Minutes

Producer Committee Meeting
October 23, 2014 10:00 a.m.
Scott Hart Building Auditorium
301 N. Roberts, Helena, Montana

Call to Order

Committee Chair David Miller called the meeting to order at 10:02 a.m.

Attendance

Committee Member	Present	Absent
David Miller, Chair	X	
Sam Hofer, Vice Chair		X
Andrew Wipf, Secretary/Treasurer	X	
Loren Dyk	X	
Michael J. Hofer	X	
Tim Huls	X	
Daron Kamerman		X
Nelson Kamerman		X
Larry Klompien		X
Jeremy Leep		X
Walter Wipf	X	
Ruben Wurz	X	

Montana Department of Livestock Staff:
George Harris, Administrator, Centralized Services Division
Chad Lee, Bureau Chief, Milk Control Bureau
Mark Curtis, Dairy Accountant, Milk Control Bureau
Linda Grady, Auditor, Milk Control Bureau
Rob Stutz, Montana Department of Justice, Agency Legal Services (attorney representing the Montana Department of Livestock)

Guests:
Rob Adamson, Meadow Gold
David Lewis, Northwest Dairy Association
Ed Waldner, Riverview Colony

Approval of Minutes from July 14, 2014

Loren Dyk moved and Ruben Wurz seconded the motion to approve the minutes of the July 14, 2013 meeting as submitted. The motion carried. All members voted in favor.

New Business

Sale of Surplus Milk

David Miller informed the committee that the Producer Committee was almost placed in a position in which would have been responsible to market surplus milk in August. Before reversing its decision, Meadow Gold had communicated that it was no longer going to market surplus milk. Any plant has that option at any time. This is something that has never happened before. Mr. Miller wanted the committee to be aware that marketing the surplus can become the committee's responsibility. The committee may market the milk directly or hire a marketer to market milk on behalf of the committee. Mr. Miller opened the floor for discussion on the Producer Committee's role in marketing surplus milk. No comments were made.

Chad Lee provided a report that covered several aspects of marketing surplus milk, including:

- administrative rules related to marketing surplus milk;
- the role of surplus milk sales in the calculation of quota and excess prices; and
- statistics on the volume, gains and losses, and hauling charges of bulk and packaged surplus milk marketed from October 2012 through September 2014.

Mr. Miller invited the committee and public to ask questions and make comments during the report. Because of this, comments from the public and the Department of Livestock staff on the sale of surplus milk were interspersed with committee discussion.

Rob Adamson stated [with regard to the requirement of pool handlers to purchase surplus milk from other pool handlers before purchasing raw milk from out-of-state] that the requirement applied to the need for raw milk to meet in-state market needs, not for production destined for out-of-state markets. Mr. Lee concurred with Mr. Adamson's statement of clarification.

After Mr. Lee explained that the Producer Committee has authority to incur expenses to market surplus milk, David Lewis stated it was important to note that currently there are no charges to the pool or the producers [by the distributors] for the service of marketing the surplus milk.

Discussion followed Mr. Lee's explanation of how the surplus sale gain/loss and hauling charges impact the calculation of quota and excess prices. Mr. Adamson noted that some farmers think that out-of-state milk sales are a drag on blend prices, that the farmers do not see the value that is being added back to Class III milk through the surplus gain. Mr. Adamson stated that it would be easier to see the value if the out-of-state sales were presented separately from Class III and the full value was shown. Tim Huls stated that the surplus gain information is presented in the Producer Report provided to producers following pooling. Mr. Huls suggested that the Milk Control Bureau could modify the report to highlight the information.

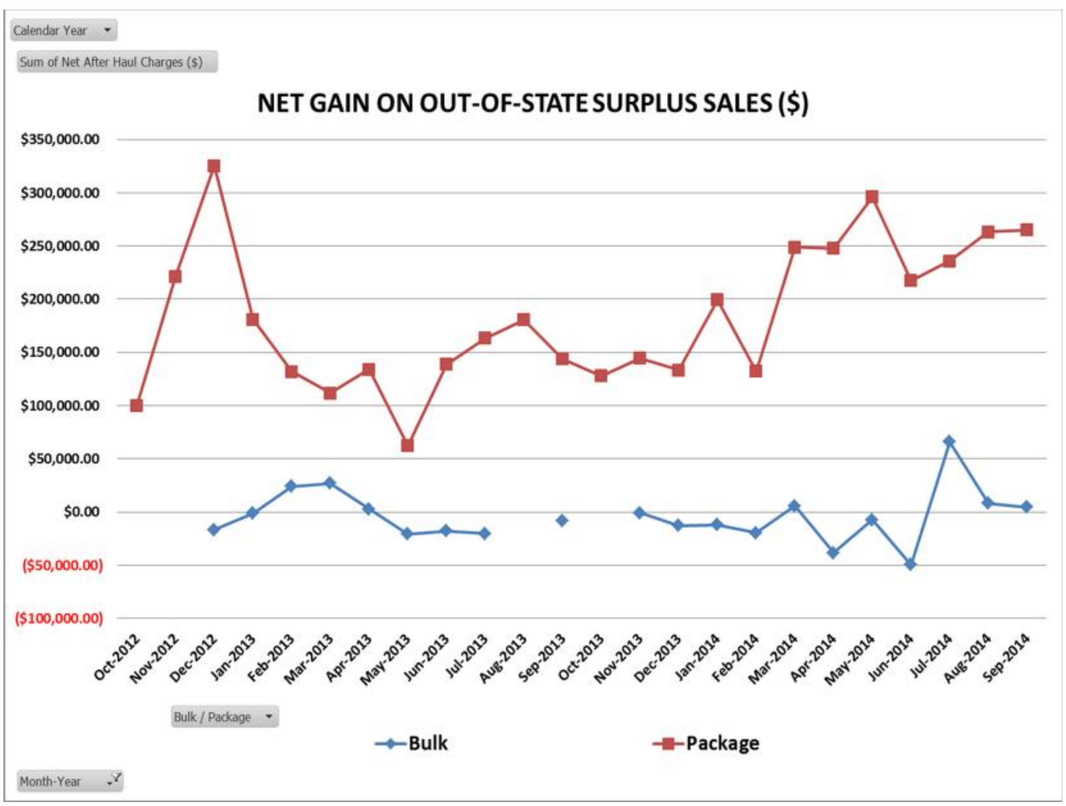
Mr. Lee explained how the prices used to determine the value of surplus packaged milk sold out-of-state are not in rule but are based upon an agreement between Meadow Gold and Darigold.

- The price used to determine the value received for out-of-state packaged milk for Meadow Gold is Federal Class I (the mover price).

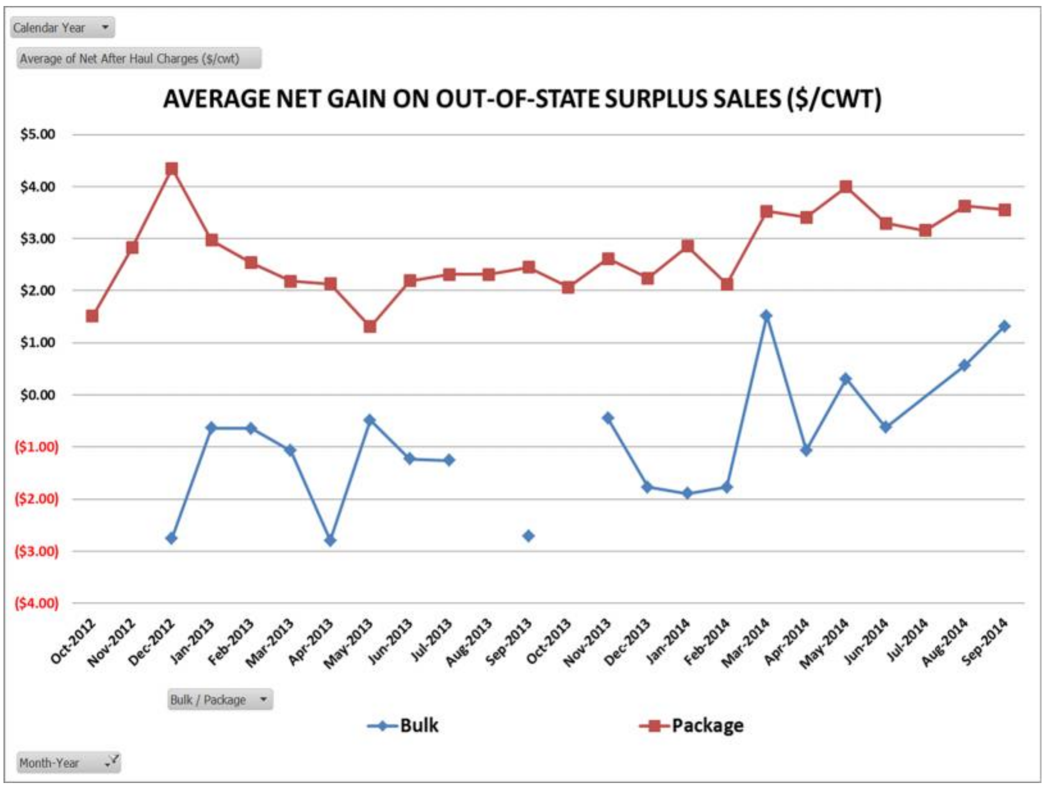
- The price used to determine the value received for out-of-state packaged milk for Darigold is Federal Class I - $0.50/cwt (the mover minus $0.50), except for packaged milk sold into the Wyoming market, where the price used is Federal Class I, the same as Meadow Gold's price.

Mr. Adamson confirmed that the mover price (Federal Class I) is used by Meadow Gold for determining value of surplus milk sold out-of-state as packaged milk and stated that for markets where the companies compete, the price reported to the Milk Control Bureau is the same. Mr. Adamson explained that the reason for Darigold using the "minus $0.50" price is that Darigold is selling into markets that Meadow Gold would not serve from Montana (Colorado, Utah, southern Idaho). The discount is to allow for freight to get the milk to those markets. Mr. Lewis agreed and stated that without the discount, Darigold would not be selling milk into those markets. Mr. Lee noted that when Darigold sells packaged milk into the Colorado market, Federal Order rules covering the Colorado market require Darigold to pay a minimum price that triggers a compensatory payment, which Darigold must pay into the Montana pool or to the related Federal Order. Darigold's practice has been to add the compensatory payment to the value it reports for packaged surplus milk sales.

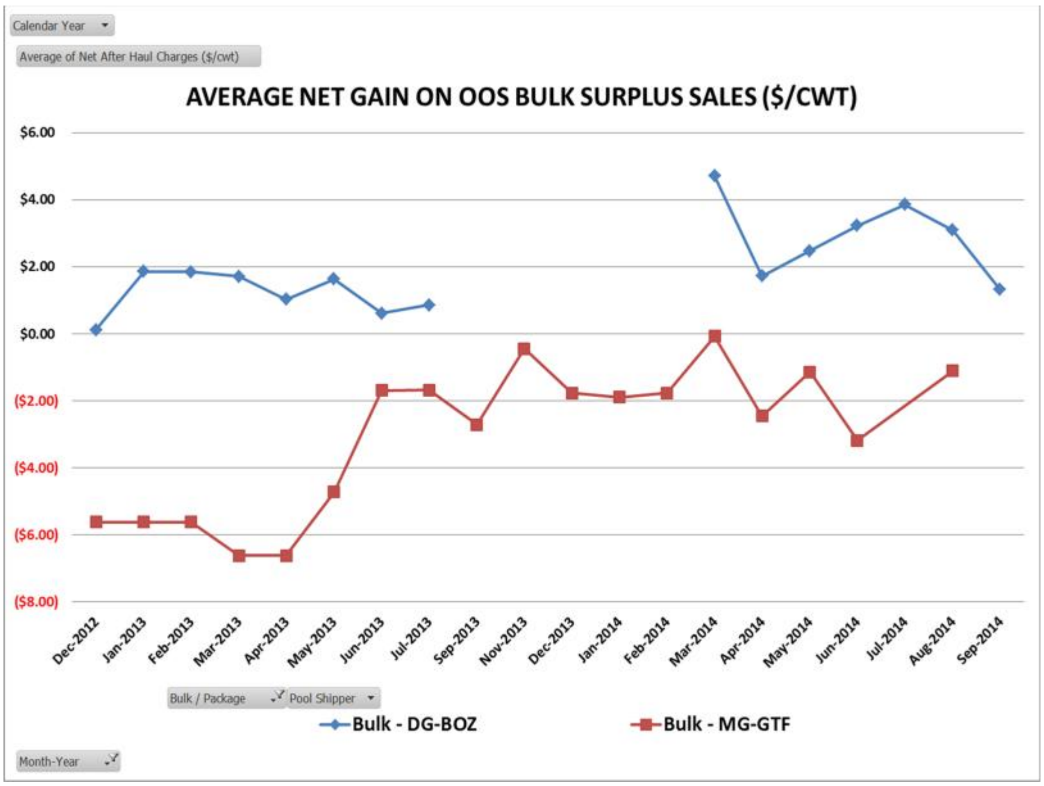
Discussion followed Mr. Lee's display of a chart showing the net gain on out-of-state surplus sales (after hauling) for packaged milk and bulk milk sales. See chart below. Mr. Adamson commented that the chart shows the value that is being brought to the farmers when the pool handlers package milk for sale out-of-state instead of selling that same milk in bulk form.



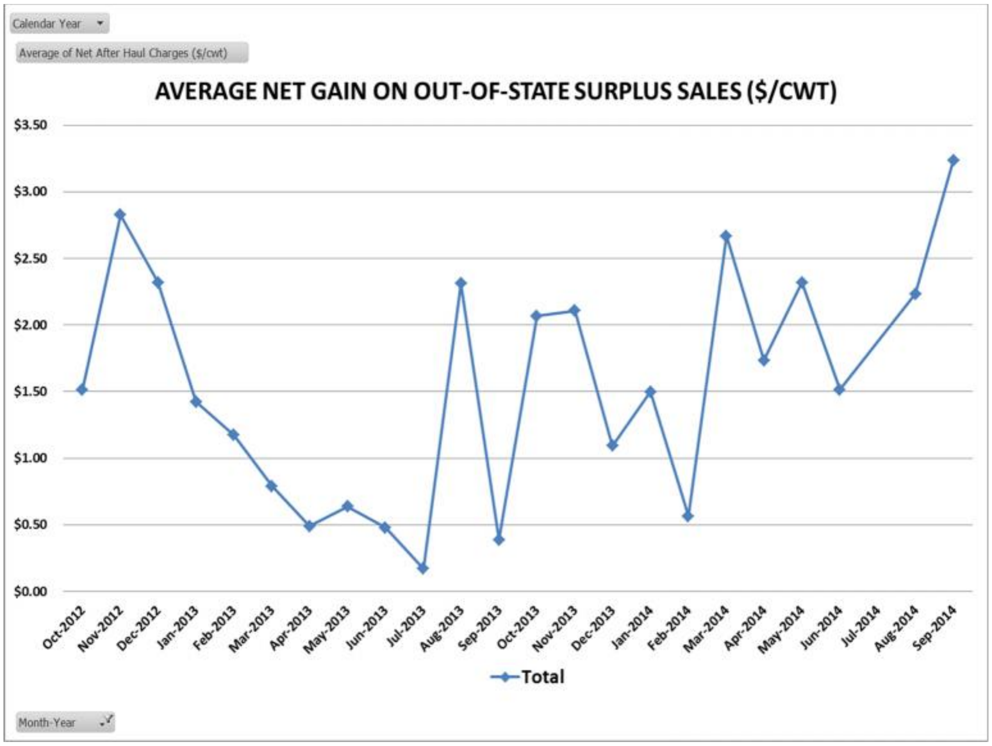
Discussion followed Mr. Lee's display of a chart showing the average unit net gain ($/cwt) on out-of-state surplus sales (after hauling) for packaged milk and bulk milk sales. See chart below. Mr. Huls commented that the chart shows that the greater the portion package sales make up surplus sales (vs. bulk sales), the more farmers benefit. Mr. Lewis commented that the benefit is two-fold because the plants also benefit by running at capacity, which lowers costs and keeps the plants active. Mr. Adamson stated that even though the pool handlers are paying $2.55/cwt less [the difference between Federal Class I and Montana Class I] for the milk that is packaged and sold out-of-state, there is a clear benefit to producers. Mr. Adamson said that even though $2.55/cwt sounds like a lot of money, it is about $0.25/gallon less. Mr. Adamson added that milk cannot be trucked to Casper, Wyoming for $0.25/gallon and that pool handlers need to be able to reach out to other markets because Montana does not have a large population.



Mr. Lee presented a chart that showed the average net gain ($/cwt) on out-of-state bulk milk sales comparing sales by Darigold and Meadow Gold. See chart below. Mr. Lee attributed the difference between the pool handlers to Darigold's internal agreements on sales price (Federal Class IV, which has been strong in recent months) and freight ($2.19/cwt on nonmember milk). Mr. Lee noted that the internal sales price and freight rates may change when the current contract expires in August 2015. Mr. Lewis stated that hopefully Darigold will always be able to offer a bulk out-of-state purchase price that will exceed what is available to Meadow Gold because the transactions will not be on spot market basis. Mr. Adamson informed the committee that Meadow Gold offers surplus milk to Darigold first before marketing out-of-state. Mr. Adamson stated that Darigold's internal agreement was a major help to the Montana pool and illustrated the difficulty of spot market marketing by describing a market situation in the summer of 2012, when the best offer to Meadow Gold was Federal Class IV - $7/cwt, before deducting freight. This resulted in a difference of $10/cwt between Darigold's price and what Meadow Gold could receive on the spot market. Mr. Lewis explained that what enabled the agreement to happen [the internal rates described for Darigold Montana bulk surplus] was that Country Classic had the Costco contract, which was attractive to Darigold because it enabled Darigold to gain access to Costco to sell other dairy products through Costco. Ruben Wurz asked what would happen when the contract [terms from the Country Classic merger with Darigold] runs out. Mr. Lewis responded that the details are not yet known, but that it would be similar to what is happening now.



George Harris asked Mr. Lee to further clarify whether the surplus milk sales provisions have benefited the pool. In response, Mr. Lee showed the following chart, which shows the average net gain ($/cwt) of out-of-state surplus milk sales (bulk and packaged milk combined). Mr. Lee stated that the chart showed how much more the pool had been paid over the Montana Class III price for surplus milk sold out-of-state (bulk and packaged milk combined).



After Mr. Lee discussed haul charges from shipping surplus milk, Mr. Lewis stated that after the Darigold merger agreement ends, Darigold may ship some bulk surplus milk from Western Montana to Spokane. Mr. Lewis stated that the farmers' freight charge would cover much of the cost of the haul, with the outcome being a way to market bulk surplus milk out-of-state while curbing haul charges.

At the conclusion of Mr. Lee's report on the sale of surplus milk, Mr. Miller asked the committee if there were any more questions. Mr. Wurz asked whether the pool handler makes money on selling bulk surplus milk. Mr. Adamson responded that the pool handler did not.

Mr. Adamson explained to the committee what is involved for Meadow Gold to market the surplus milk. Meadow Gold pays the hauler, even though the cost of freight is between the producers and the hauler. Meadow Gold holds the purchase of the surplus milk on their receivables. Meadow Gold prepares invoices for the surplus milk sales. Meadow Gold arranges the sale of the milk, for which there are not many interested buyers. Meadow Gold has two interested buyers: Innovative Food Solutions (IFS) and Glanbia. Innovative Food Solutions offers a price for the month prior to delivery. Glanbia does not offer a price until the month after the milk has been delivered and utilized in the manufacture of cheese. Administrative complexity arises in recording the receivables for milk marketed to Glanbia because the dollar amount initially recorded in invoices to Glanbia has to be adjusted in the following month.

Mr. Lewis stated that Darigold is a processor wholly owned by a farmer-owned cooperative (Northwest Dairy Association). Mr. Lewis further explained that Darigold would not purchase at a price lower than Class IV or Class III or however the plant utilizes the milk. Darigold will not turn away member milk. Darigold does not have to call Glanbia and ask what it is willing to pay because Darigold always sell the milk internally. Mr. Lewis noted that Darigold has worked better with Meadow Gold than Country Classic previously did.

Mr. Huls made the following comments to provide historical perspective on the marketing of surplus milk. Originally, the Montana Class III price was the price for surplus and the processors had the ability to make or lose money on the sale of surplus milk. The industry became concerned because one processor was handling all of the surplus milk and there was a belief that too much money may have been lost collectively in the pool because of that processors opportunity to make money. So the industry changed the rules to the current system where the profit is distributed or the loss absorbed by the pool. Mr. Huls' concern is that the current system does not incentivize processors to do the best job of marketing surplus milk. Mr. Huls believes that the processors are doing the best job because they want the producers to stay in business, but they are not being compensated to market the milk. Mr. Huls expressed concern that the committee, if it took over the role of marketing the milk, would wind up selling the milk on the spot market at the lowest price and therefore does not want the committee to become responsible for marketing surplus milk. Loren Dyk commented that marketing the milk is not the committee members' expertise. Mr. Huls stated that the committee struggles to get a meeting quorum to approve transfers of quota and asked how the committee would be able to carry out the business of marketing the surplus milk in a way that makes everyone happy.

Mr. Adamson stated that Meadow Gold does not want to stop marketing surplus milk and that he wanted to inform the committee of what is being done to market the surplus milk. Mr. Adamson further stated that he wanted the committee's support and trust that he is doing the best that he can. Mr. Huls commented that the purpose of the discussion was to address whether the producer of Montana were being served by the system as it exists and with the people marketing the milk or whether there were problems that need to be addressed. Mr. Huls expressed that based on the information presented in the charts at the meeting, he feels comfortable that the system is working. Mr. Huls stated that if the committee were to market the surplus milk, the Milk Control Bureau would not be assisting and the committee would have to hire more than one person to market and coordinate logistics to do the job being done by Meadow Gold and Darigold.

Mr. Lewis was asked to provide an overview of changes that might arise from the expiration of the Darigold – Country Classic agreement (in August 2015). Mr. Lewis stated that he does not see a lot changing, that there is no plan to move the Costco bottling out of Bozeman. Mr. Lewis noted that if the Costco account was lost, Darigold would have to ship more milk out in bulk and that it would probably be sent to Jerome or Spokane. Milk shipped to Spokane would likely be sent directly from western Montana dairies at an additional hauling charge of $0.10 - $0.20/cwt. It was discussed that if Darigold lost the Costco account, Meadow Gold would likely not be the supplier taking over the account. Mr. Lewis stated that he did not think it would be a case of Darigold losing the Costco account, rather whether it could afford to keep the account.

Mr. Adamson asked the committee whether it was comfortable with how Meadow Gold is marketing the surplus milk and stated that if the committee is not comfortable, that it needs to look long term at an alternative. Mr. Huls responded that under the current situation, it appears that cooperation between Meadow Gold and Darigold is better than ever and that he would support how things are being done. Mr. Lee asked Mr. Adamson how Meadow Gold makes its decision between selling bulk surplus milk between IFS and Glanbia. Mr. Adamson responded that Meadow Gold takes a known price over an unknown price, and IFS offers a known price. Mr. Adamson added that if the committee wants Meadow Gold to sell to Glanbia, it would do so. Mr. Adamson stated that the only thing he is using in determining what is “most advantageous” is known price over unknown price.

Mr. Miller asked the committee members supplying Meadow Gold for questions or comments pertaining to the marketing of surplus milk. After no comments were offered, Mr. Dyk asked about the status of the reverse osmosis plant proposed by the Montana Milk Producers Association at the June 10, 2014 meeting of the Board of Milk Control. Ed Waldner stated that since the Montana Milk Producers Association (MMPA) cannot buy surplus milk the project is dead. Mr. Waldner also stated that a feasibility study was completed that indicated that there was not enough excess milk from the members of MMPA to support the plant. Mr. Adamson asked the committee whether it would be worthwhile to have the pool retain $0.05 - $0.10/cwt to invest (as a pool) in a reverse osmosis or cheese plant. Mr. Adamson noted that if Darigold lost the Costco account, another market would be needed for an additional six million pounds of surplus milk. Mr. Lewis responded that Darigold has offered to put in a reverse osmosis plant if the Costco account is lost and that building the plant before then is not necessary because it could be built in a short period of time.

Mr. Huls stated that the meeting had been beneficial and expressed appreciation for the information presented. Mr. Huls stated that the committee could benefit from the type of information presented on a more frequent basis and suggested that the committee meet quarterly in Helena. Mr. Adamson stated that if the Milk Control Bureau only has to collect information on the last quarter, a greater level of detail can be provided.

There was brief discussion about the status of the enforcement of the twelve-day rule.

<u>Producer / Quota Committee Assessment</u>
Mr. Miller informed the committee that Department of Livestock staff raised questions pertaining to the assessment used to fund Producer Committee activity and invited Mr. Harris to speak on the issues.

Mr. Harris stated that in the process of restructuring the Milk Control Bureau, he asked staff to review all of the procedures and bring potential problems to his attention. The Administrative Rules of Montana 32.24.505 establishes the Producer Committee. Mr. Harris’s concerns relate to Mr. Lee being asked to sign checks from a private account to pay for meals and per diem of the committee at rates higher than rates established by administrative rule for state boards. Mr. Harris informed the committee that he instructed Mr. Lee not to sign any checks.

Mr. Huls asked whether there was a difference [in compensation / reimbursement rates] between state boards funded by the General Fund vs. industry-funded committees. Mr. Harris responded that there was not.

Mr. Harris stated that the Board of Milk Control is a public entity and that the Producer Committee is in the administrative rules and is making public policy. Mr. Harris informed the committee that they meet as a legal body representing the state, not representing just Darigold or Meadow Gold.

Mr. Lewis asked why an assessment for the Producer Committee was withheld from his milk check. Mr. Lee responded that the assessment is also in question.

Rob Stutz addressed the committee, stating that the Producer Committee is a public body established by rules adopted by the Department of Livestock pursuant to statutory authority. The committee has to comply with the administrative rules of the State of Montana and make sure it has authority for the assessment. Mr. Stutz informed the committee that if it wants to be a purely private committee, there is a significant amount of work to be done to remove the committee from the administrative rules and remove it from the authority provided by the administrative rules.

Mr. Lewis stated that he did not think the industry would want to convert the committee to a private committee. Mr. Lewis then asked when the assessment was last in place and inquired about the committee's current account balance. Mr. Lee responded that he believed the assessment was last collected in 2012 and that the current balance was $4,130.61. Mr. Lee further explained how his concern developed regarding the assessment and compensation to the committee.

Mr. Stutz stated that he had not seen anything in the code or rules that address levying an assessment to fund the activities of the Producer Committee.

Mr. Miller encouraged anyone with some history on the committee assessments and compensation to contact himself, Chad Lee, or George Harris. Mr. Huls suggested that Milk Control Bureau staff examine committee minutes. Mr. Lee replied that bureau staff had located minutes from an August 1990 committee meeting where a motion establishing an assessment and rates of compensation and mileage reimbursement to committee members was made and passed. Mr. Lee noted that he had limited time to review the minutes prior to the meeting and read a paragraph from the August 28, 1990 minutes that preceded the motion:

> [Bill] "Ross informed the committee that it wasn't possible for the board to institute an assessment so the bureau could pay the producer committee members to attend quota meetings because it doesn't qualify as official state business nor is it for administering the Act."

Mr. Lee expressed strong disagreement with Bill Ross's statement and stated his belief that if the Department of Livestock determines that there is no authority for the committee to levy an assessment, costs could be covered out by the administrative assessment collected by the Milk Control Bureau. Mr. Lee said that if it was necessary to adjust the administrative assessment to have sufficient funds, the process for adjusting the administrative assessment would be followed. Mr. Harris agreed and emphasized that if an adjustment was needed to cover Producer Committee costs, it would come through the administrative fund, through a state funds and records, not through a private fund. Mr. Harris stated that based on his 37 years of experience in state government, Bill Ross' interpretation was not correct. Mr. Stutz informed the committee that he also disagreed with Bill Ross' interpretation.

Mr. Huls suggested that additional research be completed so that the committee could have a more informed discussion. Tim Huls moved to table the discussion on the Producer Committee Assessment. Loren Dyk seconded the motion. The motion carried. All members voted in favor.

Mr. Harris informed the committee that the Department of Livestock will make a determination soon regarding the authority for a separate Producer Committee assessment and the allowable reimbursement of members of the committee.

Public Comment

None

Adjournment

Tim Huls moved and Loren Dyk seconded the motion to adjourn the meeting. The motion carried. All members voted in favor.

Meeting adjourned at 12:05 p.m.

[redacted] ______________ **David Miller, Producer Committee Chairman**

Date: 5-7-15