This document is scheduled to be published in the
Federal Register on 03/07/2014 and available online at
http://federalregister.gov/a/2014-04693, and on **FDsys.gov**

DEPARTMENT OF AGRICULTURE

Agricultural Marketing Service

7 CFR Parts 1005 and 1007

[Doc. No. AMS-DA-09-0001; AO-388-A17 and AO-366-A46; DA-05-06-A]

Milk in the Appalachian and Southeast Marketing Areas; Final Partial Decision on Proposed Amendments to Marketing Agreements and to Orders

AGENCY: Agricultural Marketing Service, USDA.

ACTION: Proposed rule.

SUMMARY: This final decision proposes to permanently adopt revised transportation credit balancing fund provisions for the Appalachian and Southeast milk marketing orders. Specifically, this document Establishes a variable mileage rate factor using a fuel cost adjustor to determine the transportation credit payments of both orders; increases the transportation credit assessment rate for the Appalachian order to $0.15 per hundredweight; and establishes a zero diversion limit standard on loads of milk requesting transportation credits. Separate decisions will address the proposed adoption of an intra-market transportation credit provision for the Appalachian and Southeast orders and for increasing the transportation credit rate assessment for the Southeast order. This final decision is subject to producer approval. Producer approval for this action will be determined concurrently with amendments adopted in a separate final decision that amends the Class I pricing and other provisions of the Appalachian, Southeast, and Florida milk marketing orders.

FOR FURTHER INFORMATION CONTACT: Erin Taylor, USDA/AMS/Dairy Programs, Order Formulation and Enforcement Branch, STOP 0231-Room 2971, 1400 Independence

Avenue, SW, Washington, DC 20250-0231, (202) 720-7183, e-mail address: Erin.Taylor@ams.usda.gov.

SUPPLEMENTARY INFORMATION: This final decision proposes to permanently adopt amendments that: 1) Establish a variable transportation credit mileage rate factor which uses a fuel cost adjustor in both orders; 2) Increase the Appalachian order's maximum transportation credit assessment rate to $0.15 per hundredweight (cwt); and 3) Establish a zero diversion limit standard on loads of milk requesting transportation credits.

This administrative action is governed by the provisions of sections 556 and 557 of Title 5 of the United States Code and, therefore, is excluded from the requirements of Executive Order 12866.

The amendments to the rules proposed herein have been reviewed under Executive Order 12988, Civil Justice Reform. They are not intended to have a retroactive effect. If adopted, the proposed amendments would not preempt any state or local laws, regulations, or policies, unless they present an irreconcilable conflict with this rule.

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

Regulatory Flexibility Act and Paperwork Reduction Act

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 proposed rule would 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 marketing 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 farms. For purposes of determining a handler's size, if the plant is part of a larger company operating multiple plants that collectively exceed the 500-employee limit, the plant will be considered a large business even if the local plant has fewer than 500 employees.

During January 2006, the time of the hearing, there were 3,055 dairy farmers pooled on the Appalachian order (Order 5) and 3,367 dairy farmers pooled on the Southeast order (Order 7). Of these, 2,889 dairy farmers (95 percent) in Order 5 and 3,218 dairy farmers (96 percent) in Order 7 were considered small businesses.

During January 2006, there were a total of 37 handlers operating plants associated with the

Appalachian order (22 fully regulated plants, 11 partially regulated plants, 2 producer-handlers and 2 exempt plants). A total of 52 plants were associated with the Southeast order (31 fully regulated plants, 9 partially regulated plants and 12 exempt plants). The number of plants meeting the small business criteria under the Appalachian and Southeast orders were 9 (24 percent) and 18 (35 percent), respectively.

The amendments that are recommended for permanent adoption in this decision revise the transportation credit provisions of the Appalachian and Southeast orders. The Appalachian and Southeast orders contain provisions for a transportation credit balancing fund. To partially offset the costs of transporting supplemental milk into each marketing area to meet fluid milk demand at distributing plants during the months of July through December, handlers are charged an assessment year-round to generate revenue used to make payments to qualified handlers.

The adopted amendments establish a variable mileage rate factor that would be adjusted monthly by changes in the price of diesel fuel (a fuel cost adjustor) as reported by the Department of Energy for paying claims from the transportation credit balancing funds of the Appalachian and Southeast orders. Prior to their interim adoption, the mileage rate of both orders was fixed at 0.35 cents per cwt per mile.

The adopted amendments increase the transportation credit assessment rate for the Appalachian order. Specifically, the maximum assessment rate for the Appalachian order is increased to $0.15 per cwt. The transportations credit assessment rate for the Southeast order is increased by actions taken in a separate rulemaking (73 FR 14153). The higher assessment rate is intended to minimize the proration and depletion of the order’s transportation credit balancing fund during those months when supplemental milk is needed. The higher assessment rate for the

Appalachian order adopted in this decision is necessary due to expected higher mileage reimbursement rates arising from escalating fuel costs, the transporting of milk over longer distances and the expected continuing need to rely on supplemental milk supplies arising from declining local milk production in the marketing areas.

The transportation credit assessment rate for the Southeast order was increased from 10 cents per cwt to 20 cents per cwt on an interim basis (71 FR 62377). Subsequent to this increase, a separate rulemaking affecting the Southeast order proposed an additional increase in the assessment rate to 30 cents per cwt. A tentative partial decision (73 FR 11194), effective February 25, 2008, describes the record evidence supporting a 30 cents per cwt transportation credit assessment rate. The 30 cents per cwt assessment rate was then adopted on an interim basis (73 FR 14153) effective March 18, 2008. Since these separate decisions address the higher assessment rate, there is no further consideration to this issue in this proceeding.

Proposals published in the hearing notice as Proposal 2, seeking to establish an intra-market transportation credit provision for the Appalachian and Southeast orders, and Proposal 5, seeking to reduce the volume of milk diverted to plants located outside of the Appalachian and Southeast milk marketing areas, will be addressed in a separate decision. No further discussion of these proposals is made in this decision.

The adopted amendments also amend the Producer milk provisions of the Appalachian and Southeast orders by eliminating the current ability to pool diverted milk associated with supplemental milk receiving a transportation credit payment. As previously indicated in the tentative partial final decision of this rulemaking (71 FR 54118), this decision does not specifically adopt the Dean Foods Company proposal (published in the hearing notice as

Proposal 4), but agrees with the need to limit diverted milk pooled on the order made possible by supplemental milk eligible to receive transportation credits.

Prior to amendments adopted on an interim basis, the Appalachian and Southeast orders provided transportation credits on supplemental shipments of milk for Class I use provided the milk was from dairy farmers who are not defined as a “producer” under the orders. A producer under the order is defined as a dairy farmer who: 1) during the immediately preceding months of March through May and not more than 50 percent of the milk production of the dairy farmer, in aggregate, is received as producer milk by either order during those 3 months; and 2) produced milk on a farm not located within the specified marketing areas of either order. The provisions of each order provide the market administrator the discretionary authority to adjust the 50 percent milk production standard to assure orderly marketing and efficient handling of milk in the marketing areas.

Adoption of the proposed amendments will be applied to all Appalachian and Southeast order handlers and producers, which consist of both large and small businesses. Since the adopted amendments will affect all producers and handlers equally regardless of their size, the amendments would not have a significant economic impact on a substantial number of small entities.

The Agricultural Marketing Service 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.

This notice does not require additional information collection that needs clearance by the Office of Management and Budget (OMB) beyond currently approved information collection.

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

No other burdens are expected to fall on the dairy industry as a result of overlapping Federal rules. This rulemaking proceeding does not duplicate, overlap, or conflict with any existing Federal rules.

Prior documents in this proceeding

Notice of Hearing: Issued December 22, 2005; published December 28, 2005 (70 FR 76718).

Tentative Partial Decision: Issued September 1, 2006; published September 13, 2006 (71 FR 54118).

Interim Final Rule: Issued October 19, 2006; published October 25, 2006 (71 FR 62377).

Preliminary Statement

A public hearing was held upon proposed amendments to the marketing agreement and the orders regulating the handling of milk in the Appalachian and Southeast marketing areas. The hearing was held, pursuant to the provisions of the Agricultural Marketing Agreement Act of 1937 (AMAA), as amended (7 U.S.C. 601-674), and the applicable rules of practice and procedure governing the formulation of marketing agreements and marketing orders (7 CFR part 900).

The proposed amendments set forth below are based on the record of a public hearing held in

Louisville, KY, on January 10-12, 2006, pursuant to a notice of hearing issued December 22, 2005, published December 28, 2005 (70 FR 76718).

Upon the basis of the evidence introduced at the hearing and the record thereof, the Administrator, on September 1, 2006, issued a Tentative Partial Decision, published in the Federal Register on September 13, 2006 (71 FR 54118) containing notice of the opportunity to file written exception thereto.

The material issues on the record of hearing relate to:

1. Transportation Credits
    - A. Establishing a variable mileage rate factor.
    - B. Increasing the maximum assessment rates.
    - C. Establishing diversion limit standards.

Findings and Conclusions

This final decision specifically addresses proposals published in the hearing notice as Proposals 3, 1, and certain objectives of Proposal 4. Proposal 3 seeks to establish a variable mileage rate factor (MRF) using a fuel cost adjustor. Proposal 1 seeks to increase the maximum transportation credit assessment rates for both orders. The intent of Proposal 4 is to discourage the volume of milk pooled by diversions by reducing the amount of transportation credits a handler could receive. A complete discussion and findings on these three proposals appears after the summary of testimony.

Proposal 2, seeking to establish an intra-market transportation credit provision for both the Appalachian and Southeast orders and Proposal 5, seeking to reduce the volume of milk diverted to an out-of-area plant, will be addressed in a separate decision. Accordingly, no further references to Proposals 2 and 5 will be made in this decision.

The following findings and conclusions on the material issues are based on evidence presented at the hearing and the record thereof:

1. Transportation Credits.

A. Establishing a variable mileage rate factor

A proposal, published in the hearing notice as Proposal 3, seeking to establish a variable mileage rate factor (MRF) that uses a fuel cost adjustor in the transportation credit payment provisions in both the Appalachian and Southeast orders, is recommended for permanent adoption. At the time of the hearing, the two orders provided for a fixed mileage rate of $0.035 per cwt per mile. The proposal was offered by Dairy Farmers of America, Inc. (DFA). DFA is a dairy farmer member-owned Capper-Volstead cooperative that at the time of the hearing had 12,800 member farmers whose milk was pooled throughout the Federal order system, including on the Appalachian and Southeast orders.

A witness appearing on behalf of Southern Marketing Agency, Inc. (SMA) and Dairy Cooperative Marketing Association, Inc. (DCMA) testified in support of Proposal 3. SMA and DCMA are marketing agencies-in-common operating in the southeast region of the country. Members of SMA at the time of the hearing included Arkansas Dairy Cooperative Association; Dairy Farmers of America, Inc.; Dairymen's Marketing Cooperative, Inc.; Lone Star Milk Producers, Inc.; and Maryland & Virginia Milk Cooperative Association, Inc. Members of DCMA at the time of the hearing included the abovementioned members of SMA; Zia Milk Producers Association; Select Milk Producers Association; Cooperative Milk Producers Association, Inc.; and Southeast Milk, Inc. Dairylea Cooperative, Inc. also requested that the witness testify on their behalf and in support of Proposal 3.

The SMA witness testified that the southeastern region of the United States is experiencing declining milk production while the population and demand for fluid milk are increasing. As a result, the witness stated that handlers servicing the Appalachian and Southeast marketing areas must continually seek supplemental supplies of milk from outside their normal milksheds. The witness added that the volume of supplemental milk needed to meet demand that cannot be met by local production and the distances from where the supplemental milk is obtained continues to increase. The witness explained that these marketing conditions cause the transportation credit balancing funds to be depleted at a rate faster than the rate at which handlers are assessed.

The SMA witness presented monthly fuel cost data for the United States and nine U.S. sub-regions from the Energy Information Administration of the United States Department of Energy (EIA). Relying on EIA data, the witness asserted that the cost of diesel fuel has escalated sharply in recent years. According to the witness, the national average diesel fuel price in mid-1997 was reported to be approximately $1.15 to $1.17 per gallon while the national average diesel fuel price in mid-2005 was reported to be $2.20 to $2.50 per gallon. The witness emphasized that diesel fuel prices are much higher than the prices that existed when the transportation credit provisions were first implemented in 1996 and amended in 1997.

The SMA witness noted that the cost of hauling has also increased. Relying on EIA data, the SMA witness estimated the cost of hauling to be in the range of $1.75 to $1.80 per loaded mile in 1997, whereas the cost in 2005 was about $2.35 per loaded mile. As diesel fuel costs have increased, the witness explained, so have other costs such as equipment, insurance, and labor.

The SMA witness emphasized that there have been no adjustments made to the MRF of the transportation credit provisions since they were last amended in 1997. The witness recounted that the original mileage rate was reduced by 5 percent, from $0.037 per cwt per mile to $0.035 per cwt per mile in 1997.

The SMA witness explained that in 1997, approximately 94 to 95 percent of the transportation costs of supplemental milk were covered by transportation credit balancing fund payments. The witness reiterated that since no adjustments have been made to the orders' transportation credit reimbursement rate since 1997, the percentage of hauling costs covered by the transportation credits today are substantially less than those in 1997.

According to the SMA witness, the use of a fixed mileage rate is not responsive to changes in hauling costs. The witness explained that Proposal 3 would compute a variable transportation credit mileage rate per cwt per mile that would adjust with changes in the cost of diesel fuel. The witness stressed the importance of, and the need for, keeping information on hauling costs current by using independent fuel cost data. The witness stated that hauling cost rates, adjusted for changes in fuel costs, are common in the industry.

The SMA witness illustrated components used to calculate the proposed variable MRF. According to the witness, a monthly average diesel fuel price, a reference diesel fuel price, an average mile-per-gallon truck fuel use, a reference hauling cost per loaded mile and a reference load size are the components needed to calculate the proposed variable MRF.

Using EIA data for the United States and nine U.S. sub-regions, the SMA witness explained that using the Lower Atlantic and Gulf Coast EIA regions in computing the monthly mileage rates would be reflective of the Appalachian and Southeast marketing areas. Relying on EIA data, the witness explained that the Lower Atlantic region is comprised of the states of Virginia, West Virginia, North Carolina, South Carolina, Georgia, and Florida. Similarly, the witness added, the Gulf Coast region is comprised of Alabama, Mississippi, Arkansas, Louisiana, Texas, and New Mexico. According to the witness, of the nine sub-regions described by the EIA, the Lower Atlantic and Gulf Coast regions best reflect the Appalachian and Southeast marketing areas geographically. The witness also noted that according to EIA data, the diesel fuel costs for these two regions are among the lowest reported nationally.

In establishing a reference diesel fuel price for the proposed transportation credit mileage rate calculation, the SMA witness relied on EIA retail diesel fuel prices for the time period of October to November 2003. During that period, the witness said, diesel fuel prices averaged $1.48 per gallon nationally and ranged from $1.42 per gallon in the Lower Atlantic to $1.43 per gallon in the Gulf Coast EIA regions. Due to relatively little fluctuation of diesel fuel prices during October to November 2003, the witness was of the opinion that this period is a fair and conservative timeframe on which to establish a reference diesel fuel price. The witness concluded by suggesting $1.42 per cwt per mile should be used as the reference diesel fuel price.

The SMA witness submitted a random selection of actual milk hauler bills as the basis for computing the reference hauling cost component of the proposed MRF. According to the witness, actual origination and destination points, miles moved, and rates and fuel surcharges per loaded mile were depicted on each hauling bill. For the month of October 2005, the witness stated that hauling costs ranged from $1.89 to $2.70 per loaded mile, with the average being $2.48 per loaded mile. In order to be consistent with the timeframe used for the reference diesel fuel price, the witness submitted selected milk hauling bills from October to November 2003 as the basis for determining the reference hauling cost. The witness testified that for this time period the simple average hauling rate charged per loaded mile in the Southeast was $1.9332 and $1.8913, respectively, and averaged $1.9122. Accordingly, the witness offered that the average hauling rate of $1.91 per loaded mile should become the reference hauling cost used in calculating the MRF.

The SMA witness provided data compiled by the United States Department of Transportation (USDOT) on combination truck fuel economy. According to the witness, the USDOT data indicated that the average miles traveled per gallon for a combination truck in 2002 was 5.2. The witness was of the opinion that dairy industry fuel economy is similar, as it ranges between 5.0 to 6.0 miles per gallon. Accordingly, the witness advocated using a 5.5 miles per gallon fuel consumption rate in computing the proposed MRF. The witness also testified that a 5,600 gallon tanker, at its fullest capacity, can carry 48,160 pounds of milk. Therefore, the witness explained, 48,000 pounds should be the reference load size used in calculating the MRF.

The SMA witness summarized that Proposal 3 calculates a variable monthly MRF by using: 1) EIA data from a base period defined as October and November 2003, 2) hauling cost of $1.91 per loaded mile, 3) a reference diesel fuel rate of $1.42 per gallon, 4) a fuel economy of 5.5 miles per gallon and 5) a load size of 48,000 pounds.

The SMA witness explained that the proposed mileage rate would be calculated by averaging the four most recent weeks of retail on-highway diesel prices for both the Lower Atlantic and Gulf Coast, as reported by the EIA prior to each order's announcement of the Advance Class milk prices. According to the witness, the proposed mileage rate would then be computed and included in each order's announcement of Advanced Class milk prices that are announced publicly on or before the 23rd of the month.

The SMA witness stressed that, for a variety of reasons, the proposed mileage rate computation reflects less than the actual cost of hauling. The witness asserted that the proposed mileage rate is based on costs of hauling from 2003, rather than a more current timeframe, and therefore would only reflect changes in the cost of diesel fuel since that time. The witness also reiterated that the proposed mileage rates would apply only to Class I milk shipped in excess of 85 miles, directly from farms to plants. The SMA witness was of the opinion that transportation costs will continue to increase and that adopting the proposed changes to the transportation credit provisions will avoid exhausting the transportation credit balancing fund before costs are reimbursed.

The SMA witness asserted at the time of the hearing that they were incurring substantial losses in supplying supplemental milk for Class I use to the Appalachian and Southeast marketing areas. The witness indicated that hauling costs in supplying supplemental milk exceed $15 million annually.

A comment filed by SMA in response to the Tentative Final Decision reiterated support for the adoption of Proposal 3.

Six DFA farmer-members testified in support of Proposal 3. According to these witnesses, it is the cooperative members of SMA who are acting as handlers to supply the supplemental fluid milk needs of both marketing areas. According to the witnesses, this results in additional costs that are absorbed by the dairy farmer members of the cooperatives that comprise SMA. The witnesses argued that hauling costs and the distances supplemental milk must be hauled continue to increase.

The six DFA dairy farmer witnesses were of the opinion that Proposal 3 is a reasonable solution to deal with the continued production decline and population driven demand increase in the southeastern region of the United States. The witnesses were of the opinion that using a fuel adjustor that moves up and down with changes in the cost of diesel fuel would more adequately cover the costs of transporting supplemental milk to the two marketing areas.

A post-hearing brief submitted by DFA, and supported by SMA, reiterated support for adopting a fuel cost adjustor.

A post-hearing brief was submitted on behalf of Arkansas Dairy Cooperative Association (ADCA) in support of Proposal 3. According to ADCA, its members' milk does not usually qualify for transportation credit payments because it is typically pooled on the Southeast and Central orders year-round. However, ADCA noted that its members are impacted by the cost of hauling supplemental milk into the southeast because of its membership in a marketing agency-in-common.

A post-hearing brief was submitted on behalf of Dairymen's Marketing Cooperative, Inc. (DMCI) in support of Proposal 3. The brief emphasized that as fuel costs continue to increase, the Class I differential surface becomes more outdated and unable to reflect the costs of moving milk.

A post-hearing brief was submitted on behalf of Lone Star Milk Producers (Lone Star) in support of Proposal 3 because it would establish updated mileage rates for payments from the transportation credit balancing funds. The brief stated that the hauling cost factor used to develop the mileage rate for the transportation credit balancing fund has not been updated since the mid 1990's and is inadequate.

A post-hearing brief submitted by Maryland & Virginia Milk Producers Cooperative

Association, Inc. (Maryland & Virginia) reiterated support for the adoption of Proposal 3.

A post-hearing brief was submitted on behalf of South East Dairy Farmers Association (SEDFA). The brief expressed support for a variable mileage rate based on the changes in the cost of diesel fuel. The brief stated that the industry uses a consistent fuel economy estimate of 5.0 to 6.0 miles per gallon when calculating expected milk transportation costs. The brief stressed that the extreme rise in diesel fuel prices in recent months has made the adoption of Proposal 3 critical for producers who incur the cost of hauling milk to the market.

A witness appearing on behalf of Southeast Milk, Inc. (SMI) testified in support of Proposal 3. SMI is a dairy marketing cooperative with, at the time of the hearing, approximately 300 dairy farmer members in Florida, Georgia, Alabama, and Tennessee. The SMI witness stated that relying on cost indexes of other government agencies determined on a national scale makes the data less subject to manipulation by any given industry.

A witness testified on behalf of Dean Foods Company (Dean) in support of Proposal 3. According to the witness, Dean owns and operates 8 plants regulated by the Appalachian marketing area and 10 plants regulated by the Southeast marketing area. The Dean witness agreed with the benefit of using an adjustor in determining the MRF to reflect changes in fuel prices over time. However, the witness also was of the opinion that the MRF should be reduced to 95 percent in order to be consistent with the Secretary’s past decisions that transportation credits do not encourage the uneconomic movement of milk or inefficiencies.

The Dean witness testified that the marketing areas are in need of supplemental milk supplies and that supplying such milk presents challenges. Nevertheless, the witness expressed concern for the continuing and potential future abuse of transportation credits. The witness asserted that current order provisions allow supplemental milk to receive transportation credits, when such milk is not demanded. Moreover, the witness stressed that there is no assurance that transportation credit balancing fund payments would flow to the dairy farmer members of the cooperatives acting as handlers located in the two marketing areas regardless of the producers' status as independent or cooperative members.

A post-hearing brief submitted on behalf of Dean reiterated support for Proposal 3, indicating that disorderly marketing conditions exist because the milk supply in the Southeastern United States is deficit and the cost of supplying the market is not borne equally. Additionally, a comment filed by Dean in response to the Tentative Final Decision expressed continued support for the adoption of Proposal 3.

A dairy farmer who supplies milk to Dean testified in support of the intent of Proposal 3. The witness stated that a dynamic mileage rate that adjusts to the energy markets is better than a static factor that is unable to adjust in response to changes in energy costs.

A dairy farmer who markets milk to Dean through Dairy Marketing Service (DMS) testified in favor of Proposal 3. The witness stated that using a variable MRF derived from a source outside of the dairy industry, such as the USDOT, would help decrease the chances of industry participants manipulating the information that should be used in calculating a MRF.

A witness appearing on behalf of Land O'Lakes, Inc. (LOL) testified in support of Proposal 3. LOL is a dairy farmer member-owned Capper-Volstead cooperative with, at the time of the hearing, over 4,000 member farmers whose milk is pooled on 6 Federal Orders. The witness stated that its members' milk located in the Northeast and Midwest have provided supplemental supplies to both the Appalachian and Southeast marketing orders for the past 10 years.

According to the witness, LOL supplies supplemental milk to the Appalachian and Southeast orders and experiences high milk hauling costs. The witness asserted that using diesel fuel prices as the basis for the MRF would make it responsive to actual costs incurred by the handlers moving milk into these two deficit markets.

A post-hearing brief submitted by LOL reiterated support for the adoption of Proposal 3. The brief said that in order to fulfill the supplemental milk needs of the Appalachian and Southeast order marketing areas, milk is sourced from 28 States. According to the brief, this demonstrates that the distance milk must travel has further increased, thereby strengthening the justification for the adoption of Proposal 3. Additionally, a comment filed by LOL in response to the Tentative Final Decision expressed continued support for the adoption of Proposal 3.

An independent dairy farmer from Tennessee testified in opposition to any changes to the Appalachian or Southeast marketing orders. The witness testified that additional government intervention in moving milk was not necessary and that supply and demand should be relied upon to dictate what services are needed. The witness asserted that amending the orders as proposed would change the way milk is moved, thereby hindering efficient milk hauling. The witness also was of the opinion that there is no assurance that transportation credits received for supplying supplemental milk would truly reach the market's producers. The witness expressed concerns that the proposed increases in the transportation credit rate could affect producer decisions and producer blend prices.

A witness testified on behalf of the Kentucky Dairy Development Council (KDDC). KDDC is a member-based organization that, at the time of the hearing, represented approximately 1,360 dairy farmers in Kentucky. The witness did not state support for or opposition to the proposals presented at the hearing. The witness was of the opinion that noncompetitive pricing is discouraging milk production in the southeastern United States. The witness was of the opinion that farm milk prices in Kentucky and in the Southeastern States have eroded and that KDDC was opposed to any Federal Order changes which would further erode farm prices. The witness did testify in support of changes to the orders that would strengthen the position of dairy farmers in Kentucky and in other Southeastern States.

A post-hearing brief submitted by KDDC in support of Proposal 3 said that Proposal 3 would benefit Kentucky dairy farmers by providing assistance in recovering market service costs.

B. Increasing the maximum assessment rate

A proposal, published in the hearing notice as Proposal 1, offered by DFA, that seeks to increase the maximum transportation credit balancing fund assessment rates for the Appalachian and Southeast orders is adopted. Specifically, the maximum transportation credit balancing fund assessment rate in the Appalachian order is increased by $0.055 per cwt on Class I milk for an amended rate of $0.15 per cwt. The Southeast order’s maximum assessment rate was increased by $0.10 per cwt for an amended rate of $0.20 per cwt and implemented on an interim basis. Subsequent to the interim adoption of the $0.20 per cwt assessment rate, a separate rulemaking increased this rate to $0.30 per cwt (73 FR 14153). Accordingly, this decision would permanently adopt the higher assessment rate for the Appalachian order only.

A witness appearing on behalf of DCMA and SMA testified in support of Proposal 1. As previously described in testimony regarding Proposal 3, the SMA witness said that the current transportation credit provisions provide for the collection of a maximum transportation credit assessment to handlers on all Class I milk for the Appalachian and Southeast marketing areas year-round. While the market administrator has the discretion to waive the maximum transportation credit assessments if deemed necessary, the SMA witness explained that the market administrator of each order collected the maximum assessments in 2004 and 2005. However, the witness said that the collected assessments in both orders had been insufficient to pay the requested credits, thereby necessitating the prorating of payments from the transportation credit balancing fund.

The SMA witness stated that even with the November 1, 2005, implementation of a transportation credit assessment increase of $0.03 per cwt for both orders, the assessment rate will likely not be able to ensure payments from the transportation credit balancing funds on all milk eligible to receive payment.

The SMA witness estimated that the transportation credit assessment rate for the Appalachian order for 2004 would have needed to be $0.0889 per cwt and $0.0953 per cwt for all of 2005 to cover all of the transportation credits requested. The witness also estimated that the Southeast order transportation credit assessment rate would needed to have been $0.1318 per cwt and $0.1246 per cwt in 2004 and 2005, respectively, to cover all requested credits. Additionally, the witness noted that the transportation credits requested for both the Appalachian and Southeast marketing orders for the months of July, September, and October of 2005 exceeded the transportation credits requested in all of 2004. The witness said this also demonstrates that increased volumes of supplemental milk were transported from locations farther from the marketing areas.

The witness said that the reason the market administrators prorated payments from the transportation credit balancing funds was because the rate of assessments exceeded collections.

The witness was of the opinion that this occurred because more supplemental milk was sourced from more distant locations.

Relying on market administrator data, the witness concluded that only 55 percent of the actual cost of transporting supplemental milk was covered by the transportation credit payments in the Appalachian order in 2004. Similarly, only 39 percent of the actual cost was covered for the Southeast order during the same period. The witness further estimated that in 2005, only 53 percent and 43 percent of the actual hauling costs for supplemental milk would be covered for the Appalachian and Southeast orders, respectively.

In explaining the need for the adoption of Proposal 3, the SMA witness reiterated that the combined effect of higher mileage hauling rates and the increased distance from which supplemental milk had to be hauled, resulted in a smaller portion of actual transportation costs being funded with transportation credits compared to the rate in 1997. The witness was of the opinion that transportation costs will continue to increase, making it necessary to again increase the assessment rate.

Further illustrating the need to increase the maximum transportation credit assessment rate, the SMA witness indicated that if a transportation credit reimbursement rate of $0.046 per cwt per mile had been in place rather than the current rate of $0.035 per cwt per mile, the Appalachian order would have required an assessment of $0.133 per cwt in 2004 and an assessment of $0.1415 per cwt in 2005, to prevent the prorating of transportation credit claims. Similarly, the witness stated that for the Southeast order, the assessment rate would have needed to have been $0.1927 per cwt in 2004 and $0.1869 per cwt in 2005.

The SMA witness testified that the different rates of transportation credit balancing fund assessments proposed for the Appalachian and Southeast orders reflect the differing costs of supplying supplemental milk into each marketing area. The witness stated that while the transportation credit assessment was waived for 2 months during 2002 and 2003 in the Appalachian order, assessments were not waived for the Southeast order. The witness asserted that while both orders rely on some of the same sources for supplemental milk, the Appalachian marketing area, at the time of the hearing, received most of its milk from the more northern Mid-Atlantic States while the Southeast marketing area received most of its supplemental milk from States located to the west and southwest of the marketing area. Furthermore, the witness added that different assessment rates for the two orders are warranted because at the time of the hearing, supplemental milk moved greater distances to service the Southeast market than it did to service the Appalachian market.

The six DFA dairy farmer witnesses that testified in support of Proposal 3 also testified in support of increasing the transportation credit assessments for both orders. The witnesses were of the opinion that the assessment increases would generate funds needed to maintain a sufficient transportation credit fund balance capable of paying on eligible claims. In addition, the witnesses were of the opinion that the orders' current location adjustments were not able to reflect the rapidly increasing costs of transporting milk from where it is located to where it is needed. Similarly, the witnesses stated that over-order premiums cannot be garnered from the market to offset rapidly increasing transportation costs.

The six DFA dairy farmer witnesses were also of the opinion that the intent of increasing the transportation credit assessment rates was a reasonable solution to mitigate continued production declines and the increasing demand for milk in the southeastern United States due to continued population increases in that region. The witnesses added that the markets' producers face higher fuel costs and longer hauling distances associated with obtaining supplemental milk. When producers go out of business, the witnesses said, the gap between supply and demand widens thereby increasing the cost of supplying the market with supplemental milk.

Post-hearing briefs submitted by DFA reiterated the position and testimony of SMA in support of increasing the transportation credit assessment rates immediately.

A post-hearing brief was submitted on behalf of Select Milk Producers, Inc. (Select) and Continental Dairy Products, Inc. (Continental) in support of Proposal 1. At the time of the hearing, Select's members were located in New Mexico, Texas, Kansas, and Oklahoma, while Continental's members were located in Indiana, Michigan, and Ohio. The brief stated that both cooperatives supply the Appalachian and Southeast marketing areas with supplemental milk. Select and Continental expressed support for proponent's hearing testimony in favor of increasing the transportation credit assessment rates of the two orders. The brief stated that while the proposals under consideration will not fix long-term marketing and transportation problems, Proposal 1 should be adopted in conjunction with USDA's consideration of alternative approaches aimed at correcting the milk deficit problems in the southeast region of the United States.

The Select/Continental brief expressed the opinion that blend prices, not Class I prices, provide the economic incentive to supply milk to a marketing area. The brief stated that when producers in a large marketing area share the same blend price, the incentive to move milk within the large marketing area is greatly diminished. In addition, the brief indicated that the pricing of diverted milk ignores the value of milk to the market where pooled, which results in milk being pooled that is not available to meet the Class I needs of the market.

A post-hearing brief was submitted on behalf of Southeast Dairy Farmer Association (SEDFA). The brief expressed support for Proposal 1 as published in the hearing notice. SEDFA represents cooperative and independent producers who are regular and supplemental milk suppliers located in and outside of the Appalachian and Southeast marketing areas.

The SEDFA brief asserted that whether milk is produced inside or outside of the two marketing areas, the cost of moving Class I supplemental milk should be borne by the marketplace. The brief stated that while the reimbursement of actual hauling costs is much lower than in 1997, the amount of supplemental milk being brought into the marketing areas is increasing. The brief concluded that because reimbursement of actual hauling cost is smaller, the higher costs not reimbursed have fallen disproportionately on producers. The brief agreed with Lone Star and Maryland & Virginia that the $0.03 increase in the transportation credit assessments implemented in November 2005[1] would be insufficient to cover the expected transportation credit claims during 2006.

A witness appearing on behalf of LOL testified in support of Proposal 1. The LOL witness agreed with other proponents that the transportation credit balancing fund for both orders has been insufficient to support transportation credit payments. While the witness supported the transportation credit assessment increases effective in November 2005, the witness did not think that this would be sufficient to reimburse future claims.

A post-hearing brief submitted by LOL reiterated its support for the adoption of Proposal 1. The brief indicated that the southeast region of the country is not able to fulfill Class I demands during any season of the year and must rely on a supplemental milk supply from about 28 States outside the Appalachian and Southeast marketing areas. The brief noted that transportation credits installed in the southeastern region in 1996 were based on the recognition that the region's Class I needs could only be met by supplemental milk from dairy farms located outside of the region.

A witness testifying on behalf of Dean expressed cautious support for increasing the transportation credit assessment rates of the two orders because the availability of additional credits must be balanced with consideration for abuses and undesired results. The witness was of the opinion that handlers who receive such credits are also pooling milk on the orders through the diversion process which does not actually serve the markets' Class I needs.

A post-hearing brief submitted on behalf of Dean agreed with proponents of Proposal 1 that disorderly marketing conditions exist. The brief stated that the southeast area's milk supply is deficit and the cost of supplying the market is not borne equally.

A witness testified on behalf of SMI in opposition to Proposal 1. The witness characterized transportation credits as a subsidy. The witness further expressed that subsidizing the transportation of milk produced outside of the marketing areas results in economic disincentives for local milk production and provides incentives for local milk supplies to be replaced by milk from outside the two marketing areas. The witness noted that when transportation credits were first adopted in 1996, the average Class I utilization of the southeast region was in the mid-80 percent range. Since the implementation of transportation credits, the witness said, Class I utilization had fallen to the 60 percent range. It was the opinion of the witness that transportation credit provisions are contributing to declining milk production in the two marketing areas.

---

[1] 70 FR 59221

The SMI witness testified that transportation credits should be eliminated. As an alternative, the witness suggested: 1) establishing a method whereby Class I prices could be adjusted based on more regional marketing conditions; 2) adopting a base-excess plan; 3) increasing the current Class I differential level; and 4) any other provisions that would encourage local milk production.

A Kentucky dairy farmer testified in opposition to Proposal 1. The witness argued that providing transportation credits devalues local milk, which results in lower prices to local producers and causes declining milk production in the two marketing areas. The witness expressed concern that Proposal 1 would encourage more milk from outside the marketing areas to be pooled on the orders even though it is not delivered to either marketing area on a daily basis, as is the locally produced milk. According to the witness, local producers are not able to receive the full value for local production because transportation credits give price advantages to producers located far from the marketing areas. The witness concluded by stating that pooling milk located outside of both marketing areas does not represent Class I use and therefore this milk should not be pooled on the Appalachian or Southeast orders.

A dairy farmer witness who supplies milk to Dean testified in opposition to Proposal 1. The witness viewed increasing assessment rates on transportation credits as detrimental to those dairy farmers who are located in the Appalachian and Southeast marketing areas and who regularly supply the Class I needs of the market. The witness was of the opinion that Proposal 1 lacks safeguards on the amount of additional milk that could be pooled on the orders by diversion. The witness said that this additional pooled milk would unnecessarily lower the blend price received by producers and essentially result in out-of-area milk supplies becoming less expensive relative to milk produced in-area. As a consequence, the witness said, local in-area producers will be forced out of business because of lower prices. Should this occur, the witness said, the need for additional out-of-area supplemental milk supplies would further increase to meet the Class I needs of the marketing areas.

The witness suggested that instead of providing additional transportation credits, a review of the level of Class I differentials and a review of diversions and touch-base provisions should be considered in another hearing.

An independent dairy farmer from Tennessee testified against making any changes to the Appalachian and Southeast marketing orders, including the adoption of Proposal 1. In addition to the witness' testimony regarding Proposal 3 as was already described, the witness was of the opinion that additional government intervention to provide for increasing the transportation credit assessment rate was not necessary and that supply and demand forces should dictate what services are needed. The witness asserted that amending the orders as proposed would change the way milk is transported and would hinder efficient handling of milk. The witness was of the opinion that there would be no assurance that the transportation credits would benefit the producers who were pooled on the two orders and had incurred the additional costs of servicing the Class I market.

A dairy farmer, who also markets milk to Dean through DMS, testified in opposition to Proposal 1. The witness said that local producers of the Appalachian and Southeast marketing areas are unable to supply all the fluid milk needs of the two marketing areas because local milk production in these areas is declining. The witness suggested that if Proposal 1 were adopted, an accounting of the total transportation costs of all milk movements should be supplied to the market administrators and be made available for public inspection. The witness also suggested making changes to the level of adjustments of milk prices by location (location adjustments) as an alternative to increasing the transportation credit assessment rate. The witness said if location adjustments were changed, the pooling standards for both orders would also need to be adjusted. Specifically, the witness suggested increasing the number of days' production needed to touch base, or increasing the performance standards of the orders.

A post-hearing brief submitted by the Kentucky Dairy Development Council (KDDC) supported Proposal 1.The brief noted that increasing the transportation credit assessment rate would benefit Kentucky dairy farmers by providing assistance in recovering costs associated with serving the market.

C. Establishing diversion limit standards

A proposal submitted by Dean Foods, published in the hearing notice as Proposal 4, seeks to reduce a handler's ability to utilize transportation credits to qualify producers for pooling on the orders. The intent of the proposal is to limit the pooling of additional surplus milk on the orders through the diversion process. At the time of the hearing, large volumes of milk were being pooled through diversions on the Appalachian and Southeast orders from locations distant from the marketing areas. While Proposal 4 would provide incentives to limit the pooling of milk through the diversion process, it would do so indirectly by limiting the payment of transportation credits. This decision chooses to directly limit diversions by establishing a zero diversion limit on milk that receives transportation credits.

A witness appearing on behalf of Dean testified in support of Proposal 4 while also expressing cautious support for the proposed transportation credit assessment increase (Proposal 1). The witness was of the opinion that handlers supplying supplemental milk to the two marketing areas receive a financial benefit from pooling diverted milk on the orders even though the milk does not ultimately serve the fluid market. The witness explained that while the diverted milk typically does not serve the two markets, it seeks to be pooled on the two orders because the blend prices are higher than what this milk could receive if pooled on other Federal orders.

The Dean witness testified that the establishment of large marketing orders has created new marketing problems. According to the witness, when the Federal order system had a larger number of smaller markets, each order's marketwide pools were small. Markets with large populations relative to associated milk, the witness explained, had higher Class I utilizations and higher blend prices to attract supplemental milk supplies. Markets with significant supplies of milk and smaller populations, the witness related, had lower Class I utilizations and producers pooled in those markets were provided with the economic incentive to look for higher returns from markets with higher blend prices. The witness further explained that smaller marketing areas limited the size of the Class I market and, in turn, limited how much milk could be pooled by diversion. The witness said that when orders were smaller, there were disincentives to pooling milk and the orders were more effective in limiting a handler's ability to pool milk through diversions. According to the witness, the relative value of diverted milk was tied to its distance from the market.

The Dean witness also testified that the Class I price surface adopted during Federal milk order reform changed the relative relationship of milk value to its distance from the market.

According to the witness, the location value of diverted milk prior to reform was determined by adjusting milk value according to its distance from an order's pricing point. The witness said this resulted in each plant having a different location adjustment value to its milk receipts depending on the order on which its receipts were pooled. The witness explained that the further milk was located from the order's pricing point, the less likely it was to be pooled as a diversion.

The Dean witness expressed concern that no longer valuing milk relative to the order on which it is pooled had a material effect on the value of pooling milk located far from the market by diversion. The witness was of the opinion that the flatter Class I price surface, with fixed differential levels by county, places a value on milk that is not reflective of its value to the marketing order where pooled making it economically desirable to pool milk located far from the market through the diversion process. The witness was also of the opinion that this served to provide the incentive for pooling distant milk by diversion.

The Dean witness testified that even though there are closer milk supplies, distant milk is being pooled on both orders. The witness further asserted that transportation credits amplify the pooling of milk on the orders, which does not service the markets' Class I needs. The witness was of the opinion that pooling distant milk by diversion clearly results in disorderly marketing conditions within the two markets. According to the witness, when such milk is pooled, local farmers who are consistently serving the Class I needs of the markets receive a needlessly lower blend price.

According to the Dean witness, the objective of Proposal 4 is to modify the receipt of transportation credits depending on a handler's specific service to the Class I need of the markets and to lower transportation credit payments to those handlers who have higher levels of diversions. The witness stated that the current reimbursement rate of transportation credits is the same for each handler regardless of the level of its relative service to the fluid market. The witness explained that when a handler delivers 100 percent of its receipts to a pool distributing plant, it receives transportation credits at the same rate as a handler delivering only the minimum volume needed to meet the pooling qualifications. The witness conveyed that the handlers meeting only the minimum pooling standards are then able to divert milk which is not actually available to the market. Additionally, the witness indicated that adjusting a handler's receipt of transportation credits in this way will maintain and help extend the transportation credit balancing funds.

The Dean witness acknowledged the need for balancing because distributing plants do not typically need to receive milk every day of the week. However, the witness asserted that unlimited diversions undermine the purpose of the Federal order system. The witness explained that the proposed 30 percent diversion limit on supplemental milk seeking transportation credits is reasonable because a distributing plant typically receives milk five days per week. The need to divert milk 2 days per week, the witness explained, justifies the 30 percent diversion limit. The Dean witness explained that based on data provided by the market administrator, there are handlers in both orders who divert significantly more pounds of milk than the orders need to balance the Class I demands of pool distributing plants, and yet still receive transportation credits.

A post-hearing brief submitted on behalf of Dean reiterated support for the adoption of Proposal 4 provided that Proposals 1 and 3 are adopted. The brief stated that Proposal 4, when adopted in conjunction with Proposals 1 and 3, would tend to limit the abuse of transportation credits on supplemental milk for Class I use as a result of the cap on the receipt of transportation credits by handlers suggested in Proposal 4. The brief also stressed that, if adopted, the provisions detailed in Proposal 4 would lead to the exercise of some control over the amount of milk that would be pooled on the orders through the diversion process.

A dairy farmer who supplies milk to Dean testified in support of Proposal 4. The witness agreed with Dean and other witnesses that orders should only pool the milk of producers who truly serve the Class I needs of the market, otherwise revenue essentially leaves the two marketing areas. According to the witness, this loss of revenue leads area dairy farmers to exit the industry, thereby further reducing the availability of local milk supplies and increasing the need for acquiring more milk produced from far outside the marketing areas. The witness was of the opinion that it is the shipments of supplemental milk into the marketing areas that provide the ability to pool milk by diversion when it is not available to the market.

A witness from SMI testified in support of Proposal 4, provided Proposals 1 and 3 are adopted.

A Kentucky dairy producer testified in support of Proposal 4 and said that supplemental milk receiving transportation credits should be subject to some limits on the amount of additional milk that can be pooled by diversion. The witness was of the opinion that transportation credits give producers located outside the marketing areas a price advantage because their diverted milk receives the blend price of the orders.

A witness appearing on behalf of LOL testified in opposition to Proposal 4. The witness noted that transportation credits were established to attract supplemental milk and to partially offset the cost of hauling supplemental milk into the deficit markets. The witness explained that the orders' specify the conditions that must be met to be eligible to receive transportation credit payments. The current transportation credit provisions, the witness said, already limit payments for supplemental milk from outside the marketing areas to include only the milk of dairy farmers who are not defined as "producers" under the orders. The witness also said that payments are limited to Class I pounds and are not paid on the first 85 miles of hauling milk from farms to the plant receiving supplemental milk.

The LOL witness stressed that additional limitations would do nothing to encourage the delivery of needed supplemental milk into the marketing areas during the short production months. The witness was of the opinion that if the intent is to change the diversion limits of the orders, then those changes should be addressed in a separate hearing.

A post-hearing brief submitted by LOL reiterated its position given at the hearing opposing Proposal 4. The brief also stated that Proposal 4 improperly assumes that all handlers supplying supplemental milk have equal access to distributing plants and that distributing plants' Class I use of milk is the same as the Class I utilization of the two markets.

A witness appearing on behalf of SMA also testified in opposition to Proposal 4. The witness was of the opinion that the orders touch-base and diversion limit standards already provide sufficient safeguards to pooling milk not needed for Class I use. The SMA witness explained that it is difficult to establish specific diversion limits on supplemental milk, as contained in Proposal 4, because of individual differences in the balancing needs of each distributing plant, noting that these needs continually change. The witness emphasized that difficulties in balancing the orders' pool distributing plants exist year-round, and that suppliers sometimes have no control over factors that may alter balancing needs. The witness noted that some of SMA's purchase agreements for supplemental milk included arrangements where transportation credit payments are paid directly to the supplying cooperative. In this regard, the witness expressed concern that providing a separate diversion limit on milk receiving transportation credit payments would unfairly penalize the cooperative when a distributing plant overestimates its need for supplemental milk. The witness stated that extreme variations in daily, weekly, and monthly deliveries to pool distributing plants occur. Relying on market administrator data for January 2004 through October 2005 that showed the ratio of the highest delivery to lowest delivery day, the witness concluded that a 30 percent reserve factor would not have been sufficient to cover distributing plant balancing needs.

The SMA witness also was of the opinion that Proposal 4 would give pool distributing plant operators an advantage over cooperatives who, in their capacity as handlers, are supplying supplemental milk. The witness said that while cooperatives handle the majority of supplemental milk for the orders, they may receive little or no transportation credit payments under Proposal 4. According to the witness, a diversion limit could only benefit those handlers in nearer proximity to the marketing areas.

A post-hearing brief was submitted on behalf of ADCA in opposition to Proposal 4. The brief stressed that the seasonality of production in the southeastern region is the highest in the country and as such, a greater reserve of milk must be available. The brief concluded that Proposal 4 would create inequities between handlers supplying supplemental milk while also encouraging uneconomic movements of milk.

A post-hearing brief was submitted on behalf of DMCI in opposition to Proposal 4. The brief asserted that there are too many unanswered questions as to how Proposal 4 would be applied. The brief stated that a distributing plant's reserve milk needs are an individual business decision and should only be limited by the order's pooling provisions.

A post-hearing brief submitted by DFA and other SMA members reiterated their opposition to Proposal 4. The brief noted that during many months, a 30 percent diversion limit is insufficient to cover balancing needs. Therefore, if Proposal 4 were implemented, the brief said, it could disproportionately affect different supplemental supplies and distributing plants in the marketing areas.

A post-hearing brief was submitted on behalf of Lone Star in opposition to Proposal 4. The premise of its opposition was that Proposal 4 would establish a "one-size-fits-all" diversion limit for all Class I handlers. The brief noted that a distributing plant's reserve milk needs are individual decisions in response to its customer base and seasonal changes in demand. The brief expressed the opinion that the orders already provide for some of the most strict diversion limit standards and touch-base requirements in the Federal order system.

Comments and Exceptions

Comments filed by Dean in response to the tentative partial decision supported the proposed amendments as recommended by USDA. The brief offered support of USDA's alternative to Proposal 4 which, in its opinion, more directly addressed the problem of pooling diverted milk that is associated with supplemental milk supplies. Dean also stated that since the Department's alternative continued to address the intent of Proposal 4, it would support the adoption of Proposals 1 and 3. In brief, Dean expressed that USDA's decision adequately addressed concerns it expressed at the hearing regarding pooling abuse and ensuring that transportation credits only reimburse handlers for a portion of the supplemental hauling costs.

Comments filed on behalf of SMA also expressed support for the amendments recommended in the tentative final decision. SMA stated that the recommended amendments would ensure that there are sufficient funds available to fund the transportation credit balancing fund and that transportation credits would better reflect the changing costs of supplying supplemental milk to the southeastern region. Comments filed on behalf of LOL supported the adoption of Proposals 1 and 3. LOL stated that increasing the transportation credit assessment rates and updating the payment rate to better reflect the cost of fuel were long overdue improvements to the two orders' transportation credit provisions. However, LOL took exception with USDA's recommendation regarding Proposal 4 (pooling of diverted milk through supplemental milk supplies). LOL argued that by not allowing diversions on supplemental milk supplies, supplemental milk suppliers located outside of the marketing areas would bear the burden of balancing the markets' seasonal milk needs. LOL also argued that while USDA asserted in the tentative final decision that limiting diversions on supplemental milk supplies would increase blend prices to the orders' dairy farmers, no analysis was provided to verify the claim. Additionally, LOL wrote that the record reveals the problem with diversions is greater in the Southeast marketing area and therefore unique marketing conditions call for unique provisions in each order.

Findings/Discussion

The issue before USDA in this decision is the consideration of changes to the transportation credit and closely related provisions of the Appalachian and Southeast milk marketing orders. Transportation credit provisions have been a feature of the current orders (and their predecessor orders) since 1996. The need for transportation credit provisions arose from a consistent need to import milk from considerable distances to the marketing areas during certain months of the year when local milk production was not sufficient to meet Class I demands. Transportation credit provisions provide payments to handlers to cover a portion of the costs of hauling supplemental milk supplies into the Appalachian and Southeast marketing areas during the months of January, February, and July through December – a time period during which supplemental milk is needed to meet the demand for Class I milk at distributing plants.

The transportation credit provisions are designed to distinguish between producers who regularly supply the Appalachian and Southeast markets from producers who are <u>supplemental suppliers</u> (not regular suppliers) of these markets. Only milk from producers who are both located outside of the marketing area and who are not considered "producers" of the order is eligible to receive transportation credits.

The record reveals that the Appalachian marketing area, and in particular, the Southeast marketing area, are chronically unable to meet Class I demands. Local milk production relative to demand has declined and is expected to continue declining. Consequently, local milk production is not always able to fulfill the Class I needs of the markets which necessitates the need for supplemental milk from distant locations. As local milk production has eroded, the volume of supplemental milk needed for fluid use has increased, while at the same time the distance from the marketing areas from which the supplies are obtained has increased. This development is particularly evident for the Southeast marketing area. These combined factors have caused the transportation credit balancing fund (TCBF) to be insufficient in covering requested transportation credit payments. The TCBF will likely not be able to cover future requested payments unless the amendments contained in this decision are adopted.

While both marketing areas are able to supply the Class I needs of their respective markets during the spring “flush” months without the need for transportation credits, the record clearly indicates that both orders are unable to fully supply their fluid needs with local production during the last 6 months of the year. The chronic shortage of milk for fluid uses during this period has worsened over time, especially in the Southeast marketing area. Evidence shows that the trend of declining production relative to demand will result in an increased need for supplemental milk supplies and it is likely that this trend will continue into the foreseeable future.

Variable Mileage Rate Factor – A fuel cost adjustor

Based on record evidence, this decision continues to find that the mileage rate factor (MRF) used to determine the payment of transportation credits should include a fuel cost adjustor as proposed in DFA’s Proposal 3.

The original fixed mileage rate for both orders was $0.037 per cwt per mile when the transportation credit provisions were first established in 1996. The computation of the transportation credit payments was based on the total miles supplemental milk was shipped from its point of origination to its destination – the receiving pool distributing plant. In 1997, several amendments were made to the transportation credit provisions of the orders that included a reduction of the mileage rate from $0.037 per cwt per mile to the current $0.035 per cwt per mile.[2]

Additional amendments made in 1997 to the transportation credit provisions specified the exclusion of the first 85 miles supplemental milk was hauled from farms in determining the total miles shipped. Additionally, the 1997 amendments eliminated the use of the orders’ producer settlement fund as a source of revenue for the payment of transportation credits on supplemental

[2] 62 FR 39738

milk when the TCBF was unable to pay net transportation credit claims. No other amendments have been made to the MRF used in the transportation credit provisions since 1997.

Proposal 3 adjusts the MRF accordingly with changes in the cost of diesel fuel. Specifically, the component factors used in the determination of the variable MRF used in the calculation of TCBF payments include: a monthly average diesel fuel price; a reference diesel fuel price; an average mile-per-gallon truck fuel use; a reference hauling cost per loaded mile; and a reference load size.

The Energy Information Administration (EIA) data for the United States and nine U.S. sub-regions are a reliable and reasonable data source to be used in the establishment of certain components required to determine a variable MRF. The data are representative of diesel fuel prices in the Appalachian and Southeast marketing orders and can be relied upon as a basis upon which adjustments to the MRF can be made. Reliance on EIA data, as it is independent and unbiased, will make determination of the MRF objective and uniformly applicable to all handlers.

The proponent's suggested that the use of the Lower Atlantic and Gulf Coast EIA regions in the computation of monthly mileage rates for the Appalachian and Southeast orders is reasonable. The record reveals that the Lower Atlantic and Gulf Coast regions best reflect the Appalachian and Southeast marketing areas geographically. Additionally, the record reflects that the diesel fuel prices reported for these two regions are among the lowest in the country. Hence, it is appropriate to utilize these geographically defined data sets in the mileage rate calculations.

The record reveals that fuel prices and other factors impacting hauling prices have increased greatly since the establishment of transportation credits. Specifically, the record indicates that current diesel fuel prices exceed those prices that prevailed when transportation credit provisions were first implemented in 1996 and amended in 1997. The national average diesel fuel prices in mid-1997 were reported to be approximately $1.15 to $1.17 per gallon, while the national average diesel fuel price in mid-2005 was reported to be $2.20 to $2.50 per gallon. Additionally, while diesel fuel prices have increased, all other costs impacting hauling have also increased. According to the record, EIA data indicates that hauling costs ranged from $1.75 to $1.80 per loaded mile in 1997 and were about $2.35 per loaded mile in January 2006. Establishing a reference diesel fuel price for the MRF calculation using the EIA retail diesel fuel prices from October to November 2003 data is reasonable. According to the EIA data, national average diesel fuel costs during this period demonstrated price stability relative to any other time between 1997 and 2005.

From October to November 2003, national diesel fuel prices fluctuated by only $0.001. Specifically, diesel fuel prices averaged $1.48125 per gallon in October 2003 and $1.48225 per gallon in November 2003. Similarly, the record shows that, for both the Lower Atlantic and Gulf Coasts, diesel fuel prices ranged from $1.4210 to $1.43075 per gallon between October and November 2003. The stability of diesel fuel prices during October to November 2003 supports this period as a reasonable point in time for use in determining a reference diesel fuel price. Therefore, the record supports using $1.42 per gallon as the reference diesel price in the MRF calculation.

Evidence submitted by SMA provides a basis for the determination of a reference average hauling cost per loaded mile as a component for determining the MRF. The evidence consisted of data randomly selected from actual hauler bills paid to cooperatives during October and

November 2003, and October and November 2005. The record supports the use of hauling cost data from October and November 2003 as a basis for the calculation of a reference hauling cost in the MRF consistent with the time frame used for the reference diesel price.

The randomly selected hauling bills depict actual origination and destination points of the milk hauled, miles traveled, and the rates and fuel surcharges per loaded mile for each bill. For the month of October 2005, the data indicate that hauling costs ranged from $1.89 to $2.70 per loaded mile, with an average cost of $2.48 per loaded mile. Data also show that the simple average hauling rate charged per loaded mile in the Southeast marketing area was $1.9332 and $1.8913 in October and November 2003, respectively, yielding a two-month simple average cost of $1.9122 per loaded mile. Therefore, it is reasonable to conclude that a reference hauling rate of $1.91 per loaded mile be used as a component in the MRF calculations[3].

Another component needed in the calculation of the MRF is the average number of miles traveled per gallon of fuel used in transporting milk. Combination truck fuel economy data, regularly maintained by the United States Department of Transportation, indicates that the average miles per gallon for a combination truck was 5.2 in 2002; and 5.1 in 2003. The record also consists of testimony revealing that the dairy industry typically estimates fuel economy at between 5.0-6.0 miles per gallon. Therefore, given that 5.5 miles per gallon is the median point, and the goal of this decision is to promote efficiencies, the record finds that a 5.5-mile per gallon fuel consumption rate is reasonable and should be used to compute the MRF.

---

[3] It should be noted that as a result of the Emergency Hurricane hearing held for the Appalachian, Florida and Southeast marketing orders during the fall of 2004, a reasonable haul rate used to determine how handlers would be compensated for the transportation costs of extraordinary movements of milk was established for a temporary time period. Specifically, a maximum of $2.25 per loaded mile hauling rate was established (69 FR 71697).

The record also supports the use of 48,000 pounds as a reasonable reference load size for determining the MRF. Data reveal that a 5,600 gallon tanker truck at maximum capacity can carry 48,160 pounds of milk. Therefore, 48,000 pounds is appropriate for use as the reference load size component in calculating the MRF.

Proposal 3 would calculate the MRF by averaging the four most recent weeks of weekly retail on-highway diesel prices for both the Lower Atlantic and Gulf Coast, as reported by the EIA. Record evidence supports announcing the monthly MRF at the same time as Advanced Class Prices, on or before the 23rd of the month. This way, handlers will know in advance the rate at which transportation credits will be paid.

Table 1 shows an example of the calculation of the MRF to be used in the transportation credit provisions:

Table 1 -- Example of the Calculation of the Transportation Credit Mileage Rate Factor (MRF) For July 2011 [1].

EIA Weekly Retail On-Highway Diesel Fuel Prices [2]	Lower Atlantic	Gulf Coast
5/23/2011	3.943	3.935
5/30/2011	3.897	3.884
6/06/2011	3.891	3.877
6/13/2011	3.905	3.896

Monthly average diesel fuel price [3]:		**$**	**3.904**	**per gallon**
Reference diesel fuel price:	-	$	1.420	per gallon
Fuel price difference [4]:		$	2.484	per gallon
Reference truck fuel use:	÷		5.5	miles per gallon
Fuel cost adjustment factor [5]:		$	0.451	per loaded mile
Reference haul cost:	+	$	1.910	per loaded mile
Fuel-adjusted haul cost [6]:		$	2.362	per loaded mile

Reference load size:	÷ 48,000	pounds
July 2011 Mileage Rate Factor [7]:	**$ 0.00492**	**dollars per cwt per mile**

1 As announced on June 17, 2011, with the Announcement of Advanced Class Prices.

2 Dollars per gallon. Reported every Monday by the Energy Information Administration of the U.S. Department of Energy.

3 Calculated by rounding down to three decimal places the average of the four most recent weeks of retail on-highway diesel fuel prices for the Lower Atlantic and Gulf Coast EIA regions combined prior to the Advanced Class Price announcement.

4 Calculated by subtracting the reference diesel fuel price of $1.42 per gallon from the calculated average diesel fuel price for the month.

5 Calculated by dividing the fuel price difference by 5.5 miles per gallon fuel use and rounding down to three decimal places.

6 Calculated by adding fuel cost adjustment factor for the month to the reference haul cost of $1.91 per loaded mile.

7 Calculated by dividing the fuel-adjusted haul cost by the number of hundredweights (cwt's) on the reference load size (48,000 pounds = 480 cwt's) and rounding down to five decimal places.

Concern exists that relying on a variable MRF may result in reimbursing the total, rather than a portion, of the hauling costs on supplemental milk. In this regard, a variable MRF that is consistent and reflective of the original intent of the transportation credit provisions of the Appalachian and Southeast orders is necessary. As already discussed, approximately 94 to 95 percent of the total transportation costs on supplemental milk were covered by the TCBF payments for both orders in 1997. However, the record reveals that for 2005, 53 percent and 42 percent of the total transportation costs for the Appalachian and Southeast orders, respectively, were covered by TCBF payments.

Due to a number of unknown variables, it is not possible to predetermine the percent of the total transportation costs that will be reimbursed by TCBF payments. However, the transportation credit provisions already contain precautionary measures for how the MRF is calculated. The record indicates that reference diesel fuel prices and reference hauling costs per loaded mile are components of the mileage rate calculation and are based on 2003 data that are more current than the data considered and adopted in 1997 establishing a fixed mileage rate.

Finally, current transportation credit provisions do not include the first 85 miles that supplemental milk is shipped from farms in determining the total miles shipped. This feature also plays a part to safeguard against excessive transportation credit payments.

Maximum Assessment Rates

This decision continues to find that the transportation credit assessment rate in the Appalachian order should be increased to $0.15 per cwt on all Class I milk pooled.[4]

As discussed earlier in this decision, transportation credit provisions of the Appalachian and Southeast orders were originally established to partially offset the cost of transporting supplemental milk supplies into each marketing area to meet fluid milk demands. The transportation credit assessment rates have been increased twice in an effort to ensure that the TCBF would be sufficient to meet the expected claims. When first established for the Appalachian, Southeast, and predecessor orders (Orders 5, 7, 11 and 46), the maximum transportation credit assessment charged to Class I handlers was $0.06 per cwt for each order. The first increase, adopted in 1997, raised the maximum assessment by $0.005 per cwt for the Appalachian order and by $0.01 per cwt for the Southeast order.[5] The second increase in the maximum assessment rates for both orders became effective in November 2005.[6] The maximum assessment rates for both orders were increased by $0.03 per cwt, from $0.065 to $0.095 per cwt for the Appalachian order, and from $0.070 to $0.10 per cwt for the Southeast order.

The hearing record reveals that the Appalachian order was able to pay all transportation credit claims for every month since implementation through September 2004. For the remainder

[4] The Southeast order transportation credit assessment rate has subsequently been increased in a separate rulemaking proceeding (73 FR 14153).
[5] 62 FR 39738
[6] 70 FR 59221

of 2004, the Appalachian Market Administrator began prorating the transportation credit payments.

Specifically, the record shows that for the Appalachian order, 41, 39, and 43 percent of the transportation credit claims were paid in October, November, and December of 2004, respectively. The Appalachian order paid 90 percent and 31 percent of the claims in September and October of 2005, respectively. Despite the assessment rate increase that became effective November 2005, the evidence indicates that only 58 percent of the transportation credit claims for the Appalachian order were paid. Table 2 below illustrates the percent paid from the TCBF for the Appalachian order:

Table 2 -- Percent of Transportation Credits Paid

Percent of Transportation Credits Paid	Appalachian Marketing Area FO 5
Jul 04	100.0
Aug 04	100.0
Sep 04	100.0
Oct 04	40.6
Nov 04	39.0
Dec 04	45.7
Jul 05	100.0
Aug 05	100.0
Sep 05	91.9
Oct 05	30.6
Nov 05 *	58.5

* Effective November 1, 2005, the transportation credit assessment rates were increased by 3 cents for the Appalachian order.
Source: Appalachian Market Administrator data.

The record demonstrates that at a transportation credit mileage rate of $0.0035 per cwt per mile, the TCBF assessment for Appalachian marketing area has been insufficient to pay all transportation credit claims, especially during the time when payment of credits was most needed. Preventing the prorating of the transportation credit reimbursement payments would have required a higher assessment rate. Evidence submitted by the SMA witness showed that the maximum transportation credit assessment rate for the Appalachian order would have needed to be $0.0889 and $0.0953 per cwt, for 2004 and 2005, respectively. Such evidence further supports the need to increase the transportation credit assessment rate.

The adoption of the variable MRF that is calculated and adjusted with changes in diesel fuel prices (as presented in Proposal 3), will most likely increase the current mileage rate of $0.035 per cwt per mile. Relying on EIA data, the record reveals that applying the calculated mileage rates to the months of July through December 2005 would have resulted in transportation credit mileage rates ranging from $0.0432 to$ 0.0461 per cwt per mile for both orders. If a transportation credit mileage reimbursement rate of $0.046 per cwt per mile had been in place, rather than the current rate of $0.035 cents per cwt, the maximum transportation credit assessments needed for the Appalachian order to ensure that the TCBF covered all claims, would have been $0.133 and $0.1415 per cwt for 2004 and 2005, respectively. This analysis supports concluding, and this final decision continues to find, that increasing the Appalachian order maximum transportation credit assessment rate, as contained in Proposal 1, by $0.055 , to $0.15 per cwt is warranted.

Precautionary measures, which decrease the likelihood that the rate of assessments occurs in excess of actual handler claims, are currently provided for within the transportation credit provisions of the orders. The transportation credit provisions provide the market administrator the authority to reduce or waive assessments as necessary to maintain sufficient fund balances for the payment of the transportation credits requested. Therefore, increasing the maximum transportation credit assessment rate will not result in an accumulation of funds beyond what is needed to pay transportation credit claims and no additional precautionary measures are necessary beyond those currently provided.

The record supports concluding that local milk production is expected to continue declining within both marketing areas and will result in an even greater reliance on supplemental milk to meet the fluid milk needs of the markets. Record evidence shows a constant increase in both the volume and the distance, from which supplemental milk supplies are obtained. It is reasonable to conclude that future transportation credit claims will increase. In this regard, it is important to prevent exhausting the TCBF before the payment of claims on the supplemental milk have been met. Doing so is consistent with the fundamental purposes of the transportation credit provisions. Therefore, increasing the transportation credit assessment rate as contained in Proposal 1, will better assure that the rate of assessments will keep pace with the payments from the TCBF.

Diversion Limit Standard for Supplemental Milk

The intent of a proposal offered by Dean, published in the hearing notice as Proposal 4, seeks to provide a method to limit the amount of additional milk being pooled by diversion on the Appalachian and Southeast orders. As proposed, Dean’s proposal would change the amount of transportation credits paid on eligible supplemental milk depending on the amount of milk delivered to plants other than pool distributing plants – this includes diversions to plants located outside of the marketing areas and deliveries to pool supply plants. Simply put, the greater the volume of diversions, the lower the amount of transportation credits paid. In this regard, Dean's proposal attempts to provide an incentive to limit diversions <u>indirectly</u> by reducing transportation credits paid on supplemental milk. This decision agrees with the need to limit pooling diverted milk on the orders that is linked to supplemental milk deliveries to distributing plants. Rather than attempt to create disincentives to pooling diverted milk indirectly, this decision addresses the issue <u>directly</u> by adopting a zero diversion limit standard on supplemental milk deliveries to distributing plants that receive transportation credits.

The record reveals that the volume of supplemental milk needed to serve the Class I needs of the marketing areas has grown over time and is expected to continue growing. Supplemental milk is representing a greater percentage of the Southeast market's total Class I utilization. The record reveals that for the months of July through December, supplemental milk accounted for 16 percent of total Class I utilization in 2004. For 2005, such supplemental milk as a percent of total Class I utilization increased to 19 percent.

In addition, the record indicates that, for the Southeast marketing area, the monthly weighted average distance supplemental milk eligible to receive transportation credits traveled ranged from 578 to 627 miles, during July through December 2000. During July through November 2005, the weighted average distance increased, ranging from 682 to 755 miles. The amount of supplemental milk receiving transportation credits during 2005 was nearly 686 million pounds. In 2000 and 2004 the amounts were 363 million and 541 million, respectively. This represents an 89 percent increase in the amount of supplemental milk receiving transportation credits from 2000 to 2005 and a 27 percent increase since 2004.

For the Southeast order, the record reveals that total diversions at locations outside of the

Appalachian and Southeast marketing areas totaled 883.4 million pounds in 2004. Total diversions outside of the marketing areas for 2005, not including the months of November and December, were 965.6 million pounds, an increase of 9.3 percent from 2004. Such data for November and December 2005 are not contained in the record. For the months of January through June, when transportation credits <u>are not</u> available, total diversions outside the marketing areas increased almost 18 percent from 2004 to 2005. During the time period of July through October, when transportation credits <u>are</u> available, such diversions increased over 27 percent from 2004 to 2005. It is reasonable, given the trend of the data, that the percentage increase from 2004 would have been greater than 27 percent if data had been available for the months of November and December 2005.

It is reasonable to conclude that diversions outside the Appalachian and Southeast marketing areas are most likely attributed to supplemental milk that is eligible to receive transportation credits. The record reveals that for the Southeast marketing area, the 27 percent increase in the amount of milk receiving transportation credits from 2004 through 2005 corresponds with the 27 percent increase of diversions outside the marketing areas between 2004 and 2005. It is also reasonable to conclude from the record that it is in the interest of the handler supplying supplemental milk, and in this case, the cooperatives in their capacity as handlers, to maximize the value of diversions. Doing so would require pooling the maximum amount of diverted milk to the closest location from where supplemental milk was sourced. Therefore, relying on data provided by the Market Administrator for the Southeast marketing area for the months when transportation credits are available, the calculated total maximum diverted pounds associated with supplemental milk would have totaled over 178 million pounds in 2004, and over 226 million pounds in 2005. On the basis of these calculations, an estimate of diversions attributed to supplemental milk is 64 percent of total diversions for both 2004 and 2005, ranging from 56 percent to 77 percent of the total known diversions outside the marketing areas.

The contribution from diversions associated with supplemental milk as compared to total outside diversions is nearly three times greater than the contribution of the supplemental milk to Class I utilization. As previously discussed, for 2004 and 2005, supplemental milk represented about 15.9 and 19 percent, respectively, of total Class I utilization. However, estimated diversions attributable to supplemental milk represent approximately 64 percent of total diversions. Clearly, not only do transportation credits offset the costs of hauling supplemental milk to the markets, they also contribute to pooling much more milk on the orders through the diversion process.

For the Appalachian order, data contained in the record is much more limited for determining the diversions arising from transportation credit eligible supplemental milk. What can be reasonably concluded is that the pooling of diverted milk linked to supplemental milk is not occurring on nearly the magnitude as is the case for the Southeast order. For the Appalachian order, evidence indicates that total diversions at locations outside of the Appalachian and Southeast marketing areas, for the time period of January through June, increased by 64.4 percent from 2004 to 2005. Total diversions from the time period of July through November, when transportation credits are available, decreased over 20 percent from 2004 to 2005.

For the Appalachian order, only 2 months of data – October and November 2005 - is available to estimate the maximum diversions that could be associated with supplemental milk. Relying on Appalachian Market Administrator data, it is estimated that the maximum diversions from transportation credit eligible milk during October and November 2005 were approximately 34 percent and 28 percent, respectively, of the total diversions at locations outside the Appalachian and Southeast marketing areas. Supplemental milk on the Appalachian order for October and November 2005 was approximately 19 percent, and 16 percent, respectively, of the total Class I milk pooled.

Pooling the diversions of this milk differs from pooling diverted milk that is part of the regular supply of milk of the marketing area. Pooling diverted milk associated with transportation credit eligible supplemental milk, allows more milk to be pooled on the order than normal. Pooling this milk is different than pooling milk that is part of the regular supply for the marketing area. The difference is that producers of milk eligible to receive transportation credits <u>are not</u> a part of the regular and consistent supply of milk that serves the Class I needs of the markets. In fact, transportation credit qualifying criteria <u>exclude</u> the milk of producers who are regularly pooled on the orders. These producers are, therefore, supplemental suppliers of milk to the Appalachian and Southeast marketing areas.

Pooling diverted milk arising from supplemental milk eligible to receive transportation credits not only offsets the intended benefit of increasing the supply of milk for fluid uses, it also lowers blend prices to those producers who regularly and consistently supply the Class I needs of the markets. Higher blend prices provide important economic signals—the incentive to: 1) continue supplying the markets; 2) increase local production; and 3) attract the milk of producers to become regular and consistent suppliers.

Lowering blend prices received by producers who regularly supply the markets relative to producers who supply supplemental milk sends contradictory pricing signals. Lower blend prices do not send the proper price signals to local producers to increase local production or to continue supplying the Class I needs of the markets. Furthermore, lower blend prices fail to create the price signals necessary to attract a regular and consistent milk supply.

The availability of transportation credits on supplemental milk has clearly provided a platform to pool additional diverted milk at locations distant to the marketing areas. Milk diverted from supplemental producers is more likely to be diverted at locations far from the marketing areas. The record reveals that suppliers of the supplemental milk to the Appalachian and Southeast marketing areas pool diverted milk at locations as far away as California and Utah. Supplemental milk suppliers benefit in three ways: 1) receiving reimbursement for costs of transporting milk to the deficit markets; 2) receiving cost savings from the diverted milk not transported to the marketing areas; and 3) receiving higher blend prices on the diverted milk that would have otherwise been pooled on a different order with a typically lower blend price.

The pooling of milk that is not part of the regular and consistent supply of milk which serves the Class I needs of the market is contradictory to the intent of an order's pooling standards and provisions. The pooling standards of the orders serve to identify the milk of producers who regularly and consistently serve the Class I needs of the marketing areas. Pooling milk that is available but not immediately needed for Class I use is provided through diversion limit standards. Diversion limit standards provide the criteria for determining how much additional milk can be pooled on the orders. Diverted milk in this context reflects the legitimate reserve supply of milk available to serve the Class I needs of the marketing areas and, therefore, receives the blend price of the orders.

Since implementation of Federal milk order reform, there have been many formal rulemakings that have amended orders to more properly identify the milk of producers which should and should not be pooled on the orders. The milk of producers who are the consistent and reliable suppliers serving the Class I needs of the market should be pooled even when it is not immediately needed for Class I use. However, this foundational principle of orderly marketing in milk marketing orders is essentially disregarded for 6 months each year when the orders allow the pooling of diverted milk from producers who are specifically identified as not being "producers" under either of the orders.

The lowering of blend prices by pooling such diverted milk is an unintended outcome not foreseen when the transportation credit provisions of the Appalachian and Southeast orders were implemented and amended. As the blend prices are reduced so is the incentive for local milk production. The markets become less capable of supplying their own Class I needs and supplemental milk supplies needed to meet Class I needs are not likely to be supplied without reliance on additional transportation credits.

The pooling of diverted milk associated with supplemental milk would seem to offer substantial benefits to cooperative suppliers. The record reveals that when transportation credits were first implemented, well over 90 percent of hauling costs were offset. The record further reveals that more recent conditions suggest that only about 45 percent is being reimbursed. This clearly represents a burden borne by the cooperatives supplying supplemental milk.

Pooling diverted milk at locations far from the marketing areas based on supplemental milk eligible to receive transportation credits would provide additional revenue to help offset hauling costs not covered by the current transportation credit assessment rates. This diverted milk receives the blend price of the order where it is pooled. The benefit is that the blend price received on such diverted milk, on either the Appalachian or Southeast order, is historically higher than the price the milk would otherwise receive.

As presented above, this final decision adopts a variable mileage rate factor that will reimburse hauling costs at a level more reflective of actual costs, in addition to a significantly higher transportation credit assessment. To the extent that it is necessary to offset the higher costs of transporting supplemental milk, the adoption of a variable MRF and the increase in the transportation credit assessment rates should significantly reduce or eliminate the need to seek generating revenue to offset hauling costs at the expense of the producers who are regularly and consistently supplying milk to meet the Class I needs of the two marketing areas.

LOL took exception with the proposed zero diversion limit standard arguing that it would shift the burden of balancing the southeastern markets' seasonal milk needs onto the markets' supplemental milk suppliers. LOL also argued that USDA should provide an analysis to verify that adoption of this standard would, in fact, increase the orders' blend prices.

The transportation credit provisions of the Southeast and Appalachian orders are designed to attract supplemental milk supplies for Class I use when the orders' regular supplies cannot meet demand. Supplemental suppliers choose to provide this service and are subsequently compensated by receiving the orders' blend price and the ability to receive a transportation credit to reimburse them for part of the hauling cost. If, at any time, a supplemental supplier does not believe they are adequately compensated for their service, they may cease providing supplemental supplies. This decision continues to find that allowing milk diversions on supplemental milk supplies receiving a transportation credit lowers the TCBF monies available to supplemental milk loads that are actually delivered to the southeastern markets, and ultimately decreases the blend price paid to the orders' producers. A quantitative assessment is not necessary to conclude that the pooling of this diverted milk on the orders is disorderly and should not occur.

Rulings on Proposed Findings and Conclusions

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

General Findings

The findings and determinations hereinafter set forth supplement those that were made when the Appalachian and Southeast orders were first issued and when they were amended. The previous findings and determinations are hereby ratified and confirmed, except where they may conflict with those set forth herein.

The following findings are hereby made with respect to the aforesaid marketing agreements and orders:

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

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

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

Rulings on Exceptions

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

Marketing Agreement and Order

Annexed hereto and made a part hereof are two documents – a Marketing Agreement regulating the handling of milk and an Order amending the order regulating the handling of milk in the Appalachian and Southeast marketing areas, that was approved by producers and published in the Federal Register on October 25, 2006 (71 FR 62377). These documents have decided upon as the detailed and appropriate means of effectuating the foregoing conclusions.

It is hereby ordered that this entire decision and the Marketing Agreement annexed hereto be published in the Federal Register.

Determination of Producer Approval and Representative Period

The month of July 2013 is hereby determined to be the representative period for the purpose of ascertaining whether the issuance of the order, as amended and as hereby proposed to be amended, regulating the handling of milk in the Appalachian and Southeast marketing areas is approved or favored by producers, as defined under the terms of the order as hereby proposed to be amended, who during such representative period were engaged in the production of milk for sale within the aforesaid marketing area.

List of Subjects in 7 CFR Parts 1005 and 1007

Milk Marketing Orders.

Order Amending the Order Regulating the Handling of Milk in the Appalachian and Southeast Marketing Areas

This order shall not become effective until the requirements of § 900.14 of the rules of practice and procedure governing proceedings to formulate marketing agreements and marketing orders have been met.

Findings and Determinations

The findings and determinations hereinafter set forth supplement those that were made when the orders were first issued and when they were amended. The previous findings and determinations are hereby ratified and confirmed, except where they may conflict with those set forth herein.

(a) Findings. A public hearing was held upon certain proposed amendments to the tentative marketing agreements and to the orders regulating the handling of milk in the Appalachian, Florida and Southeast marketing areas. The hearing was held pursuant to the provisions of the Agricultural Marketing Agreement Act of 1937, as amended (7 U.S.C. 601-674), and the applicable rules of practice and procedure (7 CFR part 900).

Upon the basis of the evidence introduced at such hearing and the record thereof, it is found that:

(1) The said orders as hereby amended, and all of the terms and conditions thereof, will tend to effectuate the declared policy of the Act;

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

(3) The said orders as hereby amended regulate the handling of milk in the same manner as, and are applicable only to persons in the respective classes of industrial or commercial activity specified in, a marketing agreement upon which a hearing has been held.

Order Relative to Handling

It is therefore ordered, that on and after the effective date hereof, the handling of milk in the Appalachian and Southeast marketing areas shall be in conformity to and in compliance with the terms and conditions of the orders, as amended, and as hereby amended, as follows:

For the reasons set forth in the preamble, 7 CFR parts 1005and 1007 are proposed to be amended as follows:

1. The authority citation for 7 CFR parts 1005 and 1007 continues to read as follows:

Authority: 7 U.S.C. 601-674, and 7253.

PART 1005 - MILK IN THE APPALACHIAN MARKETING AREA

2. Section 1005.13 is amended by revising paragraphs (d)(3) and (d)(4) to read as follows:

§ 1005.13 Producer milk.

* * * * *

(d) * * *

(3) The total quantity of milk so diverted during the month by a cooperative association shall not exceed 25 percent during the months of July through November, January, and February, and 35 percent during the months of December and March through June, of the producer milk that the cooperative association caused to be delivered to, and physically received at, pool plants during the month, excluding the total pounds of bulk milk received directly from producers meeting the conditions as described in § 1005.82(c)(2)(ii) and (iii), and for which a transportation credit is requested;

(4) The operator of a pool plant that is not a cooperative association may divert any milk that is not under the control of a cooperative association that diverts milk during the month pursuant to paragraph (d) of this section. The total quantity of milk so diverted during the month shall not exceed 25 percent during the months of July through November, January, and February, and 35 percent during the months of December and March through June, of the producer milk

physically received at such plant (or such unit of plants in the case of plants that pool as a unit pursuant to § 1005.7(d) during the month, excluding the quantity of producer milk received from a handler described in § 1000.9(c) of this chapter and excluding the total pounds of bulk milk received directly from producers meeting the conditions as described in § § 1005.82(c)(2)(ii) and (iii), and for which a transportation credit is requested;

* * * * *

3. Section 1005.81 is amended by revising paragraphs (a) and (b) to read as follows:

§ 1005.81 Payments to the transportation credit balancing fund.

(a) On or before the 12th day after the end of the month (except as provided in § 1000.90 of this chapter), each handler operating a pool plant and each handler specified in § 1000.9(c) shall pay to the market administrator a transportation credit balancing fund assessment determined by multiplying the pounds of Class I producer milk assigned pursuant to § 1005.44 by $0.15 per hundredweight or such lesser amount as the market administrator deems necessary to maintain a balance in the fund equal to the total transportation credits disbursed during the prior June-February period. In the event that during any month of the June-February period the fund balance is insufficient to cover the amount of credits that are due, the assessment should be based upon the amount of credits that would had been disbursed had the fund balance been sufficient.

(b) The market administrator shall announce publicly on or before the 23rd day of the month (except as provided in § 1000.90) the assessment pursuant to paragraph (a) of this section for the following month.

4. Section 1005.82 is amended by revising paragraphs (d)(2)(ii) and (d)(3)(iv) to read as

follows:

§ 1005.82 Payments from the transportation credit balancing fund.

*   *   *   *   *

(d)   *   *   *

(2)   *   *   *

(ii) Multiply the number of miles so determined by the mileage rate for the month computed pursuant to § 1005.83(a)(6);

*   *   *   *   *

(3)   *   *   *

(iv) Multiply the remaining miles so computed by the mileage rate for the month computed pursuant to § 1005.83(a)(6);

*   *   *   *   *

5. Add Section 1005.83 to read as follows:

§ 1005.83 Mileage Rate for the Transportation Credit Balancing Fund.

(a) The market administrator shall compute a mileage rate each month as follows:

(1) Compute the simple average rounded to three decimal places for the most recent four (4) weeks of the Diesel Price per Gallon as reported by the Energy Information Administration of the United States Department of Energy for the Lower Atlantic and Gulf Coast Districts combined.

(2) From the result in paragraph (a)(1) in this section subtract $1.42 per gallon;

(3) Divide the result in paragraph (a)(2) of this section by 5.5, and round down to three

decimal places to compute the fuel cost adjustment factor;

(4) Add the result in paragraph (a)(3) of this section to $1.91;

(5) Divide the result in paragraph (a)(4) of this section by 480;

(6) Round the result in paragraph (a)(5) of this section down to five decimal places to compute the mileage rate.

(b) The market administrator shall announce publicly on or before the 23rd day of the month (except as provided in § 1000.90 of this chapter) the mileage rate pursuant to paragraph (a) of this section for the following month.

PART 1007 – MILK IN THE SOUTHEAST MARKETING AREA

6. Section 1007.13 is amended by revising paragraphs (d)(3) and (d)(4) to read as follows:

§ 1007.13 Producer milk.

*   *   *   *   *

(d)   *   *   *

(3) The total quantity of milk diverted during the month by a cooperative association shall not exceed 25 percent during the months of July through November, January, and February, and 35 percent during the months of December and March through June, of the producer milk that the cooperative association caused to be delivered to, and physically received at, pool plants during the month, excluding the total pounds of bulk milk received directly from producers meeting the conditions as described in section 1007.82(c)(2)(ii) and (iii), and for which a transportation credit is requested;

(4) The operator of a pool plant that is not a cooperative association may divert any milk that is not under the control of a cooperative association that diverts milk during the month pursuant to paragraph (d) of this section. The total quantity of milk so diverted during the month shall not exceed 25 percent during the months of July through November, January and February, and 35 percent during the months of December and March through June of the producer milk physically received at such plant (or such unit of plants in the case of plants that pool as a unit pursuant to § 1007.7(e)) during the month, excluding the quantity of producer milk received from a handler described in § 1000.9(c) of this chapter, excluding the total pounds of bulk milk received directly from producers meeting the conditions as described in section 1007.82(c)(2)(ii) and (iii), and for which a transportation credit is requested.

* * * * *

7. Section 1007.81 is amended by revising paragraph (b) to read as follows:

§ 1007.81 Payments to the transportation credit balancing fund.

* * * * *

(b) The market administrator shall announce publicly on or before the 23rd day of the month (except as provided in § 1000.90 of this chapter) the assessment pursuant to paragraph (a) of this section for the following month.

8. Section 1007.82 is amended by revising paragraphs (d)(2)(ii) and (d)(3)(iv) to read as follows:

§ 1007.82 Payments from the transportation credit balancing fund.

* * * * *

(d) * * *

(2) * * *

(ii) Multiply the number of miles so determined by the mileage rate for the month computed pursuant to § 1007.83(a)(6); * * * * *

(3) * * *

(iv) Multiply the remaining miles so computed by the mileage rate for the month computed pursuant to § 1007.83(a)(6);

* * * * *

9. Add a new Section 1007.83 to read as follows:

§ 1007.83 Mileage Rate for the Transportation Credit Balancing Fund.

(a) The market administrator shall compute the mileage rate each month as follows:

(1) Compute the simple average rounded to three decimal places for the most recent 4 weeks of the Diesel Price per Gallon as reported by the Energy Information Administration of the United States Department of Energy for the Lower Atlantic and Gulf Coast Districts combined.

(2) From the result in paragraph (a)(1) in this section subtract $1.42 per gallon;

(3) Divide the result in paragraph (a)(2) of this section by 5.5, and round down to three decimal places to compute the fuel cost adjustment factor;

(4) Add the result in paragraph (a)(3) of this section to $1.91;

(5) Divide the result in paragraph (a)(4) of this section by 480;

(6) Round the result in paragraph (a)(5) of this section down to five decimal places to

compute the MRF.

(b) The market administrator shall announce publicly on or before the 23rd day of the month (except as provided in § 1000.90 of this chapter) the mileage rate pursuant to paragraph (a) of this section for the following month.

[This marketing agreement will not appear in the Code of Federal Regulations.]

Marketing Agreement Regulating the Handling of Milk in Certain Marketing Areas

The parties hereto, in order to effectuate the declared policy of the Act, and in accordance with the rules of practice and procedure effective thereunder (7 CFR part 900), desire to enter into this marketing agreement and do hereby agree that the provisions referred to in paragraph I hereof, as augmented by the provisions specified in paragraph II hereof, shall be and are the provisions of this marketing agreement as if set out in full herein.

I. The findings and determinations, order relative to handling, and the provisions of § _____ to _____ [7] all inclusive, of the order regulating the handling of milk in the __________[8] marketing area (7 CFR Part ______[9]) which is annexed hereto; and

II. The following provisions: § _________[10] Record of milk handled and authorization to correct typographical errors.

(a) Record of milk handled. The undersigned certifies that he/she handled during the month of __________[11], ________ hundredweight of milk covered by this marketing agreement.

---

[7] First and last section of order.
[8] Name of order.
[9] Appropriate Part number.
[10] Next consecutive section number.
[11] Appropriate representative period for the order

(b) Authorization to correct typographical errors. The undersigned hereby authorizes the Deputy Administrator, or Acting Deputy Administrator, Dairy Programs, Agricultural Marketing Service, to correct any typographical errors which may have been made in this marketing agreement.

Effective date. This marketing agreement shall become effective upon the execution of a counterpart hereof by the Department in accordance with Sec. 900.14(a) of the aforesaid rules of practice and procedure.

In Witness Whereof, The contracting handlers, acting under the provisions of the Act, for the purposes and subject to the limitations herein contained and not otherwise, have hereunto set their respective hands and seals.

Signature

By (Name)---

(Title)--

(Address)---

(Seal)

Attest---

Dated: February 25, 2014

Rex A. Barnes
Associate Administrator

BILLING CODE 3410-02 P

[FR Doc. 2014-04693 Filed 03/06/2014 at 8:45 am; Publication Date: 03/07/2014]