

California Nonfat Dry Milk

Background

Since 1973, the California Department of Food and Agriculture (Department) has utilized sales reports to collect data from California processing plants producing nonfat dry milk (NFDM). On both a weekly and monthly basis, the Department receives and audits sales of NFDM. Using the sales data from all reporting processing plants, the Department then computes a weighted average price of NFDM called the California Weighted Average Price (CWAP). The CWAP is one of the commodity prices that are used directly in the Class 1 and Class 4a pricing formulas.

Presently, the sales reports include all types of Extra Grade and Grade A NFDM sold to wholesale customers for human consumption, regardless of length of storage, container size or sales volume. The reported types of NFDM include low-, medium-, and high-heat, organic, and rBST free powders; however, the reports do exclude sales of other powdered milks, ~~including fortified NFDM~~, instant NFDM, whole milk powder, skim milk powder and skim milk powder blends. Additionally, all types of sales are included in the reports. These sales include spot market sales, short- and long-term contracted sales consisting of fixed or indexed prices, and government sales to the Commodity Credit Corporation (CCC). There are some sales that are excluded from the reports, specifically inter-company sales to other plants that belong to the same organization or coop as the reporting plant.

The methodology of the auditing procedure has been essentially the same since 1973, except for a change that occurred in 1996. Prior to 1996, if the total weekly or total monthly weighted average NFDM price sold and reported by an individual processing plant was below the federal support purchase price offered through the CCC, then the reported price of the plant was increased or adjusted upward to the level of the federal support purchase price for the calculation of the CWAP. By making this adjustment, all of the weighted average prices of NFDM sales by all reporting plants considered in the CWAP would be at least at the level of the federal support purchase price. However, after the change in 1996 to the present, the calculated CWAP includes reported prices exactly as they are reported without upward adjustment, even if the reported price is below the federal support purchase price. Therefore, all NFDM prices in the current sales reports are considered at their reported price in the calculation of the CWAP.

Current Issues

In the beginning of 2007, NFDM prices and reporting procedures became an issue in the dairy industry because of differences in the price of NFDM among various price series. On average, between 2002 and 2006, the CWAP, the NASS NFDM price that is used in the Federal Class IV pricing formula, and the

Dairy Market News Western-Mostly (DMN) NFDM price remained within three cents per pound of each other. For the same time period, the Oceania Skim Milk Powder averaged as much as 30 cents below to 10 cents above the other three price series.

However, starting in late 2006 through the beginning of 2007, there began to be divergence among the different price series. While the NASS and CWAP prices stayed within 5 cents of each other from October 2006 to March 2007, the DMN and Oceania prices increased rapidly above the CWAP and the NASS. Relative to the CWAP and NASS prices, the Oceania price increased from 15 cents higher in October 2006 to 35 cents higher in March 2007. Similarly, the DMN price increased from 5 cents higher in October 2006 to 15 cents higher in 2007. Because of these relative changes in the price series, many in the dairy industry began to question whether the NASS and CWAP prices were reflective of actual market conditions for NFDM.

Shortly thereafter, USDA undertook a review of the NASS NFDM survey procedure and discovered that not all reporting plants were following their required procedures. As a result, revisions were made and the NASS price then converged with the DMN and Oceania prices. Given that the auditing procedures for the CWAP differ from the survey procedure of NASS, the CWAP price continued to remain below the other prices until June 2007.

In light of the differences in the NASS and CWAP procedures, the dairy industry compared the two procedures in order to determine the cause(s) of the difference in the two price series. One important difference between the survey procedures of NASS and the auditing procedure of the Department is the inclusion of long-term contracted sales by the Department and the exclusion of such sales by NASS. Because long-term contracted sales can carry a lower price relative to the other types of sales, these sales can influence the CWAP causing it to be lower than the NASS price. Another difference between the CWAP and the NASS NFDM price is the inclusion of high-heat NFDM in the CWAP price and its exclusion in the NASS price.

During the spring of 2007, members of the industry initiated discussion regarding the CWAP and the auditing procedures used by the Department to establish the CWAP. Customarily, the NFDM sales reports and the procedures used by the Department to collect and audit NFDM sales information to establish the CWAP are a result of input from the California dairy industry. The Department has historically held informal industry meetings in order to discuss and initiate changes to the procedure. Accordingly, there was an industry meeting to discuss this issue on May 16, 2007, and also further discussion during the Dairy Advisory Council meeting on May 31, 2007.

Upcoming Hearing

On June 15, 2007, Western United Dairymen (WUD) petitioned the Department for a public hearing to revise the weekly and monthly NFDM sales reports. In their petition, WUD recognized that revisions to the sales reports can be done in an informal, administrative fashion rather than through the formal public hearing process; however, WUD opined that the discussion of this issue at the industry meetings cited above, lacked the disclosure of information necessary to arrive at the best resolution. Therefore, WUD sought to pursue this issue through the hearing process. Shortly thereafter on June 18, 2007, Milk Producers Council (MPC) petitioned the Department for a public hearing to amend the Stabilization Plans by replacing the CWAP with a NFDM price series published in the Dairy Market News. Because the MPC petition proposes an amendment to the Stabilization Plans, the formal hearing process would be necessary in order to consider and implement this type of proposed amendment.

On June 29, 2007, the Department called a public hearing for August 28, 2007, to consider not only the MPC proposed amendments to the Stabilization Plans and the WUD proposed revisions to the NFDM sales reports, but also any other alternative proposals received by July 31, 2007. The Department received two alternative proposals, one by The Alliance of Western Milk Producers (Alliance) and the other by Dairy Institute of California (Institute). The Alliance proposes one change to the current NFDM sales reporting procedure, which is to exclude the sales of organic NFDM. The Institute proposes the Department follow the NFDM sales report specifications that were recently set forth in the recent interim final rule from USDA's Agricultural Marketing Service for Dairy Product Mandatory Reporting Program. Specifically, the Institute proposes to adjust the Department's current reporting procedure by excluding the sales of NFDM older than 180 days, excluding high-heat NFDM, and excluding forward pricing sales or contracted sales where the sale price is set (not adjusted) 30 or more days prior to the transaction completion. Additionally, the Institute proposes to adjust the Department's current reporting procedure by limiting quantities of NFDM reported to 25 kilogram bags, 50 pound bags, totes, and tanker sales.