

**STATEMENT**

**PROPOSAL NO. 2**

**NORTHEAST FEDERAL MILK ORDER HEARING**

**DOCKET NOS. AO-14-A70; DA-02-01**

**HELD SEPTEMBER 10, 2002**

**IN ALEXANDRIA, VIRGINIA**

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**ON BEHALF OF**

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## **PROPOSAL NO. 2.**

We propose two amendments to the pool plant definition in Section 1001.7. These are as follows:

### **Section 1001.7 Pool plant.**

1. Amend Section 1001.7 C (1) and (2) to increase the applicable shipping percentages by 5 percent over the entire qualifying period August through December, each year. The revised rate in subparagraph (1) for August and December, would be 15 percent and the performance standard contained in subparagraph (2) for each of the months September through November, would be 25 percent of receipts.
2. Remove paragraph (h)(7), which authorizes "split plants" (pool and non-pool segments) in the same plant facility.

### **JUSTIFICATION:**

Since the inception of the Reform Order, a major milk drain has been taking place in the Northeast in the fall months, making it increasingly difficult for fluid milk handlers to procure enough milk to satisfy demand. This drain occurs largely because spot milk is moved from the Northeast to other areas by transfer, diversion, or shift of producers at seasonally high prices, without having to maintain appropriate association with the Northeast Order for pooling purposes.

While milk has not been as "tight" this year compared with 2000 and 2001, we think the situation will change markedly during September through November, 2002. We also are aware that some of the "extra" milk in the market this spring and early summer, stems from earlier "switching" or "dumping" milk back into the Northeast from southeastern Order areas where it had been used as "reserve" milk.

Therefore, proponents think long-term action is needed to alleviate the milk shortages regularly occurring in the fall for Order 1 fluid milk handlers as well as corrective measures to lessen the extent to which Federal Order 1 carries the reserve milk for other

market areas. We think this can best be accomplished by raising the pool performance standards in the fall, when the milk is needed most. An increase in the shipping standards is made necessary, because we find that an increasingly greater share of the milk in the Northeast is being “leveraged”, via revised cooperative 9 C provisions, to favor the needs of some handlers over others, creating inequities and disorderly marketing in the process. Our proposed 5-percent increase in the shipping requirement under Proposal No. 2, will do much to correct the fall milk shortage problem, provided other safeguards , such as an effective “call” provision, is also maintained in the Order.

While we recognize the common desire among handlers to market their milk to best advantage, we also consider it the prime responsibility of Order provisions to assure that an adequate supply remains to fulfill the class 1 needs of marketing area consumers. It is inappropriate, therefor, for the Order to allow the complete withdrawal of producer milk during July through November each year, followed by a “re-pooling” of the same milk in Order 1 in the “flush” production season. This unduly burdens both handlers and producers who then wind up having to carry the “surplus” reserves otherwise associated with another market.

The proposed 5-percent increase in qualification requirement during August through December, is modest and not without precedent. The resulting shipping standards are similar to those previously in effect in the former New England and Middle Atlantic Orders, prior to the merger in 2000 and they match those established August through November, 2000 and 2001, under the “call” orders promulgated by the market administrator.

To fully appreciate the current pool qualification issues in the Northeast, one must understand the significant structural changes that have taken place in the market since adoption of the Reform

Order. Perhaps the most important change affecting pool qualification, is the new cooperative 9 C provisions adopted under Reform. Another involves the “loose” pooling requirements, particularly with respect to allowable diversions and the degree to which producer milk must “touch base” with pool plants in the primary market.

The new 9 C provision (Section 1001.9, paragraph C) has placed the larger Northeast cooperatives in a strong position to direct a larger share of market milk to best advantage wherever it may be most needed. The issues are—to which markets?—and for whom?—and for how much?

Prior to Order Reform, the New England Order had a similar “9 (d)” cooperative pooling provision, but it was restricted to members only. This difference is important, because the current 9 C standards permit other cooperatives (normally smaller) and “independent” producers, to join the 9 C unit of a larger cooperative willing to take the responsibility to “pool” the milk and direct its marketing. Subsequent merger activity among milk dealers coinciding with other changes in corporate market structure within the region, has resulted in the shifting of large blocs of independent producers, primarily associated with pool distributing (PD) plants, into these larger Co-op 9 C units. This gave the cooperative 9 C units involved a “leading edge” in pool qualification ability, due to the high degree of shipments to class 1 PD plants made possible by the added “independents”. The 9 C cooperative pooling “advantage” for some, has reached the point that an increase of 10 to 15 percent in shipping requirement, should not pose a qualifying problem for the parties. That is, unless they misuse it to pool too much manufacturing milk or sell too much milk to other markets, most notably to the southeast.

This 9 C unit pooling advantage is now being used extensively to “leverage” the inclusion of other “independent” producers and “smaller” cooperatives, associated primarily with

manufacturing operations, into their expanded 9 C unit—for the privilege of guaranteed pooling – at a service fee. The degree to which the cooperative decides to take on the pooling responsibility for additional manufacturing milk, directly affects their ability to respond to our proposed higher shipping standards. And what has happened as a result of extending the “pooling guarantee? The answer is fewer and fewer sources of reserve milk supply for fluid milk handlers, and that is our main concern for the future.

According to the Handler Location Index released by the market administrator in April 2001, only 9 of the 150 northeastern plants listed (as partially or fully regulated or exempt under Order No 1), were classified as “pool supply (PS) plants. Prior to Order Reform, there used to be more. Of the 9 PS plants remaining, only 3 are proprietary—(Fleur-de-Lait in New Holland, PA, Queensboro Farms in Canastota, NY, and Emkay Trading in Arcade, NY). The rest were cooperatively owned. While one might suggest the reduction in number of PS plants was simply the result of plant closings, such conclusion does not hold up. Why? Because several of the former reserve PS plants simply converted to non-pool status. And the change in status was made easier with “guaranteed pooling” and unlimited diversion privileges, under Order Reform.

The extent to which cooperative “9 C” milk has been gaining market share, is clearly demonstrated in TABLE 2, attached to this statement. This Table gives a breakdown of total market milk produced by cooperatives and independent producers. It also shows the “market share” represented in the expanded “9 C” units. From the data in TABLE 2, we find that average milk production covered in 9 C units, is now greater than total co-op milk receipts by more than 100 million lbs. a month. We also call attention to the fact that “9 C” milk now represents more than 80 percent of all milk produced for the Northeast Order. Consequently, it is imperative that all cooperatives understand that the market tools provided them under current 9 C provisions,

carries with it awesome responsibility to see to it that consumer fluid milk needs in Order 1 are given top priority at all times.

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The second amendment to the pool plant definition proposed by our group, officially noticed in Proposal No. 2, called for the removal of paragraph (h)(7) set forth in Section 1001.7 of the Order. We note too that identical amendment is proposed by the Association of Dairy Cooperative in the Northeast (ACDNE).

The provision, designed to enable special “split-plant” status ( both pool and non-pool within the same facility) is proposed to be removed.

**JUSTIFICATION:**

The new Reform Order has been too liberal in its pooling standards. Since its inception in January 2000, the reform provisions have encouraged abusive “pool riding” practices. This provision is one of them. It no longer serves the purpose for which it was originally intended and could be used to the detriment of orderly marketing procedure.

Original purpose of the “split-plant” designation, was to set-aside a portion of receiving facilities as “non-pool” to receive and handle Grade B milk, separate from Grade A milk received at the “pool” section of the handler’s facility. We understand the provision is not normally approved by the market administrator, except for this purpose. For example, we understand it might be used to separate non-pool Grade B Amish produced milk from other Grade A milk in the plant.

The problem with it; however, is that, once approved, it provides a means whereby the handler may establish a pooling pattern very detrimental to the public interest and orderly marketing. The underlying problem is that this provision may be used to “ride” the pool, especially if the Order enables unrestricted diversions, as the Northeast Order presently does. Milk from distant “split

plants” can be readily pooled and qualified under Order 1, with minimal shipments during the qualifying period. After full qualification is achieved, the handler may then add substantially to receipts at the “pooled” portion of the plant (beginning January 1 and continuing through July 31), while, at the same time, continuously diverting milk to non-pool plant(s). Most importantly, it could provide the means to draw the higher PPD from the Order 1 pool, without ever making a meaningful contribution to the market.

Since it is our understanding the provision is not currently being used by handlers located within the Order 1 marketing area, we concur with the ADCNE cooperatives, that it be removed from the Northeast Order as soon as it is practicable to do so.

This concludes our statement on Proposal No. 2.