

Exhibit ____

Testimony of Warren Taylor, Owner of Snowville Creamery

Member of AIDA

Federal Order Hearing Week of May 18, 2009

Docket No. AO-14-A78, et al.

My name is Warren Taylor. I am the owner of Snowville Creamery in Pomeroy, Ohio. Snowville Creamery is an exempt plant, now processing about 130,000 pounds per month of Class 1 milk. We started construction of our plant after meeting with our market administrator and confirming plans to become a producer-handler as volume increased. We believed a reasonable payback would require at least 500,000 pounds per month in Class 1 sales. We began production and distribution of pasture-grazed minimum processed milk in December 2007. The business is owned entirely by myself and my wife, Victoria Taylor. It is now an informal partnership with the dairy farmer couple of Bill Dix and Stacy Hall, on whose 350 acre, 230 cow seasonal dairy farm the milk processing plant was built.

We are growing our business, constantly gaining sales. More importantly, stores see gains in their total milk sales, showing we are not just cannibalizing sales from other milk, but increasing per capita consumption in our new customers. Every week we receive additional testimonials from customers extolling the glorious taste of our milk. These testimonials include people who had been drinking soy milk, parents whose children refused to drink milk or drank very little, and people who had lost their enthusiasm for milk years ago. These testimonials demonstrate clearly and convincingly that all milk is not the same. We are producing a milk that tastes dramatically different from the vast majority of milk available, conventional or organic. We have given consumers a new choice, and our dairy farmers a price well above market.

You can call me a dairy nerd. My father Bert was one of the gentlemen of the 1950 through 1985 American Dairy Industry. He earned a Dairy

Technology degree from Ohio State University in 1953, where he was on the dairy products judging team that won the national contest. He went on to help organize and run the annual National Dairy Producers Judging Contest for twenty years, and was honored with appointment to the Board of Directors of DIFSA, the Washington DC dairy organization which preceded IDFA.

I grew up in a home where dairy products were celebrated and appreciated. We had hand cranked ice cream regularly. Although meat was a Sunday treat, there was always plenty of milk and cottage cheese. Velveeta was unknown in our home. I was raised on fine sharp Wisconsin, New York, and Vermont cheddar. The owners of Columbus area dairy processing plants were regular visitors to our home, as were OSU Dairy Tech professors and grad students. I received a dairy tech degree in 1974 and was at the headquarters of the world's largest fluid milk processor by 1977.

In my ten years at Safeway from 1977 to 1987, the dairy industry changed dramatically, as fluid milk consumption declined, farmer income declined, and gallon jugs became the norm. Child obesity rates began to rise as children's consumption of milk declined and 30% fat cheese and cheese like foods became the principal end products of America's dairy cows, instead of Class 1 fluid drinking milk. Compromises in quality were made. We learned that when plastic jugs were introduced, widespread complaints about the flat oxidized flavor resulting from light exposure could be greatly reduced by pasteurizing at about ten degrees Fahrenheit higher temperature, say 175° instead of 165°. The cooked flavor of the higher pasteurization masked the oxidized flavor. Milk became a low cost commodity.

After ten years at Safeway Dairy Division headquarters and a couple of years as Director of Application Engineering for Cherry-Burrell, I started a process design consulting firm specializing in the dairy industry. It became the world's largest pure consulting firm doing food process design. We were responsible for many major projects including the last

high capacity fluid milk plant in America for Santee Dairies in Los Angeles, much of Dannon Yogurt Companies process design including the process for what became the Activa probiotics drink, Daisy Brand Sour Cream's new Dallas plant which is the largest sour cream plant in the world, and the largest fluid milk plant in all of Europe for Arla Foods. Other projects included Land of Lakes first UHT and consolidated culture products plant, and a \$120 million aseptic facility for Slimfast. In all of these projects my Safeway experience, knowledge of plant operations, and understanding of the economies of scale and facility operating costs were key to our unique contribution.

As American investment in dairy plants declined, I looked to apply my knowledge to design an efficient small scale on farm milk bottling plant in my community. I hoped to learn whether providing a premium pasture grazed minimally processed milk might increase per capita consumption. Other hopes included:

- Supporting local family farms by providing a higher value outlet for raw milk than is offered by the large national cooperatives.
- Providing jobs for local residents with safe and satisfying working conditions, opportunity for progress and personal development, and the pride of helping provide healthful food to the community.
- Providing milk as fresh as practical from cow to consumer, as contrasted with common usage of the term "fresh" to mean "not spoiled".
- Promoting pasture grazed dairy farming without the use of recombinant Bovine Growth Hormone (rBGH).
- Providing consumers the choice of supporting these principles.

In one of the most impoverished and un-employed counties in Ohio this is a model and prototype for future arrangements in other rural locations. The economic spin-off of this local economic development is great. We have seven full-time employees and seven part-time employees. The payroll of these local workers contributes to the local economy and tax base.

Our small local dairy is responsible and responsive to the community. We believe that providing basic needs of life should be done in a way to contribute to the common good. We give consumers the choice of supporting a more rational, sustainable, and healthful world and self, by consuming our dairy products. We believe this excellent milk will reverse children's 30 year decline in fluid milk consumption, and help solve the current health/obesity crisis. I believe the current decline in fluid milk consumption is related to minimum cost production methods and more extreme processing for the longer shelf life required when distributing from large centralized facilities.

Snowville Creamery makes it possible to give consumers truly fresh milk, on their retail grocery store shelves the day after the cows are milked. With daily deliveries and nearby responsive processing capability, our consumers enjoy our dairy products within days of the cows producing the milk. By contrast today's dairy products usually reach consumers one or two weeks after milking. I believe we represent an exciting and promising future, especially for smaller family farms: local differentiated premium milk.

Market Access

The economics of retail grocery store delivery with refrigerated distribution trucks are brutal. The industry cost estimate for a single delivery with a forty foot semi truck is \$250. We believe our costs are between \$25 and \$50 per delivery, depending upon distance between stores, and distance from our production facility. Even then we simply cannot economically supply small "Mom & Pop" stores, health foods stores, or convenience stores which commonly sell \$100 worth of our milk a week. The cost of delivery exceeds the profits until we are delivering at least \$250 worth of milk a week. The proposals from a NMPF and IDFA are based on the clear understanding that the only real cost effective high volume sales available are in the stores which are controlled and supplied largely by IDFA members. The restrictive verbiage proposed which prevents producer-handlers from co-branding

is based on protecting the large lucrative supermarket business and relegating smaller producers to costly less than desirable small retailers. That's not a level playing field.

At the typical local store our \$2.99 per half gallon competes with milk which sells for \$1.99 per half gallon. At that price we both probably make about 10% on the retail gross as profit. At least one week per month our typical store puts their half gallon milk on sale for \$1.00. Our milk goes from costing 50% more to costing three times as much. When this happens our sales drop about 15%. Unfortunately, we get no notification when the milk will go on sale, so we cannot be prepared to adjust our deliveries to the store. We routinely must take back unsold milk when half gallons are on sale. At least one other week per month the gallon milk is put on sale for \$2.99 per gallon. When this happens, half gallon sales also drop, usually about 10%. Again, this is disruptive to our marketing and results in unsold returns. It's not a level playing field.

One reason for low dairy farmer income is the below reasonable loss leader pricing set by vertically integrated grocery chains such as Kroger and Safeway. About 70% of fluid milk is sold in plastic gallon jugs at a price which is usually near cost. An indication of the disconnect between raw milk pricing and commodity fluid milk pricing is the common practice of a processing plant bottling a generic labeled milk which retails for perhaps \$0.50 less than the identical milk in an identical jug with a different name brand label. While this is an amusing façade of customer choice, it more accurately displays the relative impact of the alleged \$0.15 per gallon raw milk cost difference which NMPF and IDFA purport causes disorderly marketing and unfair advantage. Nothing, really.

Market Support

After struggling and failing to get access to large regional and national stores, we began to supply the two Whole Foods Markets in Columbus last August. Within three weeks we were the biggest selling fluid milk in both stores. Whole Foods asked us to supply their two stores in Cincinnati. There again, we became the best selling milk in both stores

in less than a month. We then began supplying the two Whole Foods Markets in Cleveland in November and were the best selling milk in those stores by December.

The difference between Whole Foods and the other grocery stores we have been serving was their sincere support of our milk, and their willingness to give Snowville Creamery shelf space commensurate with growing sales. Whole Foods is committed to encouraging local suppliers, and appreciates our production principals of sustainability, animal welfare, and high quality wholesome minimally processed milk. As such, they are willing to allow us to succeed and even supplant their own house brand as their largest selling milk.

Given honest access to the market, and a level playing field, we can excel. We are still looking to receiving the benefits of a level playing field from major grocery stores

We recently began supplying a grocery store chain right here in Cincinnati. In one of their larger stores there are seventy five shelves of milk in the dairy case. Seventy three of those shelves are filled with Dean Foods milk including the Trauth Dairy label, the grocery store generic label, Horizon Organic, Nature's Basket Organic, and Over The Moon. There are only two other shelves available there, both supplied with milk from Organic Valley. These two IDFA members completely monopolized the milk case until we arrived.

It will be interesting to see if we can establish a toe hold in these stores and grow our market. This grocery store chain seems sincerely committed to encouraging local food producers. Unfortunately, they only have four stores in the entire Cincinnati area which have a demographic promising to our milk and the size large enough to support the twice weekly deliveries necessary to properly supply our fresh relatively short shelf life milk.

The Proposals

As an exempt plant, I support the principles of Proposal 2 from NMPF which explains that: "Given growth in farm size and growing economies of size in milk processing, it is reasonable to increase the size exemption to 450,000 pounds per month, and we propose to do so". In supporting this concept in Proposal 2, I also speak for two other Ohio exempt plants, Hartzler Family Dairy, Inc. in Wooster and H.D. Organics, Inc. in Utica. We all could serve an increasing consumer demand for local fresh premium milk if the exempt limit was raised.

While we agree with the basic premise, in today's world a fluid milk plant of only 450,000 pounds per month cannot be economically constructed and operated. Instead, I believe that 1,000,000 pounds for month is more realistic in providing sufficient volumes for an economical operation. Please refer to "A Cost and Returns Evaluation of Alternative Dairy Products to Determine Capital Investment and Operational Feasibility of a Small-Scale Dairy Processing Facility", from the *Journal of Dairy Science* 2007: This well prepared recent study found that even a facility processing 644,000 pounds per month would have a substantially negative net present value or profitability. I quote the following:

- "Fluid milk plants have closed due to inefficient economies of scale, and because the product – beverage milk – is essentially an indistinguishable commodity. It is very difficult for a processor to position a fluid brand to strategic advantage. The exceptions seem to prove the rule."
- "The 5-farm (644,000 pounds per month) fluid plant would need a 6% increase in present value of reserves, which translates to a \$0.24 increase in the price received per gallon of milk sold".
- "It is unlikely that the fluid processing plants would be able to overcome the baseline revenue shortfalls or the high level of expenses to reach a break-even point".

As a member of AIDA, I also support proposals 23, 24, and 25. Producer-handlers, especially those operating below 10,000,000 pounds per month, must depend on their milk having a value added component, due to lack of large scale efficiencies enjoyed by larger processors. This added value should be reflected all the way back to producer-handler, without being diluted by pooling.

The Organic Dairy Industry has proved that value can be added on the farm by the production method. The FMMOS has been an unfair market distorting manipulation which has redistributed that wealth and value to non-organic commodity lowest cost dairy producers with which organic competes.

John Kennedy famously stated that life is not always fair. The marketplace favors the older established companies. The increasing consolidation and growing size of dairy handlers and processors confirms this fact. Neither Kroger nor Safeway have built a new high volume fluid milk plant in over twenty years. Their capital costs are long since paid off and depreciated. Any new producer-handlers entering the marketplace will find the cost of capital will likely exceed all other costs except raw milk itself. This economic disadvantage far exceeds \$0.15 per gallon. There is no need to grandfather producer-handlers.

One of the last new fluid milk plants built in America was in Nevada, by Dean Foods, to take advantage of a market distorting manipulation of the 2005 Milk Regulatory Equity Act which was supposedly enacted to remove just such market distorting advantages from producer-handlers.

Diversity and Consumer Choice

While there will always be a commodity milk business based on lowest cost, there has also always been other business models based on value added differentiation, which is what most producer-handlers follow. The lowest cost commodity milk business will always serve the vast majority of customers. But a portion of consumers want differentiated milks, particularly locally produced milks from farms following business models

other than lowest cost commodity production. These customers place value on knowing the specific farm producing the milk and the farming methods used. They increasingly value pasture grazed or grass fed milk, for instance.

Let's be honest, the commodity milk market is declining with a continuous decline in fluid milk consumption. There is no sign that this trend will change.

In contrast, our local, minimally processed pasture grazed milk is growing. I have brought 25 unsolicited testimonies from consumers who find our particular and different milk has led to their increased consumption. They know that all milk is not the same, and this milk has a much higher value to them. That value belongs to the small local farmer whose production method created it. It will always be a small part of the fluid market, and no threat to the commodity processors or the FMOS.

Testimony in these hearings has included the fact that smaller dairy farmers have a tremendous cost of production disadvantage, 4 to 5 dollars per hundred weight. If these farms are able to have any future, it must be through adding value or government subsidies. They cannot possibly compete with commodity milk. They are not on a level playing field. Is our future one that willingly eliminates all small dairy farms below 1,000 cows? Perhaps it is if proposals 1 and 26 are accepted.

I believe in diversity, in a variety of business models, and choices for both dairy farmers and consumers in the marketplace. Most grocery stores in Ohio offer between 3 and 5 different ultra pasteurized out of state organic milks, but few have a locally produced pasture grazed cream line milk, although consumers want it. For those consumers to be served, small vertically integrated producer-handlers must be an available option for entrepreneurial dairy farmers.

Thank you for the opportunity to present my outlook and experience.