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Dairy Provisions in the 2014 Farm Bill (P.L. 113-79)

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Summary

The 2014 farm bill (P.L. 113-79), which was signed into law on February 7, 2014, makes significant changes to the structure of U.S. dairy support programs, including the elimination of several major price and income support programs from the 2008 farm bill (P.L. 110-246), the extension of several smaller dairy programs, and the addition of two new programs.

Three of the principal dairy support programs under the 2008 farm bill—the Dairy Product Price Support Program (DPPSP), the Milk Income Loss Contract (MILC) program, and the Dairy Export Incentives Program (DEIP)—are eliminated. These programs are replaced by two new support programs that are authorized for the five-year period of the 2014 farm bill, FY2014-FY2018—the Margin Protection Program (MPP) and the Dairy Product Donation Program (DPDP).

The MPP is a voluntary program that makes a payment to participating farmers when a formula-based national margin—referred to as the Actual Dairy Production Margin (ADPM) and calculated as the national average farm price for all milk minus a national-average feed cost ration—falls below a producer-selected insured margin that can range from $4.00 per hundredweight (cwt.) to $8.00/cwt. in $0.50/cwt. increments. According to USDA final rules (released August 29, 2014), MPP payments are based on a farm-level production history and a producer-selected coverage level that ranges from 25% to 90%—the product of these two items yields the covered production history (CPH). Producers must pay an annual administrative fee of $100 for each participating dairy operation, and a premium that rises steadily for higher margin protection levels starting at the $4.50/cwt. margin level. The minimum $4.00/cwt. margin is fully subsidized and has no farmer-paid premium. The premium structure is further divided based on the volume of CPH—lower premiums are charged for the first 4 million pounds (lbs.) of CPH, higher premiums are charged on CPH above 4 million lbs. As an incentive to encourage participation by smaller dairy operations (with CPH under 4 million lbs.), premiums will be reduced by 25% across the board for all margin protection levels except the $8.00/cwt. level during calendar 2014 and 2015.

The DPDP requires USDA to procure and distribute certain dairy products when the ADPM falls below $4.00/cwt. for two consecutive months. DPDP dairy product distribution is required to target individuals from low-income groups and not be allowed for resale into commercial markets. Purchases and distribution under the DPDP end after three months or if the U.S. price for certain dairy products is significantly above world prices.

Several programs from the 2008 farm bill were extended through FY2018 including the Dairy Forward Pricing Program, the Dairy Indemnity Program, and certain provisions to augment the development of export markets under the National Dairy Promotion and Research Program (i.e., the dairy check off program). In addition, the final bill adopted a provision that requires USDA to adhere to standard rulemaking procedures.

Separately, federal milk marketing orders have permanent statutory authority and continue intact, as does the Livestock Gross Margin for Dairy Cattle program (LGM-D) and the suite of Dairy Import Tariff Rate Quotas (TRQs) that limit access to the U.S. domestic market by lower-priced foreign dairy products. The permanent Dairy Price Support Program contained in the Agricultural Act of 1949 (P.L. 81-439) is suspended but would be reactivated should MPP expire at the end of FY2018 without replacement or extension.

Contents

Figures

Tables

Appendixes

Contacts

Introduction

After several years of growing producer discontent with the apparent ineffectiveness of the federal dairy price support program and growing concerns about rapidly escalating dairy feed costs, the U.S. dairy industry advocated for substantial changes in the nature of federal dairy support. As a result, the 2014 farm bill (the Agricultural Act of 2014; P.L. 113-79), which was signed into law on February 7, 2014, makes significant changes to the structure of U.S. dairy support programs including the elimination of several major price and income support program provisions from the 2008 farm bill (the Food, Conservation, and Energy Act of 2008, P.L. 110-246), the extension of several smaller dairy programs, and the addition of two new programs.

This report describes the major dairy provisions contained in the 2014 farm bill as well as Congressional Budget Office (CBO) cost projections of historical program outlays compared with outlays under the new dairy programs.[1] The report also includes a discussion of potential issues related to the new dairy policies. Finally, a table at the end of this report (**Table A-1**) provides a side-by-side comparison of dairy provisions from the 2008 and 2014 farm bills.[2]

Reaching a final compromise on U.S. dairy policy, as contained in the 2014 farm bill, was a long and arduous task involving considerable debate over what the nature and role of federal support programs should be. The following section provides background on the shift of federal support from dairy product prices to the dairy operating margin.

Origins of the New Dairy Policy

Federal dairy price supports were first established by federal law in 1949 and modified in subsequent legislation including the 2008 farm bill (P.L. 110-246), which established the Dairy Product Price Support Program (DPPSP).[3] DPPSP indirectly supported the farm price of fluid milk at $9.90 per hundred lbs. (i.e., hundredweight or cwt.) through government purchases of dairy products from dairy processors at statutorily set prices.[4] The program was countercyclical, in that government purchases occurred when product prices were low, and ceased as product prices rose above support levels. However, by the mid-1990s, the annual farm price of milk had

[1] This report borrows from the discussion of new dairy programs in "The Dairy Subtitle of the Agricultural Act of 2014," PDMP Information Letter 14-01, by Marin Bozic, John Newton, Andrew M. Novakovic, Mark Stephenson, and Cameron S. Thraen, revised September 5, 2014; and "Highlights of the FSA Final Rule on the Margin Protection Program for Dairy Producers (MPP-Dairy)," PDMP Information Letter 14-02, by Andrew M. Novakovic, Aug. 29, 2014.

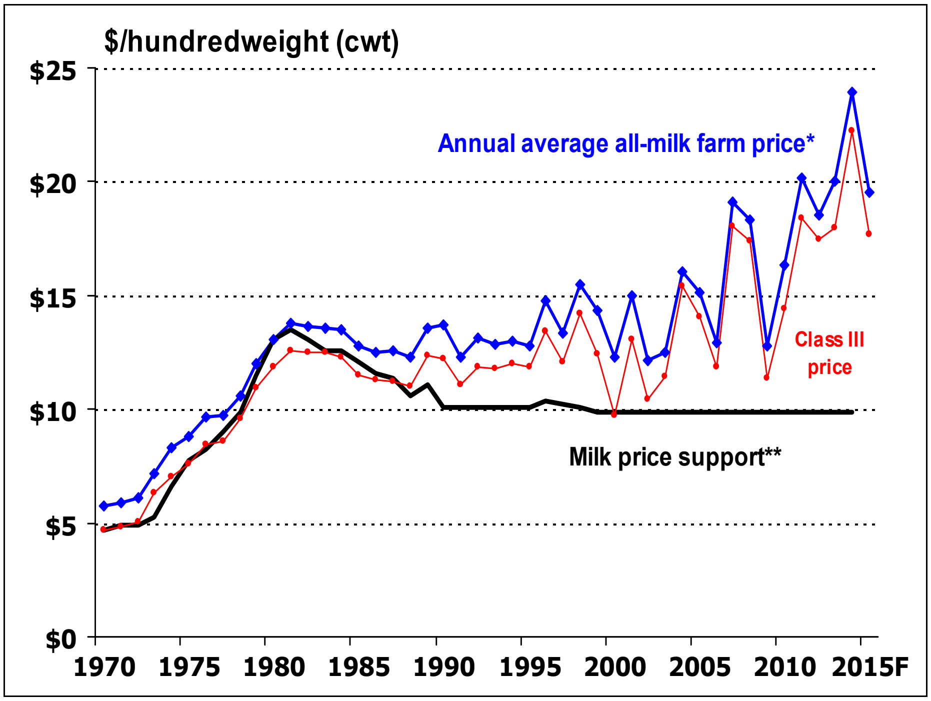
[2] For a comparison of new 2014 farm bill dairy policy provisions with previous law as well as with both the House and Senate farm bill proposals—the Senate-passed S. 954 and the House-passed H.R. 2642—see CRS Report R43076, *The 2014 Farm Bill (P.L. 113-79): Summary and Side-by-Side*.

[3] The U.S. government purchased storable dairy commodities in 1933 and 1941 as a way to shore up farm milk prices and provide food for needy families. During WWII, the same mechanism was used to ensure adequate production. In the tumultuous economic aftermath of WWII, this means of supporting farm milk prices was made permanent through the Dairy Price Support Program of the Agricultural Act of 1949.

[4] The original program—named the Dairy Price Support Program—had a statutorily determined support price for fluid milk (e.g., $9.90 per cwt. in the mid-2000s). The program was renamed by the 2008 farm bill when direct fluid milk price support was shifted to indirect support via government purchases of manufactured products including butter, cheese, and milk powder at statutorily established prices.

trended higher, albeit subject to an increasingly volatile pattern (**Figure 1**), whereas the federal support rate was flat at $9.90 per cwt.

Figure 1. Milk Prices Moved Well Above Previous Support Levels By 1990



Source: U.S. Dept. of Agriculture, World Agricultural Supply and Demand Estimates (WASDE), September 11, 2014.

Notes: National average price received by farmers, all milk, and the announced Class III price, are USDA data; 2014 and 2015 prices are USDA forecasts. ** The national price support for milk was statutorily established at $9.90 per cwt. from 1998 until 2008. Beginning in 2008, government purchase prices were established for individual dairy products, but with essentially the same effect as supporting raw milk at $9.90 per cwt. These price supports were repealed by the 2014 farm bill (P.L. 113-79).

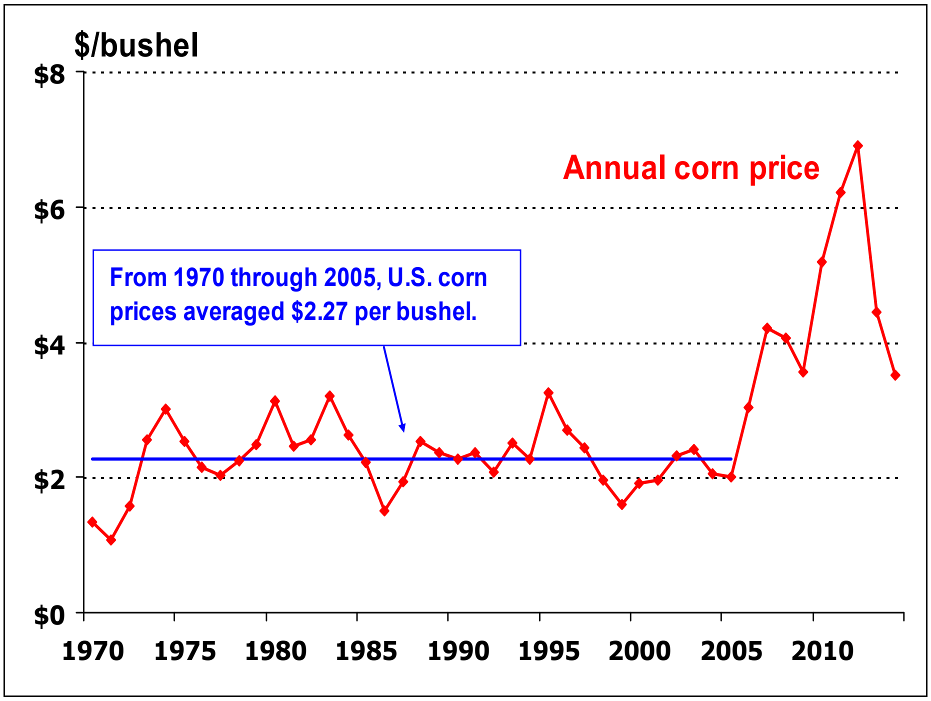
Volatile milk prices made planning more difficult and made dairy producers more vulnerable to unexpected or sustained increases in the cost of feed (the major cost component of dairy production). Milk producers have argued since the early 1990s that support levels had become too low, relative to market prices and costs of production, to provide meaningful support. More recently, milk producers argued that support based strictly on the price of milk failed to account for the sharp escalation of feed costs that has occurred since 2006 (**Figure 2**).

After the emergence of the U.S. ethanol industry as a major source of corn demand in 2006, coupled with a series of weather-related, below-trend yield years (especially 2010-2012) for the U.S. corn crop, U.S. feed grain markets surged to new price levels by 2012 that were nearly three times above the levels that had persisted during the previous four decades. Rising feed costs are of particular concern to dairy producers because they represent a substantial portion of the cost of milk production—in 2011, feed costs accounted for 80% of operating costs and 54% of total costs of milk production (compared with 71% and 37% shares during the 2000-2004 period).[5]

[5] USDA, Economic Research Service (ERS), Commodity Costs and Returns data, retrieved on July 23, 2012, from (continued...)

The combination of volatile milk market prices rising well beyond support levels coupled with rapidly rising feed costs contributed to a shifting of focus away from price supports and towards protecting or guaranteeing some portion of the margin between milk prices and feed costs.

Figure 2. Feed Prices, Led by Corn, Have Risen Sharply Since 2006



Source: USDA, WASDE, September 11, 2014. The national average price received by farmers for corn for the 2012 crop year averaged a record $6.89 per bushel. The 2013 price is estimated by USDA at $4.45 per bushel and the 2014 price is forecast at $3.50 per bushel.

Notes: Corn is the principal feed grain used in the United States. Prices for other feed grains and hay are closely correlated with the price of corn.

This refocusing of policy interest on the dairy operating margin was formalized by a proposed dairy margin protection program published in June 2010 by the National Milk Producers Federation (NMPF) called the Foundation for the Future (FTF).[6] A version of the FTF was introduced in the 112th Congress as H.R. 3062, The Dairy Security Act (DSA), by House Agriculture Committee Ranking Member Collin Peterson on September 23, 2011. Through the legislative process FTF eventually evolved into the new dairy program described in the following sections. An appendix at the end of this report (**Appendix**) provides additional detail on the legislative debate behind the new dairy policy.

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http://www.ers.usda.gov/data-products/milk-cost-of-production-estimates.aspx.

[6] See the NMPF Foundation for the Future website at http://www.futurefordairy.com/.

Dairy Provisions in the 2014 Farm Bill

The 2014 farm bill repealed several previously existing dairy programs, extended others, added some new programs, and was silent on several existing dairy programs that derive their authority from outside of the farm bill. Each of these aspects is briefly summarized below.

Programs Repealed

The three major price and income support programs from the 2008 farm bill are eliminated. These include the following.[7]

- The **Dairy Product Price Support Program (DPPSP)** is repealed immediately. DPPSP mandated that USDA directly support the price of cheese, nonfat dry milk, and butter through acquisitions at statutorily set minimum purchase prices in order to support the farm price of milk at $9.90 per hundred lbs. or hundredweight (cwt.). The program also included USDA resale of acquired dairy products under certain price and stock-volume conditions. Some variation of a dairy price support program has been in effect since the Agricultural Act of 1949 first required USDA to support the farm price of milk.
- The **Milk Income Loss Contract (MILC)** program is temporarily extended until September 1, 2014, or until the implementation date of the new margin program (described below), whichever comes earlier and after which it is permanently repealed. MILC is a counter-cyclical payment program first authorized in the 2002 farm bill (P.L. 107-171) that makes payments available on up to 2.985 million lbs. of milk whenever the monthly Boston Class I price of fluid milk falls below a threshold of $16.94/cwt. adjusted for feed cost changes.
- The **Dairy Export Incentives Program (DEIP)**, originally authorized by the 1985 farm bill (P.L. 99-198), is repealed immediately. DEIP provided cash bonuses to U.S. dairy exporters when certain international dairy market conditions were met.

The **Federal Milk Marketing Order Review Commission**—established by the 2008 farm bill (§1509) to conduct a comprehensive review and evaluation of FMMO and non-FMMO systems—is also repealed effective immediately. The review commission-which was subject to annual funding appropriations—was never funded.

Programs Extended

Certain other programs that were reauthorized by the expired 2008 farm bill (P.L. 110-246) are extended through the life of the 2014 farm bill—that is, FY2018. These include the following.

- The **Dairy Forward Pricing Program** allows farmers to voluntarily enter into forward price contracts with milk handlers for pooled milk used for

[7] More detailed descriptions of the previous-law dairy programs, DPPSP, MILC, and DEIP, are available in CRS Report R42736, *Dairy Policy Proposals in the Next Farm Bill* and CRS Report RL34036, *Dairy Policy and the 2008 Farm Bill.*

manufactured products (Classes II, III, and IV) under Federal Milk Marketing Orders (FMMOs). The program allows regulated handlers to pay farmers in accordance with the terms of a forward contract instead of paying the minimum FMMO blend price for pooled milk. The prices paid by milk handlers under the contracts are deemed to satisfy the minimum price requirements of FMMOs. The 2014 farm bill allows for new contracts until September 30, 2018, but no contract can extend beyond September 30, 2021.

- The **Dairy Indemnity Payment Program (DIPP)** makes payments to dairy producers when a public regulatory agency directs them to remove their raw milk from the commercial market because it has been contaminated by pesticides, nuclear radiation or fallout, or toxic substances and chemical residues other than pesticides through no fault of their own. Payments also are made to manufacturers of dairy products, but only for products removed from the market because of pesticide contamination.
- The **Dairy Promotion and Research Program** is a generic dairy product promotion, research, and nutrition education program, funded by a mandatory 15¢/cwt. assessment on milk produced and marketed in the 48 contiguous states. Importers in all 50 states, the District of Columbia, and Puerto Rico must also pay an assessment rate of 7.5¢/cwt. of the milk equivalent in imported dairy products. USDA issues regulations on the time and method of importer payments.

Continuation of Existing Programs Under Non-Farm-Bill Authority

Certain dairy programs derive their operating authority outside of the farm bill and simply continue to operate independent of the enactment of the 2014 farm bill. These include, but are not limited to the following.

- **Federal Milk Marketing Orders (FMMOs)**, which exist under permanent authority, established by federal law in the Agricultural Marketing Agreement Act of 1937, are 10 geographically defined fluid milk marketing areas. The FMMO system regulates milk marketing across state lines but within these 10 explicitly defined and geographically aligned multi-state regions.[8] Within each FMMO, dairy processors or handlers (i.e., milk buyers) are required to pay a minimum price for farm milk depending on its end use.
- **Dairy Import Tariff Rate Quotas (TRQs)** are a system of product-specific import quotas—with low in-quota tariffs and high, often-prohibitive above-quota tariffs—designed to protect higher-priced domestic dairy products by limiting the importation of lower-priced foreign dairy products. Dairy TRQs are part of the Harmonized Tariff Schedule of the United States and are unaffected by changes made in the 2014 farm bill.[9]
- The **Dairy Price Support Program** is authorized under "permanent farm law" contained in the 1949 Agricultural Act, but is suspended by periodic passage of

[8] See USDA, AMS, Dairy Programs, "Federal Milk Marketing Orders," listed under "Programs and Services" at http://www.ams.usda.gov/AMSv1.0/dairy.

[9] For details by product, see the Harmonized Tariff Schedule of the United States (2012) (rev. 2), Chapter 4, pp. 2-7.

new farm legislation.[10] Under permanent law, USDA is required to purchase manufactured milk and butterfat products in sufficient quantities to raise demand in order to raise the farm price of fluid milk to the equivalency of 75% to 90% of a 1910-1914 parity price index—which would result in milk support prices near $40/cwt. double the average all-milk farm price of $20/cwt. during 2013. Reversion to permanent dairy law has been referred to as the "milk price cliff."

- The **Dairy Product Mandatory Reporting Program** requires manufacturers to report to USDA the price, quantity, and moisture content of dairy products sold. Quarterly audits are to be undertaken to ensure compatibility between submitted information and related dairy market statistics.
- The **Livestock Gross Margin Insurance for Dairy (LGM-D)** is an ongoing pilot program available for purchase from private insurers through USDA's permanently authorized federal crop insurance program. LGM-D provides protection to dairy producers when feed costs rise or milk prices drop. Gross margin is the market value of milk minus feed costs. LGM-D uses futures prices for corn, soybean meal, and milk to determine the expected gross margin and the actual gross margin.[11]
- The **Fluid Milk Processor Promotion Program**, established by the 1990 farm bill (P.L. 101-624) with subsequent reauthorizations, develops and finances generic advertising programs designed to maintain and expand markets and uses for fluid milk products produced in the contiguous 48 states and the District of Columbia. The program is funded through a 20¢/cwt. assessment paid by processors on all milk processed for fluid consumption. The fluid milk order was approved by a referendum among fluid milk processors and became effective December 10, 1993. The program originally required periodic congressional reauthorization; however, the 2002 farm bill gave it permanent authority.

Revival of a Previously Expired Provision

The 2014 farm bill also included a provision (§1410(d)) that removed the expiration dates in U.S. code (7 U.S.C. 7235[a][2]) related to the petition and approval by California dairy producers to designate the state of California as a separate Federal Milk Marketing Order (FMMO) with the potential to use a Class I quota plan to determine individual producer payments. California currently operates its dairy industry under a state marketing order, but in recent years has been considering adopting an FMMO in order to alter its current milk class pricing structure. By removing the expiration dates, the 2014 farm bill actively revives the FMMO option for California's dairy industry.

USDA's Agricultural Marketing Service would still have to receive a formal petition from California's producers and conduct a hearing to collect evidence about the market and hear testimony on desired provisions before California's dairy producers actually decide whether to adopt—via referendum—an FMMO.

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[10] For a discussion of "permanent farm law" see CRS Report R42442, *Expiration and Extension of the 2008 Farm Bill.*

[11] For more information on the LGM-D insurance program, see http://www.rma.usda.gov/pubs/rme/lgmdairy.pdf.

New Programs

The 2014 farm bill replaced the repealed price support programs—DPPSP, MILC, and DEIP—with two new support programs that are authorized for the five-year period of the 2014 farm bill, FY2014-FY2018—the Margin Protection Program (MPP) and the Dairy Product Donation Program (DPDP). These two programs are described in the following two sections.

The Margin Protection Program (MPP) for Dairy Producers

MPP Implementation Specifics

USDA was mandated to establish a new margin protection program (MPP) for dairy producers no later than September 1, 2014. Although the dairy provisions of the 2014 farm bill provide important structure and direction concerning the application of the new programs, substantial detail concerning the actual functioning of the new programs is contained in the USDA implementation regulations. The final regulations for both the MPP and DPDP were released on August 29, 2014, and the enrollment period began on September 2, 2014, at which point both new dairy programs became operational.[12]

Defining the Margin

MPP is a voluntary program intended to provide milk producers with protection from low operating margins. A key aspect of the MPP is creating a timely and transparent measure of an average dairy-production operating margin that will be useful across all dairy production regions. For MPP purposes, the operating margin is defined as the difference between the farm-level price of a hundred lbs. of milk—referred to as hundredweight or cwt. of milk—and the cost of an average feed ration necessary to produce a cwt. of milk. To construct this margin, MPP will use USDA-reported monthly national average price data for all classes of milk (called the all-milk price) and for the three principal feeds that represent the bulk of purchased feeds in dairy rations (corn, soybean meal, and alfalfa hay) to construct an estimate of the operating margin (see box below).

MPP Eligibility

All U.S. dairy producers are eligible to participate in the margin protection program.[13] If a dairy operation consists of more than one dairy producer, all of the dairy producers shall be treated as a single dairy producer for purposes of participation in the margin protection program.[14] If a dairy producer operates two or more dairy operations, each dairy operation shall separately register to participate in the margin protection program. Participating dairy producers are prohibited from reconstituting a dairy operation for the purpose of capturing payments under MPP.

[12] Federal Register, Vol. 79, No. 168, Friday, August 29, 2014, p. 51453 (7 C.F.R. Part 1430).

[13] If a foreign person or entity owns any or all of the dairy operation, that share is disqualified from participating.

[14] In other words, multiple owners must agree to the same MPP coverage terms.

Calculating the "Margin"

Actual Dairy Production Margin (ADPM) = Milk Returns over Feed Costs

The ADPM is defined as the difference between the monthly national average "all-milk" farm price and an average, formula-derived monthly value for the cost of a representative dairy feed ration.[15]

Margin per cwt. = (All-Milk Price per cwt.) – (Feed Cost per cwt.)[16]

Weighted Feed Cost Formula

The average price paid for feed used by a nationally representative dairy operation to produce a cwt. of milk is based on price data for the three major feed ingredients—corn, soybean meal, and alfalfa hay. Monthly price data for these three feedstuffs are combined into a weighted feed cost estimate per cwt. of milk production using the following formula.[17]

Feed Cost per cwt. = (1.0728 x corn price) + (0.00735 x soybean meal price) + (0.0137 x alfalfa hay price)

where the corn price is in $/bushel and the soybean meal and alfalfa hay prices are in $/ton.

MPP Is a National Average

It is important to note that the MPP is calculated as a national average margin. All participating dairy operations will face the same national ADPM estimate, irrespective of their individual circumstances. Thus, the MPP does not guarantee an individual producer's margin. Instead, it is assumed that each producer's margin will vary in a way that is correlated with the national average.[18] This formulation is used, in part, because the data are both transparent and readily available at the national level, thus facilitating its routine and timely calculation, and also because feed costs traditionally are the most variable component of dairy production operating margins.

The component mix of feed rations likely varies substantially across regions and individual dairy operations based on local pasture, feed preferences, and other conditions. In addition, important milk production costs are necessarily excluded from this formula, including labor, utilities, depreciation, capital, veterinary services, and nutritional supplements. Thus, this operating margin formula is a crude indicator of dairy profitability. To the extent that excluded operating cost items and relevant feed ration vary greatly across individual operations, this variation will likely be addressed by individual producers when determining their desired level of margin coverage.

The dairy operation must have commercial milk sales in the United States (or its territories) at the time of enrollment. Each participating dairy producer must be "actively engaged" in the dairy farm business. Participating dairy operations must certify compliance with two conservation provisions—highly erodible land conservation and wetlands conservation.

Signing Up for Margin Protection

The initial enrollment period of September 2, 2014, to November 28, 2014, covers, separately, both the last four months of the 2014 program year and the full 2015 program year. In future

[15] Monthly prices received by farmers for their milk, and the cost of their primary feedstuffs, corn, and alfalfa hay, are published monthly in *Agricultural Prices*, National Agricultural Statistics Service (NASS), USDA. The average wholesale price for soybean meal, another essential component of the dairy feed ration, Central Illinois, is reported in *Market News,* Agricultural Market Service (AMS), USDA.

[16] If the ADPM calculation produces a negative number, then the margin will be considered zero.

[17] The feed cost formula is intended to represent the dairy ration that would be consistent with recommended nutrition to pounds of milk including the dairy cow and the herd complement of dry cows, hospital cows and youngstock at the average U.S. milk yield per cow. For a detailed description of the feed cost formula derivation, see *Foundation for the Future*, NMPF, June 2010, pp. 16-19; at http://www.futurefordairy.com/.

[18] This differs from the LGM-D program which offers similar margin insurance, but it allows the producer to select different quantities of two feeds: corn and soybean meal. In addition, LGM-D uses the Federal Order Class III futures price reported on the Chicago Mercantile Exchange, and not the USDA-NASS reported U.S. All-Milk price.

years, the registration period will run from July 1 through September 30. To participate in MPP for any given year, each dairy operation must sign up and pay an annual registration fee of $100.[19] The administrative fee is due by the end of the enrollment period. Failure to pay the fee precludes the operation from receiving any payments under the program until any outstanding fee has been paid.

Participation in MPP is voluntary. However, once a dairy operation is enrolled in the MPP, it is in the program through 2018 unless there is some change in ownership, including both who is the owner and what share of the operation they own. The operation may defer enrolling until a later year, but once enrolled it must participate for each remaining year through 2018—the exception would be if the producer retires or dies, or the dairy operation is dissolved. As a result, a participating dairy operation is committed to paying at least the minimum $100 annual administration fee for each year in the program.

At the initial sign-up, each dairy operation must complete Form CCC-781 to establish its identity, eligibility, and production history (see box below).

Production History (PH)

At the initial sign up, the annual milk production history (**PH**) of a participating operation is defined as the highest annual milk marketings of the dairy operation during any one of the three calendar years 2011, 2012, or 2013. Special provisions are made for new dairy operations that were not yet in operation for a full year during the 2011 to 2013 period. These dairy operations may choose between two methods to extrapolate their available production history to a 12-month equivalent: Option 1—they base the extrapolation on the volume of actual milk marketings for the months that the dairy operation has been in operation using a monthly production index calculated by USDA; or Option 2—they use an estimate of their annual milk marketings based on the farm's actual milking herd size and the national average yield data published by USDA.

In subsequent years (i.e., 2014 and beyond), USDA shall adjust each participating farm's PH to reflect any increase in the national average milk production. This allows an operator's margin protection coverage potential to grow with the national average. If an individual farm expands its milk production more rapidly than the national average increase, then that portion of his expanded milk production that is in excess of the national average increase will not be eligible for coverage under MPP. Also, producers who do not enroll until later years will forego any adjustments that occur prior to their first year of enrollment.

Choosing a Margin Protection Coverage Level

Once CCC-781 is submitted and approved, and the $100 administration fee has been paid, the dairy operation is considered enrolled in the $4/cwt. margin protection level with a 90% coverage level—referred to as Catastrophic Coverage. This is the minimum (or default) protection level for a dairy operation. Dairy producers may, on an annual basis, change their MPP coverage level (see box below). Every participating dairy operation has the annual choice of selecting both higher margin protection levels up to $8/cwt. and PH coverage in a range from 25% to 90%. Higher coverage levels must be paid for with premiums (described below) that vary based on the CPH and producer-selected margin threshold.

[19] USDA is instructed to use the fees collected under MPP to cover administrative costs incurred in carrying out the program.

Margin Protection Options Under MPP

Margin Protection Level and Coverage Level

Under MPP, each year a participating producer may select both the margin protection level, which ranges from $4.00/cwt. to $8.00/cwt. in $0.50/cwt. increments, and the coverage level or portion of the farm's PH that the producer wants to protect, ranging from 25% to 90% in 5% increments. If no selection is made by a participating producer, then his coverage level reverts to the Catastrophic Coverage default of $4/cwt. at 90% PH.

The ADPM, PH, margin protection level ($4/cwt. to $8/cwt.), and coverage level (25% to 90%) are used jointly to determine when a MPP payment is made; what the payment total will be for a participating dairy operation; and what the annual premium or cost will be for the selected coverage levels (see description below on payments and premiums).

Covered Production History (CPH)

By applying the producer-selected coverage level to the operation's PH, each operation's covered production history (CPH) is obtained. The CPH is a critical variable in determining the applicable premium rates and total premium fees that each operation must pay to participate.

CPH = (Selected Coverage %) * (PH)

If producers want to register for a higher coverage level, they must do so during the enrollment period using Form CCC-782. Failure to successfully submit CCC-782 during the enrollment period results in margin protection equal to the default Catastrophic Coverage of a $4/cwt. margin threshold at 90% PH coverage.

Periodicity of Margin Calculations

Consecutive Two-Month Periods

For purposes of evaluating when a margin payment has been triggered and, if so, the amount of the payment, the ADPM is calculated in specific two-month periods. Each calendar year is broken into the following two-month periods: January-February, March-April, May-June, July-August, September-October, and November-December.

Note that a low single-month average margin does not trigger a margin protection payment if the two-month average is above the trigger. For example, assume a producer has selected a $6.00 margin threshold. Then a January margin of $5.80/cwt. followed by a February margin of $6.30/cwt. produces a two-month average of $6.05/cwt., which would fail to trigger the margin threshold.

One-Month Period Average Margins

Average margins are calculated for one-month periods for purposes of evaluating whether a Dairy Product Distribution Program (DPDP) threshold has been triggered (described in detail below). DPDP purchases and distributions are triggered when the ADPM average is less than $4.00/cwt. for two consecutive months.

No Cap or Limit on Participation

Unlike the MILC program, where payments each fiscal year were limited to the first 2.985 million lbs. of milk for producers with an adjusted gross income (AGI) under $500,000, participation in the MPP has no explicit cap related to a producer's AGI or the size of a dairy operation—in other words, there is no production or dollar payment limitation associated with the dairy margin program. Instead, margin protection payments would be limited by how much of a producer's historical milk marketings are covered by the program (i.e., the CPH).

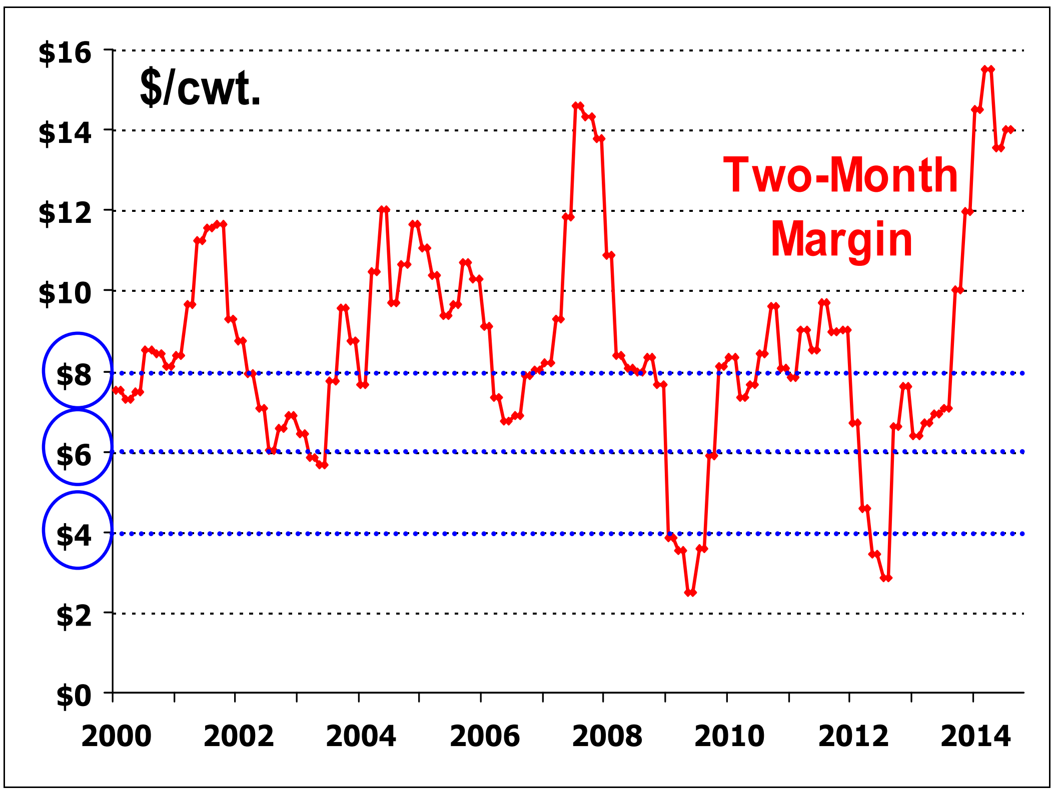
Producers who sign up for MPP are ineligible to sign up for the Livestock Gross Margin for Dairy Cattle program (LGM-D) offered by USDA's Risk Management Agency (RMA).[20] Producers may complete pre-existing LGM-D contracts at the time of their first enrollment; however, they will not be allowed to receive an MPP payment until their LGM-D contract is completed.

Timing of Payments

USDA is instructed to determine the ADPM as soon as possible after the necessary prices are reported in order to expedite the payments. However, NASS full-month price estimates—not preliminary estimates—must be used for both months in calculating the two-month average. As a result, the two-month average margin calculation will not be available until a full month after the two-month period has expired. For example, the January-February ADPM will not be available until the end of March when USDA's *Agricultural Prices* report is issued with full-month, farm-prices-received estimates for February. Thus, if an MPP payment is triggered by the January-February ADPM, the payment will not begin until April.

If a producer is in arrears on payment of administration fees and/or premiums for higher coverage levels (described below), then no payment will be made.

Figure 3. Historical Dairy Operating Margin: (All-Milk Price) Less (Avg. Feed Cost)



Source: Margin (national average all-milk price minus average cost of feed ration) calculated by CRS using USDA data (*Agricultural Prices*, August 28, 2014) and based on the two-month periods: Jan.-Feb., Mar.-Apr., May-June, July-Aug., Sept.-Oct., and Nov.-Dec.

[20] For more information on the LGM-D insurance program, see http://www.rma.usda.gov/pubs/rme/lgmdairy.pdf.

MPP Payments

Whenever the calculated Actual Dairy Production Margin (ADPM) falls below the selected MPP margin threshold for a consecutive two-month period, a payment will be made on the selected coverage-level portion of a participating producer's PH—referred to as the covered production history or CPH. The MPP payment rate per cwt. is equal to the difference between the selected MPP threshold and the average ADPM as calculated for that two-month period.

MPP Payment Rate per cwt. = (Selected MPP Threshold) – (2-month average ADPM)

Each two-month period is assigned an equal share of a participating producer's CPH—since there are six periods, each share will be equal to CPH/6. To determine the total MPP payment for a specific two-month period, the MPP payment rate times the coverage percent is applied to the producer's CPH, but prorated to a two-month period (i.e., CPH divided by six).

MPP Total Payment per period = (MPP Payment Rate) * (CPH/6)

MPP payments will continue as long as the ADPM is less than the selected MPP margin threshold for consecutive two-month periods. MPP payments cease when the ADPM reaches or exceeds the selected MPP margin threshold for a two-month period.

Example of MPP Payment Calculation

Suppose that for a particular two-month period the average all-milk price is $20.00/cwt. and the formula-determined feed ration per cwt. is $15.50, such that the ADPM is $4.50/cwt. Consider a dairy producer that traditionally has about 500 cows in his operation, but that is slowly expanding. The producer has selected a $6.50/cwt. MPP margin threshold with a 90% coverage level. Assume his PH is 12 million lbs. (or 120,000 cwt.). The covered production history for a single two-month period is:

CPH/6 = [(120,000 cwt.) * (90%)]/6 = 18,000 cwt.

The MPP payment for the two-month period would be based on the difference between the selected $6.50 margin threshold and the lower ADPM:

MPP Payment Rate per cwt. = $6.50 - $4.50 = $2.00

The MPP payment for the two-month period equals the payment rate times the CPH:

MPP Payment = ($2.00) * (18,000 cwt.) = $36,000

Note that the MPP payment example is for a specific two-month period and would have to be recalculated for each succeeding two-month period based on any changes in the average margin. MPP payments would continue as long as the two-month ADPM is less than the selected MPP margin level. These two-month payments are in contrast to the annual administrative fee and the MPP premium, which are only paid once in a year.

Likelihood of an MPP Payment

The historical frequency of the average margin levels (**Table 1**) provides information concerning the likelihood of future payments at different margin thresholds. Using ADPM estimates for successive two-month periods since January 2000, the ADPM has been below $4/cwt. in about 7% of the two-month periods and above $8/cwt. in 58% of the periods. Margins within the $6/cwt. to $8/cwt. range occurred in about 30% of the two-month periods. During this same period (January 2000 to March 2014), the national average ADPM was $8.61/cwt. Thus, the maximum MPP coverage level of $8.00/cwt. represents 93% of the national average ADPM.

See **Figure 3** for a depiction of how often the monthly margin would have fallen below the $8.00/cwt., $6.00/cwt., and $4.00/cwt. thresholds since January 2000.

Table 1. Margin Distribution, January 2000 through August 2014

Margin Range	Number of Months	Share (%)
Margin < $4.00	12	6.8%
$4.00 ≤ Margin < $6.00	8	4.5%
$6.00 ≤ Margin < $8.00	54	30.7%
Margin > $8.00	102	58.0%
Total	**176**	**100%**

Source: CRS calculations, using USDA data and based on the two-month period margins (Jan.-Feb., Mar.-Apr., May-June, July-Aug., Sept.-Oct., and Nov.-Dec.), as described in the box entitled, "Milk Production Coverage Under Margin Protection," where Margin per cwt. = (All-Milk Price per cwt.) – (Feed Cost per cwt.).

MPP Premiums

Participating producers must pay premiums that start at the $4.50/cwt. margin protection level and rise with higher coverage levels up to the $8.00/cwt. maximum. No premium is charged for the minimum $4.00/cwt. margin protection. The premium schedule also differentiates based on the level of covered production history (CPH). A substantially lower premium schedule is used for the first 4 million lbs. of CPH (**Table 2**). In addition, a special 25% discount is available for premiums on the first 4 million pounds of CPH during each of calendar 2014 and 2015.

The premium rate differential based on APH is significant because, in 2011, approximately 88% of U.S. dairy farms had annual milk production of 4 million lbs. or less, and they produced about 25% of total U.S. milk volume.[21]

Annual premiums are calculated as the product of the premium rate per cwt. (from **Table 2**) and the coverage production history (CPH).

MPP Premium = (Premium Rate) * (CPH)

[21] Farm-size shares are from "Farms, Land in Farms, and Livestock Operations," NASS, USDA, February 17, 2012, and total milk production is from "Milk Production, Disposition, and Income," NASS, USDA, April 25, 2012.

Table 2. MPP Premium Rates per Hundredweight (cwt.) of CPH

All values are in $/cwt.

	1st 4M lbs. of CPH		CPH > 4M lbs.
Margin Protection Level	**Discounted Premium[a]**	**Premium**	**Premium**
$4.00	$0.000	$0.000	$0.000
$4.50	$0.075	$0.010	$0.020
$5.00	$0.01875	$0.025	$0.040
$5.50	$0.030	$0.040	$0.100
$6.00	$0.04125	$0.055	$0.155
$6.50	$0.0675	$0.090	$0.290
$7.00	$0.1625	$0.217	$0.830
$7.50	$0.225	$0.300	$1.060
$8.00	$0.475	$0.475	$1.360

Source: 2014 farm bill (P.L. 113-79; §1407).

Note: M = million; CPH = Covered Production History = (PH) * (selected Coverage %).

a. Premiums on the first 4 million lbs. are reduced by 25% during each of calendar years 2014 and 2015.

Thus, the premium rate varies with the volume of covered production history (CPH) of the participating dairy operation (i.e., whether it has greater or less than 4 million lbs. of CPH), and the level of margin protection selected (from $4.00/cwt. to $8.00/cwt. in $0.50/cwt. increments).

Premium Calculation Method

The CPH is split into two components—the first 4 million lbs., and the remaining CPH above 4 million lbs. Dairy producers with a CPH in excess of 4 million lbs. would be charged the lower premium rate on the first 4 million lbs. of CPH and the higher premium rate on the amounts of CPH above that.

Example of MPP Premium Rate Calculation

Suppose a dairy producer with an APH of 120,000 cwt. selects a $6.50/cwt. MPP margin protection level with a 70% coverage level. First, the APH is adjusted by the coverage level as:

CPH = APH * (coverage level) = (120,000 cwt.) * (70%) = **84,000 cwt**.

The annual premium will be calculated as follows.

For the first 4 million lbs. (or 40,000 cwt.) of CPH, use the MPP premium rate of $0.09/cwt.:

MPP Premium-1 = ($0.09) * (40,000 cwt.) = $3,600.

For CPH above the first 4 million lbs. (or 84,000 cwt. – 40,000 cwt.) use the MPP premium rate of $0.29/cwt.:

MPP Premium-2 = ($0.29) * (44,000 cwt.) = $12,760.

The **Total MPP Premium** is the sum: $3,600 + $12,760 = **$16,360**.

This MPP premium is in addition to the annual administrative fee of $100.

Premium payments may be paid in full by the end of the enrollment period, or they may be paid in tranches, with the first 25% of the total premium paid no later than February 1 of the relevant year, with the remaining premium balance paid no later than June 1 of the relevant year.[22] The 2014 farm bill states that a participating dairy operation that fails to pay its administrative fee and/or premiums remains legally obligated for such charges, and may not receive any payments under MPP until such charges are fully paid.

Margin Coverage Distinction: $6.50/cwt. vs. $7.00/cwt.

Separately, it is worth noting that the premium structure strongly encourages participation at the $6.50/cwt. level for CPH greater than 4 million lbs. To raise the margin coverage level an additional $0.50/cwt. (from $6.50/cwt. to $7.00/cwt.), an additional $0.54/cwt. of premium must be paid (i.e., $0.83/cwt. - $0.29/cwt.). The total premium cost for insuring 70% of the APH of 120,000 cwt. at a margin of $7.00/cwt. for the same hypothetical scenario would be $40,120—more than double the premium cost of $16,360 for $6.50/cwt. margin protection.

The Dairy Product Donation Program (DPDP)

According to the 2014 farm bill, USDA shall establish and administer a Dairy Product Donation Program (DPDP) to (1) address low dairy operating margins, and (2) provide nutrition assistance to individuals in low-income groups.

A result from the dairy policy debate that preceded the final 2014 farm bill (see **Appendix**) was as follows. It is generally agreed that dairy operating margins are low when the equilibrium between milk supply and demand is out of balance with supply exceeding demand. The original proponents of the dairy margin program had argued that an additional policy feature—a supply disincentive component—should be added that would work to reduce supply and bring the milk supply-demand equation back into balance at a higher margin. Opponents of this concept argued that the government should not manage supplies, but should instead work to enhance demand to rebalance the milk supply and demand. This latter argument won out in conference when conferees proposed an entirely new "demand enhancing" program—DPDP.

DPDP Program Activities

USDA must announce and undertake DPDP activities whenever the actual dairy production margin (ADPM) is $4.00/cwt. or less for each of the immediately preceding 2 months.[23] When DPDP has been triggered, USDA must immediately purchase dairy products, at prevailing market prices, until such time as one of the termination conditions (described below) is met.

[22] According to the August 29 final rule, participating producers must pay at least 50% of the premium (plus the administrative fee) by the end of the enrollment period; however, USDA officials have indicated that this was felt to be onerous, and it has been revised to at least 25% payment by February 1, as indicated in the text. USDA, *Notice MPP-3*, "Announcing Registration and Coverage Election Period for 2014 and 2015 Margin Protection Program for Dairy Producers," August 28, 2014.

[23] Note that this is not the two-month average ADPM, but rather the ADPM for each of two consecutive months.

USDA must consult with public and private nonprofit organizations—organized to feed low-income populations—in order to determine the types and quantities of dairy products to purchase under the DPDP. USDA must distribute, not store, the purchased dairy products. USDA is directed to use the funds, facilities, and authorities of the Commodity Credit Corporation (CCC) to implement and administer the DPDP.

DPDP Distribution of Purchases

The 2014 farm bill directs USDA to distribute, but not store, the dairy products purchased under DPDP so as to encourage greater domestic consumption by diverting them to persons in low-income groups as determined by USDA. USDA shall use public and private nonprofit organizations for distribution of DPDP dairy products to provide, without cost or waste, nutrition assistance to individuals in low-income groups. DPDP purchases are expected to be made in package sizes suitable for immediate household use, to best accommodate the immediate distribution requirement of the 2014 farm bill. Any organization receiving dairy products under the DPDP may not sell the products back to commercial markets.

DPDP Program Termination Conditions

USDA must terminate its DPDP activities whenever any one of the following conditions occurs.

1. After three consecutive months of purchases, the DPDP purchases are required to cease, even if the **margin remains < $4.00/cwt.**, until there have been at least two more consecutive months of margins below $4.00/cwt.
2. If the **margin is > $4.00/cwt.** for the preceding month, DPDP purchase activities must cease until the original requirements (i.e., margin < $4.00/cwt. for two consecutive months) are met again.
3. USDA will stop making DPDP purchases, even if the **margin remains < $4.00/cwt.**, if the U.S. price for dairy products is significantly above world market prices. In particular:
    a. USDA will stop making DPDP purchases, when **$3.00/cwt. < margin < $4.00/cwt.** for the preceding month and either:
        i. the U.S. cheddar cheese price > 105% of world price, or
        ii. the U.S. non-fat dry milk price > 105% of world price; or
    b. USDA will stop making DPDP purchases, when the **margin < $3.00/cwt.** for the preceding month and either:
        i. the U.S. cheddar cheese price > 107% of world price, or
        ii. the U.S. non-fat dry milk price > 107% of world price.

The 2014 farm bill gives USDA the latitude to determine which domestic and international prices of cheddar cheese and non-fat skim milk powder will be used to assess the DPDP termination conditions. If DPDP purchases are suspended due to domestic prices being sufficiently above world prices, margins would be tracked for the next two months, and purchases could resume after three months if conditions permit.

Budget Outlays: Historical and Projected

USDA outlays for the major dairy support programs have trended downward since the 1980 farm bill period (**Table 3**). An outlook for strong dairy product prices for the next several years in the CBO May 2013 baseline accounts for the relatively small net outlay projections of $161 million over 5 years (FY2014-FY2018) and $250 million over 10 years (FY2014-FY2023) for the major dairy programs, assuming an extension of dairy policy as it existed under the 2008 farm bill.

Table 3. U.S. Dairy Programs, Historical and Projected USDA Outlays

($ millions)

Farm Bill	Fiscal Years	DPPSP	Market Loss Assistance	MILC	DEIP	Total
1980	FY1981 - FY1985	10,592	—	—	—	10,592
1985	FY1986 - FY1990	6,221	—	—	8	6,229
1990	FY1991 - FY1996	1,388	—	—	544	1,932
1996	FY1997 - FY2002	2,284	1,000	—	481	3,765
2002	FY2003 - FY2007	1,120	—	2,538	90	3,748
2008[a]	FY2008 - FY2012	280	290	1,091	28	1,688
CBO 5-year Projections for FY2014-FY2018						
CBO Baseline[b]	FY2014 - FY2018	27	11	99	25	161
P.L. 113-79	FY2014 - FY2018	—	—	—	—	+241
CBO 10-year Projections for FY2014-FY2023						
CBO Baseline[b]	FY2014 - FY2023	47	18	140	45	250
P.L. 113-79[c]	FY2014 - FY2023	—	—	—	—	+912

Sources: Historical data are assembled by CRS using various USDA data sources; projected data for FY2014-FY2023 are from the Congressional Budget Office (CBO), May 2013 Baseline for Farm Programs, May 14, 2013.

Notes: USDA's Commodity Credit Corporation total outlays do not include the implicit costs to consumers of tariff-rate quotas which limit access to cheaper international products. Also, there are no federal outlays for FMMOs other than for their administration.

a. Data for FY2012 are not final, while FY2013 data are not complete and have been excluded from this table.

b. Projections from the CBO May 2013 baseline, assuming continuation of current law.

c. CBO cost estimates of the effects on direct spending and revenues of the conference agreement on H.R. 2642, the Agricultural Act of 2014, as reported on January 27, 2014, as scored against CBO's May 2013 baseline. See CBO letter to Chairman Frank Lucas, Committee on Agriculture, U.S. House of Representatives, January 28, 2014.

According to CBO, replacing current dairy policy with the new dairy programs of the 2014 farm bill will result in projected additional budgetary outlays above baseline over the 5-year (FY2014-FY2018) and 10-year (FY2014-FY2023) periods of $241 million and $912 million, respectively, under the Agricultural Act of 2014 (P.L. 113-79).[24] In other words, the total 5-year and 10-year

[24] See CBO letter to Chairman Frank Lucas, Committee on Agriculture, U.S. House of Representatives, January 28, 2014.

outlays projected by CBO under the new dairy programs are $402 million and $1.162 billion, respectively, thus continuing the downward trend in program outlays per farm bill period.[25]

Dairy Issues

Because the MPP and DPDP are new programs that differ notably from previous support programs, several questions have been raised concerning their implementation and potential cost, as well as their effect on U.S. and international dairy markets and consumers. History provides some indications but solid evidence will likely only emerge with implementation. Some of the more noteworthy related issues are briefly discussed here.

1. Will DPDP Activities Supplement or Offset Commercial Sales?

As Bozic et al (2014) have noted:[26]

> The fundamental question is whether or not the end-users of donated products would have purchased them on commercial markets anyway. If these donations are strictly additive to total dairy usage then the amount of dairy products served in Food Banks or other settings is increased. If the donation displaces commercial purchases that would have been made with other cash resources, then total commercial sales of dairy products would actually decline.
>
> To the extent that these donations are going to programs that have limited resources and continuously unmet needs, it is not unreasonable to speculate that commercial displacement will be minimal.

2. Will MPP Work as a Safety Net? If So, With What Consequences?

Economic analysis indicates that, by focusing on the national average milk operating margin rather than strictly on the price of milk and offering a range of margin protection and coverage choices, U.S. dairy producers, regardless of their geographic location or management style, will be provided with substantial opportunity to manage their milk-production risk environment under the new dairy programs.[27]

Another related, but unanswered question is, if MPP is effective as a safety net, will its subsidized premiums crowd out private sector risk markets?

3. Will Production Incentives Result from MPP and DPDP?

The margin protection program will likely have a risk reduction effect, and the fixed premium structure likely has a significant federal subsidy component embedded in it—although the actual extent of implicit subsidy has yet to be assessed. This combination can be expected to provide some degree of production incentives to participating milk producers.

Overly strong production incentives can disrupt the traditional market signals that lead to reduced milk production via herd culling.[28] Furthermore, MPP provisions could inadvertently result in a policy framework that gives advantage to "lumpy" over "incremental" growth at the farm level as

[25] These estimates are the sum of the baseline score (which assumed a continuation of the 2008 farm bill) and the additional cost attributable to the new dairy programs 2014 farm bill.

[26] M. Bozic et al. "The Dairy Subtitle of the Agricultural Act of 2014," PDMP Information Letter 14-01, Jan. 31, 2014.

[27] John Newton and Cam Thraen, "The Dairy Safety Net Debate of 2013 Part III: The Compromise Dairy Safety Net Solution," *farmdocdaily.com*, Dept. of Agr. and Cons. Econ., Univ. of Illinois Urbana-Champaign, Feb. 12, 2014.

[28] M. Bozic et al. "The Dairy Subtitle of the Agricultural Act of 2014," PDMP Information Letter 14-01, Jan. 31, 2014.

producers may choose to respond by starting new dairy operations at new locations to be able to enroll new milk production in the MPP.

The nature by which DPDP will be implemented and its subsequent effect on dairy markets is unknown at present. Will DPDP act as a catalyst for further milk production by artificially inflating the true underlying demand for dairy products, thus encouraging greater milk production and leading to lower prices and higher program payments down the road?

Unlike early versions of the Dairy Security Act—the precursor to the dairy subtitle contained in the 2014 farm bill—which contained a strong production disincentive component in the form of the proposed Supply Management Program, MPP has only a mild disincentive in the form of its exclusion of new milk production in excess of the national average milk production growth rate. If producers act in unison to expand production beyond normal annual growth rates, even that milk restriction is minimized.

4. Can the MPP Program be Gamed by Participants?

MPP does not follow sound insurance principles—premiums are not set to reflect the risk environment in milk and feed markets but instead are fixed over the life of the farm bill. This fixed premium structure combined with the ability of the producer to annually choose a margin insurance level creates incentives to adversely game the program to one's financial advantage.[29]

Publicly available information on futures contract prices from the Chicago Mercantile Exchange for milk and feed can be used to forecast near-term milk production margins that, in turn, indicate the probability of indemnity payments under various MPP coverage levels. As a result, strong adverse gaming incentives exist for participants in the MPP. Economic analysis suggests that the adverse gaming incentives can be reduced or mitigated by specifying an earlier sign-up date for coverage decisions—for example, 60 to 90 days ahead of each year's program starting date of January 1.[30] The initial enrollment unavoidably falls within this range; however, the enrollment period of July 1 to September 30 for the out years 2016, 2017, and 2018 meets the 90-day threshold.

5. How Will MPP Payments Be Distributed Across Farm Sizes?

Economic analysis suggests that, under the fixed premium structure of the 2014 farm bill—with strong differentiation between premiums on the first 4 million lbs. and on marketings above 4 million lbs.—net expected benefits under MPP will closely align with those under the previous MILC program, but with slightly less skewed results. Farms with fewer than 100 cows would receive approximately 38% of the expected benefits (compared with 39% under MILC), while farms with over 1,000 cows would account for approximately 15% of benefits (compared with 9% under MILC) during low margin periods. Furthermore, the same analysis concluded that, "only when higher coverage levels are deep in-the-money will payments per cwt. be more consistent across farm sizes and result in the distribution of net benefits following closely to the distribution of milk production."[31]

[29] Ibid.

[30] Ibid.

[31] Ibid., p. 3.

6. What Are the Trade Implications of MPP and DPDP?

The 2014 farm bill dairy provisions made several changes that have profound implications for U.S. and international trade agreements. First and foremost, by repealing the Dairy Product Price Support Program (DPPSP) and the Dairy Export Incentive Program (DEIP), U.S. dairy programs have made a significant step in better complying with its domestic support commitments under the World Trade Organization (WTO).

During the 17-year period from 1995 through 2011 (the most recent year for which notification data is available), the implicit program costs of DPPSP have represented the single largest U.S. domestic support outlay of any single program commodity accounting for $93.5 billion ($5.5 billion annually) or 39% of all U.S. amber box domestic support notifications to the WTO.[32] Thus, the repeal of DPPSP is likely to have a substantial effect in lowering annual U.S. domestic support notifications to the WTO, and keeping U.S. domestic support outlays well below the United States' $19.1 billion ceiling.[33]

It is not yet clear how USDA will notify program outlays under MPP and DPDP—for example, possibly as amber box but exempt under the *de minimis* exclusion—but current CBO spending projections of about $1.2 billion over 10 years or about $120 million per year pale in comparison with the DPPSP's annual average notification of $5.5 billion. In addition, repeal of DEIP fulfills a general commitment by WTO members to end use of agricultural export subsidies, and brings greater pressure to bear on the European Union, Switzerland, Norway, and the rest of the world to act similarly.

Finally, U.S. dairy TRQs remain in place but are WTO legal as they were included in the original U.S. country schedule of tariffs and quotas that was approved and accepted by all WTO-member countries.

Given the very favorable market conditions for the U.S. dairy sector with near record high milk prices in 2014 coupled with prospects for relatively low feed costs, it is expected that market incentives will dominate producer decision making for the foreseeable future.

Conclusion

The answers to these questions may emerge only slowly. The new MPP and DPDP programs are likely to be implemented during a period of sustained strong milk prices, moderate to weak feed costs, and sustained large margins that, if realized, would minimize the impact of the new dairy programs (**Figure 3**).[34]

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[32] The dairy price support program notifications have been so large primarily because they have been measured by a formula that equals the difference between domestic support price of $9.90/cwt. and a world market price of $7.25/cwt. (which was fixed at the 1994 value as part of the original WTO agreement) times annual U.S. milk production; but not by how much in federal budgetary outlays were spent to support domestic milk prices.

[33] For more information, see CRS Report RS20840, *Agriculture in the WTO: Limits on Domestic Support*.

[34] For recent long-term dairy market projections, see Food and Agricultural Policy Research Institute (FAPRI), "U.S. Baseline Briefing Book", FAPRI-MU Report #02-14, March 13, 2014; at http://www.fapri.missouri.edu/.

Appendix. Debate Behind the New MPP and DPDP

As mentioned earlier in the text ("Origins of the New Dairy Policy"), a version of the National Milk Producers Federation's (NMPF's) Feed the Future (FTF) proposal was introduced in the 112th Congress as H.R. 3062, The Dairy Security Act (DSA), by House Agriculture Committee Ranking Member Collin Peterson on September 23, 2011. A modified version of DSA appeared as "Subtitle D—Dairy," in Title I of both the House-reported (H.R. 6083) and Senate-passed (S. 3240) farm bills of the 112th Congress.

Dairy Policy in the 113th Congress

In the 113th Congress, both the Senate and the House passed different farm bills (S. 954, passed by the Senate on June 10, 2013, and H.R. 2642, passed by the House on July 11, 2013) that proposed replacing the traditional set of dairy price and income support programs with a new margin-based income support program—called the Dairy Production Margin Protection Program (DPMPP) under S. 954, and the Dairy Producer Margin Insurance Program (DPMIP) under H.R. 2642. The two proposed margin programs were similar in many respects; however, the Senate bill (but not the House bill) also included an accompanying market stabilization program—the Dairy Market Stabilization Program (DMSP), which, under certain conditions, would reduce payments to participating producers for their milk marketings when the margin falls below proposed statutory thresholds.[35]

Early versions of the House farm bill in the 113th Congress also included the DMSP as part of new dairy policy. However, during the House Agriculture Committee's markup of its first version of the 2013 farm bill (H.R. 1947) in May 2013, an amendment (H.Amdt. 228) was introduced by Representatives Goodlatte and Scott that proposed removing the DMSP from H.R. 1947 and making some minor adjustments to DPMPP. The Goodlatte-Scott amendment (GSA) was defeated in committee by a vote of 28 to 26. The amendment was reintroduced during the House floor debate of H.R. 1947 and passed by a vote of 291-135 (May 15, 2013). However, the full House voted to reject the amended farm bill (195-234) on June 20, 2013. On July 11, 2013, the full House passed (by a vote of 216-208) a second version of the 2013 farm bill (H.R. 2642) which included the Goodlatte-Scott amendment—thus removing DMSP and replacing DPMPP with DPMIP.

Conference Committee Resolves Differences

The differences between the Senate- and House-passed farm bills were resolved when conferees reported a conference agreement on January 27, 2014 (the Agricultural Act of 2014, H.R. 2642/H.Rept. 113-333). The dairy supply management debate was resolved when the conferees included an entirely new program—the Dairy Product Distribution Program (DPDP)—focused on demand enhancement, rather than supply control. Prior to the conference, the dairy debate had been limited to whether a supply management component should be included in the final bill—the concept of a DPDP did not emerge until conference. The full House and Senate approved the conference agreement on January 29 and February 4, respectively, and the President signed the measure into law on February 7, 2014 (P.L. 113-79).

[35] For a detailed discussion of differences in dairy provisions between the House-passed H.R. 2642 and the Senate-passed S. 954, see CRS Report R42736, *Dairy Policy Proposals in the Next Farm Bill*.

Table A-1. Title I, Subtitle D- Dairy: Comparison of 2014 Farm Bill With Prior Law

Prior Law/Policy—Dairy	Enacted 2014 Farm Bill (P.L. 113-79)
Dairy Programs	
Repeal or Reauthorization of Dairy Programs	
Dairy Product Price Support Program. Mandates the direct support of cheese, nonfat dry milk, and butter at specified prices for five years (through December 31, 2012). Specifies minimum purchase prices of: block cheese, $1.13/lb.; barrel cheese, $1.10/lb.; butter, $1.05/lb.; and nonfat dry milk, $0.80/lb (same levels previously used to support the farm price of milk at $9.90 per hundred lbs. or hundredweight (cwt.)) Allows USDA sale of acquired products when market prices rise to 110% of purchase price. Allows reduction of mandated purchase prices when USDA acquisitions exceed specified levels. Expired on December 31, 2013, following a one-year extension. ***[7 U.S.C. 8771]***	Repealed. ***[Sec. 1421]***
Milk Income Loss Contract (MILC) Program. MILC is a counter-cyclical payment program. When the monthly farm price of fluid milk falls below $16.94/cwt., all dairy farmers are paid an amount equal to 45% of the difference between $16.94 and the lower market price. Payments per farm are limited to the first 2.985 million lbs. of annual production. For the month of September 2013, the payment factor and the payment quantity were 34% and 2.4 million lbs., respectively. The $16.94/cwt. threshold price must be adjusted upward whenever feed costs are above $7.35/cwt. Beginning on September 1, 2013, the Nat'l. Avg. Dairy Feed Ration Cost trigger rises from $7.35/cwt. to $9.50/cwt. MILC program expired September 30, 2013. ***[7 U.S.C. 8773]***	**Milk Income Loss Contract (MILC) Program**. Although extended temporarily, MILC is repealed effective the earlier of: the date the new Margin Protection Program (MPP, see below) is operational or September 1, 2014. During the MILC extension period the payment rate shall be calculated using the pre-September 2013 parameters of 2.985 million lbs. for the payment limit, a $7.35/cwt. feed ration threshold, and a 45% rate as applied to both (1) the difference between the $16.94/cwt. threshold price (as adjusted by feed ration cost estimates) and the lower market price, and (2) the extent to which the national average dairy feed ration cost exceeds $7.35/cwt. to be used to adjust upward the $16.94/cwt. threshold price. ***[Sec. 1422]***
Dairy Export Incentive Program. Provides cash bonus payments to U.S. dairy exporters, subject to World Trade Organization obligations to limit export subsidies. Intended to counter foreign (mostly EU) dairy subsidies. Expired September 30, 2013. ***[15 U.S.C. 713a-14]***	Repealed. ***[Sec. 1423]***
Dairy Forward Pricing Program. Authorizes a dairy forward pricing program. Prices paid by milk handlers under the contracts are deemed to satisfy the minimum price requirements of federal milk marketing orders. Applies only to milk purchased for manufactured products (Classes II, III, and IV), and excludes milk purchased for fluid consumption (Class I). Expired on September 30, 2013. ***[7 U.S.C. 8772]***	Extended through FY2018. Allows for new contracts until September 30, 2018, but no contract can extend beyond September 30, 2021. ***[Sec. 1424]***
Dairy Indemnity Program. Authorizes payments to dairy farmers when a public regulatory agency directs removal of their raw milk from the market because of contamination by pesticides, nuclear radiation or fallout, or toxic substances and other chemical residues. Expired December 31, 2013. ***[7 U.S.C. 4501]***	Extended through FY2018. ***[Sec. 1425]***

Prior Law/Policy—Dairy	Enacted 2014 Farm Bill (P.L. 113-79)
Dairy Promotion and Research Program. The Dairy Producer Stabilization Act of 1983 authorized a generic dairy product promotion, research, and nutrition education program, funded by a mandatory $0.15/cwt assessment on milk produced/marketed in the 48 contiguous states. Importers in all 50 states, the District of Columbia, and Puerto Rico must also pay an assessment rate of $0.075/cwt. on the milk equivalent in imported dairy products. Authorizes USDA to issue regulations on time and method of importer payments. Expired September 30, 2013. ***[7 U.S.C. 4504]***	Extended through FY2018. ***[Sec. 1426]***
Inclusion of California as Separate Federal Marketing Order. Upon the petition and approval of California dairy producers in the manner provided in Section 608c of this title, the Secretary shall designate the state of California as a separate Federal milk marketing order (FMMO). The order covering California shall have the right to reblend and distribute order receipts to recognize quota value. USDA was required to announce any such proposed amendment to FMMOs by April 4, 1998, and to implement such amendment by April 4, 1999. ***[7 U.S.C. 7253(a)(2)]***	**Inclusion of Additional Order.** Adds a provision to remove the expiration date for USDA to act upon a petition from California dairy producers for designation as a separate FMMO. ***[Sec. 1410(d)]***
Federal Milk Marketing Order Review Commission. As established by the 2008 farm bill ***[Sec. 1509]***, the FMMO Review Commission is mandated to conduct a comprehensive review and evaluation of (1) FMMO system, and (2) non-FMMO systems.	Repealed. ***[Sec. 1427]***
Definitions	
No comparable provision.	**Actual Dairy Production Margin:** difference between all-milk price and average feed cost. ***[Sec. 1401(1)]***
No comparable provision.	**All-Milk Price:** the national average price received, per cwt. of milk, by dairy operations. ***[Sec. 1401(2)]***
No comparable provision.	**Average Feed Cost:** the average price paid for feed used by a dairy operation to produce a cwt. of milk, as determined by the formula—1.0728 x (corn price per bu.) + 0.00735 x (soybean meal price per ton) + 0.0137 x (alfalfa hay price per ton). ***[Sec. 1401(3)]***
No comparable provision.	**Consecutive 2-Month Period:** the six 2-month periods of Jan.-Feb., Mar.-Apr., May-June, July-Aug., Sep.-Oct., and Nov.-Dec. ***[Sec. 1401(4)]***
No comparable provision.	**Dairy Operation.** An individual or entity that shares in the risk of producing milk and contributes land, labor, management, equipment, or capital to the dairy operations. ***[1401(5)]***
No comparable provision.	**Calculation of Average Feed Costs:** Corn and alfalfa hay prices are monthly national average prices received as reported by USDA in *Agricultural Prices.* The soybean meal price is the monthly price for central Illinois as reported by USDA in *Market News*. ***[Sec. 1402(a)]***

Prior Law/Policy—Dairy	Enacted 2014 Farm Bill (P.L. 113-79)
No comparable provision.	**Calculation of Actual Dairy Production Margin**: The margin is calculated for each 2-month period as the difference between the 2-month average all-milk price and the 2-month average feed cost. ***[Sec. 1402b(1)],*** to be made as soon as practicable using the full-month price of the applicable reference month. ***[Sec. 1402(b)(2)]***
Margin Protection Program (MPP) for Dairy Producers	
No comparable provision.	**Establishment of Margin Protection Program (MPP) for Dairy Producers.** USDA shall establish a margin protection program for dairy producers no later than September 1, 2014. ***[Sec. 1403]***
	Duration: The margin protection program ends on December 31, 2018. ***[Sec. 1409]***
No comparable provision.	**Eligibility for MPP.** All dairy producers are eligible to participate. ***[Sec. 1404(a)]***
No comparable provision.	**Registration:** USDA shall specify the manner and form by which a participating dairy operation may register to participate in the margin program. ***[Sec. 1404(b)(1)]***
No comparable provision.	**Treatment of Multi-Producer Dairy Operations.** If a dairy operation consists of more than one dairy producer, all of the dairy producers shall be treated as a single dairy producer for purposes of participation in the margin protection program. ***[Sec. 1404(b)(2)]***
No comparable provision.	**Treatment of Producers with Multiple Dairy Operations.** If a dairy producer operates 2 or more dairy operations, each dairy operation shall separately register to participate in the margin protection program. ***[Sec. 1404(b)(3)]***
No comparable provision.	**Annual administration fee.** An annual administration fee of $100 is required per dairy operation participating in MPP. ***[Sec. 1404(c)(2)]***
No comparable provision. **LGM-D** is an insurance program, operated by USDA's Risk Management Agency, under the permanent authority of the Federal Crop Insurance Act, as amended (7 U.S.C. 1501 et seq.).	**Relationship to Livestock Gross Margin for Dairy Program (LGM-D):** A dairy operation may participate in either MPP or the LGM-D, but not both. ***[Sec. 1404(d)]***
No comparable provision.	**Production History.** At the initial registration, the production history is equal to the highest annual milk marketings of the dairy operation during any one of the 3 calendar years 2011, 2012, or 2013. In subsequent years, USDA shall adjust the production history to reflect any increase in the national average milk production. ***[Sec. 1405(a)]*** Special provisions are made for new dairy operations. ***[Sec. 1405(b)]***

Prior Law/Policy—Dairy	Enacted 2014 Farm Bill (P.L. 113-79)
No comparable provision.	**MPP Coverage Level Threshold and Coverage Percentage.** Dairy producers are offered the annual choice of purchasing margin insurance with coverage levels ranging in $0.50/cwt. increments from a minimum of $4.00/cwt. to a maximum of $8.00/cwt. A participating producer shall elect a coverage percentage available in 5% increments equal to not more than 90%, nor less than 25% of the **Production History** of the dairy operation. ***[Sec. 1406(a)]***
No comparable provision.	**MPP Payment Threshold.** A payment is made to participating dairy operations whenever the 2-month average actual dairy production margin is less than the coverage level threshold selected by the producer. ***[Sec. 1406(b)]*** **MPP Payment Rate.** The MPP rate equals the amount that the margin is below the selected margin coverage level threshold. The **MPP Total Payment** equals the payment rate x the selected coverage % x (APH/6). ***[Sec. 1406(c)]***
No comparable provision.	**Producer Premiums for MPP.** An annual premium must be paid, equal to the product of the selected coverage %, the production history, and the premium rate per cwt. of milk. ***[Sec. 1407(a)]*** The **MPP Premium Rate** schedule varies based on the scale of operations and the selected coverage %. **For the first 4 million lbs.** of milk marketings the premium per cwt. is $0.00 for $4.00 margin coverage; $0.01 for $4.50; $0.025 for $5.00; $0.040 for $5.50; $0.055 for $6.00; $0.09 for $6.50; $0.217 for $7.00; $0.30 for $7.50; and $0.475 for $8.00. For calendar 2014 and 2015, all of the preceding premiums (except the $8.00/cwt. coverage level) are reduced by 25%. ***[Sec. 1407(b)]*** **In excess of 4 million lbs.** the premium per cwt. is: $0.00 for $4.00; $0.020 for $4.50; $0.040 for $5.00; $0.10 for $5.50; $0.155 for $6.00; $0.29 for $6.50; $0.83 for $7.00; $1.06 for $7.50; and $1.36 for $8.00. ***[Sec. 1407(c)]***
No comparable provision.	**Time for Premium Payments.** USDA is instructed to provide more than one method of payment and to use a method that "maximizes dairy operation payment flexibility and program integrity." ***[Sec. 1407(d)]***
No comparable provision.	The premium is pro-rated for new dairy producers and may be waived in the case of death, retirement, permanent dissolution, or other circumstances as judged by USDA. ***[Sec. 1407(c)]***
No comparable provision.	**Failure to Pay Administrative Fees or Premiums.** A producer that fails to pay the administrative fee or premium remains legally obligated to pay and may not receive a MPP payment until all obligations are paid. USDA may take such action as necessary to collect any unpaid obligations. ***[Sec. 1408]***

Prior Law/Policy—Dairy	Enacted 2014 Farm Bill (P.L. 113-79)
Rulemaking Requirements. Standard rulemaking procedures generally require federal agencies to issue notices and take comments on proposed rules. ***[5 U.S.C. 553(b)]***	**Administration and Enforcement.** USDA is required to promulgate regulations to address administrative and enforcement issues in carrying out the margin protection program. ***[Sec. 1410(a)]*** **Reconstitution of Dairy Operation.** USDA is required to promulgate regulations to address administrative and enforcement issues and prohibit reconstitution of a dairy operation for the purpose of the dairy producer receiving margin protection payments. ***[Sec. 1410(b)]*** **Administrative Appeals.** USDA is required to promulgate regulations to provide for administrative appeals of USDA decisions that are adverse to participants of the margin protection program. ***[Sec. 1410(c)]***
Dairy Product Donation Program (DPDP)	
No comparable provision.	**Establishment of a Dairy Product Donation Program (DPDP).** No less than 120 days after the dairy margin protection program is operational, USDA shall establish and administer a DPDP to: (1) address low dairy operating margins, and (2) provide nutrition assistance to individuals in low-income groups. ***[Sec. 1431(a)]***
No comparable provision.	**DPDP Program Trigger.** USDA shall announce and undertake DPDP activities whenever the actual dairy production margin is $4.00/cwt. or less for each of the immediately preceding 2 months. ***[Sec. 1431(b)]***
No comparable provision.	**DPDP Program Activities.** When DPDP has been triggered, USDA shall immediately purchase dairy products, at prevailing market prices, until such time as one of the termination conditions is met. USDA shall consult with public and private nonprofit organizations organized to feed low-income populations in order to determine the types and quantities of dairy products to purchase under the DPDP. ***[Sec. 1431(c)]*** The funds, facilities, and authorities of the Commodity Credit Corporation shall be available to USDA to implement and administer the DPDP. ***[Sec. 1431(g)]***
No comparable provision.	**DPDP Program Termination.** USDA shall cease DPDP activities whenever any one of the following conditions occurs: (1) USDA has made DPDP purchases for three consecutive months, even if the margin remains ≤ $4.00/cwt.; (2) the margin > $4.00/cwt. for the preceding month; (3) when $3.00/cwt. < margin < $4.00/cwt. for the preceding month and either: (a) the U.S. cheddar cheese price > 105% of world price, or (b) the U.S. non-fat dry milk price > 105% of world price; or (4) the margin ≤ $3.00/cwt. for the preceding month and either: (a) the U.S. cheddar cheese price > 107% of

Prior Law/Policy—Dairy	Enacted 2014 Farm Bill (P.L. 113-79)
	world price, or (b) the U.S. non-fat dry milk price > 107% of world price. For this section, USDA shall determine the domestic and international prices of cheddar cheese and non-fat skim milk powder. ***[Sec. 1431(d)]***
No comparable provision.	**Distribution of DPDP Purchases.** USDA shall distribute, but not store, the dairy products purchased under DPDP so as to encourage domestic consumption by diverting them to persons in low-income groups as determined by USDA. USDA shall use public and private nonprofit organizations for distribution of DPDP dairy products to provide, without cost or waste, nutrition assistance to individuals in low-income groups. ***[Sec. 1431(e)]*** Any organization receiving dairy products under the DPDP may not sell the products back to commercial markets. ***[Sec. 1431(f)]***
No comparable provision.	**DPDP Duration.** The DPDP shall end on December 31, 2018. ***[Sec. 1431(h)]***

Source: Title I- Commodities; Subtitle D—Dairy, The Agricultural Act of 2014; P.L. 113-79.

Notes: For a comparison of prior and enacted law with the provisions in the House and Senate versions of the 2014 farm bill (i.e., the Senate-Passed S. 954 and the House-Passed H.R. 2642) see CRS Report R43076, *The 2014 Farm Bill (P.L. 113-79): Summary and Side-by-Side.*

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