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# STUDENT NOTE

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## PAYMENTS TO DAIRY COOPERATIVES FROM PRODUCER SETTLEMENT FUNDS

*Jerald N. Engstrom\**

### I. INTRODUCTION

Since 1938 the Secretary of Agriculture has ordered money payments to be paid out of the New York producer settlement fund to dairy cooperatives in compensation for services performed which have benefited both cooperative members and non-members alike.<sup>1</sup> These payments have been challenged in federal courts, one of the basic issues being the scope and extent of the services a cooperative must perform to both its members and non-members in order to receive the payments. The most important judicial interpretations of cooperative payment provisions of the Agricultural Marketing Agreement Act of 1937<sup>2</sup> are contained in *Brannan v. Stark*<sup>3</sup> and *Grant v. Benson*.<sup>4</sup>

This note will discuss these cases and will indicate the statutory basis for payments out of the producer settlement fund to dairy cooperatives which perform certain marketwide services.

### II. MILK MARKETING ORDERS UNDER THE AGRICULTURAL MARKETING AGREEMENT ACT OF 1937

The Agricultural Marketing Agreement Act of 1937 was enacted to assure dairy producers a price for milk, "which shall reflect the price of feeds, the available supply of feeds and other economic conditions which affect market supply and the demand for milk or its products in the market area to which the contemplated . . . order or amendment

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<sup>1</sup> 3 FED. REG. 1945, 1949-50 (1938).

<sup>2</sup> 50 STAT. 246 (1937), 7 U.S.C. §§ 601-608 (1952) (reinstating without change 49 STAT. 750 (1935) which had been declared unconstitutional as part of the Agricultural Adjustment Act of 1933 in *United States v. Butler*, 297 U.S. 1 (1936)).

<sup>3</sup> 342 U.S. 451 (1952).

<sup>4</sup> 229 F.2d 765 (D.C. Cir. 1955), *cert. denied*, 350 U.S. 1015 (1956).

relates,"<sup>5</sup> to eliminate cutthroat competition in the marketing of milk<sup>6</sup> and to help solve the problem of milk surpluses.<sup>7</sup> To effectuate these purposes the Secretary of Agriculture was empowered under both the Agricultural Adjustment Act of 1933<sup>8</sup> and the Agricultural Marketing Agreement Act of 1937<sup>9</sup> to enter into milk marketing agreements with processors and handlers of milk. The milk marketing agreements were intended to increase the purchasing power of the producing dairy farmer by establishing minimum prices to producers and resale prices for handlers. The intended effect was to bring up the purchasing power of the producer to a point which was termed "parity."<sup>10</sup> However, it was extremely difficult for the Secretary of Agriculture to enter into voluntary marketing agreements with all handlers in a market area and the marketing agreement could be terminated by either party at his own option. For these reasons the marketing agreements were never effective in the regulation of milk, even though they still may be entered into by the Secretary of Agriculture.<sup>11</sup> However, under the 1937 act the Secretary of Agriculture was also granted the power to issue milk marketing orders establishing uniform prices to be paid to all producers in the same market area regardless of the use made of the milk, i.e., whether the milk is distributed to the consumer as fluid milk or processed into butter, cheese or other dairy products.<sup>12</sup> The power of the Secretary of Agriculture to issue milk marketing orders is necessarily limited to areas supplied by milk moving in interstate commerce or in areas in which milk moving in intrastate commerce may affect interstate commerce.<sup>13</sup> As a consequence such orders are in effect in approximately 63 areas, many of which are overlapping.<sup>14</sup>

Before the Secretary of Agriculture may issue a milk marketing order, "due notice of and an opportunity for a hearing upon," the proposed

<sup>5</sup> 50 STAT. 247 (1937), 7 U.S.C. § 608c (18) (1952).

<sup>6</sup> *Elm Spring Farm, Inc. v. United States*, 127 F.2d 920 (1st Cir. 1942); *Cosgrove v. Wickard*, 49 F. Supp. 232 (D.Mass. 1943).

<sup>7</sup> *Shawangunk Cooperative Dairies, Inc. v. Jones*, 59 F. Supp. 848 (S.D. N.Y. 1945) *rev'd on other grounds*, 153 F.2d 700 (2d Cir. 1946).

<sup>8</sup> See note 2 *supra*.

<sup>9</sup> *Ibid*.

<sup>10</sup> Parity is that price which will give to the producer a purchasing power equivalent to the purchasing price in the base period multiplied by the parity index. 52 STAT. 38 (1938) *as amended*, 7 U.S.C. § 1301(a) (1) (A), (B) (1952).

<sup>11</sup> 49 STAT. 753 (1935) 7 U.S.C. § 608b (1952).

<sup>12</sup> *Id.* § 608c.

<sup>13</sup> *Id.* § 608c(1), *United States v. Wrightwood Dairy Co.*, 315 U.S. 110, 123 (1942).

<sup>14</sup> A milk marketing order regulates all producers and handlers who supply and process milk for a city, e.g., New York City. Two milk marketing orders may cover the same geographic area, in that one producer may sell his milk to a handler supplying the New York area while his neighbor sells his milk to a handler supplying the Boston area. But only one milk marketing order would regulate any given producer. All the milk marketing orders are contained in 7 C.F.R. §§ 900-1009 (1955).

order must be provided to handlers and producers in the area to be affected by the order.<sup>15</sup> Any order issuing from the Secretary of Agriculture must have the approval of handlers of 50 per cent of the volume of milk handled in the area.<sup>16</sup> If the requisite number fail to approve the order it may still issue if two-thirds of the producers in the area approve it.<sup>17</sup>

Milk is classified under a milk marketing order according to the use made of it by the handler. There are usually two classifications, viz. class I or fluid milk and class II or non-fluid milk. For each classification the milk order sets a uniform price to be paid by each handler subject to such adjustments as are authorized by the act.<sup>18</sup> Each handler reports the total volume of milk used in each classification to the market administrator, who is appointed by the Secretary of Agriculture. The market administrator multiplies the total volume used in each classification by the class or uniform price to obtain a "total use value" for each handler. The "use value" for all the handlers are added together to obtain a "use value of the market area." From the "use value of the market area" are deducted certain "adjustments" which are specified in the milk marketing order<sup>19</sup> plus the deduction for payments to cooperatives for marketwide services when such deduction is authorized by the order. The "use value of the market area" minus the above stated deductions is divided by the total volume or pounds of milk used in the market area by all handlers in both classes to obtain a uniform or "blended price," which is the price paid to all producers subject to certain allowable adjustments authorized by the act. The only exception allowed by the act to the uniform price paid to all producers is to cooperative members in accordance with their contracts with the cooperatives.<sup>20</sup> After each handler pays the uniform price to the producers from whom he purchased milk, he will either receive from or pay to the "producer settlement fund" the amount to which his "use value" either falls short of or exceeds the uniform price.

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<sup>15</sup> 49 STAT. 754 (1935), 7 U.S.C. § 608c (3) (1952).

<sup>16</sup> 49 STAT. 758 (1935), 7 U.S.C. § 608c (9) (1952).

<sup>17</sup> *Id.* § 608c (9) (A), (B) (i), (ii) (1952). Where the producers vote on the milk marketing order when the requisite number of handlers fail to approve the order, the cooperative shall cast the votes of all its members. 49 STAT. 759 (1935), 7 U.S.C. § 608c (12) (1952).

<sup>18</sup> *Id.* at 754, 7 U.S.C. § 608c (5) (A) (1952).

<sup>19</sup> *Id.* at 755, 7 U.S.C. § 608c(5)(B)(ii) (1952). The adjustments to be made at this point are those for, "(a) volume, market, and production differentials customarily applied by the handlers subject to such order, (b) the grade or quality of the milk delivered, (c) the locations at which delivery of such is made, and (d) a further adjustment, equitably to apportion the total value of the milk purchased by any handler, or by all handlers, among producers and associations of producers, on the basis of their marketings of milk during a representative period of time."

<sup>20</sup> *Id.* § 608c (5) (F) (1952).

## III. PRODUCER SETTLEMENT FUND PAYMENTS

## A. Operation Of Producer Settlement Funds.

Under the 1937 Act, the Secretary of Agriculture was directed to implement the purposes of the act.<sup>21</sup> Pursuant to such statutory mandate the Secretary provided for the establishment in each milk marketing area of a special monetary fund, "termed a producer settlement fund." The custodian or trustee of this fund is the market administrator appointed by the Secretary. The handlers within a marketing area build up the fund by payments to it of the amount by which their individual "use value" exceeds the uniform price paid by them to all producers. Payments from the fund are made to handlers whose "use value" falls short of the uniform price which they had to pay producers. In addition to these equalization payments, dairy cooperatives in some market areas have been reimbursed for all marketwide services which they have performed. Such reimbursement payments to cooperatives, incidental in nature, are insignificant in comparison to the total amount of regular payments from the producer settlement fund to the handlers in the market area.

## B. Dairy Cooperatives and Marketwide Services.

Dairy cooperatives<sup>22</sup> now play the major role in the marketing of milk in the United States. They were originally organized by the producers to bolster the prices paid producers for milk and provide a method for the disposing of surplus milk.<sup>23</sup> They are the most representative bargaining agents for producers. Membership in an *operating* dairy cooperative is gained by selling milk to the cooperative, whereas in a *bargaining and collecting* dairy cooperative the members pay dues, based upon the amount of milk they sell to the handlers, to pay the expenses. The members own the operating cooperative, and their respective shares of ownership are in direct proportion to the amount of milk they sell to the cooperative. Membership in an operating cooperative is kept current by the retirement, usually annually, of the oldest outstanding membership;

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<sup>21</sup> 49 STAT. 753 (1935), 7 U.S.C. § 608c (1); *Waddington Milk Co. v. Wickard*, 140 F.2d 97, 101 (2d Cir. 1944).

<sup>22</sup> "An agricultural cooperative is a business organization, usually incorporated, owned and controlled by member agricultural producers, which operate for the mutual benefit of its members or stockholders as producers or patrons on a cost basis after allowing for the expenses of operation and maintenance and any other deductions for expansion and necessary reserves." HULBERT, *LEGAL PHASES OF FARMER COOPERATIVES*, U.S. DEP'T OF AGRICULTURE, F.C.S. BULLETIN No. 10 page 1 (1958).

<sup>23</sup> BEMIS, *HISTORY OF COOPERATION IN THE UNITED STATES (1888)*; *THE STORY OF FARMERS' COOPERATIVES*, U.S. DEP'T OF AGRICULTURE, F.C.S. EDUCATIONAL CIRCULAR 1 (1954).

whereas in a non-stock cooperative the net profit is distributed annually to its membership. All expenses of the cooperative are borne by its membership; significantly included within such expenses is the cost of all beneficial, marketwide services performed by the cooperatives.

In order for a cooperative to qualify for reimbursement payments from a producer settlement fund, it must perform certain marketwide services.<sup>24</sup> A marketwide service has been defined as a service which benefits both members and non-members of the cooperative.<sup>25</sup> Such services include collection of information on market conditions, formulation of proposed amendments to milk marketing orders and the representation of all producers at hearings before the market administrator. In addition to the performance of marketwide services, a cooperative must be duly incorporated under a state cooperative corporation law; all of its activities must be controlled by its members; it must have the full authority to sell its members' milk; and it must meet the requirements of the Capper-Volstead Act.<sup>26</sup> By far the most important of these requirements is the performance of marketwide services, the cost of which, if not reimbursed to the cooperative, necessarily diminishes the amount of the uniform price which the cooperative passes on to its members. Therefore, without reimbursement to the cooperatives their members would receive less than the uniform price, while the non-members would receive the uniform price plus the benefits of the marketwide services performed by the dairy cooperatives at the expense of their members.

### *C. Payments To Cooperatives Under the New York Milk Marketing Order.*

The first authorized reimbursement payments to dairy cooperatives from a producer settlement fund were made in the New York area in 1938 as part of a joint federal and state program for the regulation of milk.<sup>27</sup> These payments were made to compensate dairy cooperatives which had performed marketwide services necessitated by the complicated administration and revision of the milk orders and the rapidly changing conditions of the market. For example, during the period 1938 to 1949 there were approximately 200 changes in the New York milk

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<sup>24</sup> 7 C.F.R. § 927.76 (e) (1955).

<sup>25</sup> *Brannan v. Stark*, 342 U.S. 451, 459-460 (1952).

<sup>26</sup> To qualify under the Capper-Volstead Act, a cooperative must operate for the mutual benefit of its members. The cooperative may pay any rate of dividends it desires if it limits each member to one vote regardless of the amount of stock or equity he owns, but if any member can vote more than one vote the cooperative can not pay dividends at a rate in excess of 8 per cent per annum. The cooperative cannot deal in products of non-members to a greater extent than members. 42 STAT. 388 (1922), 7 U.S.C. §§ 291-292 (1952).

<sup>27</sup> See note 1 *supra*.

order made on 53 different occasions.<sup>28</sup> The majority of these changes were made at the instigation of the cooperatives after extensive investigation of market conditions.

In 1952 the Secretary of Agriculture and the New York Commissioner of Agriculture and Markets appointed a special committee of experts to study the relationship of dairy cooperatives to the marketing of milk in the very complex New York area.<sup>29</sup> The committee first outlined the services performed in the marketing of milk and subsequently found that these services were performed solely by the dairy cooperatives. Even more significant was the committee's finding that these services benefited not only members of the cooperatives, but all of the producers in the New York area. The committee naturally concluded, therefore, that the cooperatives performing these services should continue to be reimbursed for the cost of such services out of the New York producer settlement fund, as had been done since 1938.<sup>30</sup>

Reimbursement payments are based upon the amount of milk delivered by the producers to the cooperatives at rates set by the milk marketing order.<sup>31</sup> There is one payment to cooperatives for informational services and an additional payment to those cooperatives who maintain standby plants for disposing of surplus milk.<sup>32</sup> A cooperative's compliance with the requirements for payment is determined by the milk market administrator, and periodic proof of compliance is required by the order.<sup>33</sup>

In spite of the purported justification for reimbursement payments to cooperatives performing marketwide service—as found by the Secretary's special committee—six unaffiliated producers challenged in the United States District Court for the District of Columbia<sup>34</sup> the Secretary's authorization of reimbursement payments to cooperatives in the New York area. The challenge was based upon the ground that the Secretary of Agriculture did not possess authority under the Agriculture Marketing Agreement Act of 1937 to include provisions in the New York milk marketing order for reimbursement payments to cooperatives performing marketwide services. A similar challenge of such payments to cooperatives in the Boston area had been upheld by the United States Supreme

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<sup>28</sup> 18 FED. REG. 6459 (1953). The New York milk marketing area is supplied by approximately 50,000 producers located in six states some living up to 400 miles from New York City. "The factors of size, diversity of condition, specialization among handlers, divergency of interest, and complexity of price structures make this milkshed and regulatory program unique," thereby necessitating many changes in the milk marketing order. *Ibid.*

<sup>29</sup> 18 FED. REG. 6458 (1953).

<sup>30</sup> 18 FED. REG. 6462 (1953).

<sup>31</sup> 7 C.F.R. § 927.76 (f) (2), (4) (1955).

<sup>32</sup> *Id.* § 927.76 (e).

<sup>33</sup> *Id.* § 927.76 (b), (d).

<sup>34</sup> *Grant v. Benson*, 229 F.2d 765 (D.C.Cir. 1955), *cert. denied*, 350 U.S. 1015 (1956).

Court in 1951<sup>35</sup> on the ground that there was no statutory basis for such payments to cooperatives. In answer to the New York challenge the Court held that the Secretary's order authorizing payments to cooperatives for the performance of marketwide services was a valid exercise of power authorized by the Agricultural Marketing Agreement Act. Essential to its holding was its acceptance of the facts: (1) that the services performed by the cooperatives benefit members and non-members alike, and (2) that the services were reasonably necessary to accomplish the purposes of the statute through the method adopted.<sup>36</sup>

#### *D. The Statutory Basis For Reimbursement Payments to Cooperatives.*

Section 608c (7) (D) provides that milk marketing orders shall contain "terms and conditions" which are "incidental to, and not inconsistent with" the provisions of this act "and necessary to effectuate the other provisions of such order." A fundamental purpose of the 1937 Act, as provided in section 608c (5) (B) (ii), is to establish "uniform prices for all milk" irrespective of the use made of the milk. For the accomplishment of this purpose the Secretary of Agriculture has been empowered to issue milk marketing orders establishing uniform prices. Specific "terms and conditions" enumerated in the act may be included in the marketing orders. Other "terms and conditions" may be included at the Secretary's discretion if they are "incidental to, and not inconsistent with" those enumerated in the act and which "are necessary to effectuate" the orders. The responsibility of deciding what is necessary and what is incidental for inclusion in milk orders is that of the Secretary of Agriculture whose statutory function is the devising of appropriate methods for pricing milk.<sup>37</sup> It was pursuant to this statutory mandate that the Secretary included in the New York order provisions authorizing reimbursement payments to cooperatives out of the producer settlement fund for marketwide services, the performance of which had been specifically required by the Secretary's New York order.<sup>38</sup> The market-

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<sup>35</sup> *Brannan v. Stark*, 342 U.S. 451 (1952).

<sup>36</sup> 229 F.2d at 770.

<sup>37</sup> See note 21 *supra*.

<sup>38</sup> 7 C.F.R. § 927.76(e) (1955). The New York order required the cooperatives to perform the following marketwide services: "(1) Analyzing milk marketing problems and their solution, conducting market research and maintaining current information as to all market developments, preparing and assembling statistical data relative to prices and marketing conditions, and making an economic analysis of all such data; (2) determining the need for the formulation of amendments to the order and proposing such amendments or requesting other appropriate action by the Secretary or the market administrator in the light of changing conditions; (3) participating in proceedings with respect to amendments to the order, including the preparation and presentation of evidence at public hearings, the submission of appropriate briefs and exceptions, and also participating, by voting or otherwise, in the referenda relative



wide services performed by the cooperatives have been both necessary and incidental to the Secretary's method of providing uniform prices for milk as required by section 608c (5). It is very evident, therefore, that by virtue of the Secretary's statutory authorization to establish a method for the uniform pricing of milk, he has the authority to order reimbursement payments to cooperatives performing marketwide services. Without this authority the uniform pricing of milk would be impossible.

Section 608c (5) (B) (ii) (d) was also relied on by the Secretary as a statutory basis for payments to cooperatives. This section provides for certain variations or adjustments in the uniform price of milk including "a further adjustment, *equitably* to apportion the total value of the milk purchased by any handler, or all handlers, among producers and *associations of producers*, on the basis of their marketings of milk during a representative period of time."<sup>39</sup> (Emphasis added.) Since the members of cooperatives bear the expense of the marketwide services performed by their cooperatives, the price they receive for their milk is less than the uniform price paid to producers, while non-members—not sharing in the expenses of marketwide services—receive the full uniform price. A remedy for this inequitable result has been provided by reimbursement payments to cooperatives for their marketwide services. This remedial "adjustment" apportions "equitably" the value of milk among all producers. Hence, payments to cooperatives from the producers settlement fund come within the express provisions of the act.<sup>40</sup> An opposite conclusion would make impossible the establishment of a uniform price unless the market administrator assumes the responsibility for the

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to amendments; (4) participating in the meetings called by the market administrator, such as meetings with respect to rules and regulations issued under the order, including activities such as the preparation and presentation of data at such meetings and briefs for submission thereafter; (5) conducting a comprehensive educational program among producers—i.e., members and nonmembers of cooperatives—and keeping such producers well informed for participation in the activities under the regulatory order and, as a part of such program, issuing publications that contain relevant data and information about the order and its operation, and the distribution of such publication to members and, on the same subscription basis, to nonmembers who request it, and holding meetings at which members and nonmembers may attend; and (6) in the case of a cooperative or federation which receives an additional payment under paragraph (f) (4) or (5) of this section, operating marketing facilities, or having within its membership federated cooperatives operating marketing facilities, i.e., pool plant(s), at which is received at least 25 per centum, by weight, of the milk marketed by all the members of the cooperative or by all the members of the federated cooperatives."

<sup>39</sup> The *Senate Agriculture Committee* in its report on proposed amendments to the Agricultural Adjustment Act of 1933 stated that section (ii) included authority to make a further adjustment in payments to producers upon the basis of their production records during a representative period of time. This would allow the operation of the so called "base payment plan" for payments to producers. Subsection (d) of (ii) is the authority for operation of the base payment plan. S. REP. No. 1011, 74th Cong., 1st Sess. 11 (1935).

<sup>40</sup> See note 4 *supra*.

performance of the services now performed by the cooperatives.<sup>41</sup> In such event he would be reimbursed out of the producer settlement fund for the expense of such services.<sup>42</sup>

### III. THE BOSTON ANOMALY

In *Brannan v. Stark*,<sup>43</sup> the United States Supreme Court denied the existence of a statutory basis for payments to cooperatives from the Boston area producer settlement fund. The payments had been made since 1941 as directed by provisions of the Boston milk marketing order.<sup>44</sup> The Boston order differed from the earlier New York order in two major respects. First, the Boston order had not been supported by elaborate findings of fact to the effect that the cooperatives performed marketwide services of benefit to members and non-members alike; whereas the New York order was based upon elaborate findings of fact to the effect that the cooperatives did perform marketwide services. Second, there was no provision in the Boston order requiring cooperatives to perform marketwide services. The Court found that the services to be performed by cooperatives in the Boston area were performed for the direct benefit of the cooperatives' memberships and were but incidentally helpful to the other producers.<sup>45</sup> The Court logically concluded that the allowance of payments to cooperatives for non-marketwide services would make impossible the payment of a uniform price to all producers because non-members—not recipients of benefits resulting from marketwide services—would receive less than members of the cooperatives. In effect the Boston payments were for milk, not services.

It is clear therefore that the Boston *Brannan v. Stark* case is not irreconcilable with the New York *Grant v. Benson* holding. The former, unlike the latter, was not supported by elaborate findings of fact as to the performance of marketwide services by cooperatives. In Boston the payments were for milk; whereas in New York they were for services of marketwide benefit.

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<sup>41</sup> The market administrator could perform effectively certain of the services now performed by cooperatives if he so desired under § 608c (5) (E) of the Agricultural Marketing Agreement Act of 1937. But as to others, such as education of the members, he would have a difficult if not impossible task. Also if he performs all the functions now performed by the cooperative, there would be little advantage for a producer to belong to a cooperative and, as such, the cooperatives would suffer greatly. This would be contrary to the Federal Government's policy of fostering cooperatives and would be harmful to the public as a whole.

<sup>42</sup> 49 STAT. 755 (1935), 7 U.S.C. § 608c (5) (E) (1952).

<sup>43</sup> *Brannan v. Stark*, 342 U.S. 451 (1952).

<sup>44</sup> 6 FED. REG. 3767 (1941).

<sup>45</sup> *Supra* note 43 at 459-460.

## IV. CONCLUSION

The Agricultural Marketing Agreement Act authorizes reimbursement payments to dairy cooperatives under certain conditions. In view of the valid provisions of the New York milk marketing order, a cooperative, to be eligible for payments from the producer settlement fund, must perform marketwide services required by the milk marketing order. *Brannan v. Stark* does not prohibit all payments to cooperatives. Cooperatives in any market area, required by the milk market order in effect in the area to perform marketwide services, should be reimbursed for the expense of such services.