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Joyce Dawson, Hearing Clerk
STOP 9200-Room 1083
United States Department of Agriculture
1400 Independence Avenue SW
Washington, DC 20250-9200

**Re: Milk in the Pacific Northwest and Arizona-Las Vegas Marketing Areas;
Docket No. AO-368-A32; AO-271-A37; DA-03-04B**

Dear Hearing Clerk:

I am the general legal counsel for Mallorie's Dairy, Inc. Mallorie's is one of the three dairies in the Pacific Northwest Marketing Area affected by the proposed rule changing the milk marketing order to limit producer-handler status to those entities with route disposition of fluid milk products of less than three million pounds per month. This comment is in opposition to the proposed rule.

The Agricultural Marketing Service did not properly consider the economic impact of this action on small entities and improperly certified that the proposed rule would not have a significant economic impact on a substantial number of small entities. Producer handlers in the Pacific Northwest Marketing Areas have always been considered "small businesses" for purposes of the Regulatory Flexibility Act. The USDA's treatment of the producer-handlers as small businesses is contained in the 1999 Federal Order Reform Department of Agricultural Marketing Service 7 CFR Part 1124 under the section referring to The Regulatory Flexibility Act on Page 24, paragraph 3. Attached are the relevant provisions of the rule for your convenience.

The proposed rule reflects that the Agricultural Marketing Service's use of the \$750,000 gross revenue standard to determine whether a producer handler is a small business. This is an arbitrary action. It directly contradicts prior rules and the service's prior record of using a different standard to determine whether a producer-handler qualified as a small business. The certification for the Regulatory Flexibility Act issued by the Agricultural Marketing Service is invalid because there is a devastating economic impact on a substantial number of small entities when the definition of "small entities" is applied appropriately and in accord with the service's prior practices.

If the proposed rule is adopted, the cost of compliance and other expenses imposed by the government will likely force the Mallorie family to close the dairy. The economic impact must be

reconsidered and the factors below should be included in that consideration.

I represent the dairy corporation and members of the Mallorie family in personal and business matters. The dairy has employed other attorneys to assist them with the legal work regarding the question of the validity of the proposed rule. My role is to address the practical impact of the proposed rule on this family's farm. The big picture of the impact of this proposed rule and other federal legislation and regulations is missing. It should have been addressed as required by Regulatory Flexibility Act. 5 U.S.C. 601 *et seq.* The purpose of my letter is to address the big picture for the Mallorie's family farm.

1. The Direct Impact of the Costs of the Proposed Rule on Mallorie's Dairy.

Mallorie's Dairy estimates that if the dairy continues to operate at the current level, the cost of the proposed rule will be approximately \$83,000 per month. Mallorie's Dairy does not generate a profit of \$83,000 per month. Any money generated by the corporation in excess of its ordinary operating costs has been reinvested in the corporation. Reinvestment in the corporation for this family farm means paying for deferred maintenance like replacing the roof on the cow barn. The corporation has never paid any dividends in its 51-year history. The salaries of the highest paid family members working on the dairy are \$60,000 a year and \$32,000 per year. Mallorie's does not have enough money to meet the needs of the dairy and pay the costs imposed by the proposed rule.

Mallorie's Dairy's taxable income is only \$393,574 a year. The proposed rule would consume any taxable income. Six months of milk pool payments will cause them to lose more than their income. This impact cannot be ignored when the proper analysis of the impact of this rule required by the Regulatory Flexibility Act is conducted on the small entities like Mallorie's.

2. The Impact of Death Taxes on Mallorie's Dairy.

The largest shareholder in Mallorie's Dairy, Inc., is Juanita Mallorie. Juanita is aging. Her health is poor. Upon Juanita's death, more than 30% of the corporation's stock, a majority of land used by the dairy, a note owed by the dairy to Juanita, and cows owned by Juanita will be subjected to federal estate tax and Oregon Inheritance tax. Juanita's estate will pay between \$1,000,000 and \$1,500,000 in federal and state inheritance taxes.

Death taxes are based on the fair market value of assets owned by a decedent. The assets creating the death tax in Juanita Mallorie's estate are dairy assets. Juanita Mallorie has very limited liquid assets. She owns farm land, cows, dairy corporation stock and a promissory note from the dairy. The money to pay the death taxes will have to come from the sale of Juanita's land to the dairy on an installment basis, or from the cash sale of Juanita's assets to others. If the proposed rule is adopted, there will not be enough money to buy the land to pay the taxes and to pay the milk pool \$83,000 per month.

Other family farms struggle with the same inheritance tax issues. Congress passed IRC 2032A to attempt to address the problem and save family farms. IRC 2032A allows Juanita's estate to elect to reduce the taxes attributable to the value of her farmland, but the reduction is very limited and it can only be used if the children guarantee that the farm will operate for 10 years after her death. Other than the small reduction for family farmland under IRC 2032A, the taxes are due and payable within nine months of Juanita's death. The estate may qualify to pay some of the taxes on an installment basis over a five or ten-year period. If the estate qualifies for the installment option, there still will not be enough money to pay the \$83,000 monthly payments to the milk pool under the proposed rule and the annual installment payments for the death taxes.

If some of the land is sold to a third party to pay the death taxes, the 2032A reduction will not apply to the sold land and more land will need to be sold to pay the additional taxes due to the lost 2032A reduction. If a portion of the land is sold to third parties, there will be insufficient land to operate the dairy and the dairy will have no place to go. The family will be forced to close the dairy, sell the remaining land, and a housing subdivision will sit where we used to have a farm that employed more than 80 people.

The likelihood of the closure of Mallorie's Dairy, which is and always has been treated as a small entity, will be directly caused by the adoption of the proposed rule. This cannot be ignored when a proper analysis of the impact of the proposed rule on small entities is conducted.

3. Increased Cost of Land.

Mallorie's Dairy sits in the Hazel Green area of the Willamette Valley. In the past 15 years, the price of land in this area has more than tripled from \$2,000 - \$3,000 an acre in 1991 to \$14,000 an acre currently. This has created a great deal of financial pressure for all farms in the area. The increasing land prices are due to expanding suburbs. In the past, the cost of farm land in Oregon has not rapidly increased because of strong zoning laws preventing farm land from being used for any other purpose. In November of 2004, Oregon voters amended the Oregon constitution to change the impact of zoning laws. Now, land that was previously zoned exclusive farm use can be used for other purposes unless the state pays the land owner the difference between the value at farm use and the value for other uses such as residential development. Once the court cases that have been filed resolve some of the ambiguities of the law known as Measure 37, the price of farm land is expected to sky rocket.

The sky rocketing price of land will increase the real property taxes paid by the dairy, increase the pressures related to surrounding properties being converted to non-farm use, and increase the death taxes arising from the value of the property in Juanita Mallorie's estate.

4. Financial Pressure.

It is difficult to run any small business. The family members who run this dairy farm carry

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the financial pressure of employees' needs, the cost of feed, veterinary expenses, housing expenses for the animals, taxes, insurance and production of milk on the dairy side. The family members who run this dairy farm also carry the financial pressure of the processing side of the business. They deal with bottling the milk, marketing the milk, delivering the milk, keeping the retailer happy, and keeping the customer happy. In one business, Mallorie's Dairy faces the risk of what is otherwise divided into two businesses in the industry. The pressure takes a toll on the owners. The financial pressure created by the \$83,000 monthly milk pool payment is too great. It cannot be withstood in addition to the other financial pressures on this family farm.

This family has no large paycheck at the end of the day. They don't have fancy cars or expensive homes. This family has employees that are loyal to them, a community that embraces them, the appreciation of other dairymen with whom they have a well-earned reputation of being involved and helpful, retailers that love them because they provide the mom and pop stores with respect and quality products, and this family has a moral commitment to the idea that family farms are important.

In the big picture, Mallorie's Dairy is not disrupting the milk market. The percentage of the market that they serve is less than 1%. The difficulties associated with the impending death taxes, the increased cost of land and the risks of both producing and bottling the milk are too great. The proposed rule is the "\$83,000 a month straw" that will break the camel's back.

The Regulatory Flexibility Act requires the agency to address the requirements of the rule and steps taken to minimize the economic impact on small entities. The Agricultural Marketing Service did not properly consider the economic impact of this action on small entities like Mallorie's. They did not properly inquire into the scope of financial demand created by this proposed rule. They did not consider other economic factors facing family farms in conjunction with the proposed rule. If Agricultural Marketing Service had properly considered the economic impact of this action on small entities, it could not have come to the conclusion that a family farm like Mallorie's could survive the imposition of the \$83,000 monthly payment, and it could not have certified that the rule would not have a significant economic impact on small entities.

Sincerely,



HEATHER O. GILMORE

HG/gh

c Juanita Mallorie
Mallorie's Dairy, Inc.
Benjamin Yale, Esq.

DEPARTMENT OF AGRICULTURE

Agricultural Marketing Service

7 CFR Parts 1000, 1001, 1002, 1004, 1005, 1006, 1007, 1012, 1013, 1030, 1032, 1033, 1036, 1040, 1044, 1046, 1049, 1050, 1064, 1065, 1068, 1076, 1079, 1106, 1124, 1126, 1131, 1134, 1135, 1137, 1138 and 1139

DA-97-12

Milk in the New England and Other Marketing Areas; Decision on Proposed Amendments to Marketing Agreements and to Orders

AGENCY: Agricultural Marketing Service, USDA.

ACTION: Proposed rule.

7 CFR Part	Marketing Area
1000	General Provisions of Federal Milk Marketing Orders
1001	New England
1002	New York-New Jersey
1004	Middle Atlantic
1005	Carolina
1006	Upper Florida
1007	Southeast
1012	Tampa Bay
1013	Southeastern Florida
1030	Chicago Regional
1032	Southern Illinois-Eastern Missouri
1033	Ohio Valley
1036	Eastern Ohio-Western Pennsylvania
1040	Southern Michigan
1044	Michigan Upper Peninsula
1046	Louisville-Lexington-Evansville
1049	Indiana
1050	Central Illinois
1064	Greater Kansas City
1065	Nebraska-Western Iowa
1068	Upper Midwest
1076	Eastern South Dakota
1079	Iowa

population of dairy farmers. All producers, regardless of race, national origin, or disability choosing to deliver milk to a Federal order regulated handler will receive the minimum blend price.

Copies of the Civil Rights Impact Analysis can be obtained from Dairy Programs at (202) 720-4392; any Market Administrator office; or via the Internet at <http://www.ams.usda.gov/dairy/>.

The Regulatory Flexibility Act and the Effects on Small Businesses.

Pursuant to the requirements set forth in the Regulatory Flexibility Act (5 U.S.C. 601 et seq.), the Agricultural Marketing Service (AMS) has considered the economic impact of the rule on small entities and has prepared this final regulatory flexibility analysis. The Regulatory Flexibility Act provides, in summary, that when preparing such analysis an agency shall address: the need for and objectives of the rule; summary of the significant issues raised in public comments, agency assessment of the issues raised, and changes made to the proposed rule based on these issues; the kind and number of small entities affected; the recordkeeping, reporting, and other requirements; and steps taken to minimize the economic impact on small entities.

This regulatory action is in accordance with Section 143 of the Federal Agriculture Improvement and Reform Act of 1996, 7 U.S.C. §7253, (the Farm Bill) which required the Secretary of Agriculture (Secretary) to consolidate the existing 31 Federal milk marketing orders, as authorized by the Agricultural Marketing Agreement Act of 1937 (AMAA), into between 10 and 14 orders. The Farm Bill further provided that the Secretary may address related issues such as the use of utilization rates and multiple basing points for the pricing of fluid milk and the use of uniform multiple component pricing when developing one or more basic prices for manufacturing milk. The Secretary was also directed to designate the State of California as a Federal milk order if California dairy producers petition for and approve such an order. Finally, the Farm Bill specified that the Department of Agriculture use informal rulemaking to implement these reforms.

The Farm Bill required that a proposed rule be published by April 4, 1998, and all reforms of the Federal milk order program be completed by April 4, 1999. However, the Omnibus Consolidated and Emergency Supplemental Appropriations Bill, passed in October 1998, extended the time frame for implementing Federal milk order reform amendments from April 4, 1999, to October 1, 1999. The extension specified that the final decision, defined as the final rule for purposes of this legislation, be issued between February 1 and April 4, 1999, with the new amendments becoming effective on October 1, 1999. The legislation also provides that California has from the date of issuance of the final decision until

September 30, 1999, to become a separate Federal milk marketing order.

The final decision sets forth the consolidation of the current 31 Federal milk orders into 11 orders. Several issues related to the consolidation of Federal milk orders are also addressed. The final decision contains a replacement for the Class I price structure and the basic formula price. These changes set the stage for increasing efficiencies in supplying the milk needs of Class I markets and address concerns that the BFP is no longer a statistically significant measure of the value of manufacturing milk. The final decision also changes the classification of milk by (1) establishing Class IV provisions which would include milk used to produce nonfat dry milk, butter, and other dry milk powders; (2) reclassifying eggnog; and (3) making other minor classification changes. These changes recognize the position of butter and milk powders as residual products that balance the supply of milk with overall demand, and equalize the cost of competing products. Finally, this final decision expands Part 1000 to include provisions that are identical within each consolidated order to assist in simplifying the regulations. These provisions include the definitions of route disposition, plant, distributing plant, supply plant, nonpool plant, handler, other source milk, fluid milk product, fluid cream product, cooperative association, and commercial food processing establishment. In addition, the milk classification section, pricing provisions, and some of the provisions relating to payments have been included in the General Provisions. These changes adhere with the efforts of the National Performance Review - Regulatory Reform Initiative to simplify, modify, and eliminate unnecessary repetition of regulations. Unique regional issues or marketing conditions have been considered and included in each market's order provisions.

The purpose of the Regulatory Flexibility Act is to fit regulatory actions to the scale of business subject to the actions in order that small businesses are not unduly or disproportionately burdened. To accomplish this purpose, it first is necessary to define a small business. According to the Small Business Administration's definition of a "small business," a dairy farm is a "small business" if it has an annual gross revenue of less than \$500,000 and a handler is a "small business" if it has fewer than 500 employees. For the purposes of determining which dairy farms are "small businesses," the \$500,000 per year criterion was used to establish a production guideline of 326,000 pounds per month. Although this guideline does not factor in additional monies that may be received by dairy producers, it should be an inclusive standard for most "small" dairy farmers. For purposes of determining a handler's size, if the plant is part of a larger company operating multiple plants that collectively

exceed the 500-employee limit, the plant will be considered a large business even if the local plant has fewer than 500 employees.

Based on 1996 data, USDA identified approximately 80,000 of the 83,000 dairy producers (farmers) that had their milk pooled under a Federal order as small businesses. Thus, small businesses represent approximately 96 percent of the producers in the United States. By 1997 the total number of dairy producers that had their milk pooled under a Federal order had declined to about 79,000. It is estimated that nearly 76,000 are small businesses.

During 1997, 78,590 dairy farmers delivered over 105.2 billion pounds of milk to handlers regulated under the milk orders. This volume represents 68 percent of all milk marketed in the U.S. and 70 percent of the milk of bottling quality (Grade A) sold in the country. The value of the milk delivered to Federal milk order handlers at minimum order blend prices was nearly \$14.0 billion. Producer deliveries of milk used in Class I products (fluid milk products) totaled 44.9 billion pounds--42.7 percent of total Federal order producer deliveries. More than 200 million Americans reside in Federal order marketing areas--77 percent of the total U.S. population.

On the processing side, there are over 1,200 individual plants associated with Federal orders, and of these plants, approximately 700 qualify as "small businesses" representing about 55 percent of the total. During October 1997, there were more than 485 fully regulated handlers (306 distributing plants of which 111 were small businesses and nearly 180 supply plants of which about 50 percent were small businesses), 51 partially regulated handlers of which 28 were small businesses and 111 producer-handlers of which all were considered small businesses for purposes of this final RFA, submitting reports under the Federal milk marketing order program.

The Federal milk order program is designed to set forth the terms of trade between buyers and sellers of fluid milk. A Federal order enforces the minimum price that processors (handlers) in a given marketing area must pay producers for milk according to how it is utilized. A Federal order further requires that the payments for milk be pooled and paid to individual dairy producers or cooperative associations on the basis of a uniform or average price. It is important to note that a Federal milk order, including the pricing and all other provisions, only becomes effective after approval, through a referendum, by dairy producers associated with the order.

Development of this final decision began with the premise that no additional burdens should be placed on the industry as a result of Federal order consolidation and reform. As a step in accomplishing the goal of imposing no additional regulatory burdens, a review of the current reporting requirements was

completed pursuant to the Paperwork Reduction Act of 1995 (44 U.S.C. Chapter 35). In light of this review, it was determined that this final decision would have little impact on reporting, recordkeeping, or other compliance requirements because these would remain almost identical to the current Federal order program. No new forms are required; however, some additional reporting will be necessary in the orders that are adopting multiple component pricing if the current orders do not contain these provisions. Overall, there would be slight change in the burdens placed on the dairy industry.

There are two principal reporting forms for handlers to complete each month that are needed to administer the Federal milk marketing orders. The forms are used to establish the quantity of milk used and received by handlers, the pooling status of the handler, the class-use of the milk used by the handler, the butterfat content and amounts of other components of the milk. This information is used to compute the monthly uniform price paid to producers in each of the markets. Handlers in the marketing areas adopting multiple component pricing will be required to complete additional information regarding the components of the milk and to assure that proper payments are made to producers. This information is necessary to establish the values of milk on the basis of milk components and to assure that producers are paid correctly. Many handlers already collect and report this information.

This rule does not involve additional information collection that requires clearance by the Office of Management and Budget beyond the 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 which 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.

New territory, or pockets of unregulated territory within and between current order areas has been included in the consolidated marketing areas where such expansion will not have the effect of fully regulating plants that are not now regulated. The addition of these areas benefits regulated handlers by eliminating the necessity of reporting sales outside the Federal order marketing area for the purpose of determining pool qualification. Where such areas can be added to a consolidated area without having the effect of causing the regulation of any currently-unregulated handler, they are added.

Handlers not currently fully regulated under Federal orders may become regulated for two main reasons: first, in the process

of consolidating marketing areas, some handlers who currently are partially regulated may become fully regulated because their sales in the combined marketing areas meet the pooling standards of a consolidated order area. Second, a previously unregulated area in New York, Vermont, New Hampshire and Massachusetts was added on the basis of supporting information. As a result, previously unregulated handlers would become fully regulated. Because of these two reasons, 11 additional plants are expected to become fully regulated under the program. Of these 11 plants, it is estimated that 5 are small businesses that would need to comply with the reporting, recordkeeping, and compliance requirements. The completion of these reports will require a person knowledgeable about the receipt and utilization of milk and milk products handled at the plant. This most likely will be a person already on the payroll of the business such as a bookkeeper, controller or plant manager. The completion of the necessary reporting, recordkeeping, and compliance requirements does not require any highly specialized skills and should not require the addition of personnel to complete. In fact, much of the information that handlers report to the market administrator is readily available from normally maintained business records, and as such, the burden on handlers to complete these recordkeeping and reporting requirements is minimal. In addition, assistance in completing forms is readily available from market administrator offices. A description of the forms and a complete Paperwork Reduction Act analysis follows this section.

No other burdens are expected to fall upon the dairy industry as a result of overlapping Federal rules. The regulations contained in this final decision do not duplicate, overlap or conflict with any existing Federal rules.

PUBLIC COMMENTS

More than 1,000 comments were received from interested parties that specifically stated or documented they were small businesses. However, this number may not be fully representative of the number of small businesses that actually submitted comments because a majority of commenters did not indicate their size. Of the comments submitted, the majority were received from dairy producers. The comments from the producers primarily addressed the issues of Class I pricing and consolidation.

A few comments were received that specifically addressed the initial regulatory flexibility analysis (IRFA). These comments also addressed the issues of Class I pricing and consolidation and further addressed the issue of producer-handler regulation. The Small Business Administration submitted views specifically addressing exempt plant status and requesting further analysis of the impact of consolidation on previously unregulated entities, if possible.

Nearly all of the 1,000 comments addressed Class I pricing