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S.M.P.A.

March 23, 1998

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RECEIVED

Mr. Richard M. McKee
Deputy Administrator, Dairy Programs
USDA / AMS, Room 2968, South Building
Post Office Box 96456
Washington, DC 20090-6456

Re: Docket Number DA-97-12

Dear Mr. McKee:

The following comments address the proposal to consolidate and reform the Federal Milk Marketing Order Program (proposed rule). Security Milk Producers Association (SMPA) greatly appreciates the opportunity to comment on the proposed rule and is cognizant of the immense task with which the Department has undertaken. You and your staff are to be applauded on the detail-oriented manner in which you have approached this issue. Please consider the following comments in your efforts to produce a final rule.

Security Milk Producers is a cooperative association which markets over a billion pounds of milk annually. We have members in California, Arizona, and Nevada. Our herds include approximately 16.5 million pounds of Grade A, bottling quality, milk per month produced on ranches located in southern Nevada's Clark County. In fact, all milk currently produced in Clark County, Nevada is produced by SMPA members. Our customer, in southern Nevada, Anderson Dairy, markets all of their milk in the Las Vegas area. They do not, however, completely supply the needs of that ever-growing metropolitan area. The Las Vegas area is a perfect example of the decline in per capita milk production. Population continues to grow at an increasingly rapid rate, yet milk production on these dairies has actually decreased.

Consolidation

Previous correspondence from SMPA has largely been directed toward the need to consolidate all of the State of Arizona and the Clark County area of southern Nevada into one marketing order. We support the proposed consolidation and the proposed formation of an Arizona - Las Vegas federal order.

Replacement of the Basic Formula Price

SMPA supports the replacement of the current BFP with a multiple component pricing system that will determine butterfat, protein, and other solids for milk used in Class III and butterfat and solids-not-fat prices for milk used in Class IV products. We agree with USDA that the separation of manufacturing milk into two distinct classes will assure that shifts in demand for any one manufactured product will not lower the prices for milk used in all other classifications of milk. The formulas proposed in the rule seem adequate, and the make allowances and the yield factors indicated should not need to be revised. The committees tasked with creating these formulas have been thorough in their research and in our opinion, are right on the mark. Make allowances and yields will vary from place to place and from plant to plant, but as any dairyman can tell you, necessity is the mother of invention. When one finds him or her self on the down side of an equation, they must, and do, become more efficient.

Class I Price Structure

Security Milk Producers Association supports option 1a and opposes option 1b as proposed. Option 1a, from a marketing standpoint, will allow for an orderly system for marketing milk. It is very similar to the existing Class I price surface, and will not greatly disrupt the current flow of milk. One of the troublesome things with option 1b is the large variances between connecting areas. When market conditions permit, milk that normally flows efficiently one way, can very easily disrupt the normal flow of an area, such as Las Vegas, to capitalize on the higher differential. Milk would move from outside the order and displace the milk supplied locally. Another problem with 1b is the disparity between Los Angeles and Riverside / San Bernardino. Under the proposed option 1b, L.A. would have a differential of $1.22 and Riverside / San Bernardino, where a majority of the milk for L.A. is produced, would have a differential of $1.41. A handler in the Los Angeles area would have a very difficult time acquiring raw milk for its processing needs. (See attachments)

In support of option 1a, the following excerpt from one of our previous correspondences is offered, 'Fluctuations in market signals, and supply and demand, will result in a BFP that will be, at times above and, below the cost of producing milk. Coupled with a production variance of up to 30% from spring to late summer, the desert areas of the southwestern United States should have a differential high enough to ensure market demand is met. The current differential, in Phoenix, of $2.52 per cwt. was set after careful analysis of that area's yearly supply and demand, and seems adequate. The Las Vegas area, however, currently has a differential of $1.60 per cwt. This number needs to be examined. Salt Lake City, Utah has a $1.90 differential, today, which may or may not be supported (we plead ignorance, as we have no experience to draw from in that area), but the milk supply is closer, and the cost of production is lower than in Las Vegas. It is our belief that a Class I differential of between $2.00 and $2.20 per cwt. is justified in Las Vegas to ensure an adequate supply there.' Option 1a most closely accommodates the producers' need for production incentive.

Classifications of Milk

SMPA supports the proposed four classifications of milk usages.

Regional Issues - Western

Security Milk Producers is working with several other cooperatives and producer trade associations to "fine tune" a petition for USDA to promulgate a California Federal Milk Marketing Order. The petition USDA received from California Dairy Campaign is the basis of the work currently underway, and we would request USDA lend serious weight to the formation of a proposed CA federal order.

Regional Issues - Western / Proposed AZ-LV Order

Producer Milk

The proposed Arizona - Las Vegas order would set the percentage of a handler's pooled milk that may be diverted in any month at 20%. As stated previously, SMPA members produce all of the milk currently produced in Clark County. Our customer in Las Vegas, Anderson Dairy, however, currently receives and processes about half as much milk as is produced on these ranches. Our concern is that diversions set at anything less than 50% would be detrimental to our producers, financially. Currently, diversions under order 131, Central Arizona, are limited to eight days' production during four months of the year, and are unlimited the remainder of the year. We believe this creates an undue burden on the administrators of the order and may, at times, allow for disruptive marketing practices. A limit should be imposed, but not one that detracts from the orderly flow of milk.

Multiple Component Pricing

The proposed rule does not provide for multiple component pricing in the AZ-LV order. The Class I utilization for the proposed order is expected to be less than 50 percent. This 50 percent level seems to be the norm for MCP in some other proposed orders. SMPA recognizes that without UDA's manufacturing plant in the pool, Class I utilization would be near or above 80 percent and knows that MCP has not been specifically requested for this proposed order, but SMPA believes that a butterfat / protein component pricing system, like the system currently in place in the Great Basin Order 139, is in the best interest of the producer. SMPA strongly requests this system of pricing milk be incorporated into this order.

Compensatory Payments

Packaged milk from California partially regulated distributing plants regularly delivers into the proposed order. The pool obligation of a partially regulated distributing plant in the proposed order would mimic that which exists in FO 131. At the public hearings held when the Great Basin and Lake Mead Marketing Areas were combined into the existing Great Basin Order 139, it was determined that 'California partially regulated distributing plants (or any plant regulated under a State order that provides for market wide pooling of producer returns) shall incur no obligation, except for an administrative charge on the volume of fluid milk products disposed of in the marketing area, if the operator's payment to the state for subsequent distribution to dairy farmers and the operator's payment to the producer settlement fund of any order are not less than the pool obligation that such operator would have incurred if such plant had been fully regulated under the order. In the absence of market wide pooling and the allocation of returns to producers on the basis of quota milk and base milk, the payment that the California plant would have made to the state Milk Stabilization Board would have been received by the dairy farmers supplying the plant. Thus, the plants' payments to the State Milk Stabilization Board can be used in lieu of the payments received by the dairy farmers supplying the plant. Under such circumstances, this arrangement, which in essence is a modification of the Wichita Option, represents a reasonable alternative method for computing a partially regulated distributing plant's obligation to the pool.' This excerpt is taken from page 20, pages 16 through 23 are attached, of the final decision originally putting this option in the old Lake Mead order. (also see pages numbered 60 through 64 of the final decision for the Great Basin order and pages 27396 through 27398 from the Federal Register / Vol.52, No. 39 / Tuesday, July 21, 1987 / Proposed Rules.) Essentially, no payment should be required unless payments made to producers in the originating order are less than that in the order of route disposition. The object being equivalent Class I costs between California distributing plants and handlers fully regulated under the proposed AZ-LV order.

Dairy Farmer for other Markets

SMPA supports the definition of a 'dairy farmer for other markets' in the proposed order. We agree that this language is needed to prevent the pooling of surplus milk production from farms whose milk is regularly used for fluid disposition in other markets.

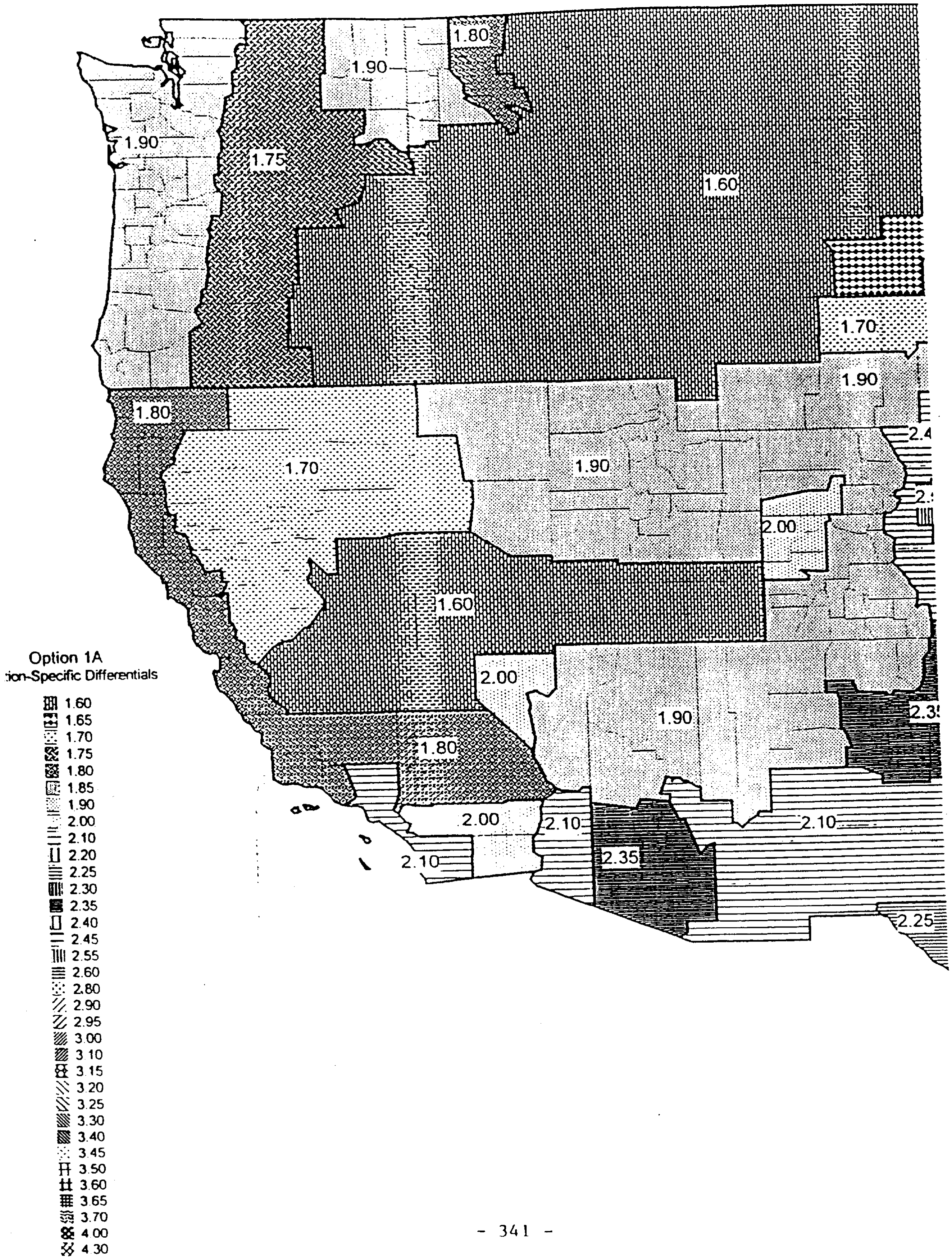
In summary, we wish to extend our gratitude to USDA for the open manner in which the Reform process is being addressed. It is comforting to know that these regulations are being drafted with all sectors of the industry having the ability to comment on their particular concerns in this manner.

Mr. McKee, I appreciate the opportunity to comment on these very important issues to you and your staff. If further clarification can be offered regarding any of the issues addressed in this letter, please call me at (909) 947-8782 extension 223.

Respectfully,

Kevin W. McLaughlin
Fluid Operations

Attachments


1.80
1.90
1.90
1.75
1.60
1.70
1.90
1.80
1.70
1.90
2.4
2.00
1.60
2.00
1.90
2.35
1.80
2.00
2.10
2.10
2.35
2.10
2.25
Option 1A
ion-Specific Differentials
1.60
1.65
1.70
1.75
1.80
1.85
1.90
2.00
2.10
2.20
2.25
2.30
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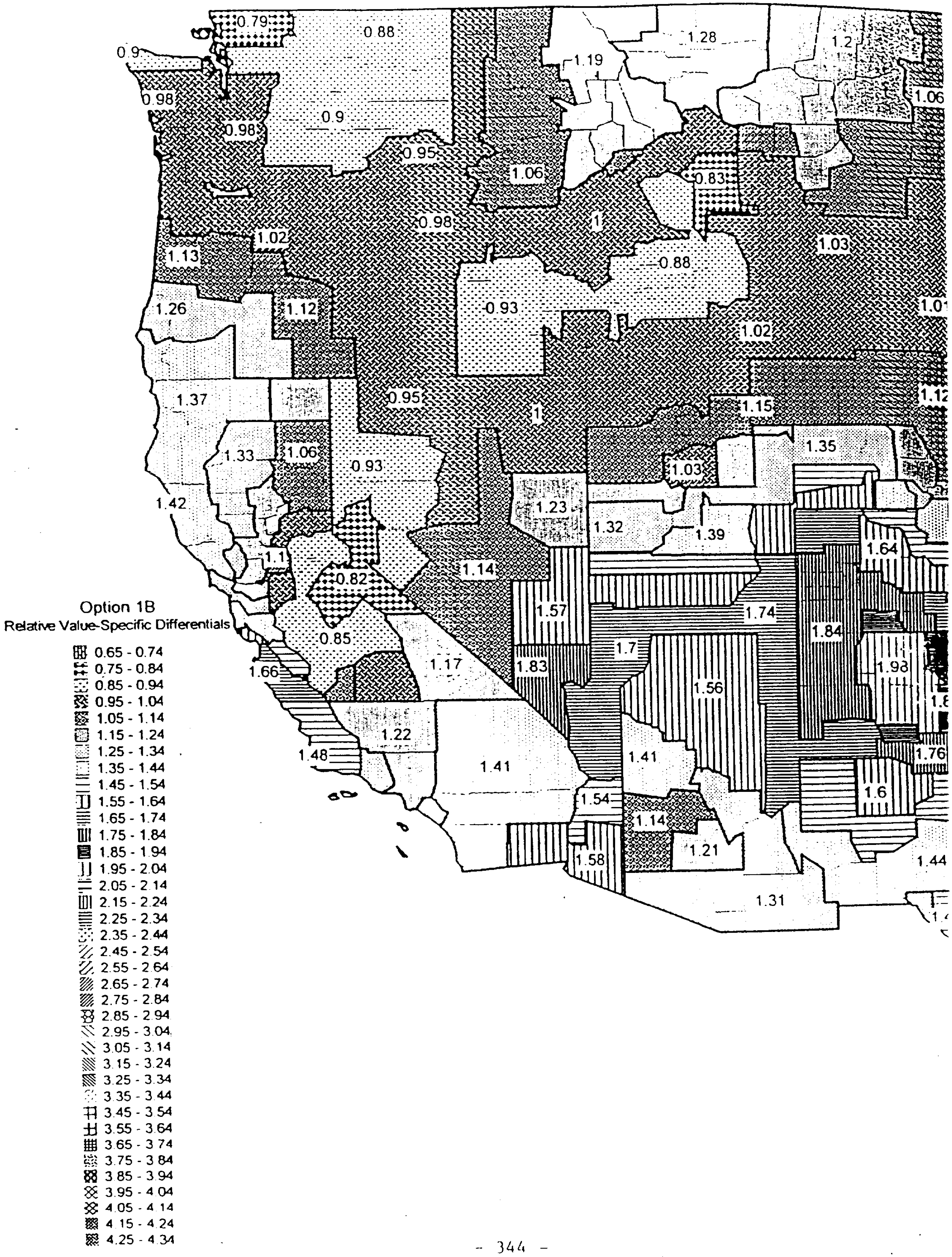

Option 1B

Relative Value-Specific Differentials

0.65 - 0.74
0.75 - 0.84
0.85 - 0.94
0.95 - 1.04
1.05 - 1.14
1.15 - 1.24
1.25 - 1.34
1.35 - 1.44
1.45 - 1.54
1.55 - 1.64
1.65 - 1.74
1.75 - 1.84
1.85 - 1.94
1.95 - 2.04
2.05 - 2.14
2.15 - 2.24
2.25 - 2.34
2.35 - 2.44
2.45 - 2.54
2.55 - 2.64
2.65 - 2.74
2.75 - 2.84
2.85 - 2.94
2.95 - 3.04
3.05 - 3.14
3.15 - 3.24
3.25 - 3.34
3.35 - 3.44
3.45 - 3.54
3.55 - 3.64
3.65 - 3.74
3.75 - 3.84
3.85 - 3.94
3.95 - 4.04
4.05 - 4.14
4.15 - 4.24
4.25 - 4.34
0.79
0.88
1.28
1.2
0.9
1.19
0.98
1.06
0.98
0.9
0.95
1.06
0.83
0.98
1
1.03
1.02
1.13
0.88
1.26
1.12
0.93
1.01
1.02
1.37
0.95
1
1.15
1.12
1.35
1.33
1.06
0.93
1.03
1.42
1.23
1.32
1.39
1.64
1.1
0.82
1.14
1.57
1.74
1.84
0.85
1.7
1.66
1.17
1.83
1.98
1.56
1.8
1.22
1.48
1.41
1.41
1.76
1.54
1.6
1.14
1.58
1.21
1.44
1.31

adopted herein will h e no effect on the operat: ı of the pool plants regulated by the Lake Mead order because the plants are not processing any of the products affected by the proposed reclassification changes. In addition, there was no opposition expressed to the adoption of the uniform classification provisions.

6. Pool obligation of a partially regulated distributing plant. The operator of a partially regulated distributing plant that is also regulated under a State order that provides for marketwide pooling of producer returns should be afforded an additional option in settlement of the plant's obligation to the producer-settlement fund. Under the added option adopted herein, a plant operator could settle his plant's obligation by paying the amount that the Class I price under the Federal order exceeds the applicable State order prices on fluid milk sales that such plant makes in the Lake Mead marketing area.

Under the present provisions of the Lake Mead order, a partially regulated distributing plant operator has three options that he may use in settlement of his pool obligations:

(a) The plant operator incurs no payment obligation if the operator purchases from any Federal milk order source an amount of milk classified and priced as Class I milk that is equivalent to such operator's fluid milk sales in the marketing area. Such purchases, however, may not be used to offset any obligation under another Federal order.

(b) The plant operator incurs no obligation under the order, except for an administrative assessment charge on the volume of fluid milk products disposed of in the marketing area, if the operator's payments to dairy farmers and to the producer-settlement fund of any Federal order are not less than the pool obligation that such operator would have incurred if such plant had been fully regulated under the order. Under this option, which is commonly referred to as the "Wichita" option, a plant operator whose payments for milk are less than the order's obligations may pay the difference either to his own dairy farmers or to the producer-settlement fund.

(c) The plant operator may choose to pay to the producer-settlement fund the difference between the Class I price and the producer blend price of the order (both prices adjusted for the location of the plant) on all fluid milk products distributed in the marketing area (less any purchases of milk classified and priced as Class I milk under any Federal order).

Lake Mead Cooperative Association proposed initially that California handlers distributing milk in the Lake Mead marketing area be provided an additional option for computing their obligations to the Lake Mead producer-settlement fund. Under such option, their obligations would be computed on the basis of the difference between the California State price and Lake Mead Federal order Class I price on fluid milk products that the California plants distribute in the Lake Mead marketing area. At the hearing the cooperative modified its initial proposal. Under its revised proposal, California-regulated handlers would be required to use the option proposed by the cooperative in accounting to the marketwide pool for milk distributed within the marketing area. However, handlers unregulated under any State or Federal order who distribute fluid milk within the Lake Mead marketing area would continue to be subject to the payment options presently in effect.

Proponent cooperative testified that more than one-quarter of the Class I route sales within tha Lake Mead marketing area are by handlers located in California Proponent noted that, although the total volume of milk involved represents a significant segment of the Lake Mead market, it does not represent a large enough percentage of each California handler's total route disposition to result in their being pooled under the Lake Mead order.

Witnesses testified that the California handlers are regulated under the California State Pooling Plan. They are required to pay for the milk they use, according to the class in which it is used, primarily on the basis of the butterfat and solids-not-fat contained in the milk. The value of all the milk received by each California handler is pooled on a marketwide basis and then redistributed to producers on the basis of the individual producer's production quota and base. Two witnesses made the point that, as a consequence, the payments received by dairy farmers supplying the individual plant have no direct relationship to the uses made of their milk by the handler receiving it, or to the amount paid into the pool by the receiving handler.

Proponents indicated that their primary interest in modifying the payment provisions for partially regulated distributing plants is to assure that the California handlers, who supply a substantial portion of the Lake Mead market, make payment for the milk they use at a rate equivalent to that paid by handlers fully regulated under the Lake Mead Federal milk order. In this regard, a witness for proponent cooperative testified that regulated handlers under a Federal order pay a price for milk used in fluid milk products that includes a Class I differential. He explained that the price differential for Class I use is a necessary incentive for dairy farmers to make available to the fluid market an adequate supply of high-quality milk. The witness stated that if the higher price paid for milk used in Class I is to serve its function of providing the additional income needed to induce an adequate milk supply, it must be insulated effectively from unfair competition. According to the witness, such insulation can be provided only by establishing compensatory payment provisions for the use of alternative lower-cost milk supplies in fluid milk products distributed in the marketing area. Such provisions, he testified, should require any fluid milk products distributed in the market by partially regulated distributing plants to meet the full price or cost requirements established under the order for milk used in fluid products by fully regulated plants.

In the case of fully regulated plants, the witness stated, the requirement that handlers operating such plants account fully for all milk and dairy products received serves to protect the fluid market from receipts of surplus milk for fluid use priced below the order's Class I price. However, he testified, full regulation of all handlers distributing fluid milk in the marketing area would not be a practicable solution to the problem of milk distributed in the marketing area that is priced below the level established by the order. In his opinion, subjecting plants that have only a minimal association with the market to full regulation may be unfair to those plants in meeting competition within their primary markets. In addition, full regulation of the plant would have the effect of diluting the blend price under the order if the plant has minimal Class I utilization.

Another approach discussed by the witness for dealing with the Class I sales in Federal order marketing areas of handlers not fully regulated is to treat such sales as surplus to the market from which they originate. Under this concept, the handler would be responsible to the pool for a payment on milk distributed within the marketing area at a rate determined by the difference between the Class I and Class III prices of the Federal rder regulating such marke ng area. The Class I-Class III price difference would eliminate the advantage gained by an unregulated plant disposing of its surplus milk in a regulated market. The witness rejected the use of this pricing concept for milk distributed in Lake Mead by California handlers since such milk is classified as a fluid milk use by the State of California and thus is subject to a higher price than the Lake Mead Class III price.

An alternative method of equalizing the cost of milk between regulated and unregulated handlers is to charge unregulated handlers the difference between the Class I price and the uniform price to producers. This alternative is already included in the Lake Mead order as an option that nonpool handlers distributing Class I milk in the marketing area may elect in computing their obligation to the pool. The rationale for this option is that milk obtained by an unregulated handler in the vicinity of the marketing area would be available for purchase at a price approximating prices paid to producers whose milk is part of the pool. The witness pointed out that while this approach seems appealing on the basis of fairness, it lacks any real applicability to the nonpool plants currently distributing milk in the Lake Mead marketing area. For one thing, he stated, an assumption underlying the Class I-blend price difference charge to nonpool handlers is that such handlers carry their own surplus supplies. The witness testified that none of the California handlers distributing milk in the Lake Mead order carry their own reserve supplies. Furthermore, because of the California State milk pricing provisions, milk is not available to California handlers at a price approximating prices paid to producers whose milk is part of the pool.

Proponent witness detailed the origins and purpose of the "Wichita" option for determining the pool obligation of a partially regulated distributing plant. Under this option, the amounts paid to producers for milk received by a nonpool distributing plant are compared to the amount which would be due the marketwide pool for such milk if the plant were a pool plant. Any amount by which the pool value exceeds the value paid to producers is due the marketwide pool to equalize the competitive positions of pool and nonpool distributing plants. According to the witness, the "Wichita"-type option contained in the Lake Mead order is not a satisfactory method of dealing with milk sold in the Lake Mead marketing area by handlers regulated under the California order. He stated that dissimilarities in the pricing and classification rules and producer payment provisions between the Federal and State orders make it impossible for the market administrator to determine precisely the amounts paid to dairy farmers who supply the raw milk for processing by California handlers distributing milk in the Lake Mead area.

The witness expressed the opinion that equity between California handlers and Lake Mead handlers would be assured if the California handlers distributing fluid milk in the Lake Mead marketing area are required to pay to the Lake Mead pool for such sales at a rate equal to the amount by which the Lake Mead Class I price, adjusted for location of the California plant, exceeds the prices effective for such products under the California order. According to the witness, the options under which California handlers currently may choose to have their obligations to the Lake Mead pool calculated would not be needed for California plants if the proposed compensatory payment method were adopted. He indicated, however, that such other options should be retained in the order in case they are needed at some future time to deal with an unregulated plant other than a California plant that might begin to distribute milk in the Lake Mead market.

A brief was filed on behalf of 3 California plants, Knudsen Corporation, Safeway Stores and Lucky Stores, in opposition to the proposal by LMCA to require California plants to pay the difference between the California price and Lake Mead Class I price on route disposition within the Lake Mead marketing area in lieu of the current payment options provided under the order. The California plant operators stated that they were not given notice prior to the hearing that the cooperative intended to propose that the order be amended to deny California plants the use of the Wichita option and require that such plants must pay to the producer-settlement fund the difference between the California class prices and the Lake Mead Class I price, adjusted for the location of the California plant, on route disposition in the Lake Mead marketing area.

In their brief, the 3 California plant operators indicated they did not prepare testimony for presentation at the hearing and did not retain any experts to examine any of proponent's witnesses since: "(1) the Wichita plan was expressly preserved in the Cooperative's proposal, as set forth in the hearing notice, (2) the Department had advised the plant operators that the hearing would proceed on the basis of proposal's preserving the Wichita option and (3) no proposal was noticed for hearing such as that advanced at the hearing."

Opponents objected primarily to the modified proposal on the basis that affected persons were unaware of the scope of the hearing by virtue of the notice that was issued. Furthermore, they contended that any proponent of a proposal that is modified while the hearing is underway has an advantage over an opponent. They noted that a proponent can prepare testimony and exhibits in support of the modified proposal while opponent will be unprepared to respond and perhaps even be absent when proposals affecting their interests are considered.

On the surface, it appears that the Department and opponents of the payment plan may have been misled regarding changes that the cooperative intended to make in the payment plan for partially regulated distributing plants. Initially, the cooperative asked the Department to call a hearing on a proposal that would require a California partially regulated distributing plant to pay to the producer-settlement fund for each hundredweight of Class I sales in the Lake Mead marketing area a payment equal to the amount by which the Lake Mead Class I price exceeds the Class I price established by the California Bureau of Milk Stabilization. A second proposal that would have also affected the payment obligations of partially regulated distributing plants would have eliminated location adjustments at plants located more than 200 miles from Las Vegas. Both proposals were withdrawn by the cooperative before a hearing notice was issued and amended proposals were submitted in their place. After the Department received the revised proposals and published them in a hearing notice, it wrote to the counsel for the three California plants in response to an inquiry and indicated...

"The proposals noticed for hearing would retain the so-called 'Wichita' option for partially regulated distributing plants that provide the market administrator with information sufficient to compute and verify the plant's classified use value of milk at the Lake Mead order prices and its payment to producers. Plants subject to state regulation that do not elect the 'Wichita' option would be required to make a compensatory payment equal to the amount that the Lake Mead Class I price exceeds the appropriate class price under such state's regulation."

The Department agrees with the contention of the opponents that the payment arrangement for California partially regulated distributing plants that was proposed by the cooperative at the hearing is a substantial modification of the proposal initially noticed for hearing. However, in view of the conclusions reached herein relative to how the order should be changed, the alleged inadequacy of the hearing notice becomes a moot issue.

The cooperative's contention that the Wichita option should not be available to California plants due to shortcomings of this payment arrangement is not a valid reason for deleting the option. The shortcomings of the Wichita option with respect to California plants can be overcome by modifying this option rather than deleting it. Accordingly, the payment options presently provided in the order for partially regulated distributing plants should be retained.

It is appropriate, however, to modify the Wichita option to overcome the shortcomings of that option pointed out by proponent cooperative. As previously noted, the Wichita option provides that a plant operator incurs no obligation, except for an administrative assessment charge on the volume of fluid milk products disposed of in the marketing area, if the operator's payments to dairy farmers and to the producer-settlement fund of any Federal order are not less than the pool obligation that such operator would have incurred if such plant had been fully regulated under the order. The shortcoming of the Wichita option, as noted by proponent cooperative, with respect to California plants is that the payments received by dairy farmers are not directly related to the payments made by the plant operator. The reason for this is due to California regulations which provide for the marketwide pooling of producer returns and the use of base milk and quota milk plans. As a consequence, the returns received by dairy farmers shipping to a given plant bear no direct relationship to the plant's obligation on milk received from such producers.

The shortcomings can be overcome by providing that a California partially regulated distributing plant (or any plant regulated under a State order that provides for marketwide pooling of producer returns) shall incur no obligation, except for an administrative charge on the volume of fluid milk products disposed of in the marketing area, if the operator's payment to the State for subsequent distribution to dairy farmers and the operator's payment to the producer settlement fund of any order are not less than the pool obligation that such operator would have incurred if such plant had been fully regulated under the order. In the absence of marketwide pooling and the allocation of returns to producers on the basis of quota milk and base milk, the payment that the California plant would have made to the State Milk Stabilization Board would have been received by the dairy farmers supplying the plant. Thus, the plant's payments to the State Milk Stabilization Board can be used in lieu of the payments received by the dairy farmers supplying the plant. Under such circumstances, this arrangement, which in essence is a modification of the Wichita option, represents a reasonable alternative method for computing a partially regulated distributing plant's obligation to the pool.

As an alternative to the current payment options available to a partially regulated distributing plant, California plants should be given the further option of paying the amount that the Lake Mead Class I price exceeds the California class prices, all adjusted for the location of the California plant, on route disposition within the marketing area plus an administrative assessment on such sales. Such payment rate should result in equivalent Class I costs between California distributing plants and handlers fully regulated under the Lake Mead order on Class I sales in the Lake Mead marketing area. Currently, such re represents a less costly alternative than the option of paying to the producer-settlement fund the difference between the Class I and uniform prices under the Lake Mead order on route disposition in the Lake Mead marketing area. Furthermore, adoption of the additional payment option will not have an adverse impact upon California plants because such payment method would be utilized only if such payment plan represents the least costly alternative.

LMCA submitted vigorous exceptions to the Department's conclusion that the payment arrangements for California partially regulated distributing plants that were proposed by LMCA at the hearing represented a substantial modification of the proposal noticed for hearing. The argument raised by exceptor that such changes represented appropriate modifications of the proposal were considered in arriving at the initial conclusion. Accordingly, no basis exists for modifying the Department's conclusion in that regard.

LMCA excepted principally to the Department's conclusion that the Wichita option should be retained in the order for use by California partially regulated distributing plants. The cooperative's objection to the continued use of the option dealt in large part with the administrative feasibility of the option. In further support of its contention that the Wichita option should not be available to partially regulated distributing plants in California, LMCA argued that "the assessment rate applicable to the California partially regulated handler pursuant to § 1139.85 simply precludes the Market Administrator from computing, auditing and verifying the monthly pool obligation that the California partially regulated plant would have incurred if such plant had been fully regulated under the Lake Mead order."

The Department recognized in the recommended decision that there are administrative problems in applying the Wichita option to California plants. For this reason, the Wichita option was modified to alleviate the prinicipal administrative problems encountered in the determination of the credit to be accorded a California plant in payment of its obligation for milk received from dairy farmers.

LMCA's argument that California plants should not be able to elect the Wichita option because of the cost of conducting audits of their full operations is not persuasive in view of their contention that the Wichita option should be available to partially regulated distributing plants that are not under State regulations. Presumably, the non-California plants that elected to use the Wichita option would have to be audited to the same extent as the California plant operators who elected the Wichita option.

It is the Department's position that the Wichita option should be uniformly available to any partially regulated distributing plant. Under such option, a partially regulated distributing plant's obligation for its milk supply is computed as though it were a fully regulated handler. As a consequence of such pricing, the partially regulated distributing plant's cost for fluid milk sold in a Federally regulated marketing area is equivalent to the costs incurred by a fully regulated handler on a similar volume of sales in such marketing area. Thus, it is not apparent from this record that a California partially regulated distributing plant that elects to use the Wichita option would have a competitive advantage over a fully regulated plant under the Lake Mead order. Under these circumstances, it is concluded that the Wichita option should be available for California handlers who elect such option as well as other handlers who elect to use such payment plan.

In retrospect, there appears to be little reason for a California partially regulated distributing plant to elect the option of having its payment obligation computed as though the plant were a fully regulated plant under the Lake Mead order. In support of that position it is noted that if the California plant is entirely a Class I operation and the California Class I price is at such a level that the plant is required under the Wichita option to make a compensatory payment to the producer-settlement fund of the Lake Mead order or to its dairy farmers at the difference between the Lake Mead Class I price adjusted for the California plant's location and the California class prices, the operator that elected the Wichita option would have to make such payment on 100 percent of his fluid milk products. In contrast, if the plant operator elected the payment proposed by exceptor, the operator could elect to make the payment rate previously detailed on only his fluid milk sales in the Lake Mead marketing area. In view of the pooling requirements under the order, such fluid milk sales would represent less than 10 percent of the plant's total fluid milk sales. In addition, the California plant that elects not to use the Wichita option would be spared the expense involved in submitting a full report of its receipts and utilization.

LMCA excepted to the Department's conclusion that California plants should not be denied the use of the option in § 1139.76(a) which permits a partially regulated distributing plant to pay to the producer-settlement fund of the Lake Mead order the difference between the Lake Mead Class I price and the blend price (both prices adjusted for the location of the plant) on fluid milk products distributed in the Lake Mead marketing area. While the cooperative contended that the use of such provision was appropriate for a plant that was not subject to State regulation, the cooperative claimed that the provision was not appropriate for California plants because they do not carry their own reserve supplies. Instead, the cooperative pointed out that such plants pay for milk on the basis of the individual plant's utilization while reserve supplies for such plants are borne by producers throughout California as the result of California's marketwide pooling of producer returns.

The Department concedes that such option should be available for use by California handlers in very limited circumstances. Such option should be available for use by California handlers only if such payment obligation results in a lesser payment obligation than the plant would incur under exceptor's proposal, i.e., the Lake Mead Class I price adjusted for the location of the plant minus the California class prices on fluid milk products distributed in the Lake Mead marketing area. Such limitation on the use of the option will meet one of the objections raised by the cooperative at the hearing to the use of such option by California handlers. In that regard, the cooperative pointed out that a compensatory payment by a California handler at the difference between the Lake Mead Class I price and the blend price in addition to the Class I price assessed under the California regulations could result in the California handler paying a higher price for milk sold in the Lake Mead marketing area than the cost for Class I milk sold in such marketing area by a fully regulated handler under the Lake Mead order. In further support of its position, the cooperative noted that a compensatory payment rate that results in a higher cost for raw fluid milk than the costs incurred by a fully regulated handler was declared invalid by the Supreme Court in its decision in the Lehigh Valley case.

The point raised by exceptor is valid and should have been discussed in detail in the Department's findings and conclusions set forth in the recommended decision. California handlers should not be assessed a higher cost than fully regulated handlers under the Lake Mead order on fluid milk distributed in the Lake Mead marketing area. Accordingly, the order should provide that the only time such option (Lake Mead Class I price less the blend price, both adjusted for plant location) should apply is when such payment rate results in a lesser payment than the difference between the Lake Mead Class I price adjusted for the plant's location minus the California Class I price on fluid milk products distributed in the Lake Mead marketing area.

RULINGS ON PROPOSED FINDINGS AND CONCLUSIONS

Briefs and proposed findings and conclusions were filed on behalf of certain interested parties. These briefs, proposed findings and conclusions and the evidence in the record were considered in making the findings and conclusions set forth above. To the extent that the suggested findings and conclusions filed by interested parties are inconsistent with the findings and conclusions set forth herein, the requests to make such findings or reach such conclusion are denied for the reason previously stated in this decision.

GENERAL FINDINGS

The findings and determinations hereinafter set forth supplement those that were made when the Lake Mead order was first issued and when it was amended. The previous findings and determinations are hereby ratified and confirmed, excpet where they may conflict with those set forth herein.

(a) The tentative marketing agreement and the order, as hereby proposed to be amended, and all of the terms and conditions thereof, will tend to effectuate the declared policy of the Act;

(b) The parity prices of milk as determined pursuant to section 2 of the Act are not reasonable in view of the price of feeds, available supplies of feeds, and other economic conditions which affect market supply and demand for milk in the marketing area, and the minimum prices specified in the tentative marketing agreement and the order, as hereby proposed to be amended, are such prices as will reflect the aforesaid factors, insure a sufficient quantity of pure and wholesome milk, and be in the public interest; and

(c) The tentative marketing agreement and the order, as hereby proposed to be amended, will regulate the handling of milk in the same manner as, and will be applicable only to persons in the respective classes of industrial and commercial activity specified in, a marketing agreement upon which a hearing has been held.

RULINGS ON EXCEPTIONS

In arriving at the findings and conclusions, and the regulatory provisions of this decision, each of the exceptions received was carefully and fully considered in conjunction with the record evidence. To the extent that the findings and conclusions and the regulatory provisions of this decision are at variance with any of the exceptions, such exceptions are hereby overruled for the reasons previously stated in this decision.

MARKETING AGREEMENT AND ORDER

Amended hereto and made a part hereof are two documents, a Marketing Agreement regulating the handling of milk, and an Order amending the

DEPARTMENT OF AGRICULTURE
Agricultural Marketing Service

7 CFR Parts 1136 and 1139

[Docket Nos. AO-309-A27 and AO-374-A11]

Milk in the Great Basin and Lake Mead Marketing Areas; Decision on Proposed Amendments to Marketing Agreements and to Orders

AGENCY: Agricultural Marketing Service, USDA.

ACTION: Proposed rule.

SUMMARY: This decision merges the Great Basin and Lake Mead Federal milk orders, based on industry proposals considered at a public hearing held March 18-20, 1986, in Salt Lake City, Utah. In addition to the presently regulated marketing areas, the merged "Great Basin" marketing area would include the presently unregulated portion of the State of Utah, two counties in Wyoming, and additional counties in Idaho. The provisions of the merged order are generally patterned after those of the two separate orders, and the present Class I price differentials at Salt Lake City and Las Vegas are maintained.

One feature of the merged order not now contained in either order includes, in the pool plant definition, a manufacturing plant located within the marketing area and operated by a cooperative association. The obligation of a partially regulated distributing plant operator regulated by a State order would be determined by the value of the fluid milk products distributed in the Federal order marketing area at the difference between the Class I price paid by the handler regulated under the State order and the applicable Federal order Class I price.

For the first time in the Federal milk order system, the merged order includes a plan for pricing milk on the basis of its protein, as well as butterfat, components. The differential value of milk used in Class I and Class II would be pooled to determine producers' shares of the higher-valued uses, and the value of protein used in Classes II and III would be pooled with the value of skim milk used in Class I to determine the value of protein in producer milk.

The merger is needed to reflect changes in market structure in that the two separately regulated areas have become, in effect, one common market. Cooperative associations will be polled to determine whether producers favor the issuance of the merged order.

FOR FURTHER INFORMATION CONTACT: Constance M. Brenner, Marketing Specialist, USDA/AMS/Dairy Division, Order Formulation Branch, Room 2968, South Building, P.O. Box 96456, Washington, DC 20090-6456, (202) 447-7183.

SUPPLEMENTARY INFORMATION: This administrative action is governed by the provisions of Sections 556 and 557 of Title 5 of the United States Code and, therefore, is excluded from the requirements of Executive Order 12291.

The Regulatory Flexibility Act (5 U.S.C. 601-612) requires the Agency to examine the impact of a proposed rule on small entities. Pursuant to 5 U.S.C. 605(b), the Administrator of the Agricultural amount due for such milk. He argued that the proposed partial payment rate constitutes an overpayment for milk delivered during the first 15 days of the month, and should be reduced to the level of the previous month's Class III price.

A witness for IMPA testified that by the time producers are paid for milk delivered during the first 15 days of the month, they have already delivered 29 days' milk production without receiving any payment at all for the milk delivered. He characterized the present payment schedule as requiring a substantial extension of credit and credit risk which dairy farmers can ill afford. The witness stated that the partial payment provides cash to producers, enabling them to pay their bills and reducing the amount of credit they otherwise would be required to extend to handlers. He testified that farmers today are in a tight cash position, and should not be faced with reduced payments for the milk they have delivered. The witness admitted that a dairy farmer who ceased milk deliveries during the second half of the month could be overpaid for his total production if the partial payment for his first 15 days' milk deliveries is determined by the rate proposed by merger proponents. Proponent witness stated that he would not be opposed to allowing authorized deductions to be made from partial payments to producers.

The partial payment rate under the order applies only to milk delivered by producers during the first 15 days of the month. It seems clear that payments made for deliveries of milk during the period should not exceed the greatest possible pool value that might accrue to such deliveries. On the other hand, producers under the order usually have delivered nearly an entire month's production before receiving any payment for any of it. This problem could be addressed by requiring partial payments to producers to be made earlier, or by requiring partial payments to be made twice during the month rather than once. In any case, neither of those alternatives was proposed or discussed in any testimony. Accordingly, the partial payment rate determined by multiplying the previous month's Class III price by 1.2 should be adopted, but should never be allowed to exceed the level of the current month's Class I price.

Partial payments at the rate adopted should not be required in the case of producers who ship milk for only a small part of the second half of the month. Given the present relationship of the uniform price and the partial payment rate, such producers would very likely be paid more for their first 15 days' delivery of milk than their entire production for the month is worth. For this reason, partial payments would be required to be made only to producers who continue to ship milk through the 17th day of the month. In addition, overpayments to producers on a partial payment basis can be avoided more easily if deductions deemed proper by the market administrator and authorized by producers are allowed to be made from producers' partial payments. Such a provision would help to assure that producer payments are more evenly spaced throughout the month, and that the deductions to be made from a producer's final payment would not exceed the total amount due to the producer for his milk production during the second half of the month.

11. Obligations of partially regulated distributing plant operators. Two options for computing the obligation to the pool of the operator of a partially regulated distributing plant that is also regulated under a State order that provides for marketwide pooling of producer returns should be eliminated. Under the provisions adopted herein, such a handler may settle his obligation only by paying the amount that the Federal order Class I value of the fluid milk products

that such plant distributes in the merged Great Basin marketing area (less Class I receipts from pool sources) exceeds the value of the milk at the applicable State order prices. Partially regulated distributing plant operators who are not regulated under a State order that provides for marketwide pooling would continue to have the same options under which their obligations to the pool are currently computed.

Under the present provisions of the Lake Mead order, every partially regulated distributing plant operator has three options that may be used in settlement of its pool obligations:

(a) The plant operator incurs no payment obligation if the operator purchases from any Federal milk order source an amount of milk classified and priced as Class I milk that is equivalent to such operator's fluid milk sales in the marketing area. Such purchases, however, may not be used to offset any obligation under another Federal order.

(b) The plant operator incurs no obligation under the order, except for an administrative assessment charge on the volume of fluid milk products disposed of in the marketing area, if the operator's payments to dairy farmers and to the producer-settlement fund of any Federal order are not less than the pool obligation that such operator would have incurred if such plant had been fully regulated under the order. Under this option, which is commonly referred to as the "Wichita" option, a plant operator whose payments for milk are less than the order's obligations may pay the difference either to its own dairy farmers or to the producer-settlement fund.

(c) The plant operator may choose to pay to the producer-settlement fund the difference between the Class I price and the producer blend price of the order [both prices adjusted for the location of the plant] on all fluid milk products distributed in the marketing area [less any purchases of milk classified and priced as Class I milk under under any Federal order].

In addition, a partially regulated distributing plant operator regulated under a State order has a fourth option under which his pool obligation may be determined:

(d) The plant operator may choose to pay to the producer-settlement fund the difference between the Class I price applicable at the location of the plant and the applicable price for the fluid milk products distributed in the marketing area as determined under the State program.

The present Great Basin order contains only options (a), (b) and (c) for determining obligations of partially regulated distributing plants. Those options will be sufficient for determining the pool obligations of such plants not regulated under a State order. For determining the obligations of such plants that are State-regulated, options (a) and (d) will be sufficient.

An IMPA witness testified that some of the options currently available to determine the pool obligations of all partially regulated distributing plant operators are inappropriate for determining the obligations of such handlers that are regulated under a State order providing for marketwide pooling. According to the witness, approximately 20 percent of the fluid milk distributed within the current Lake Mead marketing area is distributed from plants located in southern

California. He stated that these handlers are regulated under the California State Pooling Plan. Under the State Plan, he said, regulated handlers are required to pay for the milk they use, according to the class in which it is used, primarily on the basis of the butterfat and solids-not-fat contained in the milk. The value of all the milk received by each California handler is pooled on a marketwide basis and then redistributed to producers on the basis of the individual producer's production quota and base. As a consequence, the payments received by dairy farmers supplying individual plants have no direct relationship to the uses made of their milk by the handlers receiving it, or to the amounts paid into the pool by the receiving handlers.

The witness stated that the payment option currently available only to California State-regulated handlers, which prices sales in the Marketing area at the difference between the State order and Federal order prices, is a precise method of determining the exact cost difference of the products. According to the witness, the other payment options available to partially regulated distributing plant operators have no validity in comparing the cost of the products under the State and Federal orders. The witness' position was that the costs attributed to the handler in payment options (b) and (c) above do not accurately represent the actual cost of the milk used by a California-regulated handler in the fluid products distributed within the Federal marketing area. He explained that under California regulation, the price paid by handlers for milk used in fluid products is publicly announced and strictly enforced. He stated further that the milk pooling plan operated by the State of California differs so greatly from the provisions of the Federal order that the values which must be computed under options (b) and (c) above are extremely difficult to determine for California-regulated handlers. Therefore, he concluded, only the present payment option that takes into account the actual prices paid by California handlers for milk used in fluid products should be used to determine the payment obligations of such handlers. Although California handlers would be the only ones affected by the proposed provision under present marketing conditions, the witness stated that the payment provision would apply to any partially regulated distributing plant operators regulated under any State order that provides for marketwide pooling.

The representative of Safeway Stores, Inc., a company operating multiple distributing plants, one of which is a large distributing plant in southern California with fluid milk sales in the Lake Mead marketing area, testified that the company would prefer to retain in the order all of the payment options currently available to the operator of a partially regulated distributing plant. The witness also proposed changing the language of the provisions governing the obligation of a partially regulated distributing plant operator regulated by a State order. The proposed modification would determine such an obligation on the basis of the difference in value of the fluid milk products distributed in the marketing area under the State and Federal order prices, rather than multiplying the pounds of such disposition by the difference between the applicable prices. The post-hearing brief filed on behalf of the handler expressed the opinion that the importance of retaining the present payment options of a partially regulated distributing plant operator is not as great as the handler considered it to be at the hearing.

The proponents' position with regard to partially regulated distributing plant obligations was supported by a witness representing a

Great Basin pool distributing plant that had not yet begun operating at the time of the hearing. The witness supported the proposal in the interest of assuring that all handlers distributing fluid milk products in the marketing area have uniform costs for milk that is used in similar products.

Federal milk orders contain provisions that establish payment obligations of handlers who distribute fluid milk products within the marketing area, but not to an extent great enough to meet pooling standards. These obligations are imposed for the purpose of assuring that all handlers who distribute significant amounts of fluid milk products in the marketing area are subject to comparable costs for such milk. Payment obligations that would result in a cost of milk to a partially regulated distributing plant operator greater than that which would be imposed on a regulated handler would amount to a trade barrier. However, there is no indication that computing a partially regulated distributing plant operator's obligation to the pool on the basis of the difference between the values of the handler's milk under the Federal and State milk orders would be considered inequitable or a barrier to trade. Such a handler would be paying no more for milk distributed within the marketing area than the fully regulated handlers with whom the State-regulated handler is competing. At the same time, fully regulated handlers would be assured that the partially regulated handler has not obtained a competitive advantage by virtue of paying less than they are required to pay for milk used in fluid products.

Proponent witness' testimony in the hearing record is contradictory regarding proponents' intention as to whether the obligation of a partially regulated distributing plant operator should be determined on the basis of the difference in price between the Federal and State orders, or the difference in the values of the fluid milk products concerned as determined by the Federal and State orders. Most of the language in the section of the proposed merged order that deals with obligations of partially regulated distributing plant operators is identical to that in the present separate orders.

Proponents' modification of the language of the present Lake Mead order relating to such handlers that are State-regulated seemed to indicate that proponents wanted the State-regulated handlers' actual cost of milk to be the amount compared to the Federal order value in computing the handlers' pool obligation. However, in exceptions to the recommended decision, proponent argued that its testimony had been misunderstood, and explained that its intent had been to compute the obligation of partially regulated distributing plant operators at the difference between the Federal and State order Class I prices. According to proponent, variations in the butterfat and nonfat solids contents of the milk distributed by both Federally-regulated and State-regulated handlers are to be expected and have no bearing on the Class I differentials charged to handlers. Therefore, proponent stated, such variations should not be considered in any determination of the rate of compensatory payment charged to partially regulated plants.

It is recognized that the Class I prices published by the State of California are for informational and comparison purposes, and do not determine exactly what a California-regulated handler actually pays for milk used in fluid products. However, the published prices do reflect what a handler would pay for milk of a standard butterfat and nonfat solids content, as Federal order prices reflect the value of milk at a standard butterfat content. The content of both butterfat and nonfat solids in milk distributed by both State-regulated and Federally-regulated handlers can be expected to vary between handlers. It would not be appropriate for the market administrator to become involved in determining the nonfat solids and butterfat content of milk distributed in the marketing area by State-regulated handlers in order to calculate the obligations of partially regulated distributing plants. Therefore, for the purpose of determining the amount of payment to be made by State-regulated handlers distributing milk within the Federal order marketing area, consideration of the State and Federal announced Class I prices will be sufficient.

The intent of the section of the merged order dealing with the obligations of partially regulated distributing plants not regulated by a State order was to leave such obligations unchanged. { 1139.76(a)(1)(iv), as published in the recommended decision, would change the computation of obligations such a handler would have to the marketwide pool. Therefore, the language of that paragraph has been changed from the recommended decision so that those handler obligations will remain unchanged.

12. Administrative provisions - administrative assessment. The maximum rate of payments by handlers for the cost of administering the merged order should be 4 cents per hundredweight. Such payments are required if the market administrator is to perform the necessary function of administering the merged order. The 4-cent per hundredweight rate is the same as under the two separate orders, and was proposed at the hearing without objection. Continuation of the 4-cent rate should enable the market administrator to administer the merged order effectively. If experience indicates that the merged order can be administered at a lesser rate, the order provides that the Secretary may adjust the rate downward without the necessity of a hearing.

Deduction for marketing services. The maximum rate of deduction from payments to nonmember producers for the cost of providing marketing services such as butterfat and protein testing and market information should be 6 cents per hundredweight. The marketing service deduction is necessary to reimburse the market administrator for providing such services to producers for whom the services are not provided by a cooperative association.

Currently, the maximum rates under the separate orders are 6 cents under the Great Basin order and 7 cents under the Lake Mead order. A 6-cent rate, which was proposed at the hearing without objection, should enable the market administrator to provide adequate testing and information services to nonmember producers. The marketing service deduction rate, like the administrative assessment, may be adjusted downward if the maximum rate is higher than necessary.

Because operation of the merged order would require that all producers' milk be tested for protein content, the market administrator would be authorized to establish, as well as verify, producer tests. Although not proposed, such a provision is necessary because it is apparent from the hearing record that not all of the handlers of producer milk in the merged order area are equipped to test for protein content.

Merger of the administrative expense, marketing service, and producer-settlement funds. To accomplish the merger of the two orders made to a cooperative association in lieu of payments to individual producers, both the partial and final payments should be made prior to the date payments are due to individual producers.

As adopted herein, the payment schedule is the same as now provided in the present Great Basin order. Proponent proposed payment dates similar to those in the present Great Basin order, with some payment dates to cooperative associations and their members moved up by 1 or 2 days. There was no opposition to the proposed payment schedule at the hearing. However, in some cases it may be impossible for handlers to pay cooperative associations the full value of their receipts of the cooperative's member milk before the handler has had an opportunity to receive equalization payments from the producer-settlement fund. Because of the potential difficulties in making payments according to the proposed schedule, and because proponents did not explain the differences between their proposal and the payment dates in the present Great Basin order, the merged order should adopt the payment dates specified in the present Great Basin order.

Proponents included in the proposed merged order the present Great Basin rate of partial payment to producers for their milk deliveries during the first 15 days of the month of 1.2 times the previous month's Class III price. However, the witness representing Safeway Stores, Inc., proposed that the rate of partial payment be reduced to the level of the previous month's Class III price, as it is in most other Federal orders in the region, including the present Lake Mead order. In support of his proposal the witness testified that in 1961, when the higher partial payment rate was adopted, it resulted in prices lower than either the uniform price or the Class I price at the time. He stated that as the Class III price has increased, the partial payment rate has exceeded the uniform price and the Class I price. The witness said that the partial payment price has been as much as $1.68 over the uniform price and $.60 over the Class I price in recent years. He asserted that a partial payment should represent only a portion of the total amount due for the first 15 days' deliveries of milk, and certainly should not exceed the amount due for such milk. He argued that the proposed partial payment rate constitutes an overpayment for milk delivered during the first 15 days of the month, and should be reduced to the level of the previous month's Class III price.

A witness for IMPA testified that by the time producers are paid for milk delivered during the first 15 days of the month, they have already delivered 29 days' milk production without receiving any payment at all for the milk delivered. He characterized the present payment schedule as requiring a substantial extension of credit and credit risk which dairy farmers can ill afford. The witness stated that the partial payment provides cash to producers, enabling them to pay their bills and reducing the amount of credit they otherwise would be required to extend to handlers. He testified that farmers today are in a tight cash position, and should not be faced with reduced payments for the milk they have delivered. The witness admitted that a dairy farmer who ceased milk deliveries during the second half of the month could be overpaid for his total production if the partial payment for his first 15 days' milk deliveries is determined by the rate proposed by merger proponents. Proponent witness stated that he would not be opposed to allowing authorized deductions to be made from partial payments to producers.

The partial payment rate under the order applies only to milk delivered by producers during the first 15 days of the month. It seems clear that payments made for deliveries of milk during the period should not exceed the greatest possible pool value that might accrue to such deliveries. On the other hand, producers under the order usually have delivered nearly an entire month's production before receiving any payment for any of it. This problem could be addressed by requiring partial payments to producers to be made earlier, or by requiring partial payments to be made twice during the month rather than once. In any case, neither of those alternatives was proposed or discussed in any testimony. Accordingly, the partial payment rate determined by multiplying the previous month's Class III price by 1.2 should be adopted, but should never be allowed to exceed the level of the current month's Class I price.

Partial payments at the rate adopted should not be required in the case of producers who ship milk for only a small part of the second half of the month. Given the present relationship of the uniform price and the partial payment rate, such producers would very likely be paid more for their first 15 days' delivery of milk than their entire production for the month is worth. For this reason, partial payments would be required to be made only to producers who continue to ship milk through the 17th day of the month. In addition, overpayments to producers on a partial payment basis can be avoided more easily if deductions deemed proper by the market administrator and authorized by producers are allowed to be made from producers' partial payments. Such a provision would help to assure that producer payments are more evenly spaced throughout the month, and that the deductions to be made from a producer's final payment would not exceed the total amount due to the producer for his milk production during the second half of the month.

11. *Obligations of partially regulated distributing plant operators.* Two options for computing the obligation to the pool of the operator of a partially regulated distributing plant that is also regulated under a State order that provides for marketwide pooling of producer returns should be eliminated. Under the provisions adopted herein, such a handler may settle his obligation only by paying the amount that the Federal order Class I value of the fluid milk products that such plant distributes in the merged Great Basin marketing area (less Class I receipts from pool sources) exceeds the value of the milk at the applicable State order prices. Partially regulated distributing plant operators who are not regulated under a State order that provides for marketwide pooling would continue to have the same options under which their obligations to the pool are currently computed.

Under the present provisions of the Lake Mead order, every partially regulated distributing plant operator has three options that may be used in settlement of its pool obligations:

(a) The plant operator incurs no payment obligation if the operator purchases from any Federal milk order source an amount of milk classified and priced as Class I milk that is equivalent to such operator's fluid milk sales in the marketing area. Such purchases, however, may not be used to offset any obligation under another Federal order.

(b) The plant operator incurs no obligation under the order, except for an administrative assessment charge on the volume of fluid milk products disposed of in the marketing area, if the operator's payments to dairy farmers and to the producer-settlement fund of any Federal order are not less than the pool obligation that such operator would have incurred if such plant had been fully regulated under the order. Under this option, which is commonly referred to as the "Wichita" option, a plant operator whose payments for milk are less than the order's obligations may pay the difference either to its own dairy farmers or to the producer-settlement fund.

(c) The plant operator may choose to pay to the producer-settlement fund the difference between the Class I price and the producer blend price of the order [both prices adjusted for the location of the plant] on all fluid milk products distributed in the marketing area [less any purchases of milk classified and priced as Class I milk under any Federal order].

In addition, a partially regulated distributing plant operator regulated under a State order has a fourth option under which his pool obligation may be determined:

(d) The plant operator may choose to pay to the producer-settlement fund the difference between the Class I price applicable at the location of the plant and the applicable price for the fluid milk products distributed in the marketing area as determined under the State program.

The present Great Basin order contains only options (a), (b) and (c) for determining obligations of partially regulated distributing plants. Those options will be sufficient for determining the pool obligations of such plants not regulated under a State order. For determining the obligations of such plants that are State-regulated, options (a) and (d) will be sufficient.

An IMPA witness testified that some of the options currently available to determine the pool obligations of all partially regulated distributing plant operators are inappropriate for determining the obligations of such handlers that are regulated under a State order providing for marketwide pooling. According to the witness, approximately 20 percent of the fluid milk distributed within the current Lake Mead marketing area is distributed from plants located in southern California. He stated that these handlers are regulated under the California State Pooling Plan. Under the State Plan, he said, regulated handlers are required to pay for the milk they use, according to the class in which it is used, primarily on the basis of the butterfat and solids-not-fat contained in the milk. The value of all the milk received by each California handler is pooled on a marketwide basis and then redistributed to producers on the basis of the individual producer's production quota and base. As a consequence, the payments received by dairy farmers supplying individual plants have no direct relationship to the uses made of their milk by the handlers receiving it, or to the amounts paid into the pool by the receiving handlers.

The witness stated that the payment option currently available only to California State-regulated handlers, which prices sales in the marketing area at the difference between the State order and Federal order prices, is a precise method of determining the exact cost difference of the products. According to the witness, the other payment options available to partially regulated distributing plant operators have no validity in comparing the cost of the products under the State and Federal orders. The witness' position was that the costs attributed to the handler in payment options (b) and (c) above do not accurately represent the actual cost of the milk used by a California-regulated handler in the fluid products distributed within the Federal marketing area. He explained that under California regulation, the price paid by handlers for milk used in fluid products is publicly announced and strictly enforced. He stated further that the milk pooling plan operated by the State of California differs so greatly from the provisions of the Federal order that the values which must be computed under options (b) and (c) above are extremely difficult to determine for California-regulated handlers. Therefore, he concluded, only the present payment option that takes into account the actual prices paid by California handlers for milk used in fluid products should be used to determine the payment obligations of such handlers. Although California handlers would be the only ones affected by the proposed provision under present marketing conditions, the witness stated that the payment provision would apply to any partially regulated distributing plant operators regulated under any State order that provides for marketwide pooling.

The representative of Safeway Stores, Inc., a company operating multiple distributing plants, one of which is a large distributing plant in southern California with fluid milk sales in the Lake Mead marketing area, testified that the company would prefer to retain in the order all of the payment options currently available to the operator of a partially regulated distributing plant. The witness also proposed changing the language of the provisions governing the obligation of a partially regulated distributing plant operator regulated by a State order. The proposed modification would determine such an obligation on the basis of the difference in value of the fluid milk products distributed in the marketing area under the State and Federal order prices, rather than multiplying the pounds of such disposition by the difference between the applicable prices. The post-hearing brief filed on behalf of the handler expressed the opinion that the importance of retaining the present payment options of a partially regulated distributing plant operator is not as great as the handler considered it to be at the hearing.

The proponents' position with regard to partially regulated distributing plant obligations was supported by a witness representing a Great Basin pool distributing plant that had not yet begun operating at the time of the hearing. The witness supported the proposal in the interest of assuring that all handlers distributing fluid milk products in the marketing area have uniform costs for milk that is used in similar products.

Federal milk orders contain provisions that establish payment obligations of handlers who distribute fluid milk products within the marketing area, but not to an extent great enough to meet pooling standards. These obligations are imposed for the purpose of assuring that all handlers who distribute significant amounts of fluid milk products in the marketing area are subject to comparable costs for such milk. Payment obligations that would result in a cost of milk to a partially regulated distributing plant operator greater than that which would be imposed on a regulated handler would amount to a trade barrier. However, there is no indication that computing a partially regulated distributing plant operator's obligation to the pool on the basis of the difference between the values of the handler's milk under the Federal and State milk orders would be considered inequitable or a barrier to trade. Such a handler would be paying no more for milk distributed within the marketing area than the fully regulated handlers with whom the State-regulated handler is competing. At the same time, fully regulated handlers would be assured that the partially regulated handler has not obtained a competitive advantage by virtue of paying less than they are required to pay for milk used in fluid products.

Proponent witness' testimony in the hearing record is contradictory regarding proponents' intention as to whether the obligation of a partially regulated distributing plant operator should be determined on the basis of the difference in price between the Federal and State orders, or the difference in the values of the fluid milk products concerned as determined by the Federal and State orders. Most of the language in the section of the proposed merged order that deals with obligations of partially regulated distributing plant operators is identical to that in the present separate orders. However, proponents have modified the language of the present Lake Mead order relating to such handlers that are State-regulated. The modification changes the determination of such a handler's obligation from the Class I price difference under the Federal and State orders to the difference between the value of the milk used in products disposed of in the marketing area at the Federal order Class I price, adjusted for location, and the amount paid for the milk by the handler under the State program. It seems apparent that if proponents wished to use the same method of determining the obligation of a partially regulated distributing plant operator as is currently in use under the Lake Mead order, their proposed order language would have continued to follow the present language of the Lake Mead order. Therefore, there is reason to conclude that proponent intended the State-regulated handler's actual cost of milk to be the amount compared to the Federal order value in computing the handler's pool obligation.

One of the principal points proponent witness made to justify using only the Federal-State value difference to compute partially regulated handler obligations, rather than allowing such handlers a choice of payment plans, was that the precise cost to the handler of the milk distributed in the marketing area by handlers regulated under a State order is known. Payments owed by California-regulated handlers for milk used in fluid products are determined by the amount of nonfat solids and butterfat contained in the milk, plus an added value for the volume of "fluid carrier" in which those components are contained.

For informational and comparison purposes, the State of California publishes a Class I price. This price, however, is not the basis of determining what any handler actually pays for milk used in fluid products. The published California Class I price is, rather, a reflection of the value of one hundred pounds of fluid milk containing a standard amount of butterfat and nonfat solids. As such, it should not be used to determine what a California-regulated handler has already paid for milk used in fluid products.

The value of milk pooled under the California State order is likely to be affected by the addition of nonfat solids for which the handler must pay. Although proponent witness indicated that proponent does not wish the addition of nonfat solids to be included in the value considered to have been paid by the handler under the State order, such fortification does, indeed, add to the handler's cost of milk. It would be inequitable to exclude the cost of fortification from the value to be credited against the Federal order value of milk distributed in the marketing area by a State-regulated handler. The value to be attributed to nonfat solids added to fluid milk products should be determined by the applicable State-announced prices.

There should be no difficulty in establishing the Federal order value of fluid milk products distributed in the marketing area by a state-regulated handler. The same prices per hundredweight of product pounds and skim milk, adjusted for location, that are used to determine the value of producer milk used in Class I should be used. In addition, the value of butterfat in such products can be determined by multiplying the pounds of butterfat by the butterfat price to be paid producers. If the actual values of the milk under the two pooling systems are compared, any obligation of a partially regulated distributing plant operator to the pool will have been determined equitably. Therefore, the difference in value of the in-area dispositions under the Federal and State pricing systems should be used to compute the pool obligations of partially regulated handlers, rather than the difference between the appropriate Federal and State order prices.

12. *Administrative provisions—administrative assessment.* The maximum rate of payments by handlers for the cost of administering the merged order should be 4 cents per hundredweight. Such payments are required if the market administrator is to perform the necessary function of administering the merged order. The 4-cent per hundredweight rate is the same as under the two separate orders, and was proposed at the hearing without objection. Continuation of the 4-cent rate should enable the market administrator to administer the merged order effectively. If experience indicates that the merged order can be administered at a lesser rate, the order provides that the Secretary may adjust the rate downward without the necessity of a hearing.

Deduction for marketing services. The maximum rate of deduction from payments to nonmember producers for the cost of providing marketing services such as butterfat and protein testing and market information should be 6 cents per hundredweight. The marketing service deduction is necessary to reimburse the market administrator for providing such services to producers for whom the services are not provided by a cooperative association.

Currently, the maximum rates under the separate orders are 6 cents under the Great Basin order and 7 cents under the Lake Mead order. A 6-cent rate, which was proposed at the hearing without objection, should enable the market administrator to provide adequate testing and information services to nonmember producers. The marketing service deduction rate, like the administrative assessment, may be adjusted downward if the maximum rate is higher than necessary.

Because operation of the merged order would require that all producers' milk be tested for protein content, the market administrator would be authorized to establish, as well as verify, producer tests. Although not proposed, such a provision is necessary because it is apparent from the hearing record that not all of the handlers of producer milk in the merged order area are equipped to test for protein content.

Merger of the administrative expense, marketing service, and producer-settlement funds. To accomplish the merger of the two orders effectively and equitably, the reserves in the administrative expense funds that have accumulated under the individual orders should be combined. Similar procedures should be followed with respect to the marketing service and producer-settlement fund reserves of the individual orders. Any liabilities of such funds under the individual orders should be paid from the appropriate new funds established under the merged order. Similarly, obligations that are due the several funds under the individual orders should be paid to the appropriate combined fund under the merged order.

The money paid to the administrative expense fund is each handler's proportionate share of the cost of administering the order. It is anticipated that all handlers currently regulated under the two orders will continue to be regulated under the merged order. In view of this, it would be an unnecessary administrative and financial burden to allocate back to handlers the reserve funds under the individual orders and then accumulate an adequate reserve for the merged order. It is equally equitable and more efficient to combine the administrative monies accumulated under the individual orders and to pay any liabilities against such funds from the consolidated fund of the merged order.

The money accumulated in the marketing service funds of the individual orders is that which has been paid by producers for whom the market