

**7 CFR Parts 1001, 1002, 1004, 1005, 1006, 1007, 1011, 1012, 1013, 1030, 1032, 1033, 1036, 1040, 1044, 1046, 1049, 1050, 1064, 1065, 1068, 1075, 1076, 1079, 1106, 1124, 1126, 1131, 1134, 1135, 1137, 1138, 1139**

[Docket No. AO-14-A64, etc.; DA-90-017; RIN: 0581-AA37]

**Milk in the New England and Other Marketing Areas; Second Amplified Decision**

7 CFR part	Marketing area	AO Nos.
1001	New England .....	AO-14-A64
1002	New York-New Jersey .....	AO-71-A79
1004	Middle Atlantic .....	AO-160-A67
1005	Carolina .....	AO-388-A3
1006	Upper Florida .....	AO-356-A29
1007	Southeast .....	AO-366-A33
1011	Tennessee Valley .....	AO-251-A35
1012	Tampa Bay .....	AO-347-A32
1013	Southeastern Florida .....	AO-286-A39
1030	Chicago Regional .....	AO-361-A28
1032	Southern Illinois-Eastern Missouri .....	AO-313-A39
1033	Ohio Valley .....	AO-166-A60
1036	Eastern Ohio-Western Pennsylvania .....	AO-179-A55
1040	Southern Michigan .....	AO-225-A42
1044	Michigan Upper Peninsula .....	AO-299-A26
1046	Louisville-Lexington-Evansville .....	AO-123-A62
1049	Indiana .....	AO-319-A38
1050	Central Illinois .....	AO-355-A27
1064	Greater Kansas City .....	AO-23-A60
1065	Nebraska-Western Iowa .....	AO-86-A47
1068	Upper Midwest .....	AO-178-A45
1075	Black Hills, South Dakota .....	AO-248-A21
1076	Eastern South Dakota .....	AO-260-A30
1079	Iowa .....	AO-295-A41
1106	Southwest Plains .....	AO-210-A52
1124	Pacific Northwest .....	AO-368-A19
1126	Texas .....	AO-231-A60
1131	Central Arizona .....	AO-271-A29
1134	Western Colorado .....	AO-301-A22
1135	Southwestern Idaho-Eastern Oregon .....	AO-380-A9
1137	Eastern Colorado .....	AO-326-A26
1138	New Mexico-West Texas .....	AO-335-A36
1139	Great Basin .....	AO-309-A30

**AGENCY:** Agricultural Marketing Service, USDA.

**ACTION:** Second Amplified Decision.

**SUMMARY:** On May 16, 1996, the United States District Court for the District of Minnesota issued an opinion and order that directed the Secretary of Agriculture to issue a second Amplified Decision that more fully explains the conclusions reached in a Final Decision published in the Federal Register on March 5, 1993, and in the first Amplified Decision published in the Federal Register on August 17, 1994. This document responds to that order and supplements and clarifies the findings and conclusions of the Final Decision and first Amplified Decision.

**FOR FURTHER INFORMATION CONTACT:** Gino M. Tosi, Marketing Specialist, Order Formulation Branch, USDA/AMS/Dairy Division, Room 2968, South Building, P.O. Box 96456, Washington, DC 20090-6456, (202) 720-6274.

**SUPPLEMENTARY INFORMATION:** When the administrative proceeding in this matter was initiated, the Notice of Hearing listed separately the Lubbock-Plainview, Texas (Part 1120); the Texas Panhandle (Part 1132); and Rio Grande Valley (Part 1138) orders. These orders were merged effective December 1, 1991, under the name of the New Mexico-West Texas order, which is 7 CFR Part 1138. Additionally, the Georgia (Part 1007), Alabama-West Florida (Part 1093), New Orleans-Mississippi (Part 1094), Greater Louisiana (Part 1096), and Central Arkansas (Part 1108) orders were merged to form a new order named the Southeast order effective July 1, 1995 and is now 7 CFR Part 1007. The Memphis, Tennessee and Nashville, Tennessee, Orders were terminated effective July 31, 1993, and the Paducah, Kentucky, order was terminated on November 1, 1995.

Prior documents in this proceeding

Advance Notice of Proposed Rulemaking: Issued March 29, 1990; published April 3, 1990 (55 FR 12369).

Notice of Hearing: Issued July 11, 1990; published July 17, 1990 (55 FR 29034).

Extension of Time for Filing Briefs and Reply Briefs: Issued March 28, 1991; published April 3, 1991 (56 FR 13603).

Recommended Decision: Issued November 6, 1991; published November 22, 1991 (56 FR 58972).

Extension of Time for Filing Exceptions: Issued December 24, 1991; published January 6, 1992 (57 FR 383).

Final Decision: Issued February 5, 1993; published March 5, 1993 (58 FR 12634).

Proposed Termination of Order: Issued April 20, 1993; published April 27, 1993 (58 FR 25577).

Final Rule and Order: Issued April 20, 1993; published May 11, 1993 (58 FR 27774).

Referendum Order: Issued June 25, 1993; published July 1, 1993 (58 FR 35362).

Final Rule and Withdrawal: Issued August 9, 1993; published August 17, 1993 (58 FR 43518).

Correction of Final Rule: Issued November 29, 1993; published December 6, 1993 (58 FR 64110).

Amplified Final Decision: Issued August 10, 1994; published August 17, 1994 (59 FR 42422).

Related Prior Documents Germane to this Amplified Decision II

M-W Replacement:

Notice of Hearing: Issued May 12, 1992; published May 15, 1992 (57 FR 20790).

Recommended Decision: Issued August 3, 1994; published August 6, 1994 (59 FR 40418).

Final Decision: Issued January 27, 1995; published February 7, 1995 (60 FR 7290).

Final Rule: Issued April 6, 1995; published April 14, 1995 (60 FR 18952).

Examples of Setting/Changing Class I Differentials:

Final Decision: Issued October 7, 1966; published October 13, 1966 (31 FR 13272).

Final Decision: Issued August 14, 1991; published August 27, 1991 (56 FR 42240).

Final Decision: Issued September 27, 1978; published October 2, 1978 (43 FR 45520).

#### Preliminary Statement

A public hearing was held upon proposed amendments to the marketing agreements and the orders regulating the handling of milk in the New England and other marketing areas. The hearing was held, pursuant to the provisions of the AMAA and the applicable rules of practice (7 CFR Part 900), at Eau Claire, Wisconsin; Minneapolis, Minnesota; St. Cloud, Minnesota; Syracuse, New York; Tallahassee, Florida; and Irving, Texas, on September 5, 1990, through November 20, 1990. Notice of such hearing was issued on July 11, 1990, and published July 17, 1990 (55 FR 29034).

Upon the basis of the evidence introduced at the hearing and the record thereof, the Administrator, on November 6, 1991, issued his recommended decision containing notice of the opportunity to file written exceptions thereto. Following the submission of exceptions and comments on the recommended decision, a Final Decision was issued on February 5, 1993.

#### The Court's First Memorandum Opinion and Order

On April 14, 1994, the United States District Court for the District of Minnesota issued a memorandum opinion and order. The Court held that the Secretary of Agriculture's Final Decision for the "1990 National Hearing" on amending Federal milk orders was deficient in part. The Court found that the Secretary's decision to retain the existing Class I pricing structure was tantamount to a finding that the structure continued to satisfy the requirements of the AMAA as set out in § 608c(18). The Court stated this conclusion might or might not be supported by evidence from the 1990 National Hearing, but since explicit findings and explanations relative to the § 608c(18) factors were not issued, the Court was unable to make that determination. The final decision was remanded to the Secretary for 120 days for filing of an Amplified Decision.

An Amplified Decision, published in the Federal Register on August 17, 1994, provided additional findings and conclusions that addressed the material issue on the record of the 1990 National Hearing concerning Class I milk pricing and related issues. (See 59 FR 42422 *et seq.*) That document responded to the Court's questions and provided an amplified explanation of why the Secretary decided not to change the Class I pricing structure of Federal milk marketing orders and how such determination complied with the pricing requirements of § 608c(18) of the AMAA.

On May 16, 1996, the United States District Court for the District of Minnesota issued a second opinion and order expressing continued dissatisfaction with the Secretary's Final and Amplified Decisions. This second opinion again remanded the Final Decision to the Secretary of Agriculture for 120 days. According to the Court, the Final Decision, as further explained in the first Amplified Decision, failed to address adequately the Secretary's compliance with § 608c(18) of the AMAA.

After reviewing in detail the Court's second opinion and giving substantial consideration to the Court's views, the Secretary will attempt again to explain the final decisions to the Court. In this regard, however, the Secretary must first observe that the Court's conclusions appear to be based on an incomplete understanding of the purpose and evolutionary development of milk marketing orders which the Secretary attempts to clarify herein. Additionally, the approach to establishing minimum

milk prices apparently envisioned by the Court would be virtually impossible to implement and, if attempted, would result in disorderly and unsettled market conditions. Therefore, before exploring in detail the Court's second opinion and the Secretary's Final and Amplified Decisions, the historical development of the classified pricing system, the realities of the dairy industry as it relates to the marketing of milk, the precise nature of the rulemaking underlying this litigation and the current status of the classified pricing system are considered.

#### Development of Classified Pricing for Milk

Milk marketing orders are not imposed by the Federal government. To the contrary, dairy producers, often with the support of handlers, petition the Secretary to create an order regulating the handling of milk. The Secretary then investigates market conditions affecting supply and demand in the proposed order area, including the price and availability of feed. The Secretary then proposes an order which producers are entirely free to ratify or reject. (See 7 U.S.C. § 608c(8)). Producers retain the right at all times to terminate their order. (See 7 U.S.C. § 608c(16)). Thus, if producers believe that the minimum prices established under their orders do not reflect supply and demand conditions, including the cost and availability of feed, they are entirely free to seek amendment or termination of their orders or to refuse to ratify an amended order.

As the Secretary explained in the first Amplified Decision, dairy producers, over time, elected to use the Minnesota-Wisconsin (M-W) price as the Class III price and to establish Class I prices under their orders. The M-W was first incorporated into the Chicago Regional order in 1961 and was adopted in all orders by 1975. In each and every instance in which the industry requested that an order be amended to adopt the M-W, the Secretary reviewed supply and demand conditions in the order, including the price and availability of feed. After this review and consistent with § 608c(18), the Secretary found that the M-W price was a superior and appropriate measure of all of the factors required by § 608c(18) than previous pricing formulae. In each case, producers ratified the amended orders incorporating the M-W price for milk used in Class III uses. Thus, for every order in the Federal order system, the Secretary has found, based on the § 608c(18) factors, that use of the M-W price is consistent with the AMAA. If it would be instructive, the Secretary will

supply the Court with decisions from the proceedings leading to the adoption of the M-W in each milk marketing order.

The Secretary also has established Class I differentials in all orders. These differentials, too, have been ratified by each order's producers. In setting these differentials, the Secretary (and the industry generally) has been aware for decades, the Upper Midwest region of the U.S. has produced much more milk than the region required to satisfy its demand for fluid milk. No other region of the country has ever generated such vast amounts of surplus milk nor does any other region do so today. Not surprisingly then, when other regions' supplies are insufficient to satisfy demand, the Upper Midwest tends to serve as the ultimate source of additional milk supplies. Thus, areas needing milk tend to receive it either through direct shipments from the Upper Midwest or from alternative supply areas that similarly can and do rely on the Upper Midwest's reserve supplies. The farther milk must move, the higher the cost of transportation and the resulting value of milk at the destination location. Therefore, Class I differentials are set at reasonable levels and provide the economic incentive to draw milk from surplus to deficit markets. They are largely reflective of the distance of the deficit market from the alternative supply areas, including the distance from the Upper Midwest. This system, based on the M-W price and aligned pricing, has applied for decades, was largely retained in the 1985 Food Security Act (FSA), and is reflected in the Class I differentials in place today. As the Secretary found in the Final Decision, this system did not require alteration because, among other articulated reasons, "the industry for years has strongly supported a coordinated set of differentials based on fairly constant rates of change from market to market." (58 FR 12646).

It is important to note that, like the order-by-order adoption of the M-W as the Class III price, Class I differentials were not simply developed by imposing gradually increasing differentials based on distance from the Upper Midwest. Rather, in the context of adopting each order, the Secretary examined the prevailing prices which handlers were paying to attract supplies of fluid milk from nearest areas of available supply to their location. Class I prices therefore reflect the price necessary to attract milk to a particular location from the nearest sources of supply. Thus, for example, to the extent that Florida's local milk supplies are not sufficient to meet demand, it must look northward for

such additional supplies. Because the ultimate source of supply for most of the nation tends to be the Upper Midwest, handlers in turn seek supplies in a south to north general pattern. For this reason, but not due to any predetermined single basing point approach, the Class I differentials are reflective of the realities of such a south-north continuum.

Three previous rulemaking decisions provide explicit examples in establishing or changing Class I differentials. Prevailing supply and demand conditions and alternative sources of supply, not distance from Eau Claire, determined the establishment of, or modification to, a market's Class I differential. In the Upper Florida promulgation decision, the nearest alternative source of supply was identified to be Nashville, Tennessee. (See 31 FR 13272). In two other decisions, Class I differentials were established based on prevailing supply and demand conditions and in light of the development of new alternative sources of supply. In the final decision merging three southwest orders into the New Mexico-West Texas marketing area (see 56 FR 42240), Class I differentials were established for the merged order in light of prevailing marketing conditions, the establishment of new alternative milk supplies, and the relationship between the new order and the adjoining Southwest Plains and Texas marketing areas. As a result, the Class I differential in the Texas marketing area was lowered to recognize the alternative milk supply available in New Mexico. Additionally, in the final decision concerning the New England marketing area (see 43 FR 45520), Class I differentials were adjusted in light of changed alternative sources of milk supply. In all three of these decisions, the distance from Eau Claire was not even mentioned or considered. If it would be instructive, the Secretary will supply the Court with decisions from other proceedings leading to the adoption of Class I differentials in each order which similarly set Class I differentials without Eau Claire being mentioned or considered.

#### The 1990 Rulemaking

Turning to the rulemaking hearings conducted in 1990 which are the subject of the Court's second opinion, it is important to stress that this rulemaking did not address in any way the continued viability of the M-W as the automatic reflector of those supply and demand factors required by § 608c(18). The 1990 rulemaking addressed, among other things, the concerns of certain sectors of the dairy industry that the

Class I differentials established by the FSA should be overhauled. In response to those complaints, the Secretary invited the public to propose alternatives to the Class I pricing system which would provide a superior system for attaining the goals of the AMAA.

The numerous proposals submitted and supporting testimony "portray[ed] a wide range of views regarding how Federal orders should be changed or not changed." (58 FR 12645). The organization representing the interests of the Minnesota Milk Producers Association (MMPA) (as well as other Upper Midwest dairy concerns) argued in the course of the hearing that a new approach to establishing Class I milk prices should be adopted. (*Id.* at 12646). MMPA's witness, however, like all other witnesses, did not provide any specific data on the price or availability of feed in any order market and nowhere suggested that the Secretary should tie classified prices to the price or availability of feed in any one or all Federal orders. (*See generally id.*). In fact, the witness for Upper Midwest interests (including MMPA) urged the Secretary to find that the cost of producing milk (presumably including the cost and availability of feed) did not vary across the order system. (*See id.* at 12646 (witness for Upper Midwest Federal Order Coalition (UMFOC) contended that "costs of production are about the same across the country")). (*See also Trans.*, Sept. 12, 1990, pg. 162 (there is "equal cost of production across various regions.")) Although not an issue in the rulemaking, the Secretary notes that this testimony supports the view that the M-W reflects market conditions in all orders and is properly included in the orders. After reviewing the various proposals for revamping the Class I pricing system, including the UMFOC's suggested flat Class I differential across the entire order system, (*see* 58 FR 12642) the Secretary determined to retain the extant Class I system because, based on his review of supply and demand conditions in all orders, the system furthered the goals and purposes of the AMAA.

#### The Secretary's Current Undertakings

The Class I pricing system, indeed many aspects of the current order system itself, are now under renewed examination by the Secretary. Specifically, in the 1996 Farm Bill (formally known as the Federal Agriculture Improvement and Reform Act of 1996), Congress mandated that the Secretary consolidate the current number of milk marketing orders from 33 to not fewer than 10, and not more

than 14 milk marketing orders, and examine the Class I differentials for each of those new orders. In this legislation, Congress also authorized the Secretary to consider the Class I pricing system for fluid milk without reference to the existing system of Class I differentials. (See §§ 143(a) (3) and (4)). Consistent with its longstanding approach, however, Congress did not question the use of the M-W as the price "mover" of other class prices, or the classified pricing system itself, in the 1996 Farm Bill.

In light of the directives of the 1996 Farm Bill, the Secretary has undertaken proceedings to consider whether to fundamentally reshape milk pricing methods and standards. The Secretary has indicated that all options will be explored. The Secretary intends to define a preliminary order structure later this year and may, during the ensuing 18 months, revise this structure based, among other sources, on industry comments and submissions. Furthermore, the Secretary at this time anticipates issuance of a final decision on these questions in approximately two years. It is certainly possible that the issues raised in this litigation will be rendered moot once the order program is reformed.

#### The Court's Second Opinion and Remand

*Opinion Background* In its opinion, the Court correctly observes that the Upper Midwest is a chronic over-producer of milk for fluid uses and that certain regions of the country are, at times, unable to produce adequate supplies of milk to satisfy this demand. The Court then concludes, erroneously, that the Secretary established an elaborate system of price controls (*i.e.*, Class I differentials) based directly on distance from the Upper Midwest to distant markets.

As noted above, Federal milk marketing orders are not an elaborate system established to address the Upper Midwest's chronic oversupply situation. As the Secretary explained in his first Amplified Decision, the orders must be viewed in the context of the marketing conditions which led to their gradual adoption. The AMAA, insofar as it related to milk, embodies Congress's recognition that dairy farmers lacked adequate bargaining power in the market to ensure a fair price for their milk. The inherent characteristics of milk itself contribute, in large part, to this market inequity. For example, milk is highly perishable, cannot be stored for long periods of time and is bulky and expensive to transport.

Furthermore, while demand for milk is relatively stable when measured season-to-season, demand varies on a daily basis. Therefore, to ensure that adequate supplies of fluid milk are available to supply the unpredictable and changing daily demand for milk, the industry must continually produce more milk than necessary.

Milk not demanded for fluid uses, the so-called "reserve," is manufactured into dairy products such as butter, nonfat dry milk and cheese. Unlike fluid milk, manufactured dairy products can be stored and shipped economically and therefore compete in broader, indeed national, markets. Since, based on improved transportation and other factors, the market for manufactured dairy products has for decades been national in scope, these products compete on an equal footing regardless of where they are produced.

Manufactured products do, however, return a lower price to dairy farmers than milk used for fluid purposes. Before passage of the AMAA, dairy producers sometimes made uneconomic price concessions to maximize the use of their milk for fluid purposes. Thus, prior to the involvement of the Federal government, dairy farmers attempted to bargain with milk handlers for a flat price for all milk, regardless of use. But the pressures caused by the oversupplies of milk described above led to the breakdown of the flat pricing plans. Handlers would refuse to take excess milk from farmers at a flat price because it had a lower value when it was made into manufactured products. Handlers would respond by offering fluid milk to their customers at lower prices than their competitors. This in turn led to a lowering of the flat price paid to dairy farmers. In this regard, such pricing practices by handlers were viewed as "predatory," placing the entire burden of destructive price competition solely on the backs of dairy farmers.

Groups of dairy farmers, represented by their cooperatives, attempted to address such pricing practices by developing a "classified price system" whereby milk was pooled and priced according to use, much like it is done today under the AMAA. Classified pricing had come into effect in a number of large markets in the country by about 1920. However, cooperative classified pricing plans were only partially successful because their success was dependent on participation by all groups in a market and because there remained certain advantages to staying out of these voluntary pricing arrangements. The economic depression of the 1930s accentuated the problems

with voluntary classified pricing and pooling arrangements.

The AMAA, enacted in 1937, provided, insofar as it relates to milk, the framework for long-term price and market stability. Of great importance in understanding the purpose and operation of classified pricing, Congress adopted a supply-demand pricing standard to replace parity pricing. The supply-demand pricing approach is not, as the Court's second opinion suggests, a system of price controls. Rather, under this system, the minimum prices for milk established in orders respond to changing supply and demand conditions in the marketplace. Marketing orders, in this context, only establish the terms of trade between dairy farmers and handlers under a Government-supervised marketing plan. They assure, from a producer point-of-view, that a minimum uniform price (also known as the blend price) is returned to dairy farmers and, from a handler point-of-view, equity in the cost of obtaining a supply of milk. Such a plan tends to promote orderly marketing and efficient disposal of surplus milk not demanded by the fluid market, and mitigates the need by handlers to engage in predatory pricing practices.

Milk marketing orders have evolved since 1937 in response to ever-changing market conditions. As noted above, dairy farmers, including those in the Upper Midwest, concluded that orders ensured far more orderly marketing of their highly perishable product. Since most orders have remained in place, it is clear that dairy farmers are largely satisfied with the system—which has operated in approximately the same way for nearly 30 years—as they have rarely exercised their right under the AMAA to seek termination of their order. Congress, too, has not sought to reorder the essential nature of the system, including the universal adoption of the M-W price.

The foregoing provides a more complete description of the historical development of milk marketing orders and the purposes of classified pricing. In sum, it is not correct to characterize the order system, as the second Court opinion does, as the Government's response to overproduction in the Upper Midwest and periodic deficit conditions in other areas.

The Court's second opinion also states that milk prices are not determined solely by market forces, and that the Federal government has assured dairy farmers a minimum price for their milk for decades. For purposes of this discussion, the Secretary assumes that the Court has not confused the existence of the Dairy Price Support Program,

established under the Agricultural Adjustment Act of 1949 (AAA), which is applicable to all dairy farmers, whether or not associated with a Federal marketing order, with the market-determined prices enforced by milk marketing orders for farmers associated with each particular order. The AAA, through the Dairy Price Support Program, establishes a price floor that is designed to prevent further price reductions that might otherwise be warranted by supply and demand conditions.

#### *Class I Differentials and Pricing*

The Court states in its second opinion that Class I differentials are determined by the distance of a marketing area from Eau Claire, Wisconsin, and this alleged formula is "the essence of controversy between the parties." (Opinion pg. 5). The Court further notes that this alleged formula constitutes a "single basing-point pricing system." (Opinion pg. 5). The Court continues "It is simply untrue to suggest, as the Secretary does, that it is irrelevant from which geographic point prices are determined. Different basing points (presumably reflecting different assumptions regarding market specific conditions) will necessarily yield different Class I differentials." (Opinion pg. 6.)

Class I differentials were not established based on a market's distance from Eau Claire. Class I differentials were established by observations of market specific supply and demand conditions in each marketing area. The price needed to attract milk to a consumption center is constrained by the cost of obtaining and transporting milk from an alternative supply area which results in the need to establish a differential level specific to each market in achieving this end. For example, the Secretary could choose any location (or locations) and align prices to other orders based on relative fluid demand. The resulting system would be the same as the current system; prices will increase to reflect the cost of attracting milk to the deficit areas, and those prices will similarly decrease, in a stair step continuum, as the ultimate source of alternative milk supply—the Upper Midwest—is approached.

That there is a high degree of correlation between distance from the Upper Midwest region and other marketing areas is interesting but is not, in and of itself, the basis for the Secretary's establishment of such differentials. As noted above, when setting Class I differentials, the Secretary did not simply gauge the distance of the market center of an order from Eau Claire and then add a

differential representing transportation costs. To the contrary, in the promulgation of distinct and separate orders, the Secretary conducted intensive investigations of supply and demand conditions in each market. Germane to the investigations were the prevailing prices which handlers actually paid to attract a supply of milk and what supply sources the market actually tapped to get extra supplies. Only then was a Class I differential established for the market. Over time, as changing market conditions warranted, marketing orders were consolidated, covering increasingly larger geographical areas. As this occurred, there was heightened recognition of the need to coordinate class prices and to align Class I prices between orders. Thus, the mere fact that real-world market forces necessarily yielded, over time, an aligned Class I pricing system that correlates to geography simply does not mean that the enormous reserve quantities of milk in the Upper Midwest relative to other marketing areas (east of the Rocky Mountains) constitute a "single basing point." The high degree of correlation between distance from the Upper Midwest, and another area's supply-demand relationship is reflective of this reality. It justifies the current Class I differentials, not the other way around.

Of note, in the 1990 rulemaking, the Secretary solicited proposals which would, in order to be adopted, necessarily demonstrate that these assumptions were incorrect. As the Secretary found, industry participants proposed either no change, minor change, and in some instances, radical change, to the Class I pricing system. None demonstrated that the current Class I prices were not functioning, as a matter of demonstrable supply and demand patterns, sufficiently to attain the goals of the AMAA.

#### *Class I Differentials and Class I Pricing and § 608c(18) Findings*

As the Secretary explained at length, the M-W price which forms the basis for all classified pricing, automatically incorporates the price and availability of feed as well as numerous other factors. In this regard, in the underlying proceeding MMPA argued that the Secretary should find that the cost of production is uniform throughout the order system. To the extent that MMPA is correct, then, the M-W price must already reflect the cost of producing milk, including feed. Thus, under MMPA's view, by incorporating the M-W into all three classified prices the Secretary presumably has satisfied § 608c(18).

The validity of the M-W as an automatic reflector of the § 608c(18) pricing factors has become a central issue in this proceeding even though it was specifically excluded from consideration at the 1990 rulemaking. (See 55 FR 29034). The M-W price was discussed in the First Amplified Decision, but only because the Court's first opinion seemed to confuse the role of the M-W with whether or not there was a standard for determining how much reserve milk should be, or needs to be, associated with each marketing order. Nevertheless, the Secretary also explained how the M-W reflects the § 608c(18) pricing criteria factors and acts as the "mover" for all classified prices.

The Court expresses dissatisfaction with the M-W because, in its view, the M-W does not directly reflect supply and demand conditions, including the price and availability of feed, in each marketing order. The Secretary notes, however, that the M-W has been a component of every marketing order for well over 20 years in some orders and over 30 years in many others. Additionally, Congress has never suggested that the Secretary's reliance on this measure was not wholly consistent with the AMAA. Furthermore, far from maintaining that Class III prices must be order-specific, the MMPA, like every other witness at a recent national hearing concerning the M-W, argued that a uniform Class III price be used in all Federal orders. (See 60 FR 7276 (MMPA proposed that the Federal milk support price established under the AAA of 1949 be the Class III price)). Thus, Congress, the Secretary and the dairy industry all understand that a uniform Class III price can and should be used in all orders as the "mover" of Class I and Class II prices under the AMAA.

As the Court recognizes, the AMAA requires that the Secretary consider the various factors affecting supply and demand in setting minimum prices. The statute also prescribes that milk marketing orders ensure an adequate, but not excessive, supply of pure and wholesome milk and otherwise be in the public interest. Using the M-W price accomplishes precisely these goals by incorporating the fluctuations in supply and demand, as reflected by free market transactions, into classified pricing. Class I pricing therefore responds to, rather than dictates, supply and demand. The cost and availability of feed, by contrast, represent only two aspects of the supply side of the equation. Moreover, as supply factors, feed costs and availability similarly change and which the statute

specifically requires to be considered. It would not be appropriate for the Secretary to set prices which responded to constantly fluctuating conditions on one sole (and narrow) measurement when there are a host of other considerations affecting the supply of milk that themselves constantly change. Thus, to set milk prices based on these significant but limited factors rather than on the M-W, which automatically incorporates these aspects of supply, would tend to have the effect of ignoring all of the factors of supply and demand required for compliance with § 608c(18).

Of particular note, the Secretary conducted a subsequent national hearing to address the M-W price in 1992. The Secretary's call for proposals for the hearing (57 FR 26790) explicitly indicated that any proposals that would change the M-W method would have to be justified under the supply and demand pricing standards specified in § 608c(18). Since that hearing, the Secretary has determined that a modified M-W price, adjusted by a product price formula, and now referred to as the Basic Formula Price (BFP), best satisfies the statutory pricing criteria of the AMAA. Accordingly, the Secretary amended all Federal milk orders and producers everywhere affirmed the amended orders. The BFP essentially retains the features of the old M-W. It is a market-determined price, free of government regulation that represents the basic value for milk and used to adjust Class I and Class II prices. It is the basis for establishing the pricing terms-of-trade between dairy farmers and handlers because it continually responds to changing supply and demand factors as prescribed by § 608c(18). The use of a product price formula is a minor refinement that updates a previous month's price to better reflect current marketing conditions. In the final decision for improving the M-W, (60 FR 7290) the Secretary found that the economic rationale stated when the M-W was first adopted remains sound today as it was when it was adopted order-by-order from 1961 until universally adopted in 1975.

#### Class I Differentials and Class I Prices

As noted above, the M-W price is the key component in the Class I price, representing the many supply and demand factors referenced in § 608c(18). The M-W price does not, however, reflect one factor uniquely relevant to Class I fluid milk pricing: the cost of transporting milk from alternative supply sources. When the Class I differential, which largely reflects transportation costs, is added to the M-

W price, the minimum Class I price in each market is set. As marketing orders were consolidated, covering ever increasingly larger geographical areas, there was an increasing need to align Class I prices among the orders. Inter-market alignment of Class I prices is necessary so that the minimum prices do not exceed the cost of obtaining milk from alternative sources of supply. Such pricing constraints address § 608c(5)(A) which requires, among other things, uniform prices to handlers.

The Class I differential serves as that economic incentive to move milk from supply to areas where it is demanded. In reality, some milk is produced just about everywhere. Therefore, the mix of milk produced near where it will be consumed, along with milk needed from more distant locations needs to be only high enough to bring forth that additional supply that will satisfy consumer demands.

It is important to reiterate that dairy farmers are not paid the Class I price for their milk. Class I prices are minimum prices paid by handlers who use milk for fluid purposes. Their alignment both within an order and between orders is critical so that all handlers compete on an equal footing for attracting milk to their location. Dairy farmers, by contrast, receive a blend price for their milk regardless of how it is used. The blend price is neither intended to be aligned by the Secretary, nor is it intended to correlate to geography. The blend price that producers receive represents the sum total of local supply and demand conditions for milk in each marketing order area. Blend price changes (and differences in blend prices among orders) provide the economic signal for producers to make production decisions and for making marketing adjustments.

#### General Findings

The findings and determinations set forth herein have been issued in response to an opinion and order of the United States District Court, District of Minnesota, Fourth Division, issued on May 16, 1996. The findings and determinations supplement those that were previously set forth in the Final Decision issued on February 5, 1993, and published in the Federal Register on March 5, 1993, and in an Amplified Decision issued on August 10, 1994, and published in the Federal Register on August 17, 1994, with respect to the New England and other Marketing Area orders. No additional regulatory changes are necessary as a result of this second Amplified Decision.

List of Subjects in 7 CFR Parts 1001, 1002, 1004, 1005, 1006, 1007, 1011, 1012, 1013, 1030, 1032, 1033, 1036, 1040, 1044, 1046, 1049, 1050, 1064, 1065, 1068, 1075, 1076, 1079, 1106, 1124, 1126, 1131, 1134, 1135, 1137, 1138, 1139

Milk marketing orders.

Dated: September 10, 1996.

Michael V. Dunn,

*Assistant Secretary, Marketing and Regulatory Programs.*

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## DEPARTMENT OF JUSTICE

### Drug Enforcement Administration

#### 21 CFR Part 1301

RIN 1117-AA40, DEA Number 142N

#### Guidelines for Providing Controlled Substances to Ocean Vessels

**AGENCY:** Drug Enforcement Administration (DEA), Justice.

**ACTION:** Advance Notice of Proposed Rulemaking.

**SUMMARY:** DEA is considering whether to propose amending the regulations regarding the supply of controlled substances to ocean vessels to provide a means of supply more consistent with current industry practices for other materials. The decision on whether to propose amendments and the extent of any such amendments will be based on the information and comments submitted in response to this advance notice of proposed rulemaking and DEA's experience with the existing procedures and practices for supplying controlled substances to vessels.

**DATES:** Information and comments should be submitted on or before November 18, 1996.

**ADDRESSES:** Comments should be submitted in duplicate to the Deputy Assistant Administrator, Office of Diversion Control, Drug Enforcement Administration, Washington, D.C. 20537, Attn: Federal Register Representative/CCR.

**FOR FURTHER INFORMATION CONTACT:** G. Thomas Gitchel, Chief, Liaison and Policy Section, Office of Diversion Control, Drug Enforcement Administration, Washington, D.C. 20537, Telephone (202) 307-7297.

**SUPPLEMENTARY INFORMATION:** Title 21, Code of Federal Regulations (CFR), Section 1301.28 provides a mechanism for the transfer of controlled substances to ocean vessels for use in emergency