



May 27, 2008

DIRECTIVE NO. 2008-100

CONVERSION TO A SINGLE QUOTA SYSTEM

Pursuant to sections 26 and 27 of the *Marketing of Agricultural Products Act* and section 9 of the *Alberta Milk Marketing Regulation*, Alberta Milk converts to a single quota policy and introduces applicable transition procedures.

Definitions

1. The definitions in the *Alberta Milk Marketing Regulation* apply to the interpretation of this directive.
2. “Total Production Quota” is the name designated to the new single quota that replaces *fluid quota* and *market share quota*.
3. “net revenue neutral” is the model chosen to provide the conversion formula.
4. “average production costs” are equal to the total variable costs as determined in the provincial Dairy Cost Study.
5. “marginal production costs” are determined using the provincial Dairy Cost Study and are applied to changes of production. These costs are the assumed costs that are either saved or incurred by producers who will see a production change.

Procedures

6. The net revenue neutral formula seeks to convert the current dual quota system into a single quota system in a manner that is most equitable to all producers. The model operates on the primary goal that the change in producers’ expected net revenues under a single quota and their current net revenues under the dual quota system are minimized or eliminated. This is accomplished by allocating sufficient Total Production Quota to each producer so that, if they produce to that quota, their net revenue is approximately the same as it was prior to the conversion.

As a convergence of milk prices between producers is the result of this transition, a reallocation of quota serves as compensation for the change. Intuitively, a producer who will receive a lower average price for a hectolitre of raw milk than they previously received will need to produce more milk to maintain their net revenue and will therefore be allocated a larger share of the total quota than they were previously allocated. Similarly, a producer who will receive a higher average price for a hectolitre of raw milk will be allocated a lesser share of the total quota than they were previously allocated.

To perform the conversion, the net revenue neutral formula is applied to each producer based on their individual quota allocations and milk component tests. Using current prices and payment methodologies, each producer’s annual gross revenue is estimated. Each producer’s annual net revenue is then calculated by subtracting the average production costs from their estimated gross revenue.

Blended prices for butterfat, protein, and lactose and other solids are also calculated based on total revenues and sales of all classes in the province. By applying these blended prices with the producer’s current production of components and again subtracting the average production costs, the producer’s expected annual net revenue under a single quota is calculated.

The difference between the expected net revenue under a single quota and the producer's current dual quota net revenue is then used to determine what change in quota (therefore, change in production) is necessary to eliminate the difference. This change in revenue is converted into equivalent production and marginal production costs are applied. The costs applied to a producer who is receiving a higher average milk price will be equal to average production costs less producer fees and total labour. This is assumed to be the costs he would save by decreasing production to meet his reduced quota allocations. The marginal costs applied to a producer who is receiving a lower average milk price will be equal to average production costs less producer fees. This is assumed to be the costs he would incur by increasing production to meet his larger quota allocations.

Transition to a single quota is calculated using a net revenue neutral model based on the following:

- Current producer quota allocation.
- Average producer components over the 2007 calendar year.
- Average industrial prices for the dairy year 2007/08 including year-end refund.
- Current fluid price as of July 31, 2008.
- Average fluid utilization for the dairy year 2007/08.
- Total variable production costs from the 2007 Dairy Cost Study.

Transition Provisions

7. Producers that are highly impacted resulted in a change from the original marginal production costs applied to the production change. Marginal production costs applied to producers facing reduced quota allocations have been lowered and marginal production costs applied to producers receiving additional quota have been increased. The effect of this change is that quota previously unallocated by the original formula is now distributed to all producers but more quota is proportionally distributed to the highly impacted producers.
8. The 99-101% rule will be changed to include all milk for the 2007-08 dairy year. This policy change is in response to producers who have asked for greater production flexibility through the transition period.
9. A quota lease exchange will be implemented to help shift the large volume of quota leases expected in 2008-09.

Effective Date

10. This Directive comes into force August 1, 2008.

Bill Feenstra, Chairman

Mike Southwood, General Manager

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