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DEPARTMENT OF AGRICULTURE

Agricultural Marketing Service

7 CFR Parts 1140 and 1145

[Docket No. AMS-DA-08-0031; DA-08-05]
RIN 0581-AC86

Dairy Forward Pricing Program

AGENCY: Agricultural Marketing Service, USDA.

ACTION: Final rule.

SUMMARY: This final rule establishes a program for producers and cooperative associations of producers to voluntarily enter into forward price contracts with handlers for milk used for Class II, III, or IV purposes under the Agricultural Marketing Agreement Act of 1937 (AMAA). The program allows handlers regulated under the Federal milk marketing order program to pay producers and cooperative associations in accordance with the terms of a forward contract and not have to pay the minimum Federal order blend price for milk. This program is established in accordance with section 1502 of the Food, Conservation and Energy Act of 2008 (2008 Farm Bill).

DATES: Effective Date: November 3, 2008.

FOR FURTHER INFORMATION CONTACT: John R. Mengel, Chief Economist, USDA/AMS/Dairy Programs, Office of the Chief Economist, STOP 0229-Room 2753, 1400 Independence Ave., SW., Washington, DC 20250-0229, (202) 720-4664, e-mail address: john.mengel@usda.gov.

SUPPLEMENTARY INFORMATION: This rule implements a program for producers and cooperative associations of producers to enter into forward price contracts with handlers for Class II, III, or IV milk under the AMAA. This program is required to be established by the 2008 Farm Bill. The program authorizes that under the AMAA, milk handlers pay producers or cooperative associations of producers a negotiated price, rather than the Federal order minimum blend price for producer milk if subject to conditions and terms of a forward contract, provided the volume of such milk does not exceed the handler's Class II, III, and IV utilization for the month on the order that regulates the milk. The program applies to producer milk regulated under Federal milk marketing orders that is not classified as Class I milk or milk otherwise intended for fluid use

and that is in the current of interstate or foreign commerce or directly burdens, obstructs, or affects interstate or foreign commerce of Federally regulated milk. The Federal milk marketing order program consists of 10 Federal milk marketing orders (7 CFR 1001-1135). In accordance with the 2008 Farm Bill, the program prohibits forward contracts under the program from being entered into after September 30, 2012, and no forward contracts entered into under the program may extend beyond September 30, 2015.

Background

The Consolidated Appropriations Act of 2000 amended the Agricultural Marketing Agreement Act of 1937 \1\ to mandate the implementation of a Dairy Forward Pricing Pilot Program (DFPPP) through December 31, 2004. The law allowed proprietary handlers, and cooperative associations acting as milk handlers with respect to non-member milk, regulated under the Federal milk marketing order program to forward contract for deliveries of milk from producers or cooperative associations of producers at prices exempt from minimum Federal milk marketing order blend prices.\2\ The 2000 Act required that the Department conduct a study on the DFPPP to be submitted to Congress concerning impacts on milk prices paid to producers.\3\ The study, covering the period from September 2000 to March 2002, indicated that participation in the DFPPP was relatively small in terms of numbers of producers, handlers, and milk quantities. On a monthly average basis, 3.9 percent of eligible producers, 5.7 percent of proprietary manufacturing plants, and 5.3 percent of pooled milk received from eligible producers participated. The study concluded the DFPPP to be effective in reducing price volatility. The average monthly price received for contract milk was \$14.02, ranging from a low of \$13.23 to a high of \$14.86. The average monthly price of the same milk, had it not been under contract, was \$14.51, ranging from a low of \$12.04 to a high of \$17.75. Thus, the study concluded that price volatility was substantially reduced for producers and handlers that participated in the Program. Subsequent reports published by the Department, covering the entire period of the Program from September 2000 through December 2004, indicated results that were consistent with conclusions of the report submitted to Congress. The study and the final report on the DFPPP can be found at <http://www.ams.usda.gov/dairy>.

\1\ Section 23 of the Agricultural Adjustment Act (7 U.S.C. 601 et seq.), reenacted with amendments by the Agricultural Marketing Agreement Act of 1937, as enacted by Public Law 106-113 (113 Stat. 1501A-519).

\2\ See Final Rule for Dairy Forward Pricing Pilot Program, July 18, 2000; 65 FR 44408; 7 CFR Part 1140.

\3\ See A Study of the Dairy Forward Pricing Pilot Program and Its Effect on Prices Paid to Producers for Milk, October 31, 2002. Prepared for the Senate Committee on Agriculture, Nutrition and Forestry and the House Committee on Agriculture; <http://www.ams.usda.gov/dairy>.

This Final Rule removes the regulations covering the DFPPP that appeared in 7 CFR Part 1140, (7 U.S.C. 601 et seq.; as amended by

section 1001(a)(8) of Public Law 106-113) and establishes a new 7 CFR Part 1145, as mandated by the 2008 Farm Bill.

The program does not invalidate, supersede, or otherwise change any existing contractual agreements between handlers and producers. Contracts eligible under this program are those contracts beginning no earlier than the effective date of this final rule.

Executive Order 12866

This rule has been determined to be not significant for purposes of Executive Order 12866, and therefore has not been reviewed by the Office of Management and Budget.

Executive Order 12988

This rule has been reviewed under Executive Order 12988, Civil Justice Reform. It is not intended to have a retroactive effect. The adopted amendments do not preempt any state or local laws, regulations, or policies, unless they present an irreconcilable conflict with this rule. There are no administrative procedures which must be exhausted prior to judicial challenge to the provisions of this rule.

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Regulatory Flexibility Act and Paperwork Reduction Act

The legal basis for this rule is set forth in the 2008 Farm Bill, which directs the Secretary of USDA to establish a dairy forward pricing program. The 2008 Farm Bill directs USDA to establish a program under which milk producers and cooperative associations of producers are authorized to enter voluntarily into forward price contracts with milk handlers.

In accordance with the Regulatory Flexibility Act (5 U.S.C. 601-612), the Agricultural Marketing Service has considered the economic impact of this action on small entities and has certified that this rule will not have a significant economic impact on a substantial number of small entities. For the purpose of the Regulatory Flexibility Act, a dairy farm is considered a small business if it has an annual gross revenue of less than \$750,000, and a dairy products manufacturer is a small business if it has fewer than 500 employees.

For the purposes of determining which dairy farms are small businesses, the \$750,000 per year criterion was used to establish a production guideline of 500,000 pounds per month. Although this guideline does not factor in additional monies that may be received by dairy producers, it should be an inclusive standard for most small dairy farmers. For purposes of determining a handler's size, if the plant is part of a larger company operating multiple plants that collectively exceed the 500-employee limit, the plant will be considered a large business even if the local plant has fewer than 500 employees.

Based on information available from March 2008, the milk of 47,850 dairy farmers was pooled on the Federal milk marketing order system. Of the total, 44,979 dairy farmers, or 94 percent, were considered small businesses. During the same month, 317 handler plants were regulated by or reported their milk receipts to be pooled and priced on a Federal milk marketing order. Of the total, approximately 168 handler plants, or 53 percent, were considered small businesses.

The Agricultural Marketing Service (AMS) is committed to complying with the E-Government Act, to promote the use of the Internet and other information technologies to provide increased opportunities for citizen access to Government information and services, and for other purposes.

The reporting and recordkeeping requirements for this rule are minimal. Section 1601 of the 2008 Farm Bill provides that the promulgation of the regulations to establish a Dairy Forward Pricing Program shall be made without regard to the Paperwork Reduction Act of 1995 (44 U.S.C. Chapter 35). Although exempted, the requirements of the Paperwork Reduction Act were considered in developing the provisions of this rule. The provisions implementing the Dairy Forward Pricing Program have been carefully reviewed and every effort has been made to minimize recordkeeping costs or requirements.

Any handler that enters into a forward contract with a producer or cooperative association of producers must have written proof of such an arrangement. To meet other requirements for participation in this program, a handler must submit a copy of each forward contract with a producer or cooperative association of producers to the market administrator of the order which regulates the milk. Submitting this information to the milk market administrator is estimated to take five minutes or less. The handler must attach a disclosure statement to each forward contract, or otherwise make such statement part of the contract. The disclosure statement must be signed by each producer or cooperative representative entering into a forward contract. The disclosure statement explains that producers or cooperative associations of producers entering into forward contracts forfeit their rights to receive the minimum order price(s) for that portion of their milk that is subject to the contract for the duration of the contract period. Preparing the contract and attaching or including the disclosure statement is estimated to take twenty minutes or less per contract.

Any handler participating in the program will continue to file all of the reports that are required under the applicable Federal milk marketing order, as authorized under the Agricultural Marketing Agreement Act of 1937. The information collection requirements contained in the Federal milk marketing order program have been previously approved by the Office of Management and Budget (OMB) under the Paperwork Reduction Act of 1995 and have been assigned OMB Control Number 0581-0032. This includes reports of utilization of milk and monthly payroll reports that show information required by the orders. Taking into account the Dairy Forward Pricing Program, the monthly payroll report of each participating handler and the support statement sent from each participating handler to each participating producer must contain detailed accounting that distinguishes total rates used in making payment and volumes for milk under forward contract. While the resulting changes in burden are exempt from the Paperwork Reduction Act, slight modifications to the currently approved ``Handler's Report for Producer Payroll'' form will be submitted to the OMB.

If a handler's contract milk exceeds the handler's eligible milk for any month in which the specified contract price(s) are below the order's minimum prices, the handler must designate which producer milk shall not be contract milk. Preparing this notification is estimated to take five minutes or less. If the handler does not designate the suppliers of the over-contracted milk, the market administrator shall prorate the over-contracted milk to each producer and cooperative association having a forward contract with the handler.

The primary sources of data used to complete these reports are

routinely used in most business transactions. The additional reporting requirements required by this rule typically only require a minimal amount of data processing time, and the information collection and reporting burden is relatively small. Requiring the same reports for all handlers does not significantly disadvantage any handler that is smaller than the industry average.

USDA does not expect the forward contracting program to unduly burden small entities or impair their ability to compete in the marketplace. In its simplest form, a forward contract between a milk buyer and a milk producer (or cooperative) is an agreement to sell a stated quantity of milk for a specified period at a stated price. Producers and handler are able to ``lock-in'' prices, thereby minimizing risks associated with price and income volatility and enhancing their ability to obtain new or continued financing. By providing another tool to possibly reduce price risk, the program may aid small businesses in competing with larger entities that currently utilize futures and options markets, among other means, to reduce price volatility.

As previously discussed, the analysis of the DFPPP found the Program to substantially reduce price volatility for those producers who used the Program throughout the duration. The study concluded that participation in the DFPPP was small in terms of numbers of producers, handlers, and milk quantities. On a monthly average basis, 3.9 percent of eligible producers, 5.7 percent of proprietary manufacturing plants and 5.3 percent of pooled milk received from eligible producers

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participated. The study concluded the DFPPP to be effective in reducing price volatility. The average monthly price received for contract milk was \$14.02, ranging from a low of \$13.23 to a high of \$14.86. The average monthly price of the same milk, had it not been under contract, was \$14.51, ranging from a low of \$12.04 to a high of \$17.75.

Discussion of Rules Applicable to Program

Section 1502 of the 2008 Farm Bill requires the Secretary of Agriculture to establish a dairy forward pricing program. This section provides that a handler may forward contract for an amount of milk up to the volume of Class II, III, and IV milk pooled on the order by the handler under the AMAA, as amended, during a month and be exempt from the minimum Federal order blend price provisions for that milk. USDA, including Market Administrator personnel, does not determine the terms of forward contracts or enforce negotiated prices.

For producers who consider forward contracting as a risk-management tool, the ``benchmark'' price for milk is the Federal order blend price that they would receive in the absence of a forward contract. It is reasonable to expect a producer to negotiate a forward contract that would approximate the minimum blend price plus applicable premiums averaged over the forward contract period. Over time, it is reasonable to expect to see forward contract prices paid to producers below the applicable minimum order blend price in some months and above the minimum order blend price in others.

Participation in the dairy forward pricing program is voluntary for dairy farmers, dairy farmer cooperatives, and handlers. Handlers may not require producer participation in a forward pricing program as a condition for accepting milk. A producer or cooperative association may

continue to have its milk priced under the minimum payment provisions of the applicable milk order.

Producer milk under forward contract with a handler is exempt from the minimum blend price requirements offered through Federal milk orders provided the volume of such milk does not exceed the handler's Class II, III, and IV utilization for the month on the order which regulates the milk.

Any ``handler'' defined in 7 CFR 1000.9 is eligible to enter into a forward contract(s) with producers or cooperatives of producers. As defined in that section, ``handler'' includes not only the operator of a pool plant or nonpool plant, but also a broker serving as a handler as provided in Sec. 1000.9(b), a proprietary handler, and a cooperative association acting as a handler with respect to non-member milk delivered to a pool plant or diverted to a nonpool plant. Nothing in this regulation affects any contractual arrangements between a cooperative association and its members.

A handler's combined Class II, III, and IV producer milk utilization is defined in 7 CFR 1145 as the handler's ``eligible milk.'' In the case of a multi-plant handler, the handler's Class II, III, and IV producer milk utilization will be combined together for all of the handler's milk regulated under one milk marketing order. A handler will only be exempt from paying the milk marketing order's minimum blend price on its volume of ``eligible milk.'' If a handler enters into forward contracts for more than the eligible milk volume, (``over-contract'' milk) the handler must notify the Market Administrator. If the handler fails to notify the Market Administrator of payment adjustments, the Market Administrator will prorate the over-contract milk to each producer and cooperative association having a contract with the handler.

Although handlers participating in the program will not be required to pay producers and cooperative associations the minimum uniform blend or component prices for contract milk, they must continue to account to the pool for all milk they receive at the respective milk marketing order's minimum class prices. In the case of milk received by a transfer from a cooperative association's pool plant, a handler may forward contract for all such transferred milk that is not used in Class I.

In many milk markets nonpool plants regularly receive pooled milk from milk producers who are not members of a cooperative association. This milk is actually pooled by a pool plant operator or by a cooperative association through its deliveries to a pool plant. The non-member milk delivered to a nonpool plant is reported under the milk marketing order program as producer milk diverted to a nonpool plant by the cooperative association on its monthly report of receipts and utilization to the milk market administrator. Alternatively, if a cooperative association is not involved in the transaction, such milk could be reported by a pool plant operator on its monthly report of receipts and utilization.

Many nonpool plant operators who receive non-member milk that is pooled through another handler issue checks to the nonpool plant's non-member producers. They submit their payrolls showing these payments to the market administrator. Nevertheless, these nonpool plant operators are not responsible under the milk marketing order program for paying their non-member producers the minimum Federal milk marketing order price; it is the handler (either the cooperative association or pool plant operator) that pools the milk for such nonpool plants that is responsible for an underpayment under the milk marketing order program.

Accordingly, only producer milk that is subject to forward contracting with a handler in compliance with the Dairy Forward Pricing Program will be exempt from the order's minimum blend price provisions. In the case of non-member milk that is reported as producer milk by a cooperative association handler or pool plant operator, but payrolled by a nonpool plant operator, the cooperative association or pool plant operator, respectively, will be responsible for any underpayment to a nonmember producer in the event that milk under contract becomes subject to minimum milk marketing order pricing (as in the case of over-contract milk). In this way, cooperative association handlers, pool plant operators, and nonpool plant operators may continue the arrangements that have evolved to pool milk under the Federal milk marketing order program and all will be permitted to participate in the forward contracting program.

Any handler participating in the program will continue to file all of the reports that are required under the applicable Federal milk marketing order. This includes reports of receipts and utilization of milk and monthly payroll reports that show all information required by the orders. The notable differences, however, between the forward pricing program implemented in this Final Rule and the DFPPP are that handlers participating in the forward pricing program must now provide more detailed accounting in their monthly payroll reports to the market administrator and remittance information provided to participating producers (7 CFR 1---.31, 1001.73(e), 1005.73(e), 1006.73(e), 1007.73(e), 1030.73(f), 1032.73(f), 1033.73(e), 1124.73(f), 1126.73(e), 1131.73(e)). In accordance with these provisions, the monthly payroll reports of participating handlers will be required to contain detailed accounting that distinguishes gross values paid for applicable volumes of contract versus non-contract milk for each producer. Handlers participating in the DFPPP were not required to provide such detailed accounting to the market administrator. Remittance information

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from participating handlers to participating producers must clearly distinguish gross values and volumes for contract versus non-contract milk. These distinctions avoid any questions concerning compliance with Federal order minimum price requirements for participant milk not under contract.

As with the DFPPP, handlers participating in the Federal order program must submit to the market administrator a copy of each contract for which it claims exemption from the order's minimum blend pricing provisions. The contract must denote the pricing terms for contract milk. The contract must be signed prior to the first day of the first month for which the contract applies and must be received by the market administrator by the 15th day of that month. For the first month that the program is effective, contracts must be signed on or after the day on which the program becomes effective. For example, if the program becomes effective on November 15, contracts for December milk must be signed between November 15 and November 30, and copies must be received by the market administrator by December 15.

Each handler must give each contracting dairy farmer or cooperative association a disclosure statement informing them of the nature of the program and providing certain information that should be considered before entering into a forward contract. It is important that producers clearly understand on what basis they are being paid for contract milk. The disclosure statement must be signed on the same date as the

contract by the dairy farmer or cooperative association representative and will have to be returned by the handler to the market administrator together with the contract. The disclosure is less than one page long and can easily be incorporated into the body of the forward contract itself or can be handled as a supplement that may be attached to the forward contract. Any contract that is submitted to the market administrator without the disclosure statement will be considered to be invalid for the purpose of being exempt from the order's minimum pricing and will be returned to the handler.

Producers who are not members of a cooperative association should be aware that their milk weights and tests will continue to be handled in the same way by the milk market administrator even if they choose to enter into a forward contract which prices their milk on a different basis than the milk marketing order in which their milk is pooled. For example, if a producer in the Appalachian order, which prices the milk of dairy farmers on the basis of skim milk and butterfat, enters into a contract that prices milk on the basis of protein, butterfat, other solids and somatic cell count, the producer will only receive data from the milk market administrator on the skim and butterfat components to compare against the buying handler's test data. If the producer wants to verify other component tests, they must do so at their own expense.

Handlers with forward contracts remain subject to all other milk marketing order provisions. Payments specified under a forward contract must be made on the same dates as order payments which they replace. If handlers paid producers under contract at different times than producers not under contract, disorderly conditions might occur. Payments for milk covered under forward contract are required to be made by the dates specified in Sec. 1145.2(e) of the regulations.

Final Action

In accordance with the 2008 Farm Bill, this final rule establishes the dairy forward pricing program. These provisions are included in a new part 1145, which provides separate sections for Definitions, Rules Governing Forward Contracts and Enforcement of the program.

Subtitle F of Title I of the 2008 Farm Bill at section 1601 provides for an implementation timeframe and the promulgation of the regulations to establish a Dairy Forward Pricing Program without regard to the Paperwork Reduction Act (44 U.S.C. Chapter 35), the Statement of Policy of the Secretary of Agriculture, effective July 24, 1971 (36 FR 13804), and the notice and comment provisions of section 553 of Title 5, United States Code. Accordingly, these provisions are made final in this action and for the same reasons good cause exists for making this rule effective one day after publication in the Federal Register. To do otherwise would be impracticable, unnecessary, and contrary to the public interest. (5 U.S.C. 553; 5 U.S.C. 808)

List of Subjects

7 CFR Part 1140

Contract, Forward contract, Forward pricing, Milk.

7 CFR Part 1145

Contract, Forward contract, Forward pricing, Milk.

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For the reasons set forth in the preamble and under the authority of 7 U.S.C. 601 et seq., Title 7, chapter X of the Code of Federal Regulations is amended by removing a reserving part 1140 and adding a new part 1145 to read as follows:

PART 1140--[REMOVED AND RESERVED]

PART 1145--DAIRY FORWARD PRICING PROGRAM

Subpart A--Definitions

Sec.

1145.1 Definitions.

Subpart B--Program Rules

1145.2 Program.

Subpart C--Enforcement

1145.3 Enforcement.

Authority: 7 U.S.C. 8772.

Subpart A--Definitions

Sec. 1145.1 Definitions.

(a) Program means the dairy forward pricing program as established by Section 1502 of Public Law No. 110-246.

(b) Eligible milk means the quantity of milk equal to the contracting handler's Class II, III and IV utilization of producer milk, in product pounds, during the month, combining all plants of a single handler regulated under the same Federal milk marketing order.

(c) Forward contract means an agreement covering the terms and conditions for the sale of Class II, III or IV milk from a producer defined in 7 CFR 1001.12, 1005.12, 1006.12, 1007.12, 1030.12, 1032.12, 1033.12, 1124.12, 1126.12, 1131.12 or a cooperative association of producers defined in 7 CFR 1000.18, and a handler defined in 7 CFR 1000.9.

(d) Contract milk means the producer milk regulated under a Federal milk marketing order covered by a forward contract.

(e) Disclosure statement means the following statement which must be signed by each producer or cooperative representative entering into a forward contract with a handler before the Federal milk marketing order administrator will recognize the contract as satisfying the provisions of this program.

Attachment to Sec. 1145.1, paragraph (e):

Disclosure Statement

I am voluntarily entering into a forward contract with [insert handler's name]. I have been given a copy of the contract. By signing this form, I understand that I am forfeiting my right to receive the Federal milk marketing order's minimum prices for that portion of the milk which is under contract for the duration of the contract. I also

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understand that this contract milk will be priced in accordance with the terms and conditions of the contract.

Printed Name:-----
Signature:-----
Date:-----
Address:-----
Producer Number:-----

(f) Other definitions. The definition of any term in Parts 1000-1131 of this chapter apply to, and are hereby made a part of this part, as appropriate.

Subpart B--Program Rules

Sec. 1145.2 Program.

(a) Any handler defined in 7 CFR 1000.9 may enter into forward contracts with producers or cooperative associations of producers for the handler's eligible volume of milk. Milk under forward contract in compliance with the provisions of this part will be exempt from the minimum payment provisions that would apply to such milk pursuant to 7 CFR 1001.73, 1005.73, 1006.73, 1007.73, 1030.73, 1032.73, 1033.73, 1124.73, 1126.73 and 1131.73 for the period of time covered by the contract.

(b) No forward price contract may be entered into under the program after September 30, 2012, and no forward contract entered into under the program may extend beyond September 30, 2015.

(c) Forward contracts must be signed and dated by the contracting handler and producer (or cooperative association) prior to the 1st day of the 1st month for which they are to be effective and must be received by the Federal milk market administrator by the 15th day of that month. The disclosure statement must be signed on the same date as the contract by each producer entering into a forward contract, and this signed disclosure statement must be attached to or otherwise included in each contract submitted to the market administrator.

(d) In the event that a handler's contract milk exceeds the handler's eligible milk for any month in which the specified contract price(s) are below the order's minimum prices, the handler must designate which producer milk shall not be contract milk. If the handler does not designate the suppliers of the over-contracted milk, the market administrator shall prorate the over-contracted milk to each producer and cooperative association having a forward contract with the handler.

(e) Payments for milk covered by a forward contract must be made on or before the dates applicable to payments for milk that are not under forward contract under the respective Federal milk marketing order.

(f) Nothing in this part shall impede the contractual arrangements that exist between a cooperative association and its members.

Subpart C--Enforcement

Sec. 1145.3 Enforcement.

A handler may not require participation in a forward pricing

contract as a condition of the handler receiving milk from a producer or cooperative association of producers. USDA will investigate all complaints made by producers or cooperative associations alleging coercion by handlers to enter into forward contracts and based on the results of the investigation will take appropriate action.

Dated: October 24, 2008.

Lloyd C. Day,
Administrator, Agricultural Marketing Service.
[FR Doc. E8-25856 Filed 10-30-08; 8:45 am]

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