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Friday  
January 30, 1998

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**Part II**

**Department of  
Agriculture**

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**Agricultural Marketing Service**

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**7 CFR Part 1000 et al.**

**Milk in the New England and Other  
Marketing Areas; Opportunity To File  
Comments, Including Written Exceptions,  
on Proposed Amendments to Marketing  
Agreements and Orders; Proposed Rule**

**DEPARTMENT OF AGRICULTURE**

**Agricultural Marketing Service**

**7 CFR Parts 1000, 1001, 1002, 1004, 1005, 1006, 1007, 1012, 1013, 1030, 1032, 1033, 1036, 1040, 1044, 1046, 1049, 1050, 1064, 1065, 1068, 1076, 1079, 1106, 1124, 1126, 1131, 1134, 1135, 1137, 1138 and 1139**

[DA-97-12]

**Milk in the New England and Other Marketing Areas; Proposed Rule and Opportunity To File Comments, Including Written Exceptions, on Proposed Amendments to Marketing Agreements and Orders**

7 CFR part	Marketing area
1000 .....	General Provisions of Federal Milk Marketing Orders.
1001 .....	New England.
1002 .....	New York-New Jersey.
1004 .....	Middle Atlantic.
1005 .....	Carolina.
1006 .....	Upper Florida.
1007 .....	Southeast.
1012 .....	Tampa Bay.
1013 .....	Southeastern Florida.
1030 .....	Chicago Regional.
1032 .....	Southern Illinois-Eastern Missouri.
1033 .....	Ohio Valley.
1036 .....	Eastern Ohio-Western Pennsylvania.
1040 .....	Southern Michigan.
1044 .....	Michigan Upper Peninsula.
1046 .....	Louisville-Lexington-Evansville.
1049 .....	Indiana.
1050 .....	Central Illinois.
1064 .....	Greater Kansas City.
1065 .....	Nebraska-Western Iowa.
1068 .....	Upper Midwest.
1076 .....	Eastern South Dakota.
1079 .....	Iowa.
1106 .....	Southwest Plains.
1124 .....	Pacific Northwest.
1126 .....	Texas.
1131 .....	Central Arizona.
1134 .....	Western Colorado.
1135 .....	Southwestern Idaho-Eastern Oregon.
1137 .....	Eastern Colorado.
1138 .....	New Mexico-West Texas.
1139 .....	Great Basin.

**AGENCY:** Agricultural Marketing Service, USDA.

**ACTION:** Proposed rule.

**SUMMARY:** This proposed rule consolidates the current 31 Federal milk marketing orders into 11 orders. This consolidation is proposed to comply with the 1996 Farm Bill which mandates that the current Federal milk orders be consolidated into between 10 to 14 orders by April 4, 1999. This proposed rule also sets forth two options for consideration as a replacement for the Class I price

structure and proposes replacing the basic formula price with a multiple component pricing system. This proposed rule also establishes a new Class IV which would include milk used to produce nonfat dry milk, butter, and other dry milk powders; reclassifies eggnog and cream cheese; and addresses other minor classification changes. Part 1000 is proposed to be expanded to include sections that are identical to all of the consolidated orders to assist in simplifying and streamlining the orders.

**DATES:** Comments must be submitted on or before March 31, 1998.

**ADDRESSES:** Comments (two copies) should be submitted to Richard M. McKee, Deputy Administrator, Dairy Programs, USDA/AMS, Room 2968, South Building, P.O. Box 96456, Washington, DC 20090-6456. Comments also may be sent by fax to (202) 690-3410. Additionally, comments may be submitted via E-mail to: Milk\_Order\_Reform@usda.gov.

All comments should be identified with the docket number found in brackets in the heading of this document. To facilitate the review process, please state the particular topic(s) addressed, from the following list, at the beginning of the comment: consolidation, basic formula price, Class I price structure, other class prices, classification, provisions applicable to all orders, regional issues (please specify: Northeast, Southeast, Midwest, Western), and miscellaneous and administrative. If comments submitted pertain to a specific order, please identify such order.

Comments are also being requested on the Executive Order 12866 analysis, the Regulatory Flexibility Act analysis, and the Paperwork Reduction Act analysis.

Additionally, comments may be sent via E-mail to: Milk\_Order\_Reform@usda.gov.

All comments submitted in response to this proposal will be available for public inspection at the USDA/AMS/Dairy Programs, Order Formulation Branch, Room 2968, South Building, 14th and Independence Ave., S.W., Washington, D.C., during normal business hours (7 CFR 1.27(b)). All persons wanting to view the comments are requested to make an appointment in advance by calling Richard M. McKee at (202) 720-4392.

**FOR FURTHER INFORMATION CONTACT:** John F. Borovics, Branch Chief, USDA/AMS/Dairy Programs, Order Formulation Branch, Room 2971, South Building, P.O. Box 96456, Washington, DC 20090-6456, (202) 720-6274.

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**I. Legislative and Background Requirements**

*Legislative Requirements*

Section 143 of the Federal Agriculture Improvement and Reform Act of 1996. (Farm Bill), 7 U.S.C. 7253, requires that by April 4, 1999,<sup>1</sup> the current Federal

<sup>1</sup> Section 143(b)(2) requires that a proposed rule be published by April 4, 1998 and Section 143(b)(3) provides that "in the event that the Secretary is enjoined or otherwise restrained by a court order from publishing or implementing the consolidation and related reforms under subsection (a), the length of time for which that injunction or other restraining order is effective shall be added to the time limitations specified in paragraph (2) thereby extending those time limitations by a period of time

milk marketing orders be consolidated into between 10 to 14 orders. The Secretary of Agriculture (Secretary) is also directed to designate the State of California as a Federal milk order if California dairy producers petition for and approve such an order. In addition, the Farm Bill provided that the Secretary may address related issues such as the use of utilization rates and multiple basing points for the pricing of fluid milk and the use of uniform multiple component pricing when developing one or more basic prices for manufacturing milk. Besides designating a date for completion of the required consolidation, the Farm Bill further requires that no later than April 1, 1997, the Secretary shall submit a report to Congress on the progress of the Federal order reform process. The report must cover three areas: a description of the progress made towards implementation, a review of the Federal order system in light of the reforms required, and any recommendations considered appropriate for further improvements and reforms. This report was submitted to Congress on April 1, 1997. Finally, the 1996 Farm Bill specifies that USDA use informal rulemaking to implement these reforms.<sup>2</sup>

### Background

The authorization of informal rulemaking to achieve the mandated reforms of the Farm Bill has resulted in a rulemaking process that is substantially different from the formal rulemaking process required to promulgate or amend Federal orders. The formal rulemaking process requires that decisions by USDA be based solely on the evidentiary record of a public hearing held before an Administrative Law Judge. Formal rulemaking involves the presentation of sworn testimony, the cross-examination of witnesses, the filing of briefs, the issuance of a recommended decision, the filing of exceptions, the issuance of a final decision that is voted on by affected producers, and upon approval by producers, the issuance of a final order.

equal to the period of time for which the injunction or other restraining order is effective."

<sup>2</sup> Since this proceeding was initiated on May 2, 1996, the Black Hills, South Dakota and the Tennessee Valley orders have been terminated. Effective October 1, 1996, the operating provisions of the Black Hills were terminated (61 FR 47038), and the remaining administrative provisions were terminated effective December 31, 1996 (61 FR 67927). Effective October 1, 1997, the operating provisions of the Tennessee Valley order were terminated (62 FR 47923). The remaining administrative provisions of the Tennessee Valley order will be terminated before this consolidation process is completed.

The informal rulemaking process does not require these procedures. Instead, informal rulemaking provides for the issuance of a proposed rule by the Agricultural Marketing Service, a period of time for the filing of comments by interested parties, and the issuance of a final rule by the Secretary, which would become effective if approved by the requisite number of producers in a referendum.

Full participation by interested parties is essential in the reform of Federal milk orders. The issues are too important and complex for this proposed rule to be developed without significant input from all facets of the dairy industry. The experience, knowledge, and expertise of the industry and public are integral to the development of the proposed rule. To ensure maximum public input into the process while still meeting the legislated deadline of April 4, 1999, USDA developed a plan of action and projected time line. The plan of action developed consists of three phases: *developmental*, *rulemaking*, and *implementation*.

The first phase of the plan was the *developmental* phase. The use of a *developmental* phase allowed USDA to interact freely with the public to develop viable proposals that accomplish the Farm Bill mandates, as well as related reforms. The USDA met with interested parties to discuss the reform progress, assisted in developing ideas or provided data and analysis on various possibilities, issued program announcements, and requested public input on all aspects of the Federal order program. The *developmental* phase began on April 4, 1996, and concludes with the issuance of this proposed rule.

The second phase of the plan is the *rulemaking* phase. The *rulemaking* phase begins with the issuance and publication of this proposed rule. This proposed rule provides the public 60 days to submit written comments on the proposal to USDA. These comments will be reviewed and considered prior to the issuance of a final rule.

The third and final phase of the plan is the *implementation* phase. The *implementation* phase will begin after the final rule is published in the **Federal Register**. This phase will consist of informational meetings conducted by Market Administrator personnel. The objective of the informational meetings is to inform producers and handlers about the newly consolidated orders and explain the projected effects on producers and handlers in the new marketing order areas. After informational meetings have been held, referendums will be conducted. Upon

approval of the consolidated orders and related reforms by the required number of producers in each marketing area, a final order implementing the new orders will be issued and published in the **Federal Register**.

Although all of the issues regarding Federal milk order reform are interrelated, USDA has established several committees to address specific issues. The use of committees has allowed the reform process to be divided into more manageable tasks. The committees will work throughout the *developmental* and *rulemaking* phases. The committees that have been established are: Price Structure, Basic Formula Price, Identical Provisions, Classification, and Regional. The Regional committee is divided into four sub-committees: Midwest, Northeast, Southeast, and West. Committee membership consists of both field and headquarters Dairy Programs personnel. The committees have been given specific assignments related to their designated issue and have been meeting since May 1996.

In addition to utilizing USDA personnel, partnerships have been established with two university consortia to provide expert analyses on the issues relating to price structure and basic formula price options. Dr. Andrew Novakovic of Cornell University led the analysis on price structure and published a staff paper entitled "U.S. Dairy Sector Simulator: A Spatially Disaggregated Model of the U.S. Dairy Industry" and a research bulletin entitled "An Economic and Mathematical Description of the U.S. Dairy Sector Simulator"<sup>3</sup> Dr. Ronald Knutson of Texas A&M University led the analysis on basic formula price options and published two working papers entitled "An Economic Evaluation of Basic Formula Price (BFP) Alternatives" and "The Modified Product Value and Fresh Milk Base Price Formulas as BFP Alternatives."<sup>4</sup>

### Actions Completed

USDA has maintained continual contact with the industry regarding the reform process. To begin, on May 2, 1996, the Agricultural Marketing Service (AMS) Dairy Division issued a memorandum to interested parties announcing the planned procedures for

<sup>3</sup> Copies of this report may be obtained by contacting Ms. Wendy Barrett, Cornell University, ARME, 348 Warren Hall, Ithaca, NY 14853-7801, (607) 255-1581.

<sup>4</sup> Copies of these reports may be obtained by contacting Dr. Ronald Knutson, Agricultural and Food Policy Center, Dept. of Ag. Economics, Texas A&M University, College Station, TX 77843-2124, (409) 845-5913.

implementing the Farm Bill.<sup>5</sup> In this memorandum, all interested parties were requested to submit ideas on reforming Federal milk orders, specifically as to the consolidation and pricing structure of orders. Input was requested by July 1, 1996.

On June 24, 1996, USDA issued a press release announcing that a public forum would be held in Madison, Wisconsin, on July 29, 1996. The forum would address price discovery techniques for the value of milk used in manufactured dairy products. Thirty-one Senators, Congressmen, university professors, representatives of processor and producer organizations, and dairy farmers made presentations at the forum.

On October 24, 1996, AMS Dairy Division issued a memorandum to interested parties requesting input regarding all aspects of Federal milk order reform and specifically as to its impact on small businesses. USDA anticipates that the consolidation of Federal orders will have an economic impact on handlers and producers affected by the program, and USDA wants to ensure that, while accomplishing their intended purpose, the newly consolidated Federal orders will not unduly inhibit the ability of small businesses to compete.

On December 3, 1996, AMS Dairy Division issued a memorandum to interested parties announcing the release of the preliminary report on Federal milk order consolidation. The report recommends the consolidation of the current 32 Federal milk orders into ten orders. (See Appendix A for report summary.) The memorandum requested input from all interested parties on the recommended consolidated orders and on any other aspect of the milk marketing order program by February 10, 1997.

On March 7, 1997, AMS Dairy Division issued a memorandum to interested parties announcing the release of three reports that addressed the Class I price structure, the classification of milk, and the identical provisions contained in a Federal milk order. The price structure report consisted of a summary report and a technical report and discussed several options for modifying the Class I price structure. (See Appendix B for report summary.) The classification report recommended the reclassification of certain dairy products, including the removal of Class III-A pricing for nonfat

dry milk. (See Appendix C for report summary.) The identical provisions report recommended simplifying, modifying, and eliminating unnecessary differences in Federal order provisions. (See Appendix D for report summary.) Comments on the contents of these reports, as well as on any other aspect of the program, was requested from interested parties by June 1, 1997.

On April 18, 1997, AMS Dairy Division issued a memorandum to interested parties announcing the release of the preliminary report on Alternatives to the Basic Formula Price (BFP). The report contained suggestions, ideas, and initial findings for BFP alternatives. Over eight categories of options were identified with four options recommended for further review and discussion. (See Appendix E for report summary.) The memorandum requested input from all interested parties on a BFP alternative and on any other aspect of the milk marketing order program by June 1, 1997.

On May 20, 1997, AMS Dairy Division issued a memorandum to interested parties announcing the release of a revised preliminary report on Federal milk order consolidation. The revisions were based on the input received from interested parties in response to the initial preliminary report on order consolidation. (See Appendix F for report summary.) Instead of recommending 10 consolidated orders as in the first report, the revised report recommended 11 consolidated orders and suggested the inclusion of some currently unregulated territory. The memorandum requested comments from all interested parties on the recommended consolidated orders and on any other aspect of the milk marketing order program by June 15, 1997.

To elicit further input on the role of the National Cheese Exchange price in calculating the basic formula price, on January 29, 1997, the Secretary issued a press release announcing steps being taken by USDA to address concerns raised by dairy producers about how milk prices are calculated. In the press release, the Secretary requested further comments from interested parties about the use of the National Cheese Exchange in the determination of the basic formula price, which is the minimum price that handlers must pay dairy farmers for milk used to manufacture Class III products (butter and cheese) and the price used to establish the Class I and Class II prices. These comments were requested by March 31, 1997, and have been useful in analyzing alternatives to the basic formula price in context of the order reform process.

### *Public Interaction*

As a result of these announcements and the forum, more than 1,600 individual comments have been received by USDA. In addition to the individual comments, more than 3000 form letters have been received. All comments were reviewed by USDA personnel and are available for public inspection at USDA. To assist the public in accessing the comments, USDA contracted to have the comments scanned and published on a CD. The use of this technology has allowed interested parties throughout the United States access to the information received by USDA.

USDA also made all publications and requests for information available on the Internet. A separate page under the Dairy Division section of the AMS Homepage was established to provide information about the reform process. To assist in transmitting correspondence to USDA, a special electronic mail account—Milk\_Order\_Reform@usda.gov—was opened to receive input on Federal milk order reforms.

USDA personnel met continually with interested parties from May 1996 through the issuance of this proposed rule to gather information and ideas on the consolidation of Federal milk orders. During this time period, USDA personnel addressed over 250 groups comprised of more than 22,000 individuals on various issues related to Federal order reform.

USDA personnel also conducted in-person briefings for both the Senate and House Agricultural Committees on the progress of Federal milk order reforms. Since May 1996, seven briefings were conducted for the committees. The briefings advised the committees of the plan of action for implementing the Farm Bill mandates; explained the preliminary report on the consolidation of Federal milk orders; explained the contents of the reports addressing Class I price structure, classification of milk, identical provisions and basic formula price; and discussed the congressional report.

### *Public Input*

To ensure the involvement of all interested parties, particularly small businesses as defined in the following Initial Regulatory Flexibility Analysis, in the process of Federal order reform, three primary methods of contact have been used: direct written notification, publication of notices through various media forms, and speaking and meeting with organizations and individuals regarding the issue of Federal order

<sup>5</sup> Copies of this announcement and all subsequent announcements and reports can be obtained from Dairy Programs at (202) 720-4392, any Market Administrator office, or via the Internet at <http://www.ams.usda.gov/dairy/>.

reforms. In addition, information has been made available to the public via the Internet. USDA also made one written program announcement specifically requesting information from small businesses.

All announcements made by USDA have been mailed to over 20,000 interested parties, State Governors, State Department of Agriculture Secretaries or Commissioners, and the national and ten regional Small Business Administration offices. In addition, most dairy producers under the orders were notified through regular market service bulletins published by Market Administrators on a monthly basis. Press releases were issued by USDA for the May 2, 1996, December 3, 1996, January 29, 1997, March 7, 1997, and May 20, 1997, announcements, and for the July 31, 1996, public forum.<sup>6</sup> These press releases were distributed to approximately 33 wire services and trade publications and to each State Department of Agriculture Communications Officer. These methods of notification helped to ensure that virtually all identified small businesses were contacted.

Departmental personnel, both in the field and from Washington, actively met with interested parties to gather input and to clarify and refine ideas already submitted. Formal presentations, round table discussions, and individually scheduled meetings between industry representatives and Departmental personnel were held. Over 250 organizations and more than 22,000 individuals were reached through this method. Of these individuals, approximately 13,400 were identified as small businesses.

As a result of the requests for information, publication of informational reports, meetings with interested parties, and the comments, AMS has prepared this proposed rule which contains proposals addressing the following issues: the consolidation of marketing areas; basic formula price replacement and other class price issues; Class I price structure; classification of milk; provisions applicable to all orders; regional issues relating to the Northeast, Southeast, Midwest, and Western areas; and various other miscellaneous and administrative issues. Each proposal is discussed in detail following this preliminary statement that includes Executive Order 12988 and 12866 discussions, the Regulatory Flexibility

Analysis, and the Paperwork Reduction Analysis.

#### *Executive Order 12988*

This proposed rule has been reviewed under Executive Order 12988, Civil Justice Reform. This rule is not intended to have a retroactive effect. If adopted, this proposed rule will not preempt any state or local laws, regulations, or policies, unless they present an irreconcilable conflict with the rule.

The Agricultural Marketing Agreement Act of 1937, as amended (7 U.S.C. 601–674), provides that administrative proceedings must be exhausted before parties may file suit in court. Under section 608c(15)(A) of the Act, any handler subject to an order may request modification or exemption from such order by filing with the Secretary a petition stating that the order, any provision of the order, or any obligation imposed in connection with the order is not in accordance with law. A handler is afforded the opportunity for a hearing on the petition. After a hearing, the Secretary would rule on the petition. The Act provides that the district court of the United States in any district in which the handler is an inhabitant, or has its principal place of business, has jurisdiction in equity to review the Secretary's ruling on the petition, provided a bill in equity is filed not later than 20 days after the date of the entry of the ruling.

#### *Executive Order 12866*

The Department is issuing this proposed rule in conformance with Executive Order 12866. This proposed rule has been determined to be economically significant for the purposes of Executive Order 12866. When proposing a regulation which is determined to be economically significant, agencies are required, among other things, to: assess the costs and benefits of available regulatory alternatives; base regulatory decisions on the best reasonably-obtainable technical, economic, and other information; avoid duplicative regulations; and tailor regulations to impose the least burden on society consistent with obtaining regulatory objectives. Therefore, to assist in fulfilling the objectives of Executive Order 12866, the USDA prepared an initial Regulatory Impact Analysis (RIA). Information contained in the RIA pertaining to the costs and benefits of the revised regulatory structure are summarized in the following analysis. Copies of the RIA can be obtained from Dairy Programs at (202) 720-4392, any Market Administrator office, or via the

Internet at <http://www.ams.usda.gov/dairy>.

This rule proposes the consolidation of the current 31 Federal milk marketing order areas into 11 marketing order areas. The proposed marketing areas are: Northeast, Mideast, Upper Midwest, Central, Appalachian, Southeast, Florida, Southwest, Arizona-Las Vegas, Western, and Pacific Northwest. The consolidated marketing areas consist primarily of territory that is in the current Federal order markets. In addition, they would include some previously unregulated territory. At this time, California is not proposed as a Federal order. This consolidation is proposed to comply with the 1996 Farm Bill that mandates the current Federal milk order marketing areas be consolidated into between 10 to 14 marketing areas by April 4, 1999. This proposed rule also sets forth two options for consideration as a replacement for the Class I price structure and proposes replacing the basic formula price with a multiple component pricing system. These changes are proposed to address concerns that the current system of pricing Class I milk may not adequately reflect the value of Class I milk at various locations or the value of milk used in manufacturing products. The 1996 Farm Bill identified these as related issues that may be addressed in the consolidation of milk marketing orders. The proposed rule further proposes changes to classification of milk by establishing a new Class IV which would include milk used to produce nonfat dry milk, butter, and other dry milk powders; the reclassification of eggnog and cream cheese; and other minor changes. These proposed changes should improve handler reporting and accounting procedures thereby providing for greater market efficiencies. Finally, this proposed rule expands Part 1000 to include provisions that are identical within each consolidated order to assist in simplifying the orders. These provisions include the definitions of route disposition, plant, distributing plant, supply plant, nonpool plant, handler, other source milk, fluid milk product, fluid cream product, cooperative association, and commercial food processing establishment. In addition, the milk classification section, pricing provisions, and most of the provisions relating to payments have been included in the General Provisions. These proposed changes adhere with the efforts of the National Performance Review—Regulatory Reform Initiative to simplify, modify,

<sup>6</sup> Copies of these press releases may be obtained from Dairy Programs at (202) 720-4392, or via the Internet at <http://www.ams.usda.gov/news/newsrel.htm>.

and eliminate unnecessary repetition of regulations. Unique regional issues or marketing conditions have been considered and included in each market's order provisions. Not all of these changes would be considered economically significant; however, changes dealing with marketing area consolidation, the basic formula price, and the Class I pricing structure may be significant and are described further in the following sections.

Economic Impacts of Consolidation

It is impossible to determine the economic effects of the proposed marketing area consolidation on handlers, producers and consumers without using assumptions about the specific order provisions contained in the consolidated order areas. The only effect consolidation, as a single factor, can have on the various market participants is its effect on the percentage of milk used in different classes within the proposed consolidated orders. Without assumptions that include the specific class prices and milk uses in different products, there are no means of

quantifying the economic effects of consolidation.

Handlers would be affected by class prices, which would be determined by the Class I price surface option that is selected, and by the minimum prices contained in all of the orders for milk used in Classes II, III and IV. Handlers similarly located would be subject to the same minimum Class I, Class II, Class III and Class IV prices for milk. Such handlers would also be subject to the same minimum prices to be paid to producers.

Dairy farmers would be affected by the proposed consolidation of marketing areas because changes in utilization percentages would result in changes in blend prices. As in the case of effects on handlers, however, it is impossible to accurately determine a separate consolidation effect on producers, defined in monetary terms. The closest approximation to such an estimate would be the "weighted average utilization value" (WAUV). These "prices" reflect only the change in value that can be attributed to changes in utilization rates, with no assumptions about changes in the levels of the

various class prices. Such estimates, of necessity, would reflect only anticipated changes in blend prices, using class prices that would no longer be in effect under the consolidated orders. To the extent that the WAUV computations reflect some of the effect of the effect of consolidation on producer prices, they are included in this analysis. It should be noted, however, that all producers in any given current area would be affected to an equal extent by the consolidation factor.

The following table shows the potential impact of three order consolidation options on producers who supply each of the current Federal milk marketing order areas via WAUV "prices". The three consolidated options are (1) the consolidated marketing areas suggested in the December 1996 initial Preliminary Report on Order Consolidation; (2) the consolidated marketing areas suggested in the May 1997 Revised Preliminary Report on Order Consolidation; and (3) the consolidated marketing areas suggested in this proposed rule.

WEIGHTED AVERAGE UTILIZATION VALUES (WAUV)  
[Based on October 1995 information]

Consolidated Market	Marketing areas in Initial Consol. Report (Dec. 96) (Option 1)		Marketing Areas in Revised Consol. Report (May 97) (Option 2)		Marketing Areas in Proposed Rule (Option 3)	
	Consol. Mkt. WAUV (\$/cwt)		Consol. Mkt. WAUV (\$/cwt)		Consol. Mkt. WAUV (\$/cwt)	
Current Markets	WAUV using Current Mkt. Utilization (\$/cwt)	WAUV using Consol. Mkt. Utilization (\$/cwt)	WAUV using Current Mkt. Utilization (\$/cwt)	WAUV using Consol. Mkt. Utilization (\$/cwt)	WAUV using Current Mkt. Utilization (\$/cwt)	WAUV using Consol. Mkt. Utilization (\$/cwt)
	Northeast .....		\$13.46		\$13.48	
New England (F.O. 1) .....	\$13.50	13.48	\$13.52	13.51	\$13.52	13.49
NY-NJ (F.O. 2) .....	13.44	13.48	13.48	13.50	13.45	13.48
Middle Atlantic (F.O. 4) .....	13.45	13.39	13.45	13.41	13.44	13.40
Appalachian .....		14.13		13.96		13.97
Carolina (F.O. 5) .....	14.23	14.21	14.23	14.19	14.23	14.20
Tenn. Valley (F.O. 11) .....	13.92	13.95	13.92	13.93	13.92	13.94
Lville-Lex-Evan (F.O. 46) .....	n/a	n/a	13.35	13.39	13.35	13.40
Florida .....		15.05		15.05		15.05
Upper Florida (F.O. 6) .....	14.67	14.78	14.67	14.78	14.67	14.78
Tampa Bay (F.O. 12) .....	15.09	15.04	15.09	15.04	15.09	15.04
SE Florida (F.O. 13) .....	15.42	15.31	15.42	15.31	15.42	15.31
Southeast .....		14.26		14.25		14.24
Southeast (F.O. 7) .....	14.26	14.26	14.25	14.25	14.24	14.27
Mideast .....		12.96		12.94		12.92
Ohio Valley (F.O. 33) .....	12.99	13.02	12.99	13.01	12.99	13.00
E. Ohio-W. PA (F.O. 36) .....	13.07	13.00	13.10	12.99	13.07	12.97
S. Michigan (F.O. 40) .....	12.75	12.86	12.75	12.84	12.75	12.83
MI Upper Penin. (F.O. 44) .....	12.81	12.62	12.81	12.62	12.81	12.61
Lville-Lex-Evan (F.O. 46) .....	13.35	13.06	n/a	n/a	n/a	n/a
Indiana (F.O. 49) .....	12.97	12.94	12.97	12.93	12.97	12.92
Upper Midwest .....		12.60		12.62		12.60
Chicago Reg. (F.O. 30) .....	12.62	12.62	12.62	12.61	12.62	12.62
MI Upper Penin. (F.O. 44) .....	R	R	R	R	R	R
Neb.-W. Iowa (F.O. 65) .....	n/a	n/a	12.63	12.74	n/a	n/a
Upper Midwest (F.O. 68) .....	12.55	12.56	12.55	12.54	12.55	12.56
E. South Dakota (F.O. 76) .....	n/a	n/a	12.81	12.65	n/a	n/a
Iowa (F.O. 79) .....	n/a	n/a	12.69	12.67	n/a	n/a

## WEIGHTED AVERAGE UTILIZATION VALUES (WAUV)—Continued

[Based on October 1995 information]

Consolidated Market	Marketing areas in Initial Consol. Report (Dec. 96) (Option 1)		Marketing Areas in Revised Consol. Report (May 97) (Option 2)		Marketing Areas in Proposed Rule (Option 3)	
	Consol. Mkt. WAUV (\$/cwt)		Consol. Mkt. WAUV (\$/cwt)		Consol. Mkt. WAUV (\$/cwt)	
Current Markets	WAUV using Current Mkt. Utilization (\$/cwt)	WAUV using Consol. Mkt. Utilization (\$/cwt)	WAUV using Current Mkt. Utilization (\$/cwt)	WAUV using Consol. Mkt. Utilization (\$/cwt)	WAUV using Current Mkt. Utilization (\$/cwt)	WAUV using Consol. Mkt. Utilization (\$/cwt)
	Central .....		13.16		13.21	
S. IL-E. MO (F.O. 32) .....	12.93	12.90	13.00	12.95	13.00	12.88
Central IL (F.O. 50) .....	13.03	12.74	13.03	12.78	13.03	12.72
Greater K. City (F.O. 64) .....	13.22	12.90	13.22	12.95	13.22	12.88
Neb.-W. Iowa (F.O. 65) .....	12.63	12.81	n/a	n/a	12.63	12.79
E. South Dakota (F.O. 76) .....	12.81	12.68	n/a	n/a	12.81	12.67
Iowa (F.O. 79) .....	12.71	12.71	n/a	n/a	12.71	12.70
SW Plains (F.O. 106) .....	13.31	13.33	13.31	13.41	13.08	13.29
E. Colorado (F.O. 137) .....	13.27	13.31	13.27	13.38	13.27	13.27
Southwest .....		13.36		13.39		13.39
Texas (F.O. 126) .....	13.49	13.48	13.49	13.46	13.49	13.46
Central AZ (F.O. 131) .....	13.26	13.17	n/a	n/a	n/a	n/a
NM-W. Texas (F.O. 138) .....	13.00	13.09	13.00	13.07	13.00	13.07
Arizona-Las Vegas .....		n/a		13.26		13.26
Central AZ (F.O. 131) .....	n/a	n/a	13.26	13.29	13.26	13.29
Western .....		12.79		12.78		12.78
W. Colorado (F.O. 134) .....	13.41	12.84	13.41	12.82	13.41	12.82
SW ID-E. OR (F.O. 135) .....	12.63	12.68	12.63	12.68	12.63	12.68
Great Basin (F.O. 139) .....	12.83	12.81	12.81	12.79	12.81	12.79
Pacific Northwest .....		12.45		12.44		12.44
Pacific NW (F.O. 124) .....	12.45	12.45	12.44	12.44	12.44	12.44

n/a: Not applicable  
R: Restricted

For each option, a weighted average use value (WAUV) is computed for (a) the consolidated order; (b) the current order with current use of milk; and (c) the current order with projected use of milk in the consolidated order. The difference between the weighted average use values in (b) and (c) represents the potential impact on producers.

For example, in this proposed rule, the New England (F.O. 1) market's WAUV using its current utilization is \$13.52 per cwt. When the three markets are consolidated and the new consolidated utilization is used to calculate the WAUV, New England's WAUV would be \$13.49 per cwt. In this comparison, the potential impact on producers supplying the New England market area would be a decrease of three cents per cwt.

Each of the three options assumes the pool distributing plant standards suggested for each of the consolidated orders in this proposed rule; thus the calculated values in the preceding table are not directly comparable to the WAUV values published with either the initial or the revised reports on order consolidation.

#### Economic Impact of Basic Formula Price Proposal

A number of options for determining a basic formula price were considered and analyzed in the process of developing the proposed basic formula price (BFP). In addition to the proposed method of pricing components based on their value in manufactured products, other options examined by both the Agricultural Marketing Service's *Basic Formula Price Replacement Committee*<sup>7</sup> and the *University Study Committee* (USC), led by Dr. Ronald D. Knutson of Texas A & M University, were: economic formulas, futures markets, cost of production, competitive pay pricing, and pricing differentials only.

Descriptions of the two Committees' analyses, and results of their work are included in "A Preliminary Report on Alternatives to the Basic Formula Price," published in April 1997 by the Basic Formula Price Committee, Dairy

<sup>7</sup>The Basic Formula Price Committee was established in May 1996 to consider replacements for the basic formula price during the Federal order reform process. This committee and others established are described further in the "Background" portion of this proposed rule.

Division, AMS;<sup>8</sup> and the following reports from the Agricultural and Food Policy Center, Texas A&M University System:

"An Economic Evaluation of Basic Formula Price (BFP) Alternatives," AFPC Working Paper 97-2, June 1997.

"Evaluation of Final Four Basic Formula Price Options," AFPC Working Paper 97-9, August 1997.<sup>9</sup>

The primary criterion used by the BFP Committee was that any replacement BFP option reflect the supply of and demand for milk used in manufactured dairy products. At the same time, one of the USC's critical criteria for a replacement BFP was that it reliably reflect market conditions for all manufactured products.

In trying to determine the most appropriate replacement for the current BFP, which uses a survey of prices paid by manufacturing plants for non-Grade A milk updated by a product price

<sup>8</sup>Copies of this report can be obtained from Dairy Programs at (202) 720-4392, any Market Administrator office, or via the Internet at <http://www.ams.usda.gov/dairy/>.

<sup>9</sup>Copies of these reports may be obtained by contacting Dr. Ronald Knutson, Agricultural and Food Policy Center, Dept. of Ag. Economics, Texas A&M University, College Station, TX 77843-2124, or (409) 845-5913.

formula, the goal of both groups was a market-based alternative. The BFP Committee measured the extent to which each pricing option met its primary goal by tracking the options against the current BFP for a period of prior months.<sup>10</sup> The USC Committee used an econometric procedure to test the ability of the alternatives they considered to reflect supply and demand.

To the extent the goal of identifying a BFP that reflects the value of milk used in manufactured products is capable of attainment, all market participants—handlers, producers, and consumers—would be affected by the BFP replacement in the same manner as if they were operating in a free market, with no external impacts caused by regulation. Consumers can be assured that the prices generally charged for dairy products are prices that reflect, as closely as possible, the forces of supply and demand in the market.

Of the options considered and analyzed, both groups studying the issue determined that the option of pricing components of milk according to their value in manufactured products, as reflected by the sales prices of those products, best approximates the intersection of supply and demand for milk used in manufactured dairy products.

#### Economic Impact of Multiple Component Pricing Provisions

Seven of the 11 proposed orders provide for milk to be paid for on the basis of its components (multiple component pricing, or MCP). Five of the 7 MCP orders also provide for milk values to be adjusted according to the somatic cell count of producer milk. The equipment needed for testing milk for its component content can be very expensive to purchase, and requires highly-skilled personnel to maintain and operate. The cost of infra-red analyzers ranges from just under \$100,000 to \$200,000. The infra-red machines that are used by most laboratories will test for total solids and somatic cells at the same time the butterfat and protein tests are done.

Some additional information is necessary from handlers on their monthly reports of receipts and utilization to assure that producers are paid correctly. In particular, handlers would be required to report pounds of protein, pounds of other solids, and, in 5 of the orders, somatic cell information. This data would be required from each

handler for all producer receipts, including milk diverted by the handler, receipts from cooperatives as handlers pursuant to § 1000.9(c), and, in some cases, receipts of bulk milk received by transfer or diversion.

Since producers would be receiving payments based on the component levels of their milk, the payroll reports that handlers supply to producers must reflect the basis for such payment. Therefore, the handler would be required to supply the producer not only with the information currently supplied, but also: (a) the pounds of butterfat, the pounds of protein, and the pounds of other solids contained in the producer's milk, as well as the producer's average somatic cell count; and (b) the minimum rates that are required for payment for each pricing factor and, if a different rate is paid, the effective rate also. It should be noted that handlers already are required to report information relative to pounds of production, butterfat, and rates of payment for butterfat and hundredweight of milk.

Of over 74,000 producers whose milk was pooled in December 1996 under 23 orders that would be part of consolidated orders providing for multiple component pricing, the milk of 52,500 of these producers was pooled under 13 orders that currently have MCP. Handlers in these markets already have incurred the initial costs of testing milk for its component content and have already made the needed transition to reporting the additional information required for component pricing of milk.

Of the remaining 21,750 producers who would be affected by MCP provisions under a Federal order, the milk of approximately 13,000 of these producers currently is received by handlers who test or have the capability of testing for multiple components and, in many cases, somatic cells. Many of these handlers also report component results to the producers with their payments. Almost all of the producers whose milk currently is not being tested or paid for on the basis of components are located in the New England and New York-New Jersey marketing areas, which would be consolidated with the Middle Atlantic area into the proposed Northeast order.

Accommodation has been made to ameliorate handlers' expenses of testing producer milk for component content. As component pricing plans have been adopted under a number of the present Federal milk orders since 1988, the component testing needed to implement these pricing plans has been performed by the market administrators responsible for the administration of the

orders involved for handlers who are not equipped to make all of the determinations required under the amended orders. This policy would continue under this proposed rule. Thus, handlers who are unable to obtain the equipment and personnel needed to accomplish the required testing for component pricing would be able to rely on the market administrators to verify or establish the tests under which producers are paid.

#### Economic Impacts of Class I Price Changes

Several different options were considered for pricing fluid or Class I milk. These pricing options included using a market-driven basic formula price plus differentials based on location, differentials based on the ratio of milk used for fluid purposes compared to all other uses, flat differentials, flat differentials modified in high Class I use areas, and differentials based on the demand for fluid milk within a designated marketing area and the associated transportation costs. Other options considered would have decoupled Class I pricing from the basic formula price or pooled Class I differentials only (i.e., eliminated the basic formula price entirely). Finally, suggestions were considered to base Class I pricing on the cost of production and to base differentials on only regional supply and demand conditions. After analyzing these options and more than 1400 letters that were submitted from interested persons, the Department narrowed the pricing options to four and conducted extensive quantitative and qualitative analysis on them. The four options selected include location-specific differentials, relative value-specific differentials, and decoupled Class I prices with adjustors. Although four Class I price structure options are analyzed in the RIA, only two options are considered as viable replacements for the current Class I price structure in the proposed rule. However, comments are requested on all options prior to determining which option should be adopted.

Three of the four pricing options in the RIA assume that milk would be classified in the four classes of use detailed in the proposed rule. One option in the RIA has only two classes of milk and thus is not detailed in the proposed rule. For purposes of the RIA analysis, Class IV milk is priced using the proposed butter-nonfat dry milk product formula, but since the product prices proposed for use in the formula are not presently available, the Chicago Mercantile Exchange spot price for

<sup>10</sup>It was assumed that the current BFP successfully reflects the supply and demand for milk used in manufactured products.

butter and the average nonfat dry milk wholesale price reported by USDA's Dairy Market News for the Western States are substituted. Also, Class III milk is priced using the proposed cheese product formula, and the Class II milk price for the month is equal to the Class IV price for the month plus 70 cents per hundredweight (cwt).

The initial RIA assesses costs and benefits for dairy farmers, fluid milk processors, dairy product manufacturers, and consumers. The impact of each of the four Class I pricing options is measured as a change from a baseline. The model baseline was adapted from the USDA dairy baseline estimate published as part of the President's Budget for Fiscal Year 1998.<sup>11</sup> That baseline, which is a national annual projection of the supply-demand-price situation for milk and dairy products, was the basis for the market-by-market baseline of the model. Both the President's Budget Baseline and the model baseline assume the same program assumptions: namely, that the price support program will be phased out by December 31, 1999, that the Dairy Export Incentive Program will continue to be utilized, and that the Federal Milk Order Program will be continued at the same level of class prices currently in existence.

Assumptions also are made concerning the cost of production—especially feed, the commercial utilization of milk and dairy products, commercial inventories, and imports. All parameters, except those associated with the changes in the Federal Milk Order Program, are assumed to remain unchanged.

To evaluate the impacts on dairy farmers, fluid milk processors, and dairy product manufacturers of the four selected Class I pricing options, a baseline estimate was constructed assuming that the current 32 orders<sup>12</sup> would continue through the study period, 1999–2004. To make comparisons, proposed pricing points for the proposed 11 consolidated orders were identified to correspond with the base pricing zones of the 32 current marketing orders. For example, for the consolidated Appalachian Region order,

which would have the city of Charlotte as its base pricing point, prices also were identified for Knoxville and Louisville. These 3 pricing points correspond with the base pricing points of the 3 markets that are to be combined into the Appalachian regional order.

#### Location-Specific Differentials (Option 1A) Analysis

This option would establish a nationally coordinated system of location-specific Class I price differentials reflecting the relative economic value of milk by location. An important feature of the option is that it would also include location adjustments that geographically align minimum Class I milk prices paid by fluid milk processors nationwide regardless of defined milk marketing area boundaries or order pooling provisions. It is based on the economic efficiency rationale presented in Cornell University research on the U.S. dairy sector.<sup>13</sup> A basic premise of this option is that the value of milk varies according to location across the United States. The concepts of spatial price value and relative price relationships together with marketing data and expert knowledge of local conditions and marketing practices and a review of supply and demand conditions are used to develop a national Class I price structure.

Overall, the magnitude of changes in price and income under this option compared to the baseline are small. The all-milk price for all Federal order markets combined during the 1999–2004 period is estimated to average 5 cents per cwt higher. For all of the U.S. the all-milk price is estimated to average 3 cents higher. The average all-milk price at the basing point of 18 current markets could experience increases of 1 to 29 cents per cwt. At the basing point of the 13 markets, the average all-milk price could decrease from 3 to 83 cents per cwt.

The 5 markets with the greatest increases in all-milk prices were Eastern Colorado (\$0.29), New York-New Jersey (\$0.28), Tampa Bay (\$0.26), Southwest Plains (\$0.25), and Upper Florida (\$0.24). The market with the greatest reduction in price was Western Colorado (–\$0.83), Central Illinois (–\$0.66), Greater Kansas City (–\$0.53), Eastern South Dakota (–\$0.51), and Southern Illinois-Eastern Missouri

(–\$0.34). The annual average all-milk price in the previously-unregulated areas of New York and New England declined \$0.87 per cwt.

Changes in gross cash receipts, as expected, moved in the same direction as the change in the all-milk price in a given market. Over the period 1999–2004, location-specific differentials raised gross receipts in 18 markets. It appears that the estimated average annual receipts for producers in the current New York-New Jersey market increased by \$37.2 million. However, most of this increase was the result of adding to the all-milk price the current \$0.15 reduction on all milk marketings for transportation. It is expected that this apparent increase in the all-milk price and dairy farmer income would be offset by a like amount by increased transportation costs paid by the producer. The markets with the greatest estimated increase in gross receipts for milk marketing were Southwest Plains (\$11.8 million), Chicago Regional (\$10.9 million), Southern Michigan (\$10.7 million), New England (\$7.4 million), and Eastern Colorado (\$7.2 million). Gross receipts in the current Chicago Regional and Upper Midwest markets may have been expected to increase more since this option increased the Class I differentials at those points substantially. However, this option also envisions the expansion of transportation credits within the merged order to move milk which is expected to use 20 percent of the dollars generated by the higher Class I differentials. Over-order charges which currently fund transportation credits are expected to be reduced by a like amount.

The largest estimated decreases in cash receipts occur in the Southern Illinois-Eastern Missouri (–\$8.5 million), Great Basin (–\$4.1 million), Middle Atlantic (–\$2.9 million), Texas (–\$2.5 million), and Greater Kansas City (–\$2.5 million) markets. Nine other current markets would lose average annual gross cash receipts during the period 1999–2004 of less than \$2.0 million each. The previously unregulated areas of New York and New England would lose an estimated average of \$16.9 million in annual gross receipts from milk marketings. Under location-specific differentials the estimated average annual gross receipts for all Federal order markets combined increased by \$68.1 million and the entire US increased \$53.1 million compared to the baseline for the 1999–2004 period.

Fluid processors in 21 of the 32 Federal order market areas face increased Class I differentials if this

<sup>11</sup> See *Agricultural Baseline Projections to 2005, Reflecting the 1996 Farm Act*, Interagency Agricultural Projections Committee, U.S. Department of Agriculture, Office of the Chief Economist, World Agricultural Outlook Board, Staff Report, WAOB-97-1 and "Budget of the United States Government, Fiscal Year 1998."

<sup>12</sup> The following analyses were completed prior to the termination of the Tennessee Valley marketing order and thus the results identify it as a pricing point. Most of the plants and milk of the former Tennessee Valley market have become regulated under either the Southeast order or the Carolina order.

<sup>13</sup> Bishop, Phillip, James Pratt, Eric Erba, Andrew Novakovic, and Mark Stephenson, *An Economic and Mathematical Description of the U.S. Dairy Sector Simulator*, Research Bulletin 97-09, A Publication of the Cornell Program on Dairy Markets and Policy, Department of Agricultural, Resource, and Managerial Economics, Cornell University, July 1997.

option were adopted compared with Class I differentials under the baseline. Fluid processors in four of the Federal order markets and in the previously-unregulated areas of New York and New England would see no changes in Class I differentials. Fluid processors in the remaining seven Federal order markets would see decreases in Class I differentials compared with the baseline. The increases in differentials ranged from \$0.01 per cwt in the New England and New York-New Jersey markets to \$0.50 per cwt in the Upper Midwest. Decreases in Class I differentials would range from \$0.03 per cwt in the Middle Atlantic to \$0.25 per cwt in New Mexico-West Texas. Those fluid processors facing higher Class I differentials would see their monthly obligations to the markets' producer-settlement funds increase while those facing lower Class I differentials would see their obligations decrease.

With virtually no change in the amount of milk available for manufacturing, manufacturers of dairy products would face nearly the same supply and demand conditions that they now face when buying milk or selling dairy products. Manufacturers in the Southwest, where milk marketings are expected to decline, may have less milk to process while manufacturers in the Upper Midwest may find that they have slightly more milk for manufacturing.

#### Relative Value-Specific Differentials (Option 1B) Analysis

Like a location-specific differential structure, a relative value-specific differential structure would also establish a nationally coordinated system of Class I price differentials and adjustments that recognizes several low pricing areas. Option 1B relies on a least cost optimal solution from the USDSS model to develop a Class I price structure that is based on the most efficient assembly and shipment of milk and dairy products to meet all market demands for milk and its products. Option 1B relies more on the market and the negotiating ability of processors and producers to generate higher prices when needed to provide the necessary incentive to move milk in order to satisfy demand.

Three methods of phasing into the Class I differentials under Option 1B were evaluated. First, a 20-percent gradual phase-in was analyzed; then, a transitional phase-in that would offset any lost revenue was analyzed; and finally, a revenue-enhancement phase-in that would add additional revenue into the Class I price structure was analyzed.

#### Phase-in Method 1

With the gradual phase-in, the estimated all-milk price for all Federal order markets combined during the 1999–2004 period could average 8 cents per cwt lower than the baseline. The estimated average all-milk price at the basing point of 11 Federal order markets could increase from 1 to 32 cents per cwt. At the basing point of the other 21 Federal order markets, the all-milk price is estimated to decrease from 1 to 58 cents per cwt.

The 5 markets with the greatest estimated increases in average all-milk prices, for the 1999–2004 period are: New Mexico-West Texas (\$0.32), Chicago Regional (\$0.19), Tampa Bay (\$0.19), Nebraska-Western Iowa (\$0.17), and Southwest Idaho-Eastern Oregon (\$0.15). The 5 Federal order markets with the greatest estimated reductions in price are: Eastern South Dakota (–\$0.58), Michigan Upper Peninsula (–\$0.55), Western Colorado (–\$0.55), Greater Kansas City (–\$0.53), and Carolina (–\$0.46). The annual average all-milk price in the previously unregulated areas of New York and the New England states is estimated to decline by \$0.96 per cwt compared to the baseline.

Over the period 1999–2004, 1B differentials could lower producer gross cash receipts from minimum order prices in 21 of the Federal order markets. The five current markets that would have the greatest decreases were: Texas (–\$36.8 million), Middle Atlantic (–\$26.2 million), Upper Midwest (–\$15.9 million), Carolina (–\$15.2 million), and Southeast (–\$12.5 million). The annual average reduction in estimated gross receipts in the previously unregulated areas of New York and the New England states is estimated at \$18.5 million from the baseline. Estimated gross receipts increased in 11 markets. The five markets that would have the greatest increases in gross receipts were: Chicago Regional (\$31.5 million), New Mexico-West Texas (\$9.1 million), Southern Michigan (\$6.6 million), Southwestern Idaho-Eastern Oregon (\$5.8 million), and New York-New Jersey (\$5.3 million).

#### Phase-in Method 2

A possible modification to the relative value-specific differentials would be to initially raise Class I differentials by 55 cents per cwt above the level called for in the first year of transition. During the second year, Class I differentials would be set at 35 cents above the transition level; the third year, 20 cents above; and the fourth year, 10 cents above the

called-for transition differentials. At the beginning of the fifth year, Class I differentials would be fully phased in and no assistance provided.

Under this phase-in method, the estimated all-milk price for all Federal order markets combined during the 1999–2004 period could average 4 cents per cwt lower than the baseline. The estimated average all-milk price at the basing point of 12 Federal order markets could increase from 3 to 36 cents per cwt. At the basing point of 20 Federal order markets, the all-milk price is estimated to decrease from 2 to 53 cents per cwt from the baseline.

The five markets with the greatest estimated increases in average all-milk prices, per cwt, for the 1999–2004 period are: New Mexico-West Texas (\$0.36), Tampa Bay (\$0.32), Nebraska-Western Iowa (\$0.22), Upper Florida (\$0.20), and Chicago Regional (\$0.23). The five markets with the greatest estimated reductions in price are: Eastern South Dakota (–\$0.53), Western Colorado (–\$0.52), Michigan Upper Peninsula (–\$0.49), Greater Kansas City (–\$0.48), and Texas (–\$0.34). The annual average all-milk price in the previously unregulated areas of New York and the New England states is estimated to decline by \$0.93 per cwt compared to the baseline.

Over the period 1999–2004, this phase-in option would lower estimated producer gross cash receipts attributable to minimum order prices in 19 of the Federal order markets. The 5 markets with the greatest estimated decreases were Texas (–\$32.6 million), Middle Atlantic (–\$22.8 million), Upper Midwest (–\$13.9 million), Carolina (–\$10.7 million), and Arizona-Las Vegas (–\$7.6 million). The annual average reduction in estimated gross receipts in the previously unregulated areas of New York and the New England states is \$17.8 million lower than the baseline. Gross receipts from milk marketings could increase in the following markets: Chicago Regional (\$34.4 million), New York-New Jersey (\$11.7 million), Southern Michigan (\$10.4 million), New Mexico-West Texas (\$10.4 million), and Tampa Bay (\$7.0 million). Total estimated cash receipts for the combined current Federal orders would average \$40 million less for the 6-year period.

#### Phase-in Method 3

Another phase-in option would enhance prices during the transition period by \$1.10 for first year phase-in differentials, \$0.70 in the second year, \$0.40 in the third year, and \$0.20 in the fourth year. The additional price enhancement provided to dairy farmers

under this method is intended to help producers make the necessary investments and other changes to compete in a more market-oriented economy. At the beginning of the fifth year, Class I differentials would be fully phased in at the Option 1B levels.

With the use of additional revenue under this phase-in option, the estimated all-milk price for all Federal order markets combined during the 1999–2004 period could be expected to be unchanged from the baseline. The estimated average all-milk price at the basing point of 15 Federal order markets would increase from 1 to 43 cents per cwt. At the basing point of the other 17 Federal order markets, the all-milk price is estimated to decrease from 3 to 52 cents per cwt.

The five markets with the greatest estimated increases in average all-milk prices, per cwt, for the 1999–2004 period were: Tampa Bay (\$0.43) New Mexico-West Texas (\$0.41), Upper Florida (\$0.32), Nebraska-Western Iowa (\$0.26), and South Eastern Florida (\$0.26). The five markets with the greatest estimated reductions in price were: Western Colorado (–\$0.52), Eastern South Dakota (–\$0.49), Greater Kansas City (–\$0.44), Michigan Upper Peninsula (–\$0.43), and Texas (–\$0.33). The annual average all-milk price in the previously unregulated areas of New York and the New England states is estimated to decline by \$0.88 per cwt compared to the baseline. Total estimated cash receipts for the combined current Federal order markets would average \$34.9 million higher for the 6-year period.

Over the period 1999–2004, this phase-in option could lower estimated producer gross cash receipts from milk marketings in 16 of the current markets. The five current markets with the greatest decreases were: Texas (–\$28.2 million), Middle Atlantic (–\$19.0 million), Upper Midwest (–\$14.6 million), Carolina (–\$6.5 million) and Arizona-Las Vegas (–\$6.0 million). The annual average reduction in estimated gross receipts in the previously unregulated areas of New York and the New England states is estimated at \$16.9 million from the baseline. Gross receipts from milk marketings increased in 16 markets. The five markets that would have the greatest increases were: Chicago Regional (\$33.5 million), New York-New Jersey (\$19.0 million), Southern Michigan (\$14.4 million), New Mexico-West Texas (\$11.7 million), and Tampa Bay (\$9.8 million).

#### Decoupled Baseline Class I Price with Adjustors (Option 5) Analysis

A third option analyzed in the RIA would retain the current Class I differentials, but floor Class I prices in all markets at their 1996 average levels. Adjustments to this price would be made based on changes in fluid use rates and short term costs of production (i.e., feed costs). Under this option, the all-milk price for all Federal order markets combined would increase \$0.07 per cwt and the U.S. is projected to increase \$0.03 per cwt over the 6-year period. In 19 of the Federal order markets, the average all-milk price would be higher by \$0.01 to \$0.50 per cwt. In 12 Federal order markets, the average all-milk price would decrease from \$0.03 to \$0.82 per cwt.

Flooring the Class I prices at the average 1996 levels would result in higher Class I prices in all markets in 1999 and 2000 and higher all-milk prices in most markets when compared to the baseline. These increased incentives for milk production would result in greater volumes of milk for manufacturing and lower manufacturing prices.

#### Location-Specific Differentials (Option 6) Analysis

This option would establish minimum prices for milk used in Class I by adding market-specific Class I differentials to the proposed Class II price. Class II would contain all manufactured products and would be priced by a cheese product price formula using the National Agricultural Statistical Service surveyed 40-pound cheddar cheese price times 9.87 plus the Chicago Mercantile Exchange Grade A butter price times 0.238 less \$1.80. The Class I differentials in this option would be phased in over a five-year period.

In general, the Class I differentials in the central section of the country would be reduced while those in the Northwest, New England and Florida are increased. After the proposed price surface is fully phased in, 20 markets would have Class I differentials that are reduced and 10 markets would have increases.

Under this option, the all-milk price for all Federal order markets combined would decline \$0.10 per cwt over the six year period. In 23 of the Federal order markets, the average all-milk price would decline by less than \$0.01 to \$0.95 per cwt. In 9 orders, the all-milk price would increase \$0.02 to \$0.19 per cwt.

Gross cash receipts from milk marketings in the combined Federal orders would average \$148.8 million

less than the baseline for the 6-year period. Cash receipts would be lower in 23 markets and higher in 9 markets. Because of this decline in cash receipts and since it is inconsistent with the four-class system contained in the proposed rule, this Class I price option is not detailed in the Class I price structure section of the proposed rule. This two-class pricing system was found to be insufficient to recognize the different use-values of milk for reasons set forth in the Basic Formula Replacement and Classification portions of this proposed rule.

#### Other Impacts of Pricing Options

The potential impacts of the options analyzed in the initial RIA on retail prices, and thus consumers, is less certain than the impacts on other sectors of the dairy industry. In general, changes in farm milk prices and wholesale prices are passed onto consumers. However, the timing and the degree of these pass-throughs is uncertain. It is assumed that all changes in farm milk prices (fluid processor costs) and the wholesale costs of manufactured products would be passed on to the retail level without any changes in the farm-processor-retail or farm-wholesale-retail margins.

Because of the bulky and perishable nature of packaged fluid milk, all international trading of dairy products, with the exception of limited exports of fluid milk to Mexico, is in manufactured products. An appendix table in the initial RIA details USDA's baseline estimates of international and domestic prices for butter and nonfat dry milk.

Neither location-specific differentials nor relative value-specific differentials are expected to have a significant impact on domestic, wholesale dairy product prices and therefore little effect on international trade of manufactured dairy products.

#### Economic Impacts of Classification Changes

The classification of milk recommendations should not have a significant economic impact on any dairy industry participants. This proposed rule provides uniform milk classification provisions for the newly consolidated milk orders. The recommendations should improve reporting and accounting procedures for handlers and provide for greater market efficiencies.

Most of the changes regarding milk classification provisions proposed for the newly consolidated orders would simplify order language and remove obsolete language.

This proposed rule contains a modified fluid milk product definition and recommends that certain products be reclassified. The revised fluid milk product definition proposed for the new orders should provide more consistency in determining the classification of products. The inclusion of eggnog to the list of fluid milk products and the reclassification of cream cheese from Class III to Class II will cause a nominal increase in the cost of the finished product. However, these changes, which will be applicable to all handlers regulated under the new orders, should not have a significant impact on the retail price of these products. Although producers will benefit from these products being reclassified into higher utilization classes, the impact of the product classification changes on the blend price to producers will be marginal.

Another modification includes the reclassification of butter and whole milk powder from Class III to Class IV. This change merely places these market-clearing products in the new Class IV with nonfat dry milk. The change promotes market efficiency and should have a minimal impact on producers' blend prices.

One recommendation with possible economic implications concerns the treatment of milk used to produce bulk sweetened condensed milk/skim milk. Some commenters argued that the wide price difference that sometimes exists between the Class II price and the Class III-A price has put manufacturers of sweetened condensed milk at a competitive disadvantage with manufacturers of nonfat dry milk, which can be substituted for bulk sweetened condensed milk and skim milk in some higher-valued products.

Although this proposed rule does not recommend a reclassification for milk used in bulk sweetened condensed milk, it does propose a change in the relationship between the Class II and IV prices which should eliminate the price disparity that now, at times, exists. As discussed in the "Class III and Class III-A (i.e., Class IV) Milk" section of this proposed rule, the proposed new Class II price will be equal to the Class IV price plus a 70-cent differential. The coupling of the Class II and Class IV prices will largely remove the incentive to substitute nonfat dry milk for bulk sweetened condensed milk.

The recommendations regarding shrinkage provisions should provide equity among handlers, improve market efficiencies, and facilitate accounting procedures. This proposed rule provides that shrinkage be assigned pro rata based on a handler's utilization. As

discussed in the "Shrinkage and Overage" section of this proposed rule, this modification should result in a slight increase (i.e., one cent per cwt.) in the blend price paid to producers.

For the reasons stated above, the milk classification provisions proposed herein should have little economic impact on dairy industry participants.

#### *The Regulatory Flexibility Act and the Effects on Small Businesses*

Pursuant to the requirements set forth in the Regulatory Flexibility Act (RFA) (5 U.S.C. 601 *et seq.*), the Agricultural Marketing Service (AMS) has considered the economic impact of the proposed rule on small entities and has prepared this initial regulatory flexibility analysis. The RFA provides that when preparing such analysis an agency shall address: the reasons, objectives, and legal basis for the proposed rule; the kind and number of small entities which would be affected; the projected recordkeeping, reporting, and other requirements; and federal rules which may duplicate, overlap, or conflict with the proposed rule. Finally, any significant alternatives to the proposal should be addressed. This initial regulatory flexibility analysis considers these points and the impact of this proposed regulation on small entities, and evaluates alternatives that would accomplish the objectives of the rule without unduly burdening small entities or erecting barriers that would restrict their ability to compete in the dairy industry.

This regulatory action is being considered in accordance with Section 143 of the Federal Agriculture Improvement and Reform Act of 1996, 7 U.S.C. 7253, (the Farm Bill) which requires the Secretary of Agriculture (Secretary) to consolidate the existing 31 Federal milk marketing orders, as authorized by the Agricultural Marketing Agreement Act of 1937, into between 10 and 14 orders. The Secretary is also directed to designate the State of California as a Federal milk order if California dairy producers petition for and approve such an order. Finally, the Farm Bill specifies that the Department of Agriculture use informal rulemaking to implement these reforms. The Farm Bill requires that a proposed rule be published by April 4, 1998, and all reforms of the Federal milk order program be completed by April 4, 1999.

In addition to these required mandates, the Farm Bill provides that the Secretary may address related issues such as the use of utilization rates and multiple basing points for the pricing of fluid milk and the use of uniform multiple component pricing when

developing one or more basic formula prices for manufacturing milk. This proposed rule also sets forth two options for consideration as a replacement for the Class I price structure and proposes replacing the basic formula price with a multiple component pricing system. These changes are proposed to address concerns that the current system of pricing Class I milk may not adequately reflect the value of Class I milk at various locations or the value of milk used in manufacturing products. The 1996 Farm Bill identified these as related issues that may be addressed in the consolidation of milk marketing orders. The proposed rule further proposes changes to classification of milk by establishing a new Class IV which would include milk used to produce nonfat dry milk, butter, and other dry milk powders; the reclassification of eggnog and cream cheese; and other minor changes. These proposed changes should improve handler reporting and accounting procedures thereby providing for greater market efficiencies. Finally, this proposed rule expands Part 1000 to include provisions that are identical within each consolidated order to assist in simplifying the orders. These provisions include the definitions of route disposition, plant, distributing plant, supply plant, nonpool plant, handler, other source milk, fluid milk product, fluid cream product, cooperative association, and commercial food processing establishment. In addition, the milk classification section, pricing provisions, and most of the provisions relating to payments have been included in the General Provisions. These proposed changes adhere with the efforts of the National Performance Review—Regulatory Reform Initiative to simplify, modify, and eliminate unnecessary repetition of regulations. Unique regional issues or marketing conditions have been considered and included in each market's order provisions.

The purpose of the RFA is to fit regulatory actions to the scale of business subject to the actions in order that small businesses would not be unduly or disproportionately burdened. To accomplish this purpose, it first is necessary to define a small business. According to the Small Business Administration's definition of a "small business," a dairy farm is a "small business" if it has an annual gross revenue of less than \$500,00 and a handler is a "small business" if it has fewer than 500 employees. For the purposes of determining which dairy

farms are "small businesses," the \$500,000 per year criterion was used to establish a production guideline of 326,000 pounds per month. Although this guideline does not factor in additional monies that may be received by dairy producers, it should be an inclusive standard for most "small" dairy farmers. For purposes of determining a handler's size, if the plant is part of a larger company operating multiple plants that collectively exceed the 500-employee limit, the plant will be considered a large business even if the local plant has fewer than 500 employees. During the process of developing this proposed rule, USDA identified approximately 80,000 of the 83,000 dairy producers (farmers) that have their milk pooled under a Federal order as small businesses. Thus, small businesses represent approximately 96 percent of the producers in the United States. On the processing side, there are over 1,200 plants associated with Federal orders, and of these plants, approximately 700 qualify as "small businesses" representing about 55 percent of the total.

During August 1997, there were 524 fully regulated handlers (343 distributing and 181 supply plants), 134 partially regulated handlers and 111 producer-handlers submitting reports under the Federal milk marketing order program. During 1996, 83,012 dairy farmers delivered over 104.5 billion pounds of milk to handlers regulated under the milk orders. This volume represents 69 percent of all milk marketed in the U.S. and 72 percent of the milk of bottling quality (Grade A) sold in the country. The value of the milk delivered to Federal milk order handlers at minimum order blend prices was nearly \$14.6 billion. Producer deliveries of milk used in Class I products (mainly fluid milk products) totaled 45.5 billion pounds—43.5 percent of total Federal order producer deliveries. More than 200 million Americans reside in Federal order marketing areas—77 percent of the total U.S. population.

The Federal milk order program is designed to set forth the terms of trade between buyers and sellers of fluid milk. A Federal order enforces the minimum price that processors (handlers) in a given marketing area must pay producers or farmers for milk according to how it is utilized. A Federal order further requires that the payments for milk be pooled and paid to individual dairy farmers or cooperative associations on the basis of a uniform or average price. It is important to note that a Federal milk order, including the pricing and all

other provisions, only becomes effective after approval, through a referendum, by dairy farmers associated with the order.

Development of the proposed rule began with the premise that no additional burdens should be placed on the industry as a result of Federal order consolidation and reform. As a step in accomplishing the goal of imposing no additional regulatory burdens, a review of the current reporting requirements was completed pursuant to the Paperwork Reduction Act of 1995 (44 U.S.C. Chapter 35). In light of this review, it was determined that this proposed rule would have little impact on reporting, recordkeeping, or other compliance requirements because these would remain almost identical to the current Federal order program. No new forms have been proposed; however, some additional reporting would be necessary in the proposed orders that would be adopting multiple component pricing if the current orders do not already have these provisions.

There are two principal reporting forms for handlers to complete each month that are needed to administer the Federal milk marketing orders. The forms are used to establish the quantity of milk used and received by handlers, the pooling status of the handler, the class-use of the milk used by the handler, and the butterfat content and amounts of other components of the milk. This information is used to compute the monthly uniform price paid to producers in each of the markets. Handlers in the marketing areas adopting multiple component pricing would be required to complete additional information regarding the components of the milk. This information would be necessary to enable their values of milk to be determined on the basis of these components and to assure that producers are paid correctly. Many handlers already collect and report this information.

This proposed rule does not require additional information collection that requires clearance by the OMB beyond the currently approved information collection. The primary source of data used to complete the forms are routinely used in most business transactions. Forms require only a minimal amount of information which can be supplied without data processing equipment or a trained statistical staff. Thus, the information collection and reporting burden is relatively small. Requiring the same reports for all handlers does not significantly disadvantage any handler that is smaller than industry average.

New territory, or pockets of unregulated territory within and

between current order areas has been included in the proposed consolidated marketing areas where such expansion would not have the effect of fully regulating plants that are not now regulated. The addition can benefit regulated handlers by eliminating the necessity of reporting sales outside the Federal order marketing area for the purpose of determining pool qualification. Where such areas can be added to a consolidated area without having the effect of causing the regulation of any currently-unregulated handler, they are proposed to be added.

Handlers not currently fully regulated under Federal orders may become regulated for two main reasons: first, in the process of consolidating marketing areas, some handlers who currently are partially regulated may become fully regulated because their sales in the combined marketing areas would meet the pooling standards of a suggested consolidated order area. Second, previously unregulated area in New York, Vermont, New Hampshire and Massachusetts was added on the basis of requests and supporting information. As a result, previously unregulated handlers would become fully regulated. Because of these two reasons, 24 additional plants are expected to become fully regulated under the program. Of these 24 plants, it is estimated that 15 are small businesses that would need to comply with the reporting, recordkeeping, and compliance requirements. The completion of these reports would require a person knowledgeable about the receipt and utilization of milk and milk products handled at the plant. This most likely would be a person already on the payroll of the business such as a bookkeeper, controller or plant manager. The completion of the necessary reporting, recordkeeping, and compliance requirements would not require any highly specialized skills and should not require the addition of personnel to complete. In fact, much of the information that handlers report to the market administrator is readily available from normally maintained business records, and as such, the burden on handlers to complete these recordkeeping and reporting requirements is expected to be minimal. In addition, assistance in completing forms is readily available from market administrator offices. A description of the forms and a complete Paperwork Reduction Act analysis follows this section.

No other burdens are expected to fall upon the dairy industry as a result of overlapping Federal rules. This proposed regulation does not duplicate,

overlap or conflict with any existing Federal rules.

To ensure that small businesses are not unduly or disproportionately burdened based on this proposed regulation, consideration was given to several options with the intention of mitigating negative impacts. Three options, including two suggested in the preliminary reports issued by AMS in December 1996 and May 1997, were considered with regard to the consolidation of Federal orders, five options were considered as replacements for the basic formula price, and seven options were considered with regard to the development of a new Class I price structure. The following options were considered by AMS prior to and during the development of the proposed regulation.

Consolidation Options

It is impossible to determine the economic effects of marketing area consolidation on handlers, producers and consumers without using assumptions about the specific order provisions contained in the consolidated order areas. The only effect consolidation, as a single factor, can have on the various market participants is through changes in the percentage of milk used in different classes within the

proposed consolidated orders. Without assumptions that include the specific class prices and milk uses in different products, there are no means of quantifying the economic effects of consolidation.

Handlers would be affected by class prices, which would be determined by the Class I price surface option that is selected, and by the minimum prices contained in all of the orders for milk used in Classes II, III and IV. The Class I price surface options considered could have impacts on small handler entities, however, handlers similarly located would be subject to the same minimum Class I prices, regardless of the size of their operations, and all handlers would be subject to the same minimum prices for Class II, Class III and Class IV milk. Such handlers would also be subject to the same minimum prices to be paid to producers.

Producers may be somewhat more affected by consolidation of marketing areas because changes in utilization percentages would result in changes in blend prices. As in the case of effects on handlers, however, it is impossible to determine a separate consolidation effect on producers, defined in monetary terms. The closest approximation to such an estimate would be the "weighted average utilization value" (WAUV). These

"prices" reflect only the change in value that can be attributed to changes in utilization rates, with no assumptions about changes in the levels of the various class prices. Such estimates, of necessity, reflect only anticipated changes in blend prices, using class prices that would no longer be in effect under the consolidated orders. To the extent that the WAUV computations reflect some of the effect of consolidation on producer prices, they are included in this analysis under each option discussion. It should be noted, however, that all producers in any given current area would be affected to an equal extent by the consolidation factor, with no disproportionate effect on small dairy farmer entities.

The following table shows the potential impact of three order consolidation options on producers who supply each of the current Federal milk marketing order areas via WAUV "prices". The three consolidated options are (1) the consolidated marketing areas suggested in the December 1996 initial Preliminary Report on Order Consolidation; (2) the consolidated marketing areas suggested in the May 1997 Revised Preliminary Report on Order Consolidation; and (3) the consolidated marketing areas suggested in this proposed rule.

WEIGHTED AVERAGE UTILIZATION VALUES (WAUV)

[Based on October 1995 information (\$/cwt)]

Consolidated Market	Marketing Areas in Initial Consol. Report (Dec. 96) (Option 1)		Marketing Areas in Revised Consol. Report (May 97) (Option 2)		Marketing Areas in Proposed Rule (Option 3)	
	Consol. Mkt. WAUV (\$/cwt)		Consol. Mkt. WAUV (\$/cwt)		Consol. Mkt. WAUV (\$/cwt)	
	WAUV using Current Mkt. Utilization (\$/cwt)	WAUV using Consol. Mkt. Utilization (\$/cwt)	WAUV using Current Mkt. Utilization (\$/cwt)	WAUV using Consol. Mkt. Utilization (\$/cwt)	WAUV using Current Mkt. Utilization (\$/cwt)	WAUV using Consol. Mkt. Utilization (\$/cwt)
Northeast .....		\$13.46		\$13.48		\$13.47
New England (F.O. 1) .....	13.50	13.48	13.52	13.51	13.52	13.49
NY-NJ (F.O. 2) .....	13.44	13.48	13.48	13.50	13.45	13.48
Middle Atlantic (F.O.4) .....	13.45	13.39	13.45	13.41	13.44	13.40
Appalachian .....		14.13		13.96		13.97
Carolina (F.O. 5) .....	14.23	14.21	14.23	14.19	14.23	14.20
Tenn. Valley (F.O. 11) .....	13.92	13.95	13.92	13.93	13.92	13.94
Lville-Lex-Evan (F.O. 46) .....	n/a	n/a	13.35	13.39	13.35	13.40
Florida .....		15.05		15.05		15.05
Upper Florida (F.O. 6) .....	14.67	14.78	14.67	14.78	14.67	14.78
Tampa Bay (F.O. 12) .....	15.09	15.04	15.09	15.04	15.09	15.04
SE Florida (F.O. 13) .....	15.42	15.31	15.42	15.31	15.42	15.31
Southeast .....		14.26		14.25		14.24
Southeast (F.O. 7) .....	14.26	14.26	14.25	14.25	14.24	14.27
Mideast .....		12.96		12.94		12.92
Ohio Valley (F.O. 33) .....	12.99	13.02	12.99	13.01	12.99	13.00
E. Ohio-W. PA (F.O. 36) .....	13.07	13.00	13.10	12.99	13.07	12.97
S. Michigan (F.O. 40) .....	12.75	12.86	12.75	12.84	12.75	12.83
MI Upper Penin. (F.O. 44) .....	12.81	12.62	12.81	13.262	12.81	12.61
Lville-Lex-Evan (F.O. 46) .....	13.35	13.06	n/a	n/a	n/a	n/a
Indiana (F.O. 49) .....	12.97	12.94	12.97	12.93	12.97	12.92
Upper Midwest .....		12.60		12.62		12.60

WEIGHTED AVERAGE UTILIZATION VALUES (WAUV)—Continued  
 [Based on October 1995 information (\$/cwt)]

Consolidated Market	Marketing Areas in Initial Consol. Report (Dec. 96) (Option 1)		Marketing Areas in Revised Consol. Report (May 97) (Option 2)		Marketing Areas in Proposed Rule (Option 3)	
	Consol. Mkt. WAUV (\$/cwt)		Consol. Mkt. WAUV (\$/cwt)		Consol. Mkt. WAUV (\$/cwt)	
Current Markets	WAUV using Current Mkt. Utilization (\$/cwt)	WAUV using Consol. Mkt. Utilization (\$/cwt)	WAUV using Current Mkt. Utilization (\$/cwt)	WAUV using Consol. Mkt. Utilization (\$/cwt)	WAUV using Current Mkt. Utilization (\$/cwt)	WAUV using Consol. Mkt. Utilization (\$/cwt)
	Chicago Reg. (F.O. 30) .....	12.62	12.62	12.62	12.61	12.62
MI Upper Penin. (F.O. 44) .....	R	R	R	R	R	R
Neb.-W. Iowa (F.O. 65) .....	n/a	n/a	12.63	12.74	n/a	n/a
Upper Midwest (F.O. 68) .....	12.55	12.56	12.55	12.54	2.55	12.56
E. South Dakota (F.O. 76) .....	n/a	n/a	12.81	12.65	n/a	n/a
Iowa (F.O. 79) .....	n/a	n/a	12.69	12.67	n/a	n/a
Central .....		13.16		13.21		12.95
S. IL-E MO (F.O. 32) .....	12.93	12.90	13.00	12.95	13.00	12.88
Central IL (F.O. 50) .....	13.03	12.74	13.03	12.78	13.03	12.72
Greater K. City (F.O. 64) .....	13.22	12.90	13.22	12.95	13.22	12.88
Neb.-W. Iowa (F.O. 65) .....	12.63	12.81	n/a	n/a	12.63	12.79
E. South Dakota (F.O. 76) .....	12.81	12.68	n/a	n/a	12.81	12.67
Iowa (F.O. 79) .....	12.71	12.71	n/a	n/a	12.71	12.70
SW Plains (F.O. 106) .....	13.31	13.33	13.31	13.41	13.08	13.29
E. Colorado (F.O. 137) .....	13.27	13.31	13.27	13.38	13.27	13.27
Southwest .....		13.36		13.39		13.39
Texas (F.O. 126) .....	13.49	13.48	13.49	13.46	13.49	13.46
Central AZ (F.O. 131) .....	13.26	13.17	n/a	n/a	n/a	n/a
NW-W Texas (F.O. 138) .....	13.00	13.09	13.00	13.07	13.00	13.07
Arizona-Las Vegas .....		n/a		13.26		13.26
Central AZ (F.O. 131) .....	n/a	n/a	13.26	13.29	13.26	13.29
Western .....		12.79		12.78		12.78
W. Colorado (F.O. 134) .....	13.41	12.84	13.41	12.82	13.41	12.82
SW ID-E. OR (F.O. 135) .....	12.63	12.68	12.63	12.68	12.63	12.68
Great Basin (F.O. 139) .....	12.83	12.81	12.81	12.79	12.81	12.79
Pacific Northwest .....		12.45		12.44		12.44
Pacific NW (F.O. 124) .....	12.45	12.45	12.44	12.44	12.44	12.44

n/a: not applicable.  
 R: Restricted.

For each option, a weighted average use value (WAUV) is computed for (a) the consolidated order; (b) the current order with current use of milk; and (c) the current order with projected use of milk in the consolidated order. The difference between the weighted average use values in (b) and (c) represents the potential impact on producers.

For example, in this proposed rule, the New England (F.O. 1) market's WAUV using its current utilization is \$13.52 per cwt. When the three markets are consolidated and the new consolidated utilization is used to calculate the WAUV, New England's WAUV would be \$13.49 per cwt. In this comparison, the potential impact on producers supplying the New England market area would be a decrease of three cents per cwt.

Each of the three options assumes the pool distributing plant standards suggested for each of the consolidated orders in this proposed rule; thus the calculated values in the preceding table are not directly comparable to the

WAUV values published with either the initial or the revised reports on order consolidation.

During the process of developing this proposed rule, AMS issued two reports suggesting 10 and 11 marketing area boundaries, respectively, to meet the requirements of the 1996 Farm Bill. The marketing areas defined in these reports were based primarily on an analysis of receipt and distributing data from fluid distributing plants in October 1995. Over 900 comments regarding consolidation issues received thus far in the development process also have been considered: almost 50 comments prior to the December 1996 release of the Preliminary Report on Order Consolidation (Option 1); an additional 60 comments prior to the May 1997 release of the Revised Preliminary Report on Order Consolidation (Option 2); and another 800 comments since release of the revised report. These comments were filed primarily by producers and handlers. Incorporated in the marketing area boundaries suggested

in the revised report and in the proposed consolidation in this rule (Option 3) are both information contained in the comments as well as data gathered to update the information on which the earlier report(s) were based where questions were raised about the boundaries of suggested marketing areas and where marketing changes had occurred.

Option 1 (Preliminary Report on Order Consolidation, December 1996)

Based on seven criteria: ((1) Overlapping route disposition; (2) overlapping areas of milk supply; (3) number of handlers within a market; (4) natural boundaries; (5) cooperative association service areas; (6) features common to existing orders, such as similar multiple component pricing plans; and (7) milk utilization in common dairy products), 10 marketing areas (Northeast, Appalachian, Florida, Southeast, Mideast, Upper Midwest, Central, Southwest, Western and Pacific Northwest) were suggested in this

report. Data were gathered relating to the receipts and distribution of fluid milk products for all known distributing plants located in the 47 contiguous States, not including the State of California, for the month of October 1995.

The current Federal orders that comprise the initially-suggested consolidated areas are as follows: **NORTHEAST**—current marketing areas of the New England, New York-New Jersey, and Middle Atlantic Federal milk orders; **APPALACHIAN**—current marketing areas of the Carolina and Tennessee Valley Federal milk orders, and a portion of the Louisville-Lexington-Evansville Federal milk order; **FLORIDA**—current marketing areas of the Upper Florida, Tampa Bay, and Southeastern Florida Federal milk orders; **SOUTHEAST**—current marketing areas of the Southeast Federal milk order, plus 1 county from the Louisville-Lexington-Evansville Federal milk order marketing area, 15 currently unregulated Kentucky counties, and 2 currently unregulated northeast Texas counties; **MIDEAST**—current marketing areas of the Ohio Valley, Eastern Ohio-Western Pennsylvania, Southern Michigan, and Indiana Federal milk orders, plus most of the current marketing area of the Louisville-Lexington-Evansville Federal milk order, Zone 2 of the Michigan Upper Peninsula Federal milk order, and 12 counties of the Southern Illinois-Eastern Missouri Federal milk order; **UPPER MIDWEST**—current marketing areas of the Chicago Regional and Upper Midwest Federal milk orders, plus Zones I and I(a) of the Michigan Upper Peninsula Federal milk order and seven unregulated or partly regulated Wisconsin counties; **CENTRAL**—current marketing areas of the Southern Illinois-Eastern Missouri (less 12 counties included in the suggested Mideast marketing area), Central Illinois, Greater Kansas City, Nebraska-Western Iowa (less 11 currently-regulated counties suggested to be unregulated), Eastern South Dakota, Iowa, Southwest Plains, and Eastern Colorado Federal milk orders, plus 63 currently-unregulated counties in seven of the states; **SOUTHWEST**—current marketing areas of the Texas, New Mexico-West Texas, and Central Arizona Federal milk orders; **WESTERN**—current marketing areas of the Western Colorado, Southwestern Idaho-Eastern Oregon, and Great Basin Federal milk orders; and **PACIFIC NORTHWEST**—current marketing area of the Pacific Northwest Federal milk order plus 1 currently-unregulated county in Oregon.

Based on the WAUV calculations shown in the previous table, utilization rate changes due to consolidation could affect producer prices. The column labeled "Option 1" shows the WAUV for the consolidated order and each of the current orders suggested in the December 1996 report.

In the Northeast market, producers currently affiliated with the New England and Middle Atlantic would have negative impacts on their WAUV, respectively, while New York-New Jersey producers would be positively impacted. In the Appalachian market, Carolina producers should expect some negative impacts due to consolidation, while Tennessee Valley producers would experience positive effects from this consolidation. In the Florida market, Upper Florida producers would gain while Tampa Bay and Southeastern Florida producers would have a negative impact resulting from this consolidation. The Southeast market remains virtually the same as it does currently and thus, no or little impact on producer prices would be expected. In the Mideast market, producers affiliated with the Ohio Valley and Southern Michigan Federal orders would probably see increases in blend prices due to this consolidation, while producers affiliated with the Eastern Ohio-Western Pennsylvania, Michigan Upper Peninsula, Louisville-Lexington-Evansville and Indiana Federal orders would see decreases. In the Upper Midwest market, the Upper Midwest producers should see slight increases while Chicago Regional producers would probably have no impact due to this consolidation. Of all the consolidated markets, producers in the current Orders that compose the Central market probably would see the largest changes due to this consolidation: producers with the Nebraska-Western Iowa, Southwest Plains and Eastern Colorado markets may see increases, while producers affiliated with the Southern Illinois-Eastern Missouri, Central Illinois, Greater Kansas City, and Eastern South Dakota markets may see decreases. Producers with the Iowa market would probably have no impact due to this suggested Central market consolidation. In the Southwest market, producers affiliated with the New Mexico-West Texas would see increases due to this consolidation while Texas and Central Arizona producers would see decreases. In the Western market, Southwestern Idaho-Eastern Oregon producers would see increases but Western Colorado and Great Basin producers would see decreases. The Pacific Northwest market remains

virtually the same as it does currently and thus, no or little impact on producer prices would be expected.

Of approximately 83,000 dairy producers delivering milk to handlers regulated under the milk orders, about 80,000 are considered to be small businesses under the production guideline of less than 326,000 pounds per month.

As stated above, handlers are impacted more significantly by class prices and minimum prices than by expected utilization changes resulting from consolidation. Of the 371 distributing plants expected to be fully regulated under this 10-market suggested configuration under the assumptions used in the December 1996 report, an estimated 193 plants are small businesses under the criteria provided by the SBA (under 500 employees).

Option 2 (Revised Preliminary Report on Order Consolidation, May 1997)

Eleven marketing areas were suggested in this second report. Because numerous comments indicated that the boundaries of some marketing areas should be re-evaluated, and also because regulatory shifts and distributing plant distribution areas had occurred, more detailed and updated data was obtained. The same seven criteria used in Option 1 were applied in this option as well. Modifications were made to the Northeast, Appalachian, Southeast, Mideast, Upper Midwest, Central, Southwest and Western regions, as follows (only the changes to these orders are noted): **NORTHEAST**—Addition of contiguous unregulated areas of New Hampshire, Vermont and New York; the western non-Federally regulated portion of Massachusetts, the Western New York State order area, and Pennsylvania Milk Marketing Board Areas 2 and 3 in northeastern Pennsylvania; **APPALACHIAN**—Addition of all of the Louisville-Lexington-Evansville Federal order (with the exception of one county included in the suggested Southeast market) and 26 currently-unregulated counties in Indiana and Kentucky; **SOUTHEAST**—Minus 2 currently-unregulated counties in northeast Texas (in the suggested Southwest market); **MIDEAST**—Addition of Pennsylvania Milk Marketing Board Area 6 (in western/central Pennsylvania) and 2 currently-unregulated counties in New York, and minus the Louisville-Lexington-Evansville Federal order area, 12 counties in Illinois, and unregulated counties in Indiana and Kentucky (in the suggested Appalachian market); **UPPER MIDWEST**—Addition of the Iowa, Eastern South Dakota, and most of

the Nebraska-Western Iowa Federal order areas, plus currently-unregulated counties in Iowa and Nebraska; CENTRAL—Addition of 12 counties in the current Southern Illinois-Eastern Missouri Federal order that initially were suggested as part of the consolidated Mideast area, and minus the Eastern South Dakota, Iowa, and most of the Nebraska-Western Iowa Federal order marketing area; SOUTHWEST—Addition of 2 currently-unregulated northeast Texas counties that initially were suggested as part of the consolidated Southeast market and 47 currently-unregulated counties in southwest Texas, and minus the Central Arizona marketing area; ARIZONA-LAS VEGAS—this new eleventh marketing area composed of the current marketing area of the Central Arizona Federal order and the Clark County, Nevada, portion of the current Great Basin marketing area, plus eight currently-unregulated Arizona counties; and WESTERN—Minus Clark County, Nevada. The FLORIDA and PACIFIC NORTHWEST marketing areas did not change from the preliminary report.

Based on the WAUV calculations shown in the previous table, utilization rate changes due to consolidation could affect producer prices. The column labeled "Option 2" shows the WAUV for the consolidated order and each of the current orders suggested in the May 1997 report.

In the Northeast market, producers currently affiliated with the New England and Middle Atlantic orders would have negative impacts on their WAUV, respectively, while New York-New Jersey producers would remain unchanged. In the Appalachian market, Carolina producers should expect some negative impacts due to consolidation, while Tennessee Valley and Louisville-Lexington-Evansville producers would experience positive effects from this consolidation. In the Florida market, Upper Florida producers would gain while Tampa Bay and Southeastern Florida producers would have a negative impact resulting from this consolidation. The Southeast market remains virtually the same as it does currently and thus, little impact on producer prices would be expected. In the Mideast market, producers affiliated with the Ohio Valley and Southern Michigan Federal orders would probably see increases in blend prices due to this consolidation, while producers affiliated with the Eastern Ohio-Western Pennsylvania, Michigan Upper Peninsula, and Indiana Federal orders would see decreases. In the Upper Midwest market, the Nebraska-Western Iowa producers should see

increases, while Chicago Regional, Upper Midwest, Eastern South Dakota, and Iowa producers would have a decrease in producer prices due to this consolidation. In the Central market, producers with the Southwest Plains and Eastern Colorado markets would see increases, while producers affiliated with Southern Illinois-Eastern Missouri, Central Illinois, and Greater Kansas City markets may see decreases. In the Southwest market, producers affiliated with New Mexico-West Texas would see increases due to this consolidation while Texas producers would see decreases. The added Arizona-Las Vegas market is virtually the same as the Central Arizona market but a positive impact on producer prices may result from an additional handler. In the Western market, Southwestern Idaho-Eastern Oregon producers would see increases but Western Colorado and Great Basin producers would see decreases. The Pacific Northwest market remains virtually the same as it does currently and thus, no or little impact on producer prices would be expected.

Of approximately 83,000 dairy producers delivering milk to handlers regulated under the milk orders, about 80,000 are considered to be small businesses under the production guideline of less than 326,000 pounds per month. In addition, it is estimated that about 13 percent of the total milk production in Pennsylvania is represented only by the Pennsylvania Milk Marketing Board. Under this option, this production would be added to the Federal order pool and affect an undetermined number of businesses which would include both small and large producers.

As stated above, handlers are impacted more significantly by class prices and minimum prices than by expected utilization changes resulting from consolidation. Of the 379 plants expected to be fully regulated under this 11-market suggested configuration under the assumptions used in the May 1997 report, 175 plants are estimated to be small businesses on the basis of fewer than 500 employees.

The preliminary consolidation report (Option 1) stated that the Farm Bill requirement to consolidate existing marketing areas did not specify expansion of regulation to previously non-Federally regulated areas where such expansion would have the effect of regulating handlers not currently regulated. However, on the basis of data, views and arguments filed by interested persons in response to the initial Preliminary Report (Option 1) requesting that currently non-Federally regulated areas be added to some

consolidated marketing areas, the revised Preliminary Report (Option 2) suggests that such areas be added to several consolidated areas, the Northeast and Mideast market areas in particular. Approximately 20 handlers who would have been affected by the expansion of Federal order areas into currently non-Federally regulated areas were notified of the possible change in their status and encouraged to comment.

Handlers located in Pennsylvania Milk Marketing Board Areas 2, 3 and 6 are regulated under the State of Pennsylvania if they do not have enough sales in any Federal order area to meet an order's pooling standards. If such plants do meet Federal order pooling standards, the State continues to enforce some of its regulations in addition to Federal order regulations. As state-regulated handlers, they must pay a Class I price for milk used in fluid products which is often higher than the Federal order price would be. Inclusion of the Pennsylvania-regulated handlers in the consolidated marketing area would have little effect on handlers' costs of Class I milk (or might reduce them), while reducing producer returns.

#### Option 3: The Proposed Consolidation

The proposed consolidation is a result of extensive analysis of data as previously indicated and consideration of public comments submitted in response to Options 1 and 2. Extensive outreach, which is explained in the "Public Input" section, was completed. After compiling this information, the proposed order consolidation was developed to ensure industry integrity.

Eleven marketing areas are proposed in this rule, including modifications to some of the 11 marketing orders suggested in Option 2. Marketing data was further examined for some of the suggested consolidated marketing areas to determine the most appropriate configurations of the consolidated areas. Primary criteria continues to be the seven used in the two earlier reports on order consolidation. As a result of further analysis, the configurations of the Northeast, Mideast, Southeast, Upper Midwest and Central areas have changed significantly from those suggested in Option 2, and minor changes have been made to the Appalachian area. The modifications for these areas from the revised preliminary report (Option 2) are as follows: NORTHEAST—Minus some previously suggested area to be included in the Northeast (the southern tier of 3 western New York counties and Pennsylvania Milk Marketing Board Areas 2 and 3); APPALACHIAN—Minus five Kentucky counties that were part of the former

Paducah order area, now suggested to be in the Southeast market;

**SOUTHEAST**—Addition of 11 northwest Arkansas and 22 entire and 1 partial Missouri counties currently part of the Southwest Plains Federal order, 6 Missouri counties currently part of the Southern Illinois-Eastern Missouri Federal order, 16 currently unregulated southeast Missouri counties, 20 currently unregulated Kentucky counties (were suggested to be in the Appalachian market); **MIDEAST**—Minus the current Pennsylvania Milk Marketing Board Area 6 and two southwestern New York counties, all currently non-Federally regulated; **UPPER MIDWEST**—Minus the Iowa, Eastern South Dakota, Nebraska-Western Iowa Federal order areas; **CENTRAL**—Addition of the Iowa, Eastern South Dakota, Nebraska-Western Iowa Federal order areas, 68 currently-unregulated counties in Kansas, Missouri, Illinois, Iowa, Nebraska and Colorado, and minus 11 northwest Arkansas and 22 entire and 1 partial Missouri counties currently part of the Southwest Plains Federal order, 6 Missouri counties currently part of the Southern Illinois-Eastern Missouri Federal order, and 16 currently unregulated southeast Missouri counties. The **FLORIDA**, **SOUTHWEST**, **ARIZONA-LAS VEGAS**, **WESTERN** and **PACIFIC NORTHWEST** marketing areas did not change from the revised preliminary report.

Based on the WAUV calculations shown in the previous table, utilization rate changes due to consolidation could affect producer prices. The column labeled "Proposed Rule" shows the WAUV for the consolidated order and each of the current orders suggested in this proposed rule.

In the Northeast market, for producers currently affiliated with the New York-New Jersey order, the proposed option would have positive impacts on their WAUV, while New England and Middle Atlantic producers would be negatively impacted. In the Appalachian market, Carolina producers should expect some negative impacts due to consolidation, while Tennessee Valley and Louisville-Lexington-Evansville producers would experience positive effects from this consolidation. In the Florida market, Upper Florida producers would gain while Tampa Bay and Southeastern Florida producers would have a negative impact resulting from this consolidation. With the addition of marketing area to the Southeast, the WAUV for Southeast producers may be expected to be positively impacted. In the Mideast market, producers affiliated with the Ohio Valley and Southern

Michigan Federal orders would probably see increases in blend prices due to this consolidation, while producers affiliated with the Eastern Ohio-Western Pennsylvania, Michigan Upper Peninsula, and Indiana Federal orders would see decreases. In the Upper Midwest market, the Upper Midwest producers should see slight increases, while Chicago Regional producers would have no impact due to this consolidation. In the Central market, producers with the Nebraska-Western Iowa and Southwest Plains markets would see increases, producers affiliated with Southern Illinois-Eastern Missouri, Central Illinois, Greater Kansas City, Eastern South Dakota, and Iowa markets may see decreases, and Eastern Colorado producers would see no impact. In the Southwest market, producers affiliated with New Mexico-West Texas would see increases due to this consolidation while Texas producers would see decreases. Producers in the Arizona-Las Vegas market may receive a positive impact on producer prices due to an additional handler regulated in this order area. In the Western market, Southwestern Idaho-Eastern Oregon producers would see increases but Western Colorado and Great Basin producers would see decreases. The Pacific Northwest market remains virtually the same as it does currently and thus, no or little impact on producer prices would be expected.

Of approximately 83,000 dairy producers delivering milk to handlers regulated under the milk orders, about 80,000 are considered to be small businesses under the production guideline of less than 326,000 pounds per month. The additional estimated 13 percent of Pennsylvania's total milk production represented by the Pennsylvania Milk Marketing Board which would have been added in Option 2, would not be included under this option.

As stated above, handlers are impacted more significantly by class prices and minimum prices than by expected utilization changes resulting from consolidation. Of the 337 plants expected to be fully regulated under this 11-market proposed configuration, 164 plants are estimated to be small businesses on the basis of fewer than 500 employees.

Based on the comments received in response to the revised preliminary report (Option 2) it has been determined that consolidation of the existing orders does not necessitate expansion of the consolidated orders into areas in which handlers are subject to minimum Class I pricing under State regulation, especially when the states' Class I prices

exceed or equal those that would be established under Federal milk order regulation. Such regulation would have the effect of reducing returns to producers already included under State regulation without significantly affecting prices paid by handlers who compete with Federally-regulated handlers.

In an effort to avoid extending Federal regulation to handlers whose primary sales areas are outside current Federal order marketing areas, but who already are subject to similar minimum uniform pricing under State regulation, the in-area Class I disposition percentage portion of the pool distributing plant definition is proposed to be 25 percent for the Northeast order and 30 percent for the Mideast order, instead of the 10 or 15 percent used in the other nine consolidated order areas. It is estimated that five plants in Pennsylvania, Maryland and Virginia that would have been fully regulated using 15 percent would remain partially regulated, as they currently are, using 25 and 30 percent, respectively. At least three of these five handlers meet the small business criteria.

#### Exempt Plants

Options 2 and 3 both recognize the Identical Provisions Committee<sup>14</sup> determination that a handler distributing less than 150,000 pounds per month of fluid milk products does not have a significant competitive effect on the market, and that handlers of such size should, therefore, be exempt from the pricing and pooling provisions of the orders. The level of route disposition required before an exempt plant becomes regulated varies in the current orders. As recommended, any plant with route disposition during the month of 150,000 pounds or less would be exempt in the consolidated orders. This limit reflects the maximum amount of fluid milk products allowed by an exempt plant in any current Federal milk order and ensures plants that are currently exempt from regulation would remain so. Under this proposed rule, it is expected that 36 distributing plants that otherwise would be identified as fully regulated plants are identified as exempt plants. Therefore under this provision, these plants would not be subject to the pricing and pooling provisions of their respective order.

Although 150,000 pounds of fluid milk disposition per month may

<sup>14</sup>The Identical Provisions Committee was established in May 1996 to address uniformity in order provisions during the Federal order reform process. This committee and others established are described further in the "Background" portion of this proposed rule.

represent a level at which exempting a distributing plant could be expected not to have a serious detrimental impact on the ability of a Federal milk order to provide for uniform pricing to handlers and producers, it would be quite difficult to select a higher level of exemption without compromising the purposes of the regulation. The under-500-employee definition of a small business assures that nearly all single-plant milk handlers would qualify as a small business. Many of the "small" businesses may be among the largest competitors in a particular market.

In addition, numbers of employees could be expected to vary greatly with the nature of a plant's operation. For instance, the number of persons employed by two plants processing and distributing equal volumes of fluid milk products could be very different if one plant contracts out its producer milk hauling, laboratory operations and packaged product distribution, while the other plant performs all of these operations with its own employees. For this reason alone, it would be inappropriate to exempt handlers from regulation, or to impose differing regulatory burdens, on the basis of their size beyond the minimal size determined to be less than a significant competitive force in the market.

Many current Federal orders also provide regulatory exemption for a plant operated by a state or Federal government agency. For example, some states have dairy farm and plant operations that provide milk for their prison populations. As recommended, regulatory exemption would be continued under the consolidated orders unless pool plant status is desired. Additionally, regulatory exemption is intended to include colleges, universities and charitable institutions because these institutions generally handle fluid milk products internally and have little or no impact in the mainstream commercial market. However, in the event that these entities do distribute fluid milk through commercial channels, route sales by such entities, including government agencies, would be monitored to determine if Federal regulations should apply. Under this proposed rule, it is expected that 18 distributing plants would be identified as exempt based on their institutional status.

#### Producer-handlers

Also exempt from full regulation would be those entities that operate as both a producer and a handler. A primary basis for exempting producer-handlers from the pricing and pooling provisions of a milk order is that these

entities are customarily small businesses that operate essentially in a self-sufficient manner. During August 1997, 111 producer-handlers submitted reports under the Federal milk marketing order program.

#### Basic Formula Price Options

A number of options for determining a basic formula price were considered and analyzed in the process of developing the proposed basic formula price (BFP). In addition to the proposed method of pricing components based on their value in manufactured products, other options examined, by both the Agricultural Marketing Service's Dairy Division Basic Formula Price Replacement Committee and by the University Study Committee (USC), led by Dr. Ronald D. Knutson of Texas A & M University, were: economic formulas, futures markets, cost of production, competitive pay pricing, and pricing differentials only.

Descriptions of the two Committees' analyses, and results of their work are included in "A Preliminary Report on Alternatives to the Basic Formula Price," published in April 1997 by the Basic Formula Price Committee, Dairy Division, AMS; and the following reports from the Agricultural and Food Policy Center, Texas A&M University System:

"An Economic Evaluation of Basic Formula Price (BFP) Alternatives," AFPC Working Paper 97-2, June 1997.

"Evaluation of 'Final' Four Basic Formula Price Options," AFPC Working Paper 97-9, August 1997.<sup>15</sup>

The primary criterion used by the Dairy Division BFP Committee was that any replacement BFP option reflect the supply of and demand for milk used in manufactured dairy products. At the same time, one of the USC's critical criteria for a replacement BFP was that it reliably reflect market conditions for all manufactured products.

In trying to determine the most appropriate replacement for the current BFP, which uses a survey of prices paid by manufacturing plants for non-Grade A milk updated by a product price formula, the goal of both groups was a market-based alternative. The BFP Committee measured the extent to which each pricing option met its primary goal by tracking the options against the current BFP for a period of prior months, on the basis of the assumption that the current BFP

successfully reflects the supply and demand for milk used in manufactured products. The USC Committee used an econometric procedure to test the ability of the alternatives they considered to reflect supply and demand.

To the extent the goal of identifying a BFP that reflects the value of milk used in manufactured products is capable of attainment, all market participants would be affected by the BFP replacement in the same manner as if they were operating in a free market, with no external impacts caused by regulation. To the extent the goal is achieved, then, there would be no uneven impact on market participants on the basis of size. All market participants, (handlers, producers and consumers), would be affected in the same manner as if there were no regulation. However, the existence of minimum order pricing serves to assure that small handlers pay no more for their milk than larger entities (unless the market allows higher prices to be exacted from small buyers), and that small producers receive the same minimum uniform price for the milk or components of milk they produce as large producers. Consumers can be assured that the prices generally charged for dairy products are prices that reflect, as closely as possible, the forces of supply and demand in the market.

Of the options considered and analyzed, both groups studying the issue determined that the option of pricing components of milk according to their value in manufactured products, as reflected by the sales prices of those products, best approximates the intersection of supply and demand for milk used in manufactured dairy products.

#### Manufacturing Allowances

Make allowances or manufacturing allowances, one of the factors incorporated in the formulas for determining component values, may reflect more closely the manufacturing costs of large firms than those of small firms. These manufacturing costs would be used to adjust the sales prices of dairy products to the value of milk purchased to make the products. To the extent these allowances fail to reflect the full cost of manufacturing, they may require handlers to pay more for milk than they can realize from the sale of their products. On the other hand, if the manufacturing allowances more than cover the cost of manufacturing, handlers may be assured of extra margins.

Although it may appear that the use of make allowances in the computation

<sup>15</sup> These reports can be obtained from the Agricultural and Food Policy Center, Department of Agricultural Economics, Texas A&M University, College Station, Texas 77843-2124, telephone (409) 845-5913 or on the Internet at <http://AFPC1.TAMU.EDU>.

of component prices would advantage large processors because of possible economies of scale, these economies exist regardless of whether they are recognized in price computations. If the assumption is made that economies of scale exist in dairy plants and that large plants are more efficient than small plants, a manufacturing allowance that fully covers a small handler's cost of making products would merely increase the profit margin of its larger competitors. At the same time, producers unfairly would be required to subsidize the manufacturing costs of handlers who use their milk, and consumers would pay more for their dairy products than the costs of production and processing would justify.

An attempt has been made, using Cornell University studies of manufacturing costs at a number of manufacturing plants distributed around the U.S., to arrive at economically defensible make allowances. Since it is difficult to distinguish the differential effects of market-based component pricing on small and large firms engaged in manufacturing dairy products, reliance would be placed on industry participants to comment on these facets of the proposed BFP replacement.

#### Impact of Multiple Component Pricing Provisions on Small Entities

Seven of the eleven proposed orders provide for milk to be paid for on the basis of its components (multiple component pricing, or MCP). Five of the seven MCP orders also provide for milk values to be adjusted according to the somatic cell count of producer milk. The equipment needed for testing milk for its component content can be very expensive to purchase, and requires highly-skilled personnel to maintain and operate. The cost of infra-red analyzers ranges from just under \$100,000 to \$200,000. The infra-red machines that are used by most laboratories would test for total solids and somatic cells at the same time the butterfat and protein tests are done.

No new report forms are needed under multiple component pricing; however, some additional reporting is necessary to enable handlers' values of milk to be determined on the basis of components, and to assure that producers are paid correctly. For the market administrators to compute the producer price differential, handlers would need to supply additional information on their currently-required monthly reports of receipts and utilization. In addition to the product pounds and butterfat currently reported,

handlers would be required to report pounds of protein, pounds of other solids, and, in 5 of the orders, somatic cell information. This data would be required from each handler for all producer receipts, including milk diverted by the handler, receipts from cooperatives as 9(c) handlers (that is, the cooperative acts as a handler); and, in some cases, receipts of bulk milk received by transfer or diversion.

Since producers would be receiving payments based on the component levels of their milk, the payroll reports that handlers supply to producers must reflect the basis for such payment. Therefore the handler would be required to supply the producer not only with the information currently supplied, but also, (a) the pounds of butterfat, the pounds of protein, and the pounds of other solids contained in the producer's milk, as well as the producer's average somatic cell count, and (b) the minimum rates that are required for payment for each pricing factor and, if a different rate is paid, the effective rate also. Many handlers already report this additional information. It should be noted that handlers already are required to report information relative to pounds of production, butterfat and rates of payment for butterfat and hundredweight of milk to the appropriate Market Administrator.

Of over 74,000 producers whose milk was pooled in December 1996 under 23 of the current orders that would be part of consolidated orders providing for multiple component pricing, the milk of 52,500 of these producers was pooled under 13 current orders that have MCP. Handlers in these markets already have incurred the initial costs of testing milk for its component content, and have made the needed transition to reporting the component contents of milk receipts on their handler reports to the market administrators, and on their reports of what they have paid producers.

Of the remaining 21,750 producers who would be affected by MCP provisions under a Federal order (including an estimated 20,650 producers qualifying as small businesses), the milk of approximately 13,000, or 60 percent, currently is received by handlers who test or have the capability of testing for multiple components and, in many cases, somatic cells. Many of these handlers also report component results to the producers with their payments. Almost all of the producers whose milk currently is not being tested or paid for on the basis of components are located in the New England and New York-New Jersey marketing areas, which would be

consolidated with the Middle Atlantic area into the proposed Northeast order.

Accommodation has been made to ameliorate handlers' expenses of testing producer milk for component content

As component pricing plans have been adopted under a number of the present Federal milk orders since 1988, the component testing needed to implement these pricing plans has been performed by the market administrators responsible for the administration of the orders involved for handlers who have not been equipped to make all of the determinations required under the amended orders. It has been made clear in the decisions under which these plans have been adopted that handlers who would find it unduly burdensome to obtain the equipment and personnel needed to accomplish the required testing may rely on the market administrators to verify or establish the tests under which producers are paid. As noted above, however, many handlers not now subject to MCP provisions under Federal orders have nevertheless already undertaken multiple component testing and payment programs.

#### Pricing Options

Several pricing options, as discussed below, were considered as replacements for the current Class I price structure. Five of the options were determined to have a negative impact on small businesses, albeit slight or significant. These options included relative use differentials, flat differentials, modified flat differentials, demand based differentials, and a decoupled baseline Class I price with adjusters. In addition to the impacts on small businesses, these options were not considered viable based on additional qualitative analysis contained in the findings and conclusions of the proposed rule.

#### Relative Use Differentials

The use of relative use differentials based on Class I utilizations was considered as an option for replacing the Class I price structure. Using this concept, the relative use Class I differential would equal \$1.60 per hundredweight plus the relative use ratio times \$1.00. A 25 percent limit would be applied so the new differential would not exceed 125 percent of the current differential nor fall to less than 75 percent of the current differential. A percentage limit was placed on the differential changes to temper adjustments based on market supply and demand conditions.

The advantages of the system are that it allows Class I differentials to adapt to

supply and demand conditions within a given marketing area based on changes in the utilization. However, because the differentials would be allowed to change independently from neighboring areas, serious problems arise with order-to-order alignment.

The next table illustrates the Class I differentials under the proposed

consolidated orders. These differentials are not location-specific within the applicable orders. For purposes of this analysis and to provide a basis for comparison within the proposed consolidated orders, a weighted average Class I differential has been calculated for each order, based on October 1995 data. This weighted average differential

is computed by multiplying the percentage of Class I milk in each of the current orders that comprise the consolidated order by the applicable current order differential and adding the resulting amounts. This weighted average differential is not location specific for the consolidated order.

#### RELATIVE USE CLASS I DIFFERENTIALS IN PROPOSED ORDERS

[Based on October 1995 Data]

Proposed order <sup>1</sup>	Relative use ratio <sup>2</sup> (percent)	+ \$1.60 = class I diff. (\$/cwt)	Weighted av- erage diff. (\$/cwt) <sup>3</sup>	Maximum diff. range (75%–125%)	New diff (\$/cwt)	Change in diff. (\$/cwt)
Northeast .....	0.92	2.52	3.14	2.35–3.93	2.52	–0.62
Appalachian .....	4.60	6.20	2.79	2.09–3.49	3.49	0.70
Southeast .....	5.76	7.36	3.04	2.28–3.80	3.80	0.76
Florida .....	7.54	9.14	3.89	2.92–4.86	4.86	0.97
Mideast .....	1.26	2.86	1.91	1.43–2.39	2.39	0.48
Central .....	0.95	2.55	2.52	1.89–3.15	2.55	0.03
Up. Midwest .....	0.53	2.13	1.32	0.99–1.65	1.65	0.33
Southwest .....	0.93	2.53	3.01	2.26–3.76	2.53	–0.48
AZ-Las Vegas .....	1.04	2.64	2.46	1.85–3.08	2.64	0.18
Western .....	0.42	2.02	1.84	1.38–2.30	2.02	0.18
Pacific NW .....	0.55	2.15	1.90	1.43–2.38	2.15	0.25

<sup>1</sup> Based on the 11 proposed orders contained in this proposed rule.

<sup>2</sup> Relative use ratio = Class I ÷ all other uses.

<sup>3</sup> Weighted average differential for the consolidated order is computed by summing the product of the percentage of Class I milk in each current order multiplied by the applicable current order differential.

The review of this option indicates that differentials would probably have a minimal impact on small businesses, both processors and producers. For a majority of the Federal order system, producers and processors would experience Class I price increases. However, due to offsetting factors impacts would be reduced.

Class I differentials are estimated to increase from \$0.00 to \$0.48 in the Central, Mideast, and Midwestern regions. Currently, over-order charges are significantly higher and would largely absorb these differential increases. Impacts on small producers and processors would be minimal.

The Northeastern marketing area could be affected significantly by the adoption of a relative use differential because of the decrease in Class I prices and because this area has a high concentration of small businesses, both producers and processors. There are approximately 18,860 small producers and 280 small processors located in this region. Processors would pay on average \$0.62 less for Class I milk as compared to the current system. Producers would likely turn to over-order charges to try to make up for their lost revenue. If this were to occur, then small processors and producers would be placed at a competitive disadvantage to large businesses because often the small businesses do not maintain the

resources needed to effectively negotiate for supplies of milk. However, historically this region has had difficulty maintaining a large over-order premium structure and assumptions are that this would continue. If so, then all producer income would decrease slightly possibly impacting the market's milk supplies.

Large increases in Class I differentials would occur in the orders located in the Southeast. There are approximately 4,000 small producers and 30 small handlers in the Florida and Southeast areas. Class I handlers would experience increased competition from lower cost handlers in nearby markets. This may have a greater impact on small processors because of their ability to compete based on available resources. Although higher differentials would be returned to producers through the Federal order uniform price, overall producers in the Southeast markets would probably not experience any significant gains from these increased differentials due to reduced over-order premiums being charged. However, this would benefit small producers who may not be able to negotiate as effectively for over-order prices.

The Southwest market is the other market to experience decreases in differentials. Approximately 1,400 small producers and 30 small handlers would be impacted by the decrease in Class I

prices. Over-order charges currently are relatively small in this market and an attempt to increase the charges would likely occur. However, producer groups have had the same difficulty as the Northeast in maintaining an over-order structure. A \$0.48 drop in the average differential in the Southwestern market would surely be felt by producers and accelerate the exodus of producers from the East Texas supply area, most likely smaller producers who may not have significant resources to adapt to the lowered prices or who would not be able to negotiate for higher over-order prices. Producers in New Mexico and West Texas would also be affected, but the impact may not be as severe.

Processors in this region may benefit from the decrease in Federal order prices. However, if there is an increase in the over-order prices that the processors must pay, then the amount gained from the decrease would be lessened. In fact, if over-order pricing is implemented then small processors may be at a disadvantage because they may not be able to compete for milk beyond the reduction in Class I prices.

In the Western regions, Class I differentials are expected to increase slightly. Over-order charges in these markets are not as great as in the Midwestern markets and would probably be unable to totally absorb the Class I price increase. Producer pay

prices and Class I handler costs would increase slightly. All producers would benefit from the price increase, including about 690 small producers. However, about 50 small processors may be at a disadvantage. Small processors may not have the additional revenue necessary to adapt to the \$0.18 to \$0.25 per hundredweight increase in Class I prices.

Because of the limited effect of overall Class I differential changes within individual orders, relative use differentials would have a minimal effect on small businesses, both producers and processors. Areas that have decreases in Class I differentials would have a minimal negative impact on producer pay prices. Over 20,000 producers, or about 95 percent of all producers, in these regions are categorized as small businesses. On the other hand, handlers in areas with larger

increases in the Class I differentials would experience increased competition from lower cost regions. Location advantages of some small handlers would disappear while others emerge. Handler equity in these competing markets could erode placing some small handlers under greater risk. Approximately 300 handlers in the Northeast and Southwest markets are categorized as small handlers, about half of the total number of handlers.

However, the adoption of a relative use differential could have a significant impact on small businesses, both producers and processors that are located in adjacent orders. Because Class I prices would be able to change independently from each other, significant Class I price variances may begin to exist. As Class I utilization changes, these changes may be significant. This lack of alignment

between bordering orders would increase competition in areas where Class I price differences are significant having a greater impact on small businesses.

Flat Differentials

The use of flat differentials was considered as an option for replacing the Class I price structure. Under this system, all Class I differentials would be established at \$1.60 regardless of the location. Establishing the differentials at an equal level throughout the United States does not recognize the location value associated with milk. Because this value would not be reflected in the minimum price under the Federal order program, flat differentials could affect small businesses, as shown by the following table.

FLAT CLASS I DIFFERENTIALS IN PROPOSED ORDERS

(Based on October 1995 Data)

Suggested consolidated order <sup>1</sup>	Flat differential (\$/cwt)	Weighted average differential (\$/cwt) <sup>2</sup>	Change (\$/cwt)
Northeast .....	1.60	3.14	-1.54
Appalachian .....	1.60	2.79	-1.19
Southeast .....	1.60	3.04	-1.44
Florida .....	1.60	3.89	-2.29
Midwest .....	1.60	1.91	-0.31
Central .....	1.60	2.52	-0.92
Upper Midwest .....	1.60	1.32	0.28
Southwest .....	1.60	3.01	-1.41
AZ-Las Vegas .....	1.60	2.46	-0.86
Western .....	1.60	1.84	-0.24
Pacific NW .....	1.60	1.90	-0.30

<sup>1</sup> Based on the 11 proposed orders contained in this proposed rule.

<sup>2</sup> Weighted average differential for the consolidated order is computed by summing the product of the percentage of Class I milk in each current order multiplied by the applicable current order differential.

The review of this option indicates that flat differentials could change the competitive relationship between large and small processors and producers. Large processors could have a competitive advantage over small processors in negotiating with producers for supplies of milk at prices above the established minimum price. Likewise, large producers could have a better bargaining position when competing with small producers to supply a processor.

In all areas of the United States, with the exception of the Upper Midwest, producers and processors would experience significant decreases in the Class I price. The largest decrease would occur in the Florida order with the Class I price decreasing \$2.29 per hundredweight. This would result in approximately a \$2.06 decrease in the

uniform price paid to producers. Although over-order pricing has been effective in Florida, it is unlikely that the over-order prices would be able to offset this total decrease. Data regarding over-order pricing are not published but an indication of the level is provided by comparing the Federal order Class I milk price to the announced cooperatives Class I price. In Miami, Florida, during 1996, the cooperatives announced price averaged \$2.25 per hundredweight higher than the Southeastern Florida Federal order Class I price.<sup>16</sup>

Not only could producers suffer from a loss in the value of the Class I price reflected under the order, but inequity

among processors could occur in the marketplace. More of the value of milk would be negotiated above the Federal order minimum. Because this value is outside of the regulatory minimum price, there is little that would ensure that processors are paying similar prices for milk. This could impact small processors more than larger processors because of their lack of resources needed to negotiate and obtain needed supplies of milk.

The results of implementing flat Class I pricing would be the same throughout the United States where decreases occur. Areas where flat differentials would have the greatest impact are located in the Northeast, Southeast, Southwest, and Central areas. Approximately 34,400 small producers and 480 small handlers are located in these regions of the United States.

<sup>16</sup> Table 35—1996 Annual Average Announced Cooperative Class I Prices in Selected Cities, Dairy Market Statistics, 1996 Annual Summary, USDA, AMS.

The Upper Midwest would experience a slight increase in Class I prices if a \$1.60 flat differential were implemented. The Class I price would increase by \$0.19 per hundredweight which would result in about a \$0.04 increase in the uniform price. Although there are a substantial number of small producers located in this region, approximately 28,400, this increase would not impact the price that producers in this area receive for their milk. Over-order pricing is predominant in this region. Next to Florida, the Upper Midwest region has the highest announced cooperative Class I prices, between \$1.19 to \$1.79<sup>17</sup> higher than the Federal order Class I price. Because the over-order prices are substantial in this area, the \$0.19 increase in Class I prices would likely be offset by a slight decrease in over-order prices, thus the 180 small handlers and the 28,400 small producers would likely not see any increase in overall prices.

Although the use of flat differentials would require no additional reporting, recordkeeping, or compliance requirements it is not being considered as a viable replacement for the current Class I price surface because, in addition to other reasons addressed in the proposed rule, of the impact that flat differentials could have on a substantial number of small businesses both producers and processors. Flat differentials of \$1.60 per hundredweight would negatively impact more than 52,000 total small businesses.

**Modified Flat Differentials**

The use of modified flat differentials was considered as an option for replacing the Class I price structure. This option is based on the flat Class I price concept modified by the relative use price concept. Under this system, an equal differential would be established in all orders and then, in orders that were determined to be deficit based on a Class I utilization percentage, an

additional value would be added to the flat differential. Deficit orders were deemed to have a Class I utilization greater than 70 percent. If Class I use exceeds 70 percent, the Class I differential in an order would be \$2.00 + \$0.075 \* (Class I use percent—70 percent). This option assumes that markets with Class I use equal to or below 70 percent have an adequate reserve supply of milk to meet fluid needs and that markets with Class I use about 70 percent require additional milk supplies to meet fluid demand.<sup>18</sup>

As with the relative use option (Option 2), the estimated Class I differentials presented in the table are not entirely location-specific within the consolidated order. To provide a basis for comparison, a weighted average differential has been calculated based on current differentials for the consolidated orders using October 1995 data, as shown in the following table. These differentials are also not location-specific.

**MODIFIED FLAT CLASS I DIFFERENTIALS IN PROPOSED ORDERS**  
[Based on October 1995 Data]

Proposed order <sup>1</sup>	Class I use (percent)	Mod. flat diff. (\$/cwt)	Weighted avg diff. <sup>2</sup> (\$/cwt)	Change (\$/cwt)
Northeast .....	47.9	2.00	3.14	- 1.14
Appalachian .....	81.5	2.86	2.79	0.07
Southeast .....	85.2	3.07	3.04	0.03
Florida .....	88.3	3.37	3.89	- 0.52
Mideast .....	55.8	2.00	1.91	0.09
Central .....	48.8	2.00	2.52	- 0.52
Upper Midwest .....	34.5	2.00	1.32	0.68
Southwest .....	48.1	2.00	3.01	- 1.01
AZ-Las Vegas .....	48.9	2.00	2.46	- 0.46
Western .....	29.6	2.00	1.84	0.16
Pacific NW .....	35.6	2.00	1.90	0.10

<sup>1</sup> Based on the eleven proposed orders contained in this proposed rule.

<sup>2</sup> Weighted average differential for the consolidated order is computed by summing the product of the percentage of Class I milk in each current order multiplied by the applicable current order differential.

Like flat differentials, modified flat differentials do not recognize location values associated with milk. Because this value would not be reflected in the minimum price under the Federal order program, modified flat differentials could have a dramatic effect on small businesses because modified flat differentials would change the competitive relationship between large and small processors and producers. Just as with flat differentials, large processors could maintain a competitive advantage over small processors in negotiating with producers for supplies of milk at prices above the established

minimum price. Likewise, large producers might retain strong bargaining positions when competing with small producers to supply a processor.

Under this modified flat differential, only three orders would meet the necessary requirement to have a differential established above the \$2.00 flat portion, Appalachian, Southeast, and Florida. Basically, this system would be equivalent to adopting a flat Class I pricing system in most of the United States. Although in this example the impacts appear to be different, with five of the proposed orders reflecting differential increases, this is only because the flat portion of the Class I

differential is established at \$2.00 instead of \$1.60.

As with the flat differential, the Upper Midwest producers and processors would experience Federal order Class I price increases. In this example, the estimated price would increase by \$0.59 which would return approximately \$0.12 to the producers in a higher uniform price. The largest decrease would occur in the Southwest and Northeast orders with a Class I price decrease of \$1.01 and \$1.13, respectively. The use of a modifier to the flat differential based on the Class I utilization would help to mitigate the price decreases in the Southeast orders.

<sup>17</sup> Table 35—1996 Annual Average Announced Cooperative Class I Prices in Selected Cities, Dairy Market Statistics, 1996 Annual Summary, USDA, AMS.

<sup>18</sup> The 70 percent figure was merely selected for illustrative purposes and no analysis has been conducted to determine if this is an appropriate percentage.

With the use of the modifier, the three Southeast orders would not all experience decreases in Class I prices. The Appalachian order would have a \$0.07 increase while the Florida order and the Southeast order would lose \$0.52 and \$0.01, respectively. Ultimately about 4,000 producers in the Southeast and Florida areas would experience a decline in the Class I price received under Federal orders, while nearly 4,200 producers in the Appalachian area would find their Class I price increasing.

The competitive position among processors could become altered under modified Class I differentials. More of the value of milk would be negotiated above the Federal order minimum. Because this value is outside of the regulatory minimum price, nothing would ensure that processors are paying similar prices for milk. This could impact small processors more than larger processors if the smaller processors lack the resources needed to negotiate and obtain needed supplies of milk. In addition, processors in areas where the modifier becomes effective would be placed at a disadvantage because the regulated minimum price would be allowed to fluctuate and their minimum costs would not be the same as those with the flat differential or where the Class I price is allowed to adjust. The use of \$2.00 per hundredweight modified flat

differentials would require no additional reporting, recordkeeping, or compliance requirements. However, up to 34,000 small businesses could be impacted by this proposal.

**Demand Based Differentials**

The use of demand based differentials was also considered as an option for the Class I price structure. Under this system, an equal differential would be applied to all orders, and in defined demand centers, an additional component would be added to reflect the costs of transporting milk from reserve supply areas to demand centers. This option would increase the regulatory burden on all businesses, both small and large, through additional reporting, recordkeeping, and compliance requirements. Small processors could be disadvantaged under this option.

This proposal involves establishing a fluid supply area for each market from which milk production around the major bottler locations is procured and a reserve supply area would be established that would be outside the fluid supply area from which milk production is sometimes supplied to fluid handlers in the major fluid bottling locations. The Class I differential for the reserve area under this proposal would be set at \$1.00 per hundredweight. For fluid supply areas, the differential would be \$1.00 plus transportation costs

from the reserve area to the fluid demand area. Monies paid by Class I handlers through the second part of the Class I differential would be used to fund the order's system of transportation credits and balancing payments. These transportation credits and balancing payments would be provided to organizations that supply the order's fluid market.

To encourage movement of the nearest milk supply for fluid use, two restrictions would be needed. First, a handler's total transportation credits would be limited to the variable amount paid in by the handler for transportation. Second, a handler's total transportation credit would not exceed 80 percent of the handler's transportation bill on each Class I shipment or 2.8 cents per hundredweight per 10 miles (28 cents per 100 miles), whichever is less. Any residual left after paying transportation credits would be added to the \$1.00 differential and paid to all producers in the pool.

The following table contains a few examples of differentials that would apply to specific locations. These differentials are based on the farthest distance that milk for fluid use is transported, using the USDSS<sup>19</sup> model to solve for each consumption point individually as a guide for establishing the differentials.

DEMAND-BASED CLASS I DIFFERENTIALS FOR SELECTED CITIES

Selected location	Current differential (\$/cwt)	Demand-based differential (\$/cwt)	Change (\$/cwt)
Miami, FL .....	4.18	3.88	-0.30
Tampa, FL .....	3.88	2.05	-1.83
Orlando, FL .....	3.88	3.08	-0.80
New Orleans, LA .....	3.65	1.28	-2.37
Atlanta, GA .....	3.08	2.38	-0.70
New York City, NY .....	3.14	1.80	-1.34
Chicago, IL .....	1.40	1.49	-0.09
Minneapolis, MN .....	1.20	1.11	-0.09
Phoenix, AZ .....	2.52	1.00	-1.52
Dallas, TX .....	3.16	1.40	-1.76
Denver, CO .....	2.73	1.19	-1.54
Portland, OR .....	1.90	1.13	-0.77
Seattle, WA .....	1.90	1.31	-0.59
Boise, ID .....	1.50	1.06	-0.44

The review of this option from a producer viewpoint reveals that a demand based differential system is comparable to a flat differential option. Producers would only be ensured that the \$1.00 portion of the differential would be returned through the blend price. Ultimately, this option could

<sup>19</sup>US Dairy Sector Simulator model developed and run by Cornell University to solve for the

result in income losses for all producers, both large and small. Although additional money is generated by the demand based differential above the \$1.00, this additional money would be used to fund transportation costs associated with servicing the Class I market. The differentials are established

geographical spatial relationships of milk for particular uses of milk, primarily fluid.

at a lower level that would negatively impact all 82,900 producers because of the decrease in the actual value of Class I revenue that is reflected in the Federal order minimum price. Thus, the disadvantages that producers, especially small producers, might experience under a flat or modified flat differential

system are applicable to demand based differentials.

Like the two previous options, small handlers also could be disadvantaged, because less of the actual value of Class I milk is reflected under the regulated price which may lead to both processors and producer inequity. The potential negative effects discussed under flat differentials and modified flat differentials also apply to demand based differentials. In addition, the adoption of demand-based differentials would result in a significant increase in reporting, recordkeeping, and compliance activities which would impact all 1,450 handlers, but is likely to be a greater burden on small handlers. To ensure reimbursement for a portion or all of a processors handling charges, complete and detailed transportation records must be kept. New forms would be required for submission, along with copies of all transportation invoices. The additional information could require more personnel, training, and technology to automatically keep track of such information. While the costs associated with this degree of recordkeeping are not available, they could be significant enough to disadvantage small businesses.

Because the use of demand-based differentials could result in a significant increase in regulatory burdens to all handlers as well as inequity among producers and processors, demand-

based differentials are not considered a viable alternative.

**Decoupled Baseline Class I Price with Adjustors**

The use of a decoupled baseline Class I price with adjustors was considered as an option for replacing the Class I price structure. Under this system, the Class I price would be decoupled from the basic formula price, or the Class I price mover, and a base price would be established at a specified level. Adjustments to this base price would be made utilizing a supply/demand adjustor and possibly a cost of production indicator.

Under this option for Class I purposes the base price would be floored at \$13.63 per hundredweight, the November 1995 to October 1996 average BFP. This price level would be used to establish Class I prices using current differentials. A supply/demand adjustor of \$0.12 per hundredweight for each 2 percent change in the rolling average utilization would be used to change prices in each of the orders to reflect long-term trends. For example, a Class I utilization change from 44 percent to 46 percent in a market would result in a \$0.12 per hundredweight gain in the market's Class I differential. Once the utilization level changes, the new utilization rate becomes the base for future changes. Thus, if a market falls from 44 percent to 42 percent, the new

base for comparing a 2-percentage point change up or down is 42 percent.

In addition to the supply/demand adjustor, a cost of production indicator would be developed whereby Class I prices would be increased in a timely manner when input costs to dairy farmers are increasing. One such economic indicator might be feed costs. While one such adjustor was developed and submitted, it was received too late to be included in this analysis.

The following table illustrates the initial Class I differentials under the proposed consolidated orders. These differentials are not location-specific within the applicable orders. For purposes of this analysis and to provide a basis for comparison within the proposed consolidated orders, a weighted average Class I differential has been calculated for each order based on October 1995 data. This weighted average differential is computed by multiplying the percentage of Class I milk in each of the current orders that comprise the consolidated order by the applicable current order differential and adding the resulting amounts. The weighted average differential is not location-specific for the consolidated order.

Initially the differentials would be the same. However, as this option impacts production (supply) and use (demand), there would be a change in the utilization percentage, thereby causing the differentials to vary.

**INITIAL CLASS I DIFFERENTIALS IN PROPOSED ORDERS BASED ON 1995 DATA UNDER DECOUPLED BASELINE CLASS I PRICE WITH ADJUSTORS SYSTEM**

Proposed order	Weighted average differential (\$/cwt) <sup>1</sup>	Initial class I differential (\$/cwt)	Change in differential (\$/cwt)
Northeast .....	3.14	3.14	0.00
Appalachian .....	2.79	2.79	0.00
Southeast .....	3.04	3.04	0.00
Florida .....	3.89	3.89	0.00
Mideast .....	1.91	1.91	0.00
Central .....	2.52	2.52	0.00
Up Midwest .....	1.32	1.32	0.00
Southwest .....	3.01	3.01	0.00
AZ-Las Vegas .....	2.46	2.46	0.00
Western .....	1.84	1.84	0.00
Pacific NW .....	1.90	1.90	0.00

<sup>1</sup> Weighted average differential for the consolidated order is computed by summing the product of the percentage of Class I milk in each current order multiplied by the applicable current order differential.

The review of this option indicates that the decoupled baseline Class I price with adjustors would create some disruption in inter-market price alignment because Class I differentials would be allowed to adjust independently from each other and may have a serious impact on producers and

processors, particularly small producers and processors. If Class I differentials are allowed to adjust frequently, price alignments established between and among markets would disappear causing inequity among competing handlers. It is this inequity amongst handlers that would have a significant

impact on a small business's ability to compete in the marketplace.

Analysis completed by the multi-regional ERS model<sup>20</sup> indicates that the increase in prices experienced would

<sup>20</sup> Economic Research Service multi-regional model of the dairy industry.

not be sustainable. The results of the model analysis indicate that the higher floored Class I prices would impact the all milk price and after 3 years, producers would begin experiencing a decrease in the revenue initially generated by this option. This would occur because the higher blend prices (caused by higher Class I prices) would stimulate milk production which would then lead to lower manufacturing prices. Because it is the blend price that is paid to producers, the increase in the Class I prices would not be enough to offset the decrease in prices of the other classes of use and the changes in utilization which would affect the differential levels.

Initially Class I differentials would not change however, Class I prices would increase because of the inclusion of a higher floor price. With the use of a floor, the variability in Class I prices would be moderated. However, the use of the floor price may impact the 79,600 smaller producers differently than the 8,400 larger producers because the smaller producers may not have the necessary financial resources to endure such a transition.

The Proposed Class I Price Options

The options proposed in this rule are a result of extensive review of the current marketing structure and other pertinent information. Extensive outreach, as explained previously, resulted in substantial input from the public. After gathering the necessary information, two options were developed and are advanced in this proposed regulation as viable Class I price structures.

Currently, the Class I price structure recognizes that milk has value by location. By recognizing that milk has value by location, small businesses are placed more on the same competitive footing as large businesses in the minimum prices they pay for milk. The use of either location-specific differentials or relative-value differentials would provide the necessary recognition of the location value of milk but at different levels.

Location-Specific Differentials (Option 1A)

This option would establish a nationally coordinated system of location-specific Class I price

differentials reflecting the relative economic value of milk by location. An important feature of the option is including location adjustments that geographically align minimum Class I milk prices paid by fluid milk processors nationwide regardless of defined milk marketing area boundaries or order pooling provisions. A basic premise of this option is that the value of milk varies according to location across the United States.

The level of the location-specific differentials proposed in this regulation are such that small businesses would experience minimal impacts if the regulations were implemented. The differentials are based on economic model results,<sup>21</sup> current marketing conditions, and the costs of obtaining alternative supplies of milk. Since a price is established for every county under this option, the following table sets forth examples of adjusted differentials at selected cities. Map 2 and General Provisions § 1000.52, as contained in the discussion on price structure, set forth the location adjusted differentials in every county.

COMPARATIVE LOCATION-SPECIFIC CLASS I DIFFERENTIALS AT SELECTED CITIES

City	Class I differential		Difference
	Current	Loc.-specific diff	
	Dollars Per Hundredweight		
New York City, NY .....	3.14	3.15	.01
Charlotte, NC .....	3.08	3.10	.02
Atlanta, GA .....	3.08	3.10	.02
Tampa, FL .....	3.88	4.00	.12
Cleveland, OH .....	2.00	2.00	.00
Kansas City, MO .....	1.92	2.00	.08
Minneapolis, MN .....	1.20	1.70	.50
Chicago, IL .....	1.40	1.80	.40
Dallas, TX .....	3.16	3.00	(.16)
Salt Lake City, UT .....	1.90	1.90	.00
Phoenix, AZ .....	2.52	2.35	(.17)
Seattle, WA .....	1.90	1.90	.00

Other than in the southwestern portions of the United States, this proposed option would have little impact on most producers both large and small. Likewise, processors should not experience any substantial changes in their abilities to compete for milk supplies. In fact, producers and processors should experience improvements because location-specific differentials provide improvements in areas under the current system that are not as well aligned. In addition processors would experience improvements in competing for milk

<sup>21</sup> USDSS results using May and October 1996 data.

because the price is established for each county regardless of where the milk is pooled. Because more of the actual value of Class I milk is reflected in the minimum regulated price, both small producers and processors can be assured of maintaining their ability to compete for a supply of milk.

A review of the six year average quantitative analysis conducted using the ERS model, assuming implementation of the consolidated orders, four classes of use, BFP as proposed, and using location-specific differentials would result in a decrease in Class I utilization but an increase of

\$0.03 in the all-milk price. Overall, this pricing option would result in \$55 million increase in cash receipts.

The use of location-specific differentials would require no additional reporting, recordkeeping, or compliance requirements.

Relative-Value Specific Differentials (Option 1B).

A nationally coordinated system of relative-value specific Class I price differentials and adjustments that recognizes several low pricing areas is the second of two options proposed. These differentials rely on a least cost

optimal solution from the USDSS Cornell model to develop a Class I price structure that is based on the most efficient assembly and shipment of milk and dairy products to meet all market demands for milk and its products. This option relies more on the market and the negotiating ability of processors and producers to generate higher prices when needed to provide the necessary incentive to move milk in order to satisfy demand.

Relative-value specific differentials are designed to move the dairy industry into more market-oriented environment by reducing reliance on Federal regulations in establishing actual Class I milk prices. By lowering the differentials in most of the United States, marketing practices would have a greater impact on Class I values in the form of over-order prices and only the producers who perform for the market would benefit. Hence, the adoption of relative-value differentials would move

the dairy industry to rely on the negotiating abilities of both dairy farmers and processors to determine actual Class I values. Less efficient small businesses could be disadvantaged because of the lack of resources and knowledge necessary to effectively negotiate and maintain necessary price levels. Map 3 and General Provisions § 1000.52, as contained in the proposed rule, set forth the differentials in every county. The following table sets forth adjusted differentials at selected cities.

COMPARATIVE RELATIVE VALUE-SPECIFIC CLASS I DIFFERENTIALS AT SELECTED CITIES

City	Current diff.	Rel. value-specific diff.	Difference
New York City, NY .....	3.14	2.07	(1.07)
Charlotte, NC .....	3.08	1.89	(1.19)
Atlanta, GA .....	3.08	2.46	(0.62)
Tampa Bay, FL .....	3.88	3.81	(0.07)
Cleveland, OH .....	2.00	1.54	(0.46)
Kansas City, MO .....	1.92	1.45	(0.47)
Minneapolis, MN .....	1.20	1.20	0.00
Chicago, IL .....	1.40	1.65	0.25
Dallas, TX .....	3.16	1.68	(1.48)
Salt Lake City, UT .....	1.90	1.08	(0.82)
Phoenix, AZ .....	2.52	1.14	(1.38)
Seattle, WA .....	1.90	1.00	(0.90)

The level of the relative value-specific differentials proposed in this rule are such that without a phase-in and a transitional program, small businesses, particularly producers, would experience significant economic impacts. Reviewing the change in Class I differentials on an individual order basis reveals that, with the exception of producers located in the Upper Midwest region, all producers would likely face reduced income due to lower minimum Class I prices if relative value-specific differentials were implemented immediately. Producers located in the Northeast and Southwest would experience the greatest decrease.

However, with the use of a phase-in together with one of the proposed transitional program alternatives, the impacts on small businesses could be mitigated during the transition period. The use of a transition program alternative would also allow both producers and processors the opportunity to adapt their marketing practices to adjust to a new level of Class I differentials. At the conclusion of the transition period, small businesses should have adjusted to lower regulated Class I differentials and be able to compete in a more market-oriented environment.

Three possible alternatives are presented for consideration of phasing

in relative value-specific differentials to minimize the market disruption that may initially occur. Each utilizes the difference between the current differentials and the final relative value-specific differentials as the basis of the phase-in. This difference is then reduced by 20 percent during each phase-in year until the final relative value-specific differential price is achieved. The phase-in would begin in 1999 and be completed by 2003. The base differentials resulting from this transitional phase-in are set forth in the following table. The first alternative would be to phase-in to these differentials.

RELATIVE VALUE-SPECIFIC BASE DIFFERENTIALS FOR USE IN PHASE-IN PROGRAM OPTIONS

City	Current	Relative Value-Specific Base Differentials <sup>1</sup>				
		1999	2000	2001	2002	2003
Dollars Per Hundredweight						
New York City .....	3.14	2.93	2.71	2.50	2.28	2.07
Charlotte .....	3.08	2.84	2.60	2.37	2.13	1.89
Atlanta .....	3.08	2.96	2.83	2.71	2.58	2.46
Tampa Bay .....	3.88	3.87	3.85	3.84	3.82	3.81
Cleveland .....	2.00	1.91	1.82	1.72	1.63	1.54
Kansas City .....	1.92	1.83	1.73	1.64	1.54	1.45
Minneapolis .....	1.20	1.20	1.20	1.20	1.20	1.20
Chicago .....	1.40	1.45	1.50	1.55	1.60	1.65
Dallas .....	3.16	2.86	2.57	2.27	1.98	1.68
Salt Lake City .....	1.90	1.74	1.57	1.41	1.24	1.08

RELATIVE VALUE-SPECIFIC BASE DIFFERENTIALS FOR USE IN PHASE-IN PROGRAM OPTIONS—Continued

City	Current	Relative Value-Specific Base Differentials <sup>1</sup>				
		1999	2000	2001	2002	2003
Phoenix .....	2.52	2.24	1.97	1.69	1.42	1.14
Seattle .....	1.90	1.72	1.54	1.36	1.18	1.00

<sup>1</sup> Base differential obtained by taking the difference between the current differential and the final relative value-specific differential (year 2003) and multiplying by 20 percent. This value is then subtracted from the current differential to yield the 1999 base differential. This value is then deducted from each consecutive year's value until the relative value-specific differentials are achieved in 2003.

The second alternative for phasing-in to the relative value-specific differentials would consist of adding a decreasing "transitional payment" to the base differential. It would be equal to the decrease in revenue that would occur with the implementation of relative value-specific differentials during the four years of transitioning to these differentials (1999 to 2002). During this four-year period, it is projected that \$388.6 million would be removed from the Federal order system

through lowered Class I differentials in most markets. To provide the industry an opportunity to prepare for this change, a transitional payment would be added to the base differential for Class I milk. The payment would be higher in the first year and gradually be reduced thereafter to result in implementation of the relative value-specific differentials by 2003. The additional payment would equal \$0.55 per hundredweight in 1999, \$0.35 per hundredweight in 2000, \$0.20 per hundredweight in 2001, and \$0.10

per hundredweight in 2002. This offsetting of revenue is designed to temporarily reduce the impacts of implementing relative value-specific differentials, thus allowing producers an opportunity to adjust their marketing practices to adapt to more market-determined Class I pricing. The following table sets forth the adjusted Class I differentials under this revenue-neutral phase-in option for selected cities.

RELATIVE VALUE-SPECIFIC CLASS I DIFFERENTIALS WITH REVENUE NEUTRAL PHASE-IN PAYMENTS

City	Current	Class I diff. with revenue neutral phase-in				
		1999 <sup>1</sup>	2000 <sup>2</sup>	2001 <sup>3</sup>	2002 <sup>4</sup>	2003 <sup>5</sup>
Dollars Per Hundredweight						
New York City, NY .....	3.14	3.48	3.06	2.70	2.38	2.07
Charlotte, NC .....	3.08	3.39	2.95	2.57	2.23	1.89
Atlanta, GA .....	3.08	3.51	3.18	2.91	2.68	2.46
Tampa Bay, FL .....	3.88	4.42	4.20	4.04	3.92	3.81
Cleveland, OH .....	2.00	2.46	2.17	1.92	1.73	1.54
Kansas City, MO .....	1.92	2.38	2.08	1.84	1.64	1.45
Minneapolis, MN .....	1.20	1.75	1.55	1.40	1.30	1.20
Chicago, IL .....	1.40	2.00	1.85	1.75	1.70	1.65
Dallas, TX .....	3.16	3.41	2.92	2.47	2.08	1.68
Salt Lake City, UT .....	1.90	2.29	1.92	1.61	1.34	1.08
Phoenix, AZ .....	2.52	2.79	2.32	1.89	1.52	1.14
Seattle, WA .....	1.90	2.27	1.89	1.56	1.28	1.00

<sup>1</sup> 1999 applicable base differential from the previous table plus \$0.55.  
<sup>2</sup> 2000 applicable base differential from the previous table plus \$0.35.  
<sup>3</sup> 2001 applicable base differential from previous table plus \$0.20.  
<sup>4</sup> 2002 applicable base differential from the previous table plus \$0.10.  
<sup>5</sup> Final relative value-specific differentials.

The use of a revenue-neutral phase-in program would decrease the amount of cash receipts removed from the Federal order system from \$388.6 million during the four-year phase-in to a gain of \$47.8 million with the offsetting compensation implementation and then effective relative-value differentials. The decrease in the all-milk price paid to producers would also be reduced from \$0.04 per cwt to \$0.02 per cwt for the six-year average.

In fact, during the first year of offsetting compensation implementation the Class I price would increase for all but one of the Federal orders. On average, for all markets, the Class I price would increase \$0.39 per cwt, the all-

milk price would increase an average of \$0.13 per cwt, and total cash receipts would be increased by \$193.9 million compared with the baseline. Although these values would be decreased by the sixth year, with Class I prices projected to decrease for all Federal order an average of \$0.51, the all-milk prices projected to decrease an average of \$0.09, and total cash receipts projected to decrease \$128.5 million, all producers would benefit from the lessening of the impacts of moving towards the relative-value differentials.

The third approach to phasing in the relative value-specific differentials would consist of adding a decreasing "transitional payment" to the base

differential that would enhance revenue beyond what the Class I system would have generated during the four years of transitioning to the relative value-specific differentials. During this four-year period, it is projected that \$878.4 million would be added to the Federal order system through the revenue-enhanced payment. This would result in a net increase of \$489.8 million added to the system once the projected decrease resulting from the relative value-specific differentials during this period is deducted. This additional money would not only provide producers with an opportunity to prepare for and restructure their marketing practices to adapt to more

market determined Class I pricing but would also allow producers to obtain the education and resources necessary to become more effective in a more market-oriented environment. Again, the payment in the first year would be

the highest with reductions occurring thereafter to result in implementation of the relative value-specific differentials by 2003. The additional payment would equal \$1.10 per hundredweight of Class I in 1999, \$0.70 per hundredweight in

2000, \$0.40 per hundredweight in 2001, and \$0.20 per hundredweight in 2002. The following table sets forth the adjusted Class I differentials under this revenue-enhancement phase-in option for selected cities.

RELATIVE VALUE-SPECIFIC CLASS I DIFFERENTIALS WITH REVENUE ENHANCEMENT PHASE-IN PAYMENTS

City	Current	Class I diff. with revenue enhancement				
		1999 <sup>1</sup>	2000 <sup>2</sup>	2001 <sup>3</sup>	2002 <sup>4</sup>	2003 <sup>5</sup>
Dollars Per Hundredweight						
New York City, NY .....	3.14	4.03	3.41	2.90	2.48	2.07
Charlotte, NC .....	3.08	3.94	3.30	2.77	2.33	1.89
Atlanta, GA .....	3.08	4.06	3.53	3.11	2.78	2.46
Tampa Bay, FL .....	3.88	4.97	4.55	4.24	4.02	3.81
Cleveland, OH .....	2.00	3.01	2.52	2.12	1.83	1.54
Kansas City, MO .....	1.92	2.93	2.43	2.04	1.74	1.45
Minneapolis, MN .....	1.20	2.30	1.90	1.60	1.40	1.20
Chicago, IL .....	1.40	2.55	2.20	1.95	1.80	1.65
Dallas, TX .....	3.16	3.96	3.27	2.67	2.18	1.68
Salt Lake City, UT .....	1.90	2.84	2.27	1.81	1.44	1.08
Phoenix, AZ .....	2.52	3.34	2.67	2.09	1.62	1.14
Seattle, WA .....	1.90	2.82	2.24	1.76	1.38	1.00

<sup>1</sup> 1999 applicable base differential from the second previous table plus \$1.10.

<sup>2</sup> 2000 applicable base differential from the second previous table plus \$0.70.

<sup>3</sup> 2001 applicable base differential from the second previous plus \$0.40.

<sup>4</sup> 2002 applicable base differential from the second previous plus \$0.20.

<sup>5</sup> Final relative value-specific differentials.

The use of a revenue-enhancement phase-in program would increase the amount of cash receipts within the Federal order system by an average \$34.9 million for a six-year period that includes implementing and then effective relative value-specific differentials. For the six-year average, the all-milk price would be unchanged. During the first year of implementation Class I prices would increase an average of \$0.91 per cwt, all-milk prices would increase an average of \$0.30 per cwt, and total cash receipts would increase \$425 million. Although these values would decrease by the sixth year, with Class I prices down an average of \$0.48, all-milk prices down \$0.06, and total cash receipts down \$80.5 million, all producers would benefit from the lessening of the impacts of moving towards relative value-specific differentials that are more market-oriented and less governmentally regulated.

Although producers would benefit from the initial increases in the Class I prices, this may put small businesses at a disadvantage because the cost of the raw product during the initial implementation years would be higher than the current regulated minimum prices. In areas such as the Upper Midwest and Southeast where over-order pricing has been effective in establishing the actual value of Class I milk, small processors may actually

benefit from having more of the total cost of the milk reflected in the minimum price. This may increase the equity amongst the competing handlers in these regions. There are approximately 200 small handlers located in these two regions. About 600 small handlers located most other places in the United States may find that the increase in the Class I price could change their competitive relationships.

No additional recordkeeping, reporting, or compliance requirements would be necessary to implement the relative value-specific differentials discussed above.

#### The Proposed Classification Options

The classification of milk recommendations should not have a significant economic impact on a substantial number of small businesses. This proposed rule provides uniform milk classification provisions for the newly consolidated milk orders. The recommendations should improve reporting and accounting procedures for handlers and provide for greater market efficiencies.

Most of the changes regarding milk classification provisions proposed for the newly consolidated orders would simplify order language and remove obsolete language.

This proposed rule contains a modified fluid milk product definition

and recommends that certain products be reclassified. The revised fluid milk product definition proposed for the new orders should provide more consistency in determining the classification of products. The inclusion of eggnog to the list of fluid milk products and the reclassification of cream cheese from Class III to Class II will cause a nominal increase in the cost of the finished product. However, these changes, which will be applicable to all handlers regulated under the new orders, should not have a significant impact on the retail price of these products. Although producers will benefit from these products being reclassified into higher utilization classes, the impact of the product classification changes on the blend price to producers will be marginal.

Another modification includes the reclassification of butter and whole milk powder from Class III to Class IV. This change merely places these market-clearing products in the new Class IV with nonfat dry milk. The change promotes market efficiency and should have a minimal impact on producers' blend prices.

One recommendation with possible small business implications concerns the treatment of milk used to produced bulk sweetened condensed milk/skim milk. Some commenters argued that the wide price difference that sometimes exists between the Class II price and the

Class III-A price has put manufacturers of sweetened condensed milk at a competitive disadvantage with manufacturers of nonfat dry milk, which can be substituted for bulk sweetened condensed milk and skim milk in some higher-valued products.

Although this proposed rule does not recommend a reclassification for milk used in bulk sweetened condensed milk, it does propose a change in the relationship between the Class II and IV prices which should eliminate the price disparity that now, at times, exists. As discussed in the "Class III and Class III-A (i.e., Class IV) Milk" section of this proposed rule, the proposed new Class II price will be equal to the Class IV price plus a 70-cent differential. The coupling of the Class II and Class IV prices will largely remove the incentive to substitute nonfat dry milk for bulk sweetened condensed milk.

The recommendations regarding shrinkage provisions should provide equity among handlers, improve market efficiencies, and facilitate accounting procedures. This proposed rule provides that shrinkage be assigned pro rata based on a handler's utilization. As discussed in the "Shrinkage and Overage" section of this proposed rule, this modification should result in a slight increase (i.e., one cent per cwt.) in the blend price paid to producers.

For the reasons stated above, the milk classification provisions proposed herein should have little economic and regulatory impact on small businesses.

#### *Paperwork Reduction Act of 1995*

The information collection requirements contained in this proposed rule previously were approved by the Office of Management and Budget (OMB) pursuant to the Paperwork Reduction Act of 1995 (44 U.S.C. chapter 35) under OMB control number 0581-0032, through May 31, 1998. A notice of request for a three-year extension and revision of this currently approved information collection was published in the December 2, 1997, **Federal Register** (62 FR 63693), which invited comments from the public through February 2, 1998.

The amendments set forth in this proposed rule do not contain additional information collections that require clearance by the OMB under the provisions of 44 U.S.C. Chapter 35. Following is a general description of the reporting and recordkeeping requirements, reasons for these requirements and an estimate of the annual burden on the dairy industry.

*Title:* Report Forms Under Federal Milk Orders (From Milk Handlers and Milk Marketing Cooperatives).

*OMB Control Number:* 0581-0032.  
*Expiration Date of Approval:* May 31, 1998.

*Type of Request:* Extension and revision of a currently approved information collection.

*Abstract:* Federal Milk Marketing Order regulations authorized under the Agricultural Marketing Agreement Act of 1937, as amended (7 U.S.C. 601-674), require milk handlers to report in detail the receipt and utilization of milk and milk products handled at each of their plants that are regulated by a Federal Order. The data are needed to administer the classified pricing system and related requirements of each Federal Order.

Rulemaking amendments to the orders must be approved in referenda conducted by the Secretary.

The terms of each of the current milk marketing orders are found at 7 CFR Parts 1001-1199; the terms of each of the proposed orders in this document are found at 7 CFR Parts 1001-1134. The authority for requiring reports is found at 8c (5) and (7) and 8d of the Act. The current authority for requiring records to be kept is found in the general provisions at 7 CFR Part 1000.5. In this proposed rule, this authority is found in the general provisions at 7 CFR Part 1000.27. The Act also provides for milk marketing agreements, but there are none in effect.

A Federal milk marketing order is a regulation issued by the Secretary of Agriculture that places certain requirements on the handling of milk in the area it covers. It requires that handlers of milk for a marketing area pay not less than certain minimum class prices according to how the milk is used. These prices are established under an order on the basis of evidence concerning the supply and demand conditions for milk in the market. A milk order requires that payments for milk be pooled and paid to individual farmers or cooperative associations of farmers of the basis on a uniform or average price. Thus, all eligible farmers (producers) share in the market wide use-values of milk by regulated handlers.

The Report of Receipts and Utilization and the Producer Payroll Report are completed by regulated milk handlers and milk marketing cooperatives and are the principal reporting forms needed to administer the 31 Federal milk marketing orders.

The orders also provide for the public dissemination of market statistics and other information for the benefit of producers, handlers, and consumers. Each milk order is administered by a market administrator who is an agent of

the Secretary of Agriculture. Part of the market administrator's duties are to prescribe reports required of each handler, and to assure that handlers properly account for milk and milk products, and that such handlers pay producers and associations of producers according to the provisions of the order. The market administrator employs a staff that verifies handlers' reports by examining records to determine that the required payments are made to producers. Most reports required from handlers are submitted monthly to the market administrator. Confidentiality of information collection is assured through Section 608(d) of the Act, which imposes substantial penalties on anyone violating these confidentiality requirements.

The forms used by the market administrators are required by the respective milk orders that are authorized by the Act. The forms are authorized either in the general provisions (Part 1000) or in the sections of the respective orders. The forms are used to establish the quantity of milk received by handlers, the pooling status of handlers, the class-use of the milk used by the handler and the butterfat content and amounts of other components of the milk.

The frequency of performing these recordkeeping and reporting duties varies according to the form; the frequency ranges from "on occasion" to "annually" but "monthly" is perhaps most common. In general, most of the information that handlers report to the market administrator is readily available from normally maintained business records. Thus, the burden on handlers to complete these recordkeeping and reporting requirements is expected to be minimal. In addition, assistance in completing forms is readily available from market administrator offices.

Regarding the use of improved information technology to reduce the reporting and recordkeeping burden, the information requested is the minimum necessary to carry out the program. Since the type of information required to be collected and the certification and reporting of that information is required, no other alternative to the mode of information collection has been found. However, where possible, reported information is accepted using computer tapes or diskettes as alternatives to submitting the requested information on these report forms. Comments are requested to help assess the number of handlers using computers, word processors and other electronic equipment to create and store documents, as well as the extent to

which the Internet is used to exchange information.

We are confident that the information we collect does not duplicate information already available. Dairy Programs has an ongoing relationship with many organizations in the dairy industry that also respond to other governmental agencies. Thus, we are aware of the reports dairy industry organizations are submitting to other government agencies.

Information collection requirements have been reduced to the minimum requirements of the order, thus minimizing the burden on all handlers—those considered to be small as well as large entities. Forms require only a minimal amount of information which can be supplied without data processing equipment or a trained statistical staff. The primary source of data used to complete the forms is routinely used in all business transactions. Thus, the information collection and reporting burden is relatively small. Requiring the same reporting requirements for all handlers does not significantly disadvantage any handler that is smaller than industry average.

If the collection of this information were conducted less frequently, data needed to keep the Secretary informed concerning industry operations would not be available. Timing and frequency of the various reports are such to meet the needs of the industry and yet minimize the burden of the reporting public.

The collection of the required information is conducted in a manner consistent with guidelines in 5 CFR 1320.6. The orders require that the market administrator compute monthly minimum prices to producers based on monthly information. Without monthly information, the market administrator, for example, would not have the information to compute each monthly price, nor to know if handlers were paying producers on dates prescribed in the order, such as the advance payment for milk received the first 15 days of the month and the final payment which is payable after the end of the month. The Act imposes penalties for order violations, such as the failure to pay producers not later than prescribed dates. The orders require payments to and from the producer-settlement fund to be made monthly. Also, class prices are based on the monthly Basic Formula price series.

#### *Annual Reporting and Recordkeeping Burden*

*Estimate of Burden:* Public reporting burden for this collection of information

is estimated to average 0.87 hours per response.

*Respondents:* Milk Handlers and Milk Marketing Cooperatives.

*Estimated Number of Respondents:* 772.

*Estimated Number of Responses per Respondent:* 35.

*Estimated Total Annual Burden on Respondents:* 23,858 hours.

*Estimated annual cost to respondents for report preparation:* \$276,514 (23,858 hours at \$11.59 per hour). Although hourly rates vary among handlers in various localities, the wage paid to clerical workers engaged in report preparation is estimated to be comparable to about a grade GS-7, step 1.

It is important to note that the burden being reported is an estimate of the amount of time that would be required of current program participants, as was published in the Notice of Request for Extension, referenced in the introductory text of this section.

It is expected that this proposed rule would have little impact on the reporting and recordkeeping burden on handlers regulated under the Federal milk marketing order program. In fact, as a result of the consolidation of Federal orders from 31 to 11 as proposed, an overall reduction in reporting and recordkeeping requirements may occur due to greater uniformity in forms used and fewer "special" forms that currently apply to one or a few orders.

Non-substantial changes would be necessary on the required reports and records to correctly identify the new Federal market order (e.g. the current—and separate—reports for the Upper Florida, Tampa Bay and Southeastern Florida marketing areas would be combined into one report for the Florida marketing area).

#### *Request for Public Input*

Comments on the Executive Order 12866 analysis, the initial regulatory flexibility analysis, and the paperwork reduction analysis are requested. Specifically, interested parties are invited to submit comments on the regulatory and informational impacts of this proposed rule on small businesses. Comments are requested within 60 days of publication of this proposed rule in the **Federal Register**. Comments should be mailed to USDA/AMS/Dairy Programs, Order Formulation Branch, Room 2968, South Building, P.O. Box 96456, Washington, D.C. 20090-6456.

#### *Preliminary Statement*

The material issues in this proposed rule relate to:

1. Consolidation of marketing areas.
2. Basic formula price replacement and other class price issues.
3. Class I price structure.
4. Classification of milk and related issues.
5. Provisions applicable to all orders.
6. Regional issues:
  - a. Northeast Region.
  - b. Southeast Region.
  - c. Midwest Region.
  - d. Western Region.
7. Miscellaneous and administrative matters.
  - a. Consolidation of the marketing service, administrative expense, and producer-settlement funds.
  - b. Consolidation of the transportation credit balancing funds.
  - c. Proposed general findings.

#### **II. Discussion of Material Issues and Proposed Amendments to the Orders**

A discussion and explanation of the material issues and proposals contained in this rule are as follows:

##### *1. Consolidation of Marketing Areas*

Subtitle D, Chapter 1 of the 1996 Farm Bill, entitled "Consolidation and Reform of Federal Milk Marketing Orders," requires, among other things, that the Federal milk marketing orders be limited to not less than 10 and not more than 14. Over 400 public comments have been received in response to requests from USDA for public input on the subject of order consolidation. Two preliminary reports on order consolidation have been issued by the Agricultural Marketing Service's Dairy Division. The initial Preliminary Report on Order Consolidation was issued in December 1996, and the Revised Preliminary Report was issued in May 1997. The December 1996 Report suggested that the 32 Federal milk marketing orders then in existence be consolidated to 10, and the May 1997 Report suggested 11. All comments received by the Department have been considered in the development of this proposed rule.

Although the Farm Bill specifically provides for the inclusion of California as a separate Federal milk order, the provision is contingent upon petition and approval by California producers. Interest in a Federal milk order has been expressed by some California producers, but the degree of interest expressed and the input provided by the producers has not been adequate to proceed with a proposed order for California.

The preliminary reports concerning order consolidation and this proposal were prepared using data gathered about receipts and distribution of fluid milk products by all known distributing

plants located in the 47 contiguous states, not including the State of California. Data describing the sources and disposition of fluid milk products for the month of October 1995 was used to compile the initial Preliminary Report. In response to comments and questions about certain marketing area boundaries and changes in marketing conditions in some of the markets after publication of the initial Preliminary Report, data concerning these markets was updated to January 1997, and more detailed information was gathered regarding the geographic distribution of route sales by individual handlers and their specific sources of producer milk. Specifically, such information was gathered for all or parts of the initially-suggested Northeast, Appalachian, Southeast, Mideast, Central, and Western marketing areas.

The eleven marketing areas suggested in the Revised Preliminary Report on Order Consolidation have, in some cases, been modified for this proposed rule. Several of the suggested marketing areas were the subjects of numerous comments containing information that indicated that the boundaries of those areas should be re-evaluated. As a result of the comments received, marketing data was further examined and analyzed for some of the suggested consolidated marketing areas to determine the most appropriate configurations of the consolidated areas to be included in this proposed rule. The result of the examination and analysis was to modify significantly from the Revised Preliminary Report the marketing areas of the proposed Northeast, Mideast, Upper Midwest, Central, and Southeast orders, and to make minor modifications to the marketing area of the proposed Appalachian order.

As in the case of data referring to the operations of less than three handlers or producers in the initial and Revised Preliminary Consolidation Reports, some of the data used to arrive at the proposed consolidated areas is restricted from use by the public because it refers to individual fluid milk distributing plants and the origins of producer milk supply for those plants. However, the basis for the proposed marketing area boundaries is described as specifically as possible without divulging such proprietary information.

Seven primary criteria were used in determining which markets exhibit a sufficient degree of association in terms of sales, procurement, and structural relationships to warrant consolidation. These are the same criteria which were used in the two reports on order consolidation issued by the Dairy

Division (November 1996 and May 1997). The criteria are as follows:

#### 1. Overlapping Route Disposition

The movement of packaged milk between Federal orders indicates that plants from more than one Federal order are in competition with each other for Class I sales. In addition, a degree of overlap that results in the regulatory status of plants shifting between orders creates disorderly conditions in changing price relationships between competing handlers and neighboring producers. This criterion is considered to be the most important.

#### 2. Overlapping Areas of Milk Supply

This criterion applies principally to areas in which major proportions of the milk supply are shared between more than one order. The competitive factors affecting the cost of a handler's milk supply are influenced by the location of the supply. The pooling of milk produced within the same procurement area under the same order facilitates the uniform pricing of producer milk. Consideration of the criterion of overlapping procurement areas does not mean that all areas having overlapping areas of milk procurement should be consolidated. An area that supplies a minor proportion of an adjoining area's milk supply with a minor proportion of its own total milk production while handlers located in the area are engaged in minimal competition with handlers located in the adjoining area likely do not have a strong enough association with the adjoining area to require consolidation.

For a number of the proposed consolidated areas it would be very difficult, if not impossible to find a boundary across which significant quantities of milk are not procured for other marketing areas. In such cases, analysis was done to determine where the minimal amount of route disposition overlap between areas occurred, and the criterion of overlapping route disposition generally was given greater weight than overlapping areas of milk supply. Some analysis also was done to determine whether milk pooled on adjacent markets reflects actual movements of milk between markets, or whether the variations in amounts pooled under a given order may indicate that some milk is pooled to take advantage of price differences rather than because it is needed for Class I use in the other market.

#### 3. Number of Handlers Within a Market

Formation of larger-size markets is a stabilizing factor. Shifts of milk and/or plants between markets becomes less of

a disruptive factor in larger markets. Also, the existence of Federal order markets with handlers too few in number to allow meaningful statistics to be published without disclosing proprietary information should be avoided.

#### 4. Natural Boundaries

Natural boundaries and barriers such as mountains and deserts often inhibit the movement of milk between areas, and generally reflect a lack of population (limiting the range of the consumption area) and lack of milk production. Therefore, they have an effect on the placement of marketing area boundaries. In addition, for the purposes of market consolidation, large unregulated areas and political boundaries also are considered a type of natural barrier.

#### 5. Cooperative Association Service Areas

While not one of the first criteria used to determine marketing areas, cooperative membership often may be an indication of market association. Therefore, data concerning cooperative membership can provide additional support for combining certain marketing areas.

#### 6. Features or Regulatory Provisions Common to Existing Orders

Markets that already have similar regulatory provisions that recognize similar marketing conditions may have a head start on the consolidation process. With calculation of the basic formula price replacement on the basis of components, however, this criterion becomes less important. The consolidation of markets having different payment plans will be more dependent on whether the basic formula component pricing plan is appropriate for a given consolidated market, or whether it would be more appropriate to adopt a pricing plan using hundredweight pricing derived from component prices.

#### 7. Milk Utilization in Common Dairy Products

Utilization of milk in similar manufactured products (cheese vs. butter-powder) was also considered to be an important criterion in determining how to consolidate the existing orders.

#### Comments on Consolidation Criteria

Most of the comments received relative to order consolidation criteria agreed that overlapping route disposition and milk procurement are the most important criteria to consider in the consolidation process. In

addition, Class I use percentages and regulation on the basis of handler location were noted as criteria to consider. To some extent, the consolidated marketing areas included in this proposed rule do combine markets with similar Class I utilization rates rather than markets that would result in Class I use percentages being more uniform between markets. This result occurs because adjoining markets, where most of the sales and procurement competition takes place between handlers regulated under different orders, tend to have similar utilization rates rather than because the criterion is one that should be used to determine appropriate consolidations. Also, Class I utilization rates are a function of how much milk is pooled on an order with a given amount of Class I use. Differences in rates, to the extent they result in differences in blend prices paid to producers, provide an incentive for milk to move from markets with lower Class I utilization percentages to markets with higher Class I use.

Regulation of processors on the basis of their location rather than their sales areas has largely been incorporated in the proposed orders by a provision that would pool a handler under the order for the area in which the handler is located unless more than 50 percent of the handler's Class I route dispositions are distributed in another order area. This provision should help to assure that the order under which a distributing plant is pooled will change from month to month, and that a plant operator is subject to the same provisions, such as producer pay prices, as are its primary competitors.

The proposed orders also include a provision that locks plants processing primarily ultra-high temperature (UHT) milk into regulation under the order for the area in which the plant is located. Such plants often have widely dispersed route sales into a number of order areas, with sporadic deliveries to different areas. Without some type of lock-in provision, a UHT plant may be pooled in several different orders in as many months. At the same time, the plant's milk supply generally is procured from a given group of producers located in the same area as the UHT plant. Having the plant pooled under a succession of different orders with widely varying blend prices creates a disorderly condition for the producers involved.

On the basis of the distributing plant pooling standards included for all eleven orders in this proposed rule, there are only two distributing plants that would be fully regulated under an order other than the ones in which they are located. These plants are the

Superbrand Dairy Products distributing plant in Greenville, South Carolina; and the Ryan Milk Company plant in Murray, Kentucky. The Superbrand plant likely will qualify for pooling under the proposed Southeast order, and the Ryan Milk Company plant, due to the nature of its extended shelf-life products, may qualify under any of several orders, depending on its dispositions in any particular month. Additional lock-in provisions are incorporated in both of these cases to assure that the plants are pooled in the area in which they compete for a producer milk supply and, in the case of the Ryan plant, that it will be pooled consistently under one order.

Several comments advocated that all of a state's territory should be included in one Federal order to assure that all producers in a state are paid on an equitable basis, or to make it easier to maintain state statistical data. One of the primary reasons for Federal milk orders is that milk marketing occurs readily across state boundaries, making state milk marketing regulation more difficult to enforce. It is important that Federal milk marketing areas continue to recognize the free interstate movement of milk to and from milk plants. There are cases where natural boundaries such as mountains or rivers may result in part of a state having a closer marketing relationship with an adjoining state than with other areas of the same state.

The initial Preliminary Report on Order Consolidation stated that the Farm Bill requirement to consolidate existing marketing areas does not specify expansion of regulation to previously non-Federally regulated areas where such expansion would have the effect of regulating handlers not currently regulated. However, on the basis of data, views and arguments filed by interested persons in response to the initial Preliminary Report requesting that currently non-Federally regulated areas be added to some consolidated marketing areas, the Revised Preliminary Report suggested that such areas be added to several of the consolidated areas. Handlers who would be affected by the expansion of Federal order areas into currently non-Federally regulated areas were notified of the possible change in their status, and encouraged to comment.

Handlers located in Pennsylvania Milk Marketing Board (PMMB) areas 2, 3, and 6 are regulated under the State of Pennsylvania if they do not have enough sales in any Federal order area to meet an order's pooling standards. (If such plants do meet Federal order pooling standards, the State of

Pennsylvania continues to enforce some of its regulations in addition to Federal order regulations). As State-regulated handlers, they must pay a Class I price for milk used in fluid products, often higher than the Federal order price would be. Inclusion of the Pennsylvania-regulated handlers in the consolidated marketing area, as in the case of including Maine or Virginia, would have little effect on handlers' costs of Class I milk (or might reduce them), while reducing producer returns.

Based on the comments received in response to the Revised Preliminary Report on Order Consolidation it has been determined that consolidation of the existing orders does not necessitate expansion of the consolidated orders into areas in which handlers are subject to minimum Class I pricing under State regulation, especially when the states' Class I prices exceed or equal those that would be established under Federal milk order regulation. Such regulation would have the effect of reducing returns to producers already included under State regulation without significantly affecting prices paid by handlers who compete with Federally-regulated handlers.

In order to avoid extending Federal regulation to handlers whose primary sales areas are outside current Federal order marketing areas, but who already are subject to similar minimum uniform pricing under State regulation, the in-area Class I disposition percentage portion of the pool distributing plant definition is proposed to be 25 percent for the Northeast order and 30 percent for the Mideast order, instead of the 10 or 15 percent used in the other nine consolidated order areas. The higher level of in-area sales required for pool status under these proposed orders will allow State-regulated plants to operate at their current level of sales within Federal order areas without being subject to full Federal order regulation.

As in both the initial and revised preliminary reports, "pockets" of unregulated areas within and between current order areas are included in the proposed consolidated marketing areas. The addition of currently-unregulated areas to Federal milk order areas can benefit regulated handlers by eliminating the necessity of reporting sales outside the Federal order marketing area for the purpose of determining pool qualification. Where such areas can be added to a consolidated order area without having the effect of causing the regulation of any currently-unregulated handler, they are proposed to be added.

### Cornell University Study

In addition to AMS' analysis of the receipt and distribution data in the development of this proposal, researchers at Cornell University also provided input on potential consolidated marketing areas. This input was part of Cornell's partnership agreement with AMS to provide alternative analyses on Federal order reform issues. These researchers used an econometric model (the Cornell U.S. Dairy Sector Simulator, or USDSS), to determine 10-14 optimal marketing areas. Cornell's first options for 10-14 marketing areas were presented at an October 1996 invitational workshop for dairy economists and policy analysts held in Atlanta, Georgia. Based on USDSS model results, these options would result in minimum cost flows of milk using the known concentrations of milk production and population, without considering the location of milk plants. The marketing area maps that were circulated using these first results were those referenced by interested persons who cited the Cornell results in their comments on the initial Preliminary Report on Order Consolidation.

A second set of options was presented by Cornell researchers in spring 1997. These options were generated with a further-developed USDSS model. In updating the model, the researchers enhanced the inputs to its model as a means of better reflecting the actual structure of the national market for fluid milk products. These model updates allowed for determination of the minimum cost flows of: milk, intermediate and final products from producers to plants; from plants to plants; and from plants to consumers on the basis of the locations of milk supplies, dairy product processing plants, and consumers. The enhanced model is intended to provide for geographic market definition on the

basis of a resulting set of optimal, efficient simulated flows of milk and dairy products between locations.

Although the USDSS model considers important factors such as milk supply, processing, and demand locations and transportation constraints in determining the optimal consolidated marketing areas, it does not include several other important circumstances that influence dairy industry and Federal order participants or the movement of milk which must be considered in this reform process. The USDSS model does not recognize that large areas, such as California, Virginia, Maine, Montana, large portions of Pennsylvania, and Wyoming, currently are not included in Federal milk order regulation, and does not recognize the Farm Bill requirement that, if included as a Federal order, the State of California be brought in as one order confined to the borders of California. Although the USDSS model incorporates highway mileage between milk production areas and milk plants, and between milk plants and consumers, it does not recognize features such as mountain ranges that affect hauling costs and may inhibit milk from moving. By attempting to maximize efficiencies in milk marketing, the model also does not recognize the existence of competing handlers operating plants in the same city or having the extent of handlers' route dispositions influenced by the existence of plants operated by the same handler in other locations. In addition, the model does not recognize that movements of producer milk often are determined by supply contracts between cooperatives and handlers or by the location of a handler's nonmember supply.

AMS is unaware of any other analyses performed to determine or suggest consolidated marketing areas.

As noted before, AMS' analysis focused primarily on distributing plant

receipts and distribution information for October 1995, with more current information used as needed for further analysis. The data gathered by the Dairy Division from Federal Milk Market Administrators reflects actual movements of milk, both from production areas to processing plants, and from processing plants to consumption areas. This proposal considers this data, the seven criteria described fully above, and the factors not recognized in the USDSS model. Use of the USDSS may be an excellent way of determining where processing plants should be located to maximize the efficiencies of milk assembly and distribution, but is a less accurate means of determining where existing handlers actually compete for milk supplies and sales. The consolidated marketing area options presented by Cornell are not adopted because the USDSS model does not adequately reflect issues or factors that strongly affect which current marketing areas are most closely related. For this reason, this proposed rule is based on data reflecting actual distribution and procurement by fluid milk processing plants.

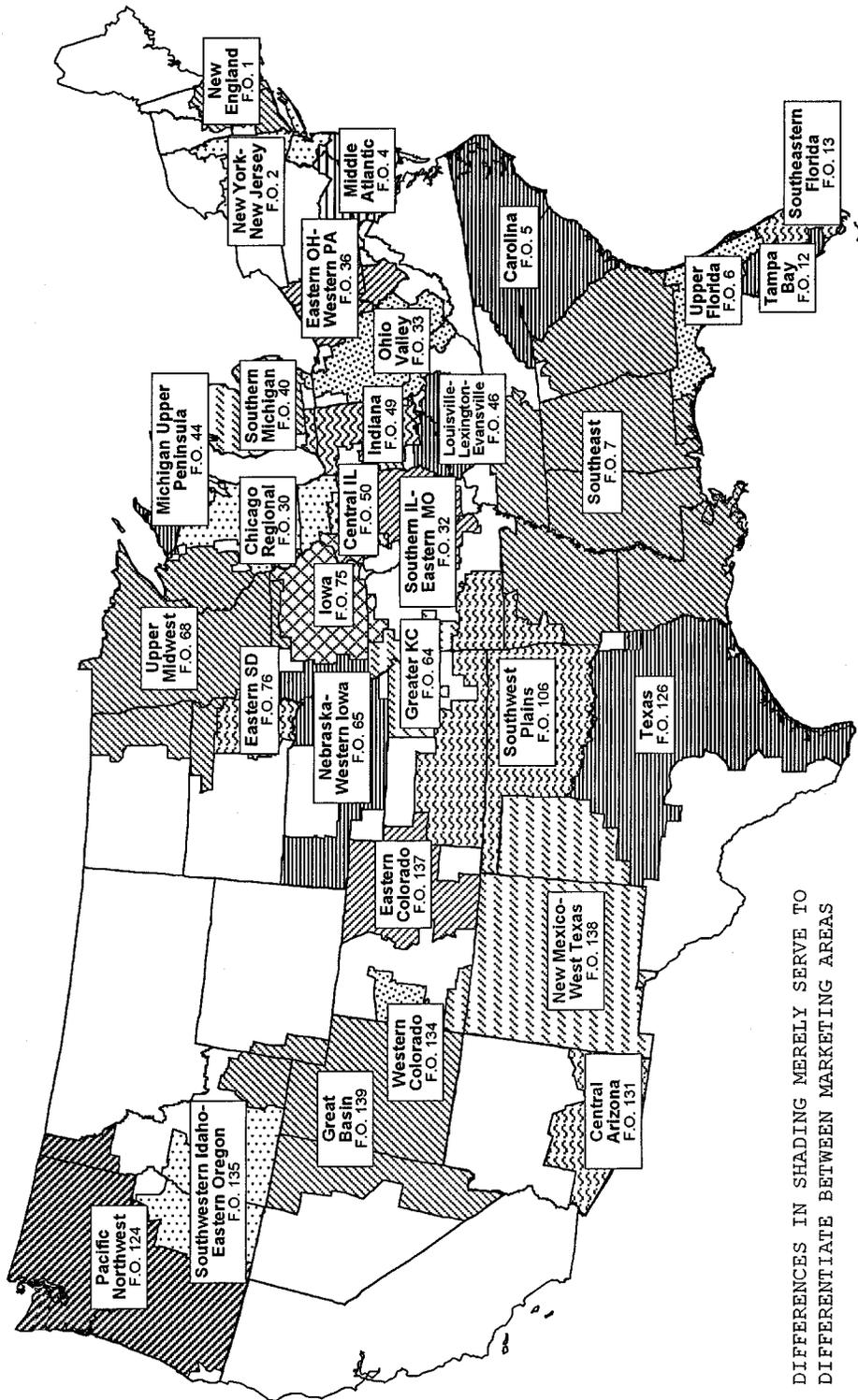
### Proposed Marketing Areas

Following are maps of the current marketing areas and the 11 proposed marketing areas, followed by brief descriptions of the proposed areas (with those modified from the Revised Preliminary Report, and the modifications, marked by \*) and the major reasons for consolidation. A more detailed description of each proposed consolidated order follows this summary.

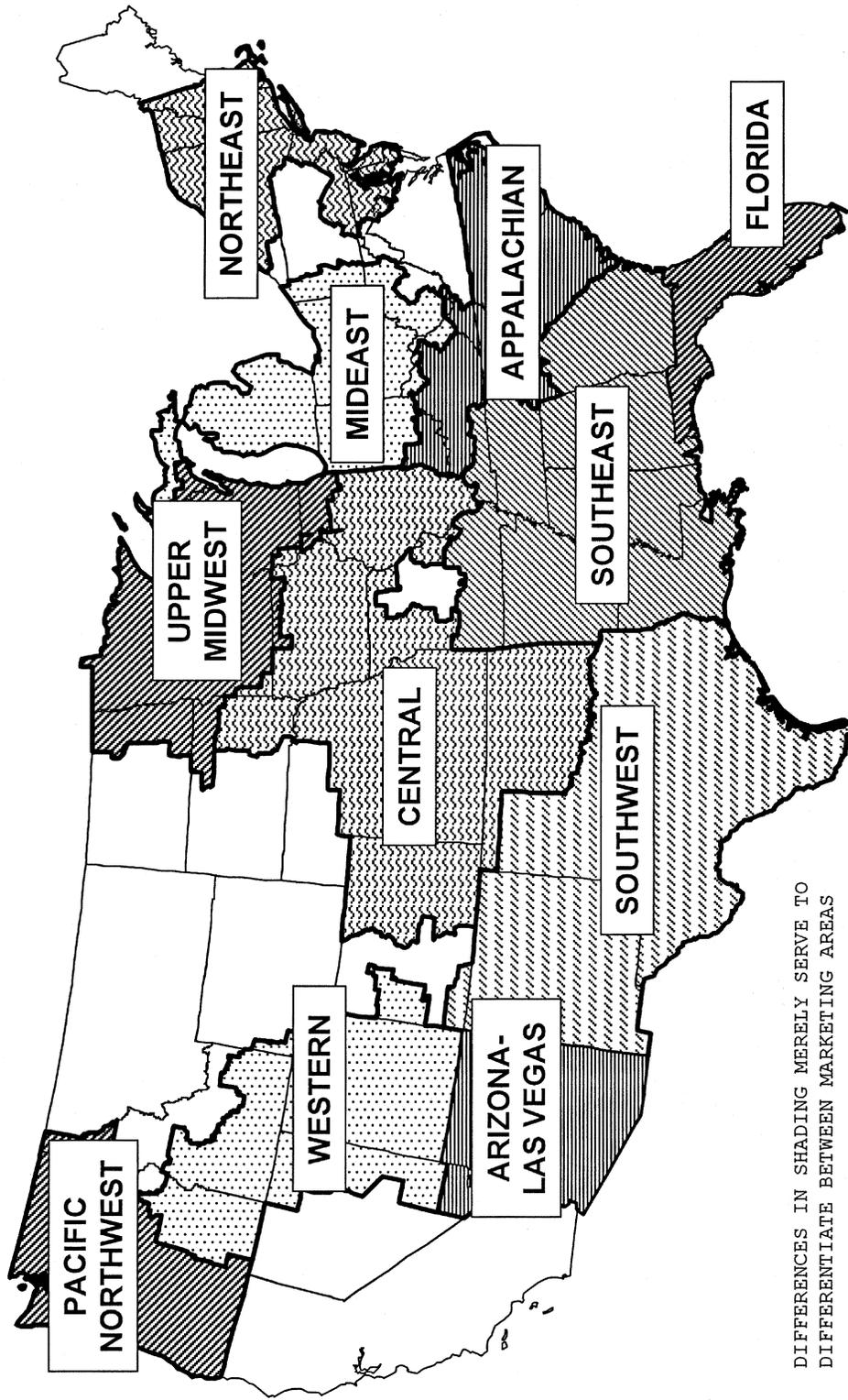
At the end of the Order Consolidation portion of the proposed rule is appended a list of distributing plants associated with each proposed marketing area, with each plant's expected regulatory status.

BILLING CODE 3410-02-P

Marketing Areas Under Federal Milk Orders as of October 1, 1997



Proposed Federal Milk Marketing Order Areas



DIFFERENCES IN SHADING MERELY SERVE TO DIFFERENTIATE BETWEEN MARKETING AREAS

### Proposed Eleven Marketing Areas

\* 1. *Northeast*—current marketing areas of the New England, New York-New Jersey and Middle Atlantic Federal milk orders, with the addition of: the contiguous unregulated areas of New Hampshire, northern New York and Vermont; the non-Federally regulated portions of Massachusetts; and the Western New York State order area. \* The areas previously suggested to be included in the expanded Northeast order area (the southern tier of 3 western New York counties and Pennsylvania Milk Marketing Board Areas 2 and 3) have not been included in the proposed Northeast marketing area. The handlers who would be added to those currently fully regulated under the three separate orders either have a sufficient percentage of their route disposition within the consolidated marketing area to meet the proposed pooling requirements or are those located in the area proposed to be added.

Reasons for consolidation include the existence of overlapping sales and procurement areas between New England and New York-New Jersey and between New York-New Jersey and Middle Atlantic. An important measure of association is evidenced by industry efforts to study and pursue consolidation of the three Federal orders prior to the 1996 Farm Bill.

\* 2. *Appalachian*—current marketing areas of the Carolina and Louisville-Lexington-Evansville (minus Logan County, Kentucky) Federal milk orders plus the recently-terminated Tennessee Valley area, with the addition of \* 21 currently-unregulated counties in Indiana and Kentucky. Five Kentucky counties that were part of the former Paducah order area and previously were suggested to be added to the Appalachian order area have been proposed for addition to the Southeast order instead.

Overlapping sales and procurement areas between these marketing areas are major factors for proposing this consolidation.

3. *Florida*—current marketing areas of the Upper Florida, Tampa Bay, and Southeastern Florida Federal milk orders.

Natural boundary limitations and overlapping sales and procurement areas among the three orders are major reasons for consolidation, as well as a measure of association evidenced by cooperative association proposals to consolidate these three marketing areas. Further, the cooperative associations in this area have worked together for a number of years to accommodate

needed movements of milk between the three Florida Federal orders.

\* 4. *Southeast*—current marketing area of the Southeast Federal milk order, plus 1 county from the Louisville-Lexington-Evansville Federal milk order marketing area; \* plus 11 northwest Arkansas counties and 22 entire and 1 partial Missouri county that currently are part of the Southwest Plains marketing area; \* plus 6 Missouri counties that currently are part of the Southern Illinois-Eastern Missouri marketing area; \* plus 16 currently unregulated southeast Missouri counties (including 4 that were part of the former Paducah marketing area); plus 20 currently-unregulated Kentucky counties (\* including 5 from the former Paducah marketing area that previously had been suggested for inclusion with the Appalachian area).

Major reasons for this consolidation include sales and procurement area overlaps between the Southeast order and these counties. The proposed addition of the Kentucky portion of the former Paducah, Kentucky, order area to the Southeast is in the nature of a fine-tuning adjustment in order boundaries. The addition of the Arkansas and Missouri counties recognizes a number of industry comments.

\* 5. *Mideast*—current marketing areas of the Ohio Valley, Eastern Ohio-Western Pennsylvania, Southern Michigan and Indiana Federal milk orders, plus Zone 2 of the Michigan Upper Peninsula Federal milk order, and currently-unregulated counties in Michigan, Indiana and Ohio. \* The current Pennsylvania Milk Marketing Board Area 6 and the two most western of the southern tier of counties in New York are not included in the proposed Mideast marketing area.

Major criteria for this proposed consolidation include the overlap of fluid sales in the Ohio Valley marketing area by handlers from the other areas proposed to be consolidated. With the consolidation, most route disposition by handlers located within the suggested Mideast order would be within the marketing area. Also, nearly all milk produced within the area would be pooled under the consolidated order. The portion of the Michigan Upper Peninsula marketing area proposed to be included in the Mideast consolidated area has sales and milk procurement areas in common with the Southern Michigan area and has minimal association with the western end of the current Michigan Upper Peninsula marketing area.

\* 6. *Upper Midwest*—current marketing areas of the Chicago Regional, Upper Midwest, Zones I and I(a) of the

Michigan Upper Peninsula Federal milk orders, and unregulated portions of Wisconsin. The \* Iowa, \* Eastern South Dakota and \* Nebraska-Western Iowa Federal order areas suggested to be added to this consolidated area in the revised report are proposed instead to be included in the Central consolidated area.

Major consolidation criteria include an overlapping procurement area between the Chicago Regional and Upper Midwest orders and overlapping procurement and route disposition area between the western end of the Michigan Upper Peninsula order and the Chicago Regional order. A number of the same cooperative associations market member milk throughout the proposed area.

The overlapping of procurement between the Chicago Regional and Upper Midwest order areas and the Iowa, Eastern South Dakota and Nebraska-Western Iowa order areas is, it was pointed out in comments received in response to the Revised Preliminary Report, due largely to milk pooled on the more southern orders when advantageous because of price differences. As a result, the volume of milk pooled on the Iowa, Eastern South Dakota and Nebraska-Western Iowa orders from Minnesota and Wisconsin fluctuates greatly, without any discernible relationship to amounts of milk needed from those areas at plants in the more southern areas.

The other consolidation criteria mentioned in the Revised Preliminary Report as reasons for consolidating the Iowa, Eastern South Dakota and Nebraska-Western Iowa order areas with the Chicago Regional and Upper Midwest areas also are applicable to the combination of these areas with the consolidated Central area.

\* 7. *Central*—current marketing areas of the Southern Illinois-Eastern Missouri, Central Illinois, Greater Kansas City, Southwest Plains, Eastern Colorado, \* Nebraska-Western Iowa, \* Eastern South Dakota and \* Iowa Federal milk orders, minus \* 11 northwest Arkansas counties and 22 entire and 1 partial Missouri county that are part of the current Southwest Plains marketing area, minus \* 6 Missouri counties that are part of the current Southern Illinois-Eastern Missouri marketing area, plus \* 54 currently-unregulated counties in Kansas, Missouri, Illinois, Iowa, Nebraska and Colorado, \* plus 14 counties in central Missouri that are not considered to be part of the distribution area of an unregulated handler in central Missouri. This configuration would leave 25 unregulated counties in central Missouri

that are intended to delineate the distribution area of Central Dairy at Jefferson City, Missouri.

Major criteria on which this proposed consolidation is based include overlapping route disposition and procurement between the current orders. The proposed consolidation would result in a concentration of both the sales and supplies of milk within the consolidated marketing area. The proposed consolidation would combine several relatively small orders and provide for the release of market data without revealing proprietary information. In addition, many of the producers in these areas share membership in several common cooperatives.

8. *Southwest*—current marketing areas of Texas and New Mexico-West Texas Federal milk orders, with the addition of two currently-unregulated northeast Texas counties and 47 currently-unregulated counties in southwest Texas.

Major criteria supporting this proposed consolidation include sales and procurement area overlaps and common cooperative association membership between the Texas and New Mexico-West Texas marketing areas, and similar marketing concerns with respect to trade with Mexico for

both orders. Addition of the currently-unregulated Texas counties will result in the regulation of no additional handlers, and will reduce handlers' recordkeeping and reporting burden and the market administrator's administrative costs.

9. *Arizona-Las Vegas*—current marketing area of Central Arizona, plus the Clark County, Nevada, portion of the current Great Basin marketing area, plus eight currently-unregulated Arizona counties.

The major criterion on which the proposed consolidation is based is sales overlap between the sole Las Vegas, Nevada, handler and handlers regulated under the Central Arizona order in both Clark County, Nevada, and unregulated portions of northern Arizona. The Grand Canyon and sparsely populated areas in the northwest part of Arizona, and the sparsely populated desert region of eastern Arizona constitute natural barriers between this and adjacent marketing areas. In addition, significant volumes of bulk and packaged milk are exchanged between the Arizona-Las Vegas area and Southern California.

10. *Western*—current marketing areas of the Western Colorado, Southwestern Idaho-Eastern Oregon, and Great Basin Federal milk orders, minus Clark County, Nevada. The major criteria on

which the proposed consolidation is based include overlapping sales between Southwestern Idaho-Eastern Oregon and Great Basin, as well as a significant overlap in procurement for the two orders in five Idaho counties. The two orders also have similar multiple component pricing plans. The Western Colorado order is included because it is a small market where data cannot be released without revealing confidential information unless combined with data pertaining to another marketing area, and has at least as great a relationship with the adjacent Great Basin market as with any other.

Collection of detailed data for individual handlers indicates that the strength of earlier relationships between the former Great Basin and Lake Mead orders that justified their 1988 merger have dwindled significantly, with the Las Vegas area now more closely related to southern California and competing most heavily with Central Arizona handlers.

11. *Pacific Northwest*—current marketing area of the Pacific Northwest Federal milk order plus 1 currently-unregulated county in Oregon. The degree of association with other marketing areas is insufficient to warrant consolidation.

TABLE 1.—MARKET INFORMATION: POPULATION, UTILIZATION, PRODUCER MILK AND WEIGHTED AVERAGE UTILIZATION VALUE (WAUV) IN PROPOSED MARKETING AREAS

Market	Population <sup>1</sup> (millions)	Class I utilization <sup>2</sup> (percent)	Producer milk <sup>2</sup> (1000 lbs.)	WAUV <sup>2,3</sup> (per cwt)
Northeast .....	51.3	47.7	2,031,976	\$13.47
Appalachian .....	17.1	82.2	440,965	13.97
Florida .....	13.8	88.3	204,541	15.05
Southeast .....	26.7	85.2	486,301	14.24
Mideast .....	31.0	55.8	1,050,656	12.92
Upper Midwest .....	18.5	34.5	1,034,318	12.60
Central .....	21.0	48.8	859,405	12.95
Southwest .....	20.9	48.1	680,232	13.39
Arizona-Las Vegas .....	5.5	48.9	181,075	13.26
Western .....	3.3	29.6	293,714	12.78
Pacific Northwest .....	8.8	35.6	493,207	12.44
Total .....	216.0	N/A	7,756,390	N/A

<sup>1</sup> Based on July 1, 1996 estimates.

<sup>2</sup> Based on October 1995 information, for plants which would be fully regulated under assumptions used in this report.

<sup>3</sup> Not a blend price—shown solely for the purpose of showing impact of consolidation on utilization.

TABLE 2.—MARKET INFORMATION: NUMBER OF PLANTS IN PROPOSED MARKETING AREAS

Market	Distributing plants <sup>1</sup>			Manufacturing and supply plants <sup>3</sup>
	Fully regulated (FR)	Exempt <sup>2</sup>	FR small businesses	
Northeast .....	79	17	42	106
Appalachian .....	29	1	13	13
Florida .....	15	2	3	4
Southeast .....	36	1	20	37
Mideast .....	56	2	36	59
Upper Midwest .....	29	1	15	301

TABLE 2.—MARKET INFORMATION: NUMBER OF PLANTS IN PROPOSED MARKETING AREAS—Continued

Market	Distributing plants <sup>1</sup>			Manufacturing and supply plants <sup>3</sup>
	Fully regulated (FR)	Exempt <sup>2</sup>	FR small businesses	
Central .....	34	2	8	83
Southwest .....	23	3	7	17
Arizona-Las Vegas .....	5	1	2	3
Western .....	11	3	6	19
Pacific Northwest .....	20	3	12	27
Total .....	337	36	164	669

<sup>1</sup> Based on October 1995 information. Excludes: (1) out-of-business plants through May 1997; and (2) new plants since October 1995.

<sup>2</sup> Exempt based on size (less than 150,000 lbs. route distribution per month).

<sup>3</sup> Based on May 1997 information.

### Descriptions of Proposed Consolidated Marketing Areas

Each of the proposed consolidated order areas is described in the text following this introduction. The criteria which were used to determine which areas should be consolidated are explained in detail. For each proposed area, the following information is included:

**Geography.** The political units (states, counties, and portions of counties) included in each area, the topography, and the climatic conditions are described for the purpose of delineating the territory to be incorporated in each proposed marketing area and describing its characteristics pertaining to milk production and consumption. This information was derived principally from Microsoft® Encarta® 96 Encyclopedia, and augmented by several U.S. atlases.

**Population.** The total population of each area and its distribution within the area is included for the purpose of identifying where milk is consumed. July 1, 1996, population estimates were obtained from "CO-96-8 Estimates of the Population of Counties and Demographic Population Change," Population Estimates Division of the U.S. Bureau of the Census.

Metropolitan Statistical Area (MSA) information is provided by the United States Office of Management and Budget (OMB), which defines metropolitan areas according to published standards that are applied to Census Bureau data. To be described as an MSA, an area (one or more counties) must include at least one city with 50,000 or more inhabitants, or a Census Bureau-defined urbanized area (of at least 50,000 inhabitants) and a total metropolitan population of at least 100,000 (75,000 in New England). Areas with more than 1 million population may be described as "consolidated metropolitan statistical areas" (CMSAs) made up of component parts designated as primary

metropolitan statistical areas (PMSAs). For purposes of the marketing area descriptions in this proposed rule, the term "MSA" also includes CMSAs and PMSAs.

**Per capita consumption.** Available data pertaining to per capita consumption is discussed to help describe how much milk is needed to supply the fluid needs of the population of each proposed marketing area. Per capita consumption numbers were estimated by state using data from a report on "Per Capita Sales of Fluid Milk Products in Federal Order Markets," published in the December 1992 issue of Federal Milk Order Market Statistics, #391, issued May 1993.

**Production.** A description of the amount and sources of milk production for the market is included for the purpose of identifying the supply area for each proposed marketing area. Production data by state and county for each Federal milk order was compiled from information collected by the offices administering the current Federal milk orders (market administrators' offices).

**Distributing plants-route disposition.** For each marketing area the number and types of distributing plants are included, with the locations of plants by population centers, to identify where milk must be delivered. This information was collected by market administrators' offices.

**Utilization.** The utilization percentages of the current individual orders and the effect of consolidation on the proposed consolidated orders are described for each proposed marketing area, with an estimate of the effect of consolidation on each current individual order's blend price. The current utilization data is published each month for each Federal milk order market. Pool data was used to calculate the effects of consolidation on utilization.

**Other plants.** The presence of manufacturing and supply plants in and near the proposed order areas, and the products processed at these plants, are described for each proposed consolidated area. This information was collected by market administrators' offices.

**Cooperative Associations.** The number of cooperative associations pooling member milk under each of the current individual orders included in each consolidated area, and the number that pool milk in more than one of the areas. This information was obtained from market administrators' offices.

**Criteria for Consolidation.** The extent to which the criteria used in identifying markets to be consolidated are supported by the marketing conditions present in each of the proposed consolidated areas is discussed.

**Discussion of comments and alternatives.** Comments filed in response to the two preliminary reports on consolidation and alternatives to the proposed consolidation are summarized and discussed for each proposed consolidated area.

### Northeast

The proposed consolidated Northeast marketing area is comprised of the current New England, New York-New Jersey, and Middle Atlantic Federal milk order marketing areas (Orders 1, 2, and 4), with currently-unregulated areas in western and northern New York and northern Vermont and New Hampshire added. The entire areas of the States of Connecticut (8 counties), Delaware (3 counties), Massachusetts (14 counties), New Hampshire (10 counties), New Jersey (21 counties), Rhode Island (5 counties), and Vermont (14 counties) would be contained within the proposed Northeast order area. In addition, the District of Columbia, 21 counties and the City of Baltimore in Maryland, 54 complete and 2 partial counties and New York City in New

York, the 15 Pennsylvania counties currently included in the Middle Atlantic marketing area, and 4 counties and 5 cities in Virginia would be included in the consolidated order. There are 169 complete and 2 partial counties and 8 cities, including the District of Columbia, in the proposed Northeast marketing area.

#### Geography

The proposed Northeast marketing area extends from the Canadian border on the north, south to northern Virginia, eastern Maryland and Delaware, with its eastern edge along the western border of Maine at the northern end of the marketing area, and along the Atlantic Ocean for the remainder. The total northeast-southwest extent of the marketing area is approximately 600 miles. The marketing area extends westward to Lake Ontario and Lake Erie in New York State (about 450 miles east to west), goes only as far west as the northern part of New Jersey (about 60 miles), and expands westward again across the eastern half of southern Pennsylvania, taking in a small part of northeast Virginia, eastern Maryland, and Delaware (about 230 miles east to west). There would be a large State-regulated area in Pennsylvania just to the west of the Northeast marketing area; and most of the State of Virginia to the south of the marketing area also is regulated under a State order. The proposed Northeast marketing area is contiguous to no other proposed consolidated marketing areas, but parts of it, in western New York State and south central Pennsylvania, are very close to the proposed Mideast area.

The northern and northwestern parts of the Northeast area are large areas of coniferous forests that are somewhat mountainous. To the south and southeast of the forested areas are areas where dairy farming predominates as the primary type of agriculture. In fact, for 4 of the 10 states that are contained within the proposed Northeast marketing area (New Hampshire, New York, Pennsylvania and Vermont) dairy products were the number 1 agricultural commodity in terms of cash receipts during 1996. Principally along the Atlantic coastline is a flatter area where other agricultural activities, including greenhouse and nursery, fruit, truck and mixed farming, take place. A near-continuous strip along the east coast of the area, from northeast Massachusetts southwest to the Baltimore area, is a major industrial area and is heavily populated.

#### Population

According to July 1, 1996, population estimates, the total population in the proposed consolidated Northeast marketing area is 51.3 million. The area is very densely populated, especially along a coastal strip extending from Boston, Massachusetts, in the northeast to Washington, D.C., in the southwest. In this proposed marketing area of approximately 170 counties, 103 are included within Metropolitan Statistical Areas (MSAs). The 22 Metropolitan Statistical Areas in the proposed Northeast marketing area account for 91.7 percent of the total market area population.

Over half of the marketing area population is located in 6 interconnected MSAs in 48 counties, extending from central New Jersey to southern New Hampshire. The six MSAs are: Springfield, Massachusetts; Boston-Worcester-Lawrence, Massachusetts/New Hampshire/Maine/Connecticut; Providence-Fall River-Warwick, Rhode Island/Massachusetts; New London-Norwich, Connecticut/Rhode Island; Hartford, Connecticut; and New York-N. New Jersey-Long Island, New York/New Jersey/Connecticut/Pennsylvania. The population in this northeastern portion of the marketing area is concentrated most heavily at its northern and southern ends—the New York City area has a population of approximately 20 million, and the Boston area's population is approximately 5.5 million. Two of the other MSAs, Hartford and Providence, each have over 1 million population. Although each of these six MSAs is described as a separate area in the population data, many of the counties involved are divided between separate MSAs.

Just southwest of the New York City MSA is the Philadelphia-Wilmington-Atlantic City, Pennsylvania/New Jersey/Delaware/Maryland MSA, with a population of 6 million. Some counties of these two MSAs are adjacent. Southwest of the Philadelphia MSA and separated from it by only one county is the Washington, DC/Baltimore, Maryland/northern Virginia MSA, with a population in the proposed marketing area of 5.7 million.

Of the 14 other MSAs in the proposed marketing area, 8 are located in New York State, with an average population of nearly 600,000 each. Two are located in Pennsylvania, with populations of .6 and .45 million. One MSA in Vermont, 1 in Delaware, and 2 in Massachusetts have average populations of 160,000.

#### Fluid Per Capita Consumption

Fluid per capita consumption estimates vary within the Northeast from 16.7 pounds per month in the more southern parts of the region to 20 pounds per month in New England. These rates would result in a weighted average of 18 pounds per month, and an estimated total fluid milk consumption rate of 920 million pounds per month for the Northeast marketing area. Approximately 730 million pounds of this fluid milk consumption would be required along the heavily-populated coastal area extending from northeast Massachusetts southwest through Washington, D.C. and northern Virginia. Northeast handlers distributed 883.7 million pounds within the proposed marketing area during October 1995. Sales within the proposed marketing area by handlers that would be regulated by other orders totaled 9.3 million pounds, sales by partially regulated handlers within the area were 10.8 million, and an additional .8 million pounds were distributed by handlers who would be partially regulated under other orders. Sales in the marketing area by exempt and government plants, and by producer-handlers totaled 6.2 million pounds.

#### Milk Production

In December 1996, over 19,000 producers from 13 states pooled 1.9 billion pounds of milk on the three orders comprising the proposed Northeast order. With the addition of the Western New York State milk order and several currently-unregulated handlers, it is probable that the Northeast pool regularly will exceed 2 billion pounds of milk per month.

Eleven of the 13 states supplying milk to the three Federal order pools are at least partly in the marketing area, and 83 percent of the producer milk pooled under the three orders in December 1996 came from just 3 states—New York (41.5 percent), Pennsylvania (31.7 percent), and Vermont (10 percent). Over 10 million pounds of milk was produced in each of fifty-eight counties: 1 county in northeast Connecticut, 3 in the most northwestern of the Maryland portion of the marketing area, 31 spread over most of New York, 1 on the western edge of northern Virginia, and 22 in southeast to south central Pennsylvania and in the eastern part of the northern tier of Pennsylvania counties, with an additional Pennsylvania county, Lancaster, accounting for over 150 million pounds of milk. Eighty percent of the markets' total producer milk was produced within the proposed marketing area. In

addition, of the 81.1 million pounds pooled under the Western New York State milk order, over 90 percent was produced within the proposed marketing area.

Less than 40 percent of the milk production for the consolidated market was produced within 100 miles of the heavily populated coastal corridor. Although the Northeast area contains two out of the top five milk-producing states in the U.S. (New York and Pennsylvania), the population of the proposed marketing area is 20 million more than the next most-populated proposed consolidated area (the Mideast area, with 31 million people). The Northeast, therefore, is a very significant milk production area with a very high demand for fluid milk and dairy products.

#### Distributing Plants—Route Disposition

Using distributing plant lists included in both the Preliminary and Revised Preliminary Reports, with the pooling standards used in the Revised Preliminary Report adjusted to 25 percent of route dispositions as in-area sales (as discussed previously in Comments on Consolidation), and updated for known plant closures through May 1997, 156 distributing plants would be expected to be associated with the Northeast marketing area. The plants associated would include 79 fully regulated distributing plants (64 currently fully regulated, 10 currently partially regulated, and 5 currently unregulated), 15 partially regulated (3 currently fully regulated, 11 currently partially regulated and 1 currently unregulated), 17 exempt plants having less than 150,000 pounds of total route disposition per month (2 currently fully regulated, 4 currently partially regulated, 2 currently exempt based on size, and 9 currently unregulated), 43 producer-handlers (42 currently producer-handlers and 1 currently unregulated), and 2 exempt plants based on institutional status (1 currently unregulated and 1 currently exempt based on institutional status).

Since October 1995, 10 distributing plants (3 in New York, 3 in Massachusetts, 3 in Pennsylvania, and 1 in Connecticut), have gone out of business.

Over half (88) of the Northeast distributing plants which were identified as being in business in October 1995 were located in the 8 Northeast MSAs that have over a million people each. This number includes 49 (or two-thirds) of the pool distributing plants. Under the proposed consolidation, it is anticipated that there would be 12 pool distributing plants in

the Boston-Worcester-Lawrence area, 10 in the Philadelphia-Wilmington-Atlantic City area, and 11 in the New York-Northern New Jersey-Long Island area. The Hartford, Connecticut, area would have 3 pool distributing plants, Providence-Fall River-Warwick would have 3, and the Washington-Baltimore area would have 6 pool distributing plants. Three pool distributing plants would be located in the Buffalo-Niagara Falls area, and 1 in the Rochester, New York, area.

Of the remaining 70 distributing plants, 14 pool distributing plants were located in other MSAs as follows: 8 in New York; 5 in Pennsylvania; and 1 in Massachusetts. Thirty-nine of the remaining distributing plants, including 11 pool distributing plants, were not located in MSAs.

For the proposed Northeast order, the in-area route disposition standard has been adjusted to 25 percent of total route dispositions from the 15-percent standard that was common to all of the suggested consolidated areas in the Revised Preliminary Report. This adjustment has been made to assure that State-regulated plants in Virginia and Pennsylvania that have sales in the proposed marketing area will not be pooled under Federal order regulation.

#### Utilization

According to October 1995 pool statistics for handlers who would be fully regulated under this Northeast order, the Class I utilization percentages for the New England, New York-New Jersey, and Middle Atlantic markets were 51, 44, and 53 percent, respectively. Based on calculated weighted average use values for (1) the current order with current use of milk, and (2) the current order with projected use of milk in the consolidated Northeast order, the potential impact of this proposed rule on producers who supply the current market areas is estimated to be: New England, a 3-cent per cwt decrease (from \$13.52 to \$13.49); New York-New Jersey, a 3-cent per cwt increase (from \$13.45 to \$13.48); and Middle Atlantic, a 4-cent per cwt decrease (from \$13.44 to \$13.40). The weighted average use value for the consolidated Northeast order market is estimated to be \$13.47 per cwt. For December 1996, combined Class I utilization for Orders 1, 2 and 4 was 44.4 percent based on 852.7 million pounds of producer milk used in Class I out of 1.919 billion total producer milk pounds.

The Northeast area is one of two proposed consolidated marketing areas that would have a significantly higher-than-average percentage of its milk used

in Class II. Currently, all three of the orders have Class II utilization between 15 and 20 percent. When the markets are combined the average for the consolidated market will be approximately 17 percent.

#### Other Plants

Located within the proposed consolidated Northeast marketing area during May 1997 were 106 supply or manufacturing plants: 13 in Vermont (4 in the Burlington area), 1 in New Hampshire and 10 in Massachusetts (all in the Boston-Worcester-Lawrence area), 1 in Rhode Island (in the Providence-Fall River-Warwick area), 7 in Connecticut (3 in the Hartford area and 4 in the New York-Northern New Jersey-Long Island area), 12 in New Jersey (all in the New York-Northern New Jersey-Long Island area), 2 in Delaware (one in the Philadelphia-Wilmington-Atlantic City area), 7 in Maryland (four in the Washington-Baltimore area), 13 in Pennsylvania (5 in the Philadelphia-Wilmington-Atlantic City area), and 40 in New York (9 in the New York-Northern New Jersey-Long Island area, 6 in the Buffalo-Niagara Falls area and 2 in the Rochester area).

Seventeen of the 106 plants are pool plants. Of these pool plants, 9 are manufacturing plants—1 manufactures primarily Class II products, 5 manufacture primarily powder, 2 manufacture primarily cheese and 1 manufactures primarily other products. There are 8 pool supply plants—1 has no primary product, but ships only to distributing plants; 5 are supply plants that manufacture primarily Class II products, and 2 supply plants manufacture primarily cheese. Of the remaining 89 nonpool plants in the Northeast marketing area, 82 are manufacturing plants—41 manufacture primarily Class II products, 1 manufactures primarily butter, 1 manufactures primarily powder, 37 manufacture primarily cheese and 2 manufacture primarily other products. Seven of the remaining nonpool plants are supply plants—2 are supply plants that manufacture primarily Class II products and 5 are supply plants that manufacture primarily cheese.

A pool supply plant that manufactures primarily cheese and a nonpool cheese manufacturing plant are located in the currently-unregulated portions of Steuben County that are proposed to be added to the consolidated Northeast marketing area.

There are also four supply or manufacturing plants in the unregulated area of New York—one in the unregulated county of Chautauqua, one in the unregulated portion of

Cattaraugus County, and two in the unregulated portion of Allegany County. One is a pool supply plant manufacturing primarily Class II products, and the remaining three are nonpool manufacturing plants—two manufacture primarily cheese and one manufactures primarily Class II products.

#### Cooperative Associations

During December 1995, 43 cooperative associations pooled their members' milk on the three Northeast orders. Three of the cooperatives pooled milk on all three orders, 2 pooled milk on both the New England and New York-New Jersey orders, and 2 others pooled milk on both the New York-New Jersey and Middle Atlantic orders. Sixty-eight percent of the milk pooled in the Northeast is cooperative association milk, with 79.3 percent of Federal Order 1 milk, 50.5 percent of Federal Order 2 milk, and 91.8 percent of Federal Order 4 milk pooled by cooperatives.

The 5 cooperatives that market milk only under Order 1 account for 25.5 percent of the milk marketed under that order by cooperative associations, and 20.2 percent of total milk marketed under Order 1. In Order 2, only 28 percent of cooperative association milk is marketed by the 27 co-ops that market milk only under Order 2. Milk marketed by these 27 cooperatives represent 14.1 percent of the total milk pooled for December 1995. Four cooperative associations marketed 45.4 percent of the milk marketed by cooperatives under Order 4. This amount of milk represented 41.7 percent of total milk pooled under Order 4 in December 1995.

#### Criteria for Consolidation

The current New England, New York-New Jersey, and Middle Atlantic Federal milk order marketing areas (Orders 1, 2, and 4) should be consolidated because of the interrelationship between Orders 1 and 2 and between Orders 2 and 4 regarding route disposition and milk supply. Ninety-four percent of fluid milk disposition by handlers who would be fully regulated under the consolidated order is distributed within the proposed marketing area. Fully regulated handlers account for 97 percent of the fluid milk products distributed within the proposed marketing area. The utilization of the three markets is similar, and several cooperative associations market their members' milk in all three markets. The three markets are surrounded by unregulated areas to the west and south, the Atlantic ocean to the east, and Canada to the north. The

adjoining Maine State milk order also serves as somewhat of a barrier to milk marketing in the northeast by limiting the association of non-Maine milk with the Maine pool.

The merger of these markets has been previously proposed by interested parties. A committee comprised chiefly of Northeast region cooperatives was formed over two years ago to study a merger of the three Federal orders. In support of a Northeast consolidation, the committee and other interested parties, including handlers and regulatory agencies, have noted: overlapping sales and procurement areas; a trend toward consolidation of cooperative processors and handlers in the region (leaving the remaining handlers with larger distributing areas and volumes); and regulation of plants by an order in which they are not located. The proponents of consolidation have indicated that consolidation would tend to solve some of the presently existing inequities and would lead to greater efficiency for handlers and order administration.

#### Discussion of Comments and Alternatives

A large number of comments, primarily from producers and producer groups, supported expansion of the Northeast consolidated marketing area into non-federally regulated areas. Comments supported the suggestions in the Revised Preliminary Report on Order Consolidation that would have extended federal order marketing areas to non-federally regulated areas which are part of the same milksheds and fluid milk markets, arguing that the surrounding federal order pool(s) are carrying the necessary surplus for the Class I sales distributed by non-regulated handlers.

Comments favoring expansion into the non-federally regulated Northeast tended to include the unregulated areas of Pennsylvania, and sometimes the unregulated counties in Maryland and West Virginia. Among the comments supporting regulation of the entire state of Pennsylvania, there were differing opinions on whether the Pennsylvania Milk Marketing Board (PMMB) area 6 should be in the Northeast or the Mideast. Comments on behalf of the Association of Dairy Cooperatives in the Northeast (ADCNE), for example, supported including PMMB Area 6 in the Northeast. These comments also supported expansion to include Allegany and Garrett counties in western Maryland. Comments from the Pennsylvania State Grange supported regulating the entire state, but including all of it in the Northeast area.

Several comments suggested including currently-unregulated portions of Massachusetts in the Northeast marketing area. According to comments from a cooperative association, the "corridor" in Massachusetts that was suggested to remain unregulated has raised questions from handlers and producers regarding equity, since the handler within the corridor competes with regulated handlers. This association also stated that the wide dispersion of the towns suggested to remain unregulated would cause added expense to handlers in reporting Class I sales inside and outside the marketing area of the Northeast order. The Massachusetts Farm Bureau Federation, Inc., comments favored regulating all areas in the Federal order to protect Massachusetts dairy producers from the unfair marketing conditions created by current "pass-through" provisions of the New York-New Jersey order. In addition, a comment filed by the Commissioner of the Massachusetts Department of Food and Agriculture favored including all of Massachusetts in the consolidated order, stating that inclusion of the currently-unregulated "corridor" would not disadvantage any handlers currently located there. The letter stated that the dairy farmers of Massachusetts will be best served with uniform regulation, which would also foster fair competition.

A comment filed by the State of Vermont favored inclusion of the currently-unregulated portions of that State in the consolidated area on the basis that expansion creates cost equity between processors.

Maine has been and continues under this proposal to be excluded from Federal order regulation. Although limited support was expressed for Maine's inclusion in the Northeast consolidated order, approximately 5 comments supporting Maine's exclusion from Federal orders have been received. Comments filed by the Maine Milk Commission stated that Maine successfully regulates prices, resulting in Maine producers receiving higher prices than farmers whose milk is pooled under Federal orders. The comments further stated that consumer prices in Maine are lower than those in New England's states and counties. The American, New York and New Jersey Farm Bureaus all supported Maine's exclusion.

Over 115 comments, including petitions with numerous signatures, opposed expansion into Pennsylvania. Some of the comments cited the enjoyment by Pennsylvania producers of price stability for the more than 50

years during which the PMMB has been regulating milk marketing within the state. Comments from producers stated a desire to avoid additional government regulations and fees. Comments stated that the PMMB individual handler pools result in greater returns to producers, and producer returns would decline if handlers are required to pay the additional fluid value into the marketwide pool to subsidize cheese/powder plants.

As stated in the introduction to the consolidation discussion, it has been determined that consolidation of the existing orders does not necessitate expansion of the consolidated orders into areas in which handlers are subject to minimum Class I pricing under State regulation, especially when the states' Class I prices exceed those that would be established under Federal milk order regulation. Handlers located in PMMB areas 2, 3, and 6 are regulated under the State of Pennsylvania if they do not have enough sales in any Federal order area to meet an order's pooling standards. When such plants do meet Federal order pooling standards, the State of Pennsylvania continues to enforce some of its regulations in addition to Federal order regulations. As State-regulated handlers, they must pay a Class I price for milk used in fluid products that often is higher than the Federal order price would be. Inclusion of the Pennsylvania-regulated handlers in the consolidated marketing area, as in the case of including Maine, would have little effect on handlers' costs of Class I milk (or might reduce them), while reducing producer returns. In view of these situations, it appears that stable and orderly marketing conditions can be maintained without extending full Federal regulation to State-regulated handlers.

Regulated plants competing for Class I sales with unregulated distributing plants in northern Vermont and New York would be subject to a competitive disadvantage if the currently-unregulated handlers are not included within the consolidated marketing area. This result would occur because the "pass-through" provision of the current New York-New Jersey order, which exempts from minimum pricing a volume of milk equivalent to a regulated handler's sales in unregulated areas in competition with unregulated handlers, is not proposed for inclusion in the consolidated Northeast order. Inclusion of the currently unregulated areas of northern New York and Vermont in the consolidated Northeast order area will assure that distributing plant operators that currently are fully regulated would be placed on an equal competitive

footing with handlers currently unregulated, while having no negative effect on the producers who would be affected.

The "corridor" cited in Massachusetts should be included in the consolidated order area, partly because the sole handler who would be affected by the regulation of that area has gone out of business. Inclusion of the area at this time would not have the negative effect of imposing regulation on a small handler, as was feared earlier, but would lighten handlers' reporting burden and the market administrator's administrative burden in keeping separate data on sales in this small unregulated area. In addition, the offshore Massachusetts counties of Dukes and Nantucket should be added to the marketing area. The only entity currently operating in those counties (a producer-handler on Martha's Vineyard) would be exempt from the pooling and pricing provisions of the order by virtue of its status as a producer-handler and by having fewer than 150,000 pounds of route disposition per month. Mainland handlers distributing milk in these two counties would find their reporting burden eased if these counties become part of the marketing area.

The Western New York State order area is proposed to be added to the consolidated Northeast area because the persons regulated under that order have so requested. Regarding New York State, only the southern tier of western New York counties should not be included in the consolidated area because their addition would make more likely the full regulation of PMMB-regulated distributing plants with sales in that small area of New York (1 full county and 2 partial counties).

#### *Appalachian*

The proposed Appalachian marketing area is comprised of the current Carolina (Order 5) and Louisville-Lexington-Evansville (Order 46) marketing areas (less one Kentucky county that is included in the proposed Southeast marketing area) as well as 64 counties and 2 cities formerly comprising the marketing area of the recently-terminated Tennessee Valley Federal Order (Order 11) and currently-unregulated counties in Indiana and Kentucky. There are 297 counties and 2 cities in this proposed marketing area.

#### *Geography*

The Appalachian market is described geographically as follows: 7 unregulated Georgia counties (formerly part of Order 11), 20 Indiana counties (17 currently in Order 46 and 3 currently unregulated), 81 Kentucky counties (47 currently in

Order 46, 16 formerly part of Order 11, and 18 currently unregulated), all North Carolina and South Carolina counties (100 and 46, respectively, and all currently in Order 5), 33 Tennessee counties (formerly part of Order 11), 8 counties and 2 cities in Virginia (formerly part of Order 11), and 2 West Virginia counties (formerly part of Order 11).

The proposed Appalachian market reaches from the Atlantic coastline westward to southern Indiana and western Kentucky's border with Illinois. It is surrounded by Illinois on the west, Indiana, northeastern Kentucky, West Virginia and Virginia to the north, the Atlantic ocean on the east, and Georgia, Alabama, western Tennessee and southwestern Kentucky to the south. Measuring the extreme dimensions, this market extends about 625 miles from its northwest corner in Indiana to its southeastern corner on the South Carolina-Georgia border, about 300 miles south-to-north from the South Carolina-Georgia border to the North Carolina-Virginia border, about 500 miles west-to-east from the Appalachian-Southeast markets' border in Tennessee to eastern North Carolina, and about 375 miles west-to-east from the Illinois-Indiana border to West Virginia and Virginia.

The Appalachian market is contiguous to 3 proposed consolidated marketing areas: the Southeast area to the southwest and south, the Central area to the west and the Mideast area to the north. Unregulated counties in West Virginia and State-regulated area in Virginia also border this market to the north. North and South Carolina have almost 500 miles of coastline on the Atlantic Ocean.

In terms of physical geography, similarities exist across the states or areas included in this market. Southern Indiana and central Kentucky are in the Interior Low Plateau region where valleys and steep hillsides are typical. In this market, the Appalachian or Cumberland and Alleghany Plateaus are found in West Virginia, Virginia, Kentucky, Tennessee and northwestern Georgia on the western edge of the Appalachian Mountains. Eastern Tennessee and both western North and South Carolina are in the Blue Ridge region, which is part of the Appalachian Mountain range. Moving eastward toward the Atlantic Ocean, the central part of the Carolinas are in the Piedmont Plateau, with the Atlantic Coastal Plain covering approximately the remaining eastern half of both these states.

Climatic types in this region vary somewhat. Humid subtropical climates typical in most of North and South

Carolina, as well as Virginia (which is affected by elevation differences) and southern Indiana. Humid continental climates are typical for northwestern Georgia, western North and South Carolina and southern West Virginia. Temperate climates are common in eastern Tennessee and central Kentucky.

Much of the proposed Appalachian area does not provide a hospitable climate or topography for dairy farming. As an agricultural pursuit, dairy farming is far down the list in the area, accounting for an average of less than five percent of all receipts from farm commodities for the states involved. Crops such as tobacco, corn and soybeans, and other livestock commodities such as cattle/calves, turkeys and broiler chickens are more prevalent in this region.

#### Population

According to July 1, 1996, population estimates, the total population in the proposed marketing area is 17.1 million. There are 24 Metropolitan Statistical Areas (MSAs) within the proposed marketing area, containing 62.3 percent of the area's population. The largest 17 contain 50 percent of the population of the market. Charlotte, North Carolina, is the largest MSA in the marketing area with a population of 1.3 million. Charlotte is located near the South Carolina border about at the mid point of the North and South Carolina border, and about 250 miles west of the Atlantic coast. Less than 100 miles to the north lies the second-largest MSA of Greensboro-Winston-Salem-High Point, North Carolina, with a population of 1.1 million. About 50 miles east of Greensboro is the third-largest MSA, Raleigh-Durham-Chapel Hill, with one million people. The Raleigh MSA abuts the Greensboro MSA. An additional four North Carolina MSAs are among the largest of the 17 MSAs containing 50 percent of the population of the proposed marketing area, for a combined population of one million. North Carolina is the most populous state in the proposed marketing area with 7.3 million; over half the population of North Carolina is located in these seven MSAs.

South Carolina is the second-most populous state in the proposed consolidated area, with 3.7 million people. The Carolinas contain two thirds of the proposed market's population. Greenville is the largest MSA in the state with a population of 900,000. Greenville is located in the northwest corner of the state. Charleston, the second-largest MSA in South Carolina, with half a million

people, is approximately at the midpoint of South Carolina's coast.

The Tennessee portion of the proposed Appalachian market has a population of 2 million, with three MSA's that are included in the largest 17 in the market. These three areas contain 1.6 million, or over 80 percent of the population in that part of Tennessee that is proposed to be part of the Appalachian marketing area. The largest Tennessee MSA is Knoxville, which is in the eastern end of Tennessee near North Carolina. Six counties make up the Knoxville MSA with a combined population of 650,000. The Johnson City-Kingsport-Bristol area, the second-largest Tennessee MSA, is located in the northeastern tip of Tennessee along the Virginia and North Carolina border, and contains almost half a million people. Chattanooga, the third-largest MSA in Tennessee, is located on the Tennessee-Georgia border, and has a population of 446,000. The three MSAs run northeast to southwest just west of the North Carolina border.

The Kentucky portion of the proposed Appalachian market contains 2.7 million people. There are two MSAs within the state that are included in the largest 17 in the market. The largest is Louisville, which lies on the border with Indiana and has a population of one million. Lexington, the second-largest Kentucky MSA, is located in the center of the state and has just under half a million people. Generally, the Kentucky counties in the proposed Appalachian marketing area are not heavily populated. Only two have populations over 100,000. They are Jefferson county, where Louisville is located, and Fayette county, home to Lexington.

Indiana counties in the Appalachian market have a population of .8 million. Only Vanderburgh county has a population over 100,000. Evansville, the only MSA in the portion of Indiana included in the Appalachian market, is in Vanderburgh county. Evansville's MSA contains 289,000 and is located on the Indiana-Kentucky border, near the Illinois state line.

There are seven Georgia counties within the proposed Appalachian marketing area, with a total population of .3 million. Three of them, Catoosa, Dade, and Walker, are part of the Chattanooga MSA. These three counties have a combined population of 124,000. The 12 Virginia counties in the proposed Appalachian market have a population of .3 million. Three of the counties, Scott, Washington and Bristol City, are part of the Johnson City-Kingsport-Bristol MSA. The two West Virginia counties within the

Appalachian market have a total population of .1 million.

#### Fluid Per Capita Consumption

Estimates of fluid per capita consumption within the proposed Appalachian marketing area vary from 15.8 per month for South Carolina to 20.4 pounds per month for Indiana. Use of 17 pounds per month as a weighted average results in an estimated 291 million pounds of fluid milk consumption for the Appalachian marketing area. Appalachian handlers' route disposition within the area during January 1997 totaled 290 million pounds, with another 18 million distributed by producer-handlers, partially regulated plants and other order plants.

#### Milk Production

In December 1996, over 4,000 producers from 359 counties in 15 states pooled 443.3 million pounds of producer milk on Orders 5, 11 and 46. Approximately 71 percent of the milk pooled on the three orders was produced within the proposed consolidated marketing area.

North and South Carolina are the only States that are located entirely within the proposed consolidated marketing area, and provided nearly all of their producers' milk to Order 5 (encompassing the entire States of North and South Carolina), with 103.7 and 34 million pounds, respectively. Neither of these states produces enough milk to meet even the fluid milk requirements of its population. Kentucky producers pooled 101.1 million pounds on the three orders, with 89 percent produced within the proposed marketing area. Tennessee producers pooled 69.9 million pounds on the three orders, principally on Order 11, with 84 percent produced within the proposed marketing area. Although Virginia is primarily outside the marketing area, producers from 40 Virginia counties supplied 68.5 million pounds of milk for the FO 11 and FO 5 markets in December 1996. Georgia producers pooled 27.6 million pounds and Indiana producers pooled 21 million pounds in December, with the balance of the milk pooled on the three orders originating in Alabama, Connecticut, Illinois, Maryland, Massachusetts, New Mexico, Pennsylvania, and West Virginia.

Thirty-four counties each supplied over 3 million pounds of milk to the three markets consolidated in this proposed area. One such county was located in New Mexico, and another in Pennsylvania. Eight were located in Kentucky, south and southwest of Lexington, and southeast of Louisville.

Eleven were located in North Carolina west of the Raleigh-Durham area, with all but one located near Greensboro, Winston-Salem, Asheville, Charlotte or Durham. Of the two South Carolina counties that supplied over 3 million pounds each, one was located northwest of Columbia, and the other northwest of Charleston. The five Tennessee counties that pooled over 3 million pounds of milk on the three orders are located in northeast and southeast Tennessee; two in the Johnson City-Kingsport-Bristol area and three southwest of Knoxville. Only one of the six counties in Virginia that supplied over 3 million pounds to Orders 5 and 11 is located within the marketing area. Five of the six are located in southwest Virginia, with the other in the northwest part of the State.

#### Distributing Plants—Route Distribution

Using distributing plant lists included in both the Preliminary and Revised Preliminary Reports and the pooling standards used in the Revised Preliminary Report, updated for known plant closures through May 1997, 33 distributing plants would be expected to be associated with the Appalachian marketing area, including 29 fully regulated distributing plants (28 currently fully regulated and 1 currently partially regulated), 2 partially regulated (both currently partially regulated), 1 exempt plant, on the basis of having less than 150,000 pounds of total route disposition per month (currently fully regulated), and 1 government agency plant (currently a government agency plant). Four of the 33 distributing plants expected to be associated with the proposed area are not in the area but are located in Virginia, including 2 fully regulated plants (1 currently fully regulated and 1 currently partially regulated), and 2 partially regulated plants (both currently partially regulated). Since October 1995, 2 distributing plants in North Carolina have gone out of business.

Under the proposed Appalachian order, there would be 17 distributing plants in the largest Appalachian MSAs having distributing plants. There would be 3 pool distributing plants in the Greensboro-Winston-Salem-High Point area. The Charleston area would have 2 pool distributing plants. The Johnson City-Kingsport-Bristol, Tennessee, area would have 2 pool distributing plants. The Greenville-Spartanburg-Anderson, South Carolina, area would have 2 pool distributing plants. The Knoxville area would have 1 pool distributing plant and 1 exempt plant, with less than 150,000 pounds of total route disposition per month. The Charlotte, Chattanooga, Lexington, Louisville, and

Evansville areas would each have 1 pool distributing plant. The Raleigh-Durham area would have one government agency plant.

Of the remaining 11 distributing plants located in the marketing area, one pool plant would be located in a North Carolina MSA and one pool plant would be located in a South Carolina MSA. The nine remaining distributing plants, all expected to be pool plants, would not be located in MSAs. Four would be in North Carolina, 3 in Kentucky, 1 in Indiana, and 1 in Tennessee.

The 27 fully regulated plants in the Appalachian marketing area had distribution totaling 362 million pounds in January 1997, with eighty percent within the proposed marketing area.

A South Carolina plant included above in the description of fully regulated distributing plants—Superbrand Dairy Products, Inc., in Greenville (about 140 miles northeast of Atlanta)—has a greater proportion of its sales in the Southeast market than in the Appalachian market. This plant currently is locked into regulation under the Carolina order based on its need to procure a milk supply in the Carolina order, although it has greater route disposition in the Southeast. This lock-in is included in the proposed Appalachian order provisions.

#### Utilization

According to October 1995 pool statistics for handlers who would be fully regulated under this Appalachian order, the Class I utilization percentages for the Carolina and Louisville-Lexington-Evansville markets and the former Tennessee Valley market were 84, 78, and 81 percent, respectively. Based on calculated weighted average use values for (1) the current order with current use of milk, and (2) the current order with projected use of milk in the consolidated Appalachian order, the potential impact of this proposed rule on producers who supply the current market areas is estimated to be: Carolina, a 3-cent per cwt decrease (from \$14.23 to \$14.20); Louisville-Lexington-Evansville, a 5-cent per cwt increase (from \$13.35 to \$13.40); and Tennessee Valley, a 2-cent per cwt increase (from \$13.92 to \$13.94). The weighted average use value for the consolidated Appalachian order market is estimated to be \$13.97 per cwt. For December 1996, combined Class I utilization for Orders 5, 11 and 46 was 75.6 percent based on 335.2 pounds of producer milk used in Class I out of 443.5 million total producer milk pounds pooled.

#### Other Plants

Also located within the proposed consolidated Appalachian marketing area during May 1997 were 13 supply or manufacturing plants: 4 in Kentucky (1 in the Louisville area), 5 in North Carolina (1 in the Charlotte-Gastonia-Rock Hill area and one in the Greensboro-Winston-Salem-High Point area), 1 in Tennessee, and 3 nonpool cheese plants in Indiana (1 in the Lexington area and one in the Louisville area). Three of the 13 plants are pool plants, or have a "pool side." Two of the three pool plants (one in Kentucky and the one in Tennessee) are "split plants," that is, one side of a plant is a manufacturing facility, and the other side receives and ships Grade A milk, and accounting is done separately. Of these pool plants, the pool sides of the 2 split plants have no primary product, shipping only to distributing plants. The nonpool side of one of these plants manufactures cheese, while the nonpool side of the other manufactures powder. The other pool plant is a supply plant that manufactures primarily Class II products. Of the other nonpool plants in the proposed Appalachian marketing area, 5 manufacture primarily cheese and 5 manufacture primarily Class II products.

#### Cooperative Associations

In December 1995, there were ten cooperatives representing producers in the proposed Appalachian marketing area. One cooperative pooled milk on all three markets. The Tennessee Valley and Louisville-Lexington-Evansville Federal orders had two cooperatives in common, while the Tennessee Valley and Carolina Federal orders had one cooperative in common. For December 1995, 80 percent of the producer milk pooled on the three markets was associated with cooperatives, and 85 percent of the cooperative-marketed milk was pooled by the four cooperatives that marketed milk on more than one of the three orders.

#### Criteria for Consolidation

Overlapping route disposition and procurement are the primary criteria on which this proposed consolidation is based. There is a stronger relationship between the three marketing areas involved than between any one of them and any other marketing area on the basis of both criteria. There is also common cooperative association affiliation between the markets.

#### Discussion of Comments and Alternatives

A comment filed on behalf of Barber Pure Milk Company and Dairy Fresh

Corporation, both in Alabama, proposed that the Florida orders and the Carolina and Tennessee Valley orders be merged with the Southeast. The commenter stated that evidence shows the Florida markets are vitally involved with other areas of the Southeast in Class I sales, obtaining milk supply, and in the disposition of surplus milk. A number of comments, including those filed by Mid-America Dairymen, Inc., and Carolina Virginia Milk Producers Association, urged that the Appalachian area be combined with the Southeast order area, primarily on the basis of milk procurement overlap in south central Kentucky. Several commenters, mainly producers, favored putting all of Kentucky in one order and most suggested adding it to the Southeast. Comments from Trauth Dairy, a Mideast pool plant under this proposed consolidation, did not specifically ask that Kentucky be put into one order, but that Trauth (at Newport, Kentucky) be placed in the same order (Appalachian) as the handlers Trauth described as its primary competition for producer milk and for retail sales in the marketplace.

As discussed under the description of the proposed consolidated Florida market, overlapping milk distribution and procurement involving the three current Florida markets is much greater within the Florida markets than between any of the Florida markets and any other market. As stated in the description of consolidation criteria, areas that supply a minor proportion of an adjoining area's milk supply with a minor proportion of their own total milk production while handlers located in the area are engaged in minimal competition with handlers located in the adjoining area do not necessarily have a strong enough association with the adjoining area to be consolidated with it. It is impossible to find a boundary across which significant quantities of milk are not procured for other marketing areas.

Consolidation of the Carolina and Tennessee Valley markets with the Southeast is not proposed because of the minor degree of overlapping route disposition and producer milk between these areas. Less than one-tenth of the milk produced in the Kentucky counties proposed to be in the Appalachian area would be pooled under the Southeast order, and approximately one-fifth of the production from the Kentucky portion of the Southeast area would be pooled under the Appalachian order.

With the exception of two Appalachian handlers who account for two-thirds of the disposition by Appalachian handlers in the Southeast order area, only a minor proportion of

the route disposition of Appalachian handlers is distributed in the proposed Southeast area. In total, Appalachian handlers distribute 11 percent of their route dispositions in the Southeast area, while Southeast handlers distribute less than 3 percent of their route dispositions in the Appalachian area.

There would be very little basis for splitting the current Order 46 area (Louisville-Lexington-Evansville) to include northern Kentucky with the proposed Appalachian area. Only 3 percent of Appalachian handlers' route disposition is distributed within the Ohio Valley order area, while less than one million pounds of Class I sales moves from the Ohio Valley area into the Order 46 area.

#### *Florida*

The proposed Florida marketing area is comprised of the three current Federal order marketing areas contained wholly in the state of Florida: Upper Florida (Order 6), Tampa Bay (Order 12) and Southeastern Florida (Order 13). There are 63 counties in this proposed area (40 in Order 6, 13 in Order 12, and 10 in Order 13).

#### *Geography*

The proposed Florida marketing area is described geographically as all counties in the State of Florida, with the exception of the four westernmost counties in the Florida Panhandle. This proposed marketing area is a large peninsula, ranging from about 140 miles in width in the north to about 50 miles in width in the south, that extends south from the southeast U.S. about 400 miles between the Atlantic Ocean and the Gulf of Mexico. Also included in the Florida market is approximately 150 miles of the Panhandle, a narrow strip of land extending west along the Gulf of Mexico from the northern part of the peninsula. The water surrounding most of Florida's peninsula constitutes a natural boundary, as east-to-west travel is limited.

Almost all of Florida has a humid subtropical climate. The southern end of the state and the islands south of the peninsula have a tropical wet and dry climate. In general, the state's climate can and does affect levels of milk production negatively. Seasonal variation in production for this market typically is greater than for most other U.S. regions. The importance of dairy farming as an agricultural pursuit in Florida is relatively minor (7 percent of total receipts from agricultural commodities), with several crops contributing more total receipts to the State's income. However, no livestock

commodity is as important in Florida as dairy farming.

#### *Population*

According to July 1, 1996, population estimates, the total population in the proposed Florida marketing area is 13.8 million. Ninety-three percent of the population of the marketing area is located in Metropolitan Statistical Areas (MSAs). The two largest MSAs are Miami-Fort Lauderdale (Miami) on the eastern side of the southern end of the peninsula, and Tampa-St. Petersburg-Clearwater (Tampa) midway on the western side of the peninsula. Broward and Dade Counties comprise the Miami population center (currently in Order 13) with a population of 3.5 million. The Tampa population center (currently in Order 12) is comprised of Hernando, Hillsborough, Pasco and Pinellas counties with a population of 2.2 million. The six counties in these two population centers represent about 41 percent of the total marketing area population.

#### *Fluid Per Capita Consumption*

Florida customarily is considered a deficit milk production state. For much of the year, milk needs to be imported from other states in order to meet the demand for fluid consumption. Based on the population figure of 13.8 million and an estimated per capita fluid milk consumption rate of 17 pounds of fluid milk per month, total fluid milk consumption in the Florida marketing area is estimated at 234.6 million pounds per month.

During October 1995, 205 million pounds of milk were disposed of in the proposed marketing area by all Florida distributing plants. Plants located outside the marketing area (mostly from the Southeast market [Order 7]) had route disposition within Florida of 20 million pounds. The discrepancy between the actual total route disposition of 225 million pounds and the estimated consumption level of 234.6 million pounds may be explained by the older than average population in Florida.

#### *Milk Production*

In December 1996, 222 million pounds of milk produced in Florida were pooled in four Federal orders; 98.5 percent of this milk was pooled on the three current Florida orders. About 370 producers located in Florida (96 percent of all Florida producers having association with Federal orders) had producer milk pooled on at least one of the three Florida markets. A small number of Florida producers had producer milk associated with Order 7,

while more than 100 Georgia producers had producer milk associated with the Florida markets. Additionally, 34 million pounds of Georgia milk was pooled on the three Florida markets; 85 percent of this milk went to Order 12.

There are 44 counties in Florida that pooled milk in at least one of the three current Florida orders. Seven of these counties produced 62.6 percent of the milk pooled.

Three counties (Gilchrist, Lafayette and Suwannee, about 75 miles west of Jacksonville) had 53.9 million pounds of producer milk. For these three counties, 85.5 percent of the December 1996 producer milk was pooled on the Tampa Bay order, which is located approximately 150 miles southeast of the counties.

More than 80 percent of Clay County's producer milk was pooled in Order 6. This county is in the Jacksonville MSA, which is the largest population center in Order 6.

About 20 million pounds of producer milk came from Hillsborough and Highland Counties, both part of the Order 12 market. However, this milk was pooled about evenly between Orders 12 and 13.

Okeechobee County, located in the Order 13 marketing area about 125 miles northwest of the Miami area, is by far the largest milk producing county in Florida. The county had 54.5 million pounds of producer milk in December 1996, almost all of which was pooled on Order 13.

#### Distributing Plants—Route Distribution

Using plant lists included in both the Preliminary and Revised Preliminary Reports and the pooling standards used in the Revised Preliminary Report, updated for known plant closures through May 1997, 15 plants would be expected to be fully regulated under the proposed Florida market. Five of these plants are located in the Miami MSA and three in the Tampa MSA. Three plants are located in mid-Florida, one in the Orlando area and two in the Lakeland-Winter Haven area. Three more are located in northeast Florida; two in the Jacksonville area, and one in Daytona Beach. Two plants having route disposition of less than 150,000—one in the Tampa MSA and the other in Citrus County (north of Tampa and west of Orlando)—would be exempt.

Slightly less than two-thirds of the proposed market's population is contained in the MSAs where fully regulated plants are located.

#### Utilization

According to October 1995 pool statistics for handlers who would be

fully regulated under this Florida order, the Class I utilization percentages for the Upper Florida, Tampa Bay, and Southeastern Florida markets were 85, 90, and 91 percent, respectively. Based on calculated weighted average use values for (1) the current order with current use of milk, and (2) the current order with projected use of milk in the consolidated Florida order, the potential impact of this proposed rule on producers who supply the current market areas is estimated to be: Upper Florida, an 11-cent per cwt increase (from \$14.67 to \$14.78); Tampa Bay, a 5-cent per cwt decrease (from \$15.09 to \$15.04); and Southeastern Florida, an 11-cent per cwt decrease (from \$15.42 to \$15.31). The weighted average use value for the consolidated Florida order market is estimated to be \$15.05 per cwt. For December 1996, combined Class I utilization for the three Florida markets was 83.9 percent based on 211,712,000 pounds of producer milk used in Class I out of 252,402,000 total producer milk pounds.

#### Other Plants

Also located within the Florida marketing area are four supply or manufacturing plants, three of which are not associated with the current markets' pools. Three ice cream plants are located in the Tampa area and one pool supply plant is in the Jacksonville area.

#### Cooperative Associations

Four cooperatives market milk in the Florida markets, and represent nearly 100 percent of the milk marketed. Florida Dairy Farmers Association is the only cooperative with membership in all three current markets. In December 1995, 60 percent of the producer milk associated with the three markets came from members of this cooperative. During this same month, Tampa Independent Dairy Farmers Association members were affiliated with the Tampa Bay and Southeastern Florida markets, while Mid-America Dairymen, Inc., and Select Milk Producers, Inc., members had producer milk on the Tampa Bay pool.

#### Criteria for Consolidation

As suggested in both the initial and Revised Preliminary Reports on Order Consolidation, the consolidated Florida market should encompass the current marketing areas of the Upper Florida, Tampa Bay and Southeastern Florida Federal milk orders. Natural boundary limitations and overlapping sales and procurement areas among the three orders are major reasons for consolidation, as well as a measure of

association evidenced by cooperative association proposals to consolidate these three marketing areas. Further, the cooperative associations in this area have worked together for a number of years to accommodate needed movements of milk between the three Florida Federal orders, and into and out of the area.

#### Discussion of Comments and Alternatives

One comment, filed on behalf of two Alabama handlers, suggested that the order areas of Florida, the Carolinas and Tennessee Valley be merged with the Southeast. The comment stated that the Florida markets are vitally involved with other areas of the southeast in Class I sales, procurement of milk supplies, and disposition of surplus milk. Although there is some overlap in these functions between the Florida markets and the Southeast order area, it is not great enough to warrant the combination of these three order areas, which have a greater degree of affinity among themselves than with any other market, with the Southeast. Given the closeness of the relationship between the current Florida markets, and the lack of any significant overlap of sales or production with other order areas, no alternatives other than those discussed were considered with regard to this area.

#### Southeast

The proposed Southeast marketing area is comprised of the current Southeast (Order 7) marketing area, portions of the current Southwest Plains (Order 106) marketing area in northwest Arkansas and southern Missouri, and six southeastern Missouri counties from the current Southern Illinois-Eastern Missouri (Order 32) marketing area. Also included are 16 currently unregulated Missouri counties, 21 currently unregulated Kentucky counties, and 1 Kentucky county that currently is part of the Louisville-Lexington-Evansville (Order 46) marketing area. There are 572 whole counties and 1 partial county (Pulaski County, Missouri) in this proposed area.

#### Geography

The Southeast market is described geographically as follows: all counties in Alabama, Arkansas, Louisiana, and Mississippi (67, 75, 64 and 82 counties, respectively), 4 in Florida, 152 in Georgia, 44 whole and 1 partial in Missouri, 62 in Tennessee and 22 in Kentucky (one—Logan County—currently is in Order 46, and 21 currently are unregulated). Of these 21 counties, 14 were part of the former

Paducah, Kentucky (Order 99) marketing area. Eleven Arkansas and 23 Missouri counties (including part of Pulaski County) are part of the current Order 106 marketing area. Six Missouri counties are part of the current Order 32 marketing area. Sixteen southeastern Missouri counties currently are unregulated (4 of these were part of the former Paducah Federal milk order).

The Southeast market spans the southeastern area of the United States from the Gulf of Mexico and the Alabama/Georgia-Florida border north to central Missouri, Kentucky, Tennessee and South Carolina, and from the Atlantic Ocean west to Texas, Oklahoma, and Kansas. Measuring the extreme dimensions, this market extends about 575 miles north to south from central Missouri to southern Louisiana and 750 miles west to east from Louisiana's border with Texas to the Atlantic Ocean coast in southern Georgia.

The Southeast marketing area is contiguous to 4 other proposed consolidated marketing areas: Florida to the southeast, the Southwest to the west, the Central to the northwest and the Appalachian to the northeast and east. Georgia's coastline on the Atlantic Ocean is about 100 miles in length, while western Florida, Alabama, Mississippi and Louisiana extend about 600 miles along the Gulf of Mexico coastline. Also contiguous to the current Southeast market are currently unregulated counties in Texas, Missouri, Kentucky (and as of October 1, 1997, the Tennessee Valley [Order 11] marketing area). The proposed consolidated marketing areas would encompass all of these counties into the Southwest, Central, Appalachian or Southeast marketing areas, with some currently-unregulated counties in central Missouri remaining unregulated under this proposal.

In terms of physical geography, the Southeast region is generally flat or gently rolling low-lying land. Relatively higher elevations which might potentially form natural barriers or obstruct easy transportation exist in northwest Arkansas and northeast Georgia.

Moving from the south to the north of the Southeast market, climates range from humid subtropical in coastal areas to warm and humid or humid continental to temperate in Tennessee and Kentucky. Warm, humid summers and mild winters are typical in the Southeast. These types of climates can severely limit the production level of dairy herds in the summer.

#### Population

According to July 1, 1996, population estimates, the total population in the proposed Southeast marketing area is 26.7 million. The 42 Metropolitan Statistical Areas (MSAs) in the proposed market account for 62 percent of the total marketing area population. Almost half of the Southeast population is located in the 17 most populous MSAs. Eight MSAs have populations greater than 500,000 each; their total population is about 35 percent of the Southeast population. Because of the large number of MSAs in the Southeast market and also because no large (i.e., greater than 500,000) population centers are added to this market under this proposal, only those areas with populations greater than 500,000 are described in greater detail.

Over 25 percent of the Southeast market's population is located in Georgia, the most populous of the Southeast market states, with 7.1 million people. Almost half of Georgia's population is concentrated in the Atlanta MSA, located about 60 miles south of the Southeast-Appalachian marketing area boundary in the northwest portion of the state. Atlanta is the largest city in the Southeast market with a population of 3.5 million.

With 4.3 million people, Alabama is the Southeast market area's third most populous state. Birmingham and Mobile, the state's two largest MSA regions, are among the top eight in population in the Southeast. The Birmingham area has a population of about 900,000 and ranks 5th in size among all Southeast area MSAs. Birmingham is located about 150 miles west of Atlanta in north central Alabama. The Mobile area is a Gulf of Mexico port city in southwestern Alabama. With a population of 520,000, Mobile is the 8th largest population center in the Southeast market area.

Louisiana is the second most populated state in the Southeast market area with 4.4 million people. Two of the Southeast's 8 largest MSAs are located in Louisiana—New Orleans, the second largest MSA with 1.3 million people and Baton Rouge, the 6th largest MSA with almost .6 million people. New Orleans is located in the state's "toe" in southeastern Louisiana. Baton Rouge also is located in Louisiana's "toe," about 80 miles west of New Orleans.

Arkansas has a total population of 2.5 million—2 million from the current Southeast marketing area and an additional 500,000 from the Arkansas portion of the Southwest Plains marketing area. The Little Rock-North Little Rock, Arkansas (Little Rock) MSA,

in the center of Arkansas, has the 7th largest population concentration in the Southeast market area with 550,000.

The portion of Tennessee in the Southeast marketing area is the fourth most populated with 3.3 million people and is home to the third and fourth largest MSAs in the Southeast. The Nashville area, with a population of 1.1 million, is located in central Tennessee. The Memphis, Tennessee/Arkansas/Mississippi MSA, also with a population of 1.1 million, is located near these three states' borders.

Other states or portions of states in the Southeast marketing area do not have MSAs with greater than 500,000 population. Mississippi, the Southeast's 5th most populous state, has a total population of 2.7 million. The Missouri, Florida and Kentucky counties in the Southeast market have populations of 1.3 million, 590,000 and 520,000, respectively.

#### Fluid Per Capita Consumption

Fluid per capita consumption estimates vary throughout the Southeast market from a low of 16 pounds of fluid milk per month in Mississippi to a high of 19 pounds in Arkansas and Kentucky. Multiplying the individual states' consumption rates by their population results in an estimated fluid milk consumption rate of 467 million pounds of fluid milk per month for the Southeast marketing area. With route distribution from the current Southeast order handlers (not including the 3 Arkansas and Missouri plants) equaling 334 million pounds within the Southeast marketing area, route distribution from these handlers is approximately 100 million pounds less than the expected consumption.

In January 1997, Georgia had the greatest "deficit"—with route distribution from Order 7 handlers falling about 42 million pounds short of the 122 million pounds of expected consumption. The state's fluid needs were met by the route distribution of about 44 million pounds into Georgia by fully regulated handlers in the proposed Appalachian and Florida markets.

Other states' "deficits" generally ranged from 4 to 11 million pounds. It is likely that handlers regulated under other Federal orders had distribution into the Southeast area. Alabama is the only state in which the amount of route distribution by Order 7 handlers is about the same as the expected consumption level.

#### Milk Production

In January 1997, 4,180 producers from 388 counties pooled 477.4 million pounds of producer milk on the current

Southeast market. Over 85 percent of the Southeast's producer milk came from Southeast market area counties. Of the 388 counties, 19 pooled over 5 million pounds each, accounting for 39 percent of Order 7's producer milk. Of these 19 counties, 2 Texas counties are located outside the proposed Southeast market area. Because of the large number of counties, only the locations for those top 19 production counties are described in greater detail. However, the volume of producer milk, number of producers (farms) and number of counties is provided for each state within the market area.

Almost 73 million pounds of milk were pooled on the Southeast market from 581 producers in 28 Louisiana parishes in January 1997. Top production parishes are Tangipahoa, Washington and St. Helena, all located in the state's "toe," north of New Orleans and northeast of Baton Rouge, each bordering Mississippi. Another high production area is centered on De Soto Parish in northwestern Louisiana. These four parishes account for over 62 million pounds of producer milk, with 76 percent coming from Tangipahoa and Washington parishes.

Almost 67 million pounds of milk were pooled on the Southeast market from 331 producers in 68 Georgia counties in January 1997. Of this volume, 64 million came from 312 producers in 64 Georgia counties in the Order 7 marketing area. The balance is associated with Georgia producers located in the marketing area of the recently-terminated Order 11 (Tennessee Valley). Top production counties are Putnam, Morgan and Macon, which pooled 27 million pounds of producer milk on Order 7.

About 65 million pounds of milk were pooled on the Southeast market from 580 producers in 46 Tennessee counties in January 1997. Of this volume, 62 million came from 562 producers in 42 Tennessee counties in the Order 7 marketing area. The balance is associated with Tennessee producers located in the marketing area of the recently-terminated Federal Order 11. Two high production counties in the state are Marshall and Lincoln, located in south central Tennessee. These counties contributed over 12 million pounds of producer milk to the Order 7 pool in January 1997.

About 61 million pounds of milk were pooled on the Southeast market from 443 producers in 48 Mississippi counties in January 1997. Top production counties are Walthall and Pike, in southern Mississippi on the state's border with Louisiana. These two counties adjoin the heavy milk

production area in Louisiana. The counties contributed 15 million pounds of producer milk to the Order 7 pool in January 1997.

About 32 million pounds of milk were pooled on the Southeast market from 408 producers in 19 Kentucky counties in January 1997. Additionally, 116 producers in 15 of these counties pooled almost 9 million pounds of producer milk on Orders 11 and 46 (Louisville-Lexington-Evansville). Two counties, Barren and Monroe, contributed over 13 million pounds of producer milk. These contiguous counties are in south central Kentucky about 80 miles northeast of Nashville, Tennessee.

Four Missouri counties—Wright, Texas, Laclede and Howell—pooled 33 million pounds of producer milk on Order 7. All of these counties currently are located in the Order 106 (Southwest Plains) marketing area in southern Missouri.

Other Southeast marketing area states or areas contribute producer milk to the Southeast marketwide pool. About 37 million pounds of milk were pooled on the Southeast market from 205 producers in 51 Alabama counties, and 25 million pounds were pooled from 343 producers in 39 Arkansas counties. Sixteen Florida producers from 6 counties (2 in the Southeast market area) pooled 3.5 million pounds on Order 7 in January 1997.

In January 1997, Order 7 producer milk also originated in Missouri counties not included in the Southeast marketing area, Texas, New Mexico, Indiana and Oklahoma. Large amounts of milk from Missouri (21 million pounds in addition to the 33 million described previously) and Texas (46 million pounds—20 million from Hopkins and Erath Counties) were associated with the Order 7 pool. It should be noted that milk does not need to be physically received at a Federal order plant regulated under the order in which the milk is pooled.

#### Distributing Plants—Route Distribution

Using distributing plant lists included in both the Preliminary and Revised Preliminary Reports and the pooling standards used in the Revised Preliminary Report, updated for known plant closures through May 1997, 47 distributing plants located in the proposed Southeast marketing area would be expected to be associated with the Southeast market (including the added territory in northwestern Arkansas and southern Missouri). These plants include 36 fully regulated distributing plants, 2 partially regulated, one exempt plant based on size, one producer-handler, and 7 government

agency plants (including university and state prison plants). None of these plants' regulatory status is expected to change as a result of the consolidation process. Of the 36 fully regulated plants, 18 are located in the largest eight MSA regions. One distributing plant located in the proposed Appalachian marketing area that has more than half of its route disposition within the Southeast marketing area would be locked into regulation under the Appalachian order.

Since October 1995, it is known that 7 distributing plants (6 fully regulated and 1 exempt) have gone out of business. These plants were located in Alabama, Arkansas, Georgia, and Missouri (1 plant each), and Mississippi (3 plants). Also, one fully regulated distributing plant, Centennial Dairy Farms, Inc., in Atlanta, GA, began packaging and distributing products in October 1996. Information for this plant is included in route dispositions reported for January 1997, the month used in this analysis.

Of the 47 distributing plants, Georgia has 7; Louisiana, 12; Mississippi, 6; Alabama, 7; Arkansas, 6; Tennessee, 5; Missouri, 2; and Kentucky, 2. No distributing plants are located in the Florida counties included in the Southeast market area.

In January 1997, the 34 plants fully regulated under Order 7 at that time had route distributions totaling 372 million pounds. About 90 percent, or 334 million pounds, was distributed within the Order 7 marketing area. Route distribution volumes from the 11 nonpool distributing plants were relatively insignificant and are not included here. These data do not include distribution information from the 3 fully regulated plants in northwest Arkansas and southern Missouri that would be included in the proposed Southeast pool. All 3 plants are operated by one handler; thus this data is proprietary information and is restricted. These plants' information is included, however, in the market information presented in the Central market discussion.

In Georgia, three pool distributing plants are located in the Atlanta area, with 2 others elsewhere in the State. Georgia also has 1 partially regulated handler and 1 government agency (state prison) plant.

Nine of Louisiana's 12 distributing plants currently are and would continue to be fully regulated (pool plants) in this proposed marketing area. Five of these 9 are located in either the New Orleans or Baton Rouge areas (2 and 3, respectively). Four other pool distributing plants are located in Louisiana. The remaining three plants

are affiliated with universities or the state prison.

Four of Mississippi's 6 currently operational distributing plants would be fully regulated pool plants in the Southeast market. Two universities also have plants.

All seven of Alabama's distributing plants are fully regulated. One is located in the Birmingham area and 2 are located in the Mobile area. Of the remaining four, 2 are in northern Alabama, one is in central Alabama, and one is in the state's southeastern corner.

Four of Arkansas' 6 currently operational distributing plants are fully regulated; two are in the Little Rock area, and the other 2 are located in northwest Arkansas. Also located within Arkansas are an exempt distributing plant and a state prison plant. All five of Tennessee's distributing plants are fully regulated. Three of the 5 are located in the Nashville area and the remaining two are in the Memphis area.

Two distributing plants that would be fully regulated under the Southeast market are located in the currently unregulated Kentucky counties that are proposed to be added to this marketing area. One is located in Fulton in the southwest corner of Kentucky on the Tennessee border, and the other about 30 miles east of Fulton.

Two Missouri plants are located in the counties proposed to be included in the Southeast area. One fully regulated plant is located in Springfield; a partially regulated plant based on October 1995 data, but exempt (by virtue of having less than 150,000 pounds of route dispositions) based on January 1997 data, is located northeast of Springfield.

#### Utilization

According to January 1997 pool statistics, the Class I utilization for the Southeast market was about 78 percent. Changes to this percentage are likely to occur with the addition of 3 pool plants or potential changes in plants' regulatory status. It is not expected that the addition of the plants would have a significant impact on producer returns in the Southeast as a result of consolidation. For December 1996, Class I utilization for the Southeast market was 73.4 percent based on 339,275,000 pounds of producer milk used in Class I out of 462,455,000 total producer milk pounds.

#### Other Plants

Also located within the Southeast marketing area during May 1997 are 37 supply or manufacturing plants: 1 in Kentucky, 5 in Alabama (including 1 in

the Birmingham area), 5 in Arkansas (including 1 in the Little Rock area), 7 in Georgia (including 4 in the Atlanta area), 3 in Louisiana (including 1 in the Baton Rouge area), 11 in Missouri, 2 in Mississippi, and 3 in Tennessee (including 1 each in the Memphis and Nashville areas). Eight of the 37 plants are pool plants. Of these pool plants, 2 primarily ship to distributing plants, 3 manufacture cheese, 1 manufactures Class II products, 1 manufactures powder and 1 primarily manufactures other products. Of the Southeast marketing area's 28 nonpool plants, 13 manufacture primarily Class II products, 3 manufacture cheese, 10 manufacture primarily other products, and 1 each manufacture primarily butter and cheese. One plant is a "split plant," with one side serving as a manufacturing facility primarily for Class II products, while the other side receives and ships Grade A milk. Accounting is done separately.

#### Cooperative Associations

In December 1995, six cooperative associations represented members marketing 78 percent of the milk pooled on the Southeast market: Mid-America Dairymen, Inc.; Associated Milk Producers, Inc., Southern Region; Carolina-Virginia Milk Producers Association, Inc.; Arkansas Dairy Cooperative Association (ADCA); Vanguard Milk Producers Cooperative (VMPC); and National Farmers Organization, Inc. ADCA and VMPC members marketed milk only in the Southeast Federal order, while the other 4 cooperatives' members marketed milk in multiple Federal orders.

#### Criteria for Consolidation

Retention of the Southeast marketing area as a single area is based on overlapping route dispositions within the marketing area to a greater extent than with other marketing areas. Procurement of producer milk also overlaps between states within the market. The need for milk from outside the market is primarily seasonal, and is not as great as the volume of milk that is pooled from other areas. There is common cooperative association membership within the marketing area.

The addition of northwest Arkansas and southern Missouri to the marketing area is primarily in response to comments received during the public comment period. The association that exists between these 2 areas, the Southeast marketing area, and the proposed Central market should continue to be monitored throughout the reform process.

#### Discussion of Comments and Alternatives

Several commenters, primarily producers, favored putting Kentucky all in one order and most suggested adding it to the Southeast. In a comment that was considered in the Revised Preliminary Consolidation Report, Georgia Milk Producers had suggested dividing the Southeast Order on the state line between Mississippi and Alabama. Over 35 form letters opposed the separation of the Southeast marketing area between Mississippi and Alabama. A more recent Georgia Milk Producers comment rescinded this position.

A comment filed on behalf of Barber Pure Milk Company and Dairy Fresh Corporation, both in Alabama, suggested that the Florida orders and the Carolina and Tennessee Valley orders be merged with the Southeast. The comment stated that evidence shows the Florida markets are vitally involved with other areas of the Southeast in Class I sales, obtaining milk supply, and in the disposition of surplus milk. As discussed under the description of the proposed consolidated Florida market, the greatest overlap in sales distribution and milk supply involving the Florida markets occurs between the three current Florida markets. A discussion of the issue of consolidating the Carolina and Tennessee Valley markets with the Southeast can be found in the description of the proposed Appalachian market.

Approximately 10 commenters suggested that southern Missouri and/or northwest Arkansas should be included in the Southeast marketing area. Mid-Am supported making both areas part of the Southeast Federal order to correct the inequity perceived by the cooperative to be caused by southwest Missouri manufacturing plants balancing the Southeast without being able to pool, and inefficient milk movements caused by blend price discrepancies. AMPI concurred, suggesting that southern Missouri historically has been a supply source for the Southeast. The Director of the Missouri Department of Agriculture contended that southern Missouri has the largest concentration of milk production in the state and serves as the reserve supply for southeastern markets. The Missouri Farm Bureau Federation also suggested including some southern Missouri counties with the Southeast. One producer also supported including southern Missouri in the Southeast Marketing Area.

It appears that a substantial amount of the milk supply pooled under the