CONGRESSIONAL BUDGET OFFICE
COST ESTIMATE

July 13, 1999

H.R. 1402

A bill to require the Secretary of Agriculture to implement the Class I milk price structure known as Option 1-A as part of the implementation of the final rule to consolidate federal milk marketing orders

As ordered reported by the House Committee on Agriculture on June 30, 1999

SUMMARY

H.R. 1402 would require the Secretary of Agriculture to modify final rulemaking procedures to change the method by which minimum prices are established for fluid milk in different regions of the country. The bill would require formal rulemaking procedures to develop pricing methods—known as marketing orders—for milk used in manufactured dairy products (cheese, butter, and nonfat dry milk) and would, pending a final rule, modify the formula for minimum cheese prices. H.R. 1402 also would extend for one year the current milk price support program (scheduled to expire December 31, 1999), delay starting the recourse loan program for commercial processors of dairy products, and require the Secretary to establish a new dairy program that would allow milk producers and cooperatives to enter into forward price contracts with milk handlers.

CBO estimates that implementing the provisions related to federal marketing orders for milk prices would not require any additional discretionary outlays over the 2000-2004 period. Enacting the bill would affect direct spending—primarily as a result of the extending current price-support programs for one year. Thus, pay-as-you-go procedures would apply. CBO estimates that enacting H.R. 1402 would reduce direct spending by $102 million in 2000 but would result in a net increase in direct spending of $149 million over the 2000-2004 period.

H.R. 1402 contains no intergovernmental mandates as defined in the Unfunded Mandates Reform Act (UMRA) and would impose no costs on state, local, or tribal governments. The bill would impose a private-sector mandate, as defined by UMRA, by requiring handlers of milk regulated by federal milk marketing orders to pay a higher price for milk than they would otherwise be required to pay. The estimated cost to the private sector of the mandate contained in this bill would exceed the threshold for private-sector mandates ($100 million in 1996, adjusted annually for inflation) established in UMRA.

ESTIMATED COST TO THE FEDERAL GOVERNMENT

The estimated budgetary impact of H.R. 1402 is shown in the following table. The costs of this legislation fall primarily within budget function 350 (agriculture).

	By Fiscal Year, in Millions of Dollars				
	2000	2001	2002	2003	2004
CHANGES IN DIRECT SPENDING					
Estimated Budget Authority	-102	241	-4	7	7
Estimated Outlays	-102	241	-4	7	7

BASIS OF ESTIMATE

For the purpose of this estimate, CBO assumes that H.R. 1402 will be enacted before October 1, 1999. The bill would require the Secretary of Agriculture to choose an alternative marketing order by that date.

One-Year Extension of Current Milk Price Support Program

H.R. 1402 would extend the milk price support program for one year and delay implementing a loan program for commercial processors of dairy products. CBO estimates that these two provisions would reduce federal outlays by $102 million in 2000 and increase federal outlays by $149 million over the 2000-2004 period.

The Federal Agriculture Improvement and Reform Act of 1996 (Public Law 104-127) terminates the milk price support program on December 31, 1999, replacing it with recourse loans available to commercial processors beginning January 1, 2000. These recourse loans would help dairy processors manage inventories of dairy products and assure a greater degree of price stability for the dairy industry during the year. The loan period extends through the end of the fiscal year in which they are made, but the Secretary of Agriculture may extend these loans for up to one additional year. (CBO assumes that the Secretary will extend recourse loans.) The Credit Reform Act of 1990 exempted all credit programs of the Commodity Credit Corporation from its provisions, and the budget therefore would record these loans on a cash basis.

Under current law, CBO estimates that the net outlays for recourse loans (loans made minus loans repaid during the same fiscal year) would be $280 million in 2000 (the first year of the program) and would be in the range of -$12 million to $7 million in subsequent years as outlays for new loans would be offset by repayments of previous loans. By delaying implementation of the recourse loan program one year (until January 1, 2001), the relatively large start-up cost for the program would be shifted from 2000 to 2001.

CBO estimates that continuing the milk price support program for one year would increase federal outlays (by increasing net purchases of dairy products and related expenses) by $178 million in 2000. Hence, the net effect of extending milk price supports and delaying recourse loans would be to reduce outlays $102 million in 2000 ($178 million in net price support cost minus $280 million in forgone recourse loan start-up costs). Outlays would increase by $241 million in 2001, as $251 million in net recourse loans would be partially offset by a reduction of $9 million in net purchases. Relatively small changes occur in subsequent fiscal years. The difference between net recourse loans forgone in 2000 ($280 million) and made in 2001 ($251 million) arises because loan activity depends on commercial stocks, for which CBO estimates different levels in 2000 and 2001.

Consolidated Federal Milk Marketing Order Provisions

As required by Public Law 104-127, the Secretary of Agriculture announced on March 31, 1999, a final decision to overhaul the federal milk marketing order program. Milk marketing orders classify milk by use, set minimum prices that handlers must pay for each class of milk, and provide for paying average prices to all dairy farmers who supply a particular region. The decision to adopt a new marketing order must be approved by producer referendums, which USDA will conduct later this year. If approved by referendum, the changes will take effect on October 1, 1999.

The most controversial aspect of milk marketing reform is the method of setting minimum prices for fluid milk. The Secretary's decision—known as Option 1-B—would probably increase fluid milk prices in the Upper Midwest and Florida and reduce prices elsewhere. Despite these regional differences, the national average price of milk is not expected to change significantly.

If enacted, H.R. 1402 would require the Secretary of Agriculture to implement an alternative method of calculating minimum fluid milk prices known as Option 1-A. This alternative method would more closely reflect the current regional distribution of fluid milk prices. The bill would not alter the requirement of Public Law 104-127 that reform of milk marketing orders be implemented by October 1, 1999.

The bill would require the Secretary to use rulemaking to develop pricing methods for milk used for cheese, butter, and nonfat dry milk and would modify the formula for setting minimum cheese prices until a final decision was approved by rulemaking (required to be completed within 10 months of enactment).

H.R. 1402 also would require the Secretary to establish a program under which milk producers and cooperatives would be authorized to enter into forward price contracts with milk handlers of federally regulated milk. CBO estimates that implementing this program would not have any significant impact on administrative costs of the Department of Agriculture.

By affecting the price of milk, changes in milk marketing orders could affect federal nutrition programs, particularly the Special Milk Program. However, CBO expects that H.R. 1402 would have a negligible impact on the Special Milk Program because the impact on retail milk prices is likely to be small.

PAY-AS-YOU-GO CONSIDERATIONS

The Balanced Budget and Emergency Deficit Control Act sets up pay-as-you-go procedures for legislation affecting direct spending or receipts. The net changes in outlays that are subject to pay-as-you-go procedures are shown in the following table. For the purposes of enforcing pay-as-you-go procedures, only the effects in the current year, the budget year, and the succeeding four years are counted.

	By Fiscal Year, in Millions of Dollars										
	1999	2000	2001	2002	2003	2004	2005	2006	2007	2008	2009
Changes in outlays	0	-102	241	-4	7	7	4	3	-1	1	1
Changes in receipts	Not applicable										

ESTIMATED IMPACT ON STATE, LOCAL, AND TRIBAL GOVERNMENTS

H.R. 1402 contains no intergovernmental mandates as defined in UMRA and would impose no costs on state, local, or tribal governments.

ESTIMATED IMPACT ON THE PRIVATE SECTOR

H.R. 1402 would impose a private-sector mandate, as defined by UMRA, by requiring handlers of milk regulated by federal milk marketing orders to pay a higher price for milk than they would otherwise be required to pay. The Secretary of Agriculture issued on March 31, 1999, final rules for the consolidation and reform of federal milk marketing orders. Such consolidation and reform was required by the Federal Agricultural Improvement and Reform Act of 1996 and will take effect October 1, 1999, if approved by producer referendum. Such approval is expected. As a part of those final rules, the Secretary established new Class I price differentials that set premiums that handlers in the various federal orders must pay for milk used for fluid purposes, such as bottled milk. H.R.1402 would require the Secretary to use a different set of Class I differentials than announced as part of the final rule. In nine of the eleven new federal order areas, the differential required by H.R. 1402 would be higher than that announced by the Secretary. Milk handlers in those areas would be required to pay producers more for milk used for fluid purposes. Based on projections of milk marketings and use, CBO estimates that handlers would be required to pay milk producers annually about $140 million more than they would without this change in the law.

Section 2 of H.R. 1402 would require the Secretary of Agriculture to use a formal rulemaking process to reconsider the Class III and Class IV minimum pricing formulas announced in the final rules issued March 31, 1999. Class III milk is that used to produce cheese; Class IV milk is that used to produce butter and milk powder. The bill would require that a new decision on those formulas be implemented within 10 months after enactment. In the interim, H.R.1402 would require the Secretary to replace the manufacturing allowance for cheese that was announced in the March 31, 1999, rules with a lower value. Substituting the lower value in the formula has the effect of raising the price that milk handlers must pay producers for fluid milk and raising the minimum price that must be paid for milk used to produce cheese, in both cases by nearly $0.24 per hundredweight. On an annualized basis the cost to milk handlers of this provision would exceed $100 million. CBO can not provide a more precise estimate because of the uncertainty of how long this provision would be in effect and how the increase in the minimum Class III price would affect prices paid to producers.

Milk producers' gross receipts would be higher by an amount corresponding to the higher costs to milk handlers that would result from enactment of H.R. 1402. The higher costs faced by handlers would be mostly passed on to consumers as higher prices for milk and milk products.

All the changes cited above are estimated relative to what is expected to happen without enactment of H.R. 1402. The final rules issued in March 1999, which are expected to become effective in October 1999, would probably reduce farm and consumer-level milk prices. The new rules, as amended by the provisions of H.R. 1402, would cause such decreases in milk prices to be smaller.

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