2003) (Order 30);
- 68 Fed. Reg. 51640 (August 27, 2003) (Order 32);
- 69 Fed. Reg. 78355 (December 30, 2004) (Order 131);
- 69 Fed. Reg. 78351 (December 30, 2004) (Order 124); and,
- 70 Fed. Reg. 4932 (January 31, 2005) (Order 1).

We note that today little California milk is associated with Order 33. However, the same thing could have been said about California milk in CY 2000 in Order 30 – there was none on the pool. But from 2001 – 2003 a large quantity of milk was pooled in the Upper Midwest Order Milk from California. The California milk pooled on Order 30 first because it was the easiest and most lucrative Order to attach to. After that option was no longer an alternative, much of the milk moved to the Central Order and then to the Western Order.

California milk moved between the Orders as provisions allowed. The parties that pooled the California milk were acting in their own self-interest and made rational economic decisions within the framework of the rules allowed. However we, much of the rest of the industry, and eventually the Secretary felt this type of pooling was disorderly and adopted regulations to limit California milk from pooling in Orders 1, 30, 32, 124 and 131. This same provision should now be brought to Order 33.

Class I Value and Performance Standards

The Mideast Order is the second largest Federal Order market in terms of Class I use with 6.546 billion pounds of Class I sales (see DFA Exhibit ___ Table 1- Annual Class I Pounds, by Federal Milk Order Marketing Area, 2004). These Class I sales provide the bulk of the revenue to producers in excess of the Class III and IV market clearing prices. In the Mideast Order, it is this revenue that generates the blended producer price differential that creates the enticement for dairy farmers and cooperatives to be part of the Order and serve the Class I market. MA Exhibit ___ DFA Request #14 - Mideast Class I Value Versus Producer Value of Producer Milk Allocated to Class I details just how much of the Mideast Order's pool values are derived from the value of Class I milk. For example, in January 2000, the skim and butterfat Class I value of the pool was $67.0 million. For these Class I deliveries, producers were paid $60.6 million (i.e., for their pounds of butterfat, true protein and other solids and the PPD on this volume). $6.4 million remained in the pool. This $6.4 million was shared on an equal per hundredweight basis, after adjusting each producer's payment for location of delivery, with all the remaining producers in the pool via the producer price differential payment. Class I sales generated these extra dollars. This table also clearly shows that the value contributed by Class I is not static. In the period covered by the table the Class I

contribution ranged from a high of $21.1 million in June 2004 to a low of $1.0 million in April 2004.

The question of who shares in these values is the key question at this hearing.

Should performance standards allow milk to opt in and out of the pool on a month-to-month basis depending on the relative blend price return - sharing in the Class I market's returns on the same basis as milk that supplies the Class I market's regular every-day, every week, every month demand? We think it should not.

Should the second largest Class I sales market have stricter performance standards than currently? We think it should.

Should Order 33 performance standards be so lenient that it does not provide enough of an economic incentive to attract in-area milk production away from manufacturing uses – causing Class I suppliers to seek supplemental milk supplies from more distant out-of-area sources at significantly higher costs? We think they should not.

Should all producers who share in the market's Class I return have a greater obligation to help offset some of the cost of supplying the market's every-day Class I needs? We think they should.

These questions form the focus of our proposals.

The decision from the 2001 Order 32 (Central Order) hearing directly addresses the relevant questions before us at this hearing and provides direction for both the proposals and the testimony and evidence provided to support them. We want to highlight a few selected paragraphs from that decision:

"The pooling standards of all milk marketing orders, including the Central order, are intended to ensure that an adequate supply of milk is supplied to meet the Class I needs of the market and to provide the criteria for identifying those who are reasonably associated with the market as a condition for receiving the order's blend price. The pooling standards of the Central order are represented in the *Pool Plant, Producer*, and the *Producer milk* provisions of the order. Taken as a whole, these provisions are intended to ensure that an adequate supply of milk is supplied to meet the Class I needs of the market. In addition, it provides the criteria for identifying those whose milk is reasonably associated with the market by meeting the Class I needs and thereby sharing in the marketwide distribution of proceeds arising primarily from Class I sales. Pooling standards of the Central order are based on performance, specifying standards that, if met, qualify a producer, the milk of a producer, or a plant to share in the benefits arising from the classified pricing of milk.

Pooling standards that are performance-based provide the only viable method for determining those eligible to share in the marketwide pool. That is because it is the additional revenue from the Class I use of milk that adds additional income and it is reasonable to expect that only those producers who consistently bear he cost of supplying the market's fluid needs should be the ones to share in the distribution of pool proceeds.

...

Pooling standards are needed to identify the milk of those producers who are providing service in meeting the Class I needs of the market. If a pooling provision does not reasonably accomplish this end, the proceeds that accrue to the marketwide pool from fluid milk sales are not properly shared with the appropriate producers. The result is the unwarranted lowering of returns of those producers who actually incur the costs of servicing and supplying the fluid needs of the market.

...

The tentative decision and this final decision find that the milk of some producers is benefiting from the blend price of the Central order while not demonstrating actual and consistent service in satisfying the Class I needs of the Central milk marketing area.

...

The reform Final Decision, as it related to the Central marketing area, did not intend or envision that the pooling standards and pooling features adopted would result in the sharing of Class I revenues with those persons, or the milk

of those persons, who would not be demonstrating a measure of service in providing the Class I needs of the Central marketing area.

...

As previously indicated, pooling milk on the Central order without demonstrating actual performance in servicing the Class I needs of the market area is neither appropriate nor intended." 68 Federal Register 51644 – 51646 (August 27, 2003)

Proposal 2 - Performance Standards

The performance standards for the Mideast Order are inadequate. Although performance standards were changed once since Federal Order Reform was implemented, these standards need further review and adjustment. Proposal 2 is offered as a cure for this issue. Current provisions - while improved from the standards set in Order reform, are still too lax and allow far more milk to be associated with the market than is appropriate to be carried as a reserve supply. The Federal Order Reform targeted goal of a 58.9% Class I use has never been achieved – except in April 2004 when most of the reserve supply exited the pool. Excess reserves depress the blend price for producers that serve the every day needs of the market. The Mideast Order has adequate reserves located in the marketing area but still imports supplemental milk supplies from reserve areas because Order values do not bid the milk away from in-area manufacturing uses. If performance standards were enhanced, the blend price would be higher providing more incentive to deliver local milk to the Class I market. Also, the enhanced standard itself would cause additional milk to deliver to the Class I market or decline to share in the pool returns - again raising prices to all the remaining pool producers. This would reduce, significantly, supplemental Class I milk transport costs and milk premiums that are paid to attract reserve milk supplies. These extra costs of transporting and procuring supplemental Class I milk are not borne equally by all producers in the

market, although all share equally in the resulting Class I returns generated by these actions.

Furthermore, we are concerned that a pooling situation may develop with milk supplies from the Mountain states, similar to the "double dipping" concerns from California milk supplies that occurred only a few months ago. Large volumes of milk could get attached to the Mideast Order from distances so far away that it can rarely if ever serve the market. This situation has already occurred in the Upper Midwest Order and we want to insure that performance standards are adequate in the Mideast Order to prevent the regular pooling of milk from distant areas when such milk does not adequately or fairly serve this market's Class I needs.

Excess Reserves - Distant Milk Concerns

Order 33's reserve supplies have been reduced from their late 2001 and early 2002 peak. This is likely as a result of the modifications implemented due to the first "performance provisions" hearing. This reduction in the reserve supply can be seen in DFA Exhibit ___ Table 3 - Comparison of Fluid Use Pounds and Reserve Supply Pounds Federal Order 1033, January 2000 -December 2004 and the accompanying chart DFA Exhibit ___ Chart 1 - Comparison of Indexed Fluid Use Pounds versus Reserve Supply Pounds Federal Order 1033, January 2000 - December 2004. DFA Exhibit _ compares reserve supplies in indexed form from January 2000 – December 2004 using January 2000 as a base. Despite the changes from the 2001 hearing, these two exhibits show that a significant amount of excess reserve supply still remains attached to the Order. For instance, the January 2004 Class III + Class IV index of 192% means that 92% more Class III and IV milk was pooled on Order 33 than in January 2000 – the advent of Federal Order Reform. This occurred even

though there was only 7% more Class I and II milk pooled. The 192% January 2000 to January 2004 relationship seems very high for this market, still it is down some from early 2002. This is even more pronounced by the difference in pounds pooled. Comparing January 2000 with January 2004 show there was 50.5 million pounds more of Class I and II receipts pooled and 338.9 million pounds more of Class III and IV receipts pooled in 2004.

Some may claim that this level of reserve supply is needed or should be a part of the Order for various reasons. But that argument must surely be weakened when, as shown by the data, the reserve readily leaves the market, and is not available to supply the Class I market any time the PPD relationship is not economically attractive. The best indicator of actual availability is that shown by "own choice" - if a milk supply chooses to opt out of the pool, then it indicates to the market an unwillingness to be a consistent supplier. DFA has had supplemental suppliers refuse to make deliveries when faced with the "opportunity" to receive a negative PPD. The rationale that a large supply should have access to the pool must be measured against its ongoing availability to actually serve the market.

MA Exhibit ___ DFA Request #1A - Mideast Producer Milk, by State 2000 - 2004 shows performance trends in geographic milk supplies pooled on the Mideast Order. The data is divided by state, by year and by month for the period January 2000 – December 2004. The states with consistent supplies pooled, but from generally outside the marketing area, show a doubling or greater volume of pooled milk since 2000. Specifically, Illinois receipts have increased from 5.9 million pounds to 11.8 million pounds; Iowa receipts from 0.9 million to 5.7 million; Minnesota receipts from 0 to 3.1 million and Wisconsin receipts from 83.5 million to 206.4 million – a 147% increase. The primary in-area milk supply states have not shown similar trends. Indiana receipts pooled on Order 33 have increased from 137.2

million pounds to 142.9 million pounds; Michigan from 425.7 to 442.7 million pounds and Ohio from 302.7 to 303.6 million pounds.

The increase in receipts from areas generally outside the marketing area has not resulted in larger volumes of shipments to pool distributing plants. MA Exhibit ___ DFA Request #3 -Mideast Marketing Area Deliveries of Producer Receipts from Illinois, Iowa, Minnesota and Wisconsin to Distributing Plants August - November 2004 gives a snapshot view of performance from these areas during the short season of 2004. Performance from Illinois sources for the period were: August – 7.8 percent, September 19.3 percent, October 10.8 percent and November 10.8 percent. From a combined (for confidentiality purposes) Minnesota and Iowa were 5.2, 13.9, 4.9 and 10.2 percents, respectively, for the same four-month period. From Wisconsin – the largest out-of-area milk supply state, the performance was a very low 4.1 percent, 7.6 percent, 3.7 percent and 4.1 percent for the period. Combined over the whole four state out-of-area milkshed, the performance was 6.4, 12.4, 6.3 and 7.0 percents, respectively. Clearly, this market performance is well below the targeted levels that we have proposed. Conversely, the remainder of the market, the geographic areas more historically associated with the marketing area, must be performing at a far higher level. The low out-of-area performance, relative to the high volume of milk pooled, has a cost to the PPD. This affects all producers in the pool. MA Exhibit ___ DFA Request #2 - Estimated Impact of Distant Milk Pooled on the Mideast Order offers a calculation of this impact at minimum Order levels only. This calculation assumes for the purpose of PPD impact that all pounds from the out-of-area milkshed were removed from the pool and the pool was recalculated with different pound/location values instead. For the fall 2004 supply season the PPD would have been higher by 11, 2, 16 and 3 cents per hundredweight. The remainder of the exhibit shows the impact for August 2003 – December 2004. Note

that there is a residual impact on the PPD in the remaining months as the large volume of milk that is qualified during the fall months reduces the PPD by as much as 40 cents per hundredweight (July 2004) in the remaining months. Also note that the months of positive affect were months when much of this milk supply was depooled.

In order to further detail our concerns about distant milk and excess reserves we requested that the Market Administrator subdivide the market into five supply-demand regions – Northern Ohio, Southern Ohio, Michigan Indiana and Pennsylvania. These regions are described graphically and with additional statistical detail on MA Exhibit ___ DFA Request #8 (a) – (e). Data making up this exhibit is for October 2004.

Exhibit 8(a) describes the Northern Ohio region – that is shaded. This region has seven pool distribution plants – Arps Dairy – Defiance OH, Consun Foods - Elyria OH, Oberlin Farms Dairy - Cleveland OH, Reiter Dairy – Akron OH, Smith Dairy – Orrville OH, Sterling Milk Company – Wauseon OH and Superior Dairy – Canton OH. These plants have a combined class I sales volume of 86.5 million pounds and there is 276.5 million pounds of milk produced in the counties within this region. With 276.5 million pounds produced and Class I demand of 86.5 million pounds, there is an adequate supply of milk from this region to meet its Class I needs and also to supply milk to other regions as well. MA Exhibit ___ DFA Request #7 Mideast Milk Marketing Area Producer Milk to Distributing Plants by Distance and Region October 2004 breaks down the deliveries of in-area milk to this region. This Exhibit includes milk delivered to each region's pool distributing plants from locations outside the marketing area - thus the average miles will be greater than if the schedule included in-area milk only. For the Northern Ohio region, there is enough milk produced with-in the region to meet the supply needs of its Class I

plants. Additionally, the average distance milk moved, from all sources, to reach this region's distributing plants was 74 miles.

Exhibit 8(b) describes the Southern Ohio region (as shaded). This region has eight pool distribution plants – Broughton Foods - Marietta OH, H. Meyer Dairy - Cincinnati OH, Reiter Dairy - Springfield OH, Tamarack Farms - Newark OH, Louis Trauth Dairy - Newport KY, United Dairy Inc. - Martins Ferry and Cincinnati OH and in Charleston WV. These plants have a combined Class I sales volume of 124.0 million pounds and there are 50.9 million pounds of milk produced in this region. This is a deficit supply region. MA Exhibit ___ DFA Request #7 shows that all of the milk produced in the region only meets 41% of the region's Class I needs, and for deliveries to distributing plants in the region – from all sources –in the region and outside of the region, milk is transported an average of 130 miles.

Exhibit 8(c) describes the Michigan region. This region has twelve pool distributing plants – Bareman Dairy - Holland MI, Country Fresh - Flint, Livonia and Grand Rapids MI, Guernsey Farms Dairy - Northville MI, Inverness Dairy - Cheboygan MI, Jilbert Dairy - Marquette MI, Liberty Dairy - Evart MI, Michigan Dairy LLC - Livonia MI, Parmalat - Grand Rapids MI, Prairie Farms Dairy, Inc. - Battle Creek MI and Quality Dairy Company - Lansing MI. These plants have a combined class I sales volume of 166.8 million pounds and there are 464.6 million pounds of milk produced in this region. Here, there is an adequate supply of milk produced in this region to meet its Class I needs and also supply milk to other regions as well. This region is the major reserve supply are for the Mideast market. MA Exhibit ___ DFA Request #7 breaks down the deliveries of in-area milk to this region. All of the milk supply for this region's distributing plants could originate from the region and of

the deliveries to distributing plants in the region, milk is transported an average of 71 miles.

Exhibit 8(d) describes the Indiana region. This region has seven pool distributing plants – Dean Foods of Rochester Indiana - Rochester IN, Eastside Jersey Dairy - Anderson IN, The Kroger Company - Indianapolis IN, Pleasant View Dairy Corporation - Highland IN, Prairie Farms Dairy, Inc. Ft. Wayne IN, Schenkels All Star Dairy - Huntington IN and Smith Dairy Wayne Division Inc. - Richmond IN. These plants have a combined class I sales volume of 110.0 million pounds and there are 132.4 million pounds of milk produced in this region. There is an adequate supply of milk from this region to meet Class I needs, but little excess to supply milk to other regions. MA Exhibit ___ DFA Request #7 breaks down the deliveries of in-area milk to this region. All of the milk supply for this region's distributing plants could originate from the region and of the deliveries to its Class I plants, milk is transported an average of 103 miles.

The Indiana Region has a north / south divide relative to supply and demand. Much of the Class I demand is located in the southern two-thirds of the state, while the majority of the supply is in the northern third. If we had chosen to make a sixth region northern Indiana could well be a "reserve supply area" and southern Indiana a deficit area.

Exhibit 8(e) describes the Pennsylvania region. This region has seven pool distributing plants - Dean Dairy Products Company - Sharpsville PA, Carl Colteryahn Dairy - Pittsburg PA, Marburger Farm Dairy - Erie PA, Schneider's Dairy - Pittsburg PA, Turner Dairy Farms, Inc. - Pittsburg PA and United Dairy - Uniontown, PA. These plants have a combined class I sales volume of 80.6 million pounds and there are 106.6 million pounds of milk produced in this region. There is

an adequate supply of milk from this region to meet Class I needs but little excess to supply milk to other regions. MA Exhibit ___ DFA Request #7 breaks down the deliveries of in-area milk to this region. All of the Class I milk supply for this region could originate from the region and of the deliveries to Class I plants in the region, milk is transported an average of 97 miles.

Combining all these regions in Exhibit 8, show for October 2004 there was 1,031,089,121 pounds of pooled producer milk. This was more than enough to supply the 568,026,459 pounds of Class I sales from Class I plants located in this region. Clearly, there exists an adequate supply and reserve from which to supply the Class I market. From MA Exhibit ___ DFA Request #7 shows that milk travels an average distance of 93 miles to meet the Class I needs of the five regions.

MA Exhibit ___ DFA Request #6 (a) Total Mideast Producer Milk Delivered from Farms Located in the Mideast Marketing Area to Distributing Plants October 2004 and #6 (b) Total Mideast Producer Milk Delivered to Distributing Plants October 2004 outlines deliveries to pool distributing plants from increments of 20 mile zones. Exhibit 6(a) shows that 99.5% of the milk from in-area farms traveled less than 360 miles to deliver to distributing plants. Exhibit #7 summarizes the average miles for the entire market to be 93 miles. Exhibit 6(b) shows Class I deliveries for the entire market – not just the in-area farms. From this it is shown that 97.6 percent of the deliveries to Class I plants originate from less than 360 miles away. This means that 2.4 percent, or approximately 15 million pounds, come from distances of 360 miles or more – at a considerably greater cost to transport.

Further confirmation that the out-of-area milk that delivers to pool plant comes with high transport cost can be concluded from MA Exhibit ___ DFA Request #1(b) Mideast Pounds of Producer Milk by State and County, #10 Mideast Differentials,

#16 Producer Milk Across Zones – Mideast Order October 2004 and #17 Producer Milk Movement Across Zones – Mideast Order Average Hauling Distance – October 2004. From the differential map, Exhibit #10, it is known that the $1.75 zone is not in the marketing area. From the state and county production summary Exhibit 1(b) the pounds of milk that is in the marketing area but in a $1.70 zone is limited to Houghton and Baranga counties in Michigan – with less than 750,000 pounds of production per month. From Exhibits #16, it can be seen that approximately 17 million pounds delivered to pool distributing plants from outside the marketing area (6.8 million from farms in the $.170 zone and 10.2 million from farms in the $1.75 zone) and from Exhibit #17 from distances of 155 miles to 677 miles. Since approximately 10.6 million pounds from the $1.70 and $1.75 zones delivered to plants in the $2.00 zone, most of the milk was hauled distances of 469 miles or more. Note that 469 miles is the lowest average delivery miles for production in the $.170 or $1.75 zone for deliveries to the $2.00 zone, as shown in Exhibit 17.

DFA Exhibit ___ Table 5 - Summary of Supplemental Milk Purchases Dairy Farmers of America October 2004 provides detail about DFA purchases of supplemental milk supplies for October 2004. The pattern and data described here is typical for the fall, short supply season. As can be seen DFA purchased 21.6 million pounds of supplemental milk for delivery to Class I customers. The transportation cost averaged $2.51 per loaded mile. Purchases were from Illinois, Michigan, Minnesota and Wisconsin and deliveries to Indiana, Ohio and Pennsylvania. Assuming a 48,000 pound delivery, a $2.51 per loaded mile rate, and 288 additional miles (Table 5 average of 381 miles minus Exhibit 7 average of 93), this milk cost an extra $1.51 – just for the transportation aspect. If less expensive supplies could have been obtained closer to the market at a lesser cost, DFA would

not have made these out-of-area supplemental purchases. DFA could not bid in-area milk supplies away from its manufacturing uses at prices less expensive than the cost of importing milk – even though adequate in-area volumes did exist.

One of the measures of orderly marketing is some semblance of price alignment within and between Federal Order markets. The entire price surface is theoretically established to facilitate milk movements to supply Class I markets.

DFA Exhibit ___ Tables 4 (a) – (e) - Comparison of Relative Returns Between Markets Federal Order 1005 and 1033 makes computations about the relative returns, after location adjustment and freight costs, between Federal Order 33 and the Appalachian Order (Order 5). The Minster, OH area is a milkshed that can deliver to either Cincinnati, OH (Order 33) or Winchester, KY (Order 5). The comparison uses a 48,000-pound load, a rate per mile of $2.20 and monthly blend prices as announced by the respective Marketing Orders. Table 4-A show that for January 2000, the relative return (blend adjusted for location less haul) from Order 5 for a delivery to Winchester, KY was $.31 per hundredweight higher than the load would have returned at Cincinnati, OH. For all of year 2000, the Order 5 delivery averaged $1.08 higher than the Order 33 delivery. In fact, in every annual comparison since Order Reform, the Order 5 delivery was higher than the Order 33 delivery, ranging in amounts from 28 cents per hundredweight (2004) to $1.08 per hundredweight (2000). In only four of 60 months did the Order 33 return exceed the Order 5 return. In 26 of the 60 months, the difference was over 50 cents per hundredweight.

While Orders are designed to establish minimum prices only, the premium level it would take in Cincinnati to attract and maintain a portion of the local milk supply

vis-à-vis the Order 5 opportunity is unrealistic. These data show that the Order 33 blend level can not attract nor maintain a local supply relative to competitive factors from the neighboring Order 5 handlers.

Examination of MA Exhibit ___ DFA Request #11 - Percent of Mideast Producer Milk Diverted to Nonpool Plants indicates that our proposal can achieve its desired effect. The provisions of Proposal 2 that affect plant shipments will obviously increase performance by their nature. Request #11 details diversion amounts subdivided by whether or not the handler is a pool distributing plant or a cooperative for each month of 2004. Clearly in the shipping months of August – February handlers in both categories have diversions in excess of 50%. In order to meet the Proposal 2's requirement limiting diversions to no more than 50% some handlers will have to ship more milk to pool distributing plants or pool less milk on the Order which will yield a higher blend price for all producers.

MA Exhibit ___ DFA Request # 21 - Estimated Impact on PPD of 10 Percent Reduction in Diversion Limitations October 2004 further defines what we feel are the potential impacts from our proposal. At our request, the Market Administrator has made an estimate of both the pounds of milk that may either be available to ship to pool distributing plants or exit the pool. If the milk exits the pool it would have a resulting positive impact on the PPD. This measure can only be viewed as a minimal calculation in terms of dollar impact. However, it is more significant in its volume measure.

The dollar calculation measures the PPD impact resulting from removing manufacturing milk from the pool and changes in the location value. For October the PPD impact was 2 cents per hundredweight. However, the volume of milk that must now either ship or exit the pool was estimated to be 63.8 million pounds – very

significant in light of the volume of supplemental milk that must be purchased for the Class I market's needs. If even half of this milk becomes available to the market at Order values, the resulting reduction in supplemental milk costs will be large as less money will be spent in give up fees and transport costs.

The following conclusions can be drawn from our data:

1) The record shows that there is a large quantity of Class I sales and adequate milk supplies in the Mideast marketing area. Much of the in-area milk is well situated to deliver to market.
2) The Mideast Order, in spite of the performance enhancements made in the 2001 Hearing, still has more reserves than can be reasonably justified and those reserves are not always available to the market when needed.
3) Relative to year 2000, volumes of milk pooled on the market from states considered to be part of the traditional market supply have remained steady or declined slightly while milk production pooled from states not considered a part to the traditional market supply has increased dramatically. This increase in out-of-area pool pounds has not been accompanied by an increase in shipments to pool distributing plants from these areas.
4) The increase in non-performing volume, from out-of-area sources, has a direct negative impact on the Mideast Order PPD. Also, the small portion of the milk that does perform does so at a significant cost to the market due to high freight costs needed to transport milk over very long distances.
5) The additional costs of procuring supplemental milk supplies are borne by only a portion of the market.
6) The Order 33 pooling provisions do not correctly define what producers should share in the market's returns.

7) **The proposals made by the proponents are modest improvements over the status quo. They affect all suppliers equally in their construct by requiring similar increases in performance from all market supply sectors during the shipping months.**
8) **Estimates made by the Market Administrator demonstrate that the proposals can have the designed impact.**
9) **In order to protect the blend price from milk supplies that do not exhibit adequate performance, Order provisions that enhance performance standards are needed.**

The market is in a difficult quandary. The solution is Proposal 2.

Proposal Language to Enhance Performance Standards

All Federal Orders have performance standards. The reasons for their existence is uniform. However, the exact standards themselves are varied to meet the unique marketing conditions existing in each order. To best fit the Mideast Order marketing conditions the following language is offered:

Amend § 1033.7 by revising paragraphs (c), (d), (d)(2) and (e)(1), to read as follows:

§ 1033.7 Pool Plant.

* * * * *

(c) A supply plant from which the quantity of bulk fluid milk products shipped to, received at, and physically unloaded into plants described in paragraph (a) or (b) of this section as a percent of the Grade A milk received

at the plant from dairy farmers (except dairy farmers described in § 1033.12(b)) and handlers described in § 1000.9(c), as reported in §1033.30(a), is not less than 40 percent of the milk received from dairy farmers, including milk diverted pursuant to § 1033.13, subject to the following conditions:

* * * * *

Our intent here is to increase the shipping percentage for milk delivered to the market from supply plants by 10%. An increase is warranted; the Hearing Record demonstrates this. A modest increase will make more milk available to the Class I market if the supply plant handler wishes to pool the same volume of milk. The increase will apply to all 7 (c) plants regardless of location or ownership. We propose no other changes in this section.

(d) A plant operated by a cooperative association if, during the months of August through November 40 percent and during the months of December through July 30 percent or more of the producer milk of members of the association is delivered to a distributing pool plant(s) or to a nonpool plant(s), and classification other than Class I is not requested. Deliveries for qualification purposes may be made directly from the farm or by transfer from such association's plant, subject to the following conditions:

(1) * * *

(2) The 30 percent delivery requirement for December through July may be met for the current month or it may be met on the basis of deliveries during the preceding twelve (12) month period ending with the current month.

* * * * *

Our intent here is to apply the same 10% increase to 7 (d) supply plants as stated above, with one exception. Present Order provisions allow a cooperative owned plant to use a "rolling annual average" to meet the shipping requirements. Our proposed change requires a "hard" limit of 40% shipments during the fall months and, if done, the rolling average concept can be used to meet the remaining months' requirements. This change retains the rolling average concept but does "raise the bar" during the short shipping season.

(e) * * *

(1) The aggregate monthly quantity supplied by all parties to such an agreement as a percentage of the producer milk receipts included in the unit during the months of August through November is not less than 45 percent and during the months of December through July is not less than 35 percent; and

* * * * * *

The only change proposed to section (e) is to raise the shipping standard by 10%.

Amend § 1033.13 by revising paragraph (d)(4), to read as follows:

§ 1033.13 Producer milk.

* * * * *

(d) * * *

(4) Of the total quantity of producer milk received during the month (including diversions but excluding the quantity of producer milk received from a handler described in § 1000.9(c) or which is diverted to another pool plant), the handler diverted to nonpool plants not more than 50 percent in

each of the months of August through February and 60 percent in each of the months of March through July.

Finally, in Section 13 (d)(4) we have also proposed a decrease in the diversion limit by 10%, which correspondingly increases shipping amounts by 10%. This change is intended to apply to all handlers in all months.

We did not propose any changes in the touch base standard. We did review that option but felt that the increase in the shipping requirements was a better alternative. The opportunity to rotate producers to avoid real shipments rendered any touch base change moot.

The result of this language change is to increase the delivery standards for all handlers by ten percent. (with a slight deviation for a cooperative owned supply plant). In light of our data showing that market reserves are still excessive and blend prices too low, we think this modest change is warranted. We had requested higher levels than granted in the last performance hearing and can appreciate the position of the Secretary to make changes gradually; so now is the time to make the next change. Other proposals that have been made for this hearing also endorse improvements in the performance standards of the Order. No proposals have been offered to weaken them. We think the Secretary should consider the fact that many of the Order's suppliers support the direction that our proposal is taking.

Proposal 7 – Depooling

Proposal 7 deals with the issue of depooling. While there is no official Order term for "depooling", the industry generally understands it to mean the process of removing pounds of milk (by class) from the pool whenever the blend return is less than the corresponding Class value to the pooling handler, and then re-associating the same milk in a later month with the pool when the return is above the class value. The pooling handler retains the higher-class value, but does not share the higher value in the Order pool and has more dollars available to pay to its milk supply than a handler that cannot depool. (By definition Class I milk must be pooled and the value shared through the pool's blend price.) This is a rational economic practice - but the consequences in a regulated environment are disorderly. Competing milk supplies do not have equal returns available to pay producers for their milk deliveries.

The Mideast Order allows handlers to choose, each month, whether or not to pool milk in Classes II and III and IV. If a handler chooses not to pool milk in a month under the Mideast Order or any Federal Order, the handler has the option in the following month to repool all of the prior month's depooled milk – without any consequences. Most Federal Orders operate in this manner. A noted exception is the Northeast Federal Order where there are significant economic consequences for a handler that chooses to depool milk.

The term, depooling, and its occurrence is not a new or even a recent Federal Order phenomenon. What is a recent phenomenon is the significant increase in price volatility that has led to more frequent occurrences of manufacturing and blend price inversions. As the volatility has occurred, it has created very high dollar value

opportunities associated with depooling. This has created a critical need to change the Order system to address depooling.

While interviewing Elvin Hollon, in preparing this testimony, he indicated that he performed depooling decision calculations for Order 30 for his employer in the 1980's and 1990's - but remembers very few price differences of the over $2.00 per hundredweight range. In an exhibit prepared for the recent Order 30 hearing, instances of negative PPD's for Order 68 were presented. For the 84 month period from 1993 to 1999, there were 16 months with negative producer price differentials. Only six of these occurrences were in excess of 50 cents per hundredweight. Additionally, Elvin could not recall more than a few times that depooling decisions extended into what was then the Indiana, Michigan, Central or Southern Illinois orders. He told me that it was the mid to late 1990's before the depooling decision-making was "regular" outside of the Upper Midwest Orders.

Assuring an adequate supply of milk for the fluid market, equitably sharing the pool proceeds in an economically justifiable manner, and promoting orderly marketing, are among the basic purposes of the Federal Order program. Orderly marketing encompasses principles that assure that milk will be delivered to its highest value use when needed and that the reserve supplies will clear the market when not needed. Marketwide pooling allows qualified producers to share in the market returns on a fair and equitable basis. It also provides incentives to efficiently supply the market. Working in conjunction with classified pricing, these principles and requirements assure an adequate supply for the fluid market.

Information presented in the Order 32 hearing showed that depooling opportunities have been present 51 times since the implementation of Federal Order Reform. In

calendar year 2000 there were 6 opportunities (3 - II, 0 - III and 3 - IV); in 2001 there were 9 opportunities (6 - II, 0 - III and 3 - IV); in 2002 there were 8 opportunities (8 - II, 0 - III and 0 - IV); in 2003 there were 14 opportunities (10 - II, 4 - III and 0 - IV); and in 2004 there have been 14 opportunities (11 - II, 3 - III and 0 - IV).

Depooling is a problem because it results in different returns for milk sales. Milk is only depooled when the result means more money for the handler who depools. Since by definition Class I milk cannot depool, the Class I sale is always disadvantaged when milk is depooled. The handler with Class I sales must draw from margins in order to pay a competitive pay price because its regulated return is less than that of the depooling handler. If it cannot or does not meet the depooled competition, the Class I handler risks losing its milk supply to a depooling handler. This results in handlers in common procurement areas facing widely different returns from the regulated pricing scheme. This is the ultimate in irony – that the source of additional value to the pool, Class I milk, is unable to be competitive with other class sales due to depooling. If one of the purposes of the Order is to provide milk for Class I sales then depooling thwarts that purpose and must be considered disorderly.

The magnitude of the difference in returns is large. DFA Exhibit ___ Table 2-E Utilization and Statistical Uniform Blend Price Federal Order 1033 CY 2004 shows that, for April, a handler unable to depool was approximately $3.78 per hundredweight behind in ability to pay versus a handler that was able to depool. For the supplier that delivered a tanker load of milk per day to a fluid bottler, that difference amounted to $56,700 for the month. If it were 10 loads per day, the disadvantage was $567,000 for the month. Differences of this magnitude would be

insurmountable for nearly any milk procurer. In May, the depooling competitive difference was approximately $1.59 per hundredweight - while much less than April, it is still a significant amount. Expressed another way, in March 2004, 1.3 billion pounds of milk was pooled on the Mideast Order including 448.2 million pounds of Class III milk. In April there was only 0.873 billion pounds in the pool and 44.8 million pounds in Class III. In May, the pool and Class III volumes was still abnormally low, but completely returned to "full pool" status in June. Much of the milk that shared in the Class I dollars generated by the Order in March opted out in April and May and returned in June to share again, without any consequences.

Looking again to MA Exhibit ___ DFA Request #14 Mideast Class I Value Versus Producer Value of Producer Milk Allocated to Class I, those who chose to depool in April, left the pool when there was $1.0 million to share and returned to the pool in June when there was $21.1 million to share. In April, the $1.0 million was shared over 329 million pounds of non-Class I milk. However, by June, there was almost 1.1 billion pounds of non-Class I milk, an almost 800 million pound increase from April, that shared in the $21.1 million. Thus, the milk that did not depool was not able to "collect more" when "more" was available to make up for the shortfall in April - because more pounds opted to share in the total pool and blended down the per unit return in June. This situation must be remedied.

Producers in common procurement areas could also face widely differing returns due to depooling – a second sign of disorderly marketing. Several of our producer witnesses will attest to this fact.

MA Exhibit ___ DFA Request #5 Milk Voluntarily Depooled on the Mideast Order – Estimated Impact on the Producer Price Differential January 2003 to December 2004 depicts the financial impact on the PPD from various levels of depooling Class II and Class III milk.

The data in the table shows that 649.3 million pounds of milk were depooled in April 2004. It also shows that the Producer Price Differential in the Cleveland zone was minus $3.78. If the milk was not depooled the Producer Price Differential would have been minus $2.12. Thus, the producer price differential would have been $1.66 per hundredweight higher without depooling, and as important, all handlers in the marketing area would have had the same level of return from the pool. In December 2003, a month of a strongly positive Producer Price Differential of $1.39, milk was not depooled. If in December 2003 milk had been depooled to the extent of April 2004's depoolings, the PPD would have been significantly more. In December 2003, the Order worked as designed and provided the economic signal and incentive for the reserve supplies of milk to remain pooled on the Mideast Order. Clearly, the order system was designed to share the December 2003 Producer Price Differential value of $1.39 – with the reserve supplies being part of the pool.

During 2003 and 2004, there were 15 months (63 percent of the time) the provisions of the marketing order malfunctioned by creating an economic incentive to depool milk from the Mideast pool - although in 8 of the months, depooling had a nominal impact on the Order's Producer Price Differential. The Order system should create economic incentives, in the form of economic penalties, to encourage the continued pooling of the reserve milk supplies when manufacturing and blend price inversions do occur. That is the principle of marketwide pooling and part of the

foundation of the Federal Order system. Changes in the Mideast Order are necessary to strengthen its foundation.

As can be evidenced from this same exhibit, the complete elimination of depooling will not eliminate negative Producer Price Differentials. In seven months during 2003 and 2004, there still would have been negative Producer Price Differential's. Again, this proceeding is not addressing the cause of negative Producer Price Differentials – but our proposal will reduce the severity of the negative impact, when it does occur, and creates the incentive for the pool to share its returns among all producers on a more consistent basis.

Differing returns in the ability to pay of up to $3.78 per hundredweight are disruptive, disorderly and greatly affect the ability to procure and maintain a milk supply for Class I customers. Being part of the federal order pool should require a commitment to availability for Class I beyond that which unencumbered depooling involves.

<u>Proposal to Limit Depooling</u>

The proposal we offer is to limit the pounds a handler can pool each month to a volume lesser than or equal to 115% of what was pooled in the prior month. This proposal may be too severe for some handlers, and may not be strong enough for others in the marketing area.

In the development of Proposal 7, the proponents reviewed the Order's pooling requirements. Among possible changes reviewed and discarded were changing the

touch base to an every month requirement and instituting a producer for other markets provision similar to that existing in Federal Order 1 and as suggested in Proposals 4, 5 and 8. Utilizing these options would have resulted in more changes and in some cases more costly changes for Order 33 handlers than are warranted by existing marketing conditions.

Proposal 7 would limit how much milk a handler could add to the pool or repool each month. Milk pooled would be limited to 115% of the previous month's pooled volume with a few exceptions. This proposal will not eliminate depooling. However, it does create economic incentives to keep the reserve supply pooled on the order by creating economic consequences, steeped in uncertain future market conditions, that in some months will prevent depooling and in other months limit its use. If any handler depools under the current regulations there are no long-term consequences. In fact, there are virtually no negative impacts for those who depool.

The level of this limitation was chosen after receiving information similar to that found in MA Exhibit ___ DFA Request 4 Monthly Change in Mideast Producer Receipts. This exhibit compares month-to-month changes in producer milk receipts for Order 33. If milk was depooled during the month, the Market Adminstrator added the amount into the monthly volume. For instance, the April 2005 pool pounds of 1.5 billion includes 649 million pounds that were depooled. Using the 115 percent factor, there does not appear to be a month that would have prevented milk from being pooled due to a month-to-month seasonal production increase – or due to the ensuing month having more days. In fact, only two months show an increase with 5 percent of the 115 percent factor. The 115 percent limitation in our proposal should accommodate the normal market situation in the Mideast Order and allow for a reasonable amount of added volume in any given month.

MA Exhibit ___ DFA Request 12 Hypothetical Depooling Allowed to Ensure Full Repooling within Three Months with 115% Repooling Limitation demonstrate that depooling is not eliminated by our proposal. This example shows that a handler could depool 34 percent of its milk and have it all requalified for the pool three months later. However, a handler choosing this option has to be fairly certain that the milk pricing environment for the ensuing months in which milk can not be completely repooled creates a favorable financial outcome – in many cases this will be a gamble at best. While not eliminating depooling, this is a modest, and in our minds reasonable, position to take to control the problem.

Restricting the pooling of milk based on prior performance is not new to Federal Orders. The Northeast Order has had a "producer for other markets" provision for many years. Under this provision, milk of a producer cannot be immediately repooled if it has been depooled and is, in fact, excluded from the pool for an extended period of time. Proposal 2 would not impose such a burden on an individual producer but limits pooling based on an aggregate total of the handler's previous month's pooled pounds.

Years ago, other Orders primarily, in the South and/or Southeast either had a producer for other markets provision or base plans to accomplish similar goals. In these markets, the intent of such provisions was to limit the sharing of the marketwide pool during the spring months to those who pooled during the fall.

An additional benefit to our proposed limitation on pooling is that it would reduce or eliminate the possible need for an increase in the Market Administrator's administrative assessment fee. In Federal Order 33, depooling has negatively

impacted the Market Administrator budget. While the Market Administrator has not yet asked for an increase in the upper limit for the fee in order to assure that the Order can properly function and do so with a reasonable budget, continued pressure from depooling may cause this to occur. With our proposal, pool volumes would be more stable. It is our view that there would be more milk continuously pooled and less need for a fee increase. At the very least, with stability in the pool volumes, it would be easier for the Market Administrator to make staffing and other operational decisions benefiting all producers in the Order.

Those who wish to maintain the right to depool will observe that the real solution to this problem is to change the manner in which Order prices are announced. We agree that if all Order prices were announced on the same day there would almost never be a negative PPD and rarely any depooling. However, the Class I segment of the market desires advanced pricing – and we feel that having advanced pricing allows producers to obtain higher prices.

The balancing sector of the market desires "after-the-month pricing" because it must absorb the reserve supply of milk no matter what the ultimate underlying commodity price. Many times the balancing volumes are greatest when commodity prices are lowest. Balancing a milk supply is a low margin business. Being forced to manufacture milk supplies with milk prices in excess of commodity prices makes it even more unprofitable. Thus, no one wants to change "their own price" to "fix the system" but eagerly suggests change for the other party. Order regulations must attempt to serve the entire market and are frequently the product of compromise – in this situation no one is willing to change. Thus this proposed solution is not a real option. Additionally, in every Hearing held since Order Reform where pricing terms and/or depooling has been an issue no proposal has been noticed (and we think none

advanced) where the Class I sector has offered to "give up" advanced pricing nor the balancing sector to give up "after month" pricing. If it were to be advanced the hearing would have to be national in scope and not on an Order-by-Order basis. Those who would advance this argument at this Hearing have now had three opportunities to present an alternative proposal and no one has done so.

Others have asked why not seek a "non" Order solution to this problem. However, those solutions are not always workable, consistent or of long lasting possibility. There is no way to recover the negative PPD value from the Federal Order. A handler that must pool is always at a disadvantage when there is a negative PPD. And when there is a positive PPD, the handler who depooled during the period of negative PPD immediately returns to share in the pool.

There has been a recent effort to recover the negative PPDs through increased fluid market service charges. While admirable and welcomed by those who supply the fluid market, this effort is not sustainable over the long term. The increased price may have contributed to the larger than normal decline in fluid milk sales in 2004. Also, the fluid plants where the negotiated fee was implemented were placed at a competitive disadvantage with fluid plants in other areas where there was no increase.

For example, Central Milk Producers Cooperative and Upper Midwest Milk Marketing Agency (CMPC and UMMA) are pricing agencies composed of some of the cooperatives that supply milk for Class I use in the Upper Midwest. CMPC and UMMA put the increased service charge (negative PPD surcharge) in place for those plants that obtain milk from the CMPC and/or UMMA membership. Not all suppliers in Order 30 were members of CMPC or UMMA. This adds to the

difficulty of maintaining a negative PPD surcharge premium. In Order 33 it was not possible to institute such a premium recovery method because the competition for fluid milk sales was to geographically diverse and not all handlers were willing to support such a construct. The fluid plant cannot always recover this increased cost from the marketplace. Many of the longer term packaged milk supply arrangements with national and regional accounts have a price adjuster for changes in the Federal Order cost of milk. There may not be any provision, however, for changes in over order prices. The fluid plant ends up "eating" this increase and the books could show red ink. This method is not a long-term workable solution.

There are other proposals that have been offered here and will be testified to later in the week. We discussed many of those proposals and feel that several of them may well work in principle but are not the best solution for the Mideast Order.

The language that we offer is as follows:

(e) The quantity of milk reported by a handler pursuant to § 1033.30(a)(1) and/or § 1033.30(c)(1) for the current month may not exceed 115 percent of the producer milk receipts pooled by the handler during the prior month. Milk diverted to nonpool plants reported in excess of this limit shall not be producer milk. Milk received at pool plants in excess of the 115 percent limit, other than pool distributing plants, shall be classified pursuant to § 1000.44(a)(3)(v). The handler must designate, by producer pick-up, which milk shall not be producer milk. If the handler fails to provide this

information the provisions of § 1033.13(d)(6) shall apply. The following provisions apply:

(1) Milk shipped to and physically received at pool distributing plants and allocated to Class I use in excess of the prior month's volume allocated to Class I use shall not be subject to the 115 percent limitation;

(2) Producer milk qualified pursuant to § ----.13 of any other Federal order in the previous month shall not be included in the computation of the 115 percent limitation, provided that the producers comprising the milk supply have been continuously pooled on any Federal order for the entirety of the most recent three consecutive months.

(3) The market administrator may waive the 115 percent limitation:

(i) For a new handler on the order, subject to the provisions of § 1033.13(e)(4), or

(ii) For an existing handler with significantly changed milk supply conditions due to unusual circumstances;

(4) Milk may be considered ineligible for pooling if the market administrator determines that handlers altered the reporting of such milk for the purpose of evading the provisions of this paragraph.

Section (e) sets out the total volume of milk that can be pooled "this month" is no more that 115% of what was pooled in the "prior month". Any milk in excess of this volume will be removed from the pool. It is the handler's responsibility to designate

which milk is not to be pooled if the limit is breached. Section (e)(1) directs that milk shipped directly to a distributing plant is exempt from the limit. In the extreme case of 100% depooling a handler can always pool his deliveries directly to a distributing plant next month and also begin to earn pooling ability for subsequent months. Section (e)(2) allows milk that has been pooled on another order to be exempted from the 115% limit so long as the milk has been continuously pooled for at least three months on some Order. This does not penalize a Mideast Order handler from being a supplemental supplier to another Order plant and also prevents a multi regional supplier from selectively depooling and moving producers around between Orders to maximize depooling gains. Sections (e)(3) and (4) allows the Market Administrator some discretion in administering the proposal to account for a new handler, drastic but explainable reasons for changes in a pooling volume, and the ability to investigate and deny pooling for instances where some type of fraud or mal-intent is discovered. Note that we do not support allowing the Market Administrator any discretion in adjusting the 115% level as, for example, allowed for in Section 7(g) of the Order for supply plants. By allowing such an adjustment, creates a concern that the Market Administrator will be called on too frequently to adjust the standard. If this occurred and changes were made it would render its intent meaningless. If a change is warranted, the normal hearing or suspension process is available to accomplish this. In the future, if after some experience with these provisions, show such discretion useful then a future hearing can propose the change.

The areas we do allow discretion clearly call for the requesting handler to provide all necessary proof and documentation needed to justify any proposed "exception". It will be up to the requesting handler to show, for example, that increasing production from the "same " producer base did exceed the 115% level; that their

business organization truly warrants being a "new handler" with no prior months base to measure from or that some combination of business assets truly results in a new handler entity. Additionally, it is not the intent of this provision to prevent a handler from adding new producers to its business. However, if those producers were added for the purpose of accommodating another handler who had depooled them, then the Market Administrator should investigate and possibly hold the handler to the 115 percent requirement. While we can never outline every possibility we feel the Market Administrator does have the ability to investigate requests and make determinations.

Transportation Credits

Proposal 9 deals with transportation credits for supplying Class I markets. Congress authorized these types of provisions in the Federal Milk Marketing Order system to help pay the costs of supplying milk to the Class I market among other reasons. In some sense it follows the economic concept of a public good in that all participants in the market benefit (from Class I sales) but it is difficult to recoup the cost associated with the good (servicing the Class I demand) from any individual in the entire market. Said another way, there are benefits derived from the market by all but some do not pay the full cost associated with those benefits.

Congressional authorization provides for various services such as in market transportation, surplus milk disposal and supplemental milk procurement. See 7 USC Section 608c(5)(J).

Other Orders authorize these types of credits. For example, Federal Order 30 provides for an assembly credit paid to all suppliers of Class I milk. This credit has existed in this region's Order since 1987 and was continued and extended in the merged Order during Federal Order Reform. When promulgated, it was soley on plant milk. Federal Order Reform extended it to direct ship milk as well.

Congressionally authorized marketwide services in the form of transportation credits also exist in the Appalachian and Southeast Orders but in a different form than in the Upper Midwest Order. There, handlers pay an additional price to fund the transportation of milk into the market from out-of-area sources. At one time, the pre-Reform Texas Order had a market wide services payment in the form of a credit to assist in the disposal of surplus milk. In 2004, a hearing for the Central Order heard a proposal where the pool would fund a credit to offset the cost of moving milk to pool distributing plants for milk used in Class I. We offer a similar proposal today.

Issues in Order 33 and Why a Transportation Credit Will Help

DFA Exhibit ___ Table 5 – Summary of Supplemental Milk Purchases Dairy Farmers of America October 2004 provides details about supplemental milk purchases by DFA during October 2004. In October, DFA purchased 21,612,207 pounds of supplemental milk from the four out-of-area states for delivery to Class I customers in Order 33. Others may have also made some purchases of supplemental milk for their customers, but this information details DFA experience solely. Supply arrangements were coordinated through the Mideast Milk Marketing Agency (MEMA) for efficiency of transport and purchase. This exhibit identifies transport cost alone. Every purchased load had additional costs associated with it. For all of

these loads there was a "give up" or premium paid over the full Federal Order value. Some of the loads purchased were made on a multi-month contractual basis and some were spot market purchases. The fees above transport costs ranged from slightly below $1.50 per hundredweight to over $3.00 per hundredweight. Please note that Proposal 9 does not contemplate any reimbursement for any fee other than a portion of the transportation cost – not currently being covered by the Order.

The milk was sourced from nine different suppliers in Michigan, Illinois, Minnesota and Wisconsin. These loads were delivered to a number of different customers in Indiana, Ohio and Pennsylvania. The table identifies the following details:

- 1.6 million pounds of milk was purchased from Illinois suppliers and delivered to Ohio customers. On average this milk supply was transported 593 miles and had a cost of $2.02 per loaded mile.
- 0.7 million pounds of milk was purchased from Michigan suppliers and delivered to Ohio and Pennsylvania customers. On average this milk supply was transported 278 miles and had a cost of $2.35 per loaded mile.
- 19.3 million pounds of milk was purchased from Minnesoata and Wisconsin suppliers and delivered to Indiana, Ohio and Pennsylvania customers. On average this milk supply was transported 368 miles and had a cost of $2.55 per loaded mile.
- For the entire milkshed, the range of average rates per loaded mile was $2.37 for Ohio deliveries, $2.54 for Indiana deliveries and $2.55 for Pennsylvania deliveries.
- The market average of $2.51 is heavily influenced by the deliveries from Minnesota and Wisconsin. These charges, while taken from

October business records are typical for the entire fall short supply season.

MA Exhibit ___ DFA Request #8 (a) – (e) Mideast Marketing Area October 2004 (maps) helps to demonstrate that Order 33 must move milk from reserve supplies in Michigan and Northern Ohio to the remainder of the market. The ratio of production to Class I use in the Michigan region shows that 64% of the supply is available for reserve supply for other regions (464.6 million pounds of producer receipts minus 166.8 million pounds of Class I sales with the result divided by 464.6 million pounds of producer receipts). This same calculation for the Northern Ohio region produces a reserve supply ratio of 69%. For the Pennsylvania region, the calculation is only 24% - barely enough reserve to service some of this region's needs. The Indiana region's ratio is 17%, again minimal. Due to the north / south divide in Indiana relative to production and sales, milk must be imported (and has been since the 1980's) from outside of Indiana to supply the sales in the southern half of the state. The Southern Ohio region is deficit 73.1 million pounds of milk to meet sales needs for October.

Supplemental milk movements from the in-area surplus regions to the regions requiring imports travel significant miles. Typical distances for movements from in-area reserve supplies in central Michigan would be 317 miles to Newark, OH (Kroger); 349 miles to Sharpsville, PA (Dean); 365 miles to Newport, KY (Trauth) and 303 miles to Akron, OH (Dean). For movements out of reserve supply areas in northern Ohio distances would range from 86 miles to Newark, OH; 133 miles to Sharpsville, PA; and 200 miles to Newport KY.

The current Order's differentials do not pay for these milk movements. The zone layout in Order 33 is wide and flat and is reflective of the Cornell model used by USDA in establishing the Class I differential grid used under Federal Orders. Due to its current flat nature, the Order 33 zone structure does not offer enough incentive to attract or move milk to Class I locations within the market. While milk does cross zones to deliver to pool distributing plants, the additional 20 cents spread between each zone does not offer enough incentive to pay for the delivery. This can be seen in MA Exhibit ___ DFA Request #16 & 17. Only 20 percent of the milk produced in the $1.80 zone moves to plants in the $2.00, $2.10, $2.20 or $2.30 zones. A reason for this is the cost of moving the milk is far greater than the Order's zone adjustment. For example, the average hauling distance for $1.80 zone produced milk delivered to the $2.20 zone is 215 miles. For a load with 48,000 pounds of milk and a cost of $2.20 per loaded mile, the additional cost of moving the milk is $.66 per hundredweight (215 miles minus 71 miles (which is the average hauling distance for deliveries in the $1.80 zone) times $2.20 per loaded mile divided by 480 hundredweights). This compares to the Order's zone incentive of moving the milk of $.40. Since much of the in-area reserve is located in Michigan and northern Ohio, we see an increasing need to transport milk from northern areas of the Order to the southern areas. Transportation credits tailored to transactional events will help offset the cost associated with these movements. This failure of the Order to have a mechanism to assist Class I suppliers in covering these costs related to supplying Class I markets, places Class I suppliers at a competitive disadvantage in the field with pay prices relative to those milk supplies not heavily serving the Class I market. Yet all producers benefit equally via the pooled returns Class I generates.

The existing differential surface was established in Federal Order Reform in 2000. The underlying data and computations were based on 1996 (with some update based

on 1998 information) data and market conditions. Many changes in the marketing area have occurred since then. Several bottling plants have closed; those that remain are larger and require more balancing. This means on the high demand days, suppliers must reach out more miles to obtain supplemental supplies and many times "leap over" the next closest milk shed because that supply is utilized by its closest demand point. Also milk supplies in the Lake States region have diminished, causing increasing competition for local milk supplies from both fluid use and manufacturing.

Costs to transport milk have increased since the differential surface was established. Some of these higher costs include labor, liability insurance and capital. Energy costs have increased also. According to US Department of Energy sources' the 1999 Midwest annual average diesel fuel price was $1.10 per gallon. The 2004 annual average was $1.7679 or a 60% increase. DFA Exhibit ___ Chart 2 Diesel Fuel Price Midwest Monthly 1999 – Date portrays this increase. While prices are off their 2004 peak, they are still higher than any recorded price prior to mid-year 2004. (source: http://tonto.eia.doe.gov/oog/ info/gdu/gasdiesel.asp)

If the differential price surface was correct in 2000 (based on 1996/1998 data), it would need some adjustment today. However, adjustments in the price surface are difficult to accomplish and are dealt with on a national instead of regional basis. Building a record in that environment is difficult. There are widely competing interests that may or may not have a direct bearing or concern on a local situation (like zone price relationships in the Mideast Order) but still attempt to influence the overall proceeding. Because changing the differential structure is so difficult we choose instead to seek a transportation credit to offset some of the cost of supplying

the local market and to insure that all producers under the Order share more equitably in the cost of this service.

Proposal 9 Mechanics

Establishing a milk price is part science and part art. The science portion is usually well supported by fact. The art portion is the interpretation of those facts that form opinions as to how best to use the facts. Our data and evidence will combine both of these concepts and reflect our view of marketing conditions.

Our proposal for a transportation credit structure establishes a rate, mileage structure, appropriate application and safeguard factors. These factors would then be applied to the appropriate milk volumes each month, at pool time. Please note we are making several modifications to Proposal 9 as published in the hearing notice. These modifications are to the applicable rate and the mileage limitation. Included in the modification to the rate is a special rate applicable for milk movements within the State of Michigan.

Rate Factor

Our choice of payment rate is not $0.0031 per mile. In the hearing notice it was $0.0040. The new rate is based on a per mile hauling charge of $2.20 divided by a 480 hundredweight pay load, set at 67% of the full rate and rounded to four places. In DFA Exhibit ___ Table 5 – Summary of Supplemental Milk Purchases Dairy Farmers of America October 2004 described earlier in our testimony we detailed per mile costs of supplemental milk purchases from Illinois, Michigan and Wisconsin. Our rate choice of $2.20 is below the market average of $2.51 and well

below the average for Wisconsin of $2.54 - where much of the supplemental milk is sourced. We have provided actual invoices from milk transport companies and summarized them on DFA Exhibit ___ Table 6. This table shows a wide range of invoices, which would support $2.20 as a reasonable choice. These invoices taken from fall months and for supplemental milk purchases from already detailed supply areas, represent transport hauls from five to more than twenty five loads of milk – enough to be representative of typical. We chose a 48,000-pound payload as representative of a wide range of market alternatives. Certainly over-the-road tanker hauls are for slightly larger volumes but many of these routes originate from farm loads that are not always the largest tanker size. In the "Hurricane Relief Hearing" held for the three southeast Orders last fall to provide compensation for extraordinary hauling costs that resulted from four hurricanes striking the Southeast US over a short period, hauling rates were put into the record that exceeded $2.20 per mile. There, proponents requested, as a safeguard, payments from the fund would be limited to not more than $2.25 per loaded mile even if documentation could be provided to justify a higher cost.

Finally we reduce the $2.20/(48,000/100) by 33% (multiplying by 67%) to keep within the concept of "Order pricing as a minimum level" standard. By allowing for some Market Administrator discretion (which we will detail later in our testimony), we think this is a reasonable level, even though in other proceedings a lower "percentage of actual" has been presented.

Mileage Factor

For the mileage exemption factor, we suggest that the first 75 miles be excluded from the mileage used in calculating the credit. This would represent individual

producer responsibility for transportation. The 75-mile limit was selected using the following concepts:

1) Relative to the marketing dynamics of Order 33, it is reasonable to include some level of producer responsibility for transporting Class I milk to market;
2) MA Exhibit ___ DFA Request #7 Mideast Marketing Area Producer Milk to Distributing Plants by Distance and Region October 2004 (described in more detail earlier in our testimony) outlines transport distances from production point to distributing plant for October 2004. The last row of data signified by "Average" identifies the average miles that milk, delivered to a Class I distributing plant within a specified region, traveled. For instance, milk delivered to distributing plants in Northern Ohio traveled an average distance of 74 miles. The MA exhibit shows that the average distance for the two reserve supply regions Michigan and Northern Ohio are 71 and 74 miles, respectively. The average transport distance for the other regions are Southern Ohio (a deficit region) 130 miles, Indiana (a "breakeven region") 103 miles and Pennsylvania (a "breakeven region") 97 miles. The entire market has an average of 93 miles of transport haul. We chose 75 miles as the level that is closest to the mileage in the reserve supply regions. Those areas will provide the most supply to other areas and in order to benefit from the credit concept, will need a mileage level that reflects closely the conditions in their area. Also this level of credit will provide benefit to the more deficit areas and help to offset the cost of supplying those markets.
3) DFA Table 7 Summary of Mileage Ranges from Market Administrator Data – October 2004 further defines MA Exhibit 7 by accumulating the mileages up to the 80 mile zone, which would include our 75 mile threshold, and examining what portion of the milk falls into the "exempt" category. The table sums milk by zone

up to the 80-mile limit, subtracts that sum from the total milk in each region and expresses the "up to 80 mile" sum as a percent of the total. The data demonstrates that the 75-mile threshold may provide benefit to approximately 41% of the total market's deliveries if they meet the credit criteria. This calculation ranges from a lower level of 20% in the northern Ohio region where supplies are more available to nearly 70% in the more deficit southern Ohio region.

4) We also chose to put a cap on the miles that could apply for the transportation credit. This cap is now 350 miles, meaning the mileage factor used in calculating the credit will not be more than 350 miles. The original notice had this limitation at 400 miles. For instance, if out-of-area milk is delivered from a distance of 400 miles, the transportation credit calculation will only use 275 miles (350 miles minus 75 miles). We chose this level after examining MA Exhibit ___ DFA Request #6(b). This exhibit shows that 350 miles covers 97.5% of the market's milk movements. We believe this is a reasonable safeguard for the proposal. Also our examination of the delivery mileages to various demand points in the market demonstrated that adequate supplies could, in most cases, be obtained from 350 miles or less.

Applicability of Credit

The credit should only apply to milk delivered from farms to pool distributing plants receiving a Class I allocation. The credit should be paid to the operator of the pool distributing plant or a qualified cooperative who is the responsible party for delivering such milk and which provides appropriate documentation of such to the Market Administrator.

Market Administrator Discretion

Our proposal allows the Market Administrator to periodically investigate the data that may effect either the rate or mileage factors and make changes in either factor if warranted. That investigation may include examination of the distances in the marketplace that milk is hauled to pool distributing plants, the charges for milk hauling, fuel costs, milk transport equipment costs and the sources of milk supplies to the market. By allowing for MA discretion we feel comfortable in requesting a rate of cost recovery of 67%. Fuel costs are variable and could impact aspects of the formula. Giving the MA some discretionary oversight will allow the formula to be adjusted appropriately if it is deemed necessary. Also if milk production continues to decline in the primary supply areas of the market, it would be a normal response for transport distances to increase. As a consequence the mileage limitations could be re-examined.

Our listing of possible discretionary items is not meant to be complete or exhaustive as additional factors may become apparent after the credit is in place. Our goal is to have the Market Administrator make the industry aware of market conditions on at least an annual basis and have the authority to change the rate or mileage factors if conditions and industry sentiment warrant a change. This process could be similar to the process that the California Department of Food and Agriculture follows with its manufacturing cost surveys. It gathers and publishes information with input from the industry but doing so does not cause any automatic change in regulation. We want to utilize the "MA discretion" process in a limited fashion here to avoid the longer hearing process.

Modification for Michigan Deliveries

Because the unique highway weight limits in Michigan allow for significantly higher tank weights than any other state in the Mideast marketing area, a modification of our proposal, not contemplated prior to the Hearing, is necessary. For loads that originate in Michigan and deliver to a pool distributing plant in Michigan a lower rate for the credit formula is necessary in order to avoid over-compensation. Carl Rasch of Michigan Milk will testify to this modification.

Effects on the PPD

MA Exhibit ___ DFA Request #15 Proposed Mideast Transportation Credits Selected Rates by Region October 2004 demonstrate the effect of our proposal on the milk movements that existed in October. Note the modification proposed for Michigan was not considered when this request was made. The effect of that change, however, should reduce the computed impact since the requested modification is a reduction in the proposed rate for a significant portion of the market.

At the time of the request we did not have an exact rate or mileage factor determined so we asked for several combinations to be examined. The computation method summarized in this Exhibit is as we proposed. In each case the Market Administrator had the necessary data to apply the correct Class I percentage at each plant. In each request the computations are made for per hundredweight / per mile rates of $0.0030, $0.0035 and $0.0040. The mileage factors exempt the first 70, 100 and 125 miles, and all computations assume a cap of 400 miles. Since our proposal is for a rate of $0.0031, with a 75 mile exemption and a 350 mile cap, the best-fit comparison is the very first example in the table – the one showing dollar

values for a 70 mile exemption and a $.0030 credit. The table shows that for October 2004, our proposal would have resulted in credits to Class I suppliers of approximately $459,081. The effect of the credit computation on the blend price would have been a reduction of approximately $0.0297 per hundredweight ($459,081 cost / October pool of 1,545,766,665 pounds).

MA Exhibit ___ DFA #19 Sample Computation of the Mideast Transportation Credit outlines each step of credit calculation for several different delivery scenarios. We agree with the explanation of each of the various scenarios.

Proposal Language for a Direct Ship Transportation Credit

1. Insert a new Section 1033.55, to read as follows:

§ 1033.55 Transportation credits.

(a) Each handler operating a pool distributing plant described in § 1033.7(a) or (b) that receives milk from dairy farmers, and each handler described in § 1033.9(c) that delivers milk to a pool distributing plant described in § 1033.7(a) or (b) shall receive a transportation credit on the portion of such milk eligible for the credit pursuant to paragraph (b) of this section.

(1) Transportation credits paid pursuant to paragraph (a)(1) and (2) of this section shall be subject to final verification by the market administrator pursuant to § 1000.77.

(2) In the event that a qualified cooperative association is the responsible party for whose account such milk is received and written documentation of this fact is provided to the market administrator pursuant to § 1033.30(c)(3) prior to the date payment is due, the transportation credits for such milk computed pursuant to this section shall be made to such cooperative association rather than to the operator of the pool plant at which the milk was received.

(b) Transportation credits shall apply to the pounds of bulk milk received directly from the farms of producers at pool distributing plants determined as

follows:

(1) Determine the total pounds of producer milk physically received at the pool distributing plant;

(2) Subtract from the pounds of milk described in paragraphs (b)(1) of this section the pounds of bulk milk transferred or diverted from the pool plant receiving the milk if milk was transferred or diverted to a nonpool plant on the same calendar day that the milk was received. For this purpose, the transferred or diverted milk shall be subtracted from the most distant load of milk received, and then in sequence with the next most distant load until all of the transfers have been offset; and

(3) Multiply the pounds determined in (b)(2) by the Class I utilization of all producer milk at the pool plant operator as described in § 1000.44. The resulting pounds are the pounds upon which transportation credits, as determined in paragraph (c) of this section, shall be applicable.

The language in sections (a and b) authorizes the calculation and payment of the transportation credit. The calculation, while paid based on filings by handlers at pool time, is subject to an audit by the market administrator at a later date. If a cooperative can demonstrate satisfactorily to the market administrator that it were responsible for delivering milk for their account, the cooperative can receive the payment.

The language in section (b) allows for payments to be made for Class I milk only and only for milk physically received at a pool distributing plant directly from a farm. This section further directs the market administrator to perform a "net calculation" so that milk is not trans-shipped through a plant for the purpose of obtaining credit. This calculation is measured daily from records supplied to the market administrator. The calculations for "net" and for Class I percentage are to be made prior to any further calculations of the credit amount. We envision that each handler would apply for credits at pool time, submit the request and supporting data with its market report and receive payment. All submissions would be subject to further verification and adjustment by the Market Administrator.

(c) Transportation credits shall be computed as follows:

(1) Determine an origination point for each load of milk by locating the county seat of the closest producer's farm from which milk was picked up for delivery to the receiving pool plant;

(2) Determine the shortest hard-surface highway distance between the receiving pool plant and the origination point;

(3) Subtract 75 miles from the lesser of the mileage so determined in paragraph (c)(2) or 350 miles;

Please note that (c) (4) was omitted from the hearing notice.

(5) Multiply the remaining miles so computed by 0.31 cent ($0.0031);

(6) Subtract the Class I differential specified in § 1000.52 applicable for the county in which the origination point is located from the Class I differential applicable at the receiving pool plant's location;

(7) Subtract any positive difference computed in paragraph (c)(6) of this section from the amount computed in paragraph (c)(5) of this section; and

(8) Multiply any positive remainder computed in paragraph (c)(7) by the hundredweight of milk described is paragraph (b)(3) of this section.

Paragraph (c) describes the actual credit calculation. The origin point for mileage is the county seat of the producer's farm on the route that is the closest location to the pool distributing plant. This combination was chosen to minimize the data needs necessary to process the credit computation. The measuring point of the closest farm was chosen to minimize the opportunity to structure a delivery to "game the system". Maintaining this data will require much effort initially, but after a database of producer / county / plant locations is established between the industry and the market administrator, upkeep and transmission of information should be easy. The remaining computation is a follows:

1) miles less 75; (this represents the producer responsibility for haul)
2) no payment is made on mileages in excess of 350 miles;
3) remaining miles time $.0031; (this represents the cost per cwt/mile)
4) subtract any positive difference between the Class I differential at

the pool distributing plant less the Class I differential of the county from which the farm location was determined; (this allows for the effect of the Order location differential to be recognized. If the difference is negative it should be ignored. We assume any milk that moves "against the zone" does so because that is the best economic choice and should not be penalized by the credit computation;

5) pay the calculated dollars to the appropriate party.

(d) The rate and mileage limits of paragraphs (c)(4) and (5) of this section may be increased or decreased by the market administrator if the market administrator finds that such adjustment is necessary to better reflect actual conditions present in the marketplace. Before making such a finding, the market administrator shall investigate the need for adjustment either on the market administrator's own initiative or at the request of interested parties. If the investigation shows that an adjustment might be appropriate, the market administrator shall issue a notice stating that an adjustment is being considered and invite data, views, and arguments. Any decision to revise either figure must be issued in writing at least one day before the effective date.

Paragraph (d) allows for Market Administrator discretion in changing both the rate and mileage factors.

(e) For purposes of this section, the distances to be computed shall be determined by the market administrator using the shortest available state and/or Federal highway mileage. Mileage determinations are subject to redetermination at all times. In the event a handler requests a redetermination of the mileage pertaining to any plant, the market administrator shall notify the handler of such redetermination within 30 days after the receipt of such request. Any financial obligation resulting from a change in mileage shall not be retroactive for any periods prior to the redetermination by the market administrator.

This section provides authority for the Market Administrator to periodically review mileage factors and make changes, if necessary. However, no change can be

retroactively applied.

2. Amend § 1033.60 by amending the introductory paragraph and adding a new paragraph (k), to read as follows:

§ 1033.60 Handler's value of milk.

For the purpose of computing a handler's obligation for producer milk, the market administrator shall determine for each month the value of milk of each handler with respect to each of the handler's pool plants and of each handler described in § 1000.9(c) with respect to milk that was not received at a pool plant by adding the amounts computed in paragraphs (a) through (i) of this section and subtracting from that total amount the value computed in paragraphs (j) and (k) of this section. Unless otherwise specified, the skim milk, butterfat, and the combined pounds of skim milk and butterfat referred to in this section shall result from the steps set forth in § 1000.44(a), (b), and (c), respectively, and the nonfat components of producer milk in each class shall be based upon the proportion of such components in producer skim milk. Receipts of nonfluid milk products that are distributed as labeled reconstituted milk for which payments are made to the producer-settlement fund of another Federal order under § 1000.76(a)(4) or (d) shall be excluded from pricing under this section.

* * * * *

(k) Compute the amount of credits applicable pursuant to § 1033.55.

This section causes the corresponding changes to be made to section 60.

Summary

In summary, we request that Order 33 incorporate provisions dealing with dual pooling as a protection against dilution of the blend from milk that does not demonstrate real performance in the market. These provisions have been incorporated or about to be incorporated in Order 1, 30, 32, 124 and 131 and

requested in Orders 5 and 7. If instituted as written, it will prevent milk from simultaneously pooling in a federal order and a state order with a market wide pool.

Secondly, Proposal 2 to enhance the performance standards. Similar changes were requested in 2001. The market needs further adjustment. While Order 33 needs to import some supplemental milk, the current standards allow far more milk to associate with those supplemental purchases than is warranted. Additionally, Proposal 2 will cause more milk to be made available from local sources or exit the pool which will increase blend returns for every day shippers. The proposal treats all suppliers equally as similar increases in standards apply to each pooling handler. The evidence indicates that the Order blend price is inadequate to pay for supplemental supplies from outside the order, attract milk away from local sources and maintain supplies when faced with competition for milk from Order 5 - to the south. This proposal is consistent with the Secretary's approach of making gradual changes towards more stringent performance provisions.

Third, Proposal 7 will curb the practice of depooling. Depooling is disorderly, causes market disruption and makes it difficult to attract a milk supply for Class I use. This proposal is consistent with those made elsewhere in the Order system. Although different in form, its regulatory purpose would be very similar to the Dairy Farmer for Other Markets provisions of Order 1 – which significantly mitigates the incidents of depooling, there. Finally, it is a key component in an effort to establish reasonable performance standards in the Order for in-area and out-of-area milk supplies.

Lastly, Proposal 9 requests a Congressionally authorized payment in the form of a transportation credit to assist those who supply the Class I market and who are incurring extra cost in doing so. The evidence demonstrates that the market has a significant cost in transportation. The cost of the movement of milk beyond the producer responsibility is substantial. This request asks for a portion of that cost to be reimbursed. The proposal is backed by data that shows it to be targeted, effective, modest and workable. Evidence has been presented to substantiate a rate, mileage limits and safeguards to the system.

Need for Emergency Provisions

There is a need for this hearing to proceed on an emergency basis.

1) The issues with depooling will be a problem in the market. Volatile dairy markets know no season. With commodity prices experiencing a recent spike, negative PPDs may again appear in the near future. Since, the Order 30 and 32 hearings, negative PPDs and depooling opportunities have again occurred.
2) Concerns with performance standards also have a very short-term time horizon. The fall shipping season will be here soon and it would be helpful to have a decision prior to that time so that Order provisions will not be an unknown factor in any planning.
3) History shows that California and milk from the Mountain states moved (pooled) very easily through the Order system, shifting from one market to the next as

regulation changed. Producers in Order 33 have no desire to experience the blend damage that occurred in Order 30, and emergency action will greatly help.

4) Finally, the longer a Record takes to process the more problematic the prospects of varying solutions become.

On behalf of DFA, Michigan Milk, Dairylea and NFO, I would like to thank you for your time. The efforts of the Mideast Order staff in preparing data for this hearing is greatly appreciated. They have a well-deserved reputation of being proactive and user friendly and that reputation was only magnified in their effort to produce data and information used here this week.