Order Code RL33475

CRS Report for Congress

Dairy Policy Issues

Updated February 9, 2007

Ralph M. Chite
Specialist in Agricultural Policy
Resources, Science, and Industry Division

Dairy Policy Issues

Summary

Two federal programs that support the price and income received by dairy farmers are expiring in 2007 — the dairy price support program and the Milk Income Loss Contract (MILC) program. The reauthorization of these and other farm commodity price and income support programs is being debated by the 110th Congress in the context of a pending omnibus 2007 farm bill.

The MILC program allows participating dairy farmers to receive a government payment when the farm price of milk used for fluid consumption falls below an established target price. In its original authorization in the 2002 farm bill (P.L. 107-171), the MILC program was scheduled to expire in 2005. However, a provision in the FY2006 budget reconciliation act (P.L. 109-171) extended MILC program authority for two years, through September 30, 2007. As a cost-saving measure, P.L. 109-171 prohibits any MILC payments for the last month of its extended authority (September 2007). Under budget rules, this means that the program will have no baseline budget spending allocated to it beyond its expiration date. The MILC program is generally supported by milk producer groups in the Northeast and the Upper Midwest. Large farmers contend that the prohibition on MILC payments for any annual milk production in excess of 2.4 million lbs. is biased against them.

The dairy price support program indirectly supports the farm price of milk through government purchases of surplus dairy products from dairy processors. The current support price is authorized at $9.90 per hundredweight (cwt.) through December 31, 2007, by the 2002 farm bill. In order to achieve the support price, USDA has a standing offer to dairy processors to purchase surplus manufactured dairy products at stated prices. Consequently, the government purchase prices usually serve as a floor for the market price of these products, which in turn indirectly supports the farm price of milk at $9.90 per cwt. Government purchases and costs have been relatively small in recent years, particularly when compared with the 1980s, when the support price was significantly higher. Most dairy farm groups view the program as a necessary safety net in a market characterized by volatile prices. Dairy processors consider the price support and MILC programs to operate at cross-purposes, which they say contributes to surplus milk production. Others are concerned that dairy support might have to be modified in order to comply with our trade obligations in the World Trade Organization.

On January 31, 2007, the Administration released a comprehensive 2007 farm bill proposal that included recommendations for both the dairy price support program and the MILC program. The Administration supports the extension of the price support program at the current level of $9.90 per cwt., viewing the program as a low-cost stabilizing influence on farm milk prices. It also supports a continuation of MILC payments at the current target price of $16.94 per cwt. In order to defray the cost of MILC program extension, the Administration recommends that the payment rate be gradually reduced over a five-year period. Annual payments to any producer would continue to be restricted to 2.4 million lbs. under the proposal.

Contents

List of Tables

Dairy Policy Issues

Milk Income Loss Contract (MILC) Payments

Background

In FY1999-FY2001, Congress provided just over $32.5 billion in emergency spending for USDA programs, primarily to help farmers recover from low farm commodity prices and natural disasters. The majority of these funds were for supplemental direct farm payments made to producers of certain commodities, primarily grains and cotton, but also including soybeans, peanuts, tobacco, and milk. Of this amount, dairy farmers received supplemental "market loss" payments of $200 million in FY1999 under the Omnibus Consolidated and Emergency Supplemental Appropriations Act, 1999 (P.L. 105-277), $125 million under the FY2000 agriculture appropriations act (P.L. 106-78), and $675 million under the emergency provisions in the FY2001 agriculture appropriations act (P.L. 106-387).

Some dairy farmer groups sought a permanent direct payment program for dairy farmers to be included in the 2002 farm bill as a means of supplementing dairy farm income when farm milk prices are low. Prior to the emergency payments made each year on an ad-hoc basis in FY1999 through FY2001, dairy farmers generally were not recipients of direct government payments. However, some groups contended that farm milk prices had been volatile in recent years and that dairy farmers needed more income stability.

Separately, the Northeast Dairy Compact, which provided price premiums to New England dairy farmers when market prices fell below a certain level, expired on September 30, 2001. These premiums were funded by assessments on fluid milk processors, whenever fluid farm milk prices in the region fell below $16.94 per hundredweight (cwt.). Supporters of the Northeast Compact had sought for an extension of the compact; the southeastern states were seeking new authority to create a separate compact. However, dairy processors and Upper Midwest producers strongly oppose regional compacts.

MILC Program Mechanics

Section 1502 of the Farm Security and Rural Investment Act of 2002 (P.L. 107-171, the 2002 farm bill) authorized a new counter-cyclical national dairy market loss payment program. (Upon implementation, USDA dubbed the program the Milk Income Loss Contract (MILC) program.) This program did not replace the dairy price support program or federal milk marketing orders, other current federal milk pricing policy tools. Instead, it was created as an alternative to regional dairy compacts and ad-hoc emergency payments to farmers, by authorizing additional federal payments when farm milk prices fall below an established target price. Authority for the MILC program expired on September 30, 2005, as required by the

2002 farm bill. However, the Deficit Reduction Act of 2005 (P.L. 109-171, S. 1932, enacted February 8, 2006) authorized a two-year extension of the program until September 30, 2007. (See “MILC Program Reauthorization” below for details.)

Under the MILC program, dairy farmers nationwide are eligible for a federal payment whenever the minimum monthly market price for farm milk used for fluid consumption in Boston falls below $16.94 per hundredweight (cwt.). In order to receive a payment, a dairy farmer must enter into a contract with the Secretary of Agriculture. Under the original farm bill authority, a producer received a payment equal to 45% of the difference between the $16.94 per cwt. target price and the market price, in any month that the Boston market price falls below $16.94. As a cost-saving measure, P.L. 109-171 reduced the payment rate from 45% to 34% effective for MILC payments in any month from October 2005 through August 2007. Under the law, a producer can receive a payment on all milk production during any month, but no payments are made on any annual production in excess of 2.4 million pounds per dairy operation.

The MILC program is akin to the Northeast Dairy Compact, which was in effect in the six New England states from 1997 until its expiration on September 30, 2001. However, under the expired dairy compact, dairy processors were required to pay the full difference between the $16.94 per cwt. fluid milk target price and any market price shortfall for fluid use milk in the compact region. The MILC program shifted the responsibility of the payment from the processor (and ultimately the consumer) to the federal government.

Although the MILC program originally expired on September 30, 2005, and was not extended until several months after that date, P.L. 109-171 allowed for USDA to make MILC payments retroactively for December 2005 through May 2006. For FY2006, USDA accepted applications in two phases. Eligible milk producers had until May 17, 2006 to sign up for payments to begin with one of the retroactive payment months (December 2005 through May 2006). After May 17, retroactive payments were no longer available, and a producer can only choose to begin receiving payments in the current month or a future month. (For a USDA fact sheet on the FY2006 MILC program, see [http://165.221.16.19/dafp/psd/MILC.htm].

MILC Payment History

USDA began accepting applications for the original MILC Program” on August 15, 2002. (See **Table 1** for MILC payment history.) Monthly market prices were sufficiently low between December 2001 and August 2003 that MILC payments were made in every month during this period. Beginning in the late summer months of 2003, market farm milk prices greatly improved, rebounding from a 25-year low that prevailed throughout most of the early months of 2003. Hence, no MILC payments were required in September through December 2003. However, farm milk prices began to decline again in the latter part of 2003. Consequently, MILC payments resumed in January and February 2004. Market farm milk prices reversed their course in the late winter months and early spring of 2004, increasing to record high levels by the spring of 2004. Market prices remained sufficiently high from May 2004 through May 2005 so that no MILC payments were required over that time period. Market prices declined to the point that a small MILC payment ($0.03 per cwt.) was made for June 2005 milk production, the only payment that was made in all of FY2005. However, market prices declined in late 2005, triggering payments in each month from December 2005 through January 2007.

Table 1. Monthly Milk Income Loss Contract (MILC) Payment Rates

Month	Payment (per hundredweight)	Month	Payment (per hundredweight)
December 2001	$0.77	Sept.- Dec. 2003	$0.00
January 2002	$0.78	January 2004	$0.83
February 2002	$0.78	February 2004	$0.95
March 2002	$0.93	March 2004	$0.79
April 2002	$1.00	April 2004	$0.02
May 2002	$1.09	May 2004-May 2005	$0.00
June 2002	$1.20	June 2005	$0.03
July 2002	$1.38	July-November 2005	$0.00
August 2002	$1.45	December 2005	$0.04
September 2002	$1.45	Jan.-Feb. 2006	$0.105
October 2002	$1.59	March 2006	$0.41
November 2002	$1.39	April 2006	$0.84
December 2002	$1.43	May 2006	$0.925
January 2003	$1.41	June 2006	$1.00
February 2003	$1.56	July 2006	$0.80
March 2003	$1.75	August 2006	$0.925
April 2003	$1.82	September 2006	$0.965
May 2003	$1.79	October 2006	$0.43
June 2003	$1.78	November 2006	$0.44
July 2003	$1.76	December 2006	$0.43
August 2003	$1.22	January 2007	$0.03

Source: USDA, Agricultural Marketing Service (AMS)

Federal Cost of MILC

For the first four years of the MILC program, its cumulative cost was just under $2.4 billion — $1.8 billion in FY2003, $221 million in FY2004, $8.8 million in FY2005, and $350.5 million in FY2006. The FY2003 total includes two fiscal years worth of payments, since retroactive payments for FY2002 were made over the course of FY2003. FY2004 and FY2005 outlays were significantly lower because market farm milk prices were much stronger than in the two previous years, reaching a record high in the summer of 2004. During the same four-year time period (FY2003-FY2006), five states accounted for just over one-half of the total payments made over the time period (see **Table 2**). The Congressional Budget Office (CBO) estimates that MILC program outlays will be $416 million in FY2007. However, this estimate can change depending on market conditions.

Table 2. MILC Payments Ranked by State, FY2003-FY2006

	FY2003	FY2004	FY2005	FY2006	FY2003-FY2006 Total
Wisconsin	$372,042,880	$41,754,746	$1,369,537	$71,838,550	$487,005,713
New York	169,423,978	17,222,870	383,632	32,257,023	219,287,503
Pennsylvania	160,673,846	19,263,582	1,352,555	27,082,715	208,372,697
Minnesota	147,400,075	15,946,997	286,412	27,169,579	190,803,063
California	122,764,930	25,142,045	1,186,734	34,913,717	184,007,426
Michigan	75,828,865	8,799,034	316,507	15,563,328	100,507,734
Ohio	68,772,479	7,550,599	194,479	11,922,216	88,439,773
Iowa	60,686,427	6,512,172	236,348	11,629,909	79,064,855
Texas	38,793,821	6,282,787	199,362	9,024,192	54,300,162
Vermont	40,826,421	4,389,019	138,325	8,126,455	53,480,220
Idaho	33,211,800	5,496,523	371,276	8,719,484	47,799,082
Missouri	36,267,942	3,426,748	128,206	6,204,901	46,027,797
Illinois	34,170,687	3,818,084	158,274	6,144,976	44,292,022
Washington	30,869,213	5,064,507	111,841	7,539,782	43,585,343
Indiana	30,180,470	3,510,016	214,743	5,255,495	39,160,723
Kentucky	31,094,215	3,364,755	96,648	4,508,582	39,064,200
Virginia	29,876,611	2,895,202	324,527	5,174,178	38,270,519
Tennessee	24,469,076	2,545,783	62,281	3,853,946	30,931,087
South Dakota	20,355,578	2,148,893	31,015	3,738,836	26,274,321
Maryland	18,132,857	1,774,254	161,405	3,184,670	23,253,185
Oregon	16,295,432	2,178,087	35,910	4,036,387	22,545,817
Utah	15,782,707	2,027,249	-18,216	3,419,809	21,211,549
Georgia	15,764,327	1,930,999	31,078	3,136,152	20,862,557
Kansas	15,747,021	1,775,859	57,526	2,765,443	20,345,849
North Carolina	15,395,265	1,766,672	35,218	2,764,319	19,961,473
Nebraska	14,835,308	1,588,040	121,518	2,544,254	19,089,119
Puerto Rico	12,388,197	4,222,742	381,336	966,771	17,959,046
New Mexico	11,493,657	2,825,129	127,273	3,354,332	17,800,392
Oklahoma	12,519,405	1,307,138	50,983	1,958,338	15,835,863
Louisiana	11,430,924	1,066,703	31,415	1,517,821	14,046,862
Florida	9,783,286	1,761,420	31,601	2,342,573	13,918,880
Maine	10,250,302	984,845	13,481	1,904,303	13,152,931
Colorado	8,754,312	1,537,030	52,001	2,051,322	12,394,666
Arizona	7,641,285	1,526,600	163,838	2,138,679	11,470,403
North Dakota	8,964,621	1,111,814	56,389	1,291,575	11,424,400
Mississippi	8,916,963	880,166	66,520	1,189,543	11,053,191
Arkansas	7,499,823	665,206	27,202	1,011,333	9,203,563
Massachusetts	6,877,027	625,496	8,973	1,113,219	8,624,715
Connecticut	6,143,097	699,449	8,509	1,145,967	7,997,022
New Hampshire	5,095,796	515,693	11,031	973,494	6,596,015
Montana	4,901,714	519,903	21,112	1,023,945	6,466,674
South Carolina	4,779,476	529,781	52,581	914,359	6,276,197
Alabama	4,286,766	512,368	3,719	593,777	5,396,629
West Virginia	3,942,927	459,851	13,707	614,441	5,030,926
New Jersey	4,012,708	373,719	2,101	596,928	4,985,455
Nevada	2,014,582	351,358	25,597	589,067	2,980,605
Delaware	1,768,299	184,425	2,947	310,154	2,265,824
Wyoming	1,015,120	101,807	2,655	205,252	1,324,835
Hawaii	407,366	117,018	46,913	52,150	623,447
Rhode Island	451,901	36,430	390	58,558	547,279
Alaska	350,368	26,291	358	35,340	412,358
Virgin Islands	100,347	7,723	83	8,682	116,835
TOTAL	**1,795,452,502**	**221,125,627**	**8,789,854**	**350,480,820**	**2,375,848,803**

MILC Issues in the 2007 Farm Bill

Funding. The 2002 farm bill required the MILC program to expire on September 30, 2005, while all other major farm commodity support programs authorized by the farm bill are scheduled to expire at the end of the 2007 crop year. Proponents of the MILC program wanted program expiration to coincide with the expiration of all other commodity support programs. Hence, a provision in the FY2006 omnibus reconciliation act (P.L. 109-171, S. 1932) extends the MILC program through September 30, 2007. It also reduces the MILC payment rate so that a recipient receives 34% of the difference between the target price and the lower market price, instead of the 45% payment rate in the recently expired program. This payment rate reduction is effective from October 2005 through August 2007.

The payment rate was reduced as a budget-saving measure in order to keep the two-year estimated cost of program extension just below $1 billion. (CBO estimated the two-year cost of the provision at $998 million, compared with $1.2 billion if the program had been extended without the payment rate reduction.) Also, in order to minimize the cost of program extension, P.L. 109-171 reduced the MILC payment rate to 0% in September 2007, the last month of program authority. This means that when the 2007 farm bill is formulated, the MILC program will have no baseline budget spending allocated to it beyond August 2007. This does not necessarily preclude the possibility of the MILC program being extended in the 2007 farm bill. However, if the total spending allocated to the farm bill is no greater than the baseline budget, the cost of the MILC program might have to be offset with reductions in spending in other farm bill programs.

Administration's Farm Bill Proposal. On January 31, 2007, the Administration released a comprehensive 2007 farm bill proposal that included several recommendations for the MILC program. The Administration supports a continuation of MILC payments at the current target price of $16.94 per cwt. In order to defray the cost of MILC program extension, the Administration recommends that the payment rate be gradually reduced over a five-year period. It proposes maintaining the payment rate at the current level of 34% through FY2008, and then reducing it to 31% in FY2009, 28% in FY2010, 25% in FY2011, 22% in FY2012, and 20% in FY2013-FY2017. Annual payments per operation would continue to be restricted to 2.4 million lbs. under the proposal. It would also base payments on historical production rather than current production in order to forestall potential challenges to the program in the World Trade Organization.

Regional Issues. Since its inception, the MILC program has been generally supported by milk producer groups in the Northeast and the Upper Midwest. Producer groups in the Northeast region viewed it as an alternative to the Northeast dairy compact. Upper Midwest producers preferred the new program to state compacts since the new program shares the price premiums nationally. Large dairy farmers have expressed concern that the MILC program causes excess milk production that in turn decreases market farm milk prices. They contend that this negatively affects their income, since their annual production is well in excess of the 2.4 million lb. payment limit, and any production in excess of 2.4 million pounds receives the market price and no federal payments. (Annual production of 2.4 million pounds is roughly equal to the annual production of a herd of approximately 120 to 130 dairy cows.)

Dairy Price Support Program

The Agricultural Act of 1949 first established the dairy price support program by permanently requiring USDA to support the farm price of milk. Since 1949, Congress has regularly amended the program, usually in the context of multi-year omnibus farm acts and budget reconciliation acts. (See **Table 3**, below, for a recent history of spending on the dairy price support program and related activities.) Most recently, Section 1501 of the Farm Security and Rural Investment Act of 2002 (P.L. 107-171, the omnibus 2002 farm bill) authorized a 5½-year extension of the program through December 31, 2007, at the then-current support price of $9.90 per hundredweight (cwt.) of farm milk. Reauthorization of the program will be debated in the context of a new omnibus farm bill this year.

Historically, the supported farm price for milk is intended to protect farmers from price declines that might force them out of business and to protect consumers from seasonal imbalances of supply and demand. USDA's Commodity Credit Corporation (CCC) supports milk prices by its standing offer to purchase surplus nonfat dry milk, cheese, and butter from dairy processors. Government purchases of these storable dairy products indirectly support the price of milk for all dairy farmers. Prices paid to the processors are set administratively by USDA at a level that should permit them to pay dairy farmers at least the federal support price for their milk.

In order to achieve the support price of $9.90 per cwt. of milk, USDA has a standing offer to processors to purchase surplus manufactured dairy products at the following prices: $1.05 per lb. for butter, $0.80 for nonfat dry milk, $1.1314 per lb. for block cheddar, and $1.1014 per lb. for barrel cheese. Whenever market prices fall to the support level, processors generally make the business decision of selling surplus product to the government rather than to the marketplace. Consequently, the government purchase prices usually serve as a floor for the market price, which in turn indirectly supports the farm price of milk at $9.90 per cwt.

Government purchases of surplus dairy products have been relatively small since late 2003, as market prices have remained above the support price during that period. In the early 1980s, the support price was $13.10 per cwt. and government purchases peaked at $2.6 billion in 1983. A gradual decline in the support price to the current level of $9.90 has significantly reduced the cost of the program from peak levels. (See **Table 3** for a history of government purchases and costs since the 1981 marketing year.)

Table 3. Dairy Price Support Purchases and Costs, 1980/81-2005/06

Marketing Year[a]	Net Removals Milk Equivalent (billion lbs.)[b]	Net Outlays (million $)	CCC Support Price ($ per cwt.)	CCC Purchases as Percentage of Production
1980-81	12.7	1,975	13.10	9.6
1981-82	13.8	2,239	13.49-13.10	10.2
1982-83	16.6	2,600	13.10	12.0
1983-84	10.4	1,597	13.10-12.60	7.6
1984-85	11.5	2,181	12.60-11.60	8.2
1985-86	12.3	2,420	11.60	8.5
1986-87	5.4	1,238	11.60-11.35	3.8
1987-88	9.7	1,346	11.10-10.60	6.7
1988-89	9.6	712	10.60-11.10	6.7
1989-90	8.4	505	10.60-10.10	5.7
1990-91	10.4	839	10.10	7.0
1991-92	10.1	232	10.10	6.7
1992-93	7.6	253	10.10	5.0
1993-94	4.2	158	10.10	2.8
1994-95	2.9	4	10.10	1.8
1995-96	0.1	-98	10.10-10.35	0.1
1996-97	0.7	67	10.20	0.4
1997-98	0.7	291	10.20-10.05	0.4
1998-99	0.3	280	10.05-9.90	0.2
1999-2000	0.8	569	9.90	0.5
2000-01	0.3	465	9.90	0.2
2001-02	0.2	622	9.90	0.1
2002-03	0.5	699	9.90	0.3
2003-04	NA	74	9.90	NA
2004-05	NA	- 104	9.90	NA
2005-06	NA	55	9.90	NA

Source: U.S. Department of Agriculture, Farm Service Agency, selected publications.

a. The marketing year is October 1-September 30.

b. The milk equivalent is the pounds of fluid milk used to manufacture cheese and butter, on a milkfat basis.

NA = Not Available

Farm Bill Issues

At issue in Congress this year is whether the dairy price support program should be extended beyond its December 31, 2007, expiration date. Funding is available in the budget baseline to extend the program at the current $9.90 per cwt. level of support. In its January 31, 2007, farm bill proposal, the Administration recommended the extension of the program, viewing it as a low-cost stabilizing influence on farm milk prices. It stated that many dairy producers see the need for a floor to be kept under farm milk prices to maintain an adequate milk supply and provide a safety net. Dairy processor groups have expressed concern that the dairy price support program in combination with MILC payments work at cross-purposes, by artificially stimulating milk production and causing persistent surpluses. They also question whether having the government as a guaranteed buyer of surplus products discourages investment to produce dairy ingredients (e.g. milk protein concentrates) that are increasingly in demand in the market.

Separately, some policymakers are concerned that because of the way domestic price support programs are viewed under our trade obligations in the World Trade Organization (WTO), modifications to dairy support might be required under a new trade agreement. Although federal outlays for the dairy price support program have been relatively small (under $100 million) in recent years (see **Table 3**), the WTO measures the level of support differently. Under our current trade obligations, the aggregate measure of support for dairy is based on how much higher the domestic support price is set above a fixed world reference price, and this imputed subsidy is applied to all domestic milk production. Using this formula, the WTO views the aggregate measure of support for the dairy price support program to be more than $4.5 billion annually, and classifies it as "amber box" or the most trade-distorting category. The current U.S. proposal in the Doha Round is to reduce its total amber box support from the current $19.1 billion to $7.6 billion. With dairy support such a large percentage of the proposed new maximum, some have expressed interest in shifting future policy away from price support to some type of WTO-compliant direct payment that is decoupled from price and production.

Federal Milk Marketing Orders

Background

The farm price of approximately two-thirds of the nation's fluid milk is regulated under federal milk marketing orders. Federal orders, which are administered by the U.S. Department of Agriculture (USDA), were instituted in the 1930s to promote orderly marketing conditions by, among other things, applying a uniform system of classified pricing throughout the market. Some states, California for example, have their own state milk marketing regulations instead of federal rules. Producers delivering milk to federal marketing order areas are affected by two fundamental marketing order provisions: the classified pricing of milk according to its end use, and the pooling of receipts to pay all farmers a blend price.

Proponents of federal orders argue that orders are necessary because dairy farmers have a competitive disadvantage vis-à-vis dairy handlers (processors) when it comes to determining prices that farmers receive for their raw, perishable milk. Federal orders regulate handlers who sell milk or milk products within a defined marketing area by requiring them to pay not less than established minimum class prices for the Grade A milk they purchase from dairy producers, depending on how the milk is used. This classified pricing system requires handlers to pay a higher price for milk used for fluid consumption (Class I) than for milk used in manufactured dairy products such as yogurt, ice cream, and sour cream (Class II products), cheese (Class III), and butter and dry milk products (Class IV products). These differences between classes reflect the different market values for the products.

Blend pricing allows all dairy farmers who ship to the market to pool their milk receipts and then be paid a single price for all milk based on order-wide usage (a weighted average of the four usage classes). Paying all farmers a single blend price is seen as an equitable way of sharing revenues for identical raw milk directed to both the higher-valued fluid market and the lower-valued manufacturing market.

Manufactured class (Class II, III and IV) prices are the same in all orders nationwide and are calculated monthly by USDA based on current market conditions for manufactured dairy products. The Class I price for milk used for fluid consumption varies from area to area. Class I prices are determined by adding to a monthly base price, a "Class I differential" that generally rises with the geographical distance from milk surplus regions in the Upper Midwest, the Southwest, and the West. Class I differential pricing is a mechanism designed to ensure adequate supplies of milk for fluid use at consumption centers. The supply of milk may come from local supplies or distant supplies, whichever is more efficient. However, local dairy farmers are protected by the minimum price rule against lower-priced milk that might otherwise be hauled into their region.

Milk Regulatory Equity Act (P.L. 109-215, S. 2120)

On April 11, 2006, the President signed into law the Milk Regulatory Equity Act (P.L. 109-215, S. 2120), which addressed several federal milk marketing order issues relevant to the western United States. Among the milk marketing order issues addressed in H.R. 4015/S. 2120 are (1) the regulation of fluid milk processors who operate a plant in a federal order area, are not regulated by that order, and ship packaged milk into a state marketing order (not a federal order); (2) the regulation of fluid processors who produce, package and distribute their milk, also known as producer-handlers or producer-distributors; and (3) the exclusion of Nevada from federal milk marketing orders.

Regulation of Certain Interstate Milk Shipments. P.L. 109-215 affects any processor (handler) of Class I (fluid-use) milk who operates a plant that is located in a federal milk marketing order area, is not regulated by the federal order because it has no sales in the federal marketing area, and has packaged fluid milk deliveries to a state that is regulated by a state marketing order. Such a plant is not currently paying a regulated price for the raw milk that is used for these dispositions or sales. The bill would require any such processor to pay into the federal order pool the minimum federal milk marketing order price for the raw milk that went into the shipments sold into the state order.

This provision is targeted at a large fluid processor who is located in Yuma, Arizona (which is part of the Arizona-Las Vegas milk marketing order area), but ships all of its packaged milk into California. Under current law and regulations, this plant's interstate shipments to California are not regulated by either the Arizona-Las Vegas order or the California state order. This provision is supported by other processors and milk producers who contend that this processor's current exclusion from paying the minimum regulated price is a "loophole" in the current federal order system, which they say provides that processor with an unfair price advantage. Opponents of this provision contend that it would adversely affect their operations and raise the price of milk to consumers. They also contend that Congress and USDA should hold hearings on the issue before any legislative changes are considered.

Producer-Handler Exemption. As defined by USDA, producer-handlers are dairy farmers who process milk from their own cows in their own plants and market their packaged fluid milk and other dairy products themselves. Producer-handlers sometimes are referred to as producer-distributors, or P-Ds. Producer-handlers may sell products directly to consumers through their own stores, directly to consumers on home-delivery routes, or to wholesale customers such as food stores, vendors, or institutions. Current regulations exempt producer-handlers from the minimum price requirements of federal milk marketing orders, but minimal reporting is required.

P.L. 109-215 requires the full regulation of any producer-handler with distribution of fluid milk in the Arizona-Las Vegas order area in excess of 3 million pounds in the previous month. The act primarily affects the same producer-handler in Arizona that is affected by the interstate milk shipment provision discussed above. Meanwhile, USDA has published a final regulation effective April 1, 2006, that establishes a 3 million lb. per month route disposition limit for a producer-handler exemption, both in the Pacific Northwest and the Arizona-Las Vegas order areas. The final USDA regulation affects at least three large producer handlers in the Pacific Northwest, as well as the Arizona producer-handler. (For USDA's final rule, see [http://a257.g.akamaitech.net/7/257/2422/01jan20061800/edocket.access.gpo.gov/2006/06-1587.htm].) The Arizona producer-handler (Hein Hettinga) is challenging the new USDA regulation in court.

The producer-handler provision is a separate issue from the provision above relating to the interstate shipment of milk, but with similar implications. Producers of regulated milk want this unregulated milk to become regulated so it will increase the blend price received by all regulated dairy farmers. Regulated processors contend that it is unfair that they have to pay the regulated price while certain handlers are exempt. The producer-handlers who would become regulated argue that this is a tax being placed on independent family farms that would ultimately result in higher prices to consumers.

Nevada Exclusion from Federal Milk Marketing Orders. Section 760 of the FY2000 agriculture appropriations act (P.L. 106-78) was intended to remove Clark County, Nevada from the Las Vegas-Arizona federal milk marketing order area so that the only handler in this county would be subject to the lower Nevada state order price for fluid milk. However, the enacted provision was phrased in a way that did not completely remove Clark County from the federal order system. The enacted language exempted any plant operating in Clark County from being subject to any federal milk marketing order. However, it did not remove Clark County from the Arizona-Las Vegas milk marketing order area. This means that milk that is currently shipped from California to Clark County is partially regulated and compensatory payments to the Arizona-Las Vegas order are required. Hence, a provision in P.L.

109-215 completely removes the state of Nevada from the marketing area definition of any order, which supporters say would end the required compensatory payments paid by California milk shippers and allow all of Nevada to be joined together in the state order.