

BEFORE THE UNITED STATES DEPARTMENT OF AGRICULTURE

2001 FEB -9 P 1: 18

In the Matter of

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**MILK IN THE NORTHEAST AND
OTHER MARKETING AREAS**

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**DOCKET NO. AO-14-A69, et al.
DA-00-03**

COMMENTS BY

**SELECT MILK PRODUCERS, INC.,
ELITE MILK PRODUCERS, INC., CONTINENTAL DAIRY PRODUCTS, INC.,
AND THE FOLLOWING TRADE ORGANIZATIONS:
WESTERN STATES DAIRY PRODUCERS TRADE ASSOCIATION,
DAIRY PRODUCERS OF NEW MEXICO, TEXAS ASSOCIATION OF DAIRYMEN,
MILK PRODUCERS COUNCIL (CALIFORNIA), CALIFORNIA DAIRY CAMPAIGN,
WESTERN UNITED DAIRYMEN (CALIFORNIA), IDAHO DAIRYMEN'S
ASSOCIATION, UTAH DAIRYMEN'S ASSOCIATION, OREGON DAIRY FARMER'S
ASSOCIATION, AND WASHINGTON STATE DAIRY FEDERATION
IN RESPONSE TO THE TENTATIVE FINAL DECISION**

1. Introduction

These comments are in response to the proposed rule ("Tentative Final Decision") of the Secretary issued on December 1, 2000. The comments represent the position of Select Milk Producers, Inc., Elite Milk Producers, Inc., Continental Dairy Products, Inc., and the following trade organizations: Western States Dairy Producers Trade Association, Dairy Producers of New Mexico, Texas Association of Dairymen, Milk Producers Council (California), California Dairy Campaign, Western United Dairymen (California), Idaho Dairymen's Association, Utah Dairymen's Association, Oregon Dairy Farmer's Association, and Washington State Dairy Federation (collectively "Select, WSDPTA and other organizations" or the "Dairy Producer Organizations").

The trade organizations represent their dairy producer members in administrative and legislative fora. These organizations promote the interests of their dairy producer members, including price regulations, not only before the Secretary but in the states in which they are located -- California, Idaho, New Mexico, Oregon, Texas, Utah and Washington. The constituent dairy producer members combined produce approximately thirty (30) percent of the Nation's milk supply. The named cooperatives have producers located in New Mexico, Texas, Ohio, Indiana, and Michigan. Milk produced on these farms is marketed in California and all FMMOs except the Northeast.

2. Filing under protest.

These comments are filed under protest. On February 2, 2001, the AMS issued a press release. A copy is attached as "Exhibit A" to this brief. That release states that the period of time for responding to the Tentative Final Decision was extended to April 6, 2001. In response to that public notice, members of Western States Dairy Producers Trade Association did not make a final decision on comments at a 12:00 noon (E.S.T.) telephone conference held on February 2, 2001. The decision was instead deferred until their meeting, Tuesday February 6, 2001. At 3:30 p.m. (E.S.T.) On February 2, 2001, I returned to my office to find that the notice deadline for the comment period was again February 5, 2001!

This is patently unfair.

The following is a draft of comments which were not fully discussed by the constituent members but is being sent for consideration in the event the comment period is not enlarged as originally promised.

3. Summary of Comments

The Dairy Producer Organizations incorporate herein their testimony at the hearing as well as the arguments made in their written arguments following the hearing into these comments. These comments are supplemental and directed to specific issues raised in the Tentative Final Decision.

The Dairy Producer Organizations respectfully request the Secretary to address the various elements of the Tentative Final Decision in the following manner:

- Modify the protein and butterfat yield formulas in the protein computation to account more accurately for butterfat recovery and whey cream.
- Maintain the adjustment to 38% moisture for cheddar cheese.
- Maintain the three cent barrel to block spread.
- Maintain the yield of one for NFDM to SNF.
- Maintain the make allowance for dry whey and NFDM at 14 cents.
- Maintain the snubber on the other solids formula.
- Reconsider the use of the NASS survey as the product price.
- Remove the separate butterfat price for Class III.

The Dairy Producer Organizations request that the Secretary revisit and modify the protein formula in the Tentative Final Decision to recognize the fact that the implied butterfat yield is too low and that cheddar cheese processing yields a valuable product in the form of whey cream.

Upon re-examination of the hearing record, the Secretary will find that there are several changes to make to this Tentative Final Decision. Those three areas include the following and will be discussed in turn below: (1) The butterfat recovery percentage in the Class III formula

should be increased; (2) the value of whey cream must be allocated for in the Class III price; and (3) the decision to create a separate Class III butterfat price should be reversed.

The Dairy Producer Organizations recognize the tremendous experience, effort and time invested by the Secretary, staff of Dairy Programs, and others in the United States Department of Agriculture (USDA) in considering the issues raised by this hearing and arriving at a Tentative Final Decision. These organizations deeply appreciate, and support, the efforts made.

The Federal Milk Marketing Orders continue to be the most successful federal program for dairy farmers. Day in and day out it contributes value to dairy farmers throughout the Nation— value that would be lost if the program was not in force. Its continued vitality is essential to the success of dairy farmers in this Nation including members of Select Milk Producers and the other Dairy Producer Organizations. Ever changing economic and technological aspects of dairy production, processing and marketing require an equally vigilant effort to insure that the Federal Milk Marketing Orders support the dairy industry and dairy producers without suffocating the industry. Though the Dairy Producer Organizations are not in full agreement with all of the terms of the Tentative Final Decision, we certainly understand that the Secretary seeks to make the Federal Milk Marketing Orders more responsive to today's markets while still supporting producers. We applaud that.

4. The percentage for the butterfat recovery used in the Tentative Final Decision is in error.

On the issue of butterfat recovery, the Dairy Producer Organizations were very disappointed and surprised that the Tentative Final Decision was silent on this point. The Dairy Producer Organizations proposed that the Class III formula include a 92% butterfat recovery factor. Our specific proposal was that the current 1.582 factor in the formula be changed to

1.617. Extensive evidence was presented on that point, but there is no reference to it whatsoever in the Tentative Final Decision.

Dr. Barbano, who is recognized as one of the top experts in the world in the area of cheese processing technology, testified at the hearing that, "The default assumption for fat recovery in cheese of 90 percent is low in relation to average cheese industry performance using average modern cheese-making technology. In my opinion, a more representative average value for large modern cheese factories would be 91.5 percent." [Hearing Transcript at page 578]. On this subject particularly, Dr. Barbano's testimony needs to be very seriously considered.

The Dairy Producer Organizations request that the Secretary revisit this issue in the Final Rule and either adopt a higher butterfat recovery in the Class III formula or explain why the evidence on this subject is being rejected.

5. The Tentative Final Decision fails to account for the value of whey cream in the Class III price.

The Dairy Producer Organizations were likewise very disappointed and surprised that the Tentative Final Decision was silent on the issue of a value for whey cream. The Tentative Final Decision specifically utilizes a butterfat recovery percentage of 90% in developing the 1.582 factor in the Class III formula, leaving 10% of the butterfat clearly unaccounted for in the product value formula. That 10% constitutes over one-third of a pound of butterfat for every hundred weight of 3.5% butterfat farmer milk processed by a cheese plant. That whey butterfat has significant value as was demonstrated in a series of answers given by Dr. Barbano to questions asked by John Vetne about the cheese making process. [Hearing Transcript at page 712-719].

In Dr. Barbano's testimony, he referred to the necessity of checking the validity of a formula by taking all the value of the products made from a hundred weight of milk delivered to

a cheese plant and subtracting out the manufacturing allowances and the milk price. If the formula correctly accounts for all the value, the net result of this exercise according to Dr. Barbano should be zero. However, as Mr. Rosenbaum pointed out in his very first question in cross-examination of Dr. Barbano, [Hearing Transcript at page 589] in the Final Rule formula, the value of the products made from a hundred weight of milk exceed the milk price plus the make allowance by over \$0.30 per cwt. In this exercise, Dr. Barbano [page 15 of Barbano's testimony] specifically included a value for whey cream. Since the Final Rule Class III formula excluded any product value consideration of the 10% of butterfat that does not end up in the cheese, it is not surprising that Dr. Barbano's exercise, which includes a whey cream value would show missing milk price revenue. By contrast, as was pointed out at the hearing, the California State run milk-pricing system expressly provides a value in its 4b formula for whey cream.

The Dairy Price Support Program historically recognized the value of whey cream in setting cheese purchase prices. As explained in the attached "Exhibit B", the Secretary offset the make allowance for cheddar cheese by 16 cents which was the estimated value of whey cream. The industry used those numbers for years and paid producers at or above the price support level and profitably sold cheese to the CCC. There is nothing in the record that would suggest that such is not the case still today.

The Dairy Producer Organizations specifically proposed a method whereby the value of whey cream could be accounted for in the Class III formula without requiring another product value factor in the formula. That proposal suggested subtracting a percentage of the value of one pound of Class IV butterfat from the Class III protein value, rather than a full pound of Class IV

butterfat as the Final Rule formula did, therefore providing for the value of whey cream in the protein price.

Dr. Barbano essentially endorsed this approach in a response to a question by Ben Yale about what could be done to address the issues he had raised within the limitations of the existing formulations. [Hearing Transcript at page777-780].

Moreover, there is no contradicting evidence that ordinary cheddar includes the process of reusing the whey cream. Though Kraft demands a higher quality by using sweet cream, it does not report its prices to NASS. [Reinke 1047, 1070]. Although Leprino does not make cheddar, its witness did testify that there is the reuse of whey cream. [Taylor 1734].

One of the arguments against the use of whey cream in valuation was that the whey cream is of less value. [Taylor 1733, 1761. Reinke 1041]. This is not true. The purpose of whey recovery is not to value butter! It is to value the protein as a residual of the butter used. The incorporation of whey cream recognizes that cheese plants are able to obtain more value of the protein, because they have more fat to bind into the cheese. It is irrelevant what the whey costs because it is not being sold as whey cream, but as full cheddar cheese. The whey cream is returned to the vat to make cheese. That cheese gets the same price per pound as the cheese made from the original vat. There is no factual basis for reducing this value. The make allowances already pay for it.

6. **Accounting for whey cream solves the problem of dropping Class III cwt. prices when butter prices rise and cheese prices are stable and therefore corrects much of the problem the separate Class III butterfat price sought to correct.**

The Dairy Producer Organizations support the Unified Comments of the Industry, which are detailed in a separate letter on the issue of a separate Class III Butterfat Price. The Dairy Producer Organizations deeply appreciate the concern that the Secretary has over the volatility of

protein value in the component pricing which the Class III Butterfat Price was designed to create. There is no readily available fix for that problem, however. The complexity of the pricing formulas in the current rules means any change in the fundamental relationship between components and class prices and between the class prices themselves will ripple through the rest of the formulas in sometimes unpredictable and undesirable ways.

One of those concerns is that the Class III price at 3.5% butterfat will decline in a steady cheese but rising butter market. This can be corrected in large part by accounting for whey cream.

A residual benefit of adopting the Western States approach of accounting for whey cream by subtracting .94 times the Class IV butterfat value from the Class III protein price is that it greatly reduces the problem in the Final Rule of the Class III 3.5 price dropping when butter prices rise and cheese prices remain constant. The Tentative Final Rule without the Class III Butterfat Price formulas results in a Class III 3.5 price to drop \$0.042 for every \$0.10 per pound increase in the butter price. On the other hand, if the adjustment of the Class IV butterfat price is made at the same percentage as the percentage for butterfat recovery implicit in the 1.582 factor (*i.e.*, 90%), then this problem is completely eliminated and any increase in the butter price has no negative impact on the Class III butterfat price.

For example, all other things being equal, if the butter price is \$1.10 per pound, dry whey at 18 cents, and the cheese price is 1.10 per pound the cwt. value of Class III would be 9.38. If the butter price rises to 1.20 per pound and the cheese price stays at 1.10 per pound the Class III cwt. price drops to 9.33 if the 90% butterfat recovery number currently in the Final Rule is equally applied to the Class IV butterfat value in the butterfat adjustment to the Class III protein price. As a result the protein formula looks like this:

(Cheese price - Make allowance * 1.405) + ((cheese price - make allowance * 1.582) - (.90 * Class IV butterfat price)) * 1.28.

If that formula is adopted, then at those times when the butter price rises the Class III cwt. price is not reduced. Thus, this would address a major issue that the Secretary identified with the Final Rule Class III formula.

These additional positive changes to the decisions the Secretary made in the Tentative Final Decision will contribute to restoring the historical relationship that existed between dairy commodity values and the milk prices derived from the M/W and BFP price formulas.

7. **The Secretary should maintain the use of 38% moisture and the 3 cent block barrel difference as provided in the Tentative Final Decision.**

The Secretary was absolutely correct in adjusting the moisture for barrels to 38% moisture. The evidence on that issue was overwhelming and not contradicted. Similarly there was nothing in the record that justified a reduction of the 3 cent adjustment for barrel cheese in the weighing of cheese prices.

8. **The Secretary Should use a yield of one for NFDM to SNF.**

The Secretary's approach in setting the yield of NFDM at one is appropriate. It recognizes the yield of NFDM and the yield of lower valued dry buttermilk powder in the process without creating an unfair burden on powder plants.

9. **The Secretary should leave the dry whey provisions alone.**

In the formulas for other solids, the Secretary proposed a 14 cent make allowance and put a snubber so that the Class III price could be reduced by adding other solids. These are excellent provisions, the logic and explanation of the Secretary is correct, and they should be maintained.

10. Other Issues

There are several other, non language, but important issues that should be also addressed. The first is the use of the Model to evaluate the final decision. The use of this Model in the Preliminary Analysis and the Economic Analysis has value, but there are serious problems with its use.

The first is that is analysis violates the AMAA. Section 608c(18) of the AMAA provides that the prices fixed by the Secretary must "reflect the price of feeds, the available supplies of feeds, and other economic conditions which affect market supply and demand for milk. . .in the marketing area to which the contemplated marketing. . .order, or amendment relates." 7 U.S.C. § 608c(18) (1980). [Emphasis added]. The Model, by its own admission, looks at the impact of the rules on a national basis, not an order basis. We recognize that from a purely economic view point such is justified. The view point required by Congress is altogether different. Unless the model addresses *intra market area* economics, it is legally flawed and reliance upon it jeopardizes any result it is used to justify.

This is not an academic or jurisprudential statement. The use of the Model as a national evaluation masks the damages of the too low Class III price in some orders such as the Western and the Upper Midwest where Class III utilization, pooled or not, is the highest in the Nation. The impact of higher NFDM prices and that corresponding increase in Class I and Class II prices, though included in the national average incorporated into the Model, have not positively impacted areas such as Idaho and Utah where the Class III is so dominant. In short, the use of an average always minimizes the brutal impact of the extremes.

Congress has long recognized this and that is why it continues to require the Secretary to look at impacts in the marketing area. It is the Congress' purview, not the Secretary's to rewrite

the law.

A second concern over the use of the Model is that it represents post hearing testimony which the parties were not allowed to cross examine, inquire, or challenge. If the Model used in analyzing the comments and resulting changes is the exact same model as presented at the hearing, this might be minimal. The Secretary needs to clearly identify if it is the same model.

11. Conclusion

Select Milk Producers and the other Dairy Producer Organizations respectfully request that the Secretary revisit the hearing record and

- Modify the protein and butterfat yield formulas in the protein computation to account more accurately for butterfat recovery and whey cream.
- Maintain the adjustment to 38% moisture for cheddar cheese.
- Maintain the three cent barrel to block spread.
- Maintain the yield of one for NFDM to SNF.
- Maintain the make allowance for dry whey and NFDM at 14 cents.
- Maintain the snubber on the other solids formula.
- Reconsider the use of the NASS survey as the product price.
- Remove the separate butterfat price for Class III.

Respectfully submitted,
BENJAMIN F. YALE & ASSOC. CO.,
LPA



BENJAMIN F. YALE, OH #0024730
KRISTINE H. REED, OH # 0066668

102 W. Wapakoneta
P.O. Box 100
Waynesfield, OH 45896
419-568-5751
419-568-6413 Fax

CERTIFICATE OF SERVICE

I hereby certify that an accurate photostatic copy of the foregoing was served upon the following this 5th day of February, 2001, by ordinary United States Mail service, postage prepaid.

The Honorable James W. Hunt, ALJ
United States Dept. of Agriculture
Room 1081, South Building
1400 Independence Avenue SW
Washington DC 20250

Constance M. Brenner
P.O. Box 96456
Washington, DC 20090-6456

Sydney Berde, Esq.
SYDNEY BERDE & ASSOCIATES P.A.
7327 East Echo Lane
Scottsdale AZ 85258

Marvin Beshore, Esq.
MILSPAW & BESHORE
P.O. Box 946
Harrisburg, PA 17108-0946

Keith Collins
Chief Economist
U.S. Department of Agriculture
Jamie L. Whitten Federal Building
Room 112-A
14th Independence Avenue, S.W.
Washington, D.C. 20250

Kathleen Merrigan
Administrator
Agricultural Marketing Service
U.S. Department of Agriculture
South Agriculture Building
Room 3071
1400 Independence Avenue, S.W.
Washington, D.C. 20250

Gregory Cooper, Esq.
Office of General Counsel
U.S. Department of Agriculture
1400 Independence Avenue, SW
Washington, D.C. 20250-1417

Charles M. English, Jr., Esq.
Wendy M. Yoviene, Esq.
Thelen Reid & Preist, LLP
701 Pennsylvania Ave. NW
Suite 800
Washington, D.C. 20004

Steve Rosenbaum, Esq.
Covington & Burling
1201 Pennsylvania Avenue, N.W.
Washington, D.C. 20044

John Vetne, Esq.
79 State Street
Newburyport, MA 01950

Larry Salathe
Agricultural Economist
U.S. Department of Agriculture
Jamie L. Whitten Federal Building
Room 112-A
14th & Independence Avenue, S.W.
Washington, D.C. 20250

Richard McKee
Deputy Administrator, Dairy Programs
Agricultural Marketing Service
U.S. Department of Agriculture
South Agriculture Building
Room 2968
1400 Independence Avenue, S.W.
Washington, D.C. 20250

John Mengel
Chief Economist, Dairy Programs
Agricultural Marketing Service
U.S. Department of Agriculture
South Agriculture Building
Room 2753
1400 Independence Avenue, S.W.
Washington, D.C. 20250

Brad Olsen, Esq.
Leprino Foods
1830 West 38th Avenue
Denver, CO 80211

Michael Dunn
Under Secretary for Marketing &
Regulatory Programs
U.S. Department of Agriculture
Administration Building (Main Building)
Room 228-W
1400 Independence Avenue, S.W.
Washington, D.C. 20250



BENJAMIN F. YALE
KRISTINE H. REED

EXHIBIT A

Release No. AMS-43-01

Becky Unkenholz (202) 720-8998

becky.unkenholz@usda.gov

Billy Cox (202) 720-8998

billy.cox@usda.gov

USDA ENJOINED FROM IMPLEMENTING CLASS III BUTTERFAT PRICE

WASHINGTON, D.C., Feb. 2, 2001 - U.S. District Court Judge Royce C. Lamberth enjoined USDA from implementing portions of the interim final amendments to Federal milk orders that became effective Jan. 1, 2001. The Judge's order restores the butterfat and protein price formulas that were implemented under Federal order reform on Jan. 1, 2000, with the following changes:

-Incorporate the 16.5-cent make allowance for cheese and the 38-percent moisture adjustment for 500-pound barrel cheese adopted in the Jan. 1, 2001, interim final amendments.

-Incorporate the 11.5-cent make allowance for butter adopted in the Jan. 1, 2001, amendments in the formula for calculating the butterfat price applicable to both Class III and Class IV.

-Incorporate the Jan. 1, 2001, nonfat solids and other solids price formulas, based on the values of these components in nonfat dry milk and dry whey.

The tentative final decision and interim rule responded to a Congressional mandate, included in the Consolidated Appropriations Act, 2000, to reconsider certain pricing formulas adopted in the final rule for the consolidation and reform of Federal milk orders.

In addition, to ensure full opportunity to comment on the tentative final decision, published on Dec. 7, 2000, the comment period is being extended to April 6, 2001. Notice of this extension will appear soon in the Federal Register.

The following market administrators can provide additional information about the injunction.

Northeast: Erik F. Rasmussen

USDA/AMS/Dairy Programs

P.O. Box 1478 (FT Point Station), Boston, MA. 02205-1478

Tel. (617) 542-8966;

email: Erik.Rasmussen@USDA.GOV

Appalachian: Arnold M. Stallings

USDA/AMS/Dairy Programs

P.O. Box 18030, Louisville, KY. 40261-0030

Tel. (502) 499-0040; email: Arnold.Stallings@USDA.GOV

Florida and Southeast: Sue. L. Mosley

USDA/AMS/Dairy Programs

P.O. Box 1208, Norcross, GA. 30091-1208

Tel. (770) 448-1194; email: Sue.Mosley@USDA.GOV

Upper Midwest: H. Paul Kyburz

USDA/AMS/Dairy Programs

Suite 210, 4570 West 77th St., Minneapolis, MN. 55435-5037

Tel. (952) 831-5292; email: Paul.Kyburz@USDA.GOV

**CFSA
Commodity
Fact Sheet**

**1994-95 DAIRY
PRICE SUPPORT
PROGRAM**

United States
Department of
Agriculture

Consolidated
Farm Service
Agency

June 1995

**BASIC
LEGISLATIVE
AUTHORITY**

The basic provisions of the Agricultural Act of 1949 (1949 Act) required that the price of milk to producers be supported at such level between 75 and 90 percent of parity as would assure an adequate supply of milk, reflect changes in the cost of production, and assure a level of farm income to maintain productive capacity sufficient to meet future needs. However, since October 21, 1981, the support price has been established by Congress either at specific price levels, or by formula related to expected surplus, rather than parity levels.

**CURRENT
LEGISLATIVE
AUTHORITY**

On November 28, 1990, President Bush signed into law the Food, Agriculture, Conservation, and Trade Act of 1990. The 1990 Act provides that the price of milk be supported at a rate not less than \$10.10 per hundredweight (cwt.) through 1995. The 1990 Act further provides that in estimating the purchases of butter, cheese and nonfat dry milk the estimated purchases will be measured on a milk equivalent, total milk solids basis.

The Secretary of Agriculture for each of calendar years 1991-1995 is required to:

- (1) Increase the support price at least 25 cents per hundredweight (cwt.) if the Department of Agriculture's (USDA) estimate of annual purchases does not exceed 3.5 billion pounds, milk equivalent.
- (2) Make no change in the support price if USDA's estimate of annual purchases exceeds 3.5 billion pounds, but not 5 billion pounds, milk equivalent,
- and (3) Decrease the support price by 25 to 50 cents per cwt. if USDA's estimate of annual purchases exceeds 5 billion pounds, milk equivalent. The support price, however, may not be reduced below \$10.10 per cwt.

For the purpose of support price determination the Secretary is instructed to deduct from the estimated level of Commodity Credit Corporation (CCC) purchases,

EXHIBIT B

*Table 1--Calculations of CCC purchase prices for dairy products
with support of \$10.10 per cwt.*

<i>Item</i>	<i>Effective May 13, 1992</i>	<i>Effective July 7, 1993</i>
Support Price for manufacturing milk, \$/cwt. at 3.67% milkfat	10.10	10.10
Support price for manufacturing milk, \$/cwt. at 3.5% milkfat	9.97	10.00
Butterfat differential: 1/	7.7	6.1
Yields per 100 pounds of milk (3.67% milkfat)		
Butter	4.48	4.48
Nonfat Dry Milk	8.13	8.13
Cheese	10.1	10.1
<u>Butter-Nonfat Dry Milk Calculation</u>		
Return to butter-powder plants, \$/cwt.	10.10	10.10
CCC manufacturing allowance for converting 100 pounds of milk (3.67% milkfat) into butter and NDM, \$/cwt.	1.22	1.22
Value of butter and NDM (U.S. average) made from 100 pounds of milk, \$/cwt.	11.32	11.32
NONFAT DRY MILK PURCHASE PRICE (rounded), \$/lb.	.9730	1.0340
Value of NDM per 100 pounds milk, \$/cwt. 2/	7.91	8.41
Value of Butter:		
Dollars per 100 pounds of milk	3.41	2.91
Dollars per pound (calculated) 3/	.7612	.6496
BUTTER PURCHASE PRICE (rounded), \$/lb.	.7625	.6500
<u>Price Calculation</u>		
Return to cheese plants, \$/cwt.	10.10	10.10
CCC manufacturing allowance for converting 100 pounds of milk (3.67% milkfat) into cheese (40-lb. blocks) and whey, \$/cwt.	1.37	1.37
Value of cheese and whey/per 100 pounds of milk, \$/cwt.	11.47	11.47
Value of .25 pounds of whey fat: \$ 4/	.19	.16
Value of cheese:		
Dollars per 100 pounds of milk	11.28	11.31
Dollars per pound (calculated) 5/	1.1168	1.1198
CHEESE PURCHASE PRICE (rounded), \$/lb.		
Block	1.1175	1.1200
Barrel	1.0875	1.0900

1/ (Butter purchase price times 0.138) - (.0028 times 3.67 price). 2/ NDM price per pound times 8.13. 3/ Value of butter per 100 pounds of milk divided by 4.48. 4/ Butter purchase price times 0.25. 5/ Value of cheese per 100 pounds divided by 10.1.