

Federal Milk Order Overview

North Dakota Legislature
Interim Agriculture Committee
Bismarck, North Dakota
April 15, 2014

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Introductions

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What is a Federal Milk Order?

- Regulation issued by U.S. Secretary of Agriculture placing certain requirements on handling of Grade A milk in a region
- Legal authority provided in Agricultural Marketing Agreement Act of 1937 (as amended)
- Administered by a Market Administrator, appointed by Secretary of Agriculture

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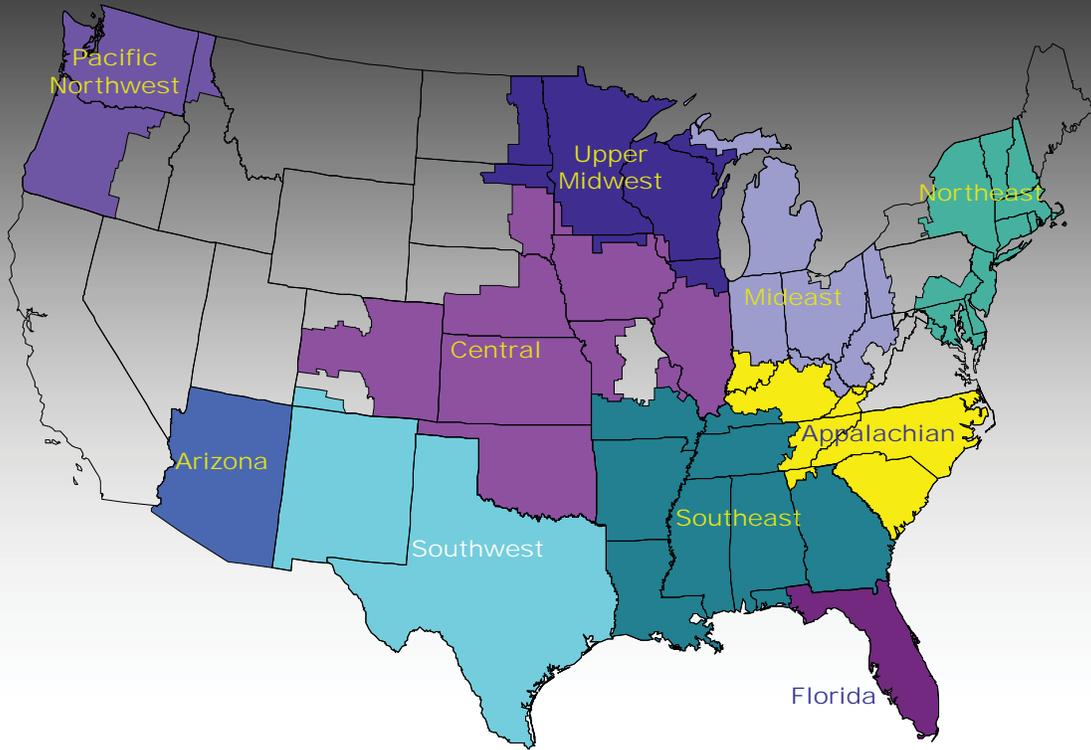
What is a Federal Milk Order?

(continued)

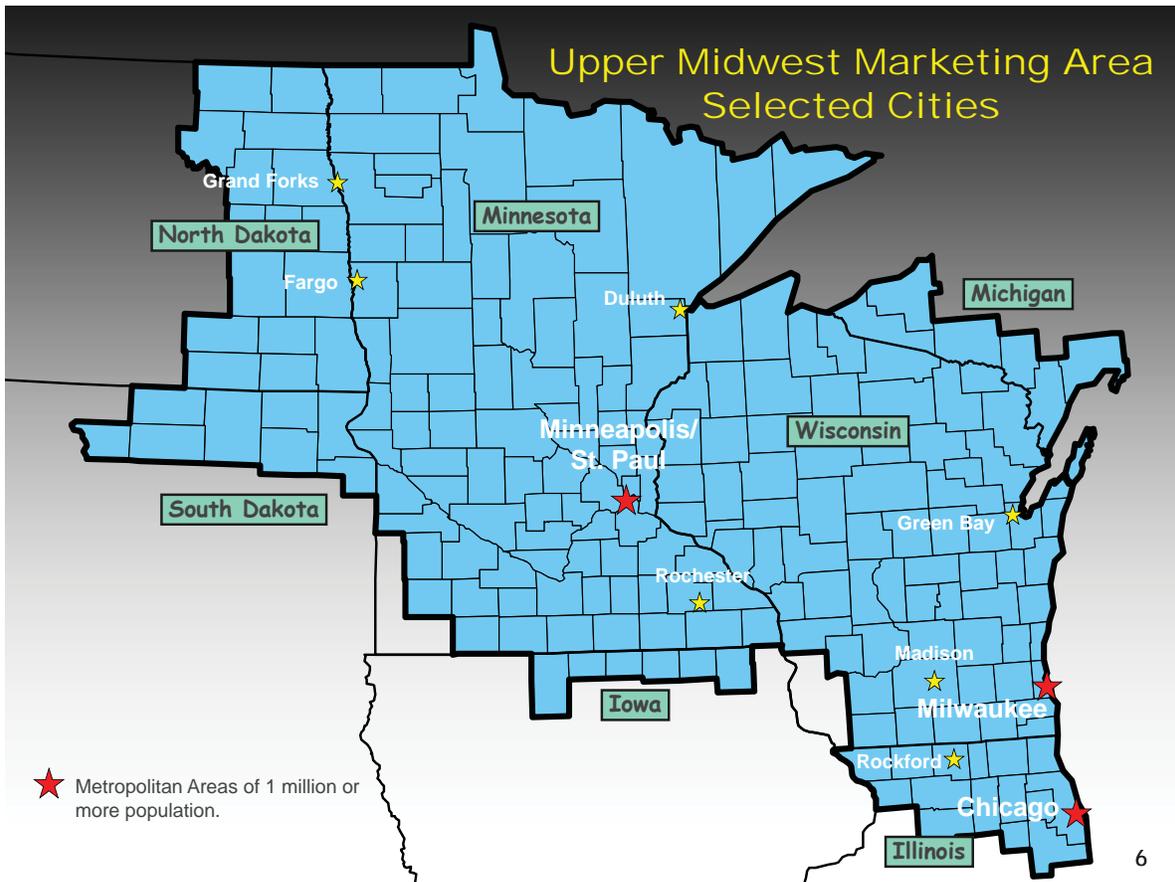
- Federal order put in place at request of local dairy farmers and their coops
 - Industry/government partnership
- Continuation subject to periodic referendums (most recent Feb. 2013)
- Funded by dairy industry (handlers). No tax dollars involved

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Federal Milk Marketing Order Areas



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“Top 10” Federal Order Benefits

- **Classified Pricing:**
 - Allow coops and other handlers to charge more for milk going into the bottle (or for other higher-valued uses) than for milk used for other purposes
- **Pooling:**
 - Allow a farmer who only delivers to a cheese plant to receive a pro-rata share of the higher-valued Class I sales (through PPD)
- **Auditing:**
 - Ensure accuracy and honesty of reports of milk sales and payments to dairy farmers. Third-party verification.

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“Top 10” Federal Order Benefits

(continued)

- **Minimum prices for producers and for milk sales from dairy coops:**
 - Set minimum prices that must be paid to producers (exemption for coop payments to member/owners) and for sales from dairy coops to other handlers
- **Over-order pricing:**
 - Provide milk pricing and classification structure so that coops may set prices for milk sales over and above Federal order prices
- **Payment dates:**
 - Orders provide required payment dates for payments to producers and for payments to dairy coops
- **Marketing Service:**
 - Verify milk tests (bf, protein, other solids, SCC). This is the only oversight of milk testing in most areas

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“Top 10” Federal Order Benefits

(continued)

- **Market Information:**
 - Provide regional and national dairy statistics, including price announcements, research papers, public presentations, and monthly newsletter
- **Voluntary:**
 - Federal orders are provided at the request of dairy farmers and their coops. An industry/government partnership. Changes to orders are usually initiated by the coops. Every producer vote provides an opportunity to remove an Order if it is not providing value to the industry.
- **Industry funded, no tax dollars used:**
 - In Upper Midwest, administrative assessment averages 3¢ per cwt. The PPD for producers averages 25¢-30¢ per cwt.

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Factors which Complicate Milk Marketing

- Produced every day
- Perishable
- Bulky and expensive to transport
- Seasonality of production
- Need for a reserve

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What a Federal Milk Order Does

- Provides classified pricing plan (value based on use). This generates revenue above the basic level.
- Provides blend prices (Producer Price Differential) to producers
- Provides for accurate weighing of milk

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What a Federal Milk Order Does

(continued)

- Provides for accurate testing of milk components
- Defines terms of trade between buyers/sellers
- Enforces minimum prices to farmers (producers) and their cooperatives
- Enforces timely payments
- Provides auditing function

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Federal Orders Do Not:

- Prevent payment of prices higher than the minimum
- Determine who milk is bought from
- Determine who milk is sold to
- Restrict new product development

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Federal Orders Do Not: (continued)

- Regulate trade practices at the “wholesale to retail” level, or at the retail level
- Regulate producers or control production
- Guarantee a market/buyer for a producer

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Federal Orders Do Not: (continued)

- Guarantee a minimum blend price level
- Prohibit milk from being marketed anywhere in the U.S.
- Prohibit movements of milk between orders
- Establish sanitary or quality standards

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Conditions Prior to Federal Orders

- Disorderly marketing. Milk strikes, price wars – violence sometimes involved
- Dairy farmers had very little bargaining power relative to processors
- Classified pricing plans, pioneered by coops, were collapsing
- Dairy farmers were often cut off by processors

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Conditions Prior to Federal Orders

(continued)

- Unfair trade practices were widespread, including:
 - Buying milk on inaccurate weights and tests
 - Paying surplus price while using the milk for fluid purposes

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Where Did Federal Milk Orders Come From?

- Federal milk orders were a result of disorderly marketing conditions for the dairy industry, especially for dairy farmers and their coops in the late 19th and early 20th century.

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Where Did Federal Milk Orders Come From? (continued)

- Long before Federal orders, industry (coops) in the Northeast tried to use a form of classified pricing to recoup the costs of:
 - Getting milk to the cities;
 - Seasonal changes in demand in the cities; and
 - Handling the balancing costs (seasonal and weekly).

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Where Did Classified Pricing Come From?

- 1880-1901 – Milk sold in Boston using classified pricing
- 1932 – 68 markets used classified pricing, mostly around cities in the East and Midwest
- 1937 – Federal orders authorized with classified pricing and pooling a central feature

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Important Concepts

- Classified Pricing
 - Handlers pay for milk based on how it is used (Class I, II, III, or IV)
- Pooling
 - Process by which total classified value of milk for the market is “pooled” allowing for a Producer Price Differential (PPD) to be determined. The PPD allows all dairy farmers in the market to share equally in the market utilization.

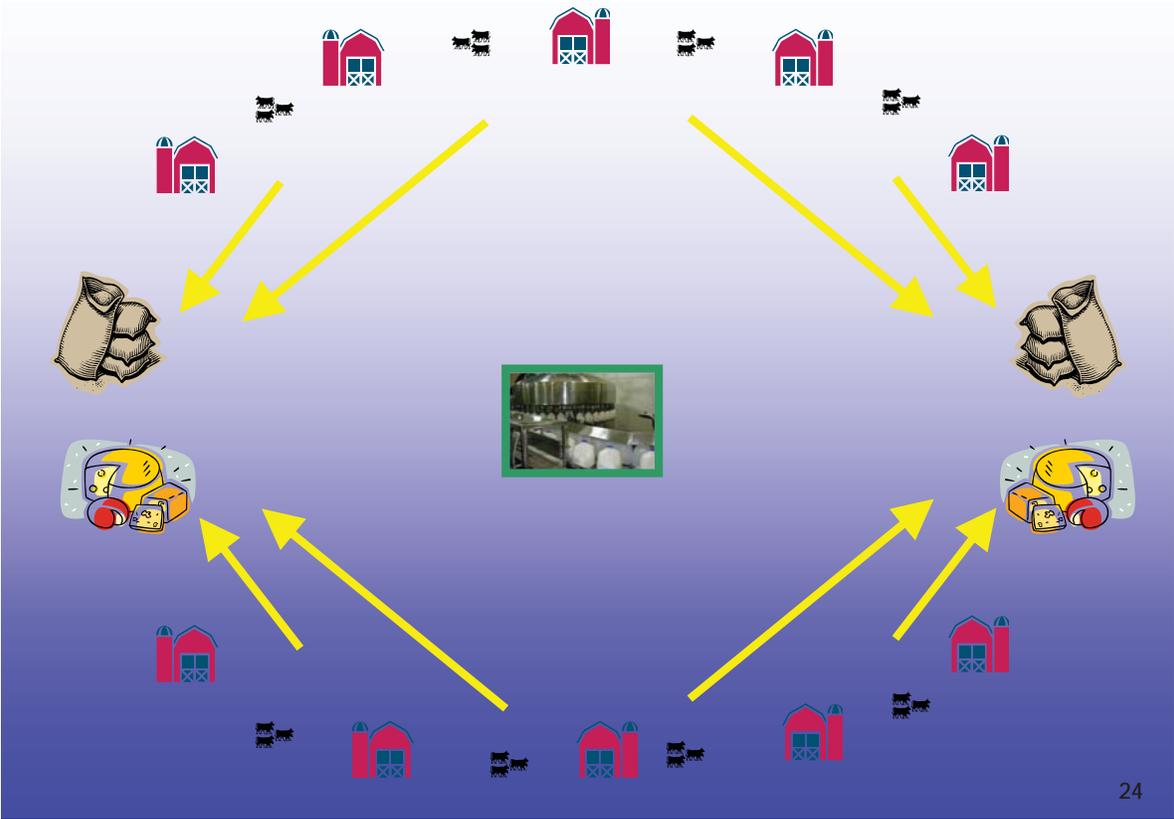
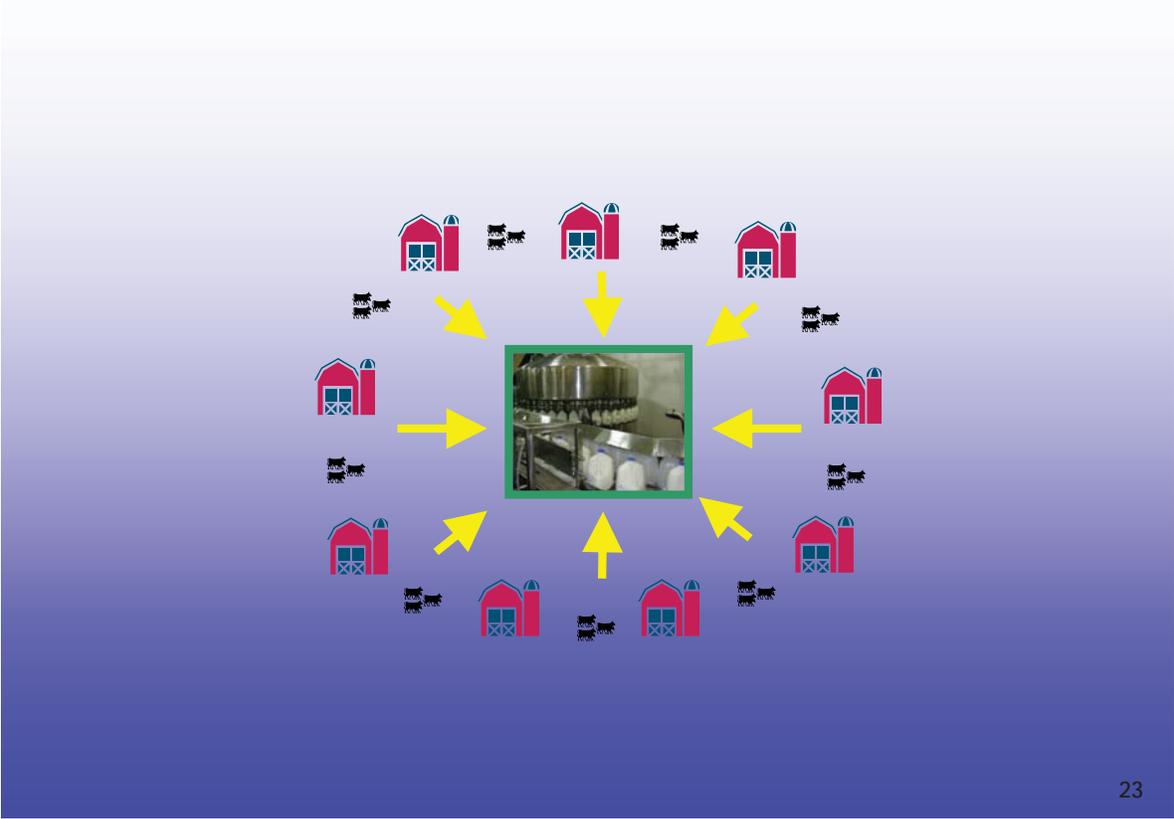
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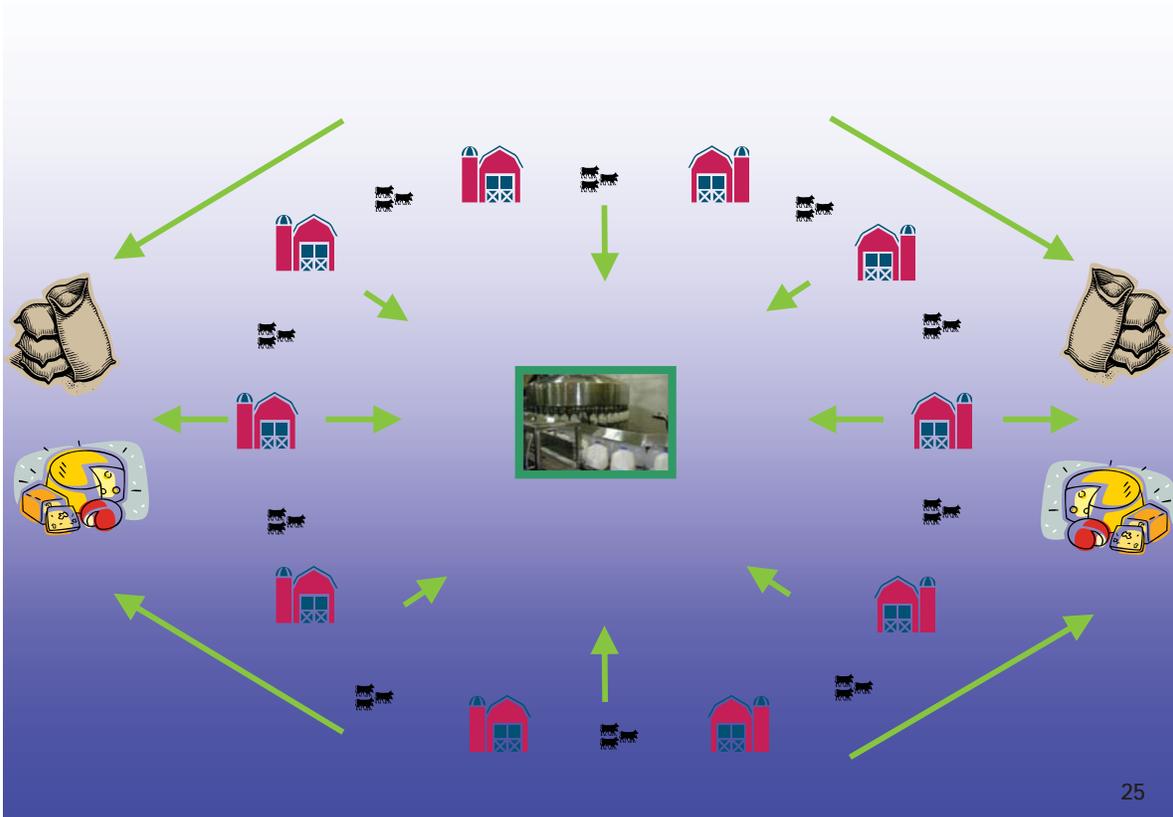


Why Was Classified Pricing Used?

- Milk has different value depending on how it's used
- Milk in the bottle (perishable, 88% water) worth more than milk used for storable products
- Higher costs to get bottled milk into cities

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Federal Orders in North Dakota

- Minnesota-North Dakota Federal Order implemented in November 1967
 - Included Fargo/Moorhead, Grand Forks and Thief River Falls areas, and surrounding milk sheds
 - Note: North Dakota Milk Marketing Board was also implemented in 1967

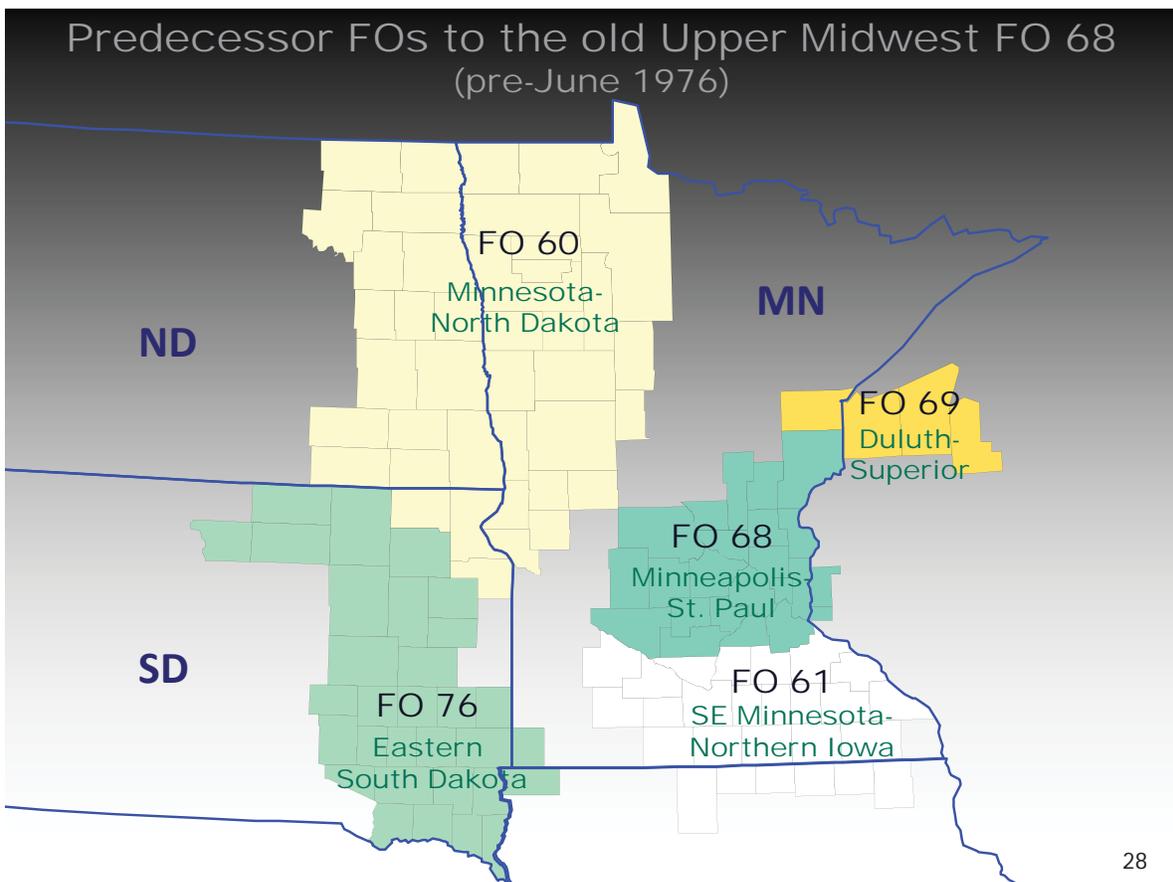


Federal Orders in North Dakota

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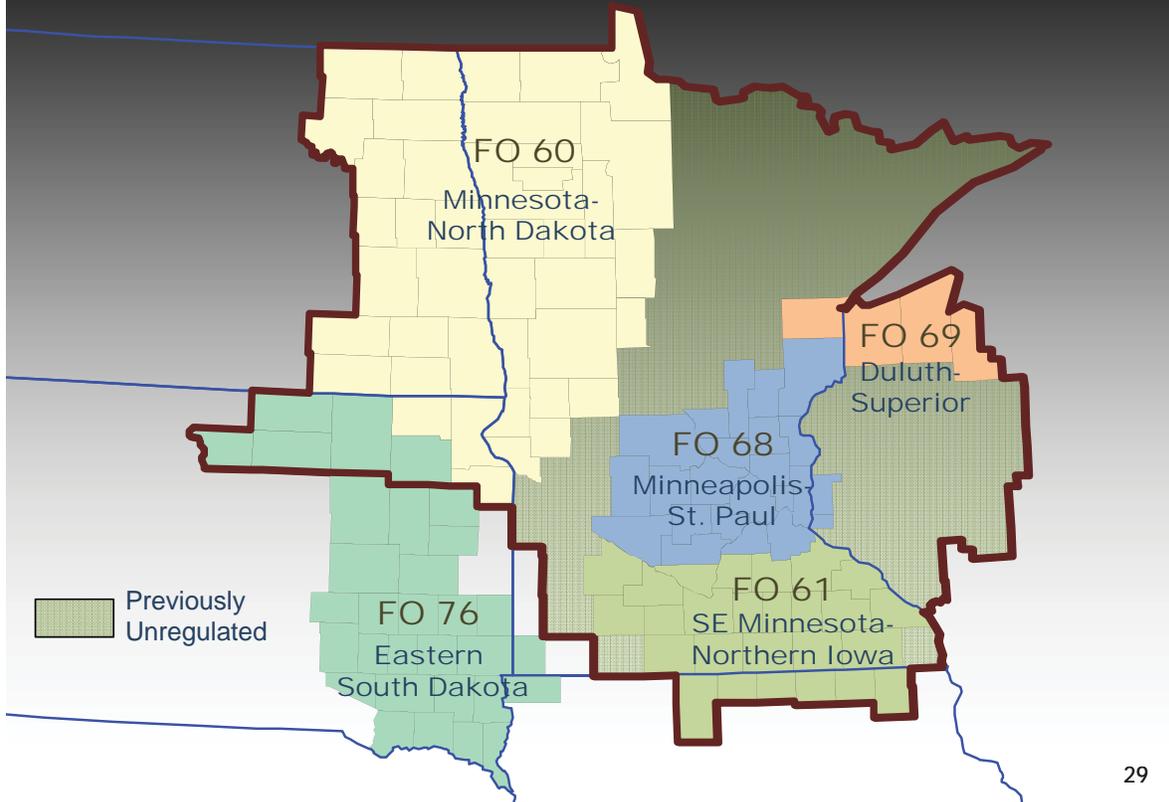
- Minnesota-North Dakota Federal Order merged with Minneapolis - St. Paul, Duluth - Superior and Southeastern Minnesota - Northern Iowa Orders in June 1976 to form Upper Midwest Federal Order
- Upper Midwest Federal Order merged with Chicago Regional Order in January 2000, name remained Upper Midwest Order.

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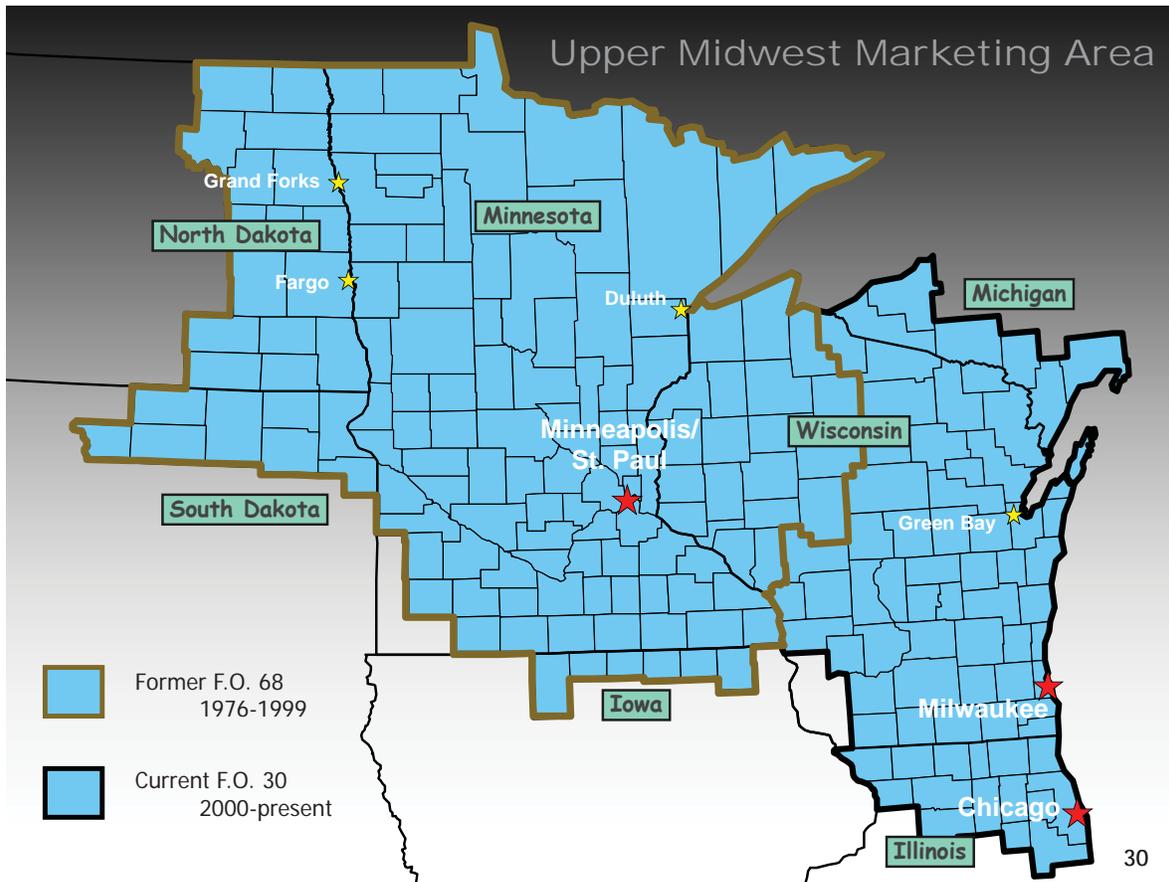


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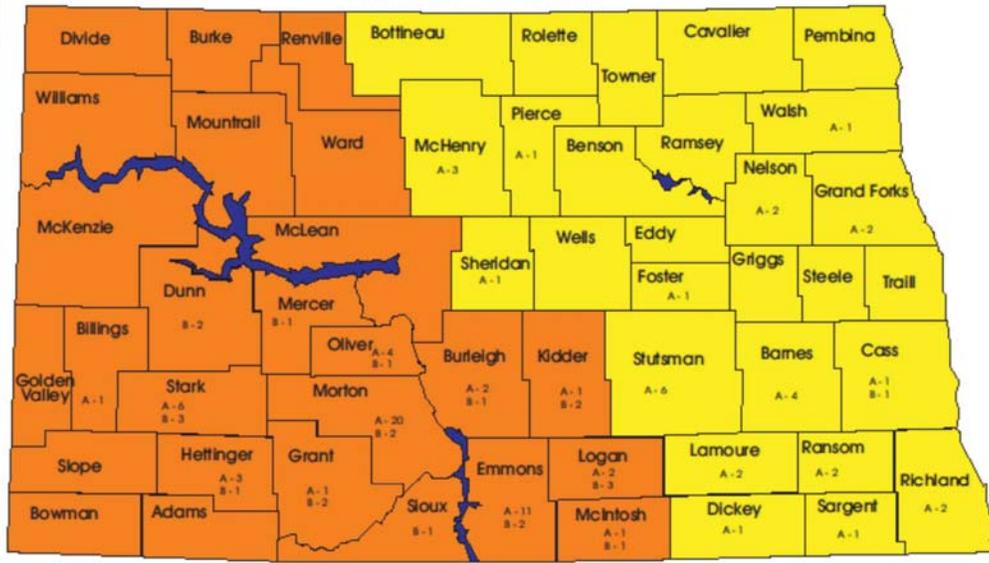
Upper Midwest Order, FO 68, as Merged June 1976



Upper Midwest Marketing Area



North Dakota Department of Agriculture Dairy Farms

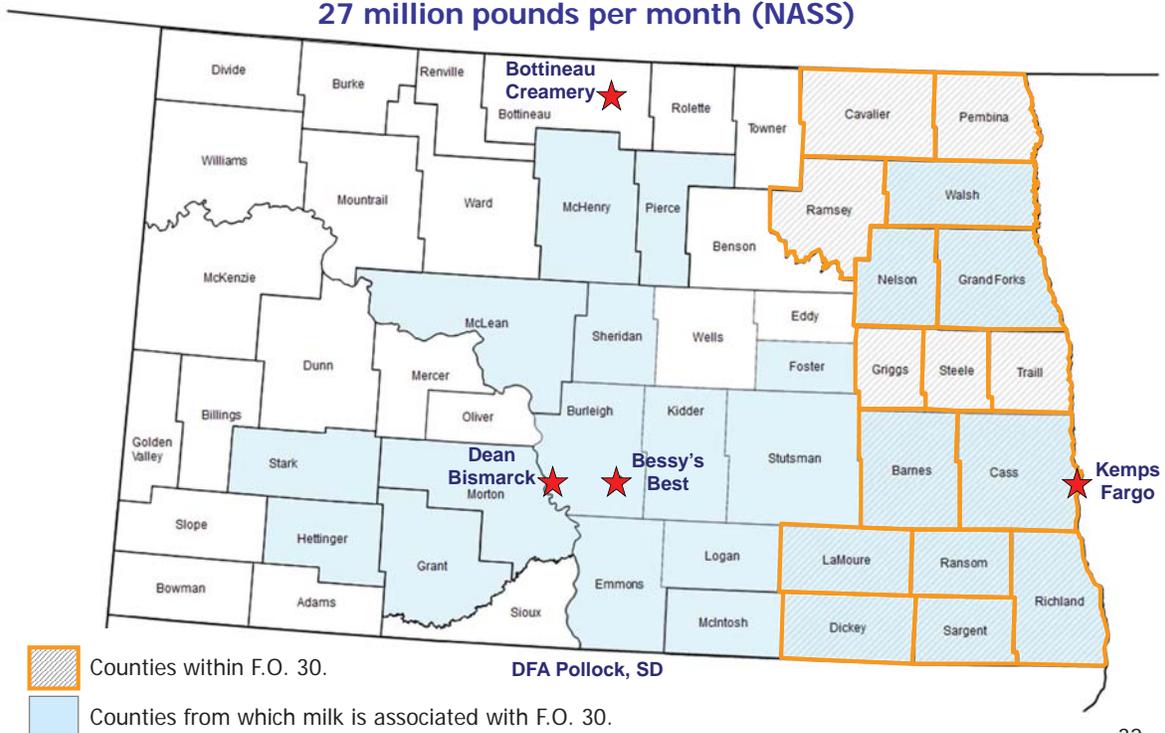


A Dairy Farms - 82
B Dairy Farms - 23

As of 3/12/2014

Plants & F.O. 30 Association

October - December 2013 ND Milk Production Averaged
27 million pounds per month (NASS)



 Counties within F.O. 30.

 Counties from which milk is associated with F.O. 30.



Exempt Plants



Section 1030.8 (e)

- Basically the exempt plants are bottling plants that distribute fluid milk products, but are allowed to be exempt from participating in the market pool (i.e. "nonpool" plants).
 - Government Agency, College or University Plants with no route disposition (Class I or fluid milk products) into commercial channels.
 - Bottling Plants with less than 150,000 pounds of route disposition per month.

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Producer-Handlers

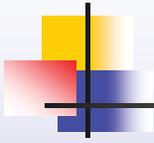


Section 1030.10

- Dairy producers who operate a farm in conjunction with a distributing plant operation from which there is route disposition (i.e. this farmer is allowed to bottle milk and still operate with nonpool plant status).
 - Basically all the milk receipts at this type of distributing plant is from his own farm production plus limited outside purchases of less than 150,000 pounds from fully regulated Federal order sources.
 - Producer-Handlers must provide reports and other records to the Market Administrator's office.



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Nonpool Plants



Section 1030.8

- Nonpool plants are those milk receiving, manufacturing, or processing plants other than pool plants.
 - Other Federal order plants
 - Producer-Handlers
 - Partially regulated distributing plants
 - Unregulated supply plants
 - Or exempt plants
 - **Example: DFA Pollock.**

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Distributing Plants



Section 1030.7 (a, b &/or e)

- Distributing plants bottle and distribute fluid milk or Class I milk in the Upper Midwest marketing area.
 - There are currently about 16 pool distributing plants on the Upper Midwest Market.
 - **Example: Kemps Fargo**



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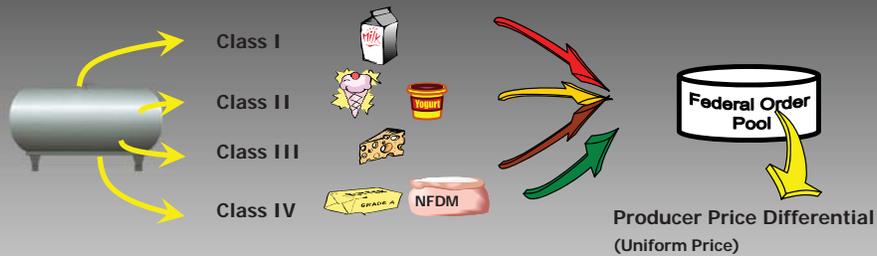
North Dakota Milk Production

Year	NASS ND Milk Production Million Pounds	Total FO 30 Pooled Milk Billion Pounds	ND Milk Pooled on FO 30 Million Pounds	ND % of FO 30
2004	465	17.3	169	1.0
2005	468	22.4	180	0.8
2006	470	26.9	206	0.8
2007	444	26.5	212	0.8
2008	418	28.0	212	0.8
2009	385	32.2	223	0.7
2010	384	33.8	269	0.8
2011	345	32.8	226	0.7
2012	347	30.7	187	0.6
2013	342	34.3	226	0.7

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Three Important Functions of a Federal Milk Order

1. Sharing the Higher-Valued Milk Utilization in the Market



2. Milk Testing Oversight

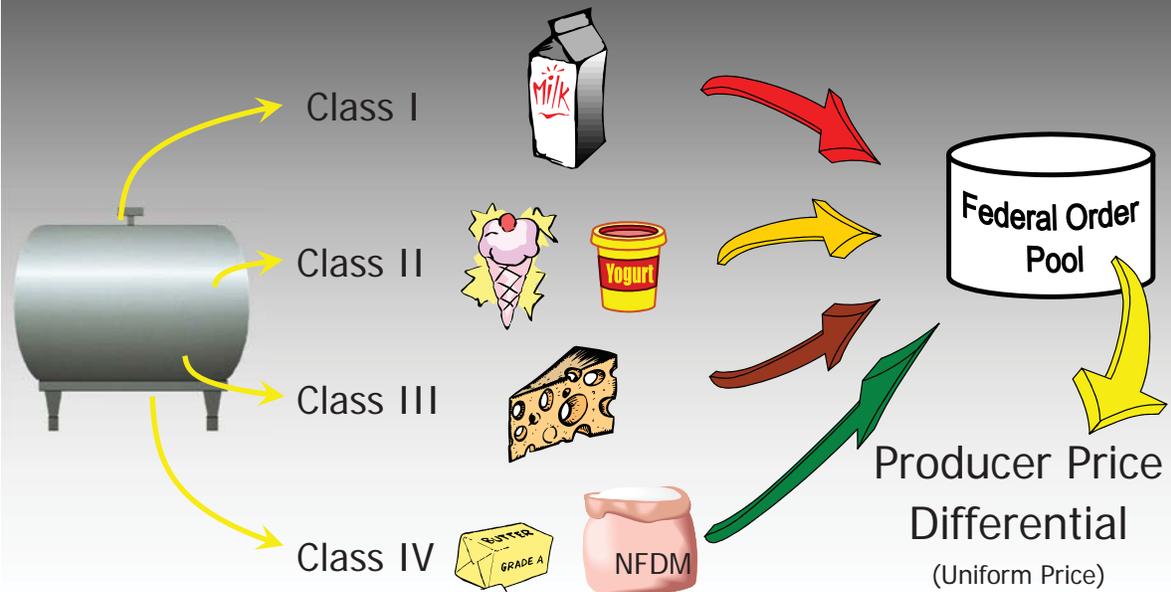


3. Market Information



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1. Sharing the Higher-Valued Milk Utilization in the Market



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Important Concepts

- Classified Pricing
 - Handlers pay for milk based on how it is used (Class I, II, III, or IV)
- Pooling
 - Process by which total classified value of milk for the market is “pooled” allowing for a Producer Price Differential (PPD) to be determined. The PPD allows all dairy farmers in the market to share equally in the market utilization.

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Pooling (Sharing)

- Pooling is the sharing of higher-valued returns to all dairy farmers (in a Federal order)
- Allows a farmer who only delivers to a cheese plant to receive a pro-rata share of the higher-valued Class I sales

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Simplified Pooling Example

		Class I Price = \$18.00		Class III Price = \$16.00	
	Pounds		Class Price		Classified Value
Class I (25%)	100,000,000	X	\$18.00	=	\$18,000,000
Class III (75%)	300,000,000	X	\$16.00	=	\$48,000,000
(100%)	400,000,000				\$66,000,000
\$ 66,000,000 ÷ 4,000,000 cwt. = \$16.50 Average Value (Statistical Uniform Price)					

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Pooling Example

(continued)

With Multiple Component Pricing

\$16.00	{	Pounds of butterfat Pounds of protein Pounds of other solids
+0.50		Producer Price Differential
\$16.50		Statistical Uniform Price



Producer Settlement Fund Example

Handler A		
Class I Use	=	100%
Class III Use	=	0%
Classified Value	=	\$18.00
Pays Producers	=	\$16.50
Pays to the PSF	=	\$1.50

Class I Price	=	\$18.00
Class III Price	=	\$16.00
Market Utilization: 25% Class I & 75% Class III		
Statistical Uniform Price	=	\$16.50

Producer Settlement Fund



Handler B		
Class I Use	=	0%
Class III Use	=	100%
Classified Value	=	\$16.00
Pays Producers	=	\$16.50
Receives from the PSF	=	\$0.50

Handler C		
Class I Use	=	25%
Class III Use	=	75%
Classified Value	=	\$16.50
Pays Producers	=	\$16.50
No Payment to or from the PSF		



How Are Producers Paid?

- Producer payments
 - Pounds of butterfat x butterfat price
 - Pounds of protein x protein price
 - Pounds of other solids x other solids price
 - Milk (cwt.) x Producer Price Differential (PPD)
 - Somatic cell adjustment, per cwt., +/- from 350,000 somatic cell count base

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Audit

- Audit program ensures integrity of program:
 - Audit handler reports for accuracy of utilization
 - Minimum payment levels and payment dates for payments to producers and cooperatives verified and enforced
 - Average many underpayment notices a month

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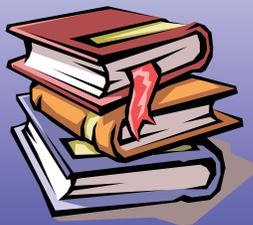
Milk Testing Oversight

- Market Administrator lab in our Chicago office
 - Verify tests of cooperatives and producers who are not members of cooperatives
 - Verify butterfat tests of bottled fluid milk
 - Work with industry testing laboratories:
 - Ensure labs are capable of accurate tests
 - Use duplicate samples to verify individual test results for certain producers

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Market Information



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COMPUTATION OF PRODUCER PRICE DIFFERENTIAL
FOR DECEMBER 2013

		Utilization Percentage	Product Pounds	Component Pounds	Rate	Value
Class I	Differential Value					\$ 5,503,730.59
	Product	11.1%	316,586,989			
	Skim Milk			311,708,286	\$15.3100	47,722,538.56
	Butterfat			4,878,703	1.5986	7,799,094.60
Class II	Product	1.9%	55,775,181			
	Nonfat Solids			4,546,046	1.7789	8,086,961.24
	Butterfat			7,082,305	1.7742	12,565,425.54
Class III	Product	86.4%	2,476,685,911			
	Protein			79,540,734	3.5390	281,494,657.66
	Other Solids			141,524,017	0.3826	54,147,088.92
	Butterfat			92,474,057	1.7672	163,420,153.57
Class IV	Product	0.6%	16,907,711			
	Nonfat Solids			837,512	1.7680	1,480,721.21
	Butterfat			7,913,403	1.7672	13,984,565.79
SCC Adjustment (Class II, III, and IV)						3,367,297.11
Total Producer Milk			2,865,955,792			\$ 599,572,234.79
Add:	Overage					32,080.13
	Inventory Reclassified					(83,450.68)
	Other Source Milk §.60(h)					0.00
	Other Source Milk §.60(i)		216,846			6,548.75
Subtract:	Transportation Credit					46,587.47

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	Nonfat Solids		837,512	1.7680	1,480,721.21
	Butterfat		7,913,403	1.7672	13,984,565.79
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	Inventory Reclassified				(83,450.68)
	Other Source Milk §.60(h)				0.00
	Other Source Milk §.60(i)		216,846		6,548.75
Subtract:	Transportation Credit				46,587.47
	Assembly Credit				252,003.77
	Credit for Reconstituted FMP				0.00
	Producer Milk Protein				325,190,580.93
	Producer Milk Other Solids				62,537,308.31
	Producer Milk Butterfat				198,542,212.64
	Producer Milk SCC Adjustment				3,803,718.34
Total Milk and Value			2,866,172,638		\$ 9,155,001.53
Add:	Location Adjustment -- Producer and Unregulated Supply Plant Milk				2,218,156.32
	One-Half Unobligated Balance Producer Settlement Fund				1,084,954.70
Total Value				0.434660	\$ 12,458,112.55
Subtract:	Producer Settlement Fund Reserve			0.044660	1,280,039.26
Producer Price Differential (Dollars Per Cwt.--Base Zone)				0.39	\$ 11,178,073.29

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2013 Market Utilization

(Billion Pounds)

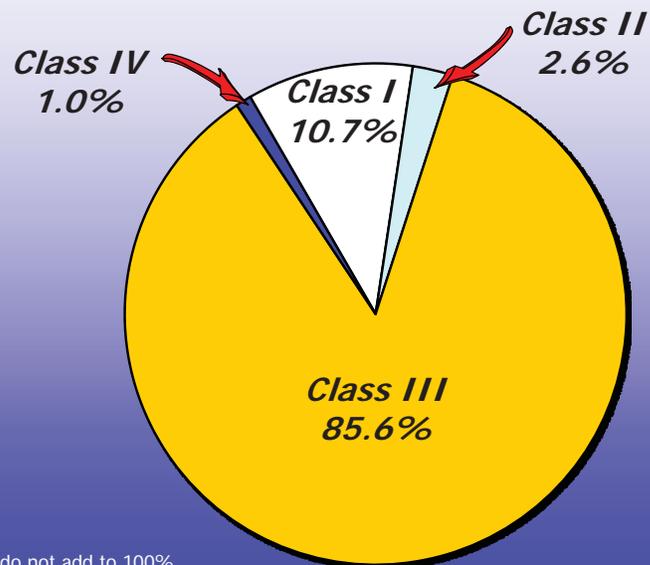
Class I (fluid)	3.7	10.7 %
Class II (creams, soft mfd.)	0.9	2.6 %
Class III (cheese)	29.4	85.6 %
Class IV (butter/powder)	0.4	1.0 %
Total	<u>34.3</u>	

Pounds do not add because of rounding, and percentages do not add to 100% because of rounding.

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2013 Market Utilization



Percentages do not add to 100% because of rounding.

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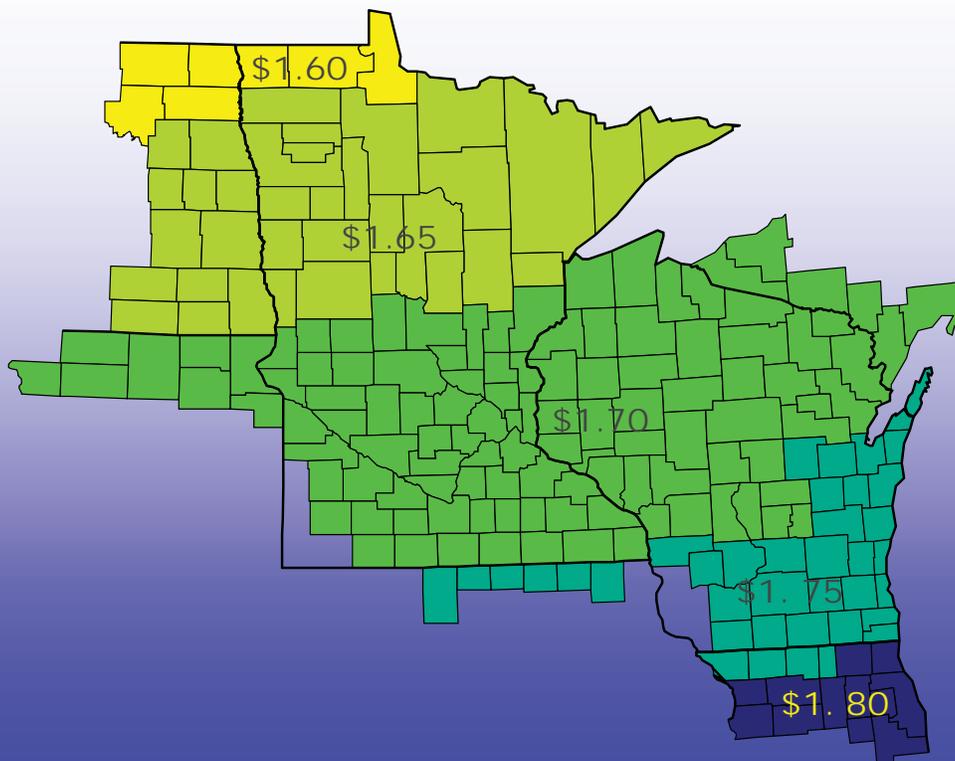


Class Prices

- Class prices are derived from the component values (i.e. butterfat, protein, other solids, and nonfat solids)
- Class I price reflects component values plus a fixed differential that varies across the U.S.
- Class I differential \$1.60 to \$1.80 in this area.

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FO 30 Price Zones



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FO 30 Class Prices & PPD

Prices are Dollars per Cwt. at Base Zone of \$1.80

2013	Class I*	Class II	Class III	Class IV	PPD*
January	20.77	18.19	18.14	17.63	0.20
February	20.01	18.49	17.25	17.75	0.32
March	19.60	18.82	16.93	17.75	0.33
April	19.46	18.73	17.59	18.10	0.25
May	19.56	18.43	18.52	18.89	0.11
June	20.73	19.14	18.02	18.88	0.30
July	20.71	19.22	17.38	18.90	0.40
August	20.68	19.27	17.91	19.07	0.34
September	20.96	19.78	18.14	19.43	0.36
October	21.00	20.56	18.22	20.17	0.38
November	22.00	20.76	18.83	20.52	0.33
December	22.17	21.66	18.95	21.54	0.39
Simple Avg.	20.64	19.42	17.99	19.05	0.31

* For the \$1.65 and \$1.60 zones, prices would be \$0.15 and \$0.20 less, respectively.

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Class I Returns

- Class I milk priced higher than other classes in Federal orders
- Over-order pricing agencies (CMPC and UMMA) add their own Class I premiums on top of the Federal order Class I price
- Class I milk averaged about \$3.97 per cwt. higher than milk used in cheese during 2008-2012 (includes F.O. Class I differential and over-order premium)
- Less than 15% of milk used in Class I, so the \$3.97 generates 51¢-62¢ if spread over all Grade A milk in the area

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Class I Returns

(continued)

- Total dollars (million) generated by Federal order Class I differential and over-order agency premium

	Federal Order	Over-Order	Total
	----- Million Dollars -----		
2008	77	96	173
2009	77	98	175
2010	76	97	173
2011	74	96	170
2012	66	89	155
5-Year Average	\$74	\$95	\$169

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Class I Returns

(continued)

- Over 5-year period, \$846 million more has been generated through regulated pricing of Class I milk than would have been generated by sales of this milk at Class III (cheese) prices

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Amendment Process

- Amendment process allows Federal orders to adapt to changing marketing conditions
- Most recent amendments
 - February 2007, October 2008 and March 2013

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Producer Approval Process

- Each time an order is amended:
 - Approval of 2/3 of affected producers required
 - Cooperatives may, if board wishes, bloc vote on behalf of their member/owners
 - Voting is always on "order as amended", not just the changes themselves
 - If there is not 2/3 approval, order will be terminated

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Amendment Process

- Industry Proposals
- Notice of Hearing
- Public Hearing
- Comment Period
- Recommended Decision (excluded if “emergency decision”)
- Comment Period
- Final Decision
- Producer Vote
- Order Amending Order
- Implementation

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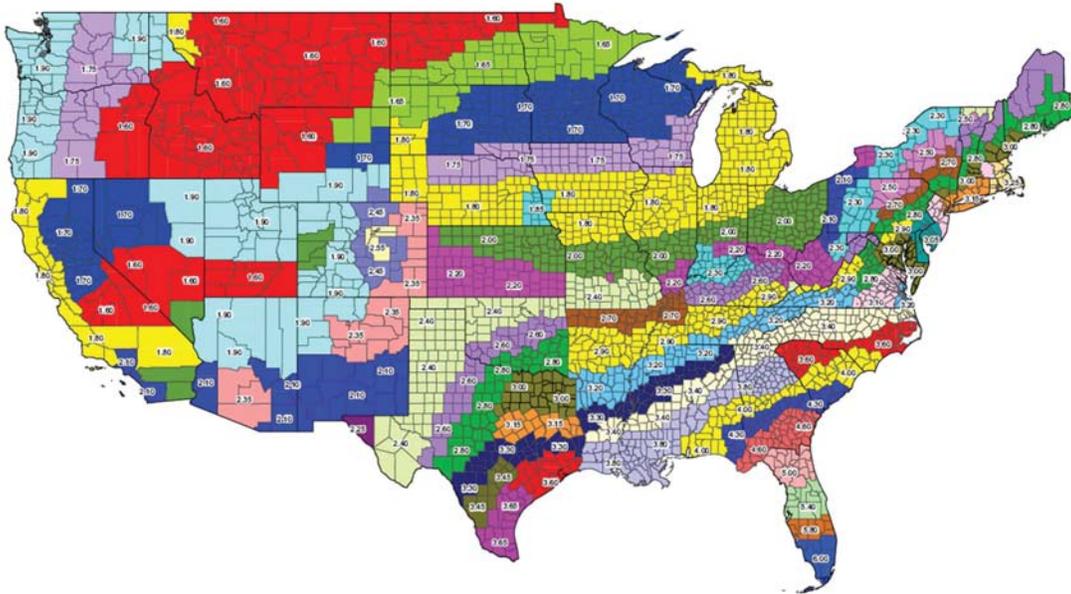


Current Federal Order Issues

- California State Order
 - Become a Federal Order?
- Price Discovery
- Class I price surface

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Federal Milk Marketing Order Class I Price Structure



Effective May 1, 2008

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Visit Our Website at:
www.fmma30.com

- Includes:
 - Price Information
 - News and Publications
 - Federal Order Amendment Actions
 - Payment Dates
 - Producer Data
 - Staff Papers
 - And Much More . . .

USDA Agricultural Marketing Service Dairy Programs
United States Department of Agriculture

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Other Contact Information

Welcome to the Upper Midwest Federal Milk Order. This web site provides public access to Federal milk order information along with other dairy industry related information.

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Questions ?

