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June 17, 2011

VIA EMAIL and FIRST CLASS MAIL

Ms. Dana Coale, Deputy Administrator
USDA-AMS-Dairy Programs
1400 Independence Avenue, SW
Washington, D.C. 20250-0225

Re: Request for hearing upon amendments to
Federal Milk Order 33, 7 C.F.R. 1033

Dear Ms. Coale:

Foremost Farms USA Cooperative, Inc., NFO Inc., and Dairy Farmers of America, Inc., hereafter, "The Cooperatives" – all of which supply milk to processors and pool the milk of producer members on Order 33 are requesting a hearing to consider changes in the Order 33 regulations dealing with the requirements for a pool distributing plant. The Cooperatives pool member milk on Order 33 and service class I sales in the Order. We estimate that approximately ninety percent (90%) of the Cooperatives' members in Order 33, and also of the nearly 7,000 producers pooled on Order 33 are small businesses. The disorderly marketing conditions supporting this hearing request are harmful to these small businesses on whose behalf this request is made.

Recent Changes in Market Conditions

Historical records indicate Superior Dairy¹ of Canton, Ohio, has been an Order 33 (and before that its predecessor Order 36) pool distributing plant for a long period of time. In recent years, Order 33 annual statistical summaries show it as a pool distributing plant for every month in 2008, 2009, and up to March of 2010. The Federal Order Reform Final Decision published in March 1999 lists a table of plants and their regulatory status, listing Superior Dairy as an Order 36 pool distributing plant in October 1997 which was expected to maintain pool plant status after the Reform Decision was implemented in 2000. At the time of the 2005 hearing (referenced in footnote 1), and according to 2004 data included in that hearing record, Superior Dairy did not have any sales in either Order 1 or Order 5 (the adjoining Orders). In April 2010, however, Superior became an Order 1 pool distributing plant and over the following months Superior has expanded its business footprint with sales now reported into seven different Orders. Most recently, as evidenced by data published by the Order 1 Market Administrator, Superior Dairy, Canton, Ohio, has become a partially regulated pool distributing plant effective with March 2011

¹ Superior Dairy, as noted on its Facebook page, [<http://www.facebook.com/pages/Superior-Dairy/151379038252331#!/pages/Superior-Dairy/151379038252331?sk=info>] manufactures a variety of dairy products including milk, half & half, cottage cheese, sour cream, chip dip, bulk ice cream, ice cream cakes and distributes them to grocery stores and other businesses such as Fisher's Foods, COSTCO, Baskin Robbins, B.J.'s and Wal Mart. Joe Soehnlén, of Superior Dairy, testified in the March 2005 Federal Order hearing dealing with performance standards and depooling issues, that Superior Dairy is a family-owned company with 235 to 255 employees, started by his grandfather in 1922. In 2005 they had 180 independent producers representing 75% of their volume, indicating a monthly volume at that time in excess of 30 million pounds, assuming average size producers.

deliveries, effectively depooling the Canton plant and milk supply². This change in status is a cause of disorderly marketing conditions.

Recently Superior Dairy acquired a previously closed, small processing property at Wauseon, Ohio. This plant appeared for the first time on the March 2011 list of pool distributing plants as published by Federal Order 1. In the same month, the Superior Dairy Canton, Ohio, plant disappeared from any Market Administrator listing of pool distributing plants but appeared in some Market Administrator reports as a partially regulated distributing plant. It appears that these events are part of an artifice designed to allow Superior Dairy - Canton to avoid full regulation by falling below the 25% route disposition requirement in any marketing area. The following description is, we believe, the explanation of how Superior Dairy's Canton plant fails the in-area distribution standard. The recently purchased Wauseon, Ohio plant is very small with a small refrigerated storage area and limited milk receiving facilities. The plant's receiving bay is too small to receive an over-the-road tanker of raw milk. For Order regulation purposes, any milk sales of substantial volume associated with the Wauseon, Ohio, plant can only come from the physical movement of packaged product, transferred into and then out of the Wauseon

² In the 2005 hearing, Superior testified in support of order amendments to limit the ability of handlers to depool milk: "MR. SOEHNLEN: [T]he major issue that has caused producers shipping to our company to call in and talk things -- talk the pricing over with me is the issue of depooling and its effects on their milk check. I have discussed this issue with many of our producers who are shipping to us and I believe that the view that I'm presenting fairly represents their interests and their wishes. So it is with this in mind that I strongly support Proposal Number 4. [This proposal seeks to establish a dairy farmer for other markets provision that would encourage a year-round pooling commitment and specify conditions for milk that was depooled to be repooled.] And I certainly would include the changes presented by Mr. Christ. I would also like to see changes similar or equivalent applied to the surrounding Orders. It is my experience that when you change one Order and leave pooling opportunities open in other Orders, it's very, very difficult to regulate human ingenuity. It just about doesn't happen."

plant. This product movement thus allows the product's ultimate distribution to be reported on the Wauseon handler report. We believe that Superior Dairy Canton is maneuvering enough Order 1 sales through the Wauseon plant and onto the Wauseon handler report to qualify Wauseon as an Order 1 pool distributing plant. This removes those Order 1 sales from the Canton plant, thereby disqualifying it from full regulation in Order 1 -- or any other Order -- by making sure no individual Order receives 25% of the Superior Dairy -- Canton's route disposition. Establishing and maintaining the current status of these plants would appear to be a challenging task requiring sales in multiple Orders and an adroit management of the milk orders of one's customers. However, we know that Superior Dairy (both locations) had sales in Orders 1, 5, 6, 7, 32 and 33 in March and in the same marketing orders plus Order 30 for April. Additionally, because of geographic proximity to non-federally regulated areas in central Pennsylvania and western New York, we expect the plant may also have sales in those unregulated areas. Consequently, by virtue of its broad geographic distribution, Superior has quite a few geographic locations to work with in its effort to avoid pool plant status.

Distributing Plant Pooling Principles in the Federal Order System

Several statements in the 1999 Final Decision for Federal Order reform summarize the Order system's views and philosophy regarding regulating pool distributing plants. The overriding theme is that similarly situated plants processing fluid milk products should be subject to the same Order regulations.

Pool Plant

The *pool plant* definition of each order describes those plants which receive milk that shares in the marketwide pool. It provides standards to identify those plants engaged in serving the fluid needs of the marketing area. Pool plants serve the fluid market to

a degree that warrants their producers sharing in the added value that derives from the classified pricing of milk. While the pool plant definition in every consolidated order provides for a set of common principles, the standards applicable to pool plants differ among the consolidated orders, reflecting the fact that marketing conditions vary across the country. The goal in drafting pooling standards is to ensure both an adequate supply of milk for fluid use and orderly marketing by allowing all milk in a marketing area the opportunity to serve the fluid market and thereby share in the pool.

There are 2 performance standards applicable to *pool distributing plants* in the consolidated orders. The first standard, which varies among orders, requires a distributing plant to have a minimum Class I utilization. Since *route disposition* includes only Class I milk, the specific standard is a measure of a distributing plant's route disposition as a percent of its total receipts of fluid milk products. This standard is generally directly related to the market's Class I utilization.

. . .
Once it is determined that a distributing plant is sufficiently associated with the fluid market to share in the pool, a second standard determines if the plant is sufficiently associated with a particular market to share in the pool applicable to that market. The "in-area" standard adopted for the consolidated orders requires that a distributing plant have 25 percent of its route disposition within a marketing area before it can be fully regulated by the order covering that marketing area.

The 15 percent in-area standard in the proposed rule has been changed to 25 percent for all orders to reflect the larger, merged marketing areas that are adopted. This change should not affect the regulatory status of any current distributing plant.

64 Fed. Reg. at 16132 (April 2, 1999)

The language in the Federal Order reform decisions which created a uniform pool distributing plant definition and the 25% level clearly intended to keep all plants regulated and not to deregulate existing pool plants. The reform decisions, by pointing out that the pre-reform qualifying percentage was generally no more than 15%, establish the historical finding of USDA

that an association at that level with a pool necessitated full pooling and full regulation. At the time and based on market conditions in the Orders, the reform decision concluded that establishing the 25% in-area route distribution standard would not create any problems because the Orders were bigger and would regulate all existing handlers in the same manner as they had been regulated. Now, some 12 years later, we see a need to change the standard.

The Decision further explained just how important maintaining consistent and constant pooling standards within an order marketing area is by providing special regulations for the unique set of plants that distribute ultra-pasteurized or aseptically-processed fluid milk products.

A special pool distributing plant provision (i.e., Section .7(b) of the consolidated orders) has been adopted for distributing plants that distribute ultra-pasteurized or aseptically-processed fluid milk products. Such plants must be located in the marketing area and must process a certain percentage of their milk receipts into ultra-pasteurized or aseptically-processed fluid milk products during the month.

...

Plants specializing in ultra-pasteurized or aseptically-processed fluid milk products tend to have erratic processing and distribution patterns reflecting the long-life nature of the product they process. In some months, they may process fluid milk products but have little or no route disposition because the products are stored in inventory. In addition, these plants often have much wider distribution patterns than do other distributing plants and, under current orders, frequently shift regulation from one order to another. This shifting regulation is disruptive to the producers and/or cooperatives supplying these plants and is an additional regulatory burden to the plant operator. ...

64 Fed. Reg. at 16132 (April 2, 1999).

The Federal Order system has reacted consistently over the years by updating regulations for distributing plants where new sales patterns or practices lead to circumstances where competing

plants are not similarly regulated. For instance, a 1988 decision, Milk in the Ohio Valley, and Louisville – Lexington – Evansville Marketing Area – [Docket Nos. AO-165-A57 and AO-123-A58], supports the historical precedent in the Orders for similarly situated plants to have a common regulatory rules base.

“...[This Decision] changes the current regulatory status of a pool distributing plant that is located in the Louisville – Lexington - Evansville marketing area but is regulated by the Ohio Valley order because a greater portion of its fluid milk products distribution is in the latter order’s marketing area. It would regulate such plant under the Louisville – Lexington – Evansville order.” Proposed Rule, signed January 7, 1988.

This Decision altered the pool distributing plant standards for a single plant emphasizing the desire of “orderliness” and thus correcting a disorderly marketing condition which caused similarly situated plants within the same competitive area to have different costs of raw milk. This proceeding noted that provisions regulating processing plants serving retail stores over a wide geographic area may need to be altered in order to assure that all handlers competing for milk procurement and sales in an order area are subject to the same price as their competition.

In the Federal Order reform distributing plant language, at least two changes in language were implemented uniformly across the system to maintain uniform regulated status for all similarly situated distributing plants. In one case, the language establishing the denominator for the minimum Class I percentage at a pool distributing plant was clarified to use only volumes physically received at the plant. This eliminated the possibility for a plant to avoid pool plant status by associating volumes of diverted non-Class I milk with the plant, thereby becoming partially regulated. In another case, the treatment of packaged transfers was changed to prevent

plants from becoming partially regulated via certain transfer transactions³.

In all these cases, the Department acted to close loopholes in language which allowed plants which were intended to be fully regulated to become partially regulated, a disorderly marketing condition.

Issues in the Mideast Order

Superior Dairy's shift to becoming a partially regulated plant causes disorderly marketing conditions to occur in the Mideast Federal Milk Marketing Order. Producer price relationships based on Order minimum values are now in question and handler competitive equity has been jeopardized.

Producer pricing is impacted by the Order's payment terms for partially regulated distributing plants. It has been our experience that while Part 1000.76 (a), (b), (c) and (d) define the payment obligations for a partially regulated handler, handlers most often opt for section (b) which is usually the lowest cost option. That option, in general, states that if a plant can demonstrate to the Market Administrator that it has paid producers in aggregate the minimum class values, it will not have any pool obligation. The test takes into account all payments made to the producer including any premiums paid. The plant is thus able to operate as if in an

³ The Final Decision stated: "However, for the single purpose of qualifying a plant as a pool distributing plant, the pool distributing plant definition has been modified to treat transfers of packaged fluid milk products to other plants as if they were route disposition of the transferring plant for the purpose of identifying the plant's association with the fluid market. **This is necessary to preclude a plant from becoming partially regulated** if the plant shipped significant quantities of packaged fluid milk products to another distributing plant." 64 Fed. Reg. at 16132 (April 2, 1999) (Emphasis supplied)

individual handler pool, avoiding payments to the marketwide pool. This can be a substantial value. The dollars otherwise payable to the pool can then be used in a competitive fashion in procuring a milk supply in competition with pool handlers. Furthermore, the provision (b) test outlined above does not require that all producers supplying milk to the partially regulated handler be paid uniformly, so adjoining producers delivering milk to similarly situated plants, or in this case the same plant, may receive widely different prices. Ironically, in the 2004 hearing referenced earlier, Superior Dairy was supporting changes in Order 33 regulations that would eliminate or greatly restrict the practice of depooling. A key reason why Superior opposed this practice was the resulting differences in producer pay prices when some handlers were able to take advantage of depooling and others could not. Clearly this is a very similar situation and warrants a change in Order regulations to eliminate the practice.

Competitive equity among pool distributing plants is also jeopardized by this situation. To estimate the magnitude of this problem, we have calculated the potential differences which may accrue to Superior Dairy in its capacity as a partially regulated distributing plant. The Cooperatives supply more than 20 processing plants within the Order 33 competitive area. Based on recent billings these fluid plants had a utilization mix of 86% Class I, 9% Class II, 3% Class III and 2% Class IV. Based on calculations from Order statistics,⁴ we would estimate Superior Dairy to utilize 40,000,000 – 50,000,000 pounds per month. Using these volumes, the average

⁴ When Superior became pooled on Order 1 in April of 2010, data published by the Order 1 Market Administrator indicates that the volume of distribution into Order 1 by Order 33 plants was reduced by about 13 million pounds per month. Attributing this volume to Superior, to be pooled on Order 1 it would represent more than 25% of the plant's total route disposition. This very conservatively implies plant volumes in the 45 million pound range.

distributing plant estimated class utilizations, actual class prices, actual market test data for Ohio, and statistical uniform blend price data, we conservatively estimate the potential advantage that could have arisen from Superior being partially regulated for the 14 months ending in February 2011 to average 80 cents per hundredweight. The dollar impact of this advantage for a plant processing 45 million pounds of milk per month is estimated to be as much as \$1,043,016 per month; and it averages just over \$362,000 per month. Since these funds are not paid to the pool, they would reduce every pool producer's PPD. These monies may then be used by the plant to gain market share for packaged fluid milk products or to procure milk supplies with a competitive advantage.

Request

The Order 33 regulations need to be amended to correct the situation where a traditional distributing plant facility, located in the heart of a Federal Milk Order marketing area, and which has been pooled continuously for many years, has been able to escape full regulation because of a loophole in the definition of 'pool plant' which enables it to split route distribution among various federal orders so that it is not pooled on any order. This is a disorderly condition threatening uniformity of treatment among both pooled producers and regulated handlers and it should be corrected with appropriate amendment to the pool plant language. As a result of our proposal, Superior Dairy would be in the same position with respect to milk cost and competitive equity with other pool distributing plants and in the same fully federally regulated position that it was in prior to March 2011.

Proposed Order Language

The Cooperatives offer the following Order language, amending the pool plant definition of Order 33:

§1033.7 Pool plant.

Pool plant means a plant, unit of plants, or a system of plants as specified in paragraphs (a) through (f) of this section, but excluding a plant specified in paragraph (h) of this section. The pooling standards described in paragraphs (c) through (f) of this section are subject to modification pursuant to paragraph (g) of this section:

(a) A distributing plant, other than a plant qualified as a pool plant pursuant to paragraph (b) of this section or §1000.7(b) of any other Federal milk order, from which during the month 30 percent or more of the total quantity of fluid milk products physically received at the plant (excluding concentrated milk received from another plant by agreement for other than Class I use) are disposed of as route disposition or are transferred in the form of packaged fluid milk products to other distributing plants. At least 25 percent of such route disposition and transfers must be to outlets in the marketing area. Plants located within the marketing area with combined route disposition and transfers of at least 50% into all Federal Order marketing areas but without 25% of route disposition and transfers into any one Federal Order will be regulated as a distributing plant in this Order.

The Cooperatives' proposal establishes an alternative test for pool distributing plant status, which is: If a plant located in the Order 33 Marketing Area has at least half of its total route disposition in Federal Order marketing areas but its sales patterns are such that no one Order has more than 25% of its sales volumes, then it would be regulated in Order 33, the order where it is physically located.

We do not believe that this proposal would have on any effect on a plant in its capacity as a small business.

We are unable to estimate the consumer impact of our proposal because of a lack of information about price transmission between processors and retailers.

We see no benefit to a pre-hearing information session. The issues are clear and simple.

Request for Emergency Consideration

Because of the competitive issue which Superior presents in Order 33 and the other Federal Orders in which it operates and the substantial dollar impact we find in the marketplace resulting from the change in regulation from pool distributing plant to partially regulated plant, we ask that the Secretary process this request under expedited hearing procedures and consider implementation without a recommended decision. The Cooperatives' producer- members are intermingled with producers supplying Superior Dairy on a direct basis – and may receive different minimum blend prices as a result of this situation. Furthermore, the Cooperatives supply milk to both Superior Dairy and its competitors and the differences in regulatory status cause disorderly market conditions which are exacerbated each day that the status remains unchanged.

A list of data requested to be provided to the Cooperatives prior to convening a hearing on the Cooperatives' request for amendment is attached.

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Should there be questions or if additional information is needed for consideration of this request, please contact me. Thank you for your assistance.

Respectfully submitted,

A handwritten signature in cursive script, appearing to read "Marvin Beshore".

Marvin Beshore, Esquire
Attorney for the Cooperatives

cc: Via Email Only
Paul A. Huber, Market Administrator, Order 33
Foremost Farms USA Cooperative, Inc.
NFO Inc.
Dairy Farmers of America, Inc.

Attachment to Order 33 Hearing Request letter - June 16, 2011

Data Requests:

We would make the following data requests for the hearing:

- 1) A list of pool plants including pool distributing plants, partially regulated plants and other order distributing plants for:
 - a. Order 33 and its predecessor Order 36 as typically published in December of each year from 1990 to 2010; and
 - b. all Orders for each month 2009 to 2011.
- 2) For Order 1, monthly data for 2010 and 2011 as regularly published and titled: “Class I Route Sales in the Northeast Marketing Area by Handlers Not Regulated Under The Order” and “Changes in the List of Handlers and Plants.”
- 3) The monthly Order 33 Market Bulletin for 2009, 2010 and 2011.