

**Testimony of
Paul G. Christ
On Behalf of
The Dean Foods Company**

**Hearing to consider amendments to the Upper Midwest
Federal Milk Marketing Order
Docket No. AO-361-A39; DA-04-01
August 16 et seq. 2004**

My name is Paul G. Christ. I reside at 245 Indian Trail, So., Afton, Minnesota 55001. I have a long background in working with Federal milk orders. From 1961 to early 1974 I worked for the Dairy Division of the Agricultural Marketing Service of U.S.D.A., both in the Washington office, and in market administrators' offices in the field. Between 1974 and 2000 I worked for Land O'Lakes, Inc., and was responsible for marketing Land O'Lakes member milk under several Federal milk orders, and when necessary, for proposing changes to those orders. Thus, I have experience both inside and outside the government in the operation and effects of individual milk orders and of the entire Federal milk order system.

Proposal Number 3

I appear here as an advocate for Dean Foods Company in support of proposal number 3. I will attempt to explain how proposal number three would work, and how it would improve the supply of milk available for fluid use, and the well-being of producers whose milk is continuously pooled.

As was stated by Evan Kinser in his earlier testimony, Dean Foods Company is interested in improving two aspects of the Upper Midwest order. The first is to increase the availability of milk for Class I use, and the second is to increase the flow of pool funds to those producers who represent a reliable supply of milk for fluid use.

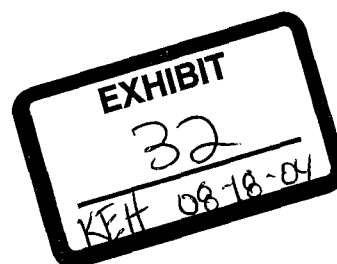
Proposal number 3 is designed to accomplish those goals.

First, I will attempt to explain how proposal number 3 would work. It would add a new subparagraph (b)(5) to the producer definition, section 1030.12. It reads as follows:

"Section 1030.12 Producer

* * * * *

(b) * * *



*(5) For any month, any dairy farmer whose milk is received at a pool plant or by a cooperative association handler described in Section 1000.9(c) if the pool plant operator or the cooperative association caused milk from the same farm to be delivered to any plant as other than as producer milk, as defined under the order in this part or any other Federal milk order, during the same month or any of the preceding 11 months, unless the equivalent of at least ten days' milk production has been physically received otherwise as producer milk at a pool **distributing** plant during the month."*

The highlighted word "distributing" plant in the last sentence of the proposal represents a modification of the published proposal. Mr. Evan Kinser offered this modification in his testimony, and my testimony will relate to the modified proposal.

The new subparagraph would exclude from the pool the milk of any dairy farmer whose milk was not continuously pooled under one or another Federal milk order during the last 12 months. The sole exception from this exclusion would be the case where the dairy farmer temporarily lost Grade A status, and whose production facility was reinstated as Grade A within 21 days. The idea behind this exclusion is to discourage milk that was depooled for economic reasons from easily becoming repooled when it is economically favorable to do so.

Dairy farmers for whom their milk is pooled when benefits exist, and is not pooled when costs exist, create a burden on producers whose milk is continuously pooled. When the producer price differential is positive there is an incentive to pool all milk used in Class III. This has the effect of averaging down the producer price differential, reducing returns to continuously pooled producers. On the other hand, when the producer price differential is negative, there is an incentive to depool all milk used in Class III. This also has the effect of averaging down the producer price differential, resulting, again, in reduced returns to continuously pooled producers. The losers in this process are the producers whose milk is kept in the pool and continues to be available to serve the needs of the fluid market.

Under proposal number 3, milk that was depooled within the last 12 months could again become repooled, if the responsible handler demonstrates that it is, in fact, available for fluid use. This is accomplished by delivering 10 days production from that dairy farmer's facility to a pool distributing plant. This demonstration would insure that pool participation would be open to any dairy farmer for whom it is technically and economically feasible to supply milk for fluid use. In effect, the proposal would not prevent depooling. However, it would make it more difficult to return such a dairy farmer's milk to the pool after it is once depooled.

This demonstration of competence to supply milk for fluid use would continue for 12 months before such formerly depooled milk could be pooled under the more flexible provisions of the order that apply to continuously pooled milk.

This proposed change would not be economically burdensome if the milk were favorably located relative to a distributing plant. However, it would make it expensive for a distant or unfavorably located dairy farmer to again become a producer and participant in the pool. It would also insure the milk for which it is not technically or economically feasible to serve the fluid market would not reenter the pool.

Dairy farmers whose milk is pooled continuously under the Upper Midwest Federal order would not be affected by this proposal. These dairy farmers shared in both the costs and the benefits of pool participation on a continuous basis.

Also, dairy farmers whose milk is pooled continuously under any other Federal milk order(s) during the preceding year would not be affected by this proposal. They could enter the Federal order 30 pool under the same flexible provisions as apply to Federal order 30 producers who were not depooled within the last year. In effect, these "other-order" producers were continuous participants in one or another Federal order pool, sharing both the costs and benefits of such participation on a continuous basis.

So, proposal number 3 would have three desirable effects:

1. Some Class III milk would stay in the pool when the producer price differential was negative, in order to avoid the extra cost of returning to the pool. This would increase the producer price differential (making it less negative) for all producers, especially those whose milk is delivered to distributing plants.
2. Some Class III milk that is depooled would never return to the pool because it is no longer technically or economically feasible to do so. This would have the effect of increasing the producer price differential whenever it is positive. Those producers whose milk is delivered to distributing plants would benefit.
3. Some Class III milk that is depooled would return to the pool, but only through regular, significant deliveries to distributing plants. This would increase the supply of milk ready and willing to serve the needs of the fluid market.

For the above reasons Dean Foods Company urges the Secretary to adopt proposal number 3.

Proposal Number 4

Dean Foods Company also offers proposal number 4 for consideration by the Secretary. It is offered as a weaker, less desirable alternative to proposal number 3, in the event that proposal number 3 is rejected. Proposal number 4 reads as follows:

“Section 1030.12 Producer

* * * * *

(b) * * *

- (5) *For any month of **February** through **June**, any dairy farmer whose milk is received at a pool plant or by a cooperative association handler described in Section 1000.9(c) if the pool plant operator of the cooperative association caused milk from the same farm to be delivered to any plant as other than producer milk, as defined under the order in this part or any other Federal milk order, during the same month, any of the 3 preceding months, or during any of the preceding months of July through **January**, unless the equivalent of at least ten days' milk production has been physically received otherwise as producer milk at a pool **distributing** plant during the month; and*
- (6) *For any month of July through **January**, any dairy farmer whose milk is received at a pool plant or by a cooperative association handler described in Section 1000.9(c) if the pool plant operator or the cooperative association caused milk from the same farm to be delivered to any plant as other than producer milk, as defined under the order in this part or any other Federal milk order, during the same or the preceding month, unless the equivalent of at least ten days' milk production has been physically received otherwise as producer milk at a pool **distributing** plant during the month.”*

We recommend modification of proposal number 4 in the same fashion as the modification to proposal number 3. The modification would change the flush shipping season from December through June to **February through June**. It would also change the short shipping season from July through November to **July through January**. Dean Foods contends that this change will provide greater assurance that more milk will stay in the pool during all the months when fluid demand is greatest relative to supply.

Finally, the modification would add the word “**distributing**” plant to the last sentence of subparagraphs (5) and (6). This would insure that deliveries for requalifying a dairy farmer's milk for pooling would be accomplished only by demonstrating that the milk is technically and economically available to the fluid market.

The difference between proposal number 3 and proposal number 4 is that, in the event that a dairy farmer's milk is depooled, the number of months for which 10 days' milk production would have to be delivered to a pool distributing plant would be fewer.

In the first case, under subparagraph (5), if milk is depooled during the period of February through June, only four months of such deliveries would be required, compared to 12 months under proposal number 3.

In the second case, also under subparagraph (5), if milk is depooled in any month of July through January, then such deliveries would be required in each month of February through June. Dean Foods is more interested in discouraging depooling in the short season than during the rest of the year.

In the third case, under subparagraph (6), if milk is depooled during the period of July through January, only two months of such deliveries would be required, compared to 12 months under proposal number 3.

Proposal number 4 would have the same general effects and benefits as proposal number 3, except that the benefits of depooling would be greater, and the costs of repooling would be smaller. Thus, the beneficial effects on continuously pooled producers would be smaller, and there would be a less abundant supply of milk available for fluid use.

Therefore, we again recommend the adoption of proposal number 3. But, if for whatever reason the Secretary chooses not to adopt proposal number 3, then we recommend the adoption of proposal number 4.

Proposal Number 5

Proposal number 5 is offered by Dean Foods Company as a less desirable alternative to both proposals number 3 and 4. It offers a different type of mechanism for limiting the amount of depooled milk that can be repooled in any given month. It is similar to proposal number 2, but puts a tighter limit on how much milk can be pooled from month to month under the order.

Proposal number 5 reads as follows:

“Section 1031.13 Producer Milk

* * * * *

(f) The quantity of milk reported by a handler pursuant to Section 1030.30(a)(1) and/or Section 1030(c)(1) for July through November may not exceed 115 percent of the producer milk receipts pooled by the handler during the prior month. Milk diverted to nonpool plants reported in excess of this limit shall be removed from the pool by the market administrator. Milk received at pool plants, other than pool distributing plants, shall be classified pursuant to Section 1000.44(a)(3)(v) and Section 1000.44(b)(3)(v). The handler must designate, by producer pickup, which milk is to be removed from the pool. If the handler fails to provide this information, the market administrator will make the determination. The following provisions apply:

(1) Milk shipped to and physically received at pool distributing plants shall not be subject to the 115 percent limitation;

- (2) *Producer milk qualified pursuant to Section _____ .13 of any other Federal Order and continuously pooled in any Federal Order for the previous six months shall not be included in the computation of the 115 percent limitation.*
- (3) *The market administrator may waive the 115 percent limitation utilizing:*
 - (i) *For a new handler on the order, subject to the provisions of Section 1030.13(f)(3), or*
 - (ii) *For an existing handler with significantly changed milk supply conditions due to unusual circumstances;*
- (4) *The market administrator may increase or decrease the applicable limitation for a month consistent with the procedures in Section 1030.7(g); and*
- (5) *A bloc of milk may be considered ineligible for pooling if the market administrator determines that handlers altered the reporting of such milk for the purpose of evading the provisions of this paragraph.”*

The mechanism for discouraging the depooling of milk under proposal number 5 is to restrict the amount of additional milk that can be pooled during July through November by a handler from one month to the next. That means that the volume of milk that is continuously pooled under Federal order 30 or any other Federal order can be pooled without hinderance or restriction. However, milk that has been depooled under this or any other order can only be gradually repooled during the short season. This means that most of the milk for which the cost of pooling is avoided during periods of negative producer price differentials cannot immediately enjoy the benefits of pooling when the producer price differential is positive.

This reduces the benefits of depooling and increases the costs of repooling during the short season (July through November). The effect is a modest discouragement of depooling.

If depooling is discouraged to any degree, producers whose milk stays in the pool will enjoy a higher (less negative) producer price differential during months when it is negative.

However, proposal number 5 provides for instant repooling of any milk that is delivered directly to a pool distributing plant. This has the desirable effect of increasing the supply of milk that is readily available to the fluid market, following a period of depooling.

It also does not restrict repooling during any month of December through June.

Proposal number 5 increases the costs of depooling with the greater percentage of a handler's milk that is depooled. The following table 1 illustrates the time it takes to repool all the milk of a handler if he depools between 10 and 90 percent of the milk under his control:

Table 1. Effect of the percentage of milk depooled on the time it takes to repool all the milk of a handler at a rate of 115 percent per month, starting with July

<u>Month</u>	<u>Percentage of milk pooled</u>								
	10	20	30	40	50	60	70	80	90
0									
1	11.5	23.0	34.5	46.0	57.5	69.0	80.5	92.0	100
2	13.2	26.4	39.7	52.9	66.1	79.4	92.6	100	
3	15.2	30.4	45.6	60.8	76.0	91.3	100		
4	17.5	35.0	52.5	70.0	87.5	100			
5	20.1	40.2	60.3	80.5	100				
6	100	100	100	100					

The point of table 1 is that the greater the proportion of milk depooled, the longer the time needed to requalify the depooled milk. This is a desirable feature of proposal number 5. Those handlers (and producers) who capture the greatest benefit from depooling, also incur the greatest loss of benefit from attempting to regain pool status.

Proposal Number 6

Proposal number 6 is offered by Dean Foods to supplement proposal number 3. It is intended to insure that a greater amount of producer milk is more readily available for transfer to a pool distributing plant for fluid use. It reads as follows:

"Section 1030.13 Producer Milk

* * * * *

(d) * * *

- (1) *Milk of a dairy farmer shall not be eligible for diversion until milk of such dairy farmer has been physically received as producer milk at a pool plant and the dairy farmer has continuously retained producer status since that time. If a dairy farmer loses producer status under the order in this part (except as a result of a temporary loss of Grade A approval not to exceed 21 days in a calendar year), the dairy farmer's milk shall not be eligible for diversion until milk of the dairy farmer has been physically received as producer milk at a pool plant;*
- (2) *The equivalent of at least four days' milk production is caused by the handler to be physically received at a pool plant in each of the months of July through November;*
- (3) *The equivalent of at least four days' milk production is caused by the handler to be physically received at a pool plant in each of the months of December through June if the requirement of paragraph (d)(2) of this section (1030.13) in each of the prior months of July through November is not met, except in the case of a dairy farmer who marketed no Grade A milk during each of the prior months of July through November."*

We are also offering minor modifications to proposal number 6, as explained by Evan Kinser. The required delivery of a producer's milk to a pool plant was changed from two days' production to four days' production.

In addition, we are abandoning the proposed change to subparagraph 1030.13 (d) (4). We believe that if there is a tighter requirement for producer milk to be received in a pool plant, there is less need to restrict the amount of milk that can be diverted.

Proposal number 6 does nothing more than insure that more producer milk is actively engaged in the process of serving the fluid market. This process starts with the production of Grade A milk, and then continues the next step of being received in a Grade A pool plant facility. If producer milk is diverted to a nonpool plant, then it is out of the Grade A marketing stream and is no longer available to the fluid market. Increasing the "touch-base" requirement insures that more milk stays in that Grade A marketing stream one more step than otherwise would be the case. The effect is to make more milk physically available for the fluid market.

Proposal number 6 would also insure that pool plant operators keep their Grade A facilities operating at a higher level of output than would be the case if more milk were diverted. In effect, more Grade A milk would be available for fluid use at all times, and pool plant operators would routinely engage in Grade A operations, thereby maintaining greater standby capacity for supplying the fluid market.

Proposal Number 7

Proposal number 7 is offered by the market administrator to insure that he can collect adequate funds through the administrative assessment to operate his office and effectively enforce the order. He does, indeed, need to do this. However, a large part of the funding problem arises from massive depooling of milk. When milk is depooled because of a negative producer price differential, no administrative assessment is paid on that milk, and the market administrator may find himself short of funds. In that event, he seeks to increase the administrative assessment on the (disadvantaged) milk that remains in the pool. This increases the financial burden on continuously pooled milk.

A better solution to the problem is to discourage or eliminate the practice of depooling. We believe that proposal number 3, in particular, would accomplish that objective, and should be adopted. Therefore, we recommend that proposal number 3 be adopted to increase the amount and the predictability of administrative revenues for the enforcement of the order by the market administrator.

We nonetheless sympathize with the market administrator who is unable to anticipate the financial risk to his operations, when some of those who receive the services and benefits he provides do not pay for them. For example, calculations made by the market administrator provide the foundation for the decision to depool milk, and depooled milk does not pay an administrative assessment. This is a bizarre state of affairs.

If an increase in the administrative assessment is to be considered, the market administrator should insure that such an increase falls on nearly all market participants. This can be done by suspending or revising downward the assessment rate during months when milk is depooled. It can then be increased when the depooled milk returns to the pool.

Of course, if proposal 3 is adopted, this risk should be reduced substantially, and maybe eliminated.

Proposal Number 8

We offer the following proposal as a conforming change to reinforce proposal number 6:

"Section 1030.7 Pool Plant

** * * * **

*(d) * * **

(2) The operator of a supply plant(s) may not include as qualifying shipments under this paragraph milk diverted directly from producer's farms pursuant to Section 1000.9(c) to plants described in paragraphs (a), (b) and (e) of this section."

This proposed change would have two desirable effects. The first would be to discourage the practice of diverting nearby milk to distributing plant in order to qualify distant milk for pooling. The distant milk may not be practically available for fluid use, but nevertheless gets pooled because the nearby diversions to a distributing plant. We prefer to insure that all milk in the pool participate to a greater degree in the Grade A marketing stream. By prohibiting the use of diversions to make qualifying shipments, some of the milk that otherwise would be qualified for pooling with virtually no performance, will now have to be qualified by physical shipments from a pool supply plant.

This improvement would also insure that more activity will take place in the Grade A facilities of pool supply plants, thereby increasing the competence of operators of such plants to serve the fluid market.

This concludes my testimony.