

# Unrest in Golden State: Challenge to \$1.1 Bil. Quota System

## Petition to Terminate CA Quota Program Circulating

by Pete Hardin

Sources in California report that a nucleus of dairy producers has started circulating a petition seeking signatures of state dairy producers in an effort to force state officials to have another referendum on the Quota Implementation Program (QIP).

Rules at the California Department of Food and Agriculture (CDFA) specify that the QIP may be subject to review if a total of 25% of active dairy farmers sign such a petition. The QIP was implemented in 2018, in advance of California's exiting state milk price regulation and joining the federal milk order program.

Effective November 1, 2018, USDA assumed regulatory responsibility for pricing California's Grade A milk. California's historic milk quota program had to be revised, in the shift from state to federal milk price regulation. Under the QIP, all Grade A milk produced in California will be assessed a fee of \$.38/cwt. to cover monthly costs of payments to producers who own quota. Payments to quota holders total as much as \$1.70/cwt. About half the producers in California have zero quota. The estimated value of all quota is approximately \$1.1 billion.

### Question: Please describe California's historic Class 1 Quota program?

Quota has been part of California's state milk pricing system for more than 40 years. Owning Quota entitles producers to as much as \$1.70 per cwt. of additional income.

The Quota program was an inducement to encourage the state's dairy producers to vote for the state pooling system in 1969. Before that, there was no sharing of milk sale revenue. Milk pricing was handled by individual contracts. Today, the entire state pool funds the Quota payout as a redistribution of milk sale revenues. Quota is no longer funded only by Class 1 revenues, as some believe.

Lon Hatamiya, MBA, JD prepared an independent analysis of Quota in 2015 called "The Economic Importance of the California Dairy Quota Program" It gives a good overview of the Quota program since its inception. But the economics Hatamiya presents is very skewed. The economic benefit of quota for the state of California, doesn't take into account the dairyman going out of business by funding Quota.

### What is the estimated total value?

California Department of Food and Agriculture (CDFA) has issued 2,215,978 pounds of quota Solids Not Fat (SNF). Based on a selling price of \$525 per pound of SNF would give you a value of \$1,164,000,000. Though today's price would be really difficult to come up with a true price.

Quota has sold in the last three months between \$470 and \$520 according to the CDFA, but some of that was sold on terms. Depending on what the terms were, you could determine the cash price of the Quota. CDFA doesn't report terms. Recently 10,000 pounds was offered up for sale to a broker who handles a lot of Quota sales. The seller wants to sell today for cash, and if he can't get the quoted price of \$500, he requested that the broker at least get him some bids no matter how low they were. To this day an offer has not been provided, which would give quota a zero value. There has always been this special handling of selling quota, the buyers are reluctant to offer a low price for quota, because it would affect their value of their own quota. For instance if someone offered \$100 that would set the new price for all of the quota and the other quota holders would be outraged at this development.

To answer your question on it, the total value of quota today would be \$0 to \$1.1 billion – probably somewhere in between.

### How many of your state's current dairy producers own Class 1 quota?

There are 1,253 dairies in California:  
537 dairies have zero quota.  
291 dairies that have less than 22% quota (they put more into the program than they receive.)  
425 dairies that have more than 22% quota.

### Question: Please explain the Quota Implementa-

Producers circulating the petition assert that the \$.38/cwt. fee assessed on all Grade A milk means a net cash-flow loss for about two-thirds of all California dairy farmers.

Logistics for circulating petitions are in place. Interested California producers may obtain a petition by calling a toll-free number: 800-478-6774 (800-4STOPQI).

Petitions must be sent to:  
Craig Gordon  
100 North Akres St.  
P.O. Box 7706  
Visalia, CA 93290-7706

The producers behind the petition are putting together a website, but that information is not available at press time.

CDFA administrative rules allow for a 90-day period to collect an adequate number of signatures, from the time the petitions start circulating. That puts an early February deadline on the project.

**The accompanying article is a question-and-answer interview with Craig Gordon, a California dairy producer, hay dealer, and citrus grower. Mr. Gordon is based in Chino.**

### tion Program and how it came to be in late 2017.

In February of 2017 the USDA published its recommended decision for the establishment of a California Federal Milk Marketing Order (CA FMMO). The recommended decision does not allow for Quota to be incorporated in the pricing and pooling provisions of a CA FMMO. It would necessitate quota to operate independently of a CA FMMO as a stand-alone program, administered by the California Department of Food and Agriculture. Secretary Karen Ross charged the Producer Review Board with developing a recommendation outlining the provisions for a stand-alone producer funded Quota program. The board conducted four public meetings between May and September of 2017 and submitted its recommendations to the Secretary. The dairy producers voted for the Quota Implementation Program (QIP) through a referendum process. The QIP will become effective now that they voted in the CA FMMO.

### Question: You are a member of the California Quota Review Board. What is that board's function?

Yes, I am a member of the Producer Review Board. Our function is to advise the Secretary in the administration of the Milk Pooling Plan for Market Milk. When the QIP becomes effective November 1, 2018 we will then be advising on the implementation of the QIP. All meetings are open to the public.

### How much Class 1 Quota do you own?

I own zero Quota; I sold it after the QIP referendum passed.

### What percentage is that amount of your total monthly milk sales?

It was only 8.6% of my milk sales, and I got just a few dollars short of \$700,000.

### Question: It was estimated that \$.38 per hundredweight would be deducted from all milk pooled in the new California federal milk order to fund payments to Class 1 Quota holders. What's the technical name for that extraction of funds from the monthly producer revenue pool?

It is a Quota assessment, and on the dairyman's check it will say Quota Revenue.

### Is that \$.38 per cwt. figure a fixed amount, or will it vary by month, depending upon how much total milk is pooled?

The Secretary shall review and/or adjust the quota premium assessment rate as needed. They are starting out with the \$.38 but we were shown charts showing, that it could be as high as \$ .60 depending on the milk supply.

### Question: How much milk do your dairy operations produce on a monthly basis?

7,686,000 lbs.

### What is your estimated monthly net cost if the monthly deduction is \$.38 per cwt.?

76,860 cwt. or \$ 29,206.80

### Question: You claim that producers holding Class 1 Quota that totals 22% (or less) of their total

monthly milk sales will end up losing money, when factoring in the \$.38 per cwt. extracted to fund payments to Quota holders? Please explain.

The quota holders who hold 22% or less of quota would pay more than they would receive. This was given to our Board by the staff of the CDFA. Example: Take our dairy producing 76,860 per month. If we generated 22% of that 76,860 at a return of \$ 1.70 per pound of milk – at \$1.70 it would return \$28,745. But you are being assessed \$ .38 on all of your milk which would be an assessment of (\$ 29,206) a loss of (\$461.80).

### Question: Your state law provides for process by which 25% or more of state dairy producers may petition the California Department of Food & Agriculture to eliminate the Class 1 Quota system. Could you please explain how that works and what CDFA's obligation to administratively respond to such a petition from 25% or more of state dairy farmers?

Under Article 11. Administration Section 1103: Upon receipt of a petition signed by at least 25 percent of market milk producers regarding the amendment or **termination of this Plan**, the Secretary shall convene the Producer Review Board to review the merits of the petition and make a recommendation to the Secretary. If the Secretary finds that the Plan no longer tends to effectuate the purpose intended, termination shall be submitted for referendum in the same manner as provided for its initial approval. Then there would be another referendum like the one that was held last year. If everybody came out and voted along their economic interests of 22% or less ownership of quota, (they have an overwhelming majority), Quota would be terminated. There isn't any mechanism in the QIP for compensating the quota holders.

### Question: You contend that roughly two-thirds of all California dairy producers will lose money on the Class 1 Quota program at the \$.38/cwt. deduction level. Please explain.

828 dairymen own less than 22% and only 425 dairies have quota more than 22%..

### Question: Is there a petition actively being prepared? How many concerned dairy farmers obtain a copy?

I have not seen an actual petition. I was contacted by a person who wanted to be anonymous, and he asked me if he got the necessary signatures on a petition to terminate Quota, would I submit a petition to the Producer Review Board.

### Question: If the Class 1 Quota program were terminated, who would be the "winners" and "losers" on a monthly cash flow basis?

The winners would be those who don't own more than 22% Quota, the losers would be those who own more than 22% Quota.

### Question: What are the implications to the banking community that has extended credit to dairy producers who have used their Class 1 Quota holdings as collateral for indebtedness?

I can't speak for the banking industry. My guess is; it would be treated just like they treat our dairies when the value of cows drops from \$2,000 a cow to \$1,100. You lose equity and your income would be \$1.70 a cwt. less income on your P&L. Quota isn't the only investment that dairymen own. When beef prices go down our beef checks reflect that new low pricing. There have been numerous, recently-built state-of-the-art dairies that have been sold at auction - not to other dairyman but to tree growers.

### Question: Since Class 1 Quota may be bought/sold, what is a good estimate of current value?

If a Quota Broker can't give a value or an offer today, you would have to conclude \$0.

### Question: Can California's federal milk order survive, if the petition process were to do away with Class 1 Quota?

Of course. The CA FMMO doesn't have Quota in its calculations. The order works without Quota, essentially quota as we knew it - has been replaced by the CA FMMO. What we have is an assessment that will be called Quota Revenue and that will show up on every Grade A producers check as a deduction for sole purpose of paying a premium to holders of quota. The holders of Quota will be extracting over \$12,000,000 a month from their fellow dairyman for as long as this QIP is in place.