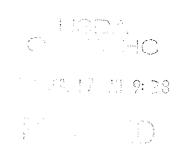
Post Hearing Brief

Docket AO-14-A78,et al



This brief is on behalf of Mid-West Dairymen's Co. and Lakeshore Federated Dairy Cooperative and Lakeshore's members-Manitowoc Milk Producers Cooperative, Milwaukee Cooperative Milk Producers, and Scenic Central Milk Producers Cooperative. These cooperatives represent over 4,000 producers marketing milk primarily on Federal Order 30. All are recognized as qualified Capper Volstead cooperatives.

Introduction. The issue, as we see it, is the existing great potential for large producer-handlers to disrupt marketing conditions with resulting chaos and disorder in the marketplace. This potential exists because under current regulations producer-handlers have no obligation to pay the classified price value to the Federal Order "pool". Currently we have been spared this disorder but this hearing record and the record of proceedings in other areas of the country tells us that it is just a matter of time-our days are numbered.

Exhibit 101 shows that Heartland Dairy, a large producer-handler located in northeast Missouri, has sales in Illinois. Heartland could easily become a direct competitor to the Mid-West Dairymen's Muller Pinehurst joint venture fluid operation. Large dairy farms could easily add a bottling operation and become a producer-handler. This can be accomplished at a lower capital cost than is the case for an existing fluid milk plant to add a raw milk production facility and become a producer-handler. (Testimony by Wilcox) My testimony called attention to a large dairy farm (7,000 cows) that had begun construction 50 miles from the Muller plant in Rockford. This farm could easily add a fluid milk plant and use the price advantage it would have as a producer-handler and compete with regulated handlers for sales in the Chicago-Rockford market area. With 7,000 cows this single farm would approach the size of all Mid-West member farms combined, have economies of scale in milk production along with the producer handler price advantage which Muller and Mid-West members do not have.

The major advantage larger producer-handlers derive from their status as a producer-handler is the avoidance of Class I price accountability to the Federal Order. All pooled regulated handlers must account to the Federal Order for the classified value (with Class I generally the highest value class) of their milk. The producer handler does not have this obligation and can achieve a considerable raw milk cost advantage compared to the regulated handler who must pay the minimum regulated Federal Order prices.

The adoption of Proposals 1 and 2 would maintain the level playing field and resulting marketplace stability we now enjoy. Other proposals presented at the hearing if adopted would not provide the same level of stability and could even create more chaotic conditions.

The Producer-Handler Advantage. A regulated Class I handler pays the appropriate Class I price. A pooled producer supplying that Class I market receives the appropriate blend price. The difference between the Class I price paid by the handler and the blend price received by the producer is the price advantage for the producer-handler. The pooled producer delivering milk to the fluid plant does not receive the price difference between the Class I price and the blend price. The regulated Class I handler does not gain the advantage offered by this price difference. This advantage is only received by a producer who also chooses to bottle his own production as a producer-handler. A producer who bottles his own milk as a regulated handler does not gain this price advantage. The producer-handler advantage is a real advantage and is evidenced in the many dollars that the regulated Class I handler and the producers supplying those regulated handlers pay to the Federal Order pool.

Milk Production Costs. Various producer-handlers testified that their milk production costs were so high that without the producer-handler advantage their milk production operation would not survive. There was a lack of testimony however which directly compared the production cost among producers of the same size using similar raw milk production methods. The basic reason for this lack of testimony is that the presence of a processing plant (or lack of a processing plant) when the milk leaves the farm bulk milk storage tank does not change the production cost of the raw milk going into the tank. The majority of the production cost information in the hearing record relates to either differences in cost due to economies of scale or differences in farm milk costs among farms due to methods of production-grazing, organic, or other types of feeding and handling. These raw milk production cost differences are due to the previously mentioned production techniques and not to one's status as a producer-handler.

A dairy farmer's milk production costs can be higher or lower than the Federal Order blend price or Class I price. A comparison of milk production costs with Federal Order price levels-be it the Class I price or the blend price- will find the difference is entirely driven by a) the economic costs of milk production and b) the Federal Order pricing factors. Milk production costs related to Federal Order prices are not driven by a farm's status as a producer-handler or not being a producer handler. A producer-handler's marketplace advantage however is driven by the difference in these cost and price factors.

<u>Producer-Handler Exemption.</u> The producer-handler exemption began as a regulatory convenience in the early days of the order program. It is not found in the original legislation

through which Federal Orders were initiated but only in subsequent regulatory language. If the exemption did not currently exist there would not be a compelling reason to create it. There are relatively few producer-handlers when compared to the entire population of dairy farmers. The existing producer-handlers have made investments and business decisions based on existing exemption regulations. Change in regulations and the application of those regulations is inevitable. It happens in all walks of life and across all levels of government.

The producer-handler exemption is based on the producer-handler's status as a dairy farmer processing and distributing his own milk. The Department has determined a dairy farmer to be a "small business" at the level of 500,000 pounds of monthly milk production. There is also a "flattening" of the milk production cost curve at approximately the 500,000 pound level of monthly milk production (Cryan testimony). The tipping point for economies of scale is at that approximate size-cost of production increases rapidly as milk volume decreases below the 500,000 pound monthly level. As the volume increases over the 500,000 pound level of monthly milk production cost of production decreases more slowly with the increasing volume. (Exhibit 23, page 11) This is further evidence that the 500,000 pound level is the right demarcation point.

Conclusions. Orderly marketing conditions will be established and maintained through the elimination of the producer-handler exemption and an increase in the size limit for an exempt plant. A small business dairy farmer with 500,000 pounds of monthly production would have 450,000 pounds of monthly Class I sales assuming 90% Class I utilization. An exemption for a producer of this size is desirable. Proposals 1 and 2 are the best way of achieving an exemption for a producer of this size. Accordingly we urge the Secretary to adopt Proposals 1 and 2 and reject all other proposals that allow an exemption that exceeds the position outlined above.

Sincerely,

Dennis Tonak

Dennis Jonak

On behalf of Mid-West Dairymen's Co and Lakeshore Federated Dairy Cooperative