



Exhibit 20

I am Jeffrey Sims; I am Assistant Secretary of Dairy Cooperative Marketing Association, Inc., hereafter referred to as DCMA, a marketing agency in common operating in the southeastern United States. My business address is 13400 U.S. Highway 42, Suite 162, Prospect, Kentucky 40059. I testify today on behalf of DCMA, whose nine Capper Volstead cooperative members are: Arkansas Dairy Cooperative Association, headquartered in Damascus, Arkansas; Cooperative Milk Producers Association, Inc., headquartered in Blackstone, Virginia; Dairy Farmers of America, Inc. headquartered in Kansas City, Missouri; Dairymen's Marketing Cooperative, Inc. headquartered in Mt. Grove, Missouri; Lone Star Milk Producers, Inc. headquartered in Windthorst, Texas; Maryland & Virginia Milk Producers Cooperative Association, Inc.; headquartered in Reston, Virginia; Select Milk Producers, Inc., headquartered in Artesia, New Mexico; Southeast Milk, Inc., headquartered in Belleview, Florida and Zia Milk Producers, Inc., headquartered in Roswell, New Mexico. Each of the members of DCMA marketed milk on one or more of the Appalachian, Florida and Southeast Federal Milk Marketing Orders during the year 2006.

Together during December 2006, DCMA member cooperatives marketed as member milk more than 69% of the producer milk pooled on the Appalachian Order, and when including milk marketed of other producers, more than 87% of the producer milk pooled on the Order. For the Florida Order, during December 2006, DCMA member cooperatives marketed as member milk more than 95% of the producer milk pooled on the Order, and when including milk marketed of other producers, more than 96% of the producer milk pooled on the Order. For the Southeast Order, during the same month, DCMA member cooperatives marketed as

member milk more than 69% of the producer milk pooled on the Order, and when milk marketed of other producers is included, more than 87% of the producer milk pooled on the Order.

DCMA is here today offering a comprehensive set of proposed amendments to the Appalachian, Florida and the Southeast Federal Milk Marketing Orders, listed as Proposals Number 1, 2 and 3 in the Notice of this hearing. DCMA wishes to thank the Secretary for hearing these proposals on an expedited schedule and for considering emergency action and the omission of a recommended decision under the rules of practice and procedure.

DCMA offers the following testimony in support of Proposals number 1, 2 and 3. For purposes of simplicity I will refer to the three-Order area as the southeast region. I will attempt to be explicit if and when referring to the specific individual Southeast Order, No. 1007.

Introduction

For at least the last quarter century, the southeastern United States has experienced declining milk production, and at the same time has seen substantial increases in population. These two factors have combined to create a milk deficit condition in the southeast unlike any other region of the United States.

Increases in Class I sales, brought on by increases in population, coupled with the decreases in milk production have left the southeast in the unenviable position of seeking milk supplies

from further and further away. According to Market Administrator statistics introduced at this hearing, during 2006 producer milk was delivered to Order 5, 6 and 7 pool plants from not less than 27 states. Just as the milkshed for the region has expanded and milk movement distances have increased for milk moved from outside the marketing area, the distance milk moves within the marketing areas has likewise increased. Exacerbating the enormity of the distances milk must move to supply the Class I demand in the southeast is a national environment of high fuel costs.

The DCMA proposal offered today is an integrated one, in that all of the elements are linked as a single package. DCMA believes the varied needs and interests of the marketers of milk - the producers, the numerous producer organizations, the processors of milk, and the southeast region's consumers can best be addressed by considering these proposed amendments together. Substantial modification or elimination of any element of the plan will reduce the plan's effectiveness, and will render the plan with insufficient support to allow DCMA to continue to pursue the plan. DCMA believes that the comprehensive approach provides benefits for all the region's dairy stakeholders.

DCMA proposes a comprehensive three-pronged package of amendments aimed at increasing the capability for the southeast region's Federal Milk Marketing Orders to attract a sufficient quantity of milk for the region. The three basic elements of the proposal are: (1) increase minimum Order Class I prices in all three of the Appalachian, Florida and Southeast Federal Milk Marketing Orders; (2) tighten percentage diversion limits in the Appalachian and Southeast Orders, while making the producer marketing area association provisions more

efficient; and (3) improve the Transportation Credit Balancing Fund provisions in the Appalachian and Southeast Orders.

I will address the three prongs of the proposal in the order just listed.

Prong One: Minimum Order Class I Prices

The history of minimum Order Class I prices over the last 25 years in the southeast region can be reported in a very brief summary. As a result of the 1985 Farm Bill, Class I differentials in much of the Federal Order program were increased. In the southeast, the Class I differential in the benchmark city of Atlanta increased from \$2.30 per hundredweight to \$3.08 per hundredweight. The \$3.08 Class I differential in Atlanta remained unchanged until the Order Reform process in the year 2000, when it was raised to \$3.10 per hundredweight, an increase of \$0.02 per hundredweight. Atlanta's Class I differential remains \$3.10 per hundredweight today.

Meanwhile, under Order Reform, the Class I differentials in the reserve supply areas outside the southeast increased at amounts sometimes greater than Class I differential increases within the southeast regions' Orders. For example, the Class I differential in Marathon County, Wisconsin, a historically heavy milk production and reserve supply area, increased from \$1.04 per hundredweight to \$1.70 per hundredweight. While the Order Reform adjustments to Class I differentials in the areas outside of the southeast were warranted, the net effect was that the spread in Class I differentials between the historic reserve supply areas

and the southeast narrowed, lessening economic incentives to move milk into the region. In other words, the Class I differential surface in some cases was flattened under Order Reform versus the surface that existed prior to Reform. Likewise, changes in Order marketing areas and pooling provisions flattened producer blend price relationships with somewhat lowered Class I utilizations in the southeast. Combined, the flatter Class I price surface and flatter blend price surfaces have reduced economic incentives to move milk into the southeast from the reserve supply areas.

Over the 1986 to 2007 period, diesel fuel prices and milk hauling costs in general have increased considerably more rapidly than have Class I differentials in the southeast. According to the U.S. Department of Energy, Energy Information Administration, hereafter referred to as the EIA, the U.S. average diesel price was \$0.94 per gallon in 1986, and averaged \$2.70 per gallon in 2006, an increase of 187 percent. Other costs of hauling such as equipment, wages, and insurance have all risen along with fuel. As we stated, for the benchmark city of Atlanta, since 1986, the Class I differential has been gone up \$0.02 per hundredweight, an increase of 0.65 percent.

Over this same time period, milk production within the southeast has continued its seemingly relentless decline, necessitating increased needs for importation of milk supplies from the reserve regions into the southeast. Greater needs for milk to move, with lessened regulated price differences upon which to move the milk has left the southeast in dire straits in obtaining needed milk supplies.

The southeast is a region which has experienced sizeable population growth over the last few years. Exhibit 21, page A provides in table form the U.S. Census Bureau population estimates for the years 2000 to 2006 for the southeastern states wholly within Orders 5, 6 and 7 of Alabama, Arkansas, Florida, Georgia, Mississippi, Louisiana, North Carolina, South Carolina, and Tennessee. The nine-state region has seen an 8.4 percent growth in population in just 6 years, compared to 6.2 percent growth for the U.S. as a whole. The southeast's population growth rate over the last six years was 135 percent of the U.S. growth rate, with no likelihood of the southeast slowing down in the near future. With more people comes more demand for milk and dairy products, and the southeast already does not have enough milk. The population growth in the nine-state southeast region from 2000 to 2006 totaled more than 4.7 million people.

Exhibit 21, pages B1 through B4 provide a snapshot of the supply-demand condition present in the Order 5, 6 and 7 areas. Pages B1 through B3 compares the producer milk produced within the Appalachian and Southeast marketing areas to the Class I milk pooled on the two Orders. Page B4 compares the milk produced within the state of Florida as reported by NASS to the Class I milk pooled on the Florida Order. Data on milk production within the Order 5 and 7 marketing areas is taken from Market Administrator Exhibit 9, page 1 and Exhibit 18, page 11. In each case, an additional calculation is made showing the supply-demand relationship with modest presumed rates of necessary reserves and Class II use. Whether just comparing the available milk production in the area to the areas' Class I use, or the areas' Class I, Class II and a reserve, the supply-demand picture is gruesome. In the Order 5 and 7 area, local in-area milk production in 2006 was only able to supply the milk used in Class I in 4 months of the year, while in Florida, in-state milk production was

insufficient to supply the Class I needs every month of 2006. When the use of milk in Class II and a modest reserve is added to the Class I use, the deficit condition in the Order 5 and 7 areas becomes year around, and the Florida deficit worsens.

Based in this analysis, the Order 5 and 7 areas can supply only about 76 percent of the milk necessary to meet Class I, Class II and reserve demands, and in the Florida area, in-state producers supply only about 66 percent of the milk necessary to meet Class I and reserve demands, on an annual basis. Annual comparisons presume milk produced in the spring would be available to meet the greater demands in the short season, which of course is not the case. In the worst month of 2006, August, the Order 5 and 7 areas supplied less than 64 percent of the milk necessary to meet Class I, Class II and reserve demands. In Florida, during its worst month of 2006, October, in-state producers provided less than 61 percent of the necessary supplies. It is then not a joke when marketers of milk state that at least one out of every three loads of milk delivered to plants in the southeast is supplemental milk. Clearly, no other region of the country has a milk supply and demand situation which even approaches the critical milk-deficit condition existing in the southeast.

The current Class I differential structure in the southeast provides insufficient Class I price differences to move milk within the region, as well as inadequate price incentives to attract supplemental milk from outside the region. Exhibit 21, pages C1 through C4 graphically represents the per-hundredweight per ten mile relationship of Class I prices as they exist in the southeast today. As can be seen from the Exhibit map diagrams, the relationship of Class I prices in the southeast is, at least using Louisville, Kentucky and Springfield, Missouri as basing points, about \$0.018 to \$0.019 per hundredweight per ten miles, while the true cost of

hauling bulk milk is more than \$0.048 per hundredweight per ten miles. Since installed in the Appalachian and Southeast Orders in December 2006, the Market Administrator mileage rate factor for use in the Transportation Credit provisions, a mileage rate which was set intentionally low, has averaged about \$0.0044 per hundredweight per mile, which is 4.4 cents per hundredweight per ten miles. When using Mt. Crawford, Virginia as the basing point, the Class I price relationships become even grimmer. In the case of Mt. Crawford, the price surface reflects a relationship of barely more than one-tenth cent per hundredweight per mile, well less than one fourth of the cost of moving milk. Using Atlanta as a basing point for the Florida area, the price surface reflects a relationship of about \$0.019 to \$0.020 per hundredweight per ten miles, slightly higher than the two Orders to the north, but still seriously inadequate to move the milk.

The long-stated purpose for the Class I price structure, which generally provides increasing Class I prices moving toward milk-deficit regions and away from reserve supply regions, is well established. The Secretary has repeatedly affirmed, and the majority of the industry concurs on the need for a structured price surface, which provides orderly incentives to move milk from reserve supply areas to where the milk is needed to supply fluid milk product demand. The Class I price surface, coupled with a traditional blend price surface, creates economic incentives for milk to be attracted out of manufacturing uses in the reserve supply areas into use in fluid milk products in the milk-deficit regions. The system functions as designed unless the price differences between reserve areas and deficit areas are insufficient to encourage the milk to move. Such has become the case with regard to the southeast's relationship in price, both within the region, and in terms of the southeast's price relationship versus the reserve milk supply areas.

The issue faced by the southeast is that Class I price differences, coupled with Class I utilization differences in the southeast versus the more well supplied regions of the U.S., are simply not enough to shake milk away from manufacturing uses in the reserve supply areas without substantial priming of the money pump with over order values. While the southeast has not gone short of milk for any extended periods of time, at least it has not yet, the orderly marketing of milk, and economically justified movements of milk will be enhanced when the regulated values of milk are more reflective of the real costs of moving milk from reserve supply areas to the milk-deficit southeast.

Left at their current levels, the Class I prices in the southeast will fall further and further away from the values necessary to move the milk, eroding and threatening orderly marketing, and jeopardizing the supply of milk to the region. The Secretary should act now to return the Class I price structure in the region to a level which is more reflective of the true location values of milk, thereby sending the economic signals necessary to bring forth a sufficient quantity of milk.

In order to partially address the issue of insufficient price incentives required to move milk to the southeast, DCMA proposes increasing minimum Order Class I prices in the Appalachian, Florida and Southeast Order marketing areas. The proposed changes to the Class I prices for plant locations in the Appalachian Order Marketing Area range from an increase of \$0.10 per hundredweight to an increase in \$1.00 per hundredweight. Proposed changes to the Class I prices for plant locations in the Florida Order Marketing Area range from an increase of \$1.30 per hundredweight to an increase of \$1.70 per hundredweight, and the proposed changes to

the Class I prices for plant locations in the Southeast Order marketing area range from an increase of \$0.10 per hundredweight to an increase of \$1.15 per hundredweight. Just as would be expected in a conventional Class I price surface, the greater increases in proposed Class I prices occur at plant locations most distant from the reserve milk supply areas.

DCMA recognizes that a national review of the Class I pricing structure under Federal Orders may be undertaken in the not too distant future. To that end, DCMA considers these proposals to be possibly temporary in nature pending any changes to the broader Class I price system which may come about from that review.

To effectuate the proposed changes in minimum Order Class I prices in the three subject marketing areas, DCMA proposes modifying section 100x.51 of each of the three southeastern region Orders by including a new provision, a "Class I price adjustment", which will be added to the Class I price "mover", and to the section 1000.52 Class I differential to obtain the monthly minimum Order Class I price.

Exhibit 21, pages D1 and D2 is a summary table of proposed Class I price adjustments and the current Class I differential by Federal Order distributing plant location within Orders 5, 6 and 7, which added together thus provides the effective proposed Federal Order Class I price surface. Included in the Notice of Hearing are the proposed complete sections 1005.51(b), 1006.51(b), and 1007.51(b), detailing the full list of proposed adjustments for all counties and parishes within the Order 5, 6 and 7 marketing areas. Exhibit 21, page E provides a color map of the proposed effective Class I price surface for the Appalachian, Florida and Southeast marketing areas.

In determining the proposed Class I prices, DCMA used combined multiple methodologies in the price surface development process, with Class I prices being built recognizing that minimum Order Class I prices must remain aligned with neighboring marketing areas which are not at this time being proposed to be amended. Given the neighboring Order Class I price alignment constraint, an acquisition cost model for procuring and moving bulk milk into the southeast from multiple potential supplemental sources outside the southeast was analyzed and the minimum cost used to establish the proposed Class I price in the most distant point in the southeast from those supplemental supplies - that point being south Florida. After establishing a Class I price for south Florida, then plant location points successively nearer the supplemental sources were analyzed, establishing prices progressively lower and lower as plant locations were nearer and nearer to the supplemental source locations.

As a check method to the bulk milk acquisition cost model and process, a second model was developed which sought minimized acquisition costs of moving packaged fluid milk products between other-order distributing plants located in Federal Order marketing areas contiguous to the southeastern Orders and plants within the southeastern Order, with further successive cost minimizations for plant to plant packaged fluid milk product movements within the southeast. Finally, the relative Class I price data supplied by the two acquisition cost models were smoothed, using industry knowledge and best professional judgment to develop the traditional Class I price surface as is proposed. We applied industry knowledge and best professional judgment and concluded which plants had sufficiently common local area producer milk procurement, sufficiently common areas of supplemental milk procurement, and

were located within near enough proximity to be in potential competition for Class I sales. These plants were grouped to the extent possible in common pricing zones.

Exhibit 21, page F provides the initial bulk milk movement and procurement calculation for south Florida, using the five possible alternative supplemental supply locations of Wayne County, Ohio; Jasper County, Indiana; Hopkins County, Texas; Lancaster County, Pennsylvania; and Franklin County, Pennsylvania. In the exhibit example, the mileage from each of the possible supplemental sources was computed to Miami, using a mileage rate of \$0.00352 per hundredweight per mile, which represents 80 percent \$0.0044 per mile, \$0.0044 being the rough average of recent Market Administrator mileage rates used in the Transportation Credit provisions of Orders 5 and 7. The calculated cost of hauling to Miami was then added to the existing Class I differential in each of the potential supplemental supply locations to get an acquisition cost for Miami using each of the alternate supply locales. In the Exhibit example, Wayne County, Ohio was the least cost supplier under the calculated bulk milk acquisition cost model, and the resulting possible Class I differential in Miami would be \$6.14 per hundredweight. After calculating the minimum cost of supplying Miami under this scenario, Class I prices at successively closer points to the reserve supply areas were calculated to develop the initial possible Class I price framework.

Exhibit 21, pages G1 and G2 provides further examples of the bulk movement model-predicted prices at various plant locations in Orders 5 and 7, using Miami as the base point.

As discussed, the second model applied cost minimizing calculations based on packaged fluid milk movements starting with plant locations contiguous to, but outside the Order 5 and 7

marketing areas. Exhibit 21, page H provides the example model calculation for packaged fluid milk delivery to Lafayette, Louisiana and Shreveport, Louisiana. Again, successive movements of packaged fluid milk movements plant to plant from the outer edge of the Order 5 and 7 marketing areas were then analyzed, moving toward Florida, and at each plant location the minimum acquisition cost determined. The mileage rate used in the packaged milk movement model was \$0.00396 per mile, approximately 80 percent of the market administrator per mile rate of \$0.0044 per mile 48,000 pound bulk milk load, factored back to a 42,000 pound packaged milk load. The packaged milk hauling cost per mile of \$0.00396 is approximately 71 to 72 percent of the real cost of hauling packaged milk.

The bulk delivery models and packaged milk movement models provided strikingly similar overall results. The models did generate some differences at a few plant points, but these were easily explained and reconciled.

Using the bulk milk movement generated price surface and the packaged fluid milk movement generated price surface as guides, a smoothed Class I price surface was developed using industry knowledge and best professional judgment to group plants into pricing zones, thus providing a traditional Class I price surface. The resulting Class I price surface is the price system proposed by DCMA today. Both the bulk milk movement and packaged milk movement models used hauling costs which are notably less than the real cost of hauling. This allowed flexibility in defining which plants were placed into which final price zones, since the initial prices generated by the two models allowed for variations. As will be seen in later data, differences between plant prices in the final Class I price surface did not exceed the real cost of hauling.

In developing the Class I price surface, all plant locations within Orders 5, 6 and 7 received some Class I price increase, with the smallest changes occurring in northern Virginia, north-central Kentucky, southern Indiana, Arkansas, southwest Tennessee, and northwest Louisiana. These plant locations all have proposed Class I price adjustments in the new sections 1005.51(b) and 1007.51(b) of \$0.10 per hundredweight. Successive tiers of plants within the marketing areas, that is, successively farther from the "outside" edge of the marketing areas see progressively increasing Class I price adjustments. According to Market Administrator analyses previously introduced as Exhibit 9, page 10, Exhibit 17, page 1, and Exhibit 18, page 1, the expected annual increase in Class I revenue in the Order 5 pool for 2004 through 2006 resulting from the Class I prices as proposed would have been \$19.3 million, \$18.6 million and \$18.3 million respectively for each year. For the Order 6 pool the additional Class I values would have been \$36.4 million, \$38.3 million and \$39.2 million respectively for each year, and for the Order 7 pool, the additional Class I values would have been \$16.8 million, \$17.1 million and \$17.7 million respectively for each year.

The Market Administrators introduced Exhibit 9, page 10, Exhibit 17, page 1, and Exhibit 18, page 1, projecting that Order base zone minimum uniform prices would increase approximately \$0.25 to \$0.26 per hundredweight, \$1.19 to \$1.22 per hundredweight, and \$0.64 per hundredweight per year in Orders 5, 6 and 7 respectively under the DCMA proposal. Increasing the minimum Order Class I prices under the three southeastern Orders, and the resulting uniform price increases will provide dual benefits, as intended in the establishment of a Class I price surface. First, the increased uniform prices resulting from increased pooled Class I revenues will send economic signals to producers currently

supplying the three Orders, hopefully encouraging additional milk production to supply the marketing areas. Second, uniform price increases in the three Orders will offer additional economic incentives for moving supplemental milk into the Orders, if sufficient milk is not available within or nearby the Orders' marketing areas. This is exactly the intent of the regulated Class I price surface.

The primary use of milk in the southeast is in fluid milk products. Some soft and hard dairy product manufacturing remains, but the number of plants located in the three marketing areas which produce these manufactured products has declined over the years, as milk production has declined. Some of the manufacturing plants which remain serve predominantly as balancing facilities, converting seasonal or weekend reserve milk supplies into storable products.

The costs of servicing Class I plants exceeds the costs of serving plants which manufacture hard products. The daily, weekly, monthly and annual fluctuations in Class I demand back up quickly onto the marketers of bulk milk to the Class I plants. Hard product manufacturing plants are not as immediately impacted by changes in the demand for their products resulting from events like school calendars, grocery store sales promotions, holidays and even predicted snowy days. Further, as Federal Order provisions and Order regulated prices suggest, hard product manufacturing plants can make their products and can store those products for much later sale. Class I plants do not have the luxury of building inventory in times of surplus and waiting for an opportune time to sell their product. Likewise Class I plants cannot hold substantial inventories while schools are on breaks, or until milk sales pick back up after the summer; they cannot build large inventories in anticipation even if they know

a grocery store chain is going to run a sales promotion on milk. Whether stored as bulk milk in a plant silo, or in jugs in refrigerated coolers, fluid milk products have a short and finite life expectancy.

Class I plants vary their receipts of bulk milk with the near-term and immediate-term needs for that milk in fluid milk products. Variation in daily receiving becomes greater and balancing requirements on their bulk milk suppliers increases, much more-so than for deliveries to hard product manufacturing facilities. This variation in processing makes supplying of bulk milk for fluid use costly. As the proportion of use in fluid milk products in a marketing area increases as a portion of its total raw milk supply, these supply and balancing costs increase proportionally. These higher costs of supplying Class I plants are reflected in the Class I differential, and the predominantly Class I Order marketing areas therefore are expected to have Class I prices reflective of these high supply and balancing costs.

The Secretary's September 1, 2006 Tentative Partial Decision on Transportation Credits in the Appalachian and Southeast Orders is replete with data and analyses regarding milk hauling costs, and the impact of diesel fuel prices on those costs. We will not over-burden this record with a rehashing of those data and analyses of the impact of diesel fuel prices on milk hauling costs, other than to provide for this record a history and update with regard to fuel costs and the changes in costs which have occurred since the 1985 Farm Bill, Order Reform, and since the Order 5 and 7 Transportation Credit hearing was held in early 2006. Exhibit 21, pages 11 through 13 provides national average diesel fuel prices annually for 1986 to 2006, and monthly for January 2000 to present for the southeast. The 1986 to 2006 annual data may be found at www-cta.ornl.gov/data/tedb25/spreadsheets/table10_04.xls, quoted from the U.S.

Department of Energy. Monthly data for January 2000 to present can be found at <http://tonto.eia.doe.gov/oog/ftparea/wogirs/xls/psw18vwall.xls#2-M Diesel Prices - All Types!A1>, USDOE/EIA. As used by the Market Administrators in the calculation of the mileage rate for transportation credits, the later data are the Lower Atlantic and Gulf Coast regions as reported by the EIA.

As previously discussed, the Class I price surface as proposed resulted from running two milk supply models, modified by industry experience and best professional judgment to arrive at the Class I price surface. To the extent possible, the existing Class I price relationship of nearby plants was preserved as current. Plants located within the same or very closely located metropolitan areas, if the Class I prices are currently the same, received the same Class I price in the proposal. Cities or groups of cities where plants had their common Class I price preserved include Little Rock and Ft. Smith, Arkansas; Atlanta, Dacula, and Braselton, Georgia; Baxley and Savannah, Georgia; Louisville, Kentucky and Holland, Indiana; Fulton and Murray, Kentucky; London and Somerset, Kentucky; Nashville and Murfreesboro, Tennessee; Memphis and Covington, Tennessee; Winston Salem and High Point, North Carolina; New Orleans, Baker, Baton Rouge, Hammond, and Lafayette, Louisiana; Kingsport and Powell, Tennessee and Lynchburg and Wirtz, Virginia; Orlando, Orange City, Tampa, Plant City, Lakeland, and Winter Haven, Florida; and Clewiston, Deerfield Beach, and Miami, Florida.

Since the underlying transportation costs which created the proposed Class I price surface have changed substantially from those which generated the current Class I price surface, there are some notable changes in plant to plant Class I price relationships. In the eastern

and southeastern portions of the Appalachian Order marketing area, Spartanburg, South Carolina is proposed to be in a \$0.20 higher Class I price zone than Winston Salem and High Point, where those cities now have the same Class I price. Mt. Crawford, Virginia is proposed to have a \$0.30 per hundredweight lower Class I price than Lynchburg and Wirtz, Virginia where those cities now have the same Class I price. Asheville, North Carolina is proposed to have the same Class I price as Winston Salem and High Point, where Asheville now has a Class I price \$0.15 lower than Winston Salem and High Point. The difference in Class I prices between Asheville, North Carolina and Spartanburg, South Carolina is proposed to be increased from \$0.15 to \$0.20 per hundredweight. Charleston, South Carolina is proposed to be in a \$0.30 higher Class I price zone than Florence, South Carolina, where those cities currently have the same Class I price.

In the northern portion of the Order 5 marketing area, Winchester, Kentucky and Madisonville, Kentucky are proposed to have the same Class I price, while currently Madisonville is priced \$0.20 higher than Winchester. Also, it is proposed the Winchester, Kentucky no longer have the same Class I price as Louisville, Kentucky and Holland, Indiana, but rather would have a Class I price \$0.30 per hundredweight higher than Louisville and Holland.

In the central portion of the Appalachian Order marketing area, Athens, Tennessee is proposed to no longer have the same Class I price as Kingsport and Powell, Tennessee, and Lynchburg, Wirtz, and Mt. Crawford Virginia. Rather, it is proposed that Athens have a Class I price \$0.20 per hundredweight higher than the first four of those locations, and \$0.50 higher than Mt. Crawford.

In the southern portion of the Southeast Order marketing area, Hattiesburg is proposed to have the same Class I price as the New Orleans – Baton Rouge area, while Hattiesburg currently has a Class I price \$0.20 per hundredweight less than New Orleans – Baton Rouge.

The west to east increase in Class I differentials as proposed, which represents the increasing costs of hauling milk from the reserve supply area in the southwest, resulted in differing proposed Class I prices across the midsection of the Order 7 marketing area. Currently Shreveport, Louisiana; Kosciusko, Mississippi; Birmingham, Alabama, and the Atlanta, Georgia metroplex all are in the Order's \$3.10 per hundredweight base zone. As proposed here, there will be an increasing Class I price adjustment moving west to east of \$0.10 per hundredweight at Shreveport; \$0.20 per hundredweight at Kosciusko; \$0.30 per hundredweight at Birmingham; and \$0.70 per hundredweight at Atlanta.

Across the Order 5 and 7 marketing areas other relationships between plant locations have changed under the Class I price proposal, representative of the increased costs of hauling between points.

In the Florida Order marketing area, all plants fall into one of three current Class I pricing zones. The DCMA proposal provides for four pricing zones in the peninsular portion of the Order 6 marketing area, although all plants will actually remain in one of three effective Class I price zones. All plants which currently have the same Class I price will likewise continue to have the same Class I price under the proposal. Currently, there is a \$0.30 per hundredweight Class I price difference between north Florida and central Florida, and likewise there is a \$0.30 per hundredweight Class I price difference between central Florida and south

Florida. Due to the increased hauling costs reflected in the proposal, there would be a \$0.40 per hundredweight Class I price difference between north Florida and central Florida, and a \$0.60 per hundredweight Class I price difference between central Florida and south Florida.

DCMA proposes that the base reporting zone for Class I prices and uniform prices be unchanged. For Order 5, prices would continue to be announced applicable for Mecklenburg County, North Carolina, for Order 6, prices would continue to be announced applicable for Hillsborough County, Florida, and for Order 7, prices would continue to be announced applicable for Fulton County, Georgia. Location adjustments for plant locations outside the base pricing zones would be based on the various plant locations' Class I differential plus the new Class I price adjustment, compared to the Class I differential plus Class I price adjustment applicable in the three Order base zones.

Exhibit 21, page J provides three examples of calculations of location adjustments under the DCMA proposal. The first example is the calculation of the location adjustment applicable for Nashville, Tennessee on the Southeast Order, a location within the Order 7 marketing area. The second example calculation is the location adjustment applicable for a load diverted and pooled on Order 7, delivered to a St. Louis., Missouri plant, which is outside the Southeast Order marketing area. The third example calculation is the location adjustment applicable for a load diverted and pooled on Order 32, delivered to an Atlanta, Georgia, plant. The second and third examples show the compatibility of the DCMA proposed Order 5, 6 and 7 language with existing Orders not a part of this Proceeding.

While the effective difference in Class I prices between plants in many instances has changed under the DCMA proposal, the number of effective price zones actually has not. Exhibit 91, page K provides a listing of the Class I differential zones in the current Orders, as well as the effective Class I prices as proposed. As can be seen, there are currently 13 effective Class I price zones in Orders 5 & 7, and 3 effective price zones in Order 6. At current, Class I differentials range from \$2.20 in Orders 5 and 7 to \$3.60, with a simple average difference from one price zone to the next of \$0.12 per hundredweight. Under the DCMA proposal, the number of effective price zones would still be 13, with a simple average difference from one price zone to the next of \$0.19 per hundredweight.

The changes in average price zone differences are supported by the increased hauling costs use to build the Class I price surface. In Orders 5 & 7, the total range in current differentials from lowest to highest is \$1.40 per hundredweight, predicated on an imputed hauling rate per ten miles of approximately 1.9 cents. As proposed, the total range in Class I prices from lowest to highest is \$2.30 per hundredweight, predicated on an imputed hauling rate per ten miles of approximately 3.5 cents. The imputed hauling costs increased approximately 84 percent, and the range in Class I prices increased about 64 percent in Orders 5 and 7.

In the Florida Order area, the current range in differentials from lowest to highest is \$0.60 per hundredweight, spread equally across three effective zones. While the proposed number of pricing zones under Order 6 is four under the DCMA proposal, the true effective number of price zones remains three, in that one proposed zone currently contains no plants. In Order 6, the current imputed hauling rate per ten miles is approximately 2.0 cents. As proposed, the total range in Class I prices from lowest to highest is \$1.00 per hundredweight, predicated on

an imputed hauling rate per ten miles of approximately 3.5 cents. The imputed hauling costs increased approximately 75 percent, and the range in Class I prices increased about 67 percent.

For Orders 5, 6 and 7, the Class I price zone system as proposed by DCMA is indicative and reflective of the imputed cost of hauling, as should be the case.

As a final check process to the smoothed Class I price surface, the data in Exhibit 21, pages L1 through L8 was developed. These data provide an analysis of the current Class I price applicable at plant locations within the Order 5, 6 and 7 marketing areas, and the current per-ten mile relationship of those locations to plant locations within the three-Order marketing areas with lower regulated Class I prices, and which are within 200 miles of the subject plant location. Likewise, the same analysis is provided showing the per-ten mile differences using the Class I price differences as proposed by DCMA. As can be seen, there are the inevitable changes in Class I price differences between plant locations resulting from the new proposed Class I price surface. However, as can be seen from the last column on the right, the differences between plant locations under the DCMA proposal do not exceed the cost of moving Class I fluid milk products between those locales, thus offering no incentive for uneconomic movements of milk.

Hauling costs have increased since the current Class I price surface was established. This fact is indisputable, and is true for movements of packaged fluid milk products as well as for bulk milk. In developing the Class I price structure which would help attract a sufficient quantity of milk for the marketing areas as proposed, DCMA had two fairly clear choices.

First, retain all the plant to plant Class I price relationships between plants in Orders 5, 6 and 7 the same as they are now, meaning that to increase regulated Class I revenues all Order 5, 6 and 7 plants would experience the same Class I price increase, or second, change the slope of the⁹ Class I price surface within the Order 5, 6 and 7 marketing areas moving west to east and north to south, and change some plant to plant Class I price relationships which have existed for at least the last seven years. In either case, plant to plant price relationships would change.

In the first option, in order to appreciably increase regulated Class I values, the plants on the western and northern outer rim of Orders 5 and 7 would see very large increases in their Order Class I prices, significantly changing those plants' price relationship with plants regulated by contiguous Orders not a part of this proceeding. In the second option, the slope of Class I prices could be changed, adding an economically justified amount to the Class I prices at the Order 5 and 7 rim plants, then with progressively increasing Class I values as we moved east and south within Orders 5, 6 and 7. Either way, somewhere plant to plant Class I price relationships would be changed. The decision DCMA made was to elect the second option, making regulated Class I price changes at all plants within Orders 5, 6 and 7, recognizing that some existing Class I price relationships would be disturbed, rather than create massive Class I price changes on the outer border of Orders 5 and 7. DCMA believes that this process provides the more orderly process for transitioning Class I values in the Order 5, 6 and 7 pools to the higher values needed to attract a sufficient quantity of milk for the three marketing areas. Further, changing the slope of the Class I price surface inside Orders 5, 6 and 7 will encourage milk to move within the Order areas, where raising Class I prices uniformly throughout the three order marketing areas would not.

To repeat the main thrust of DCMA's Class I price proposal, the increased Class I prices provided in the proposal will enhance revenues in the monthly Federal Order pools. Based on analyses completed by the Market Administrators for the three Orders, and previously described in Exhibit 9, page 10, Exhibit 17, page 1, and Exhibit 18, page 1, DCMA expects annual pooled Class I revenues in the Order 5, 6 and 7 pools to increase \$18.3 million, \$39.2 million, and \$17.7 million, respectively. These increases in Class I prices would have been anticipated to increase base zone uniform prices in 2006 by \$0.26, \$1.20 and \$0.64 per hundredweight, respectively, for the three Orders.

Increasing the minimum Order Class I prices under the three southeastern Orders will provide dual benefits, as intended in the establishment of a Class I price surface. First, the increased uniform prices resulting from enhanced pooled Class I revenues will send economic signals to producers currently supplying the three Orders, hopefully encouraging additional milk production to supply the marketing areas. Second, uniform price increases in the three Orders will offer additional economic incentives for moving supplemental milk into the Orders, if sufficient milk is not available within or nearby the Orders' marketing areas.

Redefining and changing the slope of the Class I price relationships within the southeast Orders will likewise send signals to producers to direct supplies to the most milk-deficit portions of the region.

Prong Two: Diversion Limits In Orders 5 and 7

As part of the package of proposals, DCMA proposes lowering the codified diversion limit percentages provided in sections 1005.13 and 1007.13 of the Appalachian and Southeast Orders.

Currently, percentage limits on diversions to nonpool plants in Order 5 are 25 percent of deliveries to pool plants during the months of January, February, July, August, September, October and November, and 40 percent of deliveries to pool plants during the months of March, April, May, June and December, an annual simple average of 31.25 percent. The current percentage limits on diversions to nonpool plants in Order 7 are 50 percent of deliveries to pool plants during the months of January, February, March, April, May, and June, and 33 percent of deliveries to pool plants during the months of July, August, September, October, November, and December, an annual simple average of 41.50 percent. There is an effective limit of zero diversions to nonpool plants on milk delivered to pool distributing plants in each of the two Orders and for which a transportation credit is requested.

Under the Orders, diversions to nonpool plants allow for the associating of reserve supplies with an Order's marketwide pool, without the uneconomic movement of milk to pool plants, and then ensuing transfers of surplus milk supplies from pool plants back out to nonpool plants. Appropriate diversion limits for a Federal Order marketing area must take into account the need for reserve supplies for servicing the Class I needs of the marketing area; the need for balancing supplies weekly, monthly, seasonally, and annually; and producer seasonality of production. In general, historically, the more deficit a marketing area is in terms of milk supplies compared to Class I demand, the lower the allowable diversions to nonpool plants compared to deliveries to pool plants. Diversion limits in Orders 5 and 7 reflect this general

relationship, with diversion limits which are tighter than Orders to the north and to the west, and looser than the Florida Order. However, the diversion limits in Orders 5 and 7 are in need of improvement.

DCMA proposes making the diversion limit percentages stated in the Appalachian and Southeast Orders identical. The proposal calls for diversions to nonpool plants being limited to 25 percent of deliveries to pool plants during the months of January, February, July, August, September, October and November, and 35 percent of deliveries to pool plants during the months of March, April, May, June and December. This change lowers the stated diversion limit percentages in the Appalachian Order by five percentage points in each of the months of March, April, May, June and December, resulting in a reduction in the simple average annual diversion limits in Order 5 of 2.08 percentage points. The proposal would decrease the stated diversion limit percentages in the Southeast Order by twenty-five percentage points in each of the months of January and February; by fifteen percentage points in each of the months of March, April, May, June; by eight percentage points in each of the months of July, August, September, October and November; and an increase of two percentage points in December, resulting in a reduction in the simple average annual diversion limits in Order 7 of 12.33 percentage points.

Making the codified diversion limit percentages in Orders 5 and 7 the same may tend to more closely align the monthly blend prices generated by the two Orders. While not a particular focus of this proceeding, this possible improved blend price alignment between the Appalachian and Southeast Orders could provide an ancillary benefit to the marketers of milk in the two marketing areas.

It should be noted that the changes in codified percentage diversion limits as proposed do not fully capture the real volume of milk which may be removed from the two pools as a result of the proposed changes. If the volume of producer milk delivered to pool plants were the same each month, then the volume of milk which would no longer be eligible for diversion would be 6.67 percent and 29.72 percent in the Order 5 and Order 7 pools, respectively, a substantially greater reduction than it appears when comparing the codified monthly percentage limits changes. This calculation is provided in Exhibit 21, page M. The proposed reductions in allowable diversions in the Appalachian and Southeast Orders would be on top of the reduction in allowable diversions to nonpool plants which came about as a result of the Secretary's 2006 Order 5 and 7 Transportation Credit Decision.

The proposed diversion percentages will reduce the volume of milk which may be pooled by diversion to nonpool plants on both the Appalachian and Southeast Orders, a change which should further increase producer uniform blend prices in the two Orders over and above the increases in producer uniform prices resulting from the proposed increased pooled Class I values. The benefits of the resulting increased uniform prices will complement and enhance those benefits which will accrue from increased uniform prices resulting from increased Class I prices, namely encouraging milk production from current producers, and enhanced economic incentives for movement of supplemental milk supplies into the region.

According to Market Administrator analyses, previously described in Exhibit 9, page 13 and Exhibit 17, page 1, the estimated impact on minimum Order uniform prices from decreasing percentage diversion limits in Orders 5 & 7 to the levels as proposed would be

average annual increases in uniform prices of \$0.02 and \$0.07 per hundredweight respectively.

How much uniform blend price increase any particular producer may experience as a result of the proposed changes in Class I prices under the Orders will vary based on how much the Class I price is increased at the producer's plant of delivery. Producers delivering to plants which receive greater increases in Class I prices will experience greater increases in blend prices than a producer delivering to a plant which receives a lesser Class I price increase. However, any increases in uniform blend prices to producers which result from reduced pooled diversions to nonpool plants will be uniformly experienced across all producers in the pool.

DCMA believes the diversion limit percentages as proposed properly reflect the nature of balancing the necessary reserve supplies for the two marketing areas, daily, monthly and seasonally, and will allow the appropriate volumes of milk moved to nonpool plants to be pooled on the Orders.

Exhibit 21, pages N1 through N13 and O1 through O13 provides an analysis of the receipts of milk daily by pool distributing plants regulated by Orders 5 and 7 for the period of January 2004 through December 2006. Pages N1 through N13 are data for Order 5, and pages O1 through O13 are data for Order 7. The data on daily receipts by pool distributing plants is taken from Market Administrator Exhibit 9, pages 2-5, and Exhibit 18, pages 12-15. In this analysis, each day's producer milk receipts by pool distributing plants on the Order were compared to the highest day of receipts by pool distributing plants for that month. The

difference between the highest day of receipts and each day's actual receipts for the month were then summed. This resulting total, representing the total volume of milk which was not received each day of the month versus the highest receiving day, was then divided by the month's total actual receipts by pool distributing plants. The resulting value represents in percentage terms, the necessary reserve required each month over that month's receipts to have enough milk available to cover plants' day of greatest need. Also provided is the same calculation for each Order on an annual basis.

The daily receipt data for Order 5 did not include the totality of receipts at pool distributing plants; rather, the data represent approximately 85 to 90 percent of the daily data. The pounds reported by the Order 5 Market Administrator were grossed up by the monthly reporting percentage to give a better picture of the daily volumes marketers dealt with in the marketing area. While this gross-up process presumes that the remaining unreported daily receipts data would be identical in variation to the reported portion of the receipts, we do not believe this presumption impacts the nature and results of the analysis in any significant way. If anything, DCMA believes this gross-up calculation in the Appalachian Order analysis would tend to reduce the analyzed variation in pool distributing plant receipts versus the real variation.

As would be expected, the calculated reserve factor varies month to month, and year to year depending on the actual receipts at plants and how high the highest day of receipts actually was, and for that matter, how low the lowest days of receipts were. Over the 36 month period represented in the analysis, we can see that on average about 12 to 13 percent of monthly pool distributing plant receipts is the bare minimum reserve necessary to cover daily

fluctuations in pool distributing plant receipts. On an annual basis the reserve requirement as calculated is about 22 percent at a minimum.

The analysis as shown does not presume any necessary reserve to cover daily, monthly and season variations in the producer supply, nor does it account for any general reserve requirement over and above the plants needs on the month's highest days. It would be serendipitous indeed if the day of highest milk needs by plants coincided with the day of highest production in the month, and every day's production followed the variation in daily need. Such is never the case.

Since the average reserve requirement as computed in the analysis for Order 5 versus Order 7 does not differ greatly over the 36 month period, DMCA feels having the same diversion limits in Orders 5 and 7 is a justifiable, workable and desirable procedure.

Based on the analysis described above, and allowing for a reasonable additional reserve in the tightest supply months of 10 to 12 percent above the bare minimum daily reserve requirement depicted above, DCMA proposes a limit on diversions to nonpool plants during the months of January, February, July, August, September, October and November of 25 percent of pool plant deliveries for both Order 5 and Order 7. The additional reserve proposed over the calculated bare minimum reserve detailed in the Exhibit will allow for unforeseen changes in the supply demand relationship, daily variation in producer supplies, weather occurrences, and the general need for reserves to cover the marketing areas' needs. It should be noted that the days of greatest need and days of least need are not fore-known,

and if anyone even tried to predict them, one would only be able to predict them with poor accuracy.

In order to accommodate seasonal fluctuations in dairy farmer supply, and by seasonal fluctuations we mean the spring flush, DCMA proposes a limit on diversions to nonpool plants during the months of March, April, May, and June of 35 percent of pool plant deliveries for both Orders 5 and 7. The 10 percentage points higher level of allowable diversions will permit additional volumes of diversions to nonpool plants in the spring and early summer months, above the diversion allowance in the tighter supply months, thus allowing regular producers who supply the Class I needs of the marketing areas in the tight supply months to pool all of their additional production in the flush months, as well as accommodation of the regular decline in Class I sales which occurs every summer when schools are out of session. Federal Order provisions generally recognize the need for additional diversions to nonpool plants to handle increases in producer supplies and reductions in Class I demand during the spring and early summer months.

Then we come to December, which includes the one day each year when the level of plant pool distributing plant receipts can be somewhat predicted.

December, normally considered a month of celebrations, simply is no party for marketers of milk. Around the middle of the month, schools close for the two week traditional break, Class I plants shut down or severely limit their receiving operations over the holiday period, and bulk milk marketers are left with substantial surplus milk volumes and often limited places to put it.

For the most part cows, as agnostics, do not celebrate the various December holidays, and insist on continuing to give milk every day right through the month of December.

The last half of December in every way represents as surplus a condition as the worst days in the middle of the spring flush. Looking back at Exhibit 21, pages N1 through O13, we note that without fail, December 25 each year is the day of lowest pool distributing plant producer receipts. For these reasons, December is proposed to have a limit on diversions to nonpool plants during the month of 35 percent of pool plant deliveries for both Orders 5 and 7. Nearby and adjacent Orders to the Appalachian and Southeast Orders recognize this fact and contain diversion provisions allowing greater diversions to nonpool plants in December than in the immediately preceding tight supply months.

The second part of the diversion provision prong of DCMA's three-prong proposal deals with the requisite number of days a producer must be received at a pool plant during the month in order for that producer's milk to be eligible for diversion to a nonpool plant. Currently in the Appalachian Order, a producer must be delivered to a pool plant for not less than two days during the months of January through June, and for not less than six days during the months of July through December, for the dairy farmer's milk to be eligible to be pooled by diversion. In the Southeast Order, a producer must currently be delivered to a pool plant for not less than four days during the months of January through June, and for not less than ten days during the months of July through December, for the dairy farmer's milk to be eligible to be pooled by diversion.

The producer Marketing Order association requirement, commonly referred to as the "touch base" days, defines the minimum number of days each month that a dairy farmer must supply the Class I needs of the marketing area in order to be considered sufficiently associated with that Class I marketplace, and thus his or her milk eligible for pooling by diversion to a nonpool plant.

As milk production within the Appalachian and Southeast Orders marketing areas has declined, and Class I demand grown, the milk shed for two Orders has grown geographically. The obvious result of this growth in the geographic milkshed footprint is that more producers, located more distant from the marketing areas must fill the unmet Class I needs of the marketing areas. These distant producers may very well serve the Class I needs of the marketing areas almost every month of the year, are ready to serve the marketing areas at any time as needed, yet, during short periods of time, particularly during the spring flush, or on weekends, their milk may be needed sparingly. These most distant farms represent the seasonal reserve and weekly reserve needed for the Orders.

In order to facilitate the efficient pooling of these reserve supplies, DCMA proposes reducing the touch base days in both Orders 5 and 7 to one day each month. A producer would then be eligible for diversion to a nonpool plant in any month during which the dairy farmer's milk was delivered at least one day to a pool plant. The farm would continue to be required to perform at least at that minimum level each and every month to be eligible for pooling the deliveries of that farm to nonpool plants, demonstrating that the farm's milk is indeed able to serve the Class I needs of the marketing area at any time when called upon for greater volumes.

Reducing the number of touch base days for pooling a producer will lessen the need to deliver milk of producers to pool plants when lesser volumes of milk from those producers is truly needed, thereby discouraging uneconomic movements of milk. Efficiency in delivering milk to the marketing areas requires that the most distant producers are the last producers called upon to serve the needs of the marketing area, and conversely, the most logical first producers to leave at home on days when the marketing areas are sufficiently supplied with nearer milk.

To require distant producers to deliver more days to pool plants when the milk is not truly needed requires the substitution of the more distant producers for delivery into pool plants, displacing nearer producers already serving those plants. This only adds trucking miles and marketing costs, and does not increase the supply of milk available for the marketing area. In fact, the displacing of nearer-by milk, and the requisite delivery of milk from more distant producers is a zero sum game. The more-local producer is moved out, and the distant producer is moved in, with no net gain or loss of pooled milk. Only the truckers gain.

It is important to note that the real effective limit on diversions to nonpool plants in a Federal Order is the Order's diversion limit percentages. Regardless of the number of producers who deliver milk during the month to pool plants on the Order, the volume of milk those producers market in a month, and where those producers' milk is delivered, the effective maximum diverted volume is the percentage limit in effect in the Order. DCMA has proposed reducing the diversion limit percentages as described above.

The proposal that farms be required to touch base at Order 5 and 7 pool plants one day per month for both Orders; along with the diversion limit percentages proposed above, would completely harmonize the diversion provisions of the Appalachian and Southeast Orders, and provide diversion provision alignment with other nearby and adjacent Orders. Exhibit 21, page P provides a comparison of touch-base requirements and diversion limits percentages by month for the Northeast, Mideast, Central, Southwest, and Florida Orders as current, and for the Appalachian and Southeast Orders as proposed.

The current provisions in Orders 5, 6 and 7 allow the Market Administrator discretion in setting the effective diversion percentages and touch base days at rates and requirements different from the codified provisions if marketing area supply and demand conditions warrant. DCMA supports the continuation of the provisions allowing Market Administrator discretion in changing diversion limits and touch base days. This is an important provision allowing for timely modification to the diversion limits and touch-base days if conditions in the marketing area change.

Prong Three: Transportation Credits in Orders 5 & 7

On September 1, 2006 the Secretary issued a Tentative Partial Decision which restructured the Transportation Credit Balancing Fund provisions in the Appalachian and Southeast Orders. The Tentative Partial Decision updated the hauling cost factor used in computing transportation credits, and installed a new fuel adjuster which helps keep the transportation credit mileage rate more current with changes in fuel costs. At that time, the maximum

assessments on Class I handlers used to furnish the Transportation Credit Balancing Funds were increased from \$0.095 per hundredweight to \$0.15 per hundredweight in the Appalachian Order, and from \$0.10 per hundredweight to \$0.20 per hundredweight in the Southeast Order. These were needed and appropriate amendments to the transportation credit provisions, and DCMA appreciates the Secretary's actions in this area.

The record of the 2006 Transportation Credit Proceeding and the Tentative Partial Decision are replete with analyses regarding costs of hauling and the impact of fuel costs on hauling, and there is no need to re-hash those data here. Rather, DCMA proposes new and additional changes to the Transportation Credit Balancing Fund provisions to make the provisions more relevant to the current state of milk marketing in the two Orders.

DCMA proposes four enhancements to the Transportation Credit provisions. First, we propose extending the months during which Transportation Credits are paid to the months of January and February, in addition to the months of July through December as current. DCMA proposes retaining June as an optional Transportation Credit payment month based on industry request and Market Administrator discretion. Second, DCMA proposes the payment of Transportation Credits on full loads of milk, rather than just the calculated Class I portion as current. Third, the DCMA proposal simplifies the process for determining which producers are supplemental, and therefore their milk eligible for transportation credits. Lastly, DCMA proposes raising the maximum Class I assessment for transportation credits from \$0.20 per hundredweight to \$0.30 per hundredweight in the Southeast Order.

The data on daily receipts by pool distributing plants previously described in Exhibit 21, pages N1 through N13 and O1 through O13 are also instructive regarding the months of greatest need for milk in the Appalachian and Southeast marketing areas. Likewise, a review of data in Market Administrator Exhibits 6, 7, 8, 11, 12, 13 and 14, 15 is useful in evaluating the volume of milk needed for Class I in the Orders.

The need for supplemental milk in the Order 5 and Order 7 marketing areas has become acute in the months of January and February. When transportation credits were first installed in the Orders in the middle 1990's, the available milk supplies within and nearby the marketing areas were sufficient to provide a sufficient quantity of milk for fluid use in the seasonally long months in the first half of the year. Only during the months of seasonally low production did the marketing areas require supplemental milk from more distant sources to supply the various Orders' Class I needs. Such is no longer true, and now the seasonal increase in production from producers associated with the Orders year around is not sufficient to supply the Class I milk needed within the marketing areas in January and February.

January and February regularly are months of high daily average Class I use in both the Appalachian and Southeast Orders, see Exhibit 21, page B1, and January and February are months which precede the come-on of the seasonal flush in the southeast. As a result of these factors, January and February now are months which require substantial supplemental supplies to meet the fluid milk needs of the two marketing areas. The DCMA proposal would offer marketers of milk an opportunity to recoup through the transportation credit system, a portion of the hauling costs incurred on the substantial volume of milk imported into the two marketing areas from supplemental producers during the months of January and February.

Exhibit 21, pages B1 through B3 provides additional data regarding the supply-demand relationship in Orders 5 and 7. Page B1 shows the Class I producer milk monthly for Orders 5 and 7, and for the two Orders combined, and compares the daily average Class I use each month for 2004 through 2006 to that years annual average daily Class I use. Each month's daily average use of Class I milk is then expressed as a percentage of the annual daily average use. Months with percentages greater than 100 percent had higher daily average Class I use than the annual daily average. Months with percentages less than 100 percent had lower daily average Class I use than the annual daily average. Exhibit 21, Page B2 shows the monthly volume of milk produced within the Appalachian and Southeast marketing areas that was pooled on some Federal Milk Order for the 2004 to 2006 period. Exhibit 21 Page B3 then compares the total monthly Class I producer milk in Orders 5 and 7 to the Federal Order pooled milk produced within the two marketing areas for the three year period. The data from Exhibit 21, page B3 show that on an annual basis, and in many months of the year, there are not sufficient quantities of milk produced in the Appalachian and Southeast marketing areas to meet the needs for Class I, much less any needed reserve, or any use in pool distributing plants in Class II products. When weekends and other daily and weekend balancing need are added, the deficit condition becomes even bleaker. We can see from the data that the problem is worsening.

The data on Federal Order producer milk marketings in Exhibit 21, page B2 do show some irregularities which may skew the values slightly. April 2004 is of particular note. There may have been some milk production in the region that month which was not pooled on any Order

due to price inversions. In addition, a change to the Appalachian Order marketing area in November 2005 further skews the in area milk production statistic.

Further complicating any analysis of Class I use in the Appalachian and Southeast Orders is the change in pool distributing plants which has occurred over the 2004 to 2006 period. In the Appalachian Order, six pool distributing plants closed during the three year period, one plant became regulated as a result of the Order 5 marketing area expansion, and one plant re-opened under different ownership after having been closed for about a year. In the Southeast Order, two pool distributing plants closed between January 2004 and December 2006, and one newly constructed plant opened. One plant moved back and forth from fully regulated and partially regulated status. These changes pool distributing plants can impact the Class I milk pooled on the Order.

At any rate, over the three year period, the data are clear that January and February are months of higher than average Class I use, and are months which precede the spring flush. The combination of Class I need and available producer supplies now show January and February as months when the supply-demand relationship is more like the existing transportation credit payment months in the last half of the year than the flush months of March, April and May, and thus January and February should be added to the months when Transportation Credit payments are made. Seasonal increases in supplies in the spring flush months of March, April and May support the position that transportation credits should not be paid in those months, at least not for now. These data also support these three months as the months when there is less need for supplemental supplies of milk in the two marketing areas. This issue will be explored in greater detail later.

For the full history of transportation credits in the southeastern Orders, transportation credits have been paid on the calculated Class I portion of the supplemental load of milk. Current transportation credit provisions provide that the calculation of the Class I portion of the load, whether that load is a producer milk load or an other-order plant transferred load, is the calculation used in determining the classification on an other-order plant transferred load, not agreed for Class II, III or IV use, pursuant to section 1000.44. The result is that the Class I portion of a supplemental milk load requested to receive a transportation credit is typically the Market Administrator's monthly percentage estimate of Order-average Class I use. For Order 5 this may range from 65 to 75 percent Class I, and for Order 7 this may range from 60 to 70 percent Class I. The payment of transportation credits on the calculated Class I pounds only, combined with a mileage rate for transportation credits which is by design less than the full cost of hauling, has left marketers receiving through the transportation credit system a very low percentage of the real cost of hauling.

Transportation credits, as required in section 1005.82 and 1007.82, are paid on deliveries of supplemental milk to pool distributing plants. The average use of Class I milk in pool distributing plants typically is in the upper 80 percent range, and often higher, all the while transportation credits remain paid at substantially lower Class I percentage rates.

It should be noted that even plants which are considered "all Class I" do not have all their milk classified as Class I. The extra butterfat which comes into plants from producers over and above the average use of butterfat in Class I fluid milk products gets disposed of by the plant in the form of surplus cream, which generally would be moved to a plant processing Class II or

Class IV products. The maximum Class I use in a typical "all Class I plant" then is limited to about 95 percent Class I. The result is that even in a pool distributing plant which produces only packaged fluid milk products the assessment on Class I milk for transportation credits does not cover all the milk received by the plant.

In Order 5 and Order 7 pool distributing plants whose actual dairy product production is less than virtually all Class I, the predominant second use is in Class II products. Suppliers of milk to these plants deliver the entirety of milk needed by the plant, without regard to the Class uses made of the milk by the plant. Haulers of milk charge the same rate per mile for milk delivered to a plant that produces Class I products, Class II products, or whatever. It really doesn't matter what a plant produces, the cost of moving milk to that plant is the same. So, the cost of delivering a supplemental milk load is not conditioned on the Class I utilization of a plant, and thus amount of transportation credit on that load should not be influenced by the particular use of milk in the plant, or by the Class I use of milk in the Order as a whole.

Transportation credits are paid on supplemental milk deliveries to pool distributing plants only, not to pool supply plants. DCMA supports continuation of this process in the payment of transportation credits. Limiting the payment of transportation credits to pool distributing plants will insure that the cost recovery system provided by the payment of transportation credits will not apply to the delivery of milk to hard product manufacturing plants.

Repeatedly, the Secretary has determined that delivery of supplemental milk into the Appalachian and Southeast Orders is an activity of market-wide benefit, and that the reimbursement of a portion of the costs of hauling on supplemental milk is an action which

promotes the equitable assignment of the costs of hauling this supplemental milk. Further, the Secretary has continued to find that the equitable distribution of supplemental milk hauling costs enhances orderly marketing in the two marketing areas. Expanding the payment of transportation credits to full loads of milk will further enhance orderly marketing, and will help insure sufficient supplemental milk is available for use by pool distributing plants.

In order to insure that the transportation credit provisions do not encourage uneconomic movements of milk, as previously mentioned, the mileage rate established under the transportation credit provisions has been purposely set at less than the full cost of hauling in its own right. In addition, the Transportation Credit provisions provide that on a farm-direct supplemental milk load, 85 miles is deducted from the true origin to destination mileage before calculating the Transportation Credit payment. In effect, no transportation credit is allowed on the first 85 miles of supplemental producer milk Transportation Credit load. At the current approximate mileage rate, this represents an automatic difference of about \$0.37 per hundredweight between of the Transportation Credit paid and the calculated hauling cost, again which is purposely set at less than the real cost of hauling. These protections supplant any possibility that paying of transportation credits on full loads of milk will encourage uneconomic movements of milk.

The proposal that transportation credits be paid during the months of January and February requires that the system for determining which producers are supplemental and thus their milk eligible for transportation credit payments must be amended. DCMA proposes that the process for determining whether a producer's milk is eligible to receive a transportation credit in the Appalachian and Southeast Orders be simplified. Currently, for a dairy farmer's milk to

be eligible to receive a transportation credit, the dairy farm must be located outside the Order 5 and Order 7 marketing areas, and the dairy farmer may not be a "producer" under the Order during more than 2 of the months of February through May, and no more than 50 percent of the production of the dairy farmer during those two months, in aggregate, can be received as producer milk under the Order during those 2 months. DCMA proposes that the requirement that the dairy farm must be outside the Order 5 and 7 marketing areas be retained, but proposes a more simple process for determining the limits to Order association which further define which producers are "supplemental".

Since February is currently a month included in the months which a producer may be out of the pool for determining if the producer is supplemental, and February is proposed as a month for payment of transportation credits, it is necessary to modify the months and provisions for determining which producers are supplemental.

For determining which producers qualify as supplemental suppliers to the Appalachian and Southeast Order marketing areas, DCMA proposes that a dairy farmer may not be a producer on the Order more than 45 of the 92 days in the March through May period, or must have had pooled less than 50 percent of the producer's Grade A milk on the Order during those three months combined. It is important to note that the proposal is an "either - or" process. If the producer is off the pool more than half the days, or is off the pool with more than half of his or her milk during March through May, then the producer is considered to be supplemental, and therefore his or her milk is eligible to receive a transportation credit in the immediately following transportation credit payment period of July through February, and June if applicable. Data analyzed above support March, April and May as the appropriate months to

require producers to be out of the Appalachian and Southeast Order pools in judging their status as supplemental producers.

The proposed system for determining if a producer qualifies as "supplemental" is substantially simpler than the current system, yet retains the basic elements which define a producer as supplemental. Retained would be the requirements that a supplemental producer cannot be located within either the Appalachian or Southeast Order marketing areas, and cannot be a regular producer supplying the marketing areas year around. Limiting the producer to association with the Order pool to no more than half the time or no more than half their milk is sufficient disassociation to render the producer not a regular supplier of milk to the Order.

DCMA proposes to increase the maximum transportation credit assessment allowable under the Southeast Order to \$0.30 per hundredweight of Class I milk, an increase of \$0.10 per hundredweight from the current maximum. Three factors included in this proposal will impact the payments from the Transportation Credit Balancing Funds. The proposed increases in Class I prices in Orders 5 and 7 will lessen payments from the fund, since the differences in origin point Class I prices and delivery point Class I prices will increase. Since all delivery points in Orders 5 and 7 under the Class I price proposal detailed above will see an increase in their Class I price, all calculations of differences between origin and destination Class I prices will increase. Proposals number 1 and 2 contain a conforming changes to the Order 5 and 7 language pertaining to the payment of transportation credits so that the Class I price at the origin and destination points is compared, rather than comparison of origin and destination Class I differentials as is currently specified in the Orders. The addition of the months January and February as proposed for payments of transportation credits will tend to increase

transportation credit payouts, as will the payment of transportation credits on entire loads of milk. Based on analyses by the Market Administrators of the two Orders, introduced at this hearing in Exhibit 9, pages 11 and Exhibit 13, pages 2, DCMA anticipates that the transportation credit assessment rate will be sufficient for Order 5 at the current \$0.15 per hundredweight of Class I milk, but the transportation credit assessment rate will be insufficient for Order 7 at the current \$0.20 per hundredweight of Class I milk, and should be raised to \$0.30 to cover anticipated shortfalls in the transportation credit fund resulting from the proposed amendments.

According to Exhibit 9, pages 11 the Market Administrator for Order 5 estimates that as a result of the DCMA proposal, during the July 2006 through January 2007 period, Transportation Credit payments would have totaled \$4,073,312. DCMA estimates that there would be a payment of \$313,000 for the month of February, thus bringing the total estimated Transportation Credit Balancing Fund expenditure to \$4,383,312. This amount divided by the Order 5 Class I producer milk from 2006 of 4,136,735,262 pounds suggests that, for now, the \$0.15 assessment on Class I producer milk for the Transportation Credit Balancing Fund will be sufficient.

According to Exhibit 13, pages 2 the Market Administrator for Order 7 estimates that as a result of the DCMA proposal, during the July through December 2006 period, Transportation Credit payments would have totaled \$15,704,872. DCMA estimates that there would be total payments of \$2,900,000 for the months of January and February, thus bringing the total estimated Transportation Credit Balancing Fund expenditure in Order 7 to \$18,604,872. This amount divided by the Order 7 Class I producer milk from 2006 of

4,774,045,357 pounds suggests that for 2006 the \$0.30 assessment proposed on Class I in Order 7 would have not provided sufficient funds to pay all claimed Transportation Credits. It is estimated however that the thirty cents per hundredweight Class I assessment would have been sufficient using the DCMA proposal in 2004 and in 2005. DCMA proposes that the maximum Transportation Credits assessment be set at \$0.30 per hundredweight in Order 7, and at such time as it is determined that this rate is truly insufficient, DCMA may propose its revision through another hearing proceeding.

Recent increases in the cost of fuel could have a substantial impact on the magnitude of funds paid from the Transportation Credit Balancing Funds, making the need for sufficient assessments especially relevant. The Secretary's recent Decision on Transportation Credits in Orders 5 and 7 reiterated the need to keep the Transportation Credit Balancing Funds fully funded.

As a protection to the Class I handlers funding Transportation Credits, the Order provisions direct the Market Administrator to establish Transportation Credit assessment rates that insure that handlers of Class I milk will not be charged more than what is reasonably expected to be paid out in Transportation Credits. The Transportation Credit Balancing Funds provisions afford the Market Administrator discretion in setting the assessment rates at or less than the maximum allowed by the Orders, based on projected Fund needs. Proponents continue to support this process, and the Market Administrators' discretion in setting the Transportation Credit Balancing Fund assessment rates in the two Orders insures that if payments from the fund are less than anticipated, assessments can be lowered by the Market Administrator accordingly.

An important nuance to the Transportation Credit Balancing Fund provisions is that if the Transportation Credit Balancing Fund is insufficient in a month to pay all claimed transportation credits, then the Market Administrator prorates available credits to the claimed credits, expending all the available funds that month. There is no process for recouping in the future these unpaid transportation credits if the Funds payments are prorated, meaning, that marketers of milk who are responsible for payment of the hauling costs on supplemental milk are left holding the bag on the unpaid portion of the Transportation Credit. On the other hand, Class I handlers are protected by the Order provisions if the Transportation Credit Balancing Funds become over-funded through the Market Administrator's requirement to suspend Transportation Credit Balancing Fund assessments, or to lower assessment rates. In simple terms, this is a one-sided risk proposition, Class I handlers are assured that their assessments over time will be in line with the needs for funding the Transportation Credit Balancing Funds, but the raw milk marketers are not assured of getting their hauling costs on supplemental milk covered if the Funds are less than fully furnished. For this reason, it is important that the Secretary set maximum transportation credit assessment rates and the Market Administrators set actual rates of assessment high enough to insure sufficient funds are available to cover the claimed credits.

In summary, the Appalachian and Southeast Orders, and their predecessor Orders, have had Transportation Credit Balancing Fund provisions for many years, and the Transportation Credit provisions have functioned as intended by increasing the regulated cost of Class I milk so that supplemental milk could be procured from outside the marketing areas. The

Transportation Credit Balancing Fund system should continue to be a part of the Appalachian and Southeast Orders, and needs to be improved and updated as proposed.

Integrated System Approach

As stated, the DCMA proposal is designed as an integrated and coordinated system of provision changes, designed to meet the needs of the many differing interests in the marketing areas. Just as producers must judge an Order in its entirety when deciding whether or not to approve an Order as amended, the DCMA proposal is part of the entire Order provision package, and stands together as a package of provisions.

The proposed changes to the Class I pricing and diversion limit provisions work together to send the economic signals necessary to insure that a sufficient quantity of milk is available to meet the fluid milk needs of the three marketing areas. The transportation credit provision changes and the diversion limit changes work together to encourage the importation of supplemental milk when needed, and to allow certain milk which is now part of the pooled reserve to become supplemental to the marketing areas, and not pooled year around. The transportation credit provisions work together with the Class I pricing changes to form two fronts for insuring an adequate supply to the marketing areas.

In addition to the obvious relationships of the various prongs of the proposal as described throughout this testimony, there are more subtle linkages as well. The Class I price surface as proposed is based largely on a price gradient of 80 percent of \$0.0044 per hundredweight

per mile. This rate is seemingly less than is paid under the transportation credits provisions, where the \$0.0044 per hundredweight per mile rate comes from. However, when after deducting the required 85 miles from the actual mileage before transportation credits are calculated, the actual per mile rate on Transportation Credits and the proposed Class I price surface begin to line up quite nicely. In Order 5, according to Market Administrator Exhibit 9, page 9, the average distance Transportation Credit eligible supplemental milk moved for during 2006 was 442 miles. In Order 5 the 85 mile Transportation Credit deduction represents a reduction in the effective hauling reimbursement of approximately 19 percent. In Order 7, according to Market Administrator Exhibit 18, page 4, the average distance Transportation Credit eligible supplemental milk moved for during 2006 was 707 miles. In Order 7, the 85 mile Transportation Credit deduction represents a reduction in the effective hauling reimbursement of approximately 12 percent.

Further still, the linkage of the correction of the diversion limit percentages in the Appalachian and Southeast Orders, coupled with the correction of the Class I price surface will create a blend price gradient more in line with the cost of moving milk, and more likely to bring forth a sufficient supply of milk for the region.

DCMA has endeavored to provide a system of Order provision changes which, functioning together, improve the ability for the southeastern region Orders to secure a sufficient quantity of milk for the three marketing areas. This we believe we have done.

Over Order Prices

Over order prices do exist in the southeast, and are reflective of the significant costs associated with service of predominantly fluid milk marketing areas. At present, these substantial costs incurred in supplying milk for the southeast are largely borne outside Order-regulated values. The proponents seek changes to the regulated levels of prices and to the regulated cost recovery mechanisms to give assurance that the necessary revenues will be there to help cover costs of supplying milk for the southeast; to offer assurances to the marketplace that the costs for which reimbursement is sought are indisputable; to recognize the limits in over order pricing to address these issues; and to insure uniform application of the revenues and uniform sharing of the costs.

According to data included in "Dairy Market News", Volume 73, Report 02 and Volume 74, Report 02, Class I Over Order Prices did increase in many cities during 2006 versus 2005. The simple average Class I Over Order Price for all reported cities increased \$0.25 per hundredweight from 2005 to 2006. In the southeast, for the benchmark cities of Atlanta and Miami, the simple average Class I Over Order Prices increased \$0.79 per hundredweight and \$0.67 per hundredweight, respectively from 2005 to 2006, far exceeding the national average increase. Such substantial increases in Over Order prices in the southeast in the coming year are highly unlikely, leaving the almost-certain additional increases in supply costs for moving milk into the southeast likely to go uncompensated.

Federal Order regulated prices are by definition, minimum prices. The proposals made by DCMA continue this practice of setting regulated values and cost reimbursement systems at less than full costs. Hauling costs used in the development of the Class I prices and payment

of Transportation Credits are less than the actual current cost. Over Order prices serve an important function in the price discovery process in that they can react quicker to changes in location values of milk than can the regulated values. Over order prices also compensate marketers of milk for the costs which by definition are underrepresented in the Order regulated values. Given that the DMCA proposal retains the minimalist approach in its allocation of cost values, it is reasonable to expect over order prices to continue to exist in the southeast even if this DMCA Federal Order proposal is adopted.

Disorderly conditions without amendment.

As previously discussed, the Class I price surface under Federal Milk Marketing Orders must be reflective of the relative values of milk across marketing areas, and those relative values must reasonably reflect the real costs of moving milk. Serious deterioration in the effectiveness of the Class I price surface in the southeastern Orders has resulted from a failure of the Class I price surface to keep pace with changes in the cost of milk hauling.

The southeast continues to see declines in milk production within the region, necessitating increasing volumes to be imported into the region from supplemental and distant regular sources.

The costs of procuring and sufficient quantity of milk for the southeast increases as local production decreases, in fact, the supplemental milk costs seem to accelerate faster and faster all the time.

Exhibit 21, pages Q1 and Q2 demonstrate the losses which are incurred at current minimum Order Class I price differences, hauling rates and values for deliveries of milk to pool distributing plant locations within the southeast from six potential supplemental supply locales. The hauling cost factor used is the April 2007 Market Administrator mileage rate for use in the Transportation Credit computations. Three of the supplemental supply origin points are the same as was used in the bulk milk movement and procurement analysis above, three others are different potential supply locales. In each example case, there is a loss on moving milk from the reserve supply area to the southeast. As the cost of hauling increases, and it no doubt will, the losses incurred will increase too.

Exhibit 21, pages Q3 and Q4 repeats the demonstration of transactional losses as just described above, but uses the losses which are incurred at current minimum Order uniform prices, using the average uniform price at location, adjusted from the 2006 average as published in "Dairy Market News" Volume 74, Report 05, January 29 – February 2, 2007. When using blend price differences between the reserve production areas and plant locations in the southeast the losses are only slightly less grim than when using the Class I price differences.

The southeast imports more than one third of its supply in the most deficit months of the year to cover the fluid milk needs of the three marketing areas. In round numbers, this represents more than 300,000,000 pounds of milk moved into the region monthly. If the average supplemental milk hauling and procurement transaction creates a loss of \$1.50 per hundredweight at Order values, even after the collection of Transportation Credits, the total

loss to the southeast would be more than \$4,000,000 per month. An average Order minimum price loss of one dollar and fifty cents on supplemental milk is highly conservative. Unfortunately, these costs are not evenly distributed over all producers supplying the marketing areas.

In the Transportation Credit Tentative Decision on the southeastern Orders in 1996, Docket Number AO-388-A9, et al, the Secretary states in the Conclusion section of the Decision that "Testimony and exhibits introduced at this hearing indicate that the Southeastern United States has a chronic shortage of milk" And further states that "The burden of filling the void between the supply of, and demand for, fluid milk has fallen disproportionately on cooperative associations serving these markets". In the Transportation Credit Partial Final Decision on the southeastern Orders in 1997, reopened from above Docket Number AO-388-A9, et al, the Secretary states in the Conclusion section of the Decision that "the record indicates that disorderly marketing conditions existed because of the significantly different costs that were incurred by handlers who provide the additional service versus those who do not."

The continued burdening of certain segments of the producer population with these costs of supplying milk to the southeastern Orders' handlers will exacerbate unequal returns for producers' milk, replicating the disorderly marketing conditions which existed when Transportation Credits were first installed in the southeastern Orders.

Just as the costs of procuring supplemental supplies does not fall proportionately on all producers, handlers too can see differing costs of supplemental milk. The orderly assessment

of costs on Class I milk through the regulated Class I price and Transportation Credit structure will alleviate the disorderly marketing which comes from handlers similarly situated not paying the same cost for milk.

The elements of disorderly marketing that are currently present in the southeast, inequitable returns to producers, unequal costs to handlers, and insufficient economic incentives for the procurement of sufficient quantities of milk, will be ameliorated by the DCMA package of proposals.

Over order prices can be, at any point in time, very temporary. Many non-economic pressures can impact the level of, and even the very existence of, over order prices in a region or marketing area. Reliance on over order prices to reimburse marketers of milk for such a major portion of the substantial costs of procuring and maintaining a sufficient quantity of milk for the southeast as is currently the case leaves something to be desired. Further, establishment of a representative regulated price surface offers handlers assurance that the portion of their cost of milk represented by the regulated milk values is equitably and universally applied.

Order Language

Included in Proposals number 1, 2 and 3 in the Notice of Hearing is Order language designed to effectuate the proposed amendments to the three Orders. Scattered throughout this testimony are mentions of the proposed revised Order language in reference to the particular

points of the package of proposals. For clarity, we will now summarize all of the proposed changes in Order language by pertinent section.

In sections 1005.13(d)(1) and (d)(2) and 1007.13(d)(1) and (d)(2) the provisions are amended to require a producer to deliver one day's production each month to a pool plant for that producer's milk to be eligible for pooling by diversion to a nonpool plant. In sections 1005.13(d)(3) and (d)(4) and 1007.13(d)(3) and (d)(4) the monthly diversion limit percentages are set at 25% of pool plant producer milk deliveries in January, February, July, August, September, October and November, and at 35% of pool plant producer milk deliveries in the remaining months.

In sections 1005.50(b), 1006.50(b), and 1007.50(b), the calculation of the Class I skim milk price is specified to be the sum of the monthly Class I skim milk "mover" from section 1000.50(q)(1) or (q)(2), plus the Class I differential from section 1000.52, plus the Class I price adjustment from section 1005.51(b), 1006.51(b), or 1007.51(b) as the case may be. In sections 1005.50(c), 1006.50(c), and 1007.50(c), the calculation of the Class I butterfat price is specified to be the sum of the monthly Class I butterfat "mover" from section 1000.50(q)(3), plus the Class I differential from section 1000.52 divided by 100, plus the Class I price adjustment divided by 100 from section 1005.51(b), 1006.51(b), or 1007.51(b), as the case may be.

In sections 1005.51, 1006.51, and 1007.51 the current language in each Order is renumbered as subparagraph (a), and a conforming change is made to recognize the new language in sections 1005.50, 1006.50 and 1007.50. A new subsection 1005.51(b), 1006.51(b),

1007.51(b) is added to each Order, specifying the newly created "Class I price adjustment" for each county or parish located within the three marketing areas.

In sections 1005.81 and 1007.81, conforming changes are made to require the Market Administrator to consider the historical and expected payouts from the Transportation Credit Balancing Funds in the months of July through February when setting the Transportation Credit Balancing Fund's effective assessment rate. In sections 1005.82(a)(1) and 1007.82(a)(1), the months during which Transportation Credit Balancing Fund payments are to be made is specified as July through February, and June if requested. In sections 1005.82(c)(1) and 1007.82(c)(1), language is deleted so as to provide that Transportation Credit Balancing Fund payments will be made on full loads of milk, rather than just the calculated Class I portion. In sections 1005.82(c)(2) and 1007.82(c)(2), language is provided to revise the definition of which producers are supplemental, and therefore their milk eligible for Transportation Credit Balancing Fund payments. In sections 1005.82(d)(2)(iii) and 1007.82(d)(2)(iii), as well as sections 1005.82(d)(3)(v) and 1007.82(d)(3)(v), conforming changes are made such that the origin point Class I price and the destination point Class I price are compared when computing the Transportation Credit Balancing Fund payments. Certain changes in the section 1005.82 and 1007.82 language required renumbering various subsections.

Need For Emergency Action

The notice of hearing in this proceeding invited comments on emergency conditions present in the marketing areas and seeks comments on considering emergency action and the omission of a recommended decision under the rules of practice and procedure.

The costs of hauling supplemental milk into the southeast region are real, are substantial, and are increasing, as has been fully demonstrated. Milk production is declining and population is increasing in the region. The sufficient quantity of milk for the southeast region is threatened by regulated price incentives which are insufficient to encourage milk to move into the area. Slowing growth rates in milk production nationally may make obtaining necessary supplies to meet the fluid milk product demand in the southeast especially difficult during the fall of 2007.

Proponents have demonstrated the insufficiency of current regulated price levels to send the economic signals necessary to attract a sufficient quantity of milk to the marketing areas. Substantial losses will be incurred in supplying milk to the region if the regulated prices are not adjusted to offer assurances that costs of supplying the marketing areas are covered, or worse, the region may go short of milk if marketers have no way of recovering the supply costs.

As has been stated in previous Proceedings and reaffirmed by the Secretary, the costs defined in these proposals are currently not borne equitably by all producers, exacerbating the problem. Delay in implementing these amendments only worsens the inequities present. Since these costs fall disproportionately on one segment of the producer population, the cost per hundredweight borne by those producers exceeds the cost per hundredweight for the Orders as a whole. Quick correction of this situation will preserve the orderly marketing of

milk in the region by safeguarding regulated cost recovery by those marketers of milk actually incurring the costs of maintaining the sufficient quantity of milk for the region.

The costs associated with delivering milk in and to the Appalachian, Florida and Southeast marketing areas are considerable and are ongoing. Failure to address these issues through the Federal Order program puts in jeopardy the sufficient quantity of milk for the southeast. Delay will not lessen the costs, will not see a reversal in cost trends, nor see an equitable reapportioning of the costs onto all parties in the marketing areas.

The current process for payment of the costs of milk delivery in the Appalachian, Florida and Southeastern Orders, as has been demonstrated, does not offer marketers of milk sufficient reassurance that a significant portion of costs of supplying milk will be covered. If the provisions of the Orders are left unchanged, the economics in the delivery of milk will, likely sooner than later, make such deliveries unworkable, and the supply of milk in the marketing areas will be threatened. Only quick action on the part of the Secretary will forestall such a lamentable occurrence.

The milk marketing dynamics in the southeast continue to worsen in regards to available supplies to meet the needs of the marketing areas. Exhibit 21, page R provides the 1980 to 2006 annual milk production history for the 12 southeastern states. Milk production has been dropping, on average about 2 percent per year in the southeast, but decreased 3.84 percent from 2005 to 2006. Exhibit 21, page S provides southeastern state milk production for the first quarter of 2007 versus the first quarter of 2006, and milk production in the 12

southeastern states declined a frightening 4.18 percent. Clearly, the problem of supplying milk to the southeast is worsening, and worsening at an increasing rate.

Exhibit 9, page 7, and Exhibit 18, page 3, introduced by the Market Administrators for the Appalachian and Southeast Orders show the volume of milk for which a Transportation Credit was claimed in each year of 2000 to 2006. In Order 5, Transportation Credits were requested on 489.1 million pounds of milk in 2006, versus 305.9 million pounds in 2000, an increase of 60 percent. In Order 7, Transportation Credits were requested on 819.5 million pounds of milk in 2006, versus 373.6 million pounds in 2000, an increase of 119 percent.

As we sit here today, USDA statistics show national milk production growth is also slowing, potentially leaving even less milk in reserve supply areas available for the southeast. The existence of Emergency conditions is beyond argument.

Some of the provisions as proposed to be amended here are pursuant to the marketwide service payment provisions of the Agricultural Marketing Agreement Act, and therefore deserve quick action.

As previously mentioned, DCMA recognizes that a national review of the Class I pricing structure under Federal Orders may be undertaken in the not too distant future. The question may be asked as to why DCMA has made this proposal now, versus waiting and participating in the national review of Class I prices at a later date. There are several reasons for proceeding with this request now instead of waiting. First, a national review of Class I pricing

may or may not yield changes in Orders 5, 6 and 7 other than what is proposed by DCMA today. Second, the milk supply and demand condition in the southeast is at a critical juncture, and must be addressed without delay. Third, proceeding with the package of proposals described here today certainly does not preclude DCMA from participating in the national review of Class I prices, at such time as that review is undertaken. And fourth, the cost of moving milk into the southeast is increasing almost daily, and the price incentives and cost reimbursement processes proposed by DCMA cannot wait on, nor rely on, the possibility of future changes from a national Class I price surface review.

For the above reasons, the Secretary should omit the issuance of a Recommended Decision, and follow the practice used in several other recent Proceedings and issue a Tentative Final Decision with an Interim Order, and allowing the opportunity for comments before a Final Decision and Order are issued.

Testimony Regarding Proposals 4, 5, 6 and 7

The Notice of Hearing included three proposals made by the Market Administrators for the Appalachian, Southeast and Florida Orders, listed as Proposals 4, 5 and 6, respectively. These proposals would raise the maximum assessment for Order administration under each of the three Orders to eight cents per hundredweight of producer milk, certain receipts of other source milk, and certain Class I dispositions in the marketing area by partially regulated distributing plants. DCMA is not opposed to these proposals. DCMA understands that there may be conforming changes to the Orders as required by any amendments adopted as a result of this Proceeding, and therefore is not opposed to Proposal number 7.

Summary

The proponents again wish to thank the Secretary for the opportunity to propose these emergency amendments to the Appalachian, Florida and Southeast Federal Milk Marketing Orders, and look forward to a quick decision installing the needed changes to the Orders.

This concludes my prepared statement.