

**UNITED STATES DEPARTMENT OF AGRICULTURE
BEFORE THE SECRETARY OF AGRICULTURE**

In re:) **DOCKET NOS. AO-388-A15;**
MILK IN THE APPALACHIAN AND) **AO-366-A44; AND DA-03-11**
SOUTHEAST MARKETING AREAS)

**PROPOSED FINDINGS OF FACT AND CONCLUSIONS OF LAW
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I. Introduction

The hearing record is devoid of any evidence supporting a claim that either the Southeast or the Appalachian marketing areas are experiencing disorderly marketing conditions caused by producer-handlers. Yet, proposals five and seven would require a producer-handler to contribute funds to the Producer Settlement Fund on own farm production (i.e. milk not purchased from a producer). These forced contributions will be triggered upon a producer-handler reaching Class I sales in excess of an arbitrarily selected 3,000,000 pounds per month. In fact, there is not a single producer-handler in either region that would exceed the arbitrarily selected three million pound cap. Rather, the record is replete with speculation, conjecture, and inaccurate statements woven together by Dean Foods, Prairie Farms, and Dairy Farmers of America (“DFA”) in conjunction with Southern Marketing Agency (“SMA”), in yet another anti-competitive play. The purpose of proposals five and seven is to encourage and induce the Department to regulate away a “threat” that does not exist so that these large players will never have to face real competition from innovative producer-handlers.

In contrast, proposal number eight would allow producer-handlers to purchase a regulated amount of milk to balance their supply--ten percent (10%) of the producer's monthly milk production during December through May and thirty percent (30%) during June through November. Given the evidence repeated time and again at this hearing, if any marketing area needs a reasonable purchase allowance for producer-handlers, it is the Southeast.

Michael P. Sumners, the proponent of proposal number eight and a dairy farmer residing within the geographic boundaries of the existing Southeast Marketing Area, and Sarah Farms, a producer-handler located in Yuma, Arizona with more than three million pounds of Class I route

disposition per month, submit this brief in opposition to the producer-handler limitations contained in proposals five and seven and the incorporation of producer-handler limitations in any other noticed proposal or modification thereof. Sumners and Sarah Farms support proposal eight regarding purchase allowances for producer-handlers. Michael P. Sumners and Sarah Farms do not express any opinion concerning the provisions of any proposal other than those contained expressly in this brief.

II. The Proponents Have Presented Absolutely No Evidence To Justify Any Change to Producer-Handler Regulations

If this hearing were a trial, the proponents would have lost a Motion for a Directed Finding at the conclusion of their “case.” This is the rare situation where even the witnesses for the proponents have admitted that there is no evidence supporting their proposals. Indeed, each of the three key witnesses who testified in support of a three million pound cap freely admitted that the request was not based on actual marketing conditions in Order Five or Order Seven and that no disorderly marketing conditions have occurred in either the Appalachian or Southeast marketing areas.

Since there is no evidence to support the proposed limitation on producer-handlers, then the Department must ask itself, “Why would DFA, Dean Foods, and others expend the substantial resources to advocate a position which is unsupportable by the facts?” The answer is simple. The largest cooperative in the country, the largest processor in the country, and those industry giants allied with them seek to eliminate producer-handlers from the dairy marketplace. This is a vendetta that has been pursued in courthouses, in other federal order hearings, and most recently in Orders 124 and 131. It is apparent that these dairy behemoths will use every opportunity to attempt to regulate producer-handlers out of existence. This hearing shows the

extent to which these companies will go. Evidence is not important; rationality is nonexistent; and money is no object.

The adoption of any limit on producer-handlers would represent a complete reversal of Department policy that has been in place for over 70 years. In order to make such a drastic change in policy, the Department has always required a particularly strong showing of hard facts and data demonstrating great injury or market chaos. The proponents here bear the heavy burden of proving that the marketing conditions in Orders Five and Seven have, in fact, significantly deteriorated between the completion of order reform in January 2000 and February 2004. In the past, absent such evidence, the significant changes of policy such as those requested here should not and have not been granted.

The proponents' witnesses have admitted that there is no evidence, let alone the quantum of evidence required to change long-standing department policy. The hearing record reflects that the proponents have no basis for bringing proposals five and seven to the Department. For a great deal of this brief, Sumners and Sarah Farms will rely almost entirely on the words of the proponents' supporting witnesses.

A. There is no evidence of disorderly marketing resulting from producer-handlers in Orders Five or Seven.

Witness for the proponent SMA/DFA, Elvin Hollon presented over 130 pages of typewritten testimony. Despite the voluminous testimony offered, there was no evidence of disorderly marketing conditions caused by producer-handlers in Orders Five or Seven. In fact, Mr. Hollon conceded as follows:

Q. Can you give us, please, any information for the years 2000 through now that shows that any regulated handler lost a specific account to a producer-handler in 5 or 7?

A. I cannot.

Q. Can you tell us then any information that you intend to present, or that you're aware will be presented when we finish this -- through the course of this hearing before we finish as to a specific time when a regulated handler lost a particular account to a producer-handler?

A. I am not aware of any.

Q. Can you tell us currently, as it exists today, through your testimony right this minute, any specific example of disorderly marketing created by a producer-handler in 5 or 7?

A. The thrust of our testimony has been to show examples of where disorderly marketing could exist on a perspective [sic] basis.

Q. And I didn't ask you that, Mr. Hollon. I appreciate what you said, and if they want to ask you on redirect, they can. Give me --

THE COURT: I'll allow that -- I'll allow that answer, though. I think it was responsive. Go ahead.

BY MR. RICCIARDI:

Q. Okay. Go ahead.

THE COURT: Well, he gave the answer.

THE WITNESS: I was done.

BY MR. RICCIARDI:

Q. Okay. So what your testimony is is that you think things may happen in the future, but you have no specific information that it has occurred in the past in 5 or 7, correct?

A. That is a part of our testimony.

Q. Well, then give me specific examples of where it occurred in the past in 5 or 7.

A. That wasn't the way I interpreted your question. You asked me was that the only thing that we -- the only comment that we were making -

Q. And maybe --

A. -- and I said no, it's not the only comment that we were making about producer-handlers.

Q. And I apologize. Maybe my question was poorly worded. This one will be hopefully better. Give me specific examples of any disorderly marketing that has occurred, to your knowledge, in 5 or 7 as a result of producer-handlers' activities.

A. The producer-handlers activities with regard to customers and sales movements, I'm not aware that there are any.

Hollon, 709-711. Dean Foods' witness also conceded that there are "a very small number of very small producer-handlers" in Orders Five and Seven and that their collective impact on the market is less than "negligible." Christ, 827.

Despite presenting a "study" intended to speak to disorderly marketing in Orders Five and Seven (which was prepared for a prior hearing), DFA/SMA's accountant witness admitted during cross-examination that he never took the time to look at the data regarding the impact of producer-handlers on the Appalachian and Southeast Orders.

Q. And the information that you have presented through what was marked there as exhibit 25 is that study that was used specifically for order 131. Am I correct?

A. Yes.

* * *

Q. Now. You do not have in your study, and you do not have by your testimony any specific processing costs for a producer/handler in five or seven, correct?

A. That's correct.

Q. You don't, in fact - - let me ask you a question. How many producer/handlers are there in five, currently?

A. I'm not sure. I'd have to study that.

Q. Are there any?

A. I don't know.

Q. How many producer handlers in seven?

A. I don't know that specifically, either.

Q. How many pounds of milk, if you know per month are producer/handlers selling into either of these markets?

A. I have not studied that.

Q. Tell me one example of disruptive marketing caused in five or seven by a producer/handler in the last year?

A. I have not studied producer/handlers in five or seven.

Herbein, 477, 481.¹ These statements are representative of the alleged "factual bases" for the proponents' requests.

¹ The Department, Michael Sumners, and Sarah Farms all objected to the introduction of Carl Herbein's prior testimony. See Ex. 57, 69. Herbein's testimony and Exhibits 57 and 69 are the subject of a separate Motion To

B. Regulations Must Be Based On Proof, not Speculation and Conjecture

This hearing is entirely prospective in nature. Every bit of testimony offered by the proponents was based on speculation and fear about what might happen. After arguing, without supporting evidence, that a large producer-handler can gain market share at will, the DFA/SMA witness followed the statement with this caveat, “This seems to describe the retail market scenario in Order 131, and **is the concern** in Order 7 and 5 as well.” Hollon, 664. Testimony from several witnesses referred to marketing conditions in the future tense and speculated about events that might occur as demonstrating the need for these amendments.

Absent real evidence of market disorder created by producer-handlers in Orders Five and Seven, proposals five and seven must fail. Rather than facts, proponents rely upon hyperbole and hypothesis:

Q. Let me talk about this then. Tell me, as specifically as you can, in Orders 5 and 7 what disorderly marketing conditions have occurred since Federal Order reform that would require the change in producer-handler status.

A. Our proposal deals with possibilities.

Hollon, 729 (emphasis added).

The DFA/SMA witness also asserted that large producers could become producer-handlers and take over significant Class I sales, which would supposedly ruin the Order:

Just as in the initial hearing in Phoenix, there are likely some individual in this room today who are here to get schooled on how to exploit these provisions and to learn whether this loophole will be there in the future for them to exploit. . . .

The drive to exploit this loophole is, or will, create organized disorderly

Strike. *See* 7 C.F.R. § 900.8(d)(2). The discussion of Herbein’s testimony in this brief is not a concession of its accuracy or admissibility.

marketing.

Hollon, 649-50.

Despite these claims of impending disaster, the witness admitted on cross-examination that the opportunity for these “fears” to be realized is not a new occurrence.

Q. Okay. Let's talk about startups then. You also told him that there have been, in the last several years in 5 and 7, some new larger startups in that area, correct?

A. Yes.

Q. And none of those new startups have been producer-handlers, correct?

A. That is correct.

Hollon, 771. Dean Foods' witness concurred with Mr. Hollon's assessment of new farm startups:

* * *

A. . . . [O]ne issue is the past and another issue is the future, and the prospects with the development of much larger dairy farms is greater that there will be an effect in the future.

Q. Well, you've heard the testimony, and I think it came from Mr. Hollon, and then I followed up with it. The fact is there have been a number of larger farms that he, at least, was aware of in the last three years that have begun operations in 5 and 7, and none of those have become producer-handlers, correct.

A. That's correct, and they would have been identified in the marketing industry data, yes.

Q. That's right.

A. But those farms exist, according to his testimony.

Q. And they came into play in the last three years, were built, and obviously producer-handler exemption was available then, and they chose not to take that exemption, correct?

A. That's correct.

Christ, 827-28. Quite simply, there is no forthcoming wave of producer-handlers, despite what the proponents would suggest. Indeed, the DFA/SMA witness acknowledged that if being a producer-handler were lucrative, greater numbers of them would be expected. Hollon, 701-02.

Any potential for producer-handler growth has existed in the market for many years, and the current situation is no different. However, there is still no real producer-handler activity in this market. Moreover, the addition of producer-handlers to these orders would actually help to foster the policy behind the AMAA of ensuring an adequate supply of local milk. It would be premature to enact regulations dealing with marketing conditions that do not currently exist. Speculating now puts the Department in the position of creating inefficiencies based on ignorance of future events and results.

DFA/SMA and Dean Foods have presupposed that a producer-handler presence is *per se* disruptive to the marketplace. Absent real, verifiable evidence, which is sorely lacking at this hearing, the Department cannot make any such finding. In fact, it is just as likely that producer-handlers in Order 5 and 7 would improve the marketing of milk in the areas.

C. Regulations Can Only Be Changed Based on Actual Events in Orders Five and Seven

Evidence to support a dramatic change in Department policy must come from verifiable evidence of marketing events **in the affected marketing areas only**.

Q. By rule, don't you have the opinion that the Secretary can only consider evidence relating to marketing conditions in these two Federal Order areas and no other?

A. I think prospective effects of plausible causes is a marketing condition.

Q. Do you recall when you did testify in the 131 and 124 proceedings, you were under oath, as you are today?

A. Yes, I remember.

Q. And you recall being asked some questions by Mr. English on this particular topic as to what should be considered, and let me see if you recall these questions and answers. This would be at page 1587, beginning at line 15. Now, under -- with your experience of Federal Orders, what orders are open for consideration at this proceeding? Answer: In this proceeding -- in these proceedings, there are just two orders, Federal Orders Number 124 and Number 131. Do you recall giving that answer?

A. Yes.

Q. Question: And what evidence should the Secretary be considering with respect to these proceedings? Answer: I believe by rule he's required to consider evidence relating to marketing conditions in these two Federal Order areas and none other. Do you recall giving that testimony?

A. I don't recall it specifically, but I accept that as being correct.

Christ, 815-16. In this case, the substantial restrictions on the growth of producer-handlers in Orders Five and Seven advocated by the proponents can only be adopted if the proponents come

forward with proof of market disruption directly caused by producer-handlers. No such proof exists.

Q. Sure. Can you tell me any specific producer, farmer, dairy farmer, in 5 or 7 that's been required to terminate its business due to the actions of a producer-handler?

A. Any producer who's been required to terminate their business --

Q. Yes.

A. -- through the act of a producer-handler?

Q. Yes.

A. I'm not aware of any.

* * *

Q. Thank you. Now, the last three items in Exhibit 61 are -- the last two items, excuse me, I and J, I believe you testified to this, but let's also make it clear. This is information that was specifically taken from the hearing in 131 and 124, correct?

A. This is information that was requested for that hearing that I have reviewed and detailed and asked questions about both before and at the hearing, yes.

Q. And none of the information in I and J relates to anything that has occurred currently or in the past in 5 and 7, correct?

A. Correct.

Q. This has to do with, as it says, Federal Order Number 131, correct?

A. Correct.

Hollon, 732-33, 740-41.

Notwithstanding 7 C.F.R. 900.1 *et seq.*, which outlines the rules of practice and procedure governing these proceedings, DFA/SMA ignore the rules and create their own when no proper evidence exists. The only rule that appears to govern DFA/SMA's conduct is that which furthers its economic interests. The DFA/SMA representative admitted as much:

A. [sic, Q.] The position that you adopt here -- I'm not going to read it all to you, but basically what you're saying is the proponents of this proposal seem to basically support the reason for the proposal by looking at parts of the country outside the southeast, and so you say even if there is evidence of the need for smaller and more numerous orders outside the southeast, this does not provide any evidence that more orders are needed in the southeast. That's your position.

A. That's correct.

Q. Okay. Now, with regard to the producer-handler issue, you've taken the position that the Secretary should look to an area in Arizona to try to make determinations for Federal Order 5 and 7.

A. That's not a correct characterization.

Q. That's part of what you said, isn't it?

A. The correct characterization would be that the Secretary should consider things that have happened in the Arizona market as potential to happen in the southeast.

Q. So with regard to producer-handler issues, the Secretary should look outside of Federal Orders 5 and 7. With regard to this particular proposal which you are against, the Secretary doesn't need to look outside because they don't need to look at evidence for more orders outside the southeast but only in the southeast, right?

A. No, that's not correct.

Q. Okay. So I read your statement incorrectly?

A. No, you interpreted it incorrectly.

Q. Okay. So tell me then how you can intellectually coordinate those two positions.

A. Okay. There have been several statements made at this hearing regarding the St. Louis market and the reason for doing things in this market would be its impact on St. Louis. We're saying that that's an incorrect piece of logic. We have said concurrently, at the same time, that there are situations regarding producer-handlers that have happened in other parts of the country and that that can --that logic can be applied.

Q. Okay. So, again, you don't want the Secretary to look outside of Federal Orders 5 and 7 in this particular proposal, but you do want the Secretary to look out of -- outside of Federal Orders 5 and 7 for the producer-handler issues. That's your testimony, correct?

A. Yes.

Hollon, 967-969. Evidently, when marketing conditions outside of an area subject to a hearing allegedly further DFA/SMA's objectives, such evidence must be admitted. When that evidence does not support DFA/SMA's position, it must be excluded. In other words, the sole criterion is, "What is good for DFA/SMA?". Apparently, intellectually dishonest, unfounded, or duplicitous positions are warranted if they contribute to cooperative revenues.

III. The Supporting Rationale Offered Up By the Proponents To Limit the Growth of Producer-Handlers Do Not Reflect Long-Standing Department Policy

The position of the Department on the continued exemption of producer-handlers has been made clear in the *Gore* and *Heartland* rulemaking decisions and has nothing to do with administrative convenience, efficiency of operations, milk processor assessments, or the other red herrings trotted out by the proponents.

Although the marketing of milk by producer-handlers has the potential of creating disorderly marketing conditions, it has not been found necessary to regulate fully this type of operation. In fact, the policy has been to exempt such types of operations. Such policy has been based, generally, on findings in regulatory proceedings that producer-handlers have no significant advantage in the market in their capacity as either handlers or producers as long as they are solely responsible for their production and processing facilities and assume essentially the entire burden of balancing their production with their fluid milk requirements.

54 Fed. Reg. 27179, 27182 (June 28, 1989). More recently, changes to producer-handler status were considered and dismissed during order reform.

Public comments were received regarding the extent of regulation that should apply to producer-handlers. The majority of public comments supported the status-quo regarding the regulatory treatment of producer-handlers, emphasizing that they should remain exempt from regulation in accordance with current order provisions and that the provisions should be regional in nature so as not to affect or change the current regulatory status of producer-handlers. One of the public comments received proposed that the exemption of producer-handlers from the

regulatory plan of milk orders be eliminated. **This proposal is denied.**

64 Fed. Reg. 16135 (April 2, 1999) (emphasis added). The rationale conjured by the proponents are ruses to disguise their monopolistic play as rational policy making and have nothing to do with justification for producer-handler status.

A. The Herbein/Cryan testimony is dependent on the validity of the Herbein study, which is fatally flawed in its methods and its transparency.

The author and creator of Nero Wolfe, Rex Stout, has had attributed to him the following quotation, “There are two kinds of statistics, the kind you look up and the kind you make up.” Carl Herbein won’t let anyone look up his statistics. Rather than providing a transparent analysis, his testimony is a case study in hiding the ball. Herbein’s study is comprised of hand selected data, pulled from a data base that no one can see, compiled into categories that no one can verify, adjusted for regional prices that were calculated in a way that no one can examine, and applied against prices at stores that nobody has shown the Department or the opponents. Reliance on Carl Herbein’s study is reliance on the unknown. It is reliance on the unseen and on the unverifiable. The Department has demanded in the past and should demand today more from those who wish to change policy than what DFA and Carl Herbein have offered.

Rather than show true and actual data from their own operations subject to cross-examination by the opponents, the proponents substituted the Herbein “study” as a proxy. In doing so, they denied the opponents any ability to cross-examine the truthfulness or applicability of the “facts” which Herbein propounded. In reality, the silence of true facts from the real market participants is ample evidence that the alleged price advantage of producer-handlers does not exist. Had it existed, the proponents would have provided real evidence rather than a fabricated study advanced in order to justify a predetermined result.

Mr. Herbein's testimony established that his study was conducted during the summer of 2003 while the cap figure was selected in the year 2002 or before. This timing shows that Mr. Herbein's study was (1) engineered to demonstrate a breakpoint somewhere near 3,000,000 pounds or that (2) the dartboard selection of a 3,000,000 pound cap over one year before Mr. Herbein was retained was astonishingly accurate. Of course, Mr. Herbein has not provided the Department with any of his underlying data or any way to assess the validity of his tests so the Department will never know which is the case.

The one place Mr. Herbein says we can verify his numbers says that Mr. Herbein is way off. The Cornell Study, of which official notice has been taken, involves only plants with processing volumes greater than 11.7 million pounds per month. Cornell, p. 5 ("Processing volume for all plants ranged from 1.36 million gallons to about 5.98 million gallons per month (11.7 million pounds to 51.5 million pounds).") For the data where plant costs do crossover, the costs reported by Mr. Herbein are higher than those reported by Cornell by 11 to 15 cents per gallon. Compare Herbein's range of plant processing costs for plants 12 million pounds and over (33.5 cents to 43.4 cents) to that for the Cornell Study (12.3 cents to 28.0 cents). Ex. 57, "Herbein B"; Cornell, p.15.

Not only are the SMA cooperatives asking the Department to rely on Carl Herbein's testimony, but other witnesses have used Carl Herbein's testimony to enhance or add to their own testimony. Roger Cryan of National Milk Producers Federation stated that Carl Herbein's data was quite applicable to this hearing in assessing whether a processor was efficient enough, despite the fact that the data in Dr. Cryan's analysis for plants smaller than 12,000,000 pounds of production per month is gleaned entirely from the study of Carl Herbein, which as stated above, is sorely inaccurate. Carl Herbein's data provides the lone reference for the most important

section of the Cryan testimony. Accordingly, if Mr. Herbein's testimony is faulty then, as night follows day, the testimony of Dr. Cryan must similarly be dismissed.

In addition, Mr. Herbein committed errors in his methodology, including (1) utilizing a sample size that was too small; (2) utilizing plant data from plants other than producer-handlers to predict costs for producer-handler plants; (3) utilizing plant data for plants outside Orders Five and Seven; (4) failing to account for differing product mixes and distribution; (5) utilizing adverse (or judgmental) selection as opposed to random selection; and (6) utilizing the consumer price index to adjust non-consumer costs. It is obvious that in addition to the paramount question of transparency, there are large problems with the testimony of Carl Herbein and others who rely on his "study."

B. The Justification For Selecting a Cap at Three Million Pounds Was Fabricated after the Cap Was Arbitrarily Chosen

The proponents' justification for the three million pound cap was created after the cap itself was selected. On that basis alone, the Department should reject the cap. A three million pound "cap" was first proposed in June 2002 when United Dairymen of Arizona requested a hearing on producer-handler activity in the Arizona-Las Vegas marketing area.² This arbitrarily selected number was then, presumably, carried over to this hearing.

Fundamentally, DFA/SMA, Dean Foods, Prairie Farms, and others seek to regulate producer-handlers based upon retail sales and to establish a trade barrier by denying producer-handlers access to larger marketers who have a broader geographic reach. The Department is not authorized to regulate retailers, nor is it authorized to regulate producers. This argument

² Michael P. Sumners and Sarah Farms note that the hearing notice (Ex. 1) containing the requested three million pound cap for Orders Five and Seven was published on January 23, 2004—at approximately the same time as the final week of the hearing on UDA's initial proposal in Orders 124 and 131.

demonstrates that these proposals would result in the regulation of producers who are also handlers by looking to their activity in the retail markets.

The testimony of the DFA/SMA witness demonstrates the inability of the proponents to rationalize the true impacts of producer-handler volumes on the market. Instead of aggregate producer-handler volume in the marketing area determining an “appropriate” cap, the proponents are more interested in finding that point at which a producer-handler is perceived to be a competitive factor and pre-empting that competition.

Q. Let’s assume in a marketing area you’ve got ten producer-handlers that market up to a million pounds of milk a month.

A. Each or a total?

Q. Each.

A. Each? Okay.

Q. In that market then we’ve got producer-handlers that are producing ten million pounds a month, right? Correct?

A. Correct.

Q. And – that’s fine. And in that situation, under any of the proposals that are made regarding limitations of producer-handlers, none of those producer-handlers would be limited in size.

A. Correct.

Q. Now, instead, if we take a producer-handler in that same market who produces ten million pounds a month -- so we’re taking nine participants out, and we’ve just taken the same volume and transferred it to the producer-handler, your position is that that alone would be enough to have the Secretary limit the

producer-handler exemption and make that person a regulated handler, right?

A. That would be correct if the producer-handler's volume of Class I sales in a marketing -- in any marketing area or any market where it's greater than three million pounds in a month --

Q. And the only distinction --

A. -- we would propose that they be regulated and, you know, be treated for price purposes like any other handler.

Q. And the only distinction in my hypothetical between the two things is we've taken ten participants producing ten million pounds and reduced it to one participant that is producing ten million pounds, correct?

A. Well, our proposal is that three million pounds, if there were a proposal -- perhaps you might make one -- we might give it consideration and support to move the limit from three down to one. But --

Q. Didn't ask you that, Mr. Hollon. What I asked you was the only distinction in my hypothetical was what we've done is we have the same volume. We just knocked the participants, producer-handlers, from ten down to one. Correct?

A. Yes.

Q. All right. Thanks. Now, let's take this situation. Same market. Okay? Now we've got three producer-handlers. For each marketing, 2,999,999 pounds of milk per month in that particular market.

A. Yes.

Q. In that situation, none of those producer-handlers would be required to automatically become a regulated handler under any of the proposals, correct,

because they're less than three million?

A. Correct. That's correct.

Q. And can you tell me the difference in the market in my third hypothetical versus my second? How is the market impacted differently when you have three producer-handlers at 2,999,999 versus one producer-handler at 10 million pounds?

A. Well, there's always --

Q. Other than a pound here or there?

A. There's always the possibility that the end results may be similar, so that would be one. And so there may be, indeed, an impact that may, you know, cause some relook at the situation at that date. So that situation would arise. We may come back to the Secretary and say, you know, we're concerned about this situation and we would like to do something about it. Secondly, the impact, as we have seen in other areas, of a single entity of sufficient size appears to be greater on the market than a smaller entity, and the ability to service, perhaps, a larger retail chain without the requirement of paying class prices is greater.

Q. Is that your answer?

A. Yes.

Hollon, 722-25. None of the offered justifications carry the day. If anything, the proponents have proven only that their three million pound cap number was arbitrarily selected and that attempts at any justification for this figure were made later.

IV. The Producer-Handler Provisions in Proposals Five and Seven Represent an Anti-Competitive Play by “Old Dairy”

The proponents of these proposed limitations on producer-handlers are giants in the dairy industry. Proposals five and seven were submitted by Dean Foods, the largest milk processor in the nation, and Prairie Farms, with dairy plant operations in twelve states. Southern Marketing Agency (“SMA”), who joined in supporting the producer-handler provisions in proposals five and seven represents nearly all of the milk supply in the marketing areas, including that of Dairy Farmers of America (“DFA”), the nation’s largest cooperative.

DFA may claim support for the Federal Order system, but its actions speak louder than its testimony. When the Federal Orders, in DFA’s assessment, conflict with its self-interest, out they go. “[I]f the large producer-handler can earn a return and grow his business, pressure to terminate the orders will be impossible to resist.” Hollon, 666. (See also www.dfamilk.com/newsroom/audio/Ehclip%2001.mp3 where Mr. Hollon refers to Federal Orders as “good tools” for generating revenue but explaining that the Western Order was voted out because DFA felt that “we had more revenue for DFA producers without a Western Order than with a Western Order.”) The incongruity here is that DFA speaks about regulating producer-handlers and simultaneously is deregulating an entire marketing area for the first time in modern history, with no replacement at hand.

Similarly, Dean Foods Company petitions the Department to regulate against non-existent competition, while it has constructed a large bottling facility in Clark County, Nevada that is exempt from regulation entirely. Thus, Dean Foods is currently capitalizing on the largest single unregulated population center in the nation. Ironically, at the same time as Dean Foods is taking advantage of this regulatory loophole, it is complaining that producer-handlers are

somehow “unregulated.” The fact is, however, that producer-handlers are and have always been subject to extensive government regulation and audit—more than Dean Foods’ plant in Clark County can ever be.

This hearing follows repeated regulatory hearings, lawsuits, and legislative efforts targeting producer-handlers. The producer-handler provisions in Proposals five and seven come on the heels of a three-week hearing in Orders 124 and 131 on this very issue. Dean Foods, Prairie Farms, and DFA/SMA have now bootstrapped their producer-handler proposals to this hearing. It is likewise apparent that this hearing is not the end of these maneuvers. Dean Foods, DFA, and others of their ilk will not stop until all competitors in the marketplace are eliminated—fairly or unfairly. Of course, this is not surprising given DFA’s penchant for anti-competitive activity.

In addition to openly speculating about the future ills that producer-handlers will inflict, the proponents have resorted to misstating facts in their arguments. One such fallacious argument raised by the proponents is that producer-handlers do not play by the same rules. Lee, 570. This is untrue. Every single producer and every single handler has the right to become a producer-handler at any time. Their choice to not avail themselves of the producer-handler provisions is one that they have made to their best economic advantage.

The playing field is already level; all participants have an equal opportunity to compete. Simply because some have decided that one particular course of action is most economically advantageous, that does not mean that others who have reached differing conclusions are unfairly treated or do not have the same opportunity.

Indeed, if the playing field is tilted at all, it is tilted as a matter of economic reality in favor of the larger market participants. Large processors enjoy the financial advantage of a

captive market and vertical integration. Others can leverage their size and geographic scope to gain market share regionally by shifting resources and profits from one plant to another. The comparatively smaller producer-handlers do not have any of these economic luxuries. Dean Foods has dairy sales exceeding \$8 billion per year and exerts significant national control in the dairy industry. DFA owns plants and has the ability to absorb plants, enter into joint ventures, etc. SMA controls virtually every drop of milk marketed in the area.

The canard that these regulations are required in order to “remove a regulatory loophole” is equally misleading. The use of the word “loophole” implies that someone has found a way to obtain a result in a way not contemplated by the law. That is not the case here; the producer-handler exemption is long-standing, long-debated, and has survived numerous challenges. All participants know of its existence, but few have embraced it and its appeal has been limited.

In actuality, the aim of the proponents and the other witnesses testifying in support of these proposals is to eliminate producer-handlers from the market place. *See Cryan, 584.* The goal of these changes is to stifle competition in the marketplace and to secure additional market share for the giant dinosaurs of the dairy industry. The goal is also to foreclose the establishment of innovative dairy operations that would otherwise compete with the proponents. It is nothing more.

Producer-handlers are the epitome of entrepreneurial risk takers that should be encouraged and not discouraged. The producer-handler bears, by law, the entire risk of its operation. There is an investment in livestock, real estate, property, employees, equipment, plants and facilities, shipping capacity and others. This investment is that of the producer-handler and not of the marketplace. This investment was made in reliance upon regulations and policy that has stood for over 70 years. To take fairly earned profits from these operations every

year and distribute it among their competitors or the marketplace is anti-American. It is the antithesis of capitalism. It also raises serious constitutional questions, such as violation of due process under the Fourth and Fourteenth Amendments to the Constitution.

V. Congress Has Not Authorized USDA To Regulate Producer-Handlers

The AMAA provides authority to establish minimum prices paid to producers for **purchases** of raw milk. 7 U.S.C. § 608c(5)(A). By definition, producer-handlers do not purchase milk from their farm operations. The AMAA contains specific references to producer-handlers that demonstrate a total exemption for milk produced by the entity that processes the raw milk. For example, Section 8c(5)(k)(I)(11) requires that certain tax-exempt producers be treated as producer-handlers.

Ideal Farms v. Benson, 288 F.2d 608 (3d Cir. 1961), does not accurately reflect the application of the AMAA to the situation of a true producer-handler. The Court in *Ideal Farms* misinterpreted the importance of the phrase “including producers who are also handlers.” 7 U.S.C § 608c(5)(c). Because producer-handlers were exempt from the minimum pricing required under 608c(5)(A), Congress found it necessary to limit the exemption to only that milk produced by a handler, and not to that milk which a producer might acquire from other producers. Had Congress intended the Department to require producer-handlers to pay into the pool on their own farm production, such a statement would be superfluous. In short, there are producer-handlers who only use their own milk, and there are producer-handlers who purchase additional supplies from other producers. While the Department can regulate the purchases made by the latter, it has no authority to assess the former.

The statement that the milk is “acquired for marketing” is unnecessary to give plain meaning to the statute and to effectuate its terms. The facts in *Ideal Farms* are not completely

stated. The terms of the “lease” of the farms are not stated, but it takes no imagination to figure out that the “leases” were merely a scheme to call what was truly a purchase of milk something else in order to avoid the regulations. That is not the case with producer-handlers. Under current definitions, the farm and the plant are required to be maintained at the farmer’s “sole risk and enterprise.”

A producer-handler does not “acquire” its raw milk. To acquire means, “to gain possession or control of; to get or obtain.” All of these concepts, gaining possession of, getting, and obtaining, imply the wresting of possession or ownership from a prior owner. To produce means “to bring into existence; to create.” Production is an action undertaken by the originator or the initial owner. Secondly, an “acquisition” is not necessarily a “purchase.” To purchase includes the concept of acquisition, but also contemplates an exchange of value, “the act or instance of buying.” The single entity producer-handler does not do either. To make this claim is both a legal and factual fiction and requires a leap in logic which the Department should not make.

Because the producer-handler is a single operation, any regulations that limit the ability of the producer-handler to produce additional quantities of milk will necessarily affect the producer-handler in its capacity as a producer. Congress has repeatedly expressed that the ability of the producer to produce milk shall not be regulated. *See* 7 U.S.C. § 608c(13)(B) (“No order issued under this Chapter shall be applicable to any producer in his capacity as a producer.”) The proposed amendments force the producer-handler to choose between paying into the pool for its own farm production and limiting the size of its production. To assess a producer-handler on its own farm production will necessarily regulate the operation of its farming plans. To do so violates the AMAA’s prohibition on marketing orders that regulate producers.

In addition, Congress has repeatedly expressed that the legal status of producer-handlers is not to be altered. While the most recent two farm bills did not contain such an expression of intent, Congress did not change its position on the legal status of producer-handlers. Indeed, the Department summarized the history of Congress's position on the status of producer-handlers in his proposed rules following order reform:

In the legislative actions taken by the Congress to amend the AMAA since 1965, the legislation has consistently and specifically exempted producer-handlers from regulation. The 1996 Farm Bill, unlike previous legislation, did not amend the AMAA and was silent on continuing to preserve the exemption of producer-handlers from regulation. However, past legislative history is replete with the specific intent of Congress to exempt producer-handlers from regulation. If it had been the intent of Congress to remove the exemption, Congress would likely have spoken directly to the issue rather than through omission of language that had, for over 30 years, specifically addressed the regulatory treatment of producer-handlers.

64 Fed. Reg. 16135 (April 2, 1999). Congress expressed its intent that dairy producers have the choice to elect producer-handler status. Proposal eight furthers that Congressional mandate by enabling producer-handlers in the Southeast to more successfully balance their supply and demand.

VII. The Option of Becoming a Producer-Handler Provides Producer Choice and Protects the Dairy Farmer

The purpose of the Federal Milk Marketing Orders is to provide an adequate supply of good and wholesome milk to the consuming public at a reasonable price. This is consistent with

the intent of Congress in passing the AMAA, as expressed at 7 U.S.C. § 602(4):

It is hereby declared to be the policy of Congress . . . to establish and maintain such orderly marketing conditions for any agricultural commodity enumerated in Section 8c(2) as will provide, in the interests of Producers and Consumers, an orderly flow of the supply throughout its normal marketing season to avoid unreasonable fluctuations in supplies and prices.

Additionally, 7 U.S.C. § 608c(18) refers directly to the purpose behind the establishment of minimum prices paid to producers:

The Secretary of Agriculture . . . shall fix prices as he finds will . . . insure a sufficient supply of pure and wholesome milk to meet current needs and further to assure a level of farm income adequate to maintain productive capacity sufficient to meet anticipated future needs and be in the public interest.

In recent years, the availability of a milk producer to market their milk independently of the cooperative structure has dwindled. Integration in the number of processing outlets, decreasing numbers of cooperatives, and increasing farm size has left producers in many markets with limited buyers for their product. With the advent of SMA, the differences among the remaining cooperative options become even more blurred. Michael Sumners testified that such integration and monopolization only restricts producers' ability to differentiate among outlets for their milk:

My situation is not unique. The ability of the dairy farmer to independently market his or her milk outside the cooperative structure is quickly disappearing. There are fewer and fewer cooperatives each year, fewer processing plants and

processing companies today than there were three years ago. Dean Foods has recently announced it will close even more plants.

The evidence presented at this hearing in support of the merger of Orders 5 and 7 established that two processing companies control over 40 percent of the pool plants in these orders, and the Southern Marketing Agency is responsible for marketing a huge majority of the milk sold in the Appalachian and Southeast Marketing Areas, which DFA controls the majority of the milk.

Sumners, 976. Today, a producer who feels mistreated by the dominant cooperative in his marketplace is limited in recourse. The choices available to milk producers are vanishing.

One option that has always been available to the producer, and remains an option today, is for that farmer to bottle his own product and take on the significant risk of farming and marketing. This last check on the power of a corrupt or unresponsive cooperative is placed at risk by proposals five and seven.

Rather than find ways to restrict the producer-handler option, the Department should encourage the establishment and growth of these small businesses. At a very minimum, the current policies toward producer-handlers should remain. If the milk producer is to have any control over his or her own destiny, independent of the cooperative structure, producer-handler status needs to be a viable option. In the Southeast, it is not.

Seasonal fluctuations in milk supply effectively foreclose any ability for the producer-handler to maintain a customer base throughout the year without incurring huge milk surpluses during the flush months. In most Orders, the 150,000 pound purchase allowance alleviates the strict requirements that the producer-handler use solely their own supply. However, Orders 5, 6, and 7, have no such provisions. Accordingly, the influence of producer-handlers in these Orders

has been minimal. *See* Sumners, 977-78. Proposal eight affirmatively addresses the lack of a purchase allowance and the associated balancing problems for producer-handlers:

There are no producer-handlers of consequence in these markets today, largely because they cannot balance supply economically. Producer-handlers would be a plus to the marketing area because they would directly service the Class It [sic, I] needs of the market, which are now serviced in large part by milk produced outside the area and shipped in at the expense of local producers and consumers. Producer-handlers also provide fresh milk to the consuming public at a reasonable price. In addition, producer-handlers can service niche markets and small clients, possibly ignored by larger processors. Also, producer-handlers provide competition to the marketplace, which is good for consumers and dairy farmers.

Sumners, 979.

The current situation in the Southeast is such that at least some producers feel that the true value of their milk is received by those who do not service the market:

If you look at mailbox prices, blend prices and award of [sic, over-order] charges, which are all public information, plants can be paying over \$2 award [sic, order] price for milk but receiving -- producers in southeast may be receiving blend prices or even below some months if you're a co-op member. That money has to be going somewhere, but it's not coming back to the farmers in the southeast.

Sumners, 994. Given such inequitable treatment at the hands of cooperatives, producers must have a viable club in their arsenal. The modest purchase allowances contemplated by Proposal Eight provide such an option:

Q. Tell us the reasons why you have gone ahead and provided Proposal Number 8 to the Secretary.

A. Because -- the main reason, I want to make a producer-handler option in the southeast with -- the co-ops come here (indiscernible) and -- that are all trying to regulate their (indiscernible) [sic, competition] and I would like to maybe just step out of all that and market milk, and there's fewer and fewer people to deal with, and as a dairy farmer, if you deal with a co-op, that means their legislative agenda, you're part of that. In my views -- and dairy marketing is not what their -- there are a lot of things they do that I don't agree with.

Q. Do you have an opinion as to whether or not you think it's fair at this point under Federal Orders 5 and 7 for a producer-handler not to have any type of allowance in terms of purchasing milk when milk would be required to balance?

A. Well, if you look at the other orders that do have provisions to buy milk, and these are deficit orders, and they can't buy any milk, that -- it looked like to me it ought to be more alike. And because of the southeast, the heat plus the humidity and big swings, I think what I proposed is more actual than just a straight 150. The 30 percent in the summer months is still not going to get your production up to where it is in the winter months, so you're still going to have to have a reserve that you're going to have to deal with. And it's important to have a reserve if you're selling fluid milk because some days people may diet [sic, buy it] and they [sic, the] next day they may not, so you -- you're not going to just sell all your milk as fluid if you're a producer-handler.

Sumners, 997-98. Even the proponents recognize that the presence of producer-handlers in the marketing area would contribute to efficient and orderly marketing:

Q. Okay. And if, in fact, we have producer-handlers in that area that were, in fact, producing their own milk, processing their own milk and selling their own milk, that would also tend to assist this marketing area to continue to be self-reliant, right?

A. Yes.

Hollon, 709. Given the climactic and economic conditions in the Southeast, the adoption of Proposal eight is critical.³

VIII. Conclusion

At the insistence of some of the largest publicly traded corporations and cooperatives in the United States, the Department has held a hearing on the proposed change of over seventy years of Department policy regarding producer-handlers. The industry spent three weeks in hearings looking over a mountain of exhibits, and heard from dozens of witnesses in Arizona, Washington, and Virginia. Now we have done it all over again, albeit in a somewhat abbreviated format, in Georgia. The only conclusion to be drawn is that the proponents have failed to establish any evidence, let alone the substantial proof required to justify a change to the Department's long-standing policy regarding producer-handlers. Once again, the proponents have spent more money and have parroted the same inaccurate buzzwords. The bottom line is that the Department has been provided with no justification to warrant the adoption of Proposals five and seven.

Moreover, there is no evidence that either the supply or price of milk in the two orders at

³ At a minimum, even if the Department elects not to adopt this particular proposal, it should adopt a 150,000 pound purchase allowance to conform to the provisions of virtually all other marketing orders.

issue in this hearing is fluctuating unreasonably at all; let alone as a result of producer-handler activity. Alas, there is no producer-handler activity to speak of. With or without producer-handlers, the quantity of milk previously or currently available to the consuming public is more than adequate and there are no inefficient movements of milk in the markets attributable to producer-handler activity.

For a change, the Department has a chance to improve the lot of producer-handlers in the region and foster healthy competition by adopting Proposal eight. Orders Five, Six, and Seven remain the only marketing areas in the country without a purchase allowance. This inflexibility accounts for the stark absence of significant producer-handler activity in the region and needs to be remedied.

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CERTIFICATE OF SERVICE

The foregoing was Statement was served upon the following parties on August 16, 2004, by electronic mail, FedEx Overnight Service, and /or first-class United States Mail service as indicated.

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