



**BEFORE THE UNITED STATES DEPARTMENT
OF AGRICULTURE
AGRICULTURAL MARKETING SERVICE**

**In the Matter of Milk in California;
Notice of Hearing on a Proposal to
Establish a Federal Milk Marketing
Order**

**7 CFR Part 1051
Docket No.: AO-15-0071;
AMS-DA-14-0095**

Clovis, California, September 22, 2015

Testimony of Tom Wegner

**In Support of Proposal 1 of California Dairies, Inc.,
Dairy Farmers of America, Inc., and Land O'Lakes, Inc.**

**Proposal to Establish a Federal Milk Marketing Order for the
State of California**

Cooperatives' Exhibit 3

My name is Tom Wegner. I am here on behalf of Land O'Lakes, Inc. to testify in support of Proposal 1, sponsored by California Dairies, Inc., Dairy Farmers of America, Inc., and Land O'Lakes, Inc. My business address is 4001 Lexington Avenue North, Arden Hills, MN, 55164. My current title is Director of Governance and Leader Development. From 2005 to 2015 I served as the Director of Economics and Dairy Policy for Land O'Lakes. Land O'Lakes thanks the Department for calling this hearing to consider the adoption of a California federal milk marketing order.

Land O'Lakes is a dairy cooperative with 2,200 dairy farmer member-owners. Land O'Lakes has a national membership base, whose members are pooled on the California State Program and five different federal orders. Land O'Lakes members own several cheese, butter-powder and value-added plants in the Upper Midwest, East and California. Currently, our 200 California member-owners supply us with over 16 million pounds of milk per day that are primarily processed at our two plants in California located in Tulare and Orland. We also operate a dairy dessert plant in Turlock, California.

My testimony here is in two parts: the first addresses the Part 1000 uniform federal order provisions which we proposed to adopt in the California federal order. Second, I discuss Sections 1051.60, 1051.61, and 1051.62 which concern the handler value of milk for the pool, the calculation of multiple producer component prices, how we propose to address the pool value usually referred to as the PPD, and the dates for announcement of producer prices.

Part 1000 provisions.

In drafting the proposed California federal milk marketing order, we have endeavored to avoid unnecessary complication and lengthening of the order's language. We have identified those provisions contained in part 1000 that are common to all of the existing federal milk

marketing orders and propose that all part 1000 language remains unchanged. Utilizing these identical provisions in the proposed California federal order is consistent with the Federal Order Reform Decision issued in 1999 which expanded Part 1000 and explicitly stated:

Finally, this rule 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 most 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.

64 Fed. Reg. at 16031 (1999)

In light of the complexity and specificity of several of these provisions, we requested that USDA provide witnesses to assist with explanations for the record of the operation of several of these provisions and to specific questions about them. We appreciate greatly the testimony provided by Mr. Schaefer, Mr. Mykrantz, and Mr. Wise.

The scope and purpose of Part 1000 is explicitly stated in the following:

1000.1 Scope and purpose of Part 1000

Part 1000 sets forth certain terms, definitions, and provisions which are common to and apply to Federal milk marketing order in 7 CFR, chapter X, except as specifically defined otherwise, or modified, or otherwise provided, in an individual order in 7 CFR, chapter X.

We propose that Part 1051.1 General Provisions remains unchanged. We do not propose any changes to Part 1000 which would necessarily involve other federal orders.

1051.1 General Provisions.

All Part 1000 language remains unchanged

We propose that the marketing area would be coterminous with the borders of the entire state of California. The definition of the California marketing area follows directly from the language of the 2014 farm bill (the Agricultural Act of 2014) which specifically links the quota authorization to a petition for a marketing order for the “state of California.” The proposed language for the definition of the marketing area is:

1051.2 California marketing area.

The marketing area means all territory within the bounds of the following states and political subdivisions, including all piers, docks, and wharves connected therewith and all craft moored thereat, and all territory occupied by government (municipal, State, or Federal) reservations, installations, institutions, or other similar establishments if any part thereof is within any of the listed states or political subdivisions: All of the State of California.

We propose to adopt as 1051.3, the existing uniform definition for route disposition in Part 1000:

1051.3 Route disposition.

Route disposition means a delivery to a retail or wholesale outlet (except a plant), either directly or through any distribution facility (including disposition from a plant store, vendor, or vending machine) of a fluid milk product in consumer-type packages or dispenser units classified as Class I milk.

Route disposition refers to the measurement of fluid milk sales in commercial channels. It does not include the delivery of fluid milk products to a handler’s distribution points. The distribution from such points would be considered route disposition from the milk plant where the fluid milk products were processed and packaged. The market administrator will use route disposition to determine which fluid milk sales to include in the market wide pool. The reform decision contains the following concise definition:

Route disposition is a measure of fluid milk sales in commercial channels. It is defined to mean the amount of fluid milk products delivered by a distributing plant to a retail or wholesale outlet (except a plant), either directly or through any distribution facility (including disposition from a plant store, vendor or vending

machine), of a fluid milk product in consumer-type packages or dispenser units that is classified as Class I milk.

64 Fed. Reg. at 16130 (1999)

We propose to adopt as 1051.4 the existing uniform definition for a plant in Part 1000:

1051.4 Plant.

(a) Except as provided in paragraph (b) of this section, plant means the land, buildings, facilities, and equipment constituting a single operating unit or establishment at which milk or milk products are received, processed, or packaged, including a facility described in paragraph (b)(2) of this section if the facility receives the milk of more than one dairy farmer.

(b) Plant shall not include:

(1) A separate building without stationary storage tanks that is used only as a reload point for transferring bulk milk from one tank truck to another or a separate building used only as a distribution point for storing packaged fluid milk products in transit for route disposition; or

(2) An on-farm facility operated as part of a single dairy farm entity for the separation of cream and skim or the removal of water from milk.

A plant definition is needed to specify what comprises an operating entity for federal milk order pricing and regulatory purposes and what does not comprise an operating entity. The reform decision provides a comprehensive plant definition:

A plant definition is included to specify what constitutes an operating entity for pricing and regulatory purposes. As provided in 1000.4 of the General Provisions, a plant is the land, buildings, facilities, and equipment constituting a single operating unit or establishment at which milk or milk products are received, processed, or packaged. This is meant to encompass all departments, including those where milk products are stored, such as a cooler. The plant definition does not include a physically separate facility without stationary storage tanks that is used only as a reload point for transferring bulk milk from one tank to another, or a physically separate facility that is used only as a distribution point for storing packaged fluid milk products in transit for route disposition.

64 Fed. Reg. at 16130-16131 (1999)

We propose to adopt as 1051.5, the existing uniform definition for a distributing plant in Part 1000:

1051.5 Distributing plant.

Distributing plant means a plant that is approved by a duly constituted regulatory agency for the handling of Grade A milk at which fluid milk products are processed or packaged and from which there is route disposition or transfers of packaged fluid milk products to other plants.

This provision defines the plants that process or package fluid milk products from which packaged fluid milk products are distributed into commercial channels or transferred to other plants. The reform decision contains the following definition of a distributing plant:

A distributing plant is defined as a plant that is approved by a duly constituted regulatory agency to handle Grade A milk and at which fluid milk products are processed or packaged and from which there is route disposition or transfers of packaged fluid milk products to other plants.

64 Fed. Reg. at 16131 (1999)

We propose to adopt as 1051.6, the existing uniform definition for a supply plant in Part 1000:

1051.6 Supply plant.

Supply plant means a plant approved by a duly constituted regulatory agency for the handling of Grade A milk that receives milk directly from dairy farmers and transfers or diverts fluid milk products to other plants or manufactures dairy products on its premises.

The supply plant provision provides another way for dairy farmers to qualify/associate their milk with the California federal market wide pool. The reform decision included the following language consistent with the proposed definition of a supply plant:

A supply plant is a regular or reserve supplier of bulk milk for the fluid market that helps to coordinate the supply of milk with the demand for milk in a market. A supply plant is a plant approved by a duly constituted regulatory agency for the handling of Grade A milk that receives milk directly from dairy farmers and transfers

or diverts fluid milk products to other plants or manufactures dairy products on its premises.

64 Fed. Reg. 16131-16132 (1999)

We propose to adopt as 1051.8, the existing uniform definition for a nonpool plant in Part 1000:

1051.8 Nonpool plant.

Nonpool plant means any milk receiving, manufacturing, or processing plant other than a pool plant. The following categories of nonpool plants are further defined as follows:

- (a) A plant fully regulated under another Federal order means a plant that is fully subject to the pricing and pooling provisions of another Federal order.
- (b) Producer-handler plant means a plant operated by a producer-handler as defined under any Federal order.
- (c) Partially regulated distributing plant means a nonpool plant that is not a plant fully regulated under another Federal order, a producer-handler plant, or an exempt plant, from which there is route disposition in the marketing area during the month.
- (d) Unregulated supply plant means a supply plant that does not qualify as a pool supply plant and is not a plant fully regulated under another Federal order, a producer-handler plant, or an exempt plant.
- (e) An exempt plant means a plant described in this paragraph that is exempt from the pricing and pooling provisions of any order provided that the operator of the plant files reports as prescribed by the market administrator of any marketing area in which the plant distributes packaged fluid milk products to enable determination of the handler's exempt status:
 - (1) A plant that is operated by a governmental agency that has no route disposition in commercial channels;
 - (2) A plant that is operated by a duly accredited college or university disposing of fluid milk products only through the operation of its own facilities with no route disposition in commercial channels;

(3) A plant from which the total route disposition is for individuals or institutions for charitable purposes without remuneration; or

(4) A plant that has route disposition and packaged sales of fluid milk products to other plants of 150,000 pounds or less during the month.

The nonpool plant provision describes plants that receive, process or package milk, but that don't meet the standards for being a pool plant. Examples of nonpool plants include:

- (1) Plants fully regulated under another Federal order
- (2) A producer-handler plant
- (3) A partially regulated distributing plant
- (4) A governmental agency plant
- (5) An unregulated supply plant, and
- (6) The four categories of exempt plants.

The reform decision speaks directly to the definition of what constitutes a nonpool plant:

A definition is provided in all orders describing plants which receive, process or package milk, but which do not satisfy the standards for being a pool plant. While providing for such a definition may appear redundant, this provision is useful to more clearly define the extent of regulation applicable to plants. Nonpool plants should include a plant that is fully regulated under another Federal order commonly referred to as an other order plant; a producer-handler plant, a partially regulated distributing plant that is a plant that does not qualify as a pool distributing plant, an other order plant, a producer-handler plant or a governmental agency plant; an unregulated supply plant, and an exempt plant. The definitions for these nonpool plants are not materially different than those provided in the current orders with the possible exception of an "exempt plant."

Certain plants are exempt from regulation under Federal milk orders. These plants fall into 4 categories: (1) plants that are operated by a governmental agency which have no route disposition in commercial channels; (2) plants operated by a college or university that dispose of fluid milk products only through their own facilities with no route disposition in commercial channels; (3) plants from which the total route disposition is for individuals or institutions for charitable purposes without remuneration; and (4) plants that have route disposition of 150,000 pounds or less during the month. These types of plants have little impact on the regulated market and need not be

regulated to ensure the integrity of the regulatory plan. Many current Federal orders also provide regulatory exemption for a plant operated by a state or Federal governmental agency. For example, some states have dairy farm and plant operations that provide milk for their prison populations. As provided herein, regulatory exemption would be continued under the consolidated orders unless pool plant status is requested.

Regulatory exemption also should apply to colleges, universities, and charitable institutions because these institutions generally handle fluid milk products internally and have no impact in the mainstream commercial market. However, in the event that these entities distribute fluid milk through commercial channels, route sales by such entities, including government agencies, will be monitored to determine if Federal regulation should apply. The determination and verification of exempt plant status will, from time to time, necessitate the need for the market administrator to require reports and information deemed appropriate for the sole purpose of making this determination. Such authority is currently provided in orders and should continue.

64 Fed. Reg. 16134-16135 (1999)

We propose to adopt as 1051.9, the existing uniform definition for a handler in Part 1000:

1051.9 Handler.

Handler means:

- (a) Any person who operates a pool plant or a nonpool plant.
- (b) Any person who receives packaged fluid milk products from a plant for resale and distribution to retail or wholesale outlets, any person who as a broker negotiates a purchase or sale of fluid milk products or fluid cream products from or to any pool or nonpool plant, and any person who by purchase or direction causes milk of producers to be picked up at the farm and/or moved to a plant. Persons who qualify as handlers only under this paragraph under any Federal milk order are not subject to the payment provisions of Sections _____.70, _____.71, _____.72, _____.73, _____.76, and _____.85 of that order.
- (c) Any cooperative association with respect to milk that it receives for its account from the farm of a producer and delivers to pool plants or diverts to nonpool plants pursuant to Section _____.13 of the order. The operator of a pool plant receiving milk from a cooperative association may be the handler for such milk if both

parties notify the market administrator of this agreement prior to the time that the milk is delivered to the pool plant and the plant operator purchases the milk on the basis of farm bulk tank weights and samples.

At its most basic level, federal orders define handlers to include persons who buy milk from dairy farmers. In addition, other entities may be regulated as handlers for reporting and accountability purposes under the order. Such handlers have the financial responsibility to pay dairy farmers for their milk and to file the reports of milk receipts and utilization to the market administrator. We are recommending the uniform definition of a handler.

The reform decision speaks directly to the definition of a handler:

Federal milk orders regulate those persons who buy milk from dairy farmers. Such persons are called handlers under the order. These persons have a financial responsibility for payments to dairy farmers for milk in accordance with its classified use. They must file reports with the market administrator detailing their receipts and utilization of milk.

The handler definition adopted for the consolidated orders includes the operator of a pool plant, a cooperative association that diverts milk to nonpool plants or delivers milk to pool plants for its account, and the operator of a "nonpool plant," which would encompass a producer-handler, a partially regulated distributing plant, a plant fully regulated under another Federal order, an unregulated supply plant, and an exempt plant.

In addition, "third party" organizations that are not otherwise regulated under provisions of an order are included in the handler definition. This category includes any person who engages in the business of receiving milk from any plant for resale and distribution to wholesale and retail outlets, brokers or others who negotiate the purchase or sale of fluid milk products or fluid cream products from or to any plant, and persons who, by purchase or direction, cause the milk of producers to be picked up at the farm and/or moved to a plant. Such intermediaries provide a service to the dairy industry. These persons are not, however, recognized or regulated as entities required to make minimum payments to producers. The expanded marketing chain brought about by such intermediaries has made it increasingly difficult for the market administrator to track the movement of milk from farms to

consumers. The revised handler definition enables the market administrator to more readily identify those entities.

64 Fed. Reg. at 16135 (1999)

All federal orders need to have provisions for milk that is not priced and pooled under that order. This milk, commonly referred to as other source milk, needs to be classified at the receiving handler's plant.

We propose to adopt as 1051.14, the existing uniform definition for other source milk in Part 1000:

1051.14 Other source milk.

Other source milk means all skim milk and butterfat contained in or represented by:

(a) Receipts of fluid milk products and bulk fluid cream products from any source other than producers, handlers described in Sections 1000.9(c) and 1135.11, or pool plants;

(b) Products (other than fluid milk products, fluid cream products, and products produced at the plant during the same month) from any source which are reprocessed, converted into, or combined with another product in the plant during the month; and

(c) Receipts of any milk product (other than a fluid milk product or a fluid cream product) for which the handler fails to establish a disposition.

We propose to adopt as 1051.15, the existing uniform definition for a fluid milk product in Part 1000:

1051.15 Fluid milk product.

(a) Except as provided in paragraph (b) of this section, fluid milk product shall mean any milk products in fluid or frozen form that are intended to be used as beverages containing less than 9 percent butterfat and 6.5 percent or more nonfat solids or 2.25 percent or more true milk protein. Sources of such nonfat solids/protein include but are not limited to: Casein, whey protein concentrate, milk protein concentrate, dry whey, caseinates, lactose, and any similar dairy derived ingredient. Such products include, but are not limited to: Milk, fat-free milk, lowfat milk, light milk, reduced

fat milk, milk drinks, eggnog and cultured buttermilk, including any such beverage products that are flavored, cultured, modified with added or reduced nonfat solids, sterilized, concentrated, or reconstituted. As used in this part, the term concentrated milk means milk that contains not less than 25.5 percent, and not more than 50 percent, total milk solids.

(b) The term fluid milk product shall not include:

(1) Any product that contains less than 6.5 percent nonfat milk solids and contains less than 2.25 percent true milk protein; whey; plain or sweetened evaporated milk/skim milk; sweetened condensed milk/skim milk; yogurt containing beverages with 20 or more percent yogurt by weight and kefir; products especially prepared for infant feeding or dietary use (meal replacement) that are packaged in hermetically sealed containers; and products that meet the compositional standards specified in paragraph (a) of this section but contain no fluid milk products included in paragraph (a) of this section.

(2) The quantity of skim milk equivalent in any modified product specified in paragraph (a) of this section that is greater than an equal volume of an unmodified product of the same nature and butterfat content.

We propose to adopt as 1051.16, the existing uniform definition for a fluid cream product in Part 1000:

1051.16 Fluid cream product.

Fluid cream product means cream (other than plastic cream or frozen cream), including sterilized cream, or a mixture of cream and milk or skim milk containing 9 percent or more butterfat, with or without the addition of other ingredients.

This definition was the same for all federal orders before order reform:

The current definition is uniform under all the orders and should be used in the newly merged orders. There were no comments supporting a change in this provision.

64 Fed. Reg. at 16122 (1999)

We propose to adopt as 1051.18, the existing uniform definition for a cooperative association in Part 1000:

1051.18 Cooperative association.

Cooperative association means any cooperative marketing association of producers which the Secretary determines is qualified under the provisions of the Capper-Volstead Act, has full authority in the sale of milk of its members, and is engaged in marketing milk or milk products for its members. A federation of 2 or more cooperatives incorporated under the laws of any state will be considered a cooperative association under any Federal milk order if all member cooperatives meet the requirements of this section.

The reform decision identified the benefits of a uniform provision relating to cooperative associations:

All current orders provide a definition for dairy farmer cooperative associations that market milk on behalf of their dairy farmer members. Providing for a uniform definition of a cooperative association facilitates the administration of the various order provisions as they apply to such producer organizations and recognizes the unique standing granted to dairy farmer cooperatives under the Capper-Volstead Act. Dairy farmer cooperatives are responsible for marketing the majority of the milk supplied to regulated handlers under the Federal order system.

As provided herein, a cooperative association means any cooperative marketing association of producers which the Secretary determines, after application for such recognition by the cooperative, is qualified as such under the provisions of the Act of Congress of February 18, 1922, as amended, known as the "Capper-Volstead Act." Additionally, the new orders continue to require that a cooperative association have full authority in the sale of the milk of its members and that it be engaged in making collective sales or marketings of milk or milk products for its dairy farmer members.

Several current orders provide a definition for a federation of 2 or more cooperative associations. As adopted here, all consolidated orders recognize a federation of cooperatives as satisfying the cooperative definition for the purposes of determining milk payments and pooling. Individual cooperatives of a federation of cooperatives must also meet the criteria as set forth for individual cooperative associations and their federations as incorporated under state laws.

We propose to adopt as 1051.19, the existing uniform definition for a commercial food processing establishment in Part 1000:

1051.19 Commercial food processing establishment.

Commercial food processing establishment means any facility, other than a milk plant, to which fluid milk products and fluid cream products are disposed of, or producer milk is diverted, that uses such receipts as ingredients in food products and has no other disposition of fluid milk products other than those received in consumer-type packages (1 gallon or less.) Producer milk diverted to commercial food processing establishments shall be subject to the same provisions relating to diversions to plants, including, but not limited to, Sections _____.13 and _____.52 of each Federal milk order.

This definition identifies the use of fluid milk products, fluid cream products or producer milk as ingredients at commercial food processing establishments. The reform decision offers further explanation about the need for this provision:

Packaged fluid milk products should be permitted to be transferred to a CFPE in any size, only those products that are shipped in larger-than-consumer-sized packages (i.e., larger than one gallon) should be eligible for a Class II classification. If milk is received by a CFPE in gallon containers or smaller, the milk should be priced as Class I milk since there is no way of guaranteeing that such products will not be sold for fluid use.

64 Fed. Reg. at 16123 (1999)

These two restrictions are based upon practical considerations. The integrity of the classified pricing system would be much more difficult to maintain if the market administrator were forced to audit every CFPE on a regular basis. By prohibiting the sale of fluid milk products in consumer-sized packages to a CFPE for anything but Class I use, there would be less need to regularly audit CFPEs to be sure that such products are not being sold to the public. Similarly, since packaged fluid milk products in containers larger than one gallon are rarely, if ever, found in retail outlets, it is unlikely that such products will be sold for fluid use. By restricting fluid milk product disposition by CFPEs to packaged products not larger than one gallon in size, there is reasonable assurance that milk priced as Class II will not be disposed of as fluid milk sold by the glass from a bulk dispenser.

Other Administrative Provisions from Part 1000

The provisions 1000.25 thru 1000.28 include the language necessary to authorize and direct the market administrator to operate and administer the pool; these provisions identify how to make the pool work and hold handlers accountable to the pool.

- We propose to adopt as 1051.25, the existing uniform definition for the market administrator, in Part 1000.
- We propose to adopt as 1051.26, the existing uniform definition for continuity and separability of provisions, in Part 1000.
- We propose to adopt as 1051.27, the existing uniform definition for handler responsibility for records and facilities, in Part 1000.
- We propose to adopt as 1051.28, the existing uniform definition for the Termination of obligations, in Part 1000.

The specific language contained in these four provisions is included in Cooperatives' Exhibit 3.A. *in Exhibit 35.*

We also propose to adopt as the existing uniform provisions from Part 1000 for:

Adjustment of accounts – Section 1051.77.

Charges on overdue accounts – Section 1051.78.

Assessment for order administration – Section 1051.85.

Deductions for marketing services – Section 1051.86.

Without repeating it, we support and adopt the testimony given by Mr. Mykrantz explaining the function and operation of these provisions.

**Multiple Component Pricing in the California Federal Milk Marketing Order:
Handler Value of Milk; Producer component prices; and announcements of prices
(Sections 1051.60, .61, .62);**

We propose a multiple component pricing (MCP) program based on three components – butterfat, protein and other solids. Multiple component pricing will be applicable both to handlers and producers, following the predominant FMMO model which prices components to handlers of Class I (fat and skim); Classes II and IV (fat and solids-not-fat); handlers of Class III (fat, protein, and other solids) and to producers (fat, protein, and other solids) on all milk. In discussing multiple component pricing, USDA, in the federal order reform decision, spoke to the national basis of this pricing approach:

This pricing system eliminates the need for regional yields based on regional differences in milk composition. The value of milk will be adjusted automatically based on the level of components contained in the milk in each order even though the component prices are the same nationally. This automatic adjustment means that handlers will pay the same price per pound of component but may have differing per hundredweight values based on the milk component levels, creating equity in the minimum cost of milk used for manufacturing purposes.

64 Fed. Reg. at 16100 (1999)

Fortification of milk for Class I uses to meet the California fluid milk standards will be accommodated through a fortification allowance to Class I handlers. The CDFA's fortification allowances are incorporated into the Class I pricing provisions.

We propose the following language for section 1051.60 Handler's value of milk:

1051.60 Handler's value of milk.

For the purpose of computing a handler's obligation for producer milk, the market administrator shall determine for each month the value of milk of each handler with respect to each of the handler's pool plants and of each handler described in Section 1000.9(c) with respect to milk that was not received at a pool plant by adding the amounts computed in paragraphs (a) through (i) of this section and subtracting from that total amount the values computed in

paragraphs (i) and (j) of this section. Unless otherwise specified, the skim milk, butterfat, and the combined pounds of skim milk and butterfat referred to in this section shall result from the steps set forth in Section 1000.44(a), (b), and (c), respectively, and the nonfat components of producer milk in each class shall be based upon the proportion of such components in producer skim milk. Receipts of nonfluid milk products that are distributed as labeled reconstituted milk for which payments are made to the producer-settlement fund of another Federal order under Sections 1000.76(a)(4) or (d) shall be excluded from pricing under this section.

(a) Class I value.

(1) Multiply the pounds of skim milk in Class I by the Class I skim milk price; and

(2) Add an amount obtained by multiplying the pounds of butterfat in Class I by the Class I butterfat price;

(3) Deduct for each pound of milk solids-not-fat in nonfat dry milk used for fortifying Class I products during the current month a maximum charge equal to the current Class I solids not fat price [the Class I skim milk price in the \$2.10 zone divided by 9], less the current Class IV solids not fat price established in ~~1050.53~~ *Section 1051.53*. In no case shall the deduction be less than zero cents (\$0.00) nor more than nineteen and eighty-five hundredths cents (\$.1985); and

(4) Deduct for each pound of milk solids-not-fat in condensed skim milk used for fortifying Class I products during the current month a maximum charge equal to the current Class I solids not fat price [the Class I skim milk price in the \$2.10 zone divided by 9], less the current Class II solids not fat price established in Section 1051.53. In no case shall the deduction be less than zero cents (\$0.00) nor more than nine and eighty-seven hundredths cents (\$.0987).

(b) Class II value.

(1) Multiply the pounds of nonfat solids in Class II skim milk by the Class II nonfat solids price; and

(2) Add an amount obtained by multiplying the pounds of butterfat in Class II times the Class II butterfat price.

(c) Class III value.

(1) Multiply the pounds of protein in Class III skim milk by the protein price;

(2) Add an amount obtained by multiplying the pounds of other solids in Class III skim milk by the other solids price; and

(3) Add an amount obtained by multiplying the pounds of butterfat in Class III by the butterfat price.

(d) Class IV value.

(1) Multiply the pounds of nonfat solids in Class IV skim milk by the nonfat solids price; and

(2) Add an amount obtained by multiplying the pounds of butterfat in Class IV by the butterfat price.

(e) Multiply the pounds of skim milk and butterfat overage assigned to each class pursuant to Section 1000.44(a)(11) and the corresponding step of Section 1000.44(b) by the skim milk prices and butterfat prices applicable to each class.

(f) Multiply the difference between the current month's Class I, II, or III price, as the case may be, and the Class IV price for the preceding month and by the hundredweight of skim milk and butterfat subtracted from Class I, II, or III, respectively, pursuant to Section 1000.44(a)(7) and the corresponding step of Section 1000.44(b).

(g) Multiply the difference between the Class I price applicable at the location of the pool plant and the Class IV price by the hundredweight of skim milk and butterfat assigned to Class I pursuant to Section 1000.43(d) and the hundredweight of skim milk and butterfat subtracted from Class I pursuant to Sections 1000.44(a)(3)(i) through (vi) and the corresponding step of Section 1000.44(b), excluding receipts of bulk fluid cream products from plants regulated under other Federal orders and bulk concentrated fluid milk products from pool plants, plants regulated under other Federal orders, and unregulated supply plants.

(h) Multiply the difference between the Class I price applicable at the location of the nearest unregulated supply plants from which an equivalent volume was received and the Class III price by the pounds of skim milk and butterfat in receipts of concentrated fluid milk products assigned to Class I pursuant to Sections 1000.43(d) and 1000.44(a)(3)(i) and the corresponding step of Section 1000.44(b) and the pounds of skim milk and butterfat subtracted from Class I pursuant to Section 1000.44(a)(8) and the corresponding step of Section 1000.44(b), excluding such skim milk and butterfat in receipts of fluid milk products from an unregulated supply plant to the extent that an equivalent amount of skim milk or butterfat disposed of to such plant by handlers fully regulated under any Federal milk order is classified and priced as Class I milk and is not used as an offset for any other payment obligation under any order.

(i) For reconstituted milk made from receipts of nonfluid milk products, multiply \$1.00 (but not more than the difference between the Class I price applicable at the location of the pool plant and the Class IV price) by the hundredweight of skim milk and butterfat contained in receipts of nonfluid milk products that are allocated to Class I use pursuant to Section 1000.43(d).

(j) Compute the amount of credits applicable pursuant to Section 1051.55.

Producers will be paid twice per month based on MCP calculations. They will be paid for pounds of butterfat, protein and other solids. All producers in the FMMO will receive the same component prices. There will be no somatic cell count adjustments included in the regulated prices. There will be no producer location differentials.

The reform decision identified the source of the component prices:

The butterfat, protein, and other solids prices are component prices based on the value of the use of milk in manufacturing.

64 Fed. Reg. at 16095 (1999)

USDA defined a producer price differential in the reform decision:

The producer price differential reflects the collective value of participation in the marketwide pool. Primarily, it represents the producer's pro rata share of the additional value of Class I and Class II use in the market.

64 Fed. Reg. at 16095 (1999)

In the California Order, we propose that there be no producer price differential (PPD) value, as such, paid to producers. Instead, the funds generated from the PPD value computation will be paid across all three components in a ratio representative of their value in the pool. More specifically, the market administrator will calculate the contribution of each component (butterfat, protein and other solids) to the value of the class III components to producers on an annual basis. The higher the PPD, the larger the adjustment to each component; the larger the

component's contribution to the value of the class III components to producers, the larger the share of the PPD adjustment. A negative PPD would reduce the component prices, and accordingly, the larger the component's contribution to the value of the class III components to producers, the larger the reduction to the component's price.

We are proposing to eliminate a PPD because our experience has been that producers in FMMOs find the concept of PPDs confusing, and the PPD concept adds an unnecessary level of complication to the understanding of FMMO pricing. More specifically, negative PPDs that can occur when increases in commodity prices lead to class price inversions are even more difficult to explain to producers. Additionally, since the existing state order doesn't include a PPD, we believe that eliminating a PPD will give us one less pricing complexity to explain.

The Exhibit, "1051.61 Computation of Producer Component Prices and Producer Price Differential" contains an example of the calculation of component values that have been adjusted for the PPD value. The example is based on the actual values that were reported for the month of December 2013 and reported by the Market Administrator of the Upper Midwest Marketing Area, Federal Order No. 30.

The example goes through the adjustment of the component values by the PPD reported for December 2013. The contribution of each component to the value of the Class III components to producers would be calculated by the CA FMMO market administrator; in the case of this example, those contributions are expressed as percentages and are provided to enable us to display the calculation method.

We propose the following language for section 1051.61 Computation of producer component prices and producer price differential:

1051.61 Computation of producer component prices and producer price differential.

For each month the market administrator shall compute producer component prices per pound for butterfat, protein, and other solids. The report of any handler who has not made payments required pursuant to Section 1051.71 for the preceding month shall not be included in the computation of the producer component prices, and such handler's report shall not be included in the computation for succeeding months until the handler has made full payment of outstanding monthly obligations. Subject to the conditions of this paragraph, the market administrator shall compute the producer component prices in the following manner:

1051.60 (a) Combine into one total the values computed pursuant to Section ~~1050.60~~ for all handlers required to file reports prescribed in Section ~~1051.50;~~ 1051.30;

(a.1) Subtract the value of quota premium for the month as reported to the Market Administrator by CDFA;

(b) Subtract the total values obtained by multiplying each handler's total pounds of protein, other solids, and butterfat contained in the milk for which an obligation was computed pursuant to Section 1051.60 by the protein price, other solids price, and the butterfat price, respectively;

(c) Add an amount equal to not less than one-half of the unobligated balance in the producer-settlement fund;

(d) Divide the resulting amount by the sum of the following for all handlers included in these computations:

- (1) The total hundredweight of producer milk; and
- (2) The total hundredweight for which a value is computed pursuant to Section 1051.60(g); and,

(e) Subtract not less than 4 cents nor more than 5 cents from the price computed pursuant to paragraph (e) of this section. The result shall be known as the producer price differential for the month (applicable in Section 1000.76(a)(2)).

(f) The producer butterfat protein, and other solids, prices shall be the result of the following computations.

- (1) The percentage contribution that the value of butterfat, protein, and other solids make to the value of the Class III components to producers shall be computed and announced by the Market Administrator on or before January 1 of the year for which the percentages will be applicable. The percentages will be computed

as an average based on the prior fiscal year of December 1st through November 30th.

(2) The producer butterfat price shall be the result of adding the price computed in Section 1000.50(l) to the result of multiplying the percentage butterfat contribution announced in paragraph (f)(1) by the producer price differential value and dividing the result by the handler's total pounds of butterfat contained in the milk for which an obligation was computed pursuant to Section ~~1050.60~~, ^{1051.60} and rounded to the fourth decimal place.

(3) The producer protein price shall be the result of adding the price computed in Section 1000.50(n) to the result of multiplying the percentage protein contribution announced in paragraph (f)(1) by the producer price differential value and dividing the result by the handler's total pounds of protein contained in the milk for which an obligation was computed pursuant to Section 1051.60, and rounded to the fourth decimal place.

(4) The producer other solids price shall be the result of adding the price computed in Section 1000.50(o) to the result of multiplying the percentage other solids contribution announced in paragraph (f)(1) by the producer price differential value and dividing the result by the handler's total pounds of other solids contained in the milk for which an obligation was computed pursuant to Section 1051.60, and rounded to the fourth decimal place.

We propose the following language for section 1051.62 Announcement of producer

prices:

1051.62 Announcement of producer prices.

On or before the **14th day** after the end of each month, the market administrator shall announce publicly the following prices and information:

- (a) The producer protein price;
 - (a.1) The quota premium for nonfat solids;
- (b) The producer other solids price;
- (c) The producer butterfat price; and
- (d) The statistical uniform price for non-quota milk containing 3.5 percent butterfat, shall be the sum of the producer protein price multiplied by 2.9915, the producer other solids price multiplied by 5.6935, and the producer butterfat price multiplied by 3.5.

Conclusion

Proposal one includes the uniform provisions as presented in my testimony and also presented by several USDA witnesses. Additionally we are proposing the incorporation of the CA allowance for fortification of fluid milk products and a minor modification in the PPD as I described. I will now answer any questions.