

SALE OF SURPLUS MILK TO RELATED ENTITIES

Montana Board of Milk Control

April 29, 2021

Surplus Milk Overview

ARM 32.24.150(42) defines "Surplus" as:

- (a) means all pool milk received by a pool handler originating from pool producers that exceeds the sum of the following:
 - (i) the pool handler's sales of milk sold for consumption in Montana;
 - (ii) sales or transfers of bulk unprocessed milk to other pool handlers; and
 - (iii) sales of bulk unprocessed milk to nonpool plants located in Montana.
- (b) does not include shrink, dumped milk, inventory, and fluid cream products, including fluid cream products sold in bulk.

Surplus Milk Overview

The sale of surplus milk is largely unregulated

- § 81-23-102, MCA sets forth the policy of the Milk Control Act and focuses on in-state activity
- § 81-23-103(1), MCA directs the Board to “supervise, regulate, and control the milk industry of this state, including the production, processing, storage, distribution, and sale of milk sold for consumption in this state”
- § 81-23-106, MCA states that the Milk Control Act “does not apply to foreign or interstate commerce except insofar as it may be effective in compliance with the United States constitution and with the laws of the United States”

Surplus Milk Overview

Per 32.24.523(3), surplus milk sales are reported to the Bureau in order to determine the value of pool milk via adjustments to the utilization value

ARM 32.24.523(1) requires that “[s]urplus milk must be marketed and sold in a manner that is economically advantageous to pool producers, with all gain or loss shared by all pool producers”

Surplus milk is marketed and sold directly by pool handlers, but ARM 32.24.523(2) gives the Producer Committee the authority to direct the marketing of surplus milk or take it over if the pool handler does not

Bulk Surplus Sale Adjustment:

Proceeds Received (sales price)

Less: Montana Value (based on appropriate Montana Class I, II, III Class Prices)

Less: Transportation Expenses

= Bulk Surplus Sale Adjustment

Bulk Surplus Sale Adjustment:

If **negative**, the adjustment **decreases** utilization value – **lowers quota price** (normal)

If **positive**, the adjustment **increases** utilization value – **increases quota price**

The higher the Proceeds Received, the more favorable to pool producers.

Surplus Milk Sales in Montana

(historically)

Darigold-Bozeman



Darigold-Jerome (Class IV)

Related entity
transaction

Meadow Gold-GF



Darigold-Jerome (Class IV)

Glanbia (Class III)

Schreiber (Class III)

Nelson Ricks (Class III)

Unrelated entity
transactions

Sale of Darigold-Bozeman Milk

Non-Surplus Milk

Producers



NDA



Darigold-Bozeman

Surplus Milk

Producers

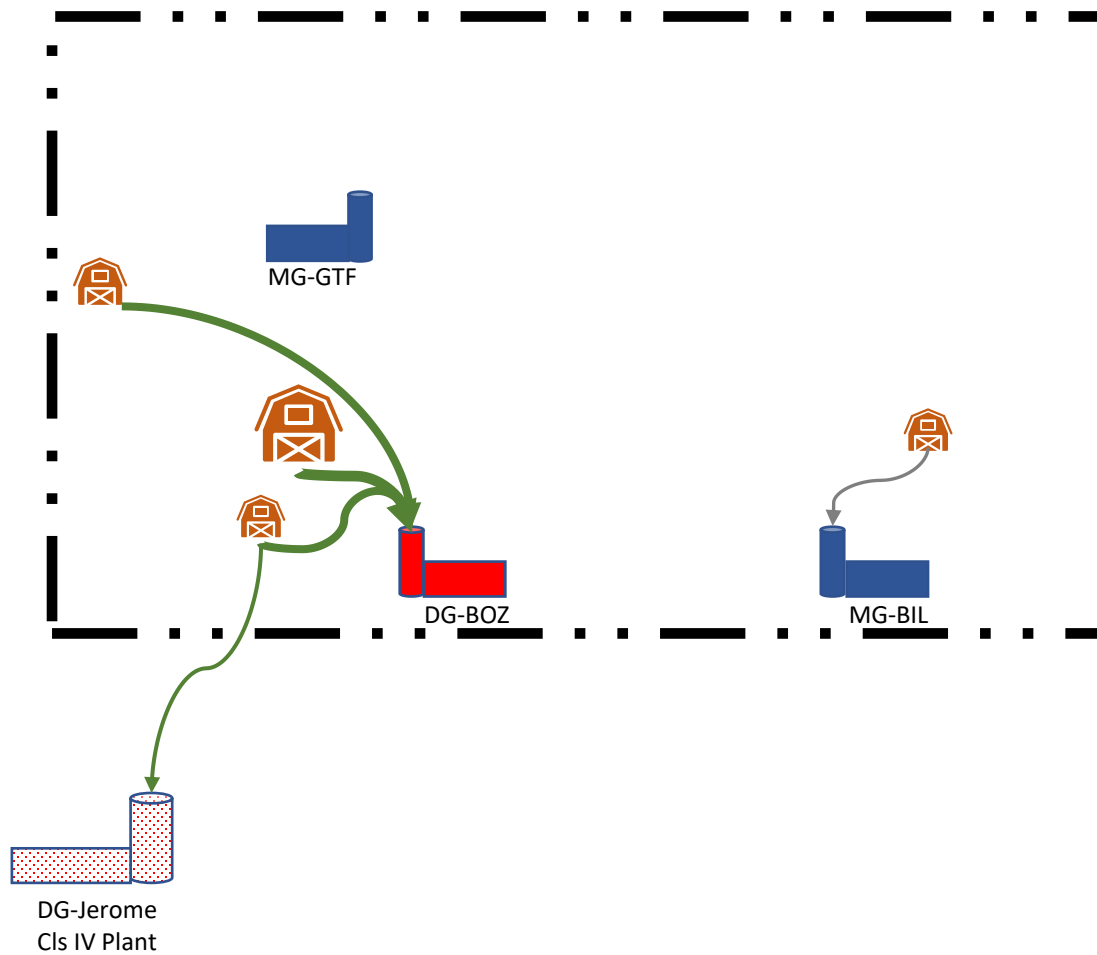


NDA

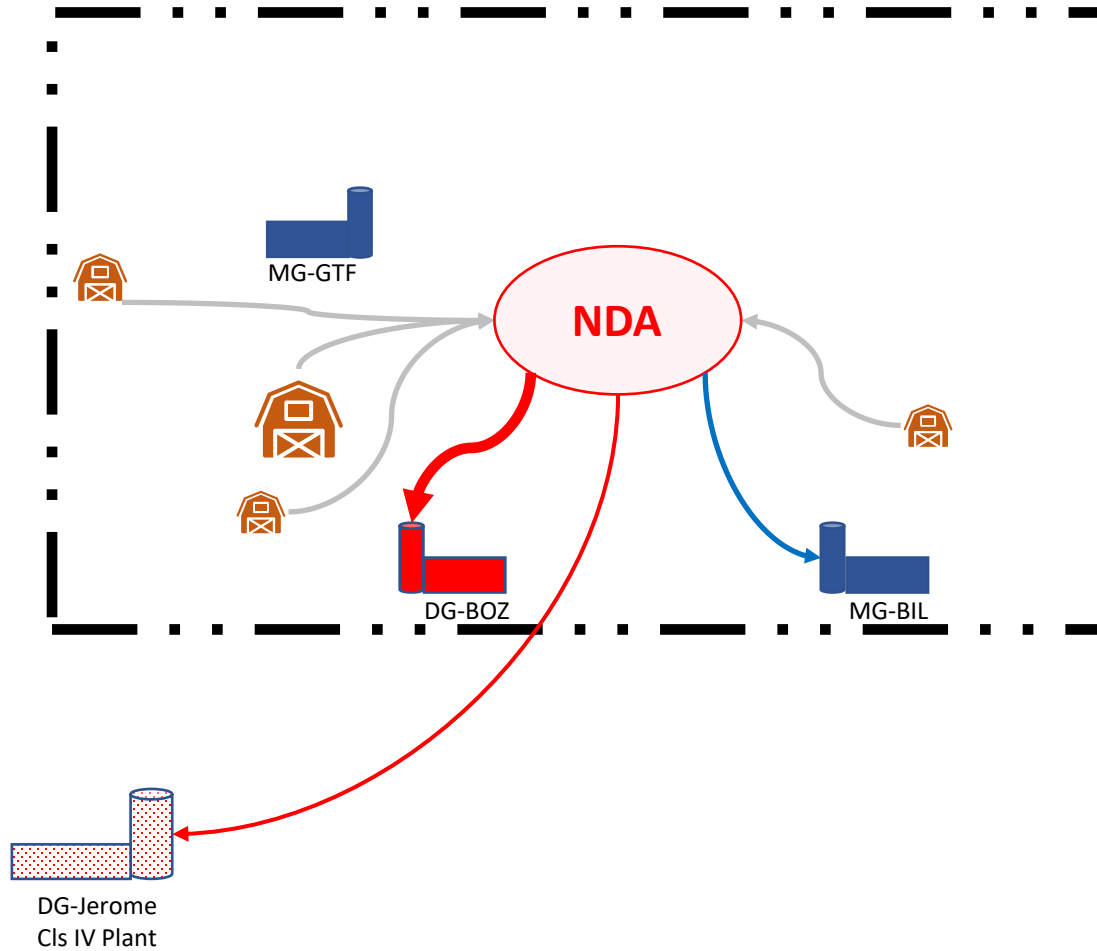


Darigold-Jerome

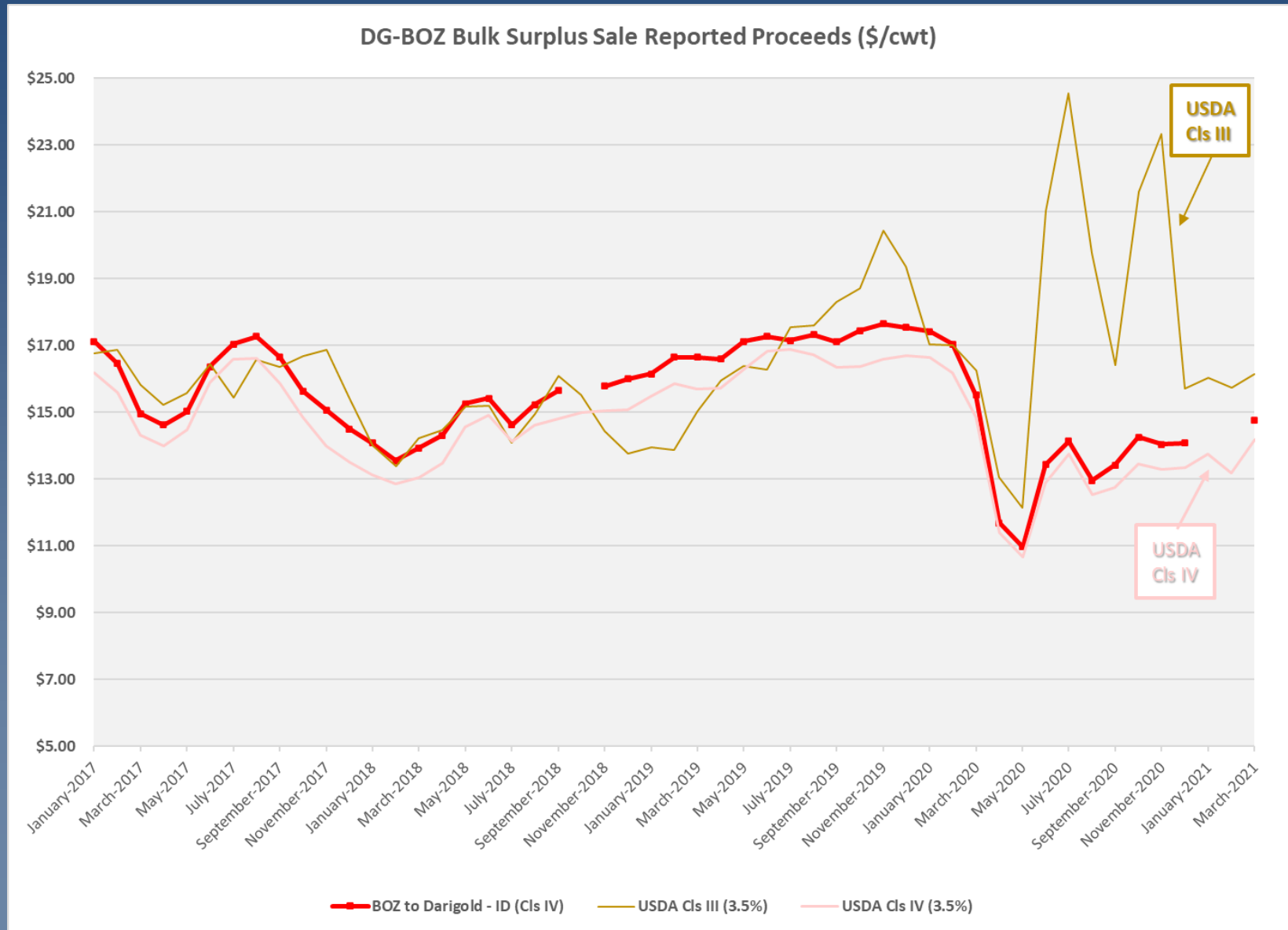
Flow of Darigold-Bozeman Surplus Milk



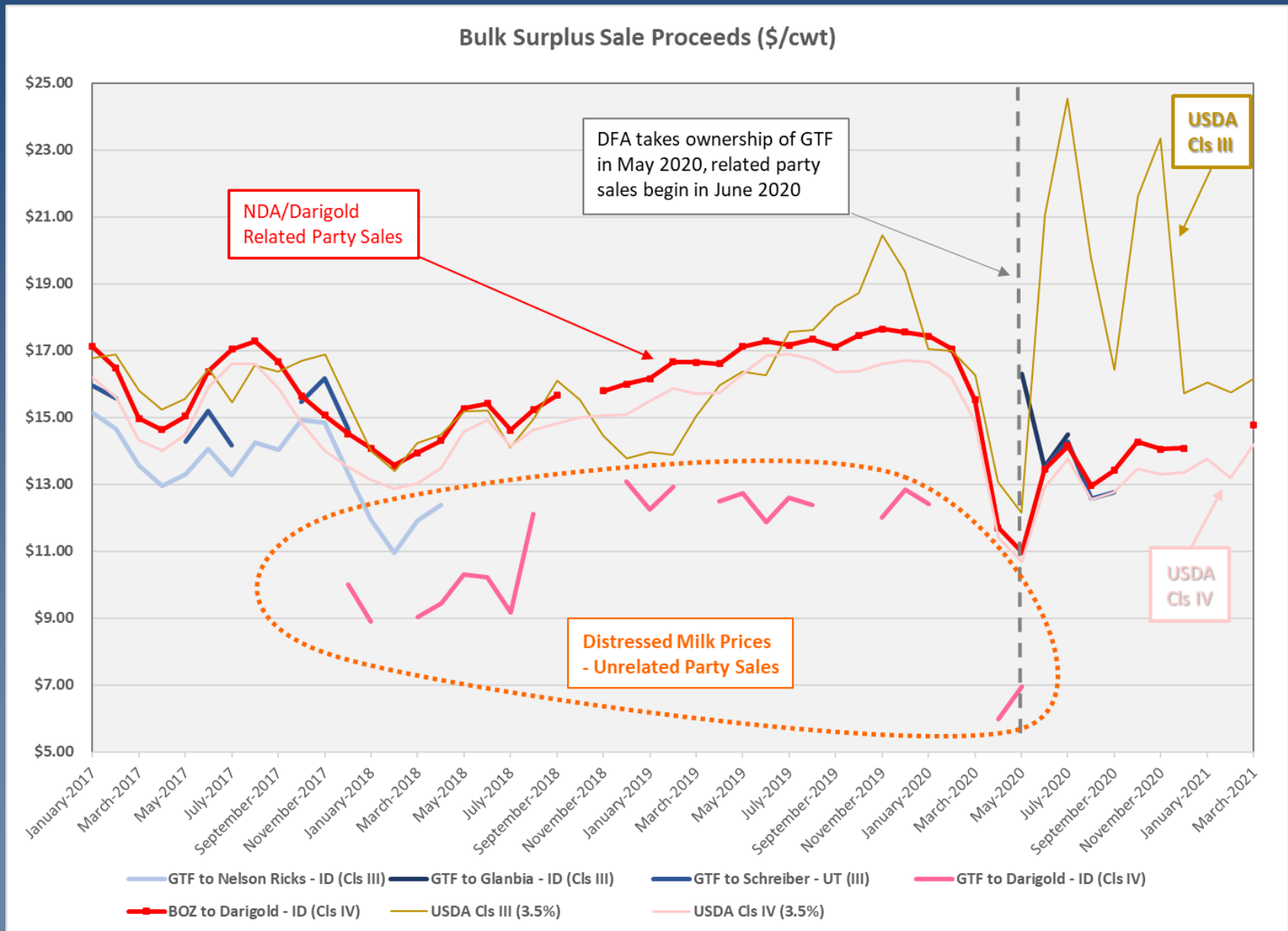
Sales of Darigold-Bozeman Surplus Milk



Analysis of Surplus Milk Sold in Bulk to Related Entities



Analysis of Surplus Milk Sold in Bulk to Related Entities



Sale of Meadow Gold-GF Surplus Milk

(before May 2020)

Producers

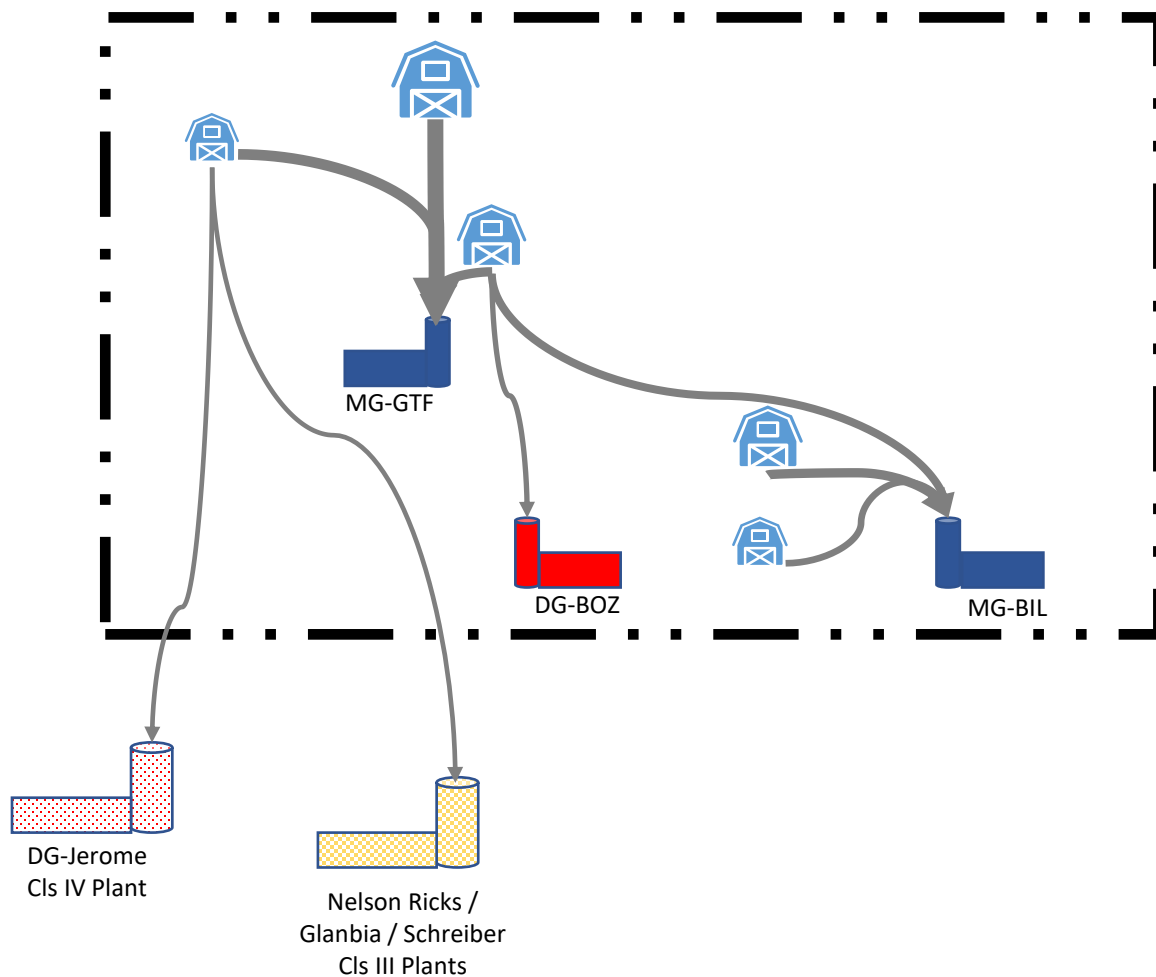


Dean Foods/Meadow Gold-GF

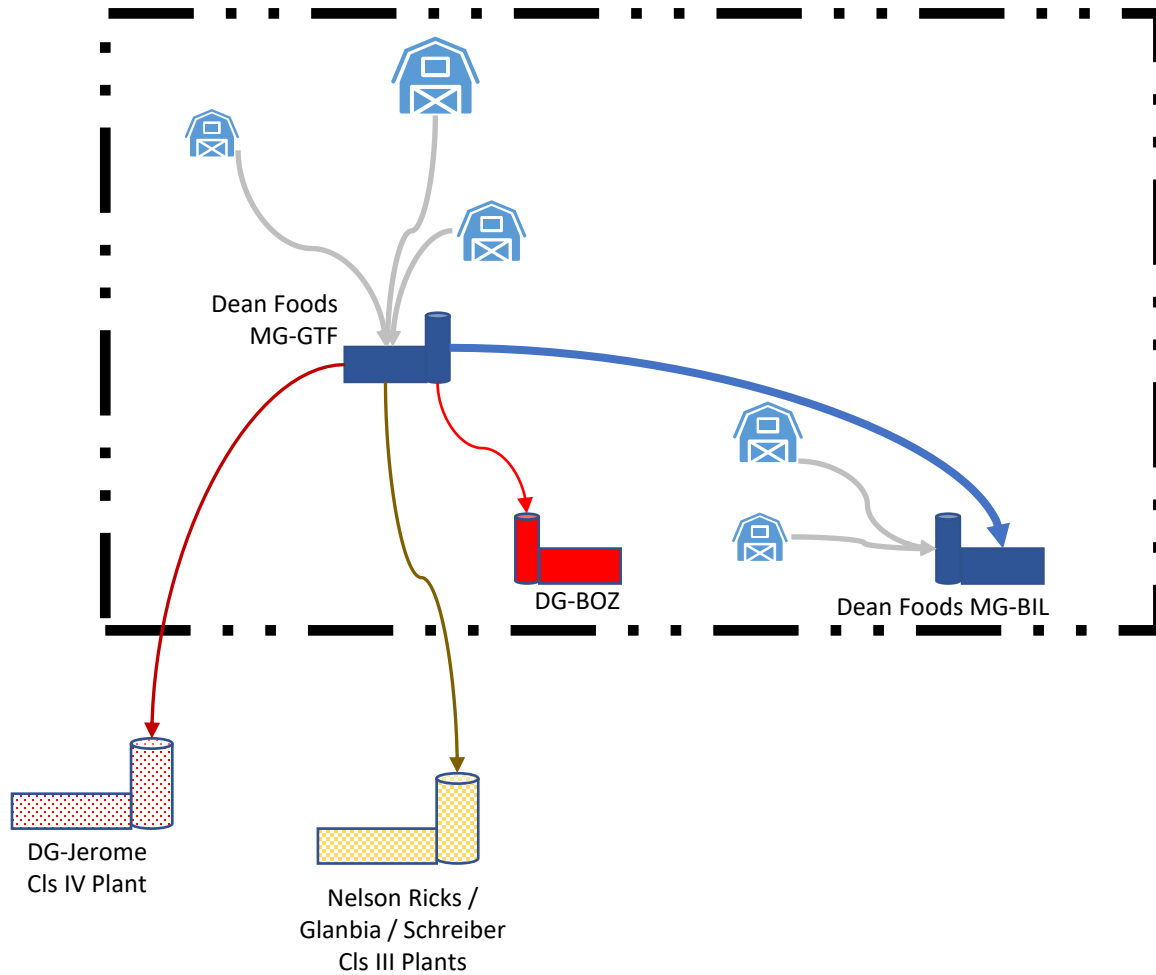


Out-of-State Plants

Flow of Meadow Gold-Great Falls Surplus Milk (before May 2020)



Sales of Meadow Gold-Great Falls Surplus Milk (before June 2020)



May 2020

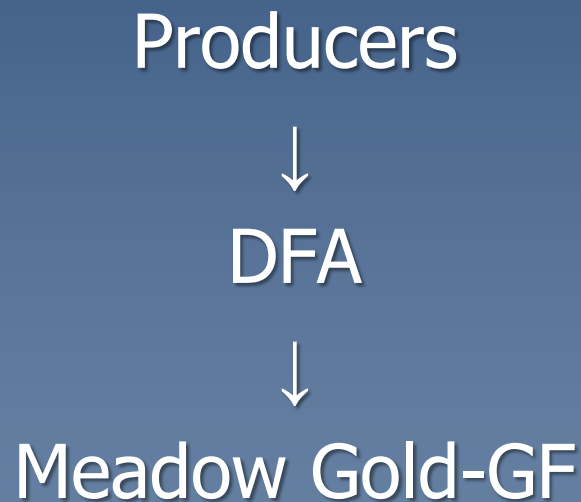
Dairy Farmers of America (DFA) owns DFA Dairy Brands Fluid, LLC (which operates the Meadow Gold-GF plant)

DFA begins marketing Meadow Gold-GF's surplus milk

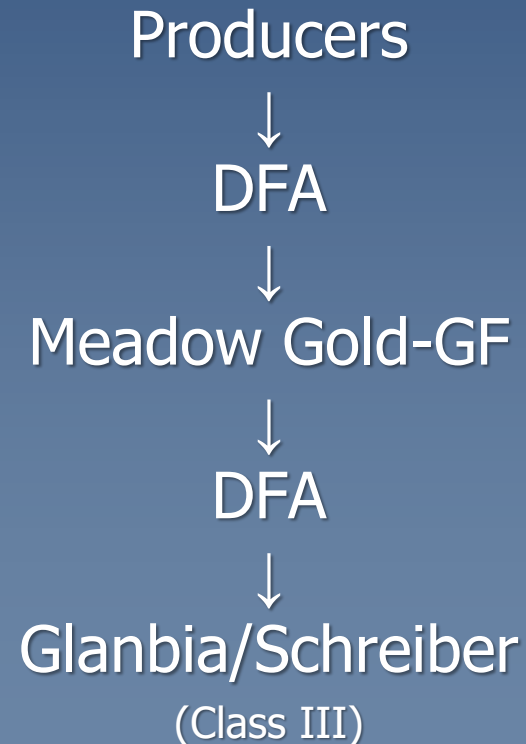
Sale of Meadow Gold-GF Milk

(May 2020)

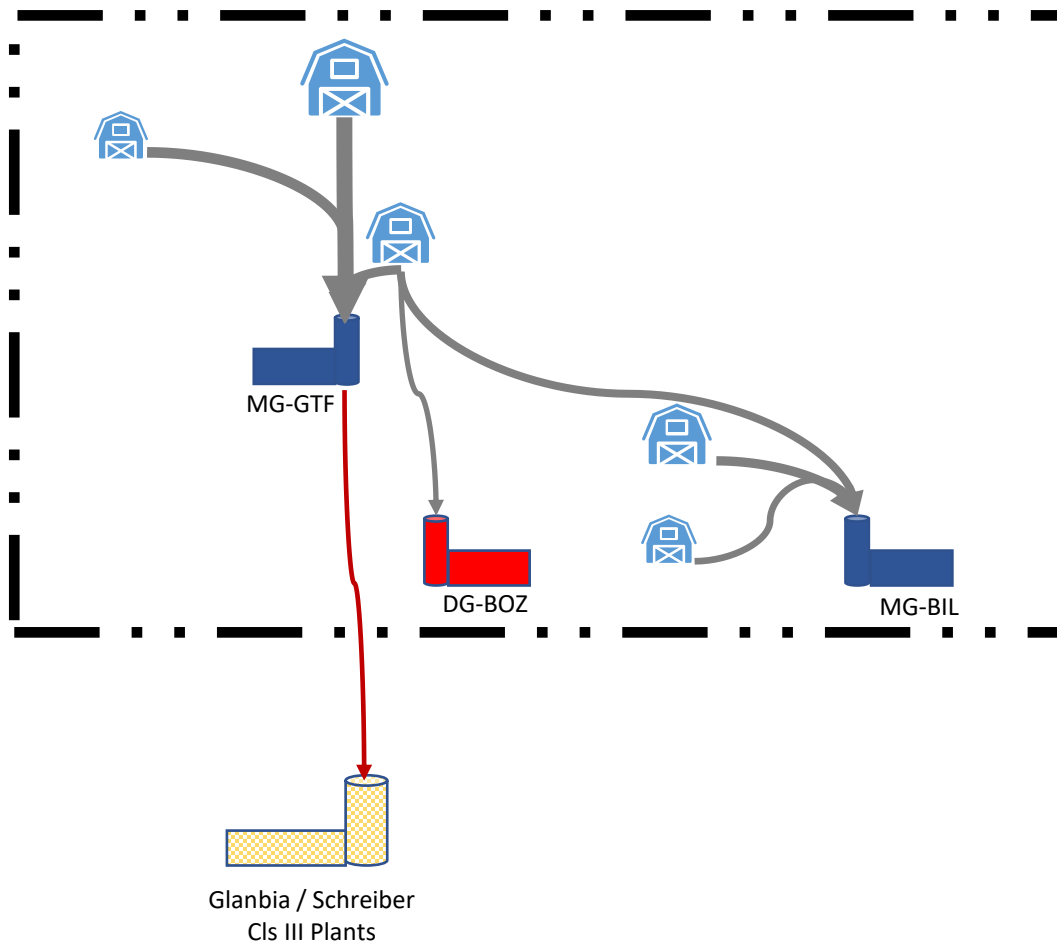
Non-Surplus Milk



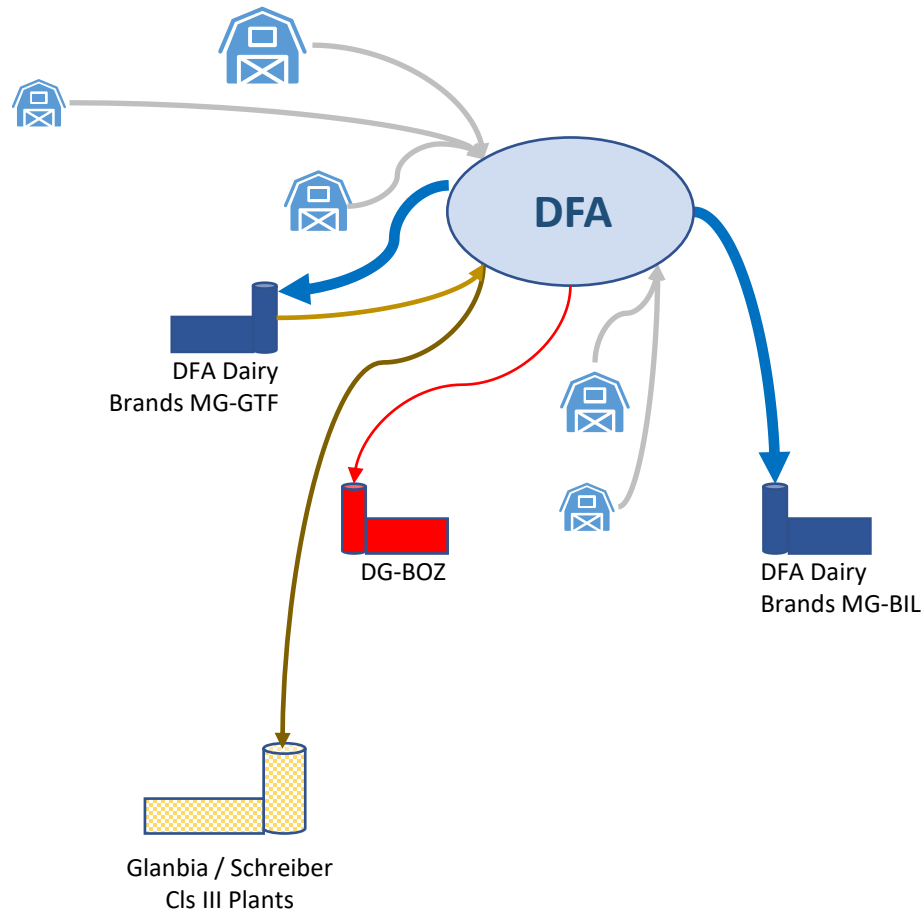
Surplus Milk



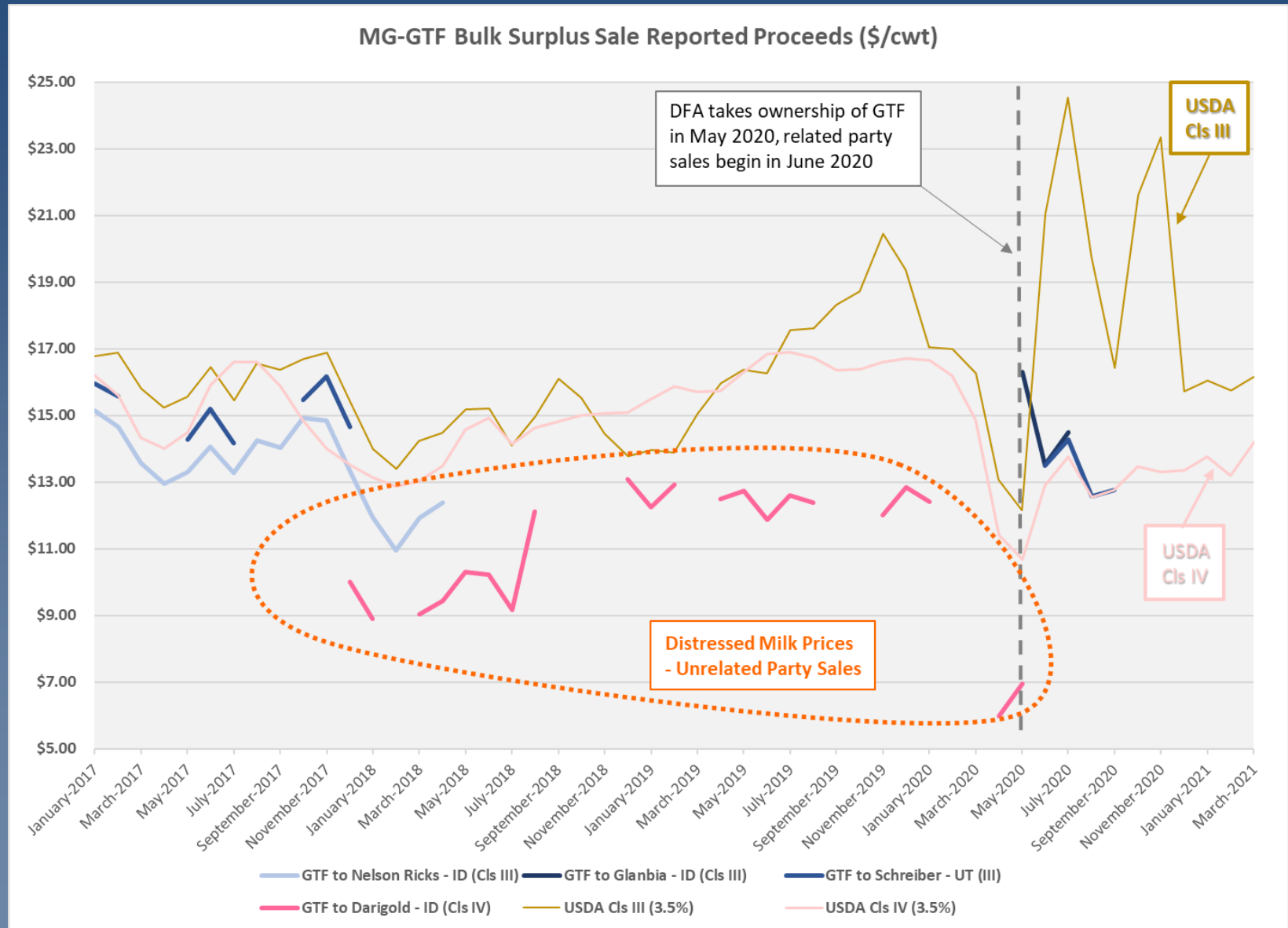
Flow of Meadow Gold-Great Falls Surplus Milk (May 2020 and after)



Sales of Meadow Gold-Great Falls Surplus Milk (June 2020 and after)

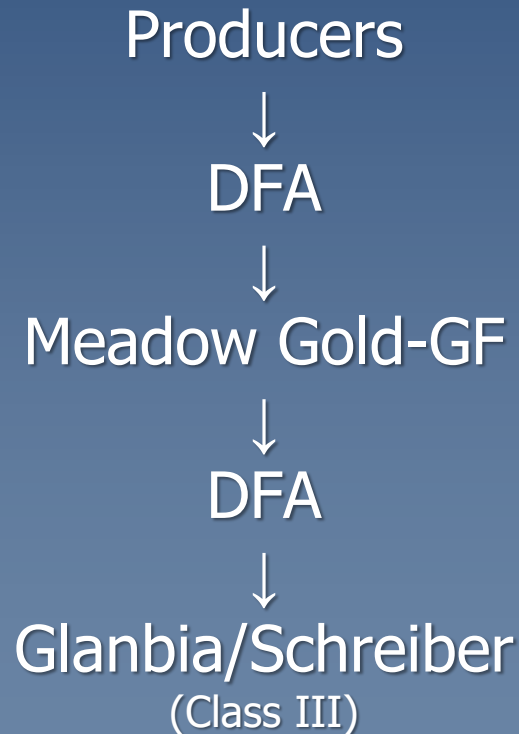


Analysis of Surplus Milk Sold in Bulk to Related Entities



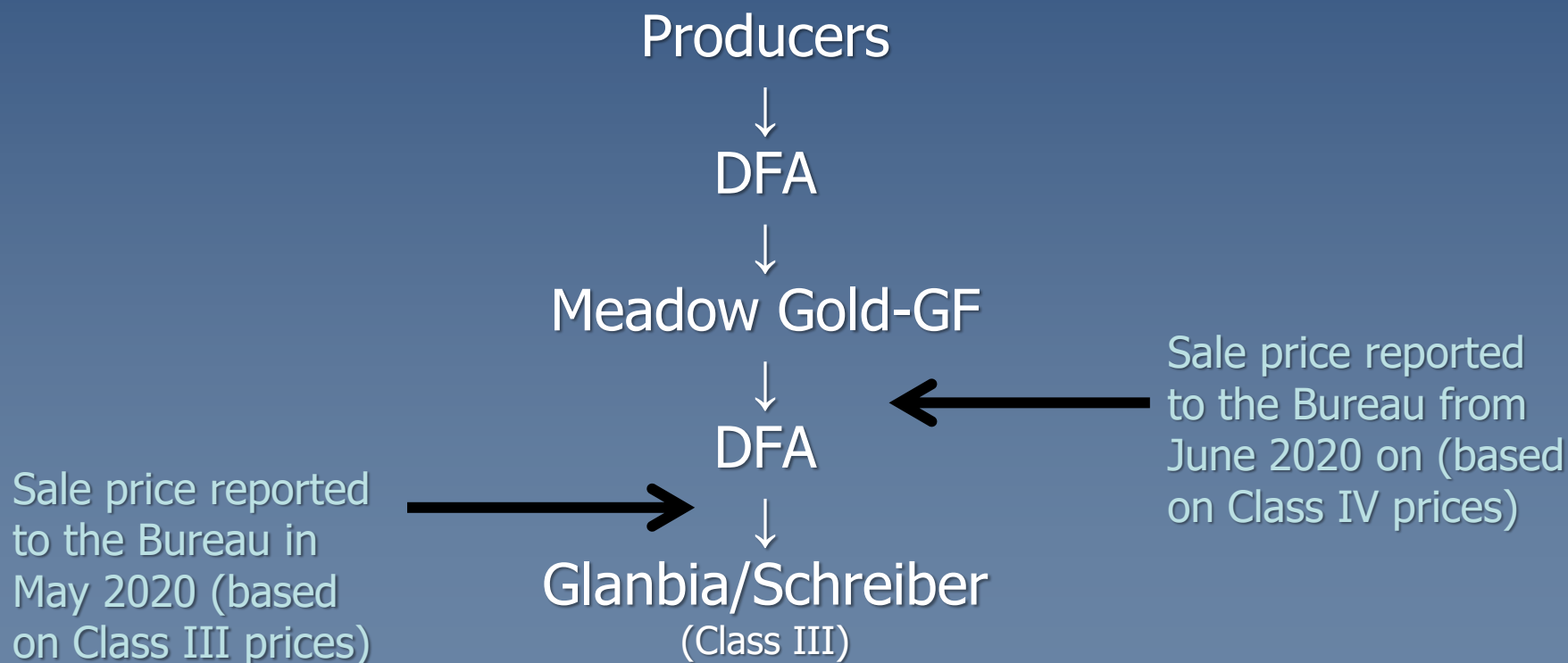
Sale of Meadow Gold-GF Surplus Milk

(after May 2020)

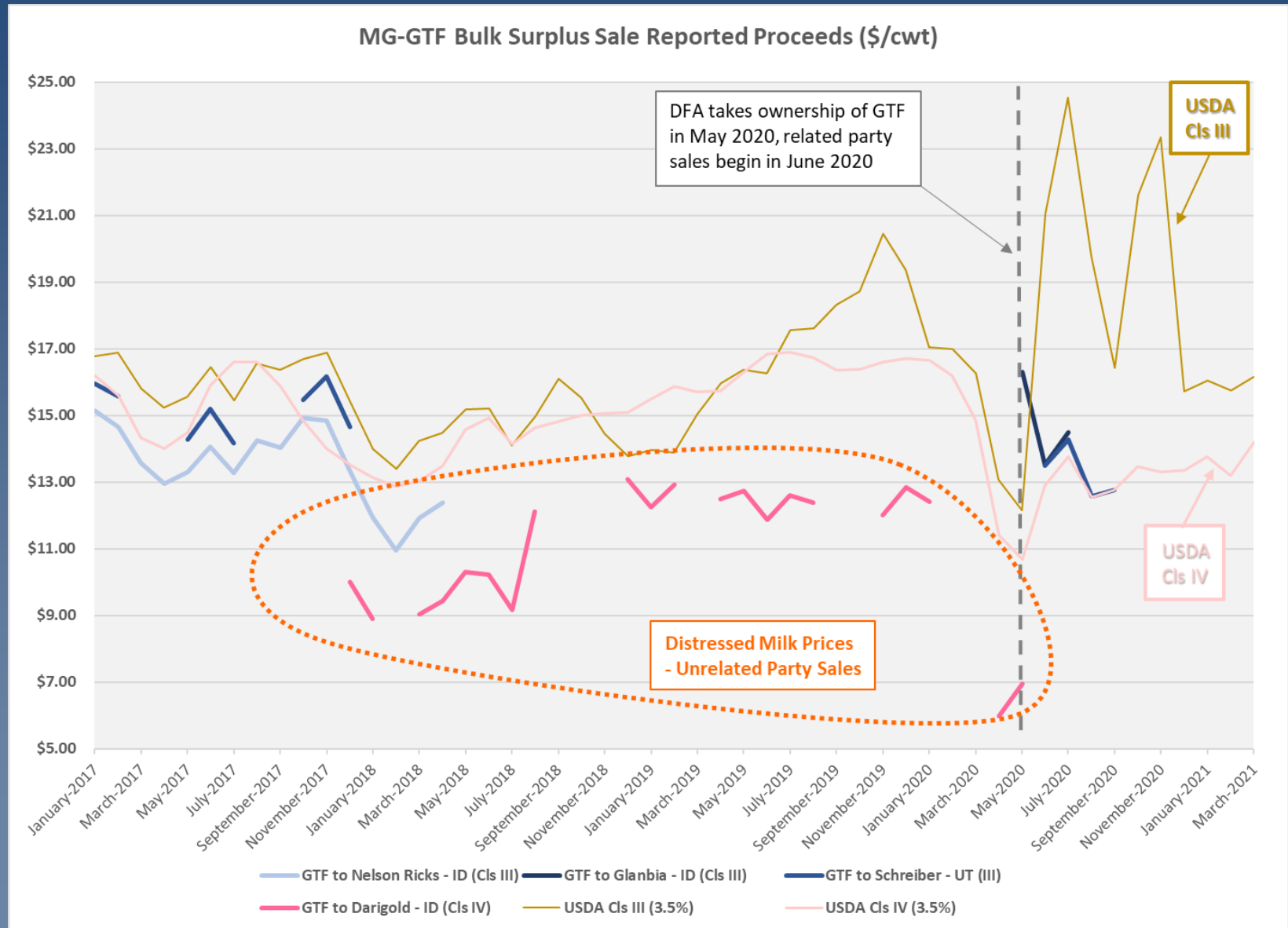


Sale of Meadow Gold-GF Surplus Milk

(after May 2020)



Analysis of Surplus Milk Sold in Bulk to Related Entities



Areas of (Potential) Concern

Sales to related entities

NDA → Darigold-Jerome

Meadow Gold-GF → DFA

Surplus sale price DFA reports to Bureau

Based on Class IV prices when milk is being used in Class III plants

Sales to Related Entities - Considerations

- Surplus milk is to be sold in a manner that is economically advantageous to producers and that all losses and gains are shared equally by producers. ARM 32.24.523(1)
- Nothing in the law prohibits outright prohibits sales between related entities
- ARM 32.24.523(2) allows the producer committee to take over the marketing of surplus milk
- ARM 32.24.470(1)(d) prohibits “[t]he extension to certain customers of special prices or services not available to all customers who purchase milk of like quantity under like terms and conditions.
- NDA has been selling surplus milk to Darigold-Jerome since at least 2014, based on the USDA Class IV price

NDA Related-Entity Sales

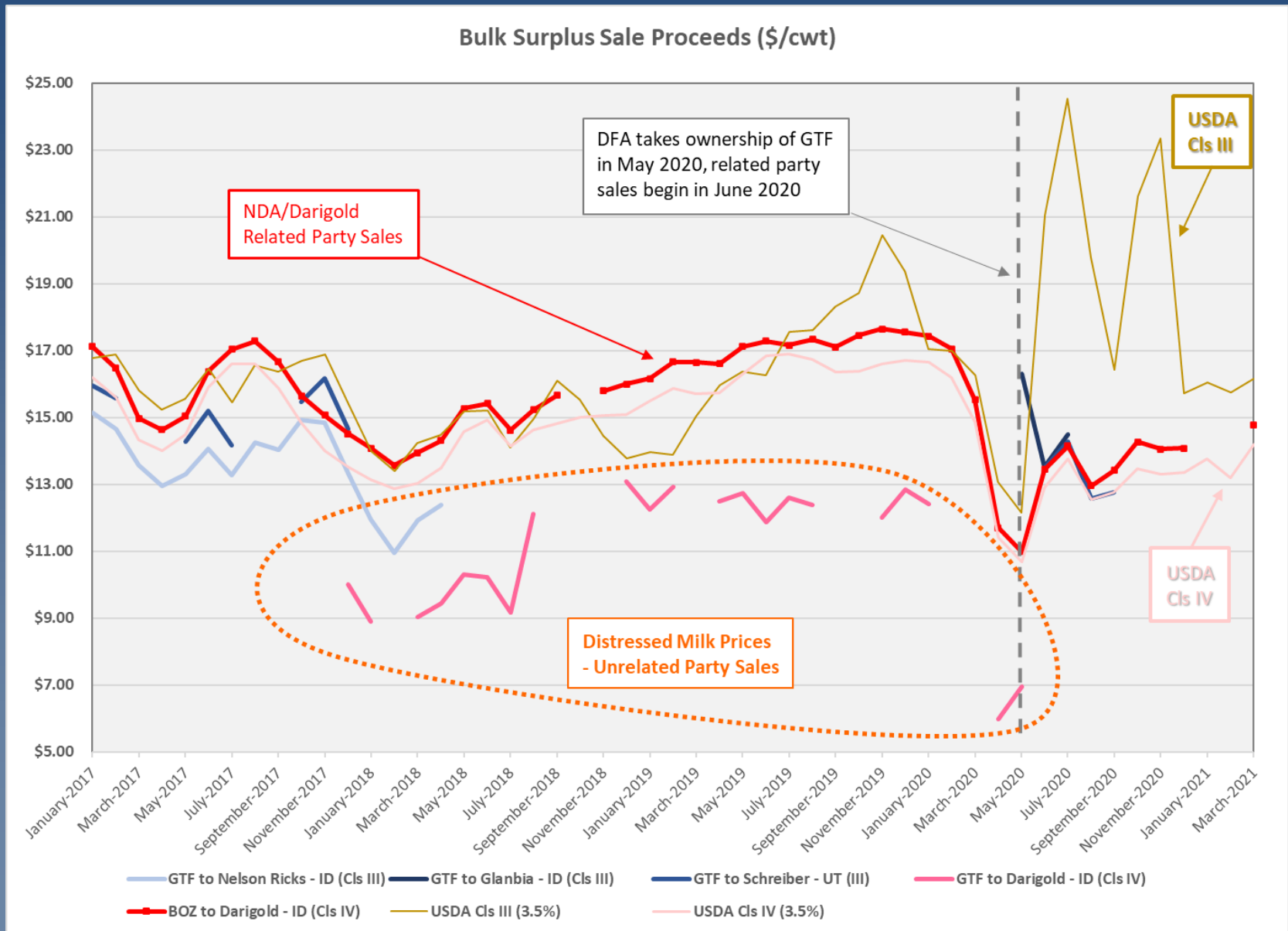
Point

- NDA has complete control over the surplus milk price that is reported to the Bureau

Counterpoints

- Bureau does not have the authority to dictate the price of milk sold out-of-state
- Idaho milk market is unregulated
- NDA has been selling surplus milk to Darigold-Jerome since at least 2014
- Reported prices (Class IV) match the use the milk is being put to (Class IV)
- Prices paid to NDA are higher than those paid to Meadow Gold-GF
- No brokerage fees for sales between related entities

Analysis of Surplus Milk Sold in Bulk to Related Entities



DFA Related-Entity Sales

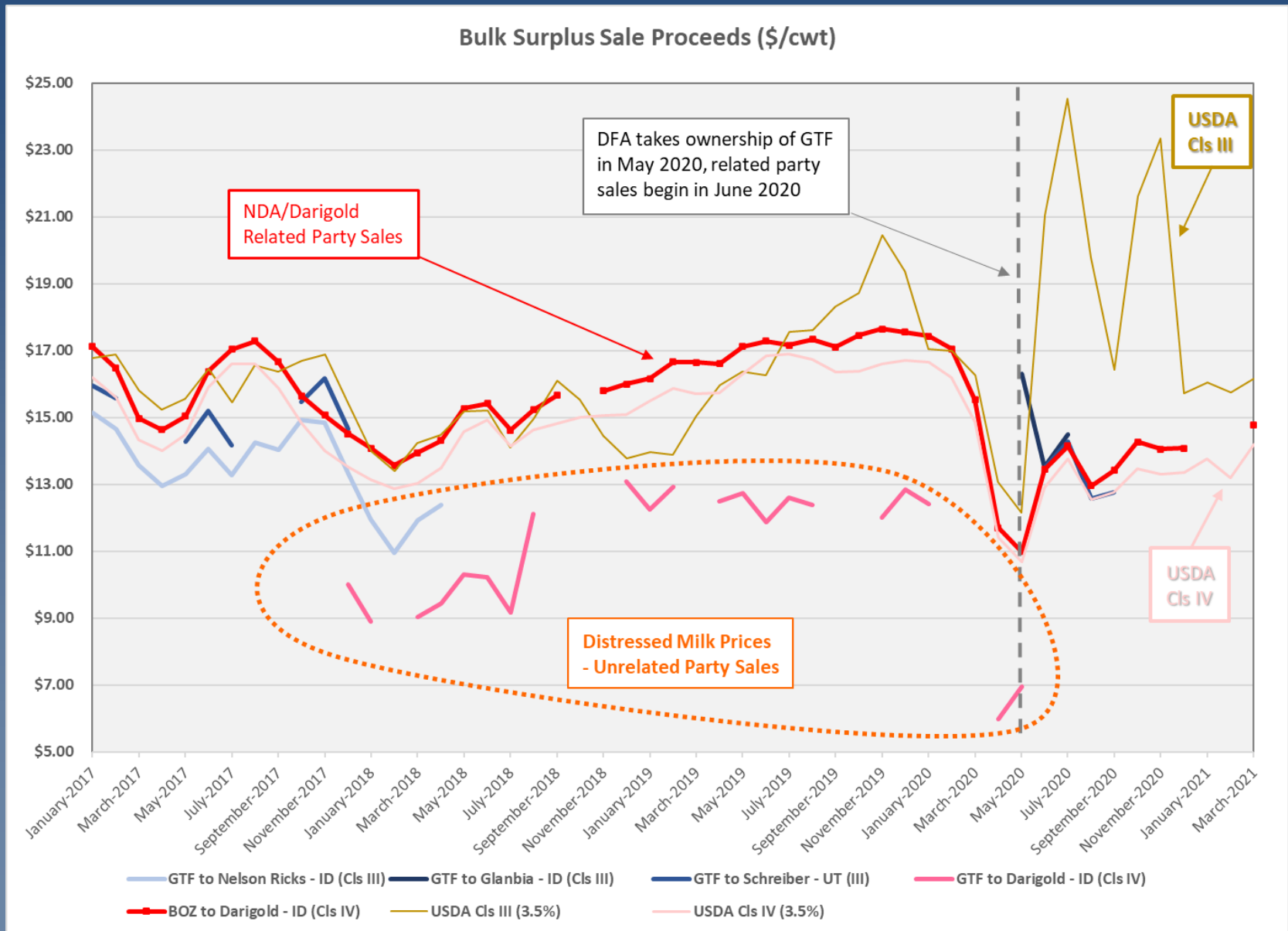
Point

- DFA has structured a sale between Meadow Gold-GF and DFA that allows it to report one price to the Bureau but collect another price from Glanbia/Schreiber
- DFA is reporting Class IV prices when milk is used for Class III purposes

Counterpoints

- Bureau does not have the authority to dictate the price of milk sold out-of-state
- Utah and Idaho markets (where milk ends up) are unregulated
- NDA has been making related entity sales for years
- The price DFA receives from Glanbia/Schreiber is not reflective of what surplus milk would yield on the open market (*see, e.g.,* prices Darigold-Jerome paid MG-GF)
- Historically, Class III and Class IV prices are not drastically different
- No brokerage fees for sales between related entities
- Freight costs have decreased under DFA; freight would be higher if DFA sent milk to Class IV plants further away

Analysis of Surplus Milk Sold in Bulk to Related Entities



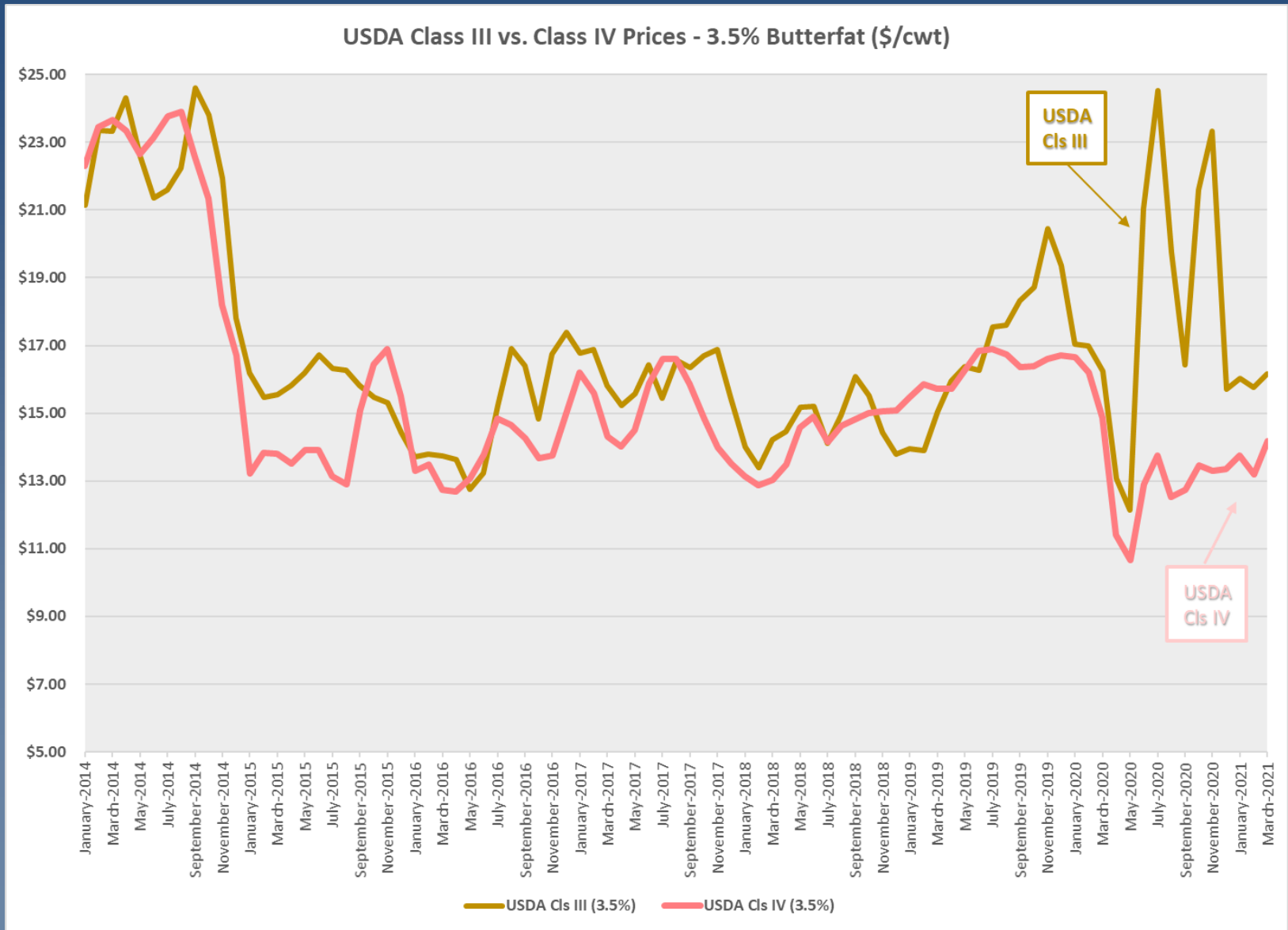
Bulk Surplus Sale Proceeds (\$/cwt)

DFA takes ownership of GTF in May 2020, related party sales begin in June 2020

Legend:

- GTF to Nelson Ricks - ID (Cls III)
- GTF to Glanbia - ID (Cls III)
- GTF to Schreiber - UT (III)
- GTF to Darigold - ID (Cls IV)
- BOZ to Darigold - ID (Cls IV)
- USDA CIs III (3.5%)
- USDA CIs IV (3.5%)

Analysis of Surplus Milk Sold in Bulk to Related Entities



Considerations for the Board

1. Is there an issue that needs Board attention?
 - a. Is surplus milk being marketed and sold in a manner that is not economically advantageous to pool producers?
 - b. Is the surplus milk being marketed and sold in a manner in which all the gains and losses are not shared by the pool producers?
 - c. Is Meadow Gold-Great Falls giving DFA a special price for surplus milk that is not available to all customers who purchase surplus milk of like quantity under like terms and conditions?
2. What action can the Board take?
3. What action should the Board take?