

## National Ingredient Strategy Implementation Policy – February 2017

Background: DFNS, DFC and the nine other provincial milk marketing boards successfully negotiated an Agreement in Principle for a National Ingredient Strategy (NIS) with the national milk processors in July 2016. The NIS is designed to position the Canadian Dairy Industry in a positive position going forward. Many challenges face our industry including: reduced producer returns; elimination of WTO subsidized exports in 2020; a growing structural surplus; aging skim drying capacity; and the need for processing investment and innovation in new technology / ingredients.

The ten provinces voted in support of the NIS, related pricing adjustments and the Harmonized Billing Mechanism in July 2016. Since then considerable effort has gone into reaching full consensus at the CMSMC and Joint Pool meetings on several elements required to implement the NIS on February 1, 2017. With the approval of these elements, the table is set for provincial NIS implementation.

This policy serves to define and connect the Harmonized Billing Mechanism, the Harmonized Billing Ratios and the National Auditing System with the Milk Pricing Regulation and Milk Classes and Categories Regulation. The interconnection of these five documents coming into force jointly is required to implement the NIS in Nova Scotia. In essence, they form a package deal and need to be considered together.

The NIS is predicated on the creation of a competitively-priced-ingredients class – Class 7 – for milk components, milk products and dairy ingredients for utilization in the production and processing of milk and dairy products, as well as for utilization and sale beyond the primary dairy processing industry to other markets in the food and food service industries (including animal feed).

Why Policy?: The NIS is a far-reaching and very technical approach that revolutionizes milk utilization reporting and pricing in Canada. As such, the parameters and rules / administrative procedures form a living document which will be updated often and as required. This policy will serve the short-term need to capture all the NIS implementation details to compliment the regulation changes. As the NIS matures the associated changes will need to be captured, not unlike other pool / national policy decisions.

Elements of the NIS: As noted, there are several concrete elements required to implement the NIS. A brief description of each element follows:

- a) **Milk Pricing Regulation** – These DFNS regulations have been updated to capture changes to class prices resulting from NIS and establish a reference to this Policy.

See <http://www.novascotia.ca/just/regulations/regs/dimilkpr.htm>

The CDC announces the Class 7 price monthly.

**SNF Price:** The CDC will calculate the SNF price for Class 7 monthly until September 2023 as follows:

Element	Proposal
SNF price reference	Lowest price SMP (Oceania, Europe or US) for the period.
Period	Monthly, using the average of published data of the most recent 4 weeks.
Margin	February 2016 Canadian processor margin \$ 0.9191/kg is deducted.
Announcement	Published in the first week of each month and used for the previous month utilisation invoicing (eg. The prices published on October 5, 2016 will be used to invoice processors for September 2016 utilisation).

**BF Price:** The CDC will calculate the monthly price for the value of the BF used in the manufacture of Class 7 products until September 2023 as follows:

Element	Proposal
BF Price reference	The lowest of the whole milk powder prices (Oceania, Europe or US) for the period.
Margin	February 2016 Canadian processor margin \$ 0.9191/kg is deducted.
SNF value	SNF value established for the ingredient class is deducted
Period	Monthly, using the average of published data of the most recent 4 weeks.
Announcement	Published in the first week of each month and used for the previous month utilisation invoicing (eg. The prices published on October 5, 2016 will be used to invoice processors for September 2016 utilisation).

**Exceptional Circumstances:** Because of the change to class 1-4 milk price changes (using formula) a National Exceptional Circumstances agreement has been reached. See Appendix 1

- b) **Milk Classes and Categories Regulation** – This Council regulation has been modified with the addition of a Class 7 definition and other changes to related classes and details. The regulation mirrors the National Milk Classification System,

as approved by the CMSMC. It needs to be clear that, while we have a starting point for NIS implementation, some of these classifications and definitions are still under review and will be updated at the national level going forward.

See <http://www.novascotia.ca/just/regulations/regs/dimilkcc.htm>

- c) **Harmonized Billing Ratios** – The HBR is an approved table containing the ratios of Class 7 and domestic protein utilization allowed for billing purposes in each category of dairy product. The negotiated ratios are mostly complete, but will be adjusted and further defined in the coming months based on additional industry consultation and agreement. As well, new products and technologies will mean additional ratios may be agreed for inclusion in the HBR table. These ratios provide a direct link between milk and ingredient utilization and the Milk Pricing Regulation / Class 7 price.
- d) **Harmonized Billing Mechanism** – The HBM is a complex set of rules to allow for all pricing and billing calculations under the NIS. Calling on the HBR, milk prices and the classification definitions, the HBM provides common rules to ensure producer incomes are protected from cannibalization and that processor invoicing is consistent across the country.
- e) **NIS National Audit System** – In developing the NIS, HMR and HBM it became clear that auditing also needed to be updated. In consultation with CDC Directors the Working Group for the Implementation of the National Ingredients Strategy (WGINIS) developed the necessary changes to the National Auditing System relative to auditing and implementing the NIS.

While there is a National Audit Standards Manual (which will be updated for NIS), for transparency and ease of reference the specific elements approved for NIS auditing will be captured in this policy. Proper audit authorities and measures are essential to ensuring the NIS is applied not only equally but also fairly across the country.

<p><b>Implementation:</b> This policy comes into force February 1, 2017 concurrent with the approval of the amendments to the Milk Classes and Categories Regulation and the Milk Pricing Regulation.</p>
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The balance of this policy, and its appendices, contain the HBR, HBM and the National Audit Information necessary for NIS implementation.

Harmonized Billing Ratios – The table in Appendix 2 was approved by the P5 Supervisory Body and the Canadian Milk Supply Management Committee at their December 2016 and January 2017 meetings. This table details the ratios based on:

- Dairy Product Protein Price Ratio for Billing at the end-use Class Price of the finished dairy products
- Ingredient Class Dairy Product Protein Price Ratio for Billing at the Ingredients Class Price

Harmonized Billing Mechanism – Appendix 3 contains the specifics of the pricing and billing mechanism that apply to pricing and billing to processors. This Appendix is based on items approved by the P5 Supervisory Body and the Canadian Milk Supply Management Committee at the July 2016, December 2016 and January 2017 meetings.

National Audit System The following background and specific points comprise the changes to the audit system to implement the NIS and ensure it is applied the same way in all provinces. This part of the policy refers to Appendix 4 & 5.

- **Given** the motion of July 2016 on the national ingredients strategy, in which the provinces agreed to establish a Class 7 for manufacturing dairy ingredients and a Harmonized Billing Mechanism (HBM) to protect the interests of producers and processors in a consistent way in each province;
- **Whereas** the purpose of this audit and billing mechanism is to:
  - Protect producers' income from cannibalization;
  - Ensure fair and uniform pricing conditions;
- **Whereas**, the 10 provinces also agreed to assign the CDC the following terms of reference:
  - Entrust the CDC to review the audit procedures and billing mechanism in each province to ensure equitable and consistent implementation, with the rules agreed to by CMSMC; and
  - Monitor and periodically report to CMSMC on implementation of the ingredients strategy and the outcomes for attainment of its objectives.
- **Whereas**, to minimize the risks of cannibalization associated with utilization of Class 7 by milk receivers and non-milk receivers (milk buyers<sup>1</sup> and non-milk buyers<sup>2</sup>),

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1. A Milk Buyer is defined as a milk processor purchasing milk directly from a provincial milk board.

2. A Non-Milk Buyer is defined as a milk and/or food processor, distributor, broker and/or exporter who does not purchase milk directly from a provincial milk board.

CMSMC members have asked CDC to amend the Auditing System in the following recommendation:

1. the CDC ensures, in consultation with provincial authorities and industry stakeholders, that the proper regulatory framework is in place at the national and provincial levels, which gives the CDC and provincial auditors the authority needed to audit and apply the Harmonized Billing Mechanism conditions on milk buyers and non-milk buyers.
  2. CMSMC members commit to implement a regulatory framework within their own jurisdictions to achieve this.
  3. In parallel, the CDC will establish a mechanism at the national level in consultation with provinces which provides the CDC and provincial auditors the authority needed to audit and apply the Harmonized Billing Mechanism on milk buyers and non-milk buyers by means of the National Auditing System.
- **Whereas** implementation of this National Auditing System will complete the provisions set out in the Harmonized Billing Mechanism (HBM);
  - **Whereas** this mechanism is essential for implementing the national ingredients strategy which must be agreed on before implementation of the ingredients strategy scheduled for February 1 in all Canadian provinces, recognizing a transition period will be required until the National Centralized Registration System (NCRS) is fully operational;

**Amend the National Auditing Standards, based on the following parameters:**

1. A **National Centralized Registration System** for all milk buyer and non-milk buyers (see Appendix 4);
2. An **Auditing and Billing Mechanisms Certification Program** that will apply in each province (see Appendix 5);
3. It is understood that:
  - Provincial auditors will continue to perform audit for all milk utilization from all milk buyers.
  - In the case of non-milk buyers, CDC is responsible to perform all the plant audits unless the provincial audit authority is designated.
  - Provincial auditors are also responsible for making arrangements for joint audit with CDC auditors when CDC determines that a risk-based audit, including spot (random) audits, involving intra-provincial, inter-provincial and international transactions is necessary.

## **Transitional Period:**

Pending the realization of the elements provided in the Amendment of the National Auditing Standards above, it is proposed to agree on a transitional period during in which:

1. Class 7 ingredient manufacturers are responsible for the destination of ingredients, as agreed in the HBM. Processor invoices and transfer of documents issued to buyers will clearly indicate that the buyer's plant records are subject to audit in compliance with HBM requirements. If an audit cannot be completed, the ingredient seller is responsible for the price adjustment in the form of an invoice at Class 1(a) price;
2. The CDC continues to issue permits under Special Class Programs. Provincial authorities will bill at Class 7 prices when required;
3. To request the CDC, jointly with WGINIS, to propose as soon as possible, in consultation with the industry, the necessary adjustments to ensure a smooth transition to the new business environment following the implementation of the National Ingredient Strategy.

**National Exceptional Circumstances for Milk Price Changes**

Recommendation #1: That the P5 Supervisory Body (P5 SB) and Western Milk Pool Coordinating Committee (WMP CC) and Newfoundland and Labrador (NL) establish the National Pricing Formula as follows:

- a. The National Pricing Formula is comprised of the following two indices:
  - i. 50% Cost of Production as established by the Canadian Dairy Commission (CDC), using the percentage change between the 3<sup>rd</sup> quarter indexed Cost of Production for the current and previous year;
  - ii. 50% Consumer Price Index, using the percentage change between the 12-month average figure ending September 30<sup>th</sup> of the current and previous year;
- b. The CDC calculates and publishes the result of this formula by no later than November 10 of each year<sup>(1)</sup>;
- c. The formula is in place until February 1, 2023. At that time, the formula will be automatically renewed unless decided otherwise;
- d. In the instance that exceptional circumstances occur as prescribed below, the results of the formula will be suspended for that year and a new adjustment may be recommended in accordance with Section 2, below;
- e. If the pools agree to adopt any adjustment to the Class 1-4 component prices, it should be done by no later than December 15<sup>th</sup>;
- f. That the Joint P5 Technical Committee/WMP Technical Committee/NL be mandated to revise the current template used to determine butterfat, protein and other solids component price adjustments for all classes in order to incorporate section 1 to 3. The Joint P5 TC/WMP TC must report to the P5 SB/WMP CC & NL by no later than October 2017.

(1) Calculation and publication of the formula result is dependent on publication of statistics Canada indices for the month of September. Historically, this data has been available in late October to early November.

Recommendation #2: That the CMSMC adopt the following approach to address exceptional circumstances:

- a. The CDC will continue to monitor market conditions, and will assess whether exceptional circumstances may exist;
- b. The CDC will, in collaboration with stakeholders, prepare a set of criteria that will serve as guidelines to determine whether exceptional circumstances exist<sup>(1)</sup>. These guidelines will be presented to stakeholders by no later than July 2017;
- c. If exceptional circumstances exist, then the CDC will advise all stakeholders<sup>(2)</sup> by no later than November 10 of the current year. The CDC will provide all relevant information deemed necessary to all stakeholders;
- d. Stakeholders will be invited to respond in writing by no later than November 25 if they wish to trigger a provision for exceptional circumstances. In the absence of formal notice, the formula will result in price changes as agreed;

- e. Should any stakeholder request a change to the pricing due to an exceptional circumstance, the CDC will invite and promote consensus amongst stakeholders. In the event no consensus is reached by November 30, the CDC will, at the time of pricing consultation, hear all parties and decide whether there will be any adjustment to the National Pricing Formula and the results by no later than December 10.

(1) These criteria may include the following: a minimum threshold for the application of the National Pricing Formula to avoid unnecessary market fluctuations, a maximum difference between expected producer revenues and cost of production as a result of applying the National Pricing Formula, etc.

(2) Stakeholder representatives are the followings: Dairy Farmers of Canada, Dairy Processors Association of Canada, Consumers' Association of Canada, and Restaurant Canada.

Recommendation #3: That the CMSMC acknowledge:

- a. The CDC will continue to set support prices for butter and skim milk powder, including the processor margin and butter carrying charges;
- b. The CDC will continue to consult stakeholders prior to publishing changes in support prices. The CDC will also inform stakeholders of the result of the National Pricing Formula;
- c. In order to maintain seasonality programs for butter, the P5 SB, WMP CC, and NL Class 4(a) butterfat price should be aligned with support price for butter as announced by the CDC. For that reason, the component pricing template must include this element along with butter carrying charges;

The CDC remains the sole administrator of the Cost of Production survey in order to ensure neutrality and provide a sound and fair measure of producer efficiency.



## Harmonized Billing Ratios

Class 1<sup>1</sup>

Corresponding end-use Class(es)	End Products	Dairy Product Protein Price Ratio for Billing at the end-use Class Price of the finished dairy products	Ingredient Class Dairy Product Protein Price Ratio for Billing at the Ingredients Class Price
1(a) 1(b) 1(c) 1(d)	Standard Fluid milk products as per provincial regulations (Federal when no provincial regulation exists) <sup>2</sup>	100% of milk protein contained in an equal volume of a fluid milk product of the same butterfat content	0%
	Fortified fluid milk products	100% of milk protein contained in an equal volume of a fluid milk product of the same butterfat content	Added milk protein and other solids above that contained in an equal volume of a fluid milk product of the same butterfat content
	Milk Meal Replacement with 50% or less dairy content	0%	100%
	Milk Beverages, milkers and creamers <sup>3</sup>	No access to Class 7 <sup>4</sup> but nothing will prevent the use of byproducts	

1. a) Milk reconstitution which has been made by the addition of water is not allowed whatever the source of water; b) Must have a casein and whey protein content at least equal to that of the raw milk used to prepare fluid milk for those products. Only non-fat solids are taken into account to determine the casein and protein content of the whey; c) That no preparation process may reduce the milk protein content or alter the ratio between caseins and whey proteins of the raw milk used to prepare these products.

2. Including flavoured milk and fortified milk

3. Subject to P5 SB /WMP CC approval of 4(a) and 4(d) SNF and class 2 to 4 BF price adjustments (revert February 1, 2016 pricing decision)

4. Discussion will continue at WGINIS

## Class 2

Class	End Products	Dairy Product Protein Price Ratio for Billing at the end-use Class Price of the finished dairy products	Ingredient Class Dairy Product Protein Price Ratio for Billing at the Ingredients Class Price
2(a)	All types of yogurts, including yogurt beverages, kefir, and lassi, excluding frozen yogurts.	February 1, 2017 to January 31, 2019: 70% February 1, 2019 and beyond :75%	February 1, 2017 to January 31, 2019: 30% February 1, 2019 and beyond :25%
2(b)	Fresh Dairy Desserts (i.e.: At least 75% fresh milk content, final product shelf life requires refrigeration)	75%	25%
	All types of ice cream, ice cream mix, whether frozen or not  Other frozen dairy products including frozen yogurts, frozen desserts, and milkshake mixes not for retail sale	100% of protein and associated other solids contained in cream <sup>5</sup>	100% of the total skim milk solids <sup>6</sup>
	All types of fudge, pudding, soup mix, and Indian sweets <sup>7</sup>	100%	0%
	Sour cream	75%	25%
	Dairy beverage shakes	No access to Class 7 <sup>8</sup> but nothing will prevent the use of by products	

5. For calculation purposes, cream is assumed to be standardized at a butterfat test of 0.4 kilograms per litre

6. For calculation purposes, skim milk is assumed to be standardized at a butterfat test of 0.001 kilograms per litre

7. Secretariat is considering removing fudge, pudding, soup mix, Indian sweets from the harmonized milk classification (not considered finished dairy products)

8. Discussion will continue at WGINIS

	Sports/Nutrition Drinks with a minimum protein content <b>2X</b> that of fluid milk products content	No access to Class 7 <sup>9</sup> but nothing will prevent the use of byproducts
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**Class 3**

<b>Class</b>	<b>End Products</b>	<b>Dairy Product Protein Price Ratio for Billing at the end-use Class Price of the finished dairy products <sup>10</sup></b>	<b>Ingredient Class Dairy Product Protein Price Ratio for Billing at the Ingredients Class Price</b>
3(a)	Cheese with a ratio of 95% as per the Federal Dairy Product Standards	95%	5%
	Cheese curds, part skim pizza cheese, pizza cheese, skim milk cheese, ricotta and all other cheese varieties falling within Class 3(a)	83%	17%
3(b)	Aged Cheddar (9 months and more as per Federal Dairy Product Standards)	100%	0%
	Cheddar, cheddar-type cheeses sold fresh	83%	17%
	Stirred curd, cream cheese, and cream cheese bases or cheese mixes, other than creamy cheese bases or cheese mixes used to process products referred to in	83%	17%

9. Discussion will continue at WGINIS

10. Excludes added protein and associated components sourced from whey and/or wheyby-products.

	another class		
	Any product not referred to in Class 3(a), 3(b), 3(c), or 3(d) made by coagulating milk, coagulating milk products, or coagulating both milk and milk products with the aid of bacteria to form a curd; excludes rennet casein curd	83%	17%
3(c)1	Feta	50%	50%
	Asiago, Gouda, Havarti, Parmesan, Swiss	95%	5%
	Munster (Muenster) Canadian-style	83%	17%
3(c)2	Brick, Colby, Farmer's, Jack, Monterey Jack, all types of Mozzarella other than Pizza Mozzarella and Part Skim Pizza Mozzarella and Mozzarella falling within Class 3(d)	83%	17%
	Pizza Mozzarella and Part Skim Pizza Mozzarella not described in Class 3(d)	63%	37%
	Paneer	50%	50%
3(d)	Standardized Mozzarella to be used strictly on fresh pizzas by establishments registered with the Canadian Dairy Commission under terms and conditions approved by the Canadian Milk Supply Management Committee	63%	37%

**Class 4**

<b>Class</b>	<b>End Products</b>	<b>Dairy Product Protein Price Ratio for Billing at the indicated Class Price</b>	<b>Ingredient Class Dairy Product Protein Price Ratio for Billing at the Ingredients Class Price</b>
4(a)	Butter and butter oil Partly-skimmed milk powders with butterfat content greater than 4% (further discussions required on the treatment of sales of this product to the food industry that would not be used in the production of another dairy product).  Other dairy products not elsewhere specified in another Class <sup>11</sup>	100%	0%
4(b)	Condensed milk or sweetened condensed milk for retail sale	50%	50%

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11. Any other product not otherwise specified is subject to review by WGINIS on a case-by-case basis.

## Appendix 3 – Pricing and Billing terms for Processors

This Appendix contains the terms that apply to pricing, billing and auditing in relation to processors and in particular the ingredients class of milk (Class 7).

### A. Introduction

Nova Scotia, along with all other provinces, has established a non-contingent dairy ingredient Class 7 for the manufacture of dairy ingredients. A monthly billing, reporting and audit mechanism that protects both parties' interests for the ingredients class is being implemented consistently in every province by producers and processors. Processors recognize that the same anti-cannibalization mechanism will be implemented in every province.

The main objectives of this Appendix include protecting producers' income from cannibalization into higher priced domestic classes, and ensuring equity and a level playing field for all dairy processors in Canada through audit and the billing mechanism.

### B. Definition of Class 7

1. In this Appendix, "Class 7" means the Class 7 class of milk as defined in the *Milk Classes and Categories Regulations*.

### C. Harmonized Billing Mechanism

2. Processors will have access to the Class 7 price for skim milk and other Class 7 dairy products and ingredients within the limits of the billing ratios established under the Harmonized Billing Ratios (see Appendix 2 of this National Ingredients Strategy Implementation Policy).
3. Billing ratios are calculated and applied on the total milk protein contained in the vat from all sources – fresh milk, domestic milk protein ingredients, and imported milk protein ingredients.
4. For cheese products falling within Class 3, total milk protein in the vat does not include milk proteins sourced from whey or whey by-products.
5. Processors using less fresh milk protein than specified by the Harmonized Billing Ratio specified for each Class in Appendix 2 will be subject to a price adjustment on that lesser amount at the difference between the higher class component prices and the Class 7 component prices.
6. For component pricing and billing purposes, the protein billing ratios are extended to cover and to capture the small amounts of butterfat and larger amounts of other components found in the equivalent volume of skim milk associated with or used in the manufacture of milk protein ingredients - for

calculation purposes, the skim milk is assumed to be standardized at a butterfat test of 0.001 kilograms per litre.

7. A price adjustment on milk purchased will apply if the butterfat sourced through Class 7 milk products and/or other dairy products or ingredients exceeds the butterfat that would be contained in a milk protein product or ingredient made from skim milk standardized at 0.001 kilograms of butterfat per litre. The price adjustment will be calculated at the difference between the higher class butterfat component price and the Class 7 butterfat component price.

#### D. Declaration

8. All processors must declare for each product, all milk protein contained in the vat from all sources – fresh milk, domestic milk protein ingredients, and imported milk protein ingredients – excludes added protein and associated components sourced from whey and/or whey by-products in the case of cheese.
9. Processors will be responsible for their ingredients destinations. Milk used to process milk products or ingredients eligible for declaration in Class 7 for sale or transfer to another dairy processing facility in Canada, whether through a third-party or not, that does not purchase or acquire milk through a provincial milk marketing board, will be billed at the end-use class price for the dairy product being made. Under such circumstances, Class 7 component prices will only apply if the purchasing dairy product processing facility consents to an end-use audit to ensure that the components are priced in accordance with the Dairy Product Billing Ratios specified in Appendix 2.
10. Processors' declarations will be managed in a strictly confidential manner.

#### E. Auditing

11. Auditors must have access for each product, to the required information on the total milk protein in the vat on a monthly basis from all sources — fresh milk, domestic milk protein ingredients, and imported milk protein ingredients. This includes all accounting records related to the purchase of all milk products and milk protein ingredients used in the manufacture of milk and manufactured dairy products. This is to ensure that all milk protein sources have been accounted in the determining the protein product billing ratios. Auditors must proceed with a validation and a reconciliation of total milk protein in the vat on a monthly basis from all sources, by variety of products and by class. This will be done through their regular auditing schedules.

#### F. Other Elements

12. Transactions between companies involving Class 7 ingredients in liquid form (e.g. skim milk, MPC, MPI) are concluded at the domestic market price; the Class

7 price applies upon final utilization under HBM parameters, with the exception of:

- In the case of registered food/further processors liquid milk ingredients can be bought at the class 7 price for purchases of 1000 liters and less (totes)per transaction, up to 10,000 litres per month;
  - In the case of exports, liquid milk ingredients may be billed at class 7;
  - It is the CMSMC's intention through WGINIS, in consultation with industry, to implement by May 1, 2017, a manner to allow transactions between milk buyers involving Class 7 ingredients in liquid form to be invoiced at the Class 7 price within the parameters of the HBM.
  - For the non-milk buyer transactions, the WGINIS, in consultation with industry, will review and further investigate the implications of invoicing liquid ingredients at domestic price versus Class 7 price and will share its findings no later than the July 2017 CMSMC meeting.
  - Prior to allowing transactions between milk buyers to be under class 7, provincial authorities, along with the CDC, must have implemented mechanisms that will allow tracking of these transactions electronically for audit purposes and that address any identified risks.
13. Liquid ingredients at the Class 7 price cannot be bought or sold through a third party (includes all forms of companies, excluding dairy processors and secondary processors, as defined in the national manual audit procedures) except for exports.
14. The special classes permit system will continue to be used by food processors, for the remaining eligible products in special classes.
15. All whole milk powder not packaged for retail sale falls within Class 7 for pricing purposes. These Whole Milk Power markets will continue to be serviced through a permit system, at Class 7 price, until the auditing and tracking rules are defined, with the objective of no later than May 1, 2017. Milk allocation parameters and rules will be further defined to meet new market initiative as soon as possible.
16. Class 7 ingredients used to reconstitute any dairy products listed in any other Class shall be reclassified in accordance with the terms of the Harmonized Billing Mechanism and invoiced accordingly.
17. The administrative measures must be monitored and revisited before the end of each dairy year.

#### G. Effective Date

18. The provisions of this Appendix take effect on February 1, 2017.



## **Appendix 4: Description of the proposed Centralized National Registration System**

### **1. Purpose of the program**

The purpose of the National Centralized Registration System is to enable registered companies with a valid registration number to utilize Class 7 components, products, and ingredients, whether they are milk buyers or non-milk buyers.

### **1.2. Coordination of the program**

The program shall be developed and administered by the CDC, in consultation with provincial audit authorities **and** is comprised of three components.

1. A web-based registration system (e.g. Class 3d)
2. The necessary legal authority for provincial and CDC auditors to coordinate audits of milk buyers and non-milk buyers when necessary.
3. A list of reporting and auditing obligations for registered companies.

### **1.3 Obligations of registered companies**

To qualify for Class 7, each registered company agrees to:

1. Obtain a valid registration number;
2. Comply with the terms set out in the Harmonized Billing Mechanism;
3. Report their utilization of components and any ingredient purchased, so that all quantities of Class 7 components are reported and used, and a global reconciliation can be performed.;
4. Submit to periodic audits under the terms of their user registration contract.
5. Following an audit, allow an auditor from a province whose eligible product was transferred to another province to submit the audit results to CDC and the auditor of the province in question;
6. Agree to pay the boards any price or volume adjustment or CDC (as applicable) through an audit adjustment for ingredient components used, as stipulated in the HBM:

- a. In the case of milk buyers, the adjustment will appear on invoices issued by the milk producers board;
  - b. In the case of non-milk buyers CDC auditor may make an appropriate adjustment or audit claim;
7. In the case of ingredient sellers:
- a. Ensure the buyer of Class 7 ingredients holds a valid registration;
  - b. For sale of ingredients to an unregistered buyer—thus ineligible for Class 7—take responsibility for their destination, which implies a component price adjustment in the form of an invoice at Class 1(a).
8. Where utilization cannot be audited despite valid user registration, the user shall be held responsible for utilization of these ingredients, which implies a component price adjustment in the form of an invoice at Class 1(a).
9. A company can lose the right to access Class 7 by having the registered number suspended or revoked<sup>1</sup> following an audit, and then must reregister under the terms to be defined<sup>2</sup>.

#### **1.4. Stages in implementing the National Registration System**

To implement this system, the following must be done in order of priority.

1. The necessary web-based administrative system needs to be developed by the CDC to:
  - Maintain the database of all registered NCRS users;
  - Enable registered companies to confirm validity of registration numbers;
  - Demonstrate, after consultation with the industry, that the data required to perform the audit procedures is treated with confidentiality;
  - Data use solely for the administration of this program can be accessed and easily integrated with provincial utilization software;
  - Provide secure access rights as necessary under the terms of the program;
  - A third-party security audit will be performed to ensure system and data confidentiality.
2. CDC will develop, in consultation with the industry, the contractual arrangements tailored for the various categories of milk and non-milk buyers

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1 A notification period will be done consistent with existing practice (i.e. special class)

2 To be defined by the National Audit Committee and included in the national audit manual

3. Class 7 ingredients manufacturers must agree that invoices and transfer of documents issued to the buyer will clearly indicate that the buyer's plant records are subject to audit in compliance with HBM requirements.
4. Provincial reporting systems must communicate all data necessary to ensure the required reporting, to perform a global reconciliation of all Class 7 component quantities used:
  - i. Data related to company to company transfers of liquid ingredients will be shared between the two provincial auditors verifying the transaction;
  - ii. Ensuring that when a milk buyer or non-buyer is audited, the auditor from a province whose eligible product has been transferred to another province submits the audit report produced for this purpose to CDC and the auditor from the province in question.
5. Make any necessary updates to the producers' reporting model to reflect Class 7 usage in the higher classes. CDC, marketing boards and provincial commissions must do what is necessary to amend provincial and federal regulations to ensure uniform application of the HBM in all provinces (e.g. national plan, provincial regulations, etc.).
6. Assess what needs to be done to integrate Class 7 into the P10 agreement.

## **Appendix 5: Description of the Provincial Audit and Billing Mechanisms Certification Program**

To be able to review each province's audit procedures and billing mechanism and to ensure fair, uniform implementation that complies with the agreed rules, it is moved that CDC establish a Provincial Billing Mechanisms Certification Program.

### **1. Purpose of the certification program**

The program's purpose is to enable CDC to:

1. Certify that reporting systems comply with the HBM;
2. Certify that audit procedures meet the requirements of the national audit manual and ensure compliance with the HBM;
3. Certify that the HBM is applied fairly and uniformly in all provinces;
4. Provide procedures for dealing with non-compliance.

### **2. Terms of application of the certification program**

To be able to implement this program, CDC should:

1. Develop this program in consultation with provincial auditors and have it adopted by CMSMC, including:
  - a. Updating of the national audit manual;
  - b. Procedures for dealing with non-compliance;
  - c. Confidentiality rules to ensure strict control of data sharing between auditors.
2. Ensure availability of the necessary human and technical resources (e.g. auditors, reporting systems, etc.).
3. Coordinate utilization audits with provincial auditors to ensure full compliance of provincial billing mechanism with P5 SB and WMP CC and CMSMC decisions.

Periodically report to CMSMC on overall audit status and implementation of the ingredients strategy and the results obtained in achieving its agreed objectives.