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**BEFORE THE SECRETARY OF AGRICULTURE
AGRICULTURAL MARKETING SERVICE**

USDA
OFFICE OF THE SECRETARY

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Milk in the Mideast Marketing Area;)
October 23-24, 2001 Hearing on)
Proposals to Amend Certain Pooling)
and Related Provisions)
_____)

RECEIVED
Docket No. AO-166-A68; DA-01-04

**BRIEF AND PROPOSED FINDINGS OF FACT AND CONCLUSIONS OF LAW
FILED ON BEHALF OF SUIZA FOODS CORPORATION**

INTRODUCTION

Suiza Foods Corporation files this Brief and Proposed Findings of Fact and Conclusions of Law with respect to the "pooling" provisions of the Mideast federal milk marketing Order Number 33 (7 C.F.R. Part 1033). Pooling provisions of federal milk orders, because they determine which producers share in the monies paid for milk, are generally viewed as most directly affecting the rights of dairy producers. However, the handlers who pay for the raw milk, in particular Class I handlers who pay the highest prices for raw milk, are also affected by pooling decisions made by the Secretary of the United States Department of Agriculture (the "Secretary"). The Secretary's charge is to establish and maintain orderly marketing conditions. 7 U.S.C. § 602(1). In order to meet this statutory obligation, the basic tenets of the federal milk order system are: (a) the setting of an adequate price intended to bring forth a sufficient supply of fluid milk and (b) uniformity of treatment of handlers and producers.

At issue in this hearing are the rules that determine which producers and under what circumstances producers may share in all the minimum price proceeds paid by handlers pursuant to the Mideast Order. These pooling provisions were adopted most recently through the process known as Federal Order Reform, an informal rulemaking process required by Congress and resulting in a significant reduction, primarily through merger, of the number of federal milk

orders. Through this consolidation process, it appears that USDA often adopted the most liberal provision for pooling selected from any one of a number of orders merged together regardless of whether the provision was actually necessary or used at the time (e.g. 1999). This process of "one from each column" does not necessarily result in orderly marketing conditions as noted by numerous witnesses at the Mideast Order hearing.

Suiza Foods Corporation operates a number of fluid milk plants on the Mideast Order, purchasing raw milk from both cooperative and independent milk sources. With certain modifications discussed at the hearing and in this Brief, Suiza supports the efforts of its dairy farmer suppliers to insure that the money it pays for milk are shared among those producers who can, do and are able to serve the Mideast Order's fluid milk market needs. Suiza takes no position on the one non-pooling provision proposal regarding the so-called advance payment (Hearing Notice, Exhibit 1, Proposal 4).

FINDINGS OF FACT AND CONCLUSIONS OF LAW

Suiza proposes the following findings of fact and conclusions of law and requests that the Secretary make a ruling on each proposed finding under the provisions of the Administrative Procedure Act, 5 U.S.C. § 557(c):

A. Suiza Foods Corporation

1. At the time of the hearing, Suiza operated 10 predominantly Class I pool distributing plants throughout Order 33. Suiza purchases and receives milk from a number of sources at these facilities including independent dairy farmers and cooperatives. Tr. 401-402.

2. Suiza's ability to obtain raw milk for Class I bottling and its resulting raw milk procurement costs are tied directly to pooling provisions of the federal milk orders. When money paid for milk is spread more widely to producers not regularly serving the Class I market,

producers shipping to the Class I market necessarily look to Class I processors to make up the difference outside the federal order minimums. Tr. 404.

3. Therefore, Class I processors have a pecuniary interest in the outcome of this hearing. Simply put, it is their money paid for their raw milk receipts that create the economic incentives over which dairy farmers are in dispute. Other fluid processors represented by the Pennsylvania Milk Dealers Association joined Suiza in raising these concerns. Tr. 329-332.

B. Pooling Provisions

4. All witnesses supported in one form or another tightening the pooling provisions of Order 33. Disagreement by hearing participants, such as it was, centered on which provisions to tighten or how tight to make them, but no witness testified in outright opposition to the proposals. Where all handlers and producers supported most of the amendments, the Secretary should certainly adopt them subject to modification herein.

5. Exhibit 5 and Tr. 143, 159, 215-216 and 226-227 indicate that there is much more than a sufficient supply of milk available for fluid needs in this market. The decisions of the Secretary and the case law that have resulted from 60 years of regulation establish that the "sufficient supply of milk" standard is a fluid milk measurement.¹ Nonetheless with a sufficient supply of milk, the fluid needs of the market may not always be served by an order system that encourages an excess reserve supply of milk to be associated with the market. Pooling provisions that are too loose are thus as likely to disrupt the market as provisions that are too tight. The parties agreed unanimously that the present circumstances are disruptive because the provisions are too loose.

¹ See generally Borden v. Butz, 544 F. 2d 312, 316 (7th Cir. 1976) (the primary purpose of a minimum fixed price system "is to bring forth an adequate supply of pure and wholesome milk" [for Borden's bottling operations of fluid milk]). See also Schepps Dairy v. Bergland, 628 F.2d 11, 17 (D.C. Cir. 1979).

6. Federal Order Reform and the resulting order provisions were principal issues at the hearing. That Reform process provided for pooling of milk based upon the theory that all existing suppliers should remain pool sources: "To assure continued pool qualifications for all handlers who are currently associated with the Mideast markets, the pool supply plant definition of the consolidated Mideast order provides for all types of supply plants that currently qualify for pooling under the four principal orders." 64 Fed. Reg. 16026 et seq. at 16158 (April 2, 1999).

7. Unfortunately, the result of this seemingly innocuous comment was that very large regional orders with multiple pooling options resulted in significant non-historically associated milk supplies suddenly becoming available to be associated with new milk orders. Ex. 5, Appendix B. Suiza does not take issue with the decisions made by various entities "using" these pooling provisions. Rather it is the obligation of the Secretary to establish and maintain orderly marketing conditions. Having uncovered the issues and facts that give rise to them, the Secretary is obligated statutorily to fix the problem.

8. Twenty-one months of operating under Federal Order reform has revealed that at least as to the Mideast Order, this policy has resulted in significant erosion of producer returns to those producers actually serving the fluid market on a regular basis. Class I processors pay the same regulated minimum prices regardless. The difference is that less of that regulated minimum price is returned to the producers shipping to the Class I market as more of the money is spread more widely to producers not regularly serving the Class I market. Tr. 404.

C. Orderly Marketing Conditions

9. Individual dairy farmers who testified at the hearing all supported tightening pooling provisions, although again, they may have asked for varying degrees of tightening. Tr. 71, 86, 105 and 391. These producers all serve the fluid market and yet their funds have been subject to significant erosion as shown in Ex. 5, Appendix C. The federal pricing structure

already creates too little incentive for producers to deliver milk to fluid distributing plants.

Absent the Secretary's immediate and emergency action with respect to the proposals submitted, what little incentive there is to deliver milk to fluid plants will largely evaporate.

10. The unanticipated negative impact on blend prices as a result of excess pooling of milk not delivered to the market (sometimes called "paper pooling") is best illustrated by comparing the Secretary's predicted results from Federal Order reform with the actual results in 2000 and 2001. Ninety-five percent of Order 33 pooled milk came from the four states of Indiana, Michigan, Ohio and Pennsylvania in 1997. 64 Fed. Reg. at 16066, c.2. Moreover, Class I and Class II utilizations were expected to be 58.7% and almost 20% for a combined total of 78.7% of the market. 64 Fed. Reg. 1t 16067, c. 1-2.

11. In December 2000, however, while the milk supplied by the four states remained relatively constant at 1,003,980,506, the total milk pooled on Order 33 had grown from an expected 1,025 million pounds to almost 1,381 million pounds. Only 72.7% of the milk pooled on Order 33 January - September 2001 was produced in the four states of Indiana, Michigan, Ohio and Pennsylvania down from the expected 95%.

12. The addition of 350+ million pounds to the pool all from sources almost entirely located outside the marketing area suggests the need to examine the underlying assumptions made by the Secretary in Federal Order reform. There was no evidence provided by any witness that this additional supply of milk constitutes a reasonable and necessary reserve for the fluid market or that the Secretary intended this milk from outside the marketing area to be pooled on this order without actually serving the fluid market. The Secretary should find that these facts, resulting in depressed blend prices, constitute a sufficient changed circumstance to enable her to make the necessary amendments. In fact, these reduced blend prices directly impact fluid milk handlers ability to attract milk to their plants. This undermines the Secretary's determination that

the price she has set for milk is sufficient to bring forth an adequate supply of fluid milk for the fluid market.

13. The failure to insure that milk is delivered to these fluid distributing plants, notwithstanding the fact that they pay the highest regulated price and the fact that an adequate supply of milk is obviously associated with this market, is a disorderly marketing condition in and of itself.² The Secretary is charged with establishing and maintaining orderly marketing conditions. 7 U.S.C. § 602(1). Therefore, the Secretary is obligated to take action as requested at the hearing in order both to establish and maintain orderly marketing conditions - that is the proper sharing of milk proceeds among those producers actually ready, willing and able to serve the fluid market in the Mideast Order.

D. Proposals

14. Suiza supports proposals 1 through 3 and 5 as modified by Suiza at the hearing. Specifically:

(a) The so-called free ride months during which no performance to the fluid market is required should be eliminated. Performance as measured by deliveries of milk to fluid milk plants can and should be measured monthly. "As a practical matter, once performance becomes a monthly requirement, both processors and producers will be better able to plan deliveries based upon the need for milk in the fall months when milk is short." Tr. 405.

(b) The month of August should be treated as a "short month" for purposes of both shipping percentages and diversion limits. "With the summer stress negatively impacting supply and the opening of schools increasing demand for fluid milk, it is wholly rational to include August among the fall months when milk is short." Id. and Tr. 228.

² See e.g. Kyes v. United States, 369 F.2d 714, 716-717 (Ct. Cl. 1966), cert. denied, 387 U.S. 929 (1967) (fundamental objective of AMAA is to effect an orderly exchange of commodities in interstate commerce to protect both the interest of the consumer and the purchasing power of the farmer.)

(c) The Market Administrator's office acknowledged that no plants qualified under the so-called split plant definition (7 C.F.R. § 1033.7(h)(7)) immediately after federal order reform. Tr. 54. Indeed regulatory use of the provision ceased prior to Federal Order reform when manufacturing grade milk was relocated to an exclusive manufactured milk facility in Indiana. The hearing record reveals that old Order 49 manufacturing milk is now received exclusively at one of two manufacturing plants, both of which are non-pool facilities with no split plant use. Tr. 405-406. This is important because again the Secretary intended as part of Federal Order reform to permit **continued** pooling of supply plants pooled at the time of consolidation and implementation. See paragraph 5, supra. However, the Secretary never said in the course of Federal Order reform that the intent was to create new mechanisms to pool. The fact that no entity was using the split plant definition (a provision that only existed in the old Order 49 prior to reform and was not used by any plant under that order in 1998) means that the provision was unnecessary for the purpose proposed by the Secretary (continued qualification for pooling of existing facilities). There is no other discussion in federal order reform regarding the necessity of maintaining this outdated provision. 64 Fed. Reg. at 16026 to 16158. The provision should be eliminated as unnecessary and unjustified.

(d) Dairy farmers should be required to make actual deliveries of milk to pool plants. Meaningful touch base provisions provide handlers with assurance of performance to the market while simultaneously protecting dairy farmers. Again the hearing participants generally agreed on touch base requirements. The question boils down to a two versus three day touch base requirement. "Without a meaningful touch base requirement, individual producer suppliers do not actually have to perform. Suiza favors such individual performance. The argument that three days shipping in effect equals four-day shipping (as a result of average producer size) is specious. In such event, the same parties should be heard to say that a one-day shipping

requirement effectively equals two days. This argument should be rejected. A three-day requirement will better ensure proper association with this market by ensuring that dairy farmers actually deliver milk to pool plants for a minimum time period.

E. Technical Issues and Conforming Changes

15. Suiza raised several technical or conforming change issues at the hearing:

(a) In order to assure that August is a performance month for all purposes, 7 C.F.R. § 1033.7(f)(3) should also be amended to read "March through July" and "August through February." Tr. 407, 228 and 275.

(b) If a net shipments provision is added to the supply plant definition, 7 C.F.R. § 1033.7(c), then in fairness and equity, the same provision should be added to 1033.7(d), the cooperative supply plant definition. Tr. 407 and 182-184. Failure to add the provision in 7(d) if added to 7(c) will merely change the incentives for cooperatives operating supply plants to become regulated under 7(d) as opposed to 7(c). The Secretary should not create that unnecessary and uneconomic incentive. No party testified otherwise, and the major proponents accepted that concept at the hearing. Tr. 182 - 184 and 274.

(c) The last sentence of 1033.7(c)(4) should survive proponents' amendment striking all of the language in that subparagraph. This is because that provision has a history that can be separated from the remainder of the section. The last sentence requires that cooperative supply plants, unit pool plants and plants qualified as a result of a supply contract with a cooperative to remain associated with the market or requalify under paragraph (c) for six months before being granted the more generous opportunities under (d), (e) or (f).

Indeed the existence of 1033(f)(3) establishes that the Secretary intends there to be a requalification period. In fact that is precisely what the Secretary stated when originally adopting the provision in the old Southern Michigan order in 1968. Official Notice requested of

Proposed Rule Making for Order 40, 33 Fed. Reg. 14465-14468 (Sept. 26, 1968). At 33 Fed. Reg. 14466 the Secretary discussed at some length creating new pooling provisions akin to 1033.7(e) and 7(f) and the fact that such plants "automatically qualified" could:

withdraw from the market if the operator so chooses. Such plant could regain pool plant status at any time by meeting the minimum monthly shipping requirements. However, to regain status under unit pooling, or as the combined shipments of direct-ship and plant supplies under § 1040.15(b)(2) or (3), the minimum shipment requirement should be met at least 6 consecutive months. This will help insure regularity of association of the plant with the market as a basis for sharing in the pool proceeds.

Acknowledging that the automatic status would no longer apply under proponents' proposals, nonetheless, the fact remains that at least as to 7(e) and 7(f) plants, the special pooling privilege available should result in "regular association". Indeed saving this language presently found in the last sentence of 7(c)(4) would go a long way toward addressing the concerns of the Pennsylvania Milk Dealers with respect to pooling decisions (see proposal number 8 and Tr. 331-334). The privilege of qualifying beyond paragraph 7(c) or 7(d) ought to have some consequences should the plant operator choose not to pool for any month. Requiring it to requalify under 7(c) for six months before permitting it to reuse 7(e) and 7(f) is a minimum requirement that is consistent with the history of the Southern Michigan order when the predecessor language of 7(e) and 7(f) was adopted back in 1968. As to 7(d), Suiza cannot find the historical basis for requiring such plants to requalify as 7(c) plants for six months. Therefore, it would appear to make sense to retain the last sentence of 7(c)(4) but without the reference to 7(d). Suiza raised this issue in its testimony and expressly reserved the opportunity to comment and take official notice of the 1968 Proposed Rule at the hearing. Tr. 402 and 523.

F. Emergency Conditions

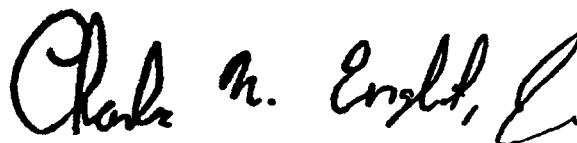
16. The statistics submitted in Exhibit 5 together with the testimony of affected dairy farmers, their representatives and the handlers unanimously establish the emergency conditions

requiring immediate action by the Secretary. Notwithstanding the more than sufficient supply of milk for fluid needs, dairy farmers are justifiably concerned about the significant and ongoing erosion in their income. Faced with the reality of falling prices nationally for manufactured products, federal order prices will be falling in the immediate future. Only prompt and emergency action from the Secretary can avoid further loss to these farmers resulting in new and greater disorderly marketing conditions. The Secretary is urged to omit a Recommended Decision and to act immediately to "establish and maintain" orderly marketing conditions in the Mideast order.

CONCLUSION

For the foregoing reasons, Suiza urges adoption of the proposals 1 through 3 and 5 as modified. Emergency action is necessary in order for the Secretary to operate the Mideast Order according to her statutory requirements.

Respectfully submitted,



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