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## WISCONSIN LEGISLATIVE COUNCIL STAFF MEMORANDUM

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DATE: March 5, 1997  
TO: REPRESENTATIVE ALVIN OTT *Al Ott*  
FROM: David J. Stute, Director  
SUBJECT: Responses--Various Questions Relating to Milk Prices

This memorandum, prepared at the request of Kim Markham of your staff, addresses several questions which you and she have raised within the context of the announcement on Friday, February 28, 1997, that the Federal Commodity Futures Trading Commission (CFTC) had newly approved the trading of basic formula price (BFP) milk futures and options contracts on the Coffee, Sugar and Cocoa Exchange (CSCE). The remainder of this memorandum consists of the questions which have been posed and responses thereto.

**1. In the materials distributed by the Governor's press office relating to the approval of trading in BFP milk futures, in referring to the National Cheese Exchange (NCE), it is stated that "... the trading activity is transparent ..." What does this mean?**

The statement containing the reference to transparency of trading activity on the NCE is taken from an 18-page CFTC report on the NCE, apparently done in connection with the application of the CSCE for approval to commence trading in milk futures. Within the context of the report, "transparency" of trading on the NCE refers to the manner of trading. Specifically, on the NCE, bids or offers to buy or sell cheese are made through open outcry by an NCE member who is on the trading floor during a trading period. Once made, that bid or offer is recorded on a large board in front of the trading floor. The information recorded is the identity of the member making the bid or offer, the form of the cheese (barrels or blocks), the number of carloads and the price. If that bid or offer is "covered" (i.e., accepted) by another member's outcry, the two participants have agreed to engage in a cash transaction for the exchange of the particular quantity of cheese at the indicated price. Further, records of the trade are kept by the NCE by voice recording and by a representative of the U.S. Department of Agriculture's (USDA) Agricultural Marketing Service, who is present at every trading session and who maintains an electronic record of bids, offers and sales.

It is this above-described activity which is characterized as "transparent." Trades are made openly by identifiable persons and a record is made of each transaction. From the

perspective of the CFTC (which is that of a regulator), trading is both visible and verifiable. Thus, it is characterized as "transparent" (i.e., said another way, what you see is what you get).

**2. What is the relationship of the CFTC's approval of milk futures and options trading on the CSCE to the NCE? Will the CFTC now monitor NCE trading?**

The CSCE trading approved by the CFTC permits the trading of cash-settled futures contracts for milk and options for such contracts. These contracts are transactions for the purchase or sale of a standard quantity of milk, at a stated price, for delivery at a later time. Being cash-settled, these contracts can be terminated prior to the date of delivery by execution of an opposite, offsetting transaction in which any changes in price which have occurred in the interim are settled in cash, rather than through completion of a contract by actual delivery of the milk itself.

By contrast to these futures contracts, trading on the NCE is restricted to cash transactions; when a trade is made on the NCE, it is "real"; that is, if a bid or offer is covered, the specified quantity of cheese *will* change hands at the agreed-upon price (plus associated NCE fees and any transportation charges).

Trading on the NCE has no formal, direct relationship to milk futures trading on the CSCE. However, because of the structure of the Federal Milk Marketing Order System, cheese prices on the NCE are "translated back" into the BFP actually paid for milk. The BFP is also the central variable in CSCE trading of BFP futures contracts.

The CFTC has regulatory responsibility for trading in futures contracts, under the Commodities Exchange Act [codified at 7 U.S.C. ss. 1-25]. Because of the interrelationship between the price for cheese on the NCE and its effect upon the BFP (explained in more detail below), the CFTC's regulatory concerns extend to the operation of the NCE, even though the NCE is restricted to cash transactions over which the CFTC has no direct regulatory authority.

Cheese is a commodity in interstate commerce. Under 7 U.S.C. s. 6c (a), it is unlawful for any person to offer to enter into, or enter into, a transaction involving any commodity, which transaction is or may be used for, among other things: (a) determining the price basis of any such transaction in interstate commerce in such commodity; and (b) the transaction is used to cause any price to be reported, registered or recorded which is not a true and bona fide price. Further, under 7 U.S.C. s. 9, if the CFTC has reason to believe that any person is manipulating or attempting to manipulate the market price of any commodity in interstate commerce, the CFTC may commence administrative proceedings which may result, among other things, in the CFTC assessing a civil penalty of not more than the higher of \$100,000, or triple the monetary gain realized by the violator. Last, 7 U.S.C. s. 13 (a) (2), provides that any person who manipulates or attempts to manipulate the price of any commodity in interstate commerce is subject to a felony punishable by a fine of not more than \$500,000 or imprisonment for not more than five years, or both, together with the costs of prosecution.

Because of the CFTC's authority over transactions which have the potential to manipulate the price of any commodity in interstate commerce, the CFTC will need to monitor NCE trading, because it establishes cheese prices. Any manipulation of prices on the NCE would

directly translate back into manipulation of the BFP for milk, which is the basis of trading in milk futures and options under the supervision of the CFTC.

**3. How does the establishment of the BFP for milk under the Federal Milk Marketing Order System, as done currently, vary from what was done formerly using the so-called "M-W Price Series"?**

Commencing January 1995, the USDA modified the Grade A milk pricing formula used to establish the BFP under the Federal Milk Marketing Order System. Prior to that time, the USDA had established the BFP for each month based on the "Minnesota-Wisconsin Price Series" (M-W price) for the prior month. This was a base price calculated by the USDA from monthly reports submitted by processing plants in Wisconsin and Minnesota receiving Grade B (manufacturing) milk. The M-W price, an aggregate of the prices paid by reporting plants to Grade B milk producers for milk used for manufacturing purposes (cheese and butter/powder) became the BFP--the minimum price to be paid in the current month for Class III milk (Grade A milk utilized for manufacturing--also, the lowest priced milk of the three basic classes of milk utilization). Since manufacturing milk in Wisconsin and Minnesota is used almost exclusively for the manufacture of cheese, the price that could be paid for such milk was heavily dependent upon the price of cheese, as established by the NCE. Therefore, the cheese price on the NCE strongly influenced the price paid to Grade B milk producers and, in turn, influenced the M-W price used to establish the Grade A BFP for the following month.

As of January 1995, the Grade A BFP calculation was modified. As modified, it starts with the M-W price, which is then adjusted to account for: (a) changes in the past month in prices for cheddar cheese, nonfat dry milk, butter and dry buttermilk; and (b) changes in the percentages of manufacturing milk used to make cheese and butter/powder in Minnesota and Wisconsin. The effect of this modification was to reduce the time lag built into the BFP; rather than basing it on a price survey which is one month out of date, the BFP now includes an adjustment to the base-month price which reflects changes in the value of manufacturing milk used in Wisconsin and Minnesota during the intervening month. The NCE price for cheese is used to make any adjustments related to changes in cheese prices. Since the overwhelming majority of the manufacturing milk in Wisconsin and Minnesota is used to make cheddar cheese, the weight given the NCE price in adjusting the base price is substantial and the final BFP price update is largely derived from NCE cheese prices.

To recapitulate, establishment of the BFP, under both the "old" M-W price and as done currently, is strongly influenced by the price of cheese on the NCE. The effect of the current system is to more quickly reflect in the month-to-month BFP any changes in the price of cheese, as determined on the NCE. According to Professor Ed Jesse of the University of Wisconsin-Madison, Department of Agricultural Economics, the primary effect is to inject more volatility into the BFP, since cheese price changes are more quickly translated into BFP changes. According to Professor Jesse, under the former pricing mechanism based exclusively on the M-W price, cheese price changes were still reflected in the producer-pay price reported by milk handlers, but handlers tended to soften cheese price swings somewhat when determining the price which they could pay their milk producers. Handlers would "cushion" their producers somewhat by narrowing their margins and absorbing part of cheese price declines and by widening their margins and not fully returning to producers increases in cheese prices on the NCE. While this cushioning

effect may still be occurring, it is no longer reflected in the BFP, because of the factoring in of recent cheese price changes on the NCE.

Please contact me at the Legislative Council Staff offices if you wish to further discuss this topic.

DJS:rjl:lah;ksm



State Senator  
*Alice Clausing*



February 10, 1997

Alan Tracy, Secretary  
Department of Agriculture, Trade, and Consumer Protection  
2811 Agriculture Drive  
Madison, WI 53708

Dear Secretary Tracy:

I would like to express my deep concern and personal displeasure with you and your department's actions relative to Senate Bill 2, the Fair Milk Price Bill.

I see an uncanny similarity between your actions on SB 2, as director of agriculture in America's Dairyland, and the unfair trading practices we are trying to outlaw by members of the NCE. Practices against the interest of dairy farmers and Wisconsin's \$3 billion dairy industry should be prohibited, whether it is in Green Bay on the National Cheese Exchange (NCE) or in Madison at the Department of Agriculture, Trade, and Consumer Protection.

Your testimony in opposition to my Fair Milk Price Bill was a personal disappointment and a real revelation to me. How can one who crafted the March 1996 draft rule prohibiting trading against interest be opposed to the same language in SB 2? It appears that serving at the pleasure of Governor Thompson, with his corporate interests in this issue, obviously is a conflict of interest for you in trying to represent Wisconsin's dairy farmers.

I am sympathetic to you being in a cabinet position, and the need to answer directly to the Governor. On the issue of regulating unfair trading practices at the NCE, you can not serve two masters - special interests and the farmers. Your position needs to be insulated from political influence. I want to allow you to once again be responsive to farmers. Therefore, I am introducing legislation to renew the State Agriculture Board's authority to appoint the DATCP Secretary.

I was alarmed by your department's grossly inflated fiscal note for SB 2. Fiscal estimates are designed to reflect the cost of a bill, not an amendment, as your department's analysis did. An amended fiscal note to make changes subsequent to adoption of a substitute amendment would have been acceptable for SB 2.

DATCP's fiscal estimate of \$411,400 on SB 2 was a 15,000% increase from your original March 1996 draft rule estimate of \$2,700. The inflated fiscal note appears to be a deliberate attempt to interfere with legislative action to prohibit unfair trading on the NCE.

The non-partisan Legislative Fiscal Bureau provided the Senate with a supplemental fiscal note of \$43,500 for SB 2. The Senate was able to proceed on the Fair Milk Price Bill, which resulted in a 28-5 vote of overwhelming support for Wisconsin dairy farmers.



The legislative process should not be used as a playground for agency mischief. Certainly, no state agency should serve as an obstructionist for elected officials or impede legislative action. Therefore, I will introduce legislation that requires all fiscal estimates to be completed by the Legislative Fiscal Bureau, which is insulated from political influence.

In spite of Senate approval of SB 2, I request an official explanation and analysis of DATCP's \$411,400 fiscal note for SB 2 and justification for the 15,000% increase from your original proposal. I would appreciate your response by February 25<sup>th</sup>.

Sincerely,



ALICE CLAUSING  
State Senator  
10<sup>th</sup> Senate District

cc: Members of the State Senate  
AC/rr

**Prepared Testimony of  
Alan T. Tracy, Secretary  
Wisconsin Department of Agriculture,  
Trade and Consumer Protection  
before the Senate Committee on  
Agriculture and Environmental Resources  
on 1997 SB 2**

**January 21, 1997**

Good morning Senator Clausen and members of the committee. Thank you for inviting me to appear before this committee to comment on SB 2. This bill prohibits "trading against interest" on the National Cheese Exchange and any actions on or off the Exchange intended to manipulate the market price of milk or cheese.

This bill is very similar to a proposed administrative rule for which our department asked the Board of Agriculture, Trade and Consumer Protection (ATCP) to authorize public hearings. Our department proposed the rule as one of many options to address problems identified by researchers at the University of Wisconsin-Madison in their report on cheese pricing and trading practices on the National Cheese Exchange. The report, released in March, 1996, was prepared at our request and with our cooperation, under our authority to investigate business practices in Wisconsin.

The ATCP Board considered action on the proposed rule in April, 1996. At that same time, the Governor announced that he would be forming a task force to "make recommendations to improve the current cheese pricing system for the benefit of the dairy industry and consumers." The Board decided to refer the rule to the Governor's Task Force for its review and recommendations.

The Governor's Task Force on Cheese Pricing completed its work and submitted its report to Governor Thompson on January 2, 1997. I believe each member of the Legislature has been sent a copy of the report; I have brought extra copies of the Task Force's report.

The Task Force has provided the Governor with a set of positive, constructive recommendations for improving the current system for cheese and milk pricing. The Task Force considered the proposed rule to prohibit trading against interest and voted 13-3 against recommending that the rule proceed. The primary reason the Task Force voted against the rule was the recognition that the likely consequence of the rule would simply be that the National Cheese Exchange would feel compelled to move out of Wisconsin. Task Force members felt that if regulation of the Exchange is warranted, it should occur at the federal level. The Task Force recommended that the Governor ask the Commodity Futures Trading Commission and the Federal Trade Commission to re-evaluate their regulatory authorities concerning the National Cheese Exchange.

In addition to the recommendation for federal regulatory oversight of the Exchange, the Task Force on Cheese Pricing has made several other recommendations that I believe will bring about constructive improvements to the cheese and milk pricing systems. The Task Force is recommending that the U.S. Department of Agriculture no longer use the National Cheese Exchange price in determining the basic formula price for milk under Federal Milk Marketing Orders. The price of milk should be based on the supply of and

demand for milk used in the manufacture of all dairy products. The Task Force has offered several ideas on how this could be accomplished. The task force is also recommending that USDA improve and expand its weekly information series on the cheese "spot" market, to provide better market information on actual supply and demand conditions for cheese.

The Task Force has made four recommendations for improving public confidence in, access to and participation in trading on the National Cheese Exchange: 1) that the NCE board consider including one or more public persons (i.e., non-NCE members) on their board; 2) that the NCE board consider imposing a limit on the daily price movement of NCE prices; 3) that the identities of buyers and sellers should be anonymous during trading; and 4) that the NCE board consider implementing more frequent trading sessions once remote electronic access to trading sessions is in place. The NCE plans to implement remote access to trading sometime in 1997.

Governor Thompson will be leading a delegation of farmers to Washington, D.C. in early February to advance the relevant Task Force recommendations with the USDA, our Wisconsin Congressional delegation, the Commodity Futures Trading Commission and the Federal Trade Commission. I believe that providing positive action is the direction we should be taking at this time. I would recommend to this committee and to the Legislature to pass a resolution to the U.S. Congress urging federal reform of milk

pricing, improved market information services and federal regulatory oversight of the Exchange.

I commend the committee for your interest and involvement in this issue. However, I respectfully submit that the passage of SB 2 would serve no constructive purpose at this time. I encourage your active support for the meaningful and positive proposals the Task Force has developed.

I would be happy to answer any questions that members of the committee may have.

**Testimony**  
**Wisconsin Federation of Cooperatives**  
**Senate Bill 2**

**Public Hearing Before the Senate Committee on Agriculture and Environmental Resources**  
**‡ January 21, 1997**

I am Will Hughes, Director of Dairy Policy and Business Development, Wisconsin Federation of Cooperatives. WFC is opposed to Senate Bill 2 as written. While we appreciate your efforts to respond to concerns related to the National Cheese Exchange, this bill is not the vehicle to address these issues.

The dairy members of Wisconsin Federation of Cooperatives believe that passage of Senate Bill 2 will put the interests of Wisconsin dairy cooperatives and their members at financial risk because this bill will jeopardize the workings of the current cash market for cheese at a time when no viable alternative exists. A cash market is needed to operate cooperatives' cheese businesses.

The bill will have the effect of restricting trading activity by dairy cooperatives who are generally manufacturers and sellers of cheese, yet routinely buy as well as sell on the National Cheese Exchange. The bill language would restrict common business practices as well as the "trading against interest" that the Legislature is trying to prevent.

If trading of cooperatives is restricted or if the National Cheese Exchange ceases to exist before improvements can be made to it, or before an alternative cash market is created, dairy cooperatives will be left without a cash market reference price on which to base their selling prices in contract and negotiated sales. A cooperative's ability to effectively bargain and negotiate fair prices will be lessened in that event, and chaos in the marketplace could result. There needs to be provision for an orderly transition from the current cash market to an alternative or an improved cash market.

There are several deliberate efforts underway that will either lessen the impact of the National Cheese Exchange on farm milk prices, improve the public confidence in the National Cheese Exchange or move toward development of an alternative cash market for cheese. WFC dairy cooperatives support these efforts.

1) USDA has indicated that it will not use the National Cheese Exchange as a component of any milk price formula for use in federal milk marketing order pricing when it reforms federal milk pricing rules unless and until public confidence in the market is no longer subject to question.

2) Efforts are underway for federal oversight of the National Cheese Exchange or any cash market alternative. Federal regulation by the Commodity Futures Trading Commission is preferable.

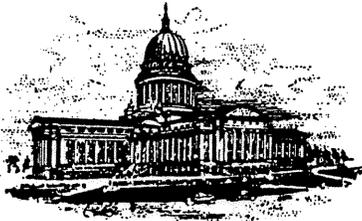
## Wisconsin Federation of Cooperatives Testimony on SB 2

3) The dairy industry is committed to either improve or replace the National Cheese Exchange in an effort to improve public confidence in the cash market for cheese. Alternative cash markets are being explored by the Coffee, Sugar, and Cocoa Exchange. The Chicago Mercantile Exchange will be considered as an alternative market as well.

The Wisconsin Federation of Cooperatives supports prompt and effective action by the dairy industry to implement these efforts as soon as possible. WFC served on the Governor's Task Force on Cheese Pricing and supports its basic recommendations.

Finally, we support the efforts of the Wisconsin Legislature and this Committee to work toward resolution of finding and maintaining a viable cash market for cheese in which there is a high degree of public confidence.

Thank you.



# Wisconsin State Assembly

P.O. BOX 8952 • MADISON, WI 53708

For Immediate Release – February 26, 1997

Contact: Sandy Chalmers (608) 266-7746; Kim Markham (608) 266-5831

## ASSEMBLY REPUBLICANS RAIL AGAINST MANIPULATION OF STATE'S DAIRY FARMERS *Assembly Speaker says politics, not helping dairy farmers, is behind Clausing/Springer proposal*

MADISON -- Assembly Speaker Ben Brancel (R-Endeavor) and a number of Assembly legislators today questioned the motives of politicians giving false hope to struggling dairy farmers.

"If dairy farmers could be helped by state regulation of the National Cheese Exchange, we would take immediate action," Brancel said. "But the bottom line is that the federal government—not state government—have responsibility for setting milk prices."

Speaker Brancel pointed out that there have been a number of attempts made to push USDA Secretary Dan Glickman to act quickly to decouple the Basic Formula Price for milk from prices set by the Cheese Exchange.

Representative Al Ott, Chair of the Assembly Agriculture Committee, said one of the first actions of the legislative session was to ask Secretary Glickman for quick action to help Wisconsin dairy farmers and to request that federal regulators take a careful look at Cheese Exchange trading practices.

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**add 1**

"It's unfortunate that dairy farmers are being given false hopes about an immediate solution to the milk-price problem," Ott said. "Unfortunately, imposing politically motivated state regulations on the Cheese Exchange here will only chase the Cheese Exchange around the country, and that won't help dairy farmers."

"We must maintain the focus on pressuring the USDA to take action to help Wisconsin's dairy farmers," Representative Sheila Harsdorf, a dairy farmer from River Falls, said. "To help Wisconsin's dairy farmers, the federal government must eliminate using the Cheese Exchange to establish the Basic Formula Price, must regulate the National Cheese Exchange wherever it is located, and must reform federal milk-marketing orders "

Representative Scott Jensen (R-Waukesha), co-Chair of the Joint Finance Committee, said, "The Cheese Exchange bill won't help a single dairy farmer in Wisconsin. This bill is a cruel hoax, and that's why the state's largest farm organizations do not support it."

According to committee hearing records on the Cheese Exchange bill, the following groups did not support the bill: Wisconsin Federation of Cooperatives, Wisconsin Farm Bureau Federation, and the National Milk Producers Federation.

Representative David Ward (R-Fort Atkinson), an active dairy farmer, said that he's felt the pinch of declining milk prices. "Federal agricultural officials need to take a long, hard look at how milk prices are set," he said. "There is no connection between increasing state regulation of the Cheese Exchange and federal milk prices."



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## WISCONSIN LEGISLATIVE COUNCIL STAFF MEMORANDUM

One East Main Street, Suite 401; P.O. Box 2536; Madison, WI 53701-2536  
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Fax (608) 266-3830

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DATE: January 27, 1997

TO: SENATOR ALICE CLAUSING, CHAIRPERSON, AND MEMBERS,  
SENATE COMMITTEE ON AGRICULTURE AND ENVIRONMENTAL  
AFFAIRS

FROM: David J. Stute, Director

SUBJECT: Senate Substitute Amendment 1 to 1997 Senate Bill 2, Relating to Regulation  
of Various Trading Practices on the National Cheese Exchange

This memorandum, prepared at your request, describes Senate Substitute Amendment 1 (LRBs0043/1) to 1997 Senate Bill 2, relating to regulation of various trading practices on the National Cheese Exchange.

Senate Bill 2 was the subject of a public hearing before your Committee on January 21, 1997. Following the conclusion of the hearing, your Committee voted introduction and adoption of Senate Substitute Amendment 1 and recommended passage of the Bill, as amended, both on votes of Ayes, 5; Noes, 0.

Senate Substitute Amendment 1 has the following features:

### **A. DEFINITIONS**

The Substitute Amendment creates several definitions:

1. "National Cheese Exchange" is defined as the cash auction market for cheese operated by the National Cheese Exchange, Inc. (hereafter, the "Exchange").
2. "Net purchase price" is defined as the net price to a purchaser or bidder, including transportation charges and transaction costs incurred by the purchaser or bidder on a completed purchase.
3. "Net sale price" is defined as the net price to a seller or offerer, excluding transportation charges and transaction costs incurred by the purchaser or bidder on a completed purchase.

### **B. DATCP DUTIES**

The Substitute Amendment newly requires the Department of Agriculture, Trade and Consumer Protection (DATCP) to:

1. Monitor all trading activity conducted on the Exchange.
2. Promulgate rules defining specific conduct that constitutes artificial manipulation of the market price for milk or cheese.

### **C. PROHIBITED CONDUCT**

The Substitute Amendment creates two specific prohibitions regarding trading on the Exchange:

1. The Substitute Amendment prohibits "trading against interest"; that is, engaging in a systematic pattern or practice of doing any of the following, either directly or through a broker, for the purpose, or with the effect, of affecting milk or cheese prices off the Exchange:
  - a. Selling or offering to sell cheese on the Exchange at a price that yields a net sale price that is less than the net sale price that the seller or offerer could have received for that cheese, at the same approximate time, off the Exchange.
  - b. Buying or bidding to buy cheese on the Exchange at a price that yields a net purchase price that is more than the net purchase price that the purchaser or bidder would have paid for that cheese, at the same approximate time, off the Exchange.
  - c. Acting primarily as a seller or offerer of cheese on the Exchange, while acting primarily as a buyer of cheese off the Exchange.
  - d. Acting primarily as a purchaser of or bidder for cheese on the Exchange, while acting primarily as a seller of cheese off the Exchange.

2. The Substitute Amendment prohibits "market manipulation"; that is, engaging individually or collectively in any plan or action related to the purchase or sale of cheese on or off the Exchange with the intent to manipulate artificially the market price of milk or cheese.

### **D. TRADING REPORTS**

Enforcement of the prohibition on trading against interest requires the comparison of conduct both on and off the Exchange. To facilitate such comparisons, the Substitute Amendment requires every person who trades on the Exchange, either directly or through a broker, to submit quarterly reports to the DATCP on a DATCP form. Reports must be submitted no later than the 15th day after the end of the calendar quarter. The report must disclose all of the following:

1. A listing of all transactions that the person engaged in *on* the Exchange during the calendar quarter, including the date of the transaction, whether the person bought or sold cheese, the quantity bought or sold and the transaction price.

2. A listing of all transactions that the person engaged in *off* the Exchange during the calendar quarter including, for each transaction in cheese, the same information described in item 1., above.

3. Any other information required by DATCP rule.

The information required to be submitted to the DATCP must be kept confidential, and may be used or disclosed by the DATCP only in connection with enforcement actions.

### E. ENFORCEMENT

The Substitute Amendment provides that a violation of the law created by the Substitute Amendment, or of a rule promulgated pursuant to it, has the same legal effect as a violation of an order issued under s. 100.20, Stats. ("Methods of competition and trade practices"). Further, the Substitute Amendment provides that the DATCP may, after notice and hearing, issue special orders that:

1. Enjoin persons found to have violated the law from engaging in trading on the Exchange, for a definite or indefinite period of time.

2. Require the Exchange to refuse trading privileges, for a definite or indefinite period of time, to any person found to have violated the law.

Orders issued by the DATCP under s. 100.20 and under the new law may be enforced by a DATCP action in circuit court, in the name of the state, to secure an injunction prohibiting violation of the order.

### F. PENALTIES

As noted above, a violation of the law created by the Substitute Amendment has the same legal effect as the violation of an order issued under s. 100.20. Under current law, violations of orders issued under s. 100.20 have a number of penalties, including criminal sanctions and private remedies. Under the Substitute Amendment, these penalty provisions are modified as follows for violations relating to transactions on the Exchange:

1. The provision in s. 100.20 (5), Stats., allowing any person suffering a pecuniary loss because of the violation of an order to sue the violator for damages and to recover twice the amount of the pecuniary loss, together with costs and attorneys' fees, does *not apply* to a violation of the law created by the Substitute Amendment.

2. The Substitute Amendment creates a new civil penalty; it provides that any person who violates the new law or rules promulgated thereunder may be required to forfeit not less than \$1,000 nor more than \$10,000 for each violation. Further, the Department of Justice (DOJ)

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no jail time

may commence an action in the name of the state to recover the forfeiture, regardless of whether the DATCP has issued a special order relating to banning a violator from trading on the Exchange or requiring the Exchange to deny trading privileges to a violator.

The current criminal penalty in s. 100.26 (3), Stats., providing that any person who violates an order issued under s. 100.20 may be fined not less than \$25 nor more than \$5,000 or imprisoned in the county jail for not more than one year, or both, is *unchanged* by the Substitute Amendment. Also unchanged is the provision in s. 100.26 (6) allowing the DATCP, the DOJ after consulting with the DATCP, or any district attorney to commence an action to recover a civil forfeiture for violations of injunctions to enforce orders. Civil forfeitures under this provision are not less than \$100 nor more than \$10,000 for each violation.

*current law*

### **G. REQUIRED RULE-MAKING**

As noted under Section B., 2., above, the DATCP is required to promulgate rules defining specific conduct which constitutes manipulation of the market price for milk or cheese. The Substitute Amendment requires that the DATCP initially promulgate these rules as emergency rules within 60 days after the effective date of Senate Bill 2. If the DATCP does not promulgate emergency rules within that time, the DATCP is required to request a meeting with the standing committees of the Senate and Assembly having jurisdiction over agricultural matters for the purpose of explaining why they have not been promulgated.

The department is required to submit proposed permanent rules defining specific conduct that constitutes manipulation of the market price for milk or cheese to the Legislative Council Rules Clearinghouse no later than October 1, 1997.

### **H. EFFECTIVE DATE**

The Substitute Amendment provides that the Act created by Senate Bill 2 takes effect on the first day of the first month beginning after publication or on July 1, 1997, whichever is later.

Please feel free to contact me at the Legislative Council Staff offices if you wish further information regarding this proposal.

DJS:jt;kja



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FROM: David J. Stute, Director

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3. "Net sale price" is defined as the net price to a seller or offerer, excluding transportation charges and transaction costs incurred by the purchaser or bidder on a completed purchase.

### **B. DATCP DUTIES**

The Substitute Amendment newly requires the Department of Agriculture, Trade and Consumer Protection (DATCP) to:

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### **C. PROHIBITED CONDUCT**

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- d. Acting primarily as a purchaser of or bidder for cheese on the Exchange, while acting primarily as a seller of cheese off the Exchange.

2. The Substitute Amendment prohibits "market manipulation"; that is, engaging individually or collectively in any plan or action related to the purchase or sale of cheese on or off the Exchange with the intent to manipulate artificially the market price of milk or cheese.

### **D. TRADING REPORTS**

Enforcement of the prohibition on trading against interest requires the comparison of conduct both on and off the Exchange. To facilitate such comparisons, the Substitute Amendment requires every person who trades on the Exchange, either directly or through a broker, to submit quarterly reports to the DATCP on a DATCP form. Reports must be submitted no later than the 15th day after the end of the calendar quarter. The report must disclose all of the following:

date  
bought or  
sold  
price  
quantity

1. A listing of all transactions that the person engaged in *on* the Exchange during the calendar quarter, including the date of the transaction, whether the person bought or sold cheese, the quantity bought or sold and the transaction price.

2. A listing of all transactions that the person engaged in *off* the Exchange during the calendar quarter including, for each transaction in cheese, the same information described in item 1., above.

3. Any other information required by DATCP rule.

The information required to be submitted to the DATCP must be kept confidential, and may be used or disclosed by the DATCP only in connection with enforcement actions.

**E. ENFORCEMENT**

The Substitute Amendment provides that a violation of the law created by the Substitute Amendment, or of a rule promulgated pursuant to it, has the same legal effect as a violation of an order issued under s. 100.20, Stats. ("Methods of competition and trade practices"). Further, the Substitute Amendment provides that the DATCP may, after notice and hearing, issue special orders that:

1. Enjoin persons found to have violated the law from engaging in trading on the Exchange, for a definite or indefinite period of time.

2. Require the Exchange to refuse trading privileges, for a definite or indefinite period of time, to any person found to have violated the law.

Orders issued by the DATCP under s. 100.20 and under the new law may be enforced by a DATCP action in circuit court, in the name of the state, to secure an injunction prohibiting violation of the order.

**F. PENALTIES**

As noted above, a violation of the law created by the Substitute Amendment has the same legal effect as the violation of an order issued under s. 100.20. Under current law, violations of orders issued under s. 100.20 have a number of penalties, including criminal sanctions and private remedies. Under the Substitute Amendment, these penalty provisions are modified as follows for violations relating to transactions on the Exchange:

1. The provision in s. 100.20 (5), Stats., allowing any person suffering a pecuniary loss because of the violation of an order to sue the violator for damages and to recover twice the amount of the pecuniary loss, together with costs and attorneys' fees, does *not apply* to a violation of the law created by the Substitute Amendment.

2. The Substitute Amendment creates a new civil penalty; it provides that any person who violates the new law or rules promulgated thereunder may be required to forfeit not less than \$1,000 nor more than \$10,000 for each violation. Further, the Department of Justice (DOJ)

2002  
11/15/02's  
sub

11/15/02's  
sub

civil - no jail time

may commence an action in the name of the state to recover the forfeiture, regardless of whether the DATCP has issued a special order relating to banning a violator from trading on the Exchange or requiring the Exchange to deny trading privileges to a violator.

The current criminal penalty in s. 100.26 (3), Stats., providing that any person who violates an order issued under s. 100.20 may be fined not less than \$25 nor more than \$5,000 or imprisoned in the county jail for not more than one year, or both, is *unchanged* by the Substitute Amendment. Also unchanged is the provision in s. 100.26 (6) allowing the DATCP, the DOJ after consulting with the DATCP, or any district attorney to commence an action to recover a civil forfeiture for violations of injunctions to enforce orders. Civil forfeitures under this provision are not less than \$100 nor more than \$10,000 for each violation.

*current law*

### **G. REQUIRED RULE-MAKING**

As noted under Section B., 2., above, the DATCP is required to promulgate rules defining specific conduct which constitutes manipulation of the market price for milk or cheese. The Substitute Amendment requires that the DATCP initially promulgate these rules as emergency rules within 60 days after the effective date of Senate Bill 2. If the DATCP does not promulgate emergency rules within that time, the DATCP is required to request a meeting with the standing committees of the Senate and Assembly having jurisdiction over agricultural matters for the purpose of explaining why they have not been promulgated.

The department is required to submit proposed permanent rules defining specific conduct that constitutes manipulation of the market price for milk or cheese to the Legislative Council Rules Clearinghouse no later than October 1, 1997.

### **H. EFFECTIVE DATE**

The Substitute Amendment provides that the Act created by Senate Bill 2 takes effect on the first day of the first month beginning after publication or on July 1, 1997, whichever is later.

Please feel free to contact me at the Legislative Council Staff offices if you wish further information regarding this proposal.

DJS:jt;kja

LRB or Bill No./Admin. Rule No.  
SB 2

Amendment No. if Applicable

ORIGINAL       UPDATED  
 CORRECTED     SUPPLEMENTAL

**FISCAL ESTIMATE**  
DOA-2048 N(R10/94)

**Subject**  
Regulation of National Cheese Exchange

**Fiscal Effect**

**State:**  No State Fiscal Effect

Check columns below only if bill makes a direct appropriation or affects a sum sufficient appropriation.

- Increase Existing Appropriation     Increase Existing Revenues  
 Decrease Existing Appropriation     Decrease Existing Revenues  
 Create New Appropriation

Increase Costs - May be possible to Absorb Within Agency's Budget  Yes  No

Decrease Costs  
See Text

**Local:**  No local government costs

1.  Increase Costs  
 Permissive     Mandatory  
2.  Decrease Costs  
 Permissive     Mandatory

3.  Increase Revenues  
 Permissive     Mandatory  
4.  Decrease Revenues  
 Permissive     Mandatory

5. Types of Local Governmental Units Affected:  
 Towns       Villages     Cities  
 Counties     Others \_\_\_\_\_  
 School Districts     WTCS Districts

**Fund Sources Affected**

GPR     FED     PRO     PRS     SEG     SEG-S

**Affected Ch. 20 Appropriations**  
20.115(1)(a)

**Assumptions Used in Arriving at Fiscal Estimate**

Summary of Bill

Senate Bill 2 (SB 2) would regulate certain trading practices on the National Cheese Exchange (a cash auction market for bulk cheese that is operated by National Cheese Exchange, Inc.). The bill would prohibit certain trading practices related to the pricing of cheese on the National Cheese Exchange that would be enforced under the state's unfair trade practices statutes, currently administered by DATCP.

Specifically, the bill would prohibit persons from engaging in individual actions or participating in any collective plan or action related to the purchase or sale of cheese on or off the National Cheese Exchange, with the intent to artificially manipulate the market price of cheese or milk.

The bill would also prohibit a practice identified as "trading against interest" defined as engaging in a systematic pattern or practice of doing the following for the purpose, or with the effect, of affecting milk or cheese prices off the National Cheese Exchange:

- 1) either by buying or selling on the Exchange at an unfavorable price compared to what could be obtained off the Exchange; or
- 2) acting primarily as a seller on the Exchange and a buyer off the Exchange, or vice versa.

Violations of the trading practices regulated under the bill would be considered an unfair method of competition or unfair trade practice and would be subject to the same court injunctions, civil forfeitures, and criminal penalties as violations under the state's general trade practice statutes and DATCP rules.

The bill would take effect on the first day of the first month after publication.

- see attached pages -

**Long-Range Fiscal Implications**

**Agency/Prepared by: (Name & Phone No.)**

Al Runde  
Daryl Hinz  
Legislative Fiscal Bureau      266-3847

**Authorized Signature/Telephone No.**

*Bob Lang*  
Robert Wm. Lang      266-3847

**Date**

January 29, 1997

### Fiscal Effect of Bill

In March, 1996, DATCP determined that it had authority under its general unfair methods of competition and trade practice authority (s 100.20) to promulgate a rule that would essentially prohibit the same conduct as SB 2 (the rule and bill are substantively identical). DATCP's fiscal note to draft rule ATCP 107 states that \$2,700 PR and .06 PR position would be needed to implement the proposed rule (the source of program revenues would be fees paid by processors of dairy products). The Department indicates that approximately 48 hours of staff time per year would be necessary to periodically monitor trading activities on the Exchange and to respond to complaints concerning alleged violations of the rule.

Although SB 2 is substantively identical to draft rule ATCP 107, in its fiscal note to SB 2 dated January 27, 1997, the Department indicates that \$411,400 GPR and 7.0 GPR positions annually would be needed (additionally, \$18,200 GPR in one-time office equipment costs are identified). The note indicates staffing would be necessary to monitor all trading activities and transactions on and off the Exchange, to conduct investigations of alleged violations, to undertake formal administrative actions against violators, for court enforcement of violations, and other administrative duties. The Department indicates that its current estimate differs from the fiscal estimate on its proposed rule because: (a) the staffing estimates for the bill were developed, in part, by reviewing the staffing requirements necessary to conduct the three and one-half-year National Cheese Exchange study in conjunction with the University of Wisconsin; and (b) it was determined that the program would no longer be a complaint based program with periodic monitoring of the Exchange but rather a more proactive program that is constantly monitoring activities and trading records on and off the Exchange, conducting investigations and proceeding with enforcement actions.

Specifically, the Department states that the following staff would be needed to enforce the provisions of SB 2: (1) two trade practice analysts would be required to observe weekly trading activity on the Exchange (the Exchange meets for approximately one-half hour each week), review trader's reports, compile summaries of trading activities on the Exchange and on futures and spot markets for cheese, butter and other dairy products; (2) three agriculture auditors to coordinate activities with the trade practice analysts to compile company specific data and conduct investigations, including financial and statistical analyses, detailed audits of transactions and summary reports with recommendations for further legal action; (3) one senior attorney to conduct legal actions against violators and prepare cases sufficient to meet the standards of proof for antitrust proceedings; and (4) one program assistant to perform various administrative duties.

The bill makes no appropriation. Essentially, the bill codifies the existing authority of DATCP to regulate in this area, as evidenced by draft rule ATCP 107. Therefore, it could be argued that, consistent with the fiscal note submitted with the proposed rule, the level of workload associated with the bill would be similar to much of DATCP's trade and consumer protection responsibilities, and would largely be determined by the priority given to it by the Department relative to its other trade practices regulation. That is, for some unfair trade practice activities (for example, minimum markup and other discriminatory pricing activities), the Department makes use of state statutes and administrative rules to establish a level playing field in the marketplace, educates the industry on those rules or statutes, and then reacts primarily to formal complaints of alleged violations. Conversely, other trade practices programs such as the dairy and grain plant security programs involve a substantial level of proactive enforcement in that staff are statutorily required to annually review the financial records and determine the financial viability of every business contracting for dairy and grain products.

In the absence of a listing of duties, appropriated funding or other specific detail, the implementation effort of a statute is largely at the discretion of the administering agency. While the work required to implement SB 2 would largely be left to the discretion of DATCP under the bill, the \$2,700 identified by the agency in March 1996 clearly contemplates a limited enforcement effort. If a more proactive enforcement stance is desired some level of staffing would be appropriate.

In some instances the Legislature has provided DATCP with additional responsibilities in regulating trade and pricing practices and has provided no additional staff or funding (for example, leaf tobacco buying and selling practices and brewers trade practices). In other instances, the Legislature has provided staff to DATCP to conduct specific statutory responsibilities. A recent example is 1993 Act 16, which provided 1.0 auditor position to enforce the statutory prohibition against unfair discrimination in drug pricing.

In order to provide a more proactive role than DATCP contemplated in ATCP 107, this estimate is based upon the provision of one position and related salary, fringe benefits and supply costs. Providing 1.0 agricultural auditor position would require \$9,900 (including one-time costs) for two months of funding in 1996-97 and have an annual cost of \$43,500.

Further, it should be noted that in many instances of consumer protection and trade regulation activities in new or evolving areas there may be an initial increase in workload in order to uncover unfair practices and determine ground rules (either through the administrative rule or formal court processes). After a period of time, this workload may be reduced (although occasional flare-ups may occur). Further, some have argued that regulation solely by Wisconsin could result in the Exchange leaving Green Bay for another state where regulation could, at least temporarily, be avoided (or could result in fewer traders on the Exchange).

#### Summary of SSA 1 to SB 2

Senate Substitute Amendment 1 (SSA 1) to SB 2 adds specific requirements that could impact the costs of implementing the bill. SSA 1 would make the following changes to SB 2: (1) require DATCP to monitor all trading activity on the Exchange; (2) require the Department to promulgate rules defining specific conduct that would constitute market manipulation (DATCP would be directed to promulgate emergency rules within 60 days of the effective date of the act and a permanent rule by October 1, 1997); (3) require those persons trading on the Exchange to submit a quarterly report to DATCP listing the date, type of transaction, quantity traded and price for all transactions made on and off the Exchange; (4) provide the Department with specific enforcement authority, including authority to refuse trading privileges of persons found in violation; (5) establish civil forfeitures of not less than \$1,000 or more than \$10,000 for each violation; (6) provide the Department of Justice with authority to commence court actions to recover a forfeiture; and (7) establish an effective date of the first day after the first month beginning after publication or on July 1, 1997, whichever is later.

While SSA 1 adds specific regulatory and enforcement provisions, DATCP determined, when it proposed ATCP 107, that it had similar authority to regulate and enforce National Cheese Exchange trading activities under its general trade practices statutory authority (for example civil forfeitures under existing statutes for unfair trade practices are not less than \$100 nor more than \$10,000 per violation).

Other provisions of SSA 1 may require additional effort by DATCP. Promulgating the emergency and permanent rules defining illegal conduct would increase workload on a temporary basis. However, it could be argued that once a rule is promulgated the enforcement burden should be eased by having prohibited conduct clearly identified. Further, the substitute amendment requires DATCP to monitor all activity on the Exchange, while SB 2 would leave the level of monitoring up to the Department (the Exchange meets for approximately one-half hour each week). Quarterly reports on trading on and off the exchange would be reviewed at some level by DATCP (however, under SB 2 or the proposed rule, DATCP, in certain instances, may have to obtain such information on its own initiative or through legal action in order to conduct an investigation).

The substitute amendment makes no appropriation (under SSA 1 any enforcement costs would be delayed until the 1997-99 biennium). Therefore, while it would appear that SSA 1 would result in an increased workload for DATCP, the overall level of monitoring and enforcement activity conducted by the agency would be largely dependent on the resources available and the priority placed on these activities by DATCP. If it is found that the position and funding identified in this estimate is insufficient to implement the requirements of SSA1, additional resources could be sought through the biennial budget process, separate legislation or the Joint Committee on Finance, after the required rules have been promulgated.

**FISCAL ESTIMATE WORKSHEET**

1997 Session

Detailed Estimate of Annual Fiscal Effect  ORIGINAL  UPDATED  
 DOA-2047(R10/94)  CORRECTED  SUPPLEMENTAL

LRB or Bill No./Adm. Rule No. Amendment No.  
 SB 2

Subject  
 Regulation of National Cheese Exchange

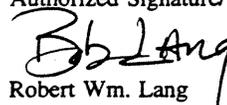
**I. One-time Costs or Revenue Impacts for State and/or Local Government (do not include in annualized fiscal effect):**

\$2,600 for office equipment

II. Annualized Costs:		Annualized Fiscal impact on State funds from:	
		Increased Costs	Decreased Costs
<b>A. State Costs by Category</b>			
State Operations - Salaries and Fringes		\$36,300	\$ -
(FTE Position Changes)		( 0 FTE)	(- FTE)
State Operations - Other Costs		\$7,200	-
Local Assistance			-
Aids to Individuals or Organizations			-
<b>TOTAL State Costs by Category</b>		\$43,500	\$ -
<b>B. State Costs by Source of Funds</b>		<b>Increased Costs</b>	<b>Decreased Costs</b>
GPR		\$43,500	\$ -
FED			-
PRO/PRS			-
SEG/SEG-S			-
<b>III. State Revenues-</b> Complete this only when proposal will increase or decrease state revenues (e.g., tax increase, decrease in license fee, etc.)		<b>Increased Rev.</b>	<b>Decreased Rev.</b>
GPR Taxes		\$	\$ -
GPR Earned			-
FED			-
PRO/PRS			-
SEG/SEG-S			-
<b>TOTAL State Revenues</b>		\$	\$ -

**NET ANNUALIZED FISCAL IMPACT**

	<u>STATE</u>	<u>LOCAL</u>
NET CHANGE IN COSTS	\$ 43,500	\$ _____
NET CHANGE IN REVENUES	\$ _____	\$ _____

Agency/Prepared by: (Name & Phone No.) Al Runde Daryl Hinz Legislative Fiscal Bureau 266-3847	Authorized Signature/Telephone No.  Robert Wm. Lang 266-3847	Date January 29, 1997
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## WISCONSIN LEGISLATIVE COUNCIL STAFF MEMORANDUM

One East Main Street, Suite 401; P.O. Box 2536; Madison, WI 53701-2536  
Telephone (608) 266-1304  
Fax (608) 266-3830

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DATE: February 3, 1997  
TO: SENATOR ALICE CLAUSING  
FROM: Dave Stute, Director  
SUBJECT: Comments on Letter From Louis P. Gentine

This memorandum, prepared at your request, comments on a statement in a January 29, 1997 letter captioned "Dear Representative" from Louis P. Gentine, Chairman and CEO of Sargento Foods, Inc., a marketer of cheese products headquartered in Plymouth, Wisconsin.

In his letter, Mr. Gentine made the following statement:

Elimination of trading on the National Cheese Exchange would severely impair the cheese industry, since thousands of daily transactions and existing marketing contracts are pegged to the price reflected on the Exchange. Senate Bill 2 would essentially freeze prices at the last price reflected on the Exchange prior to the Bill's implementation, rather than allow supply and demand to move the price when appropriate. Effectively eliminating the Exchange would also have major consequences for non-cheese companies, since the National Cheese Exchange prices are the primary component for setting the Basic Formula Price under Federal Milk Marketing Orders as well as the California State Milk Pricing Order.

Mr. Gentine's statement appears to imply that the enactment of Senate Bill 2 into law would result in the permanent cessation of all trading on the National Cheese Exchange. While that is certainly possible (no one is compelled to trade on the Exchange; the decision to participate is made by each individual member-trader), that result appears highly improbable.

Effective upon the enactment of Senate Bill 2 in its current form (as shown by Senate Substitute Amendment 1), the following actions would become illegal:

**FISCAL ESTIMATE**

DOA-2048 (R 10/94)

- ORIGINAL       UPDATED  
 CORRECTED       SUPPLEMENTAL

LRB or Bill No. / Adm. Rule No. SB2
Amendment No. (If Applicable)

**Subject**

**Proposed Act to regulate the trading practices on the National Cheese Exchange and to grant rule-making authority.**

**Fiscal Effect**

State:  No State Fiscal Effect

Check columns below only if bill makes a direct appropriation or affects a sum sufficient appropriation

- Increase Existing Appropriation       Increase Existing Revenues  
 Decrease Existing Appropriation       Decrease Existing Revenues  
 Create New Appropriation

Increase Costs - May be possible to Absorb Within Agency's Budget       Yes       No

Decrease Costs

Local:  No local government costs

1.  Increase Costs  
     Permissive       Mandatory  
 2.  Decrease Costs  
     Permissive       Mandatory

3.  Increase Revenues  
     Permissive       Mandatory  
 4.  Decrease Revenues  
     Permissive       Mandatory

5. Types of Local Governmental Unit Affected:

- Towns       Villages       Cities  
 Counties       Others \_\_\_\_\_  
 School Districts       WTCS Districts

**Fund Source Affected**

- GPR       FED       PRO       PRS       SEG       SEG-S

Affected Ch. 20 Appropriations  
20.115(1)(a)

**Assumptions Used in Arriving at Fiscal Estimate**

The proposed Act prohibits a buyer or a seller from specific practices on the National Cheese Exchange (NCE). These prohibited practices include engaging in individual or collective action relating to the buying or selling of cheese with the intention of manipulating the market price of cheese or milk. The practice of "trading against interest" is also prohibited by the proposed Act.

In order to enforce this Act, it is estimated that staff will need to monitor all trading activity on the NCE for possible violations of the Act. It is estimated that staffing requirements to enforce the Act will consist of three FTE Agriculture Auditors, two FTE Trade Practice Analysts, one FTE Senior Attorney, and one FTE Program Assistant. The staff requirements are for the continuous monitoring of cheese market transactions (including on site monitoring of the NCE), conducting investigations of alleged violations, investigative report preparations, formal administrative enforcement actions against violators, court enforcement proceedings against violators, and other administrative duties.

Two FTE Trade Practices Analysts, knowledgeable of the industry, would be required to observe weekly trading activity on the NCE; review trader's reports; compile and summarize weekly, monthly and quarterly trading activities on the futures markets for cheese, butter and other dairy products; compile and summarize activities on the spot markets for cheese, butter and other dairy products, and on the NCE. They will also identify suspected plans or actions to artificially manipulate the market price of milk or cheese. Annual hours associated with this activity are estimated at 2,120 hours.

The Trade Practices Analysts will coordinate their activities with three FTE Agriculture Auditors to conduct investigations of alleged violations. The Trade Practices Analysts and three Agriculture Auditors will identify specific company level information needed for detailed investigations. The Analysts and Auditors will conduct financial and statistical analyses and detailed audits of transactions culminating in reports and recommendations for further legal actions. Annual hours estimated for this activity are 8,290 hours.

continued

**Long - Range Fiscal Implications**

None

Agency/prepared by: (Name & Phone No.)

DATCP  
Paul Dingee (608) 224-4925

Authorized Signature/Telephone No.

*Barbara Knapp*  
Barbara Knapp (608) 224-4746

Date

1/27/97

The investigations will require the assistance of one FTE Attorney. It is anticipated that two concurrent investigations will occur per year. The Attorney will assist staff in conducting investigations, preparing formal administrative and court actions and assisting the Department of Justice. The department, based in part on its experience relating to the NCE investigation, anticipates a number of legal issues such as trade secrets and litigation. The Attorney will be required to prepare a case sufficient to meet standards of proof for antitrust case filings. Such cases are anticipated to be highly complex and need to be well documented for acceptance by the Wisconsin Department of Justice. Annual hours for this activity are 2,120.

One FTE Program Assistant is required to organize meetings, perform word processing tasks, coordinate schedules, maintain extensive data and files, and data entry and report preparation.

Staffing estimates are somewhat analogous to the staff requirements used in the collaborative study of the NCE released in 1996 by the University of Wisconsin's Department of Agriculture Economics and the Department of Agriculture, Trade and Consumer Protection. To prepare that study required the use of two FTE Professors, one FTE Program Assistant and two FTE Research Scientists from the University. In addition, part-time assistance was provided by the Department for attorneys, economists and other support staff. Costs for that study were in excess of \$600,000 over a four year period.

Permanent positions salaries are recapped as:

one Attorney	\$62,400
two Trade Practices Analysts	\$67,800
three Agriculture Auditors	\$92,200
one Program Assistant	<u>\$21,100</u>
Total	\$243,500

The projected on-going for salaries, fringes and supplies and services are \$411,400 per year. One-time costs are projected at \$18,200 for computers and other office equipment.

Estimated Activities of Two Trade Practices Analysts

Activities	Estimated Percentage	Estimated Annual Hours*
Continuous monitoring of cheese market transactions (including on-site monitoring at NCE)	10%	424
Review of trades reports on transactions	10%	424
Compilation of various weekly, monthly and quarterly trading activity reports	10%	424
Review and analyses of futures markets transactions and analyses of spot markets transactions	5%	212
Identify and report on suspected activities or plans to artificially manipulate market prices for milk and cheese	15%	636
Assist auditors in detailed investigations of suspect activities or plans to artificially manipulate the markets	30%	1272
Assist auditors in the preparation of reports on investigation findings and conclusions	15%	636
Assist in administrative and court proceedings	5%	212
Totals	100%	4240

\* Hours include allocated fringes

Estimated Activities of Three Agriculture Auditors

Activities	Estimated Percentage	Estimated Annual Hours*
Preliminary investigative field work Including: Reviewing reports on suspected activities or plans to artificially manipulate market prices from Trade Practices Analysts. Developing company specific audit programs	15%	925.5
Investigative field work (including completion of audit programs and financial analyses)	65%	4010.5
Prepare reports on investigation findings and conclusions	15%	925.5
Assist in administrative and court proceedings	5%	308.5
Totals	100%	6170

\* Hours include allocated fringes

Estimated Activities of One Program Assistant

Activities	Estimated Percentage	Estimated Annual Hours*
Perform duties for Attorney, three Auditors, and two Trade Practices Analysts, including:		
Word Processing	10%	189
Trading data entry	20%	378
Field audit and maintenance of records	30%	567
Report preparation	10%	189
Scheduling and case file management	30%	567
Total	100%	1890

\* Hours include allocated fringes

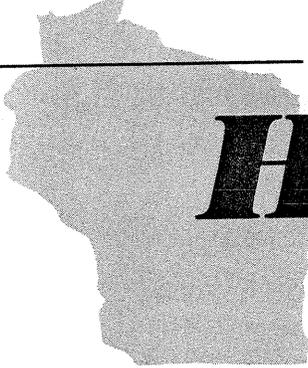
Estimated Activities of one Attorney

Activities	Estimated Percentage	Estimated Annual Hours*
Review of reports of alleged illegal activities from Analysts and Auditors	5%	106
Case file preparation for administrative or court actions that meet equivalent to FTC "standards of proof" for cases forwarded to District Attorneys and Department of Justice	85%	1802
Issue subpoenas and assist staff in investigations for case development	10%	212
Total	100%	2120

\* Hours include allocated fringes

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news from



# **HERB KOHL**

*United States Senator  
Democrat of Wisconsin*

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330 Hart Senate Office Building • Washington, D.C. 20510 • (202) 224-5653

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## **Statement of U.S. Senator Herb Kohl**

### **before the Senate Committee on Agriculture and Environmental Resources January 21, 1997**

Chairperson Clausing, Members of the Committee:

Thank you for providing me the opportunity to comment on legislation regarding regulation of trading practices on the National Cheese Exchange (NCE) by the State of Wisconsin. I applaud your efforts to be proactive on this issue, which is of such great importance to farmers, dairy product manufacturers, and consumers alike.

As a member of the Senate Agriculture Appropriations Subcommittee, I have followed closely the work of the Food Systems Research Group (FSRG) at the University of Wisconsin-Madison, and have worked to provide the FSRG with the federal funding necessary for their investigation into the trading activities on the NCE. As a result of that investigation, we have all learned a great deal about that market, and its inappropriate influence on commercial cheese prices, as well as milk prices paid to farmers.

There are many things that can be done at the federal level to address some of the issues raised by the FSRG cheese study. Together with my colleagues Senator Feingold and Congressman Obey and other members of the Wisconsin Congressional Delegation, I have taken several actions in that regard. Specifically, we have:

#### **\* Called for oversight of the NCE by the Commodity Futures Trading Commission (CFTC)**

Because the NCE is both very thinly traded, and completely unregulated, it offers great potential for price manipulation. The NCE is neither self-regulated, nor is it subject to any state or federal regulatory oversight. Therefore, we have called on the U.S. Commodity Futures Trading Commission to oversee the NCE, to help in our efforts to eliminate any potential for manipulation of that market. While the CFTC recently pledged its intention to more closely examine the operations of the NCE, federal legislation may be necessary to clarify their authority to oversee this market.

#### **\* Exploration of the Creation of Alternative Cash Markets for Cheese**

While regulatory oversight of the NCE is important and necessary, in the long run the creation of alternative cash markets will be important to any effort to bring fairness and reason to cheese pricing. Currently, despite the flaws of the NCE, it is used as a reference price for the large majority of commercial cheese sales in this country, and is also used by USDA in

determining monthly minimum prices paid to farmers for their milk. Unfortunately, because there are no other accessible prices available for use as a reference, the NCE has been allowed to have far more influence than it should. That is why Senator Feingold and I have asked the Coffee, Sugar, and Cocoa Exchange (CSCE), which already trades cheese futures contracts, to explore the creation of an alternative cash market for cheese. Such a new market has the potential to be more broadly traded, more adequately regulated, and therefore, less subject to manipulation. If successful alternative cash markets are established, it could help reduce the price volatility that we've seen on the NCE in recent years, and provide a more credible reference price.

**\* Urged the Elimination of the NCE price as a factor in the Basic Formula Price**

As part of the milk market order reform process currently being conducted by USDA, the process for setting the Basic Formula Price (BFP) will be reformed as well. I have asked that the NCE price be removed from any future calculations of the BFP, and I know that most of my colleagues in the Wisconsin Congressional Delegation agree with me in that regard. However, as long as the NCE price is used as a reference price for commercial cheese sales, it will continue to have a large influence on farmers' milk checks, particularly in Wisconsin, where cheese production is so dominant.

While these federal initiatives are an important prerequisite to any fair and reasonable reform of milk and cheese pricing, the State of Wisconsin deserves to be an equal partner in the regulation of the NCE, as well. And that is why I wholeheartedly endorse legislation to prevent price manipulation on the NCE and prohibit traders from "trading against interest" on that exchange.

Again, I thank you for the opportunity to comment on the matter of NCE regulation, and look forward to working with this Committee toward a strong state/federal partnership regarding this important matter.



STATE REPRESENTATIVE  
TOM SPRINGER

MADISON OFFICE  
P.O. BOX 8953  
MADISON, WI 53708  
(608) 266-1182

LEGISLATIVE HOTLINE  
1-800-362-9472

No

January 9, 1997

TO: All interested Legislators

FROM: Representative Tom Springer

RE: Co-sponsorship of LRB 1611/2, relating to regulation of various trading practices on the National Cheese Exchange

This LRB is the Assembly companion to Senator Clausing's legislation.

Recently a UW study concluded that a potential exists for large cheese traders to drive down prices by selling cheese instead of buying. This potential for price manipulation exists therefore, LRB 1611/2 and its Senate companion will regulate certain trading practices on the NCE.

LRB 1611/2 will prohibit persons from engaging in actions related to the sale or purchase of cheese on or off the NCE with the intent to artificially manipulate the market price of cheese or milk. Additionally, this bill will prohibit "trading against interest" which is explained fully in the LRB analysis on the back of this memorandum.

If you are interested in co-sponsoring this legislation, please contact my office at 6-1182 by Tuesday, January 21<sup>st</sup>.

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***Analysis by the Legislative Reference Bureau***

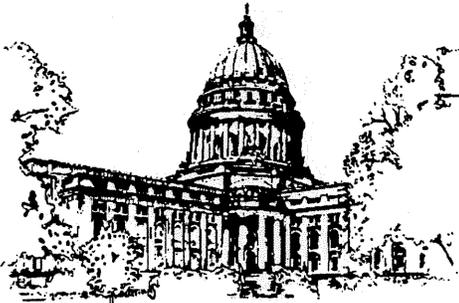
This bill regulates certain trading practices on the National Cheese Exchange, a cash auction market for cheese that is operated by the National Cheese Exchange, Inc. The bill prohibits persons from engaging in any individual action or participating in any collective plan or action related to the purchase or sale of cheese on or off the National Cheese Exchange, with the intent to manipulate artificially the market price of milk or cheese. The bill also prohibits a practice sometimes referred to as "trading against interest" for the purpose, or with the effect, of affecting milk or cheese prices off the National Cheese Exchange. "Trading against interest" means a systematic pattern or practice of any of the following, either directly or through a broker: 1) selling or offering to sell cheese on the National Cheese Exchange at a price that yields a net sale price that is less than the net sale price that the seller or offeror could have received for that cheese, at the same approximate time, off the exchange; 2) buying or bidding to buy cheese on the National Cheese Exchange at a price that yields a net purchase price that is more than the net purchase price that the purchaser or bidder could have received for that cheese, at the same approximate time, off the exchange; 3) acting primarily as a seller or offeror of bulk cheese on the National Cheese Exchange, while acting primarily as a buyer of bulk cheese off the exchange; and 4) acting primarily as a purchaser of or bidder for bulk cheese on the National Cheese Exchange, while acting primarily as a seller of bulk cheese off the exchange.

Violations of the trading practices prohibitions created in this bill have the same legal effect as a violation of an order issued by the department of agriculture, trade and consumer protection (DATCP). As a result, violations of the prohibitions are subject to possible court injunctions, civil forfeitures and criminal penalties. In addition, persons suffering a monetary loss because of a violation may also sue the violator directly and may recover double damages, costs and reasonable attorney fees.

For further information see the *state* fiscal estimate, which will be printed as an appendix to this bill.

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Jim Matson - 224-5022



State Senator

Alice Clausing



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No

December 27, 1996

TO: Legislative Colleagues

FROM: Senator Alice Clausing

RE: Co-sponsorship of LRB 1552/2, relating to regulation of various trading practices on the National Cheese Exchange

The pricing formula for raw milk is based on the price of block cheddar cheese set at the National Cheese Exchange (NCE), which is located in Green Bay. Since October, milk prices have tumbled almost 25% in line with dropping prices paid for cheese at the NCE.

A recent UW study found that major cheese traders have the potential to drive prices down by selling cheese instead of buying as they normally would. As a result, as currently organized, the NCE appears to facilitate market manipulation. Such price manipulation could contribute to the rapid decline in milk prices.

LRB 1552/2 prohibits any actions related to the purchase or sale of cheese on or off the NCE with the intent to manipulate the market price of milk or cheese. It also prohibits "trading against interest", a practice that is more fully explained in the LRB analysis printed on the back of this memo.

Considering the dire circumstances facing our dairy farmers, the state needs to do whatever it can to protect its farmers from unfair trading practices.

If you would like to co-sponsor this legislation, please contact my office at 6-7745 by Thursday, January 9<sup>th</sup>.



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***Analysis by the Legislative Reference Bureau***

This bill regulates certain trading practices on the National Cheese Exchange, a cash auction market for cheese that is operated by the National Cheese Exchange, Inc. The bill prohibits persons from engaging in any individual action or participating in any collective plan or action related to the purchase or sale of cheese on or off the National Cheese Exchange, with the intent to manipulate artificially the market price of milk or cheese. The bill also prohibits a practice sometimes referred to as "trading against interest" for the purpose, or with the effect, of affecting milk or cheese prices off the National Cheese Exchange. "Trading against interest" means a systematic pattern or practice of any of the following, either directly or through a broker: 1) selling or offering to sell cheese on the National Cheese Exchange at a price that yields a net sale price that is less than the net sale price that the seller or offeror could have received for that cheese, at the same approximate time, off the exchange; 2) buying or bidding to buy cheese on the National Cheese Exchange at a price that yields a net purchase price that is more than the net purchase price that the purchaser or bidder could have received for that cheese, at the same approximate time, off the exchange; 3) acting primarily as a seller or offeror of bulk cheese on the National Cheese Exchange, while acting primarily as a buyer of bulk cheese off the exchange; and 4) acting primarily as a purchaser of or bidder for bulk cheese on the National Cheese Exchange, while acting primarily as a seller of bulk cheese off the exchange.

Violations of the trading practices prohibitions created in this bill have the same legal effect as a violation of an order issued by the department of agriculture, trade and consumer protection (DATCP). As a result, violations of the prohibitions are subject to possible court injunctions, civil forfeitures and criminal penalties. In addition, persons suffering a monetary loss because of a violation may also sue the violator directly and may recover double damages, costs and reasonable attorney fees.

For further information see the *state* fiscal estimate, which will be printed as an appendix to this bill.

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