

**DEPARTMENT OF AGRICULTURE****Agricultural Marketing Service****7 CFR Part 984**

[Docket No. AO-192-A7; FV06-984-1]

**Walnuts Grown in California; Recommended Decision and Opportunity To File Written Exceptions to Proposed Amendments of Marketing Agreement and Order No. 984****AGENCY:** Agricultural Marketing Service, USDA.**ACTION:** Proposed rule and opportunity to file exceptions.

**SUMMARY:** This recommended decision invites written exceptions on proposed amendments to Marketing Order No. 984, which regulates the handling of walnuts grown in California (Order). The amendments were proposed by the Walnut Marketing Board (Board), which is responsible for local administration of the order. The amendments included in this recommended decision would: Change the marketing year; include "pack" as a handler function; restructure the Board and revise nomination procedures; rename the Board and add authority to change Board composition; modify Board meeting and voting procedures; add authority for marketing promotion and paid advertising; add authority to accept voluntary financial contributions and to carry over excess assessment funds; broaden the scope of the quality control provisions and add the authority to recommend different regulations for different market destinations; add authority for the Board to appoint more than one inspection service; replace outdated order language with current industry terminology; and other related amendments.

The Department of Agriculture (USDA) proposed three additional amendments: To establish tenure limitations for Board members, to require that continuance referenda be conducted on a periodic basis to ascertain producer support for the order, and to make any changes to the order as may be necessary to conform with any amendment that may result from the hearing.

The proposed amendments are intended to improve the operation and functioning of the marketing order program.

**DATES:** Written exceptions must be filed by April 16, 2007.**ADDRESSES:** Written exceptions should be filed with the Hearing Clerk, U.S. Department of Agriculture, room 1081-

S, Washington, DC 20250-9200, Fax: (202) 720-9776, or via the Internet: <http://www.regulations.gov>. All comments should reference the docket number and the date and page number of this issue of the **Federal Register**. Comments will be made available for public inspection in the Office of the Hearing Clerk during regular business hours, or can be viewed at: <http://www.regulations.gov>.

**FOR FURTHER INFORMATION CONTACT:**

Melissa Schmaedick or Kathleen M. Finn, Marketing Order Administration Branch, Fruit and Vegetable Programs, AMS, USDA, 1400 Independence Avenue, SW., Stop 0237, Washington, DC 20250-0237; Telephone: (202) 720-2491, Fax: (202) 720-8938, or e-mail: [Melissa.Schmaedick@usda.gov](mailto:Melissa.Schmaedick@usda.gov) or [Kathy.Finn@usda.gov](mailto:Kathy.Finn@usda.gov).

Small businesses may request information on this proceeding by contacting Jay Guerber, Marketing Order Administration Branch, Fruit and Vegetable Programs, AMS, USDA, 1400 Independence Avenue, SW., Stop 0237, Washington, DC 20250-0237; telephone: (202) 720-2491, Fax: (202) 720-8938, or E-mail: [Jay.Guerber@usda.gov](mailto:Jay.Guerber@usda.gov).

**SUPPLEMENTARY INFORMATION:** Prior documents in this proceeding: Notice of Hearing issued on April 18, 2006, and published in the April 24, 2006, issue of the **Federal Register** (71 FR 20902).

This action is governed by the provisions of sections 556 and 557 of title 5 of the United States Code and, therefore, is excluded from the requirements of Executive Order 12866.

**Preliminary Statement**

Notice is hereby given of the filing with the Hearing Clerk of this recommended decision with respect to the proposed amendment of Marketing Agreement and Order No. 984, which regulates the handling of walnuts grown in California, and the opportunity to file written exceptions thereto. Copies of this decision can be obtained from Melissa Schmaedick, whose address is listed above.

This recommended decision is issued pursuant to the provisions of the Agricultural Marketing Agreement Act of 1937, as amended (7 U.S.C. 601 *et seq.*), hereinafter referred to as the "Act," and the applicable rules of practice and procedure governing the formulation of marketing agreements and orders (7 CFR part 900).

The proposed amendments are based on the record of a public hearing held on May 17 and 18, 2006, in Modesto, California. Notice of this hearing was published in the **Federal Register** on April 24, 2006 (71 FR 20902). The

notice of hearing contained proposals submitted by the Walnut Marketing Board (Board), which is responsible for local administration of the order, and by the Agricultural Marketing Service (AMS).

The proposed amendments are the result of a committee appointed by the Board to conduct a review of the order. The committee met several times in 2005 and drafted proposed amendments to the order and presented them at industry meetings. The proposed amendments were then forwarded to the Board, which unanimously approved them. The amendments are intended to streamline organization and administration of the marketing order program. The Board's request for a hearing was submitted to USDA on March 3, 2006.

The Board's proposed amendments to the order are summarized below.

1. Amend the order to change the marketing year from August 1 through July 31 to September 1 through August 31. This proposal would amend § 984.7, Marketing year, and would result in conforming changes being made to § 984.36, Term of office, and § 984.48, Marketing estimates and recommendations.

2. Amend the order by specifying that the act of packing walnuts is considered a handling function. This proposal would amend § 984.13, To handle, as well as clarify the definition of "pack" in § 984.15 by including the term "shell" as a function of "pack."

3. (a) Amend all parts of the order that refer to cooperative seats on the Board, redistribute member seats among districts, and provide designated seats for a handler handling 35 percent or more of production, if such handler exists. This proposal would amend § 984.35, Walnut Marketing Board, and § 984.14, Handler.

3. (b) Amend the Board member nomination process to reflect proposed changes in the Board structure, as outlined in 3(a). This proposal would amend § 984.37, Nominations, and § 984.40, Alternate.

4. Require Board nominees to submit a written qualification and acceptance statement prior to selection by USDA. This proposal would amend § 984.39, Qualify by acceptance.

5. Change the name of the Walnut Marketing Board to the California Walnut Board. This proposal would amend § 984.6, Board, and § 984.35, Walnut Marketing Board.

6. Add authority to reestablish districts, reapportion members among districts, and revise groups eligible for representation on the Board. This

proposal would add a new paragraph (d) to § 984.35, Walnut Marketing Board.

7. Amend Board quorum and voting requirements to add percentage requirements, add authority for the Board to vote by "any other means of communication" (including facsimile) and add authority for Board meetings to be held by telephone or by "any other means of communication", providing that all votes cast at such meetings shall be confirmed in writing. This proposal would amend § 984.45, Procedure, and would result in a conforming change in § 984.48(a), Marketing estimates and recommendations.

8. Amend the order to add authority to carry over excess assessment funds. This proposal would amend § 984.69, Assessments.

9. Amend the order by adding authority to accept voluntary financial contributions. This proposal would add a new § 984.70, Contributions.

10. Amend the order to clarify that members and alternate members may be reimbursed for expenses incurred while performing their duties and that reimbursement includes per diem. This proposal would amend § 984.42, Expenses.

11. Amend the order to add authority for the Board to appoint more than one inspection service as long as the functions performed by each service are separate and do not duplicate each other. This proposal would amend § 984.51, Inspection and certification of inshell and shelled walnuts.

12. (a) Amend the order by broadening the scope of the quality control provisions and by adding authority to recommend different regulations for different market destinations. This proposal would amend § 984.50, Grade and size regulations.

12. (b) Amend the order by adding authority that would allow for shelled walnuts to be inspected after having been sliced, chopped, ground, or in any other manner changed from shelled walnuts, if regulations for such walnuts are in effect. This proposal would amend § 984.52, Processing of shelled walnuts.

13. Amend the order by adding authority for marketing promotion and paid advertising. This proposal would amend § 984.46, Research and development.

14. Amend the order to replace the terms "carryover" with "inventory," and "mammoth" with "jumbo," to reflect current day industry practices. This proposal would amend § 984.21, Handler inventory, and § 984.67, Exemption, and would also result in conforming changes being made to

§ 984.48, Marketing estimates and recommendations, and § 984.71, Reports of handler carryover.

15. (a) Amend the order to clarify and to simplify the interhandler transfer provision, and to add authority for the Board to recommend to USDA regulations, including necessary reports, for administrative oversight of such transfers. This proposal would amend § 984.59, Interhandler transfers.

15. (b) Amend the order to clarify that the Board may require reports from handlers or packers that place California walnuts into the stream of commerce. This proposal would amend § 984.73, Reports of walnut receipts.

16. Update and simplify the language in § 984.22, Trade demand, to state "United States and its territories," rather than name "Puerto Rico" and "The Canal Zone".

17. Amend the order by adding language that would acknowledge that the Board may deliberate, consult, cooperate, and exchange information with the California Walnut Commission. Any information sharing would be kept confidential. This would add a new § 984.91, Relationship with the California Walnut Commission.

In addition, USDA proposed adding three provisions that would help assure that the operation of the program conforms to current Department policy and that USDA can make any necessary conforming changes. These provisions would:

18. Establish tenure requirements for Board members. This proposal would amend § 984.36, Term of office.

19. Require that continuance referenda be conducted on a periodic basis to ascertain industry support for the order and add more flexibility in the termination provisions. This proposal would amend § 984.89, Effective time and termination.

20. Make such changes as may be necessary to the order to conform with any amendment thereto that may result from the hearing.

Twenty-five witnesses testified at the hearing. These witnesses represented walnut growers and handlers. While all witnesses supported the Board's recommended changes, several witnesses opposed USDA recommendations to establish tenure requirements and require continuance referenda.

Witnesses speaking in favor of the proposed changes addressed the need to change the structure of the Board to reflect recent changes in the industry, and the need to improve the administration, operation and functioning of the program in effect for walnuts grown in California. The order

was established in 1948 and was last amended in 1976.

Witnesses at the hearing further stated that the amendments being considered were designed to streamline the operation of the order based on accepted business procedures in the 21st century. Witnesses also stated that many of the proposed amendments would provide the program with the necessary flexibility for the future.

At the conclusion of the hearing, the Administrative Law Judge stated that the final date for interested persons to file proposed findings and conclusions or written arguments and briefs based on the evidence received at the hearing would be 30 days after the posting of the hearing transcript on the USDA Web site, or July 6, 2006. One brief was filed. The brief clarified the intent of the Board's proposed amendments and offered general support.

### Material Issues

The material issues presented on the record of hearing are as follows:

1. Whether to amend the order to change the marketing year from August 1 through July 31 to September 1 through August 31;

2. Whether to amend the order by specifying that the act of packing walnuts is considered a handling function and by clarifying that the definition of "pack" should include the term "shell";

3. (a) Whether to amend all parts of the order that refer to cooperative seats on the Board, redistribute member seats among districts, and provide designated seats for a major handler, if such handler exists (a major handler would have to handle 35 percent or more of the crop);

3. (b) Whether to amend the Board member nomination process to reflect proposed changes in the Board structure, as outlined in 3(a);

4. Whether to require Board nominees to submit a written qualification and acceptance statement prior to selection by USDA;

5. Whether to change the name of the Walnut Marketing Board to the California Walnut Board;

6. Whether to add authority to reestablish districts, reapportion members among districts, and revise groups eligible for representation on the Board;

7. Whether to amend Board quorum and voting requirements to add percentage requirements, to add authority for the Board to vote by "any other means of communication" (including facsimile), and to add authority for Board meetings to be held by telephone or by "any other means of

communication”, providing that all votes cast at such meetings shall be confirmed in writing;

8. Whether to amend the order to add authority to carry over excess assessment funds;

9. Whether to amend the order by adding authority to accept voluntary financial contributions;

10. Whether to amend the order to clarify that members and alternate members may be reimbursed for expenses incurred while performing their duties and that reimbursement includes per diem;

11. Whether to amend the order to add authority for the Board to appoint more than one inspection service as long as the functions performed by each service are separate and do not duplicate each other;

12. (a) Whether to amend the order by broadening the scope of the quality control provisions and by adding authority to recommend different regulations for different market destinations;

12. (b) Whether to amend the order by adding authority that would allow for shelled walnuts to be inspected after having been sliced, chopped, ground, or in any other manner changed from shelled walnuts, if regulations for such walnuts are in effect;

13. Whether to amend the order by adding authority for marketing promotion and paid advertising;

14. Whether to amend the order to replace the terms “carryover” with “inventory,” and “mammoth” with “jumbo,” to reflect current industry procedures;

15. (a) Whether to amend the order to clarify and to simplify the interhandler transfer provision and to add authority for the Board to recommend to USDA methods and procedures, including necessary reports, for administrative oversight of such transfers;

15. (b) Whether to amend the order to clarify reports required regarding interhandler transfers;

16. Whether to update and simplify the language in § 984.22, Trade demand, to state “United States and its territories,” rather than name “Puerto Rico” and “The Canal Zone”;

17. Whether to amend the order by adding language that would acknowledge that the Board may deliberate, consult, cooperate, and exchange information with the California Walnut Commission;

18. Whether to amend the order to limit the number of terms a member may serve on the Board at any one time to three consecutive, two-year terms; and,

19. Whether to require that continuance referenda are held every six years to determine support for continuation of the order.

#### Findings and Conclusions

The following findings and conclusions on the material issues are based on evidence presented at the hearing and the record thereof.

#### *Material Issue Number 1—Marketing Year*

Section 984.7, Marketing year, should be amended to change the marketing year from August 1 through July 31 to September 1 through August 31.

Under the current definition of the order, the California walnut marketing year begins August 1 and continues through July 31. While this marketing period was appropriate at the time of the order’s promulgation in 1948, witnesses stated that it no longer reflects the current crop cycle. Witnesses explained that, over time, new varieties of walnuts have been introduced, and the areas in which walnuts are cultivated have shifted. The newer varieties mature later than the varieties grown at the time of the program’s inception. At the same time, cultivation has slowly moved into areas that previously were not suited for walnut production. With differences in climate, soil, and water, witnesses explained that these new production areas have slightly later growing cycles. The proposed change in the marketing year would better reflect current crop cycles.

Witnesses also advocated adding language to this section that would allow the Board to recommend, subject to USDA’s approval, alternative marketing year periods. Witnesses stated that this authority would allow the industry to adjust to future changes in crop cycles without the need to undertake formal amendment of the marketing order language.

Witnesses also stated that conforming changes should be made to §§ 984.36, Term of office, and 984.48, Marketing estimates. According to the hearing record, Walnut Marketing Board member terms of office should be for a period of two years and should end on the same day as the marketing year. Currently a member’s term ends one month prior to the end of the marketing year, or on June 30. If implemented, the amended term of office would end on August 31.

Market estimates, which evaluate California walnut production and market activities, should also be amended to reflect current-day harvest cycles. If implemented, the amended market estimate would be calculated

using handler beginning inventory on September 1, and ending inventory on August 31, and would coincide with the amended marketing year.

According to the record, market estimates are typically calculated shortly after the beginning of the marketing year, prior to September 20. The proposed amendment would change this requirement to calculate market estimates prior to October 20. This proposal would maintain the amount of time between the beginning of the amended marketing year and the required market estimate calculation as currently required under the order.

Record evidence supports amending the marketing year for California walnuts from August 1 through July 31 to September 1 through August 31. This amendment would update the order’s marketing year to reflect the industry’s current growing cycle and would provide authority for the Board to recommend, with USDA approval, changes in future marketing year periods. Record evidence also supports conforming changes proposed to §§ 984.36, Term of office, and 984.48, Marketing estimates. Section 984.36 would be amended so that the end of a Board member’s term of office would coincide with the end of the amended marketing year (August 31) after a period of two years. Section 984.48 would be amended so that market estimates would be calculated using handler beginning and ending inventories coinciding with the amended marketing year. Market estimates would be required to be calculated prior to October 20.

No testimony in opposition to this proposed amendment was given. For the reasons stated above, it is recommended that § 984.7, Marketing year, be amended. Additionally, conforming changes to §§ 984.36, Term of Office, and 984.48, Marketing estimates, should also be made.

#### *Material Issue Number 2—Definition of “Pack”*

Section 984.13, To handle, should be amended to include the act of packing walnuts as a handling function. In addition, § 984.15, Pack, should be amended to include shelling, and should be modified so that packing is applicable to both inshell and shelled walnuts.

According to the hearing record, the order currently defines “to handle” as to “sell, consign, transport, or ship, or in any other way, to put walnuts into the current of commerce”. The definition does not include the specific act of packing. “Pack”, as currently defined in the order means, “to bleach, clean,

grade, or otherwise prepare inshell walnuts for market." Pack is not currently applicable to shelled walnuts.

Witnesses stated that the proposed amendment to the definition of "handle" would more accurately reflect current industry practices. Witnesses described present day situations where a grower may have his or her product cleaned by a packer. The packer cleans and grades the product to meet the standards specified under the order and prepares the product for market. Through the packing process, the product is typically inspected and certified to meet order requirements.

Witnesses explained that because the current definition of "handle" does not include the term "to pack" and the activities associated therewith, the packer is not subject to the reporting or assessment requirements under the order. Witnesses explained that because inspection and certification of the product is conducted under the care of the packer, subjecting the packer to reporting and assessment requirements of the order would result in a more efficient and accurate tracking system for California walnuts. Witnesses stated that packers should be responsible for reporting the amount of walnuts processed by their facility to the Board, and for paying assessments on those walnuts, as is currently required for walnut handlers. Witnesses also explained that if this amendment were implemented there would be approximately 5 packer entities that would qualify as handlers under the new definition.

Witnesses stated that the definition of "pack" under the order should be revised to include the act of shelling and should apply to both inshell and shelled walnuts. Currently, the definition of "pack" only applies to activities preparing inshell walnuts for market.

In the past, packers packed primarily inshell walnuts for sale during traditional holiday seasons and were not responsible for inspection certification prior to shipping product to market. At that time, shelled walnuts did not comprise a large portion of the market, and therefore were not included. According to the record, shelled walnuts have become increasingly important in terms of industry sales, specifically to the baking and confectionary industries. As a result, many packers now include the function of shelling as part of the activities undertaken to prepare walnuts for market. For this reason, witnesses stated that act of "shelling" should be included in the definition of "pack."

Record evidence supports adding the act of packing to the definition of handle. This amendment would facilitate more accurate tracking of California walnuts prepared for market, including inspection and reporting requirements as they relate to the collection of assessments. Record evidence also supports adding the act of shelling to the definition of "pack" as it would modify the term to be applicable to both shelled and inshell walnuts.

There was no opposition testimony given against this proposed amendment. For the reasons stated above, it is recommended that § 984.13, To handle, should be amended to include the act of packing walnuts as a handling function. In addition, § 984.15, Pack, should be amended to include the term "to shell" and the definition should be modified so that packing is applicable to both inshell and shelled walnuts.

#### *Material Issue Number 3a— Restructuring of the Board*

Sections 984.35, Walnut Marketing Board, and § 984.14, Handler, should be amended to remove all references to cooperative membership on the Board, to redistribute member seats among districts, and to provide designated seats for any handler handling 35 percent or more of production, if such handler exists.

Witnesses explained that when the order was established, a cooperative marketing association represented a majority share of California walnut production. Board structure accommodated representation of this large cooperative by allocating two grower and two handler seats out of a total of 10 member seats to cooperatives. The remaining seats were divided between the order's two districts, with one grower and one handler member being selected from each district, respectively, for a total of four non-cooperative member positions.

An additional grower seat was awarded to cooperatives if they represented more than 50 percent of production. Otherwise, the additional grower seat was filled as an at-large non-cooperative member position. Only growers not affiliated with cooperatives were eligible to fill the at-large seat, and that member could be from either district. Lastly, the Board nominated a public member, who was not affiliated with the growing or handling of California walnuts. Provisions for Board structure in the absence of a large cooperative was not contemplated when the order was promulgated, and thus was not provided for in the order.

According to the hearing record, the recent transition of the industry's largest

cooperative from a cooperative entity to a publicly held company was the impetus for this proposal. Witnesses expressed the need to modify the Board structure to provide for representation that accurately reflects the current industry. Witnesses advocated that the Board structure should maintain the current number of Board members and alternates, and that the allocation of member seats between grower and handler positions should remain the same (meaning 4 handler member seats, five grower member seats and one public member). However, witnesses recommended modifying the allocation of Board representation according to two possible scenarios. The two scenarios include: (1) Membership allocation that accommodates the existence of a handler handling 35 percent or more of production and, (2) membership allocation in the absence of such handler.

Witnesses stated that in the first scenario, a handler handling 35 percent or more of the crop would be afforded a designated number of seats, and nominations for those seats would be conducted by the handler. The Board would conduct all other member nominations.

In the second scenario, none of the Board membership positions would be allocated to a specific entity, and all nominations would be conducted by the Board. Proposed modifications to nomination procedures are further discussed under Material Issue No. 3b.

Evidence presented at the hearing outlines the following Board structure and membership allocation in the event that a handler representing 35 percent or more of production exists:

The Board would consist of 10 members and alternates, including one public member and alternate. Two handler members and two grower members would represent the handler handling 35 percent or more of production. Grower members filling these seats would be growers that deliver their product to that handler. Handler members would be either employees or officers of that handler.

Two handler members would represent handlers that do not handle 35 percent of production. Two grower members would be growers that do not market their product through the handler that handles 35 percent or more of the production. One grower member would represent District 1, and one grower would represent District 2.

One member would be an at-large grower member who does not market his or her product through the handler that handles 35 percent or more of the production. A public member would be

nominated by the Board and would have no affiliations with the industry as a handler or grower.

In the event that no handler handles 35 percent or more of the crop, the following Board structure is proposed:

The Board would consist of 10 members and alternates, including one public member and alternate. Two handler members and two grower members would represent District 1. Two handler members and two grower members would represent District 2. One member would represent the production area at-large. A public member would be nominated by the Board and would have no affiliations with the industry as a grower or a handler.

The proposed amendment and hearing record pertaining to this scenario does not specify whether the at-large member seat is allocated to a grower or handler. However, as previously discussed, witnesses advocated that the allocation of member seats between growers and handlers should not change as a result of the amendment. Current order language allocates the at-large seat to growers in all situations. In addition, scenario 1 of the proposed amendment allocates the at-large seat to growers. USDA therefore recommends modifying the proposed amendatory language to specify that the at-large seat under scenario 2 be allocated as a grower seat. This would achieve the intent of the industry by making the number of grower and handler seats consistent with the allocation under current order requirements.

Witnesses stated that 35 percent was determined to be a reasonable level at which a handler should be afforded designated seats on the Board. Witnesses also stated that the determination of whether or not a handler qualifies as handling 35 percent or more of the crop should be based on a calculation which averages the crop handled for the two years prior to the year in which the nominations are made.

Witnesses recognized that the potential scale of the impact of Board recommendations increases with the volume of product handled, and that any entity holding a major interest at or above the proposed 35 percent should be afforded representation. According to record evidence, there are 44 handlers that handle California walnuts. Current distribution of industry production among those handlers indicates that any handler handling 35 percent or greater of the total crop would be a major handler and therefore should be guaranteed representation on the Board.

Witnesses also provided testimony regarding allocation of Board membership in the event that there were two or more handlers handling 35 percent or more of production.

Witnesses testified that the proposed language in Material Issue No. 6, Authority to Reestablish Districts and Change Board Structure, includes a provision that would allow the Board to make recommendations, subject to the Secretary's approval, to revise the groups eligible to be represented, if such situation occurred.

In addition to amending § 984.35, Walnut Marketing Board, witnesses identified necessary changes in § 984.14, Handler. The current order definition of handler includes the term "cooperative handler." Witnesses stated that a revised definition of the term handler would remove the distinction between cooperative and independent handlers and simplify the definition.

No opposition to this proposed amendment was offered at the hearing. Record evidence supports the amendment of § 984.35, Walnut Marketing Board, and therefore, § 984.14, Handler, should be amended to remove all references to cooperative membership on the Board and to provide designated seats for a major handler, if such handler exists.

This proposal should also be modified to clarify that the at-large seat proposed in the revised Board structure for the industry when a handler handling 35 percent or more of the crop does not exist should be allocated as an at-large grower seat.

#### *Material Issue Number 3b—Nominations*

Sections 984.37, Nominations, and 984.40, Alternate, should be amended to reflect proposed changes in the Board structure, as outlined in Material Issue No. 3a.

According to record evidence, current nomination procedures are designed to accommodate cooperative membership on the Board. As described in Material Issue No. 3a, above, Board membership is presently configured to include 4 cooperative seats (2 grower and 2 handler), 4 non-cooperative seats (2 grower and 2 handler), one grower seat that is either a cooperative or non-cooperative seat, depending on the cooperative's share of production, and one public member seat.

Current nomination procedures allow for all cooperative seat nominees to be selected by the cooperative and forwarded to the Secretary for approval and appointment. According to the record, current nomination procedures do not specify the method of nominee

selection by the cooperative. The cooperative nominees selection process is independent of the Board.

All noncooperative seat nominees are selected through a ballot nomination process overseen by the Board staff, and forwarded to the Secretary for approval and appointment. Board staff is responsible for identifying all parties interested in filling Board member seats. Once a list of nominee candidates is identified, nomination ballots are sent out to all growers and handlers not associated with the cooperative. Board member nominations are given to the parties receiving the highest and second highest number of votes for their District and member seat. The names of the nominees are then forwarded to USDA for approval and appointment by the Secretary.

The public member is selected by the Board members, and then forwarded to the Secretary for approval and appointment.

According to the hearing record, the revised nomination procedures would be as follows:

In the event that a handler who handles 35 percent or more of the crop exists, nominees to fill Board seats designated for that handler would be selected by that handler and forwarded to the Board for approval. The Board would include those nominations with the other nominees and submit them to the Secretary for approval and appointment.

Accordingly, based on the hearing record, USDA recommends modifying the proposed language in § 984.37(c)(1) as published in the Notice of Hearing by removing the following language: "In such a manner that is consistent with the requirements of nominations of growers conducted by the Board. The two persons receiving the highest number of votes for the grower positions attributed to that handler (Groups (b)(2) of § 984.35) shall be nominees. The two persons receiving the third and fourth highest number of votes shall be designated as alternates." The removed statement should be replaced with the following statement: "And the names of the nominees shall be forwarded to the Board for approval and appointment by the Secretary." The USDA also recommends modifying the proposed language in § 984.37(c)(2) as published in the Notice of Hearing by removing the following language: "In such a manner that is consistent with the requirements of nominations of handlers conducted by the Board. The two persons receiving the highest number of votes for the major handler positions shall be nominees. The two persons receiving the third and fourth

highest number of votes shall be designated as alternates." The removed statement should be replaced with the following statement: "And the names of the nominees shall be forwarded to the Board for approval and appointment by the Secretary."

Witnesses also stated that the determination of whether or not a handler qualifies as handling 35 percent or more of the crop should be based on a calculation which averages the crop handled for the two years prior to the year in which the nominations are made.

Proposed language published in the Notice of Hearing does not state this requirement. Moreover, the hearing record does not state how the 35 percent threshold should be applied for the nomination of new Board members if this proposed amendment were to be implemented in 2007, when a two year average calculation would capture the transition of the cooperative to a publicly traded company. For this reason, USDA recommends the following calculation and proposes to modify order language accordingly:

If this proposed amendment is implemented, the 35 percent threshold for the first nominations held following implementation should be calculated using an average of the crop handled for the year in which nominations are made and the crop handled for the year prior to the nomination. This recommendation considers the recent transition of the industry's largest cooperative to a publicly held company. For all future nominations, the 35 percent crop handling calculation should be based on the average of the crop handled for the two years prior to the year in which nominations are made.

Further, USDA also proposes adding the following language to the beginning of § 984.37(c), as published in the Notice of Hearing: "A calculation to determine whether or not a handler who handles 35 percent or more of the crop shall be made prior to nominations. For the first nominations held upon implementation of this language, the 35 percent threshold shall be calculated using an average of crop handled for the year in which nominations are made and one year's handling prior. For all future nominations, the 35 percent handling calculation shall be based on the average of the two years prior to the year in which nominations are made."

Witnesses clarified that any grower delivering all of his or her production to the handler with designated grower seats would be considered eligible for nomination by that handler. Any grower delivering part of his or her production

to the handler in question would have the option of selecting whether or not they would participate in that handler's nomination process and serve as a grower member nominated to fill that handler's grower representation on the Board. A grower would not be eligible for nomination as both a grower representative of a major handler and as an independent grower on the Board.

According to the hearing record, owners, employees or officers of the handler handling 35 percent or more of the crop would be eligible as nominees for that handler's designated handler seats.

All nominees for remaining, non-handler-designated seats (with the exception of the public member) would be selected through a ballot nomination process overseen by the Board staff (the current non-cooperative nominee selection process, described above), and then forwarded to the Secretary for approval and appointment. The public member nominee would be selected by the Board and forwarded to the Secretary for approval and appointment.

Record evidence states that in the event a handler handling 35 percent or more of the crop does not exist, all Board nominees (with the exception of the public member) would be selected through a ballot nomination process (the current non-cooperative nominee selection process, described above). Nominees would then be forwarded to the Secretary for approval and appointment. The public member would be selected by the Board and then forwarded to the Secretary for approval and appointment.

Regarding proposed amendments to § 984.40, this section would be modified by removing all references to cooperative member seats in order to conform with the proposed changes to § 984.37. USDA recommends modifying the amendatory text as published in the Notice of Hearing by removing the last sentence of paragraph (b) of this section that refers to qualification of handler Board members to serve as temporary alternate members for other handlers. It was not the intention of the Board to propose this language and it was published in the Notice of Hearing by error.

No opposition to this proposed amendment was offered at the hearing. Record evidence supports the amendment of § 984.37, Nominations, and 984.40, Alternate, to reflect proposed changes in the Board structure, as outlined in Material Issue No. 3a. Section 984.37(c), and paragraphs §§ 984.37(c)(1) and 984.37(c)(2) should also be modified as recommended by USDA above. The last

sentence of § 984.40 should also be removed, as recommended by USDA.

#### *Material Issue Number 4—Qualify by Acceptance*

Section 984.39, Qualify by acceptance, should be amended to require Board nominees to submit a written qualification and acceptance statement prior to selection by USDA.

This proposed amendment would modify the current acceptance procedure for persons nominated to serve on the Board. Currently, the acceptance procedure for persons nominated and selected to serve on the Board involves a two-step process. First, persons nominated for consideration and possible appointment to the Board by USDA are required to complete a form indicating their eligibility to sit as a member of the Board. Once appointed by USDA, nominees must then sign an additional form indicating their acceptance of the appointment. If this amendment were implemented, the two steps could be combined into one, thus resulting in less paperwork, a shorter acceptance procedure, and improved efficiency in the acceptance process. The change means that when a nominee submits a statement confirming their eligibility, the nominee will also in that statement agree to serve if the Secretary appoints the nominee to the Board.

Record evidence supports this proposed change. No opposition to this proposed amendment was presented at the hearing. For the reasons outlined above, § 984.39, Qualify by acceptance, should be amended.

#### *Material Issue Number 5—California Walnut Board*

Sections 984.6, Board, and 984.35, Walnut Marketing Board, should be amended to change the name of the Walnut Marketing Board to the California Walnut Board.

Witnesses explained that the current use of the word "marketing" in the Board's title is confusing to persons not familiar with federal marketing order programs. The Board's activities involve generic promotion of California walnuts. Witnesses stated that the proposed name of "California Walnut Board" would more accurately represent the Board's responsibilities.

Witnesses also stated that identifying their industry's product as a product of California is particularly important in foreign markets, where the California name is often associated with a high level of quality.

Record evidence supports this proposed change. No opposition to this proposed amendment was presented at the hearing. For the reasons outlined

above, § 984.6, Board, should be amended.

*Material Issue Number 6—Authority To Reestablish Districts and Change Board Structure*

A new paragraph (d) should be added to § 984.35, Walnut Marketing Board, to add authority to the order to reestablish districts, reapportion members among districts, and revise groups eligible for representation on the Board. The intent of this proposal is to provide the Board with a tool to more efficiently respond to the changing character of the California walnut industry. In recommending to the Secretary any such changes, the following would be considered: (1) Shifts in acreage within districts and within the production area during recent years; (2) the importance of new production in its relation to existing districts; (3) the equitable relationship between Board apportionment and districts; (4) changes in industry structure and/or the percentage of crop represented by various industry entities resulting in the existence of two or more handlers handling 35 percent or more of the crop; and (5) other relevant factors.

Testimony indicates that significant changes have occurred in both the production base and industry demographics of the California walnut industry since the order was implemented. These changes suggest that flexibility in adapting to the changing character of the industry is important to the administration of the order. Witnesses stated that the order's ability to remain effective over time would be reliant on its ability to change with the needs of the industry. In this regard, witnesses proposed adding authority to the order that would allow for certain aspects of the Board's structure to be reconsidered, including: Reestablishment of districts, reapportionment of members among districts, and revisions to groups eligible for representation on the Board.

Witnesses stated that the authority to reapportion and redistrict districts within the production area would be important. According to the hearing record, walnut production has shifted over time. Competition between agriculture and urban growth for land has served as an incentive for walnut production to locate to areas previously not cultivated. Moreover, new varieties of walnuts have allowed growers to produce walnuts in areas that would not have been suited for traditional varieties of walnuts. Witnesses stated that the need to adjust district boundaries, or reallocate representation of Board seats among districts, would be important to

maintain accurate representation of shifting production within the production area.

According to the record, the authority to revise groups eligible for representation on the Board would include modifying the proportion of grower to handler seats on the Board, as well as modifying representation of entities either producing or handling a major portion of the crop.

Witnesses testified that careful industry analysis would lead to sound recommendations to USDA regarding reapportionment of members among districts, reestablishment of districts, or revisions in groups eligible for representation on the Board. If this authority were added, the Board could, at regular meetings, review its current structure using the points of consideration mentioned above. Upon completing this analysis, the Board could make a recommendation to USDA for such changes described above. Implementation of this authority would allow these changes to be pursued through the informal rulemaking process.

Given the changes that the California walnut industry has seen over time, flexibility to change the composition of the Board in step with the evolving needs of the industry would be an important tool. Witnesses stated that this authority would allow the Board to more effectively represent the industry as production and member representation demands shift. It would ensure that the Board appropriately represented the industry.

There was no opposition to the above proposal. Record evidence supports amending the order to add authority to reestablish districts, reapportion members among districts, and revise groups eligible for representation on the Board. This amendment would allow the Board, given due analysis and consideration of key factors and USDA approval, to more quickly adapt to changes within the industry. Accordingly, USDA is proposing that a new paragraph (d) be added to § 984.35, as proposed.

*Material Issue Number 7—Voting Procedures*

Section 984.45, Procedure, should be amended to add percentage requirements to quorum and voting procedures, to add authority for Board meetings to be held by telephone or by "any other means of communication", and to add authority for the Board to vote by "any other means of communication." This proposal would also add authority for the Board to recommend the minimum number of

votes that must be met when voting by any of those methods, and any other necessary procedures. In addition, this proposal would result in a conforming change to § 984.48(a), Marketing estimates and recommendations.

Witnesses stated that references to the meeting quorum requirement in this section should be amended to include a percentage equivalent of the current six-out-of-10-member minimum, or sixty percent. In addition, witnesses supported modifying the order language regarding voting requirements to state that a sixty-percent super-majority vote of the members present at a meeting should be required of all Board decisions, except where otherwise specifically provided. The order currently states that a majority vote is needed, with no percentage equivalent specified.

Witnesses stated that a conforming change should also be made to § 984.48(a), Marketing estimates and recommendations. The proposed conforming change would change the current six-out-of-10-member minimum vote requirement for the adoption of a marketing policy to sixty percent of the Board.

According to the record, the order currently requires that all Board meetings be held at a physical location. Witnesses stated that the order should be amended to allow for some meetings to be held using "other means of communication", such as telephone or videoconferencing. Witnesses stated that use of new communication technology would result in time savings while still allowing the Board to conduct its business. For example, telephone or videoconferencing technology would be helpful in providing Board meeting flexibility during harvest season when Board members find it more challenging to take time away from the field.

Additionally, short assembled meetings held to discuss non-controversial or administrative issues do not justify Board members' time and travel expenses. For this reason, witnesses stated that the authority to meet via teleconference call or videoconference, or any other means of communication recommended by the Board, could result in a more effective use of each member's time.

Witnesses stated that teleconferencing or videoconferencing should only be used as a method for conducting meetings when the meeting agenda does not contain issues that require a significant amount of deliberation, such as establishing the recommended rate of assessment.

According to the record, voting requirements for meetings other than assembled meetings should be established through informal rulemaking by USDA upon recommendation of the Board. Witnesses stated that procedures specific to each different method of meeting may need to be established. For example, while videoconferencing involves technology that allows each member to see the other members in attendance at the meeting, witnesses stated that any voting should continue to be verified through a written accounting that confirms the original votes made at the meeting. Similarly, votes made by teleconference (or telephone) would need to be followed by the submission of signed votes to the Board office by mail, or by fax or e-mail that contains a scanned copy of the original with the member's signature. Thus, witnesses stated that adding authority for the Board to recommend voting requirements and procedures would be important in order to ensure accurate and fair voting methods for each form of communication.

Witnesses speaking in favor of this amendment identified a sentence in paragraph (c) of § 984.45 as published in the Notice of Hearing that was not intended to be included in the proposed language. This sentence reads, "When any proposition is to be voted on by any of these methods, one dissenting vote shall prevent its adoption." Witnesses stated that this sentence is part of the current order language and was intended to be replaced the following sentence: "The Board, with the approval of the Secretary, shall prescribe the minimum number of votes that must be cast when voting is by any of these methods, and any other procedures necessary to carry out the objectives of this paragraph."

Witnesses stated that it is the intent of the Board that voting guidelines for all types of non-traditional meetings can be recommended and adopted as appropriate for each type of technology used. For this reason, USDA recommends modifying the proposed language for § 984.45 as published in the Notice of Hearing by removing the sentence erroneously left in the proposed language.

There was no opposition testimony given against this proposed amendment. For the reasons stated above, § 984.45, Procedure, should be amended to add percentage requirements to quorum and voting procedures, to add authority for the Board to vote by "other means of communication", and to add authority for Board meetings to be held by telephone or by "any other means of

communication." The Board would be authorized to recommend voting procedures for votes taken by means other than at traditional meetings. The proposed language for this section should be modified as recommended by USDA. This amendment should also result in a conforming change to § 984.48(a), Marketing estimates and recommendations.

#### *Material Issue Number 8—Carryover of Excess Assessment Funds*

Section 984.69, Assessments, should be amended to add authority to carryover excess assessment funds.

According to the hearing record, the order currently states that any assessment funds held in excess of the marketing year's expenses must be refunded to handlers. Refunds are returned to handlers in accordance with the amount of that handler's pro rata share of the actual expenses of the Board.

This proposed amendment would allow the Board, with the approval of the Secretary, to establish an operating monetary reserve. This would allow the Board to carry over to subsequent production years any excess funds in a reserve, provided that funds already in the reserve do not exceed approximately two years' expenses. If reserve funds do exceed that amount, the assessment rate could be reduced so as to cause reserves to diminish to a level below the two-year threshold.

According to the record, reserve funds could be used to defray expenses during any production year before assessment income is sufficient to cover such expenses, or to cover deficits incurred during any fiscal period when assessment income is less than expenses. Additionally, reserve funds could be used to defray expenses incurred during any period when any or all of the provisions of the order are suspended, or to meet any other such costs recommended by the Board and approved by the Secretary.

Record evidence supports that allowing a monetary reserve to be maintained would provide flexibility to the Board's in meeting its financial planning responsibilities. If the amendment were implemented, the Board would have the authority to decide, at regular Board meetings, whether or not to establish a monetary reserve. Currently, the Board may refund any excess assessment funds on a pro-rata basis to each handler or apply excess funds to defray administrative expenses. These options would remain available to the Board.

Record evidence supports amending the order to add authority to carryover

excess assessment funds as a financial reserve. There was no opposition testimony given against this proposed amendment. For the reasons stated above § 984.69, Assessments, should be amended.

#### *Material Issue Number 9—Contributions*

A new § 984.70, Contributions, should be added to the order to allow the Board to accept voluntary contributions to pay for expenses incurred under § 984.46, Research and development.

Witnesses stated that the order currently does not provide authority to accept voluntary contributions of any kind. If implemented, this proposed amendment would grant authority to the Board to accept voluntary contributions. Contributions could only be used to pay for research and development activities, and would be free from any encumbrances by the donor. According to the hearing record, the Board would retain oversight of the application of such contributions.

Witnesses supported this proposal by stating that it would provide the Board and the industry with valuable resources to enhance research and development activities. Record evidence indicates that any contributions used to further production research, market research and market development projects would not only benefit the industry, but also the consumer, through improved production technology and product information.

There was no opposition testimony given against this proposed amendment. For the reasons stated above, a new § 984.70, Contributions, should be added to the order to allow the Board to accept voluntary contributions.

#### *Material Issue Number 10—Reimbursement of Expenses*

Section 984.42, Expenses, should be amended to clarify that members and alternate members may be reimbursed for expenses incurred while performing their duties.

According to the hearing record, this proposed amendment would not have any impact on the current expense reimbursement activities of the Board. Rather, it would clarify and update order language to more clearly state that while Board members and alternates serve without compensation, expenses incurred while performing the duties of a Board member will be incurred.

For the reasons outline above, § 984.42, Expenses, should be amended. Record evidence supports this amendment, and no opposition to this proposal was offered at the hearing.

*Material Issue Number 11—Alternative Inspection Services*

Section 984.51 of the order provides the Board with the authority to designate an inspection service for mandatory certification of product under the order. This section should be amended to allow the Board to designate more than one inspection service, as long as the functions performed by each service shall be separate so as not to duplicate each other. Inspection and certification requirements ensure compliance with any regulations in effect under the authority of § 984.50, Grade quality and size regulations.

The purpose of this proposal is to allow handlers to take advantage of USDA's alternative inspection programs such as the Customer Assisted Inspection Program (CAIP) and the Partners in Quality Program (PIQ). Handlers who do not wish to use the alternative inspection services offered by USDA would continue to use the services of the Dried Food Administration of California (DFA) for traditional inspection services, such as end-line and lot inspections.

The proposal also specifies that "each service shall be separate so as to not conflict with each other", meaning that each inspection service would offer distinct and different services (i.e. PIQ vs. lot inspections) that do not duplicate each other. Accordingly, USDA recommends modification of the proposed regulatory language to clarify that the two inspection services will not duplicate the services of each other.

Witnesses speaking in favor of this proposal explained the importance of a handler's ability to take advantage of inspection services that would most economically fit the size and functions of his or her operation. Currently, all walnut product is inspected by DFA. While this inspection service has worked well for the industry for many years, the DFA inspection service does not accommodate inspection procedures that support larger handler economies of scale. Witnesses stated that USDA programs, such as PIQ and CAIP, are designed to fit larger scale handling operations, and therefore offer cost saving advantages that the DFA service does not. This proposal, if implemented, would allow handlers to use the alternative inspection programs offered by USDA.

Since the order's inception, the California walnut industry has used end-line inspection services provided by DFA. Under this scenario, samples of packed walnuts are examined and certified by licensed DFA inspectors at

the end of the handling and packing process.

The Federal-State Inspection Service has developed effective, less costly alternatives to traditional end-line inspection programs. One alternative, the PIQ program, is a documented quality assurance system. Under this program, individual handlers must demonstrate and document their ability to handle and pack product that meets all relevant quality requirements. Effectiveness of the program is verified through periodic, unannounced audits of each handler's system by USDA-approved auditors.

Under CAIP, USDA inspectors oversee the in-line sampling and inspection process performed by trained company staff. USDA oversight ranges from periodic visits throughout the day to a continuous on-site presence.

Witnesses at the hearing testified that a California walnut handler should be provided the flexibility to use either the DFA for traditional inspections, such as end-line or lot inspections or alternative programs such as PIQ or CAIP offered by USDA. Either inspection service can determine whether walnuts meet the minimum order requirements.

According to the hearing record, if this amendment was implemented, total industry savings of \$1 million or more could be realized on an annualized basis. Financial impact calculations provided by the Board indicate that introducing the option of using USDA PIQ and CAIP programs could result in an average per handler savings of \$156,067 for the industry's seven largest handlers. Given that the PIQ and CAIP programs are most beneficial for large handlers, as potential savings are correlated with economies of scale, it is unlikely that the smaller handlers would opt for these programs. Witnesses stated that no change in inspection costs is expected for handlers remaining with traditional DFA inspection services.

The Agricultural Marketing Service is responsible for ensuring that all handlers regulated under a marketing order program are in compliance with any regulations that are in effect. Marketing order administrative bodies have the responsibility of locally administering marketing order programs, which includes monitoring industry's compliance with order requirements, and reporting any violations to the Department for enforcement measures.

While the Department supports and encourages innovation and development of cost-saving procedures, it is important that the program maintain its integrity and that any quality or size regulations in effect are not

compromised. For this reason, USDA supports providing the Board with authority to recommend rules and regulations to administer this proposed amendment. To this end, the last sentence of paragraph (a) of § 984.51 should be modified to read as follows: The Board, with the approval of the Secretary, may prescribe procedures for the administration of this provision.

According to the hearing record, the industry's commitment to comply with grade and size regulations would not be compromised by allowing the industry to take advantage of the inspection service that best meets their needs. The authority to designate more than one inspection service would be a practical tool for the industry. It would allow grade and size standards to be maintained, yet could allow for time and cost-saving opportunities.

No opposition to this proposed amendment was offered at the hearing. Record evidence supports amending § 984.51 to allow more than one inspection service to be designated by the Board to inspect California walnuts. This proposal should also be modified as recommended by USDA above.

*Material Issue Number 12a—Quality Regulations and Different Regulations for Different Market Destinations*

Section 984.50, Grade and size regulations, should be amended to broaden the scope of quality regulations issued under the order. In addition, the authority for the Board to recommend different regulations for different market destinations should be added to this section.

Currently the order provides for the establishment of minimum grade regulations, but does not specify authority for the Board to recommend other types of quality regulations. Witnesses stated that adding this authority to the order would be an important tool.

Witnesses explained that the intent of this proposal is to broaden the scope of the order's authority to include the ability to regulate other factors of quality in addition to the current grade regulations, which reflect the U.S. Grade Standards for Walnuts. Quality standards, other than minimum grade, would be recommended by the Board for approval by USDA and would regulate certain product characteristics currently not regulated by U.S. Grade Standards for inshell or shelled walnuts. Other quality regulations could regulate, for example, moisture content or aflatoxin levels, if such proposed regulations were approved by USDA. These additional quality regulations could also regulate characteristics

currently regulated by U.S. Grade Standards at levels more stringent than existing grade regulations, if warranted for a specific market destination.

According to the hearing record, the order currently allows for the establishment of more restrictive minimum grade standards. The proposed amendment would replace this language with language specifying the Board's authority to recommend other quality standards in addition to minimum grade. Witnesses explained that the proposed modification in the order language would clarify that any additional quality standards established under the order would be guidelines recommended by the Board and would be different from grade regulation based on USDA grade standards. Witnesses stated that this distinction would reduce possible confusion in the administration of such standards.

According to the hearing record, the authority to establish different regulations for different market destinations would provide the Board with authority to formalize current trends in export market product specifications. Witnesses stated that many customers in export markets have unique product specifications in place to meet the consumer tastes and needs of their market. California walnut handlers shipping to those markets are already meeting those product specifications.

Witnesses explained that this proposed authority would result in the Board's ability to recommend uniform standards for all California walnut handlers shipping to specific export markets, if such regulation is needed. Different regulations for different market destinations would ensure that all product shipped into a particular export market would meet the same requirements. Product uniformity among California handlers serving those markets would ensure uniform quality of product, and a level playing field for foreign customers who are comparing product services from multiple handlers.

According to the hearing record, the addition of this authority is not intended to address any specific export market at this time. Witnesses stated that the market is currently functioning well, with quality product being shipped to consistently meet foreign customers' product specifications.

Witnesses stated, however, that the export market has become increasingly important to the California walnut industry. Witnesses noted that export market demand for California walnuts has increased nearly 35 percent over the past 5 years, making up a large portion

of the California walnut industry's ability to maintain positive producer returns within the context of increasing yields per acre and total industry production. Witnesses stated that ensuring product quality and uniformity is vital to the California walnut industry and its ability to maintain viable export market relationships. For this reason, witnesses stated that the authority to establish uniform guidelines for specific market destinations would be an important tool.

According to the hearing record, any proposed regulation specific to different market destinations would require deliberation among the Board members and approval by USDA.

Record evidence supports amending the order to broaden the scope of regulations issued under the order to include additional types of quality regulations. In addition, the authority for the Board to recommend different regulations for different market destinations should be added to this section. No opposition to this proposed amendment was offered at the hearing.

#### *Material Issue Number 12b—Processing of Shelled Walnuts*

Section 984.52, Processing of shelled walnuts, should be amended by adding authority to allow for shelled walnuts to be inspected after having been sliced, chopped, ground, or in any other manner changed from shelled walnuts, if regulations for such walnuts are in effect. The Act allows for the regulation of processed walnuts. This proposal would establish authority for the Board to recommend such regulations, subject to approval by the Secretary.

According to the hearing record, the order currently provides that handlers may only reprocess previously inspected walnuts that have been certified as meeting any size and grade regulations in effect. The order specifically provides that shelled walnuts may not be sliced, chopped, ground or otherwise altered unless such walnuts have been previously certified. Witnesses explained that this language was appropriate for the technology available to the industry when the order was promulgated. Such provisions were necessary in order to provide assurances that off-grade product did not enter into the stream of commerce.

Witnesses explained that more effective technology, which relies on laser color sorters and highly automated screening processes to eliminate defects throughout the sorting process, is now widely used by the industry. This current technology provides handlers with a sophisticated system of assurances that product entering the

market place meets minimum quality standards. For this reason, witnesses advocated amending the order language to allow the Board to recommend testing, certification, and minimum standards for processed walnuts. Witnesses stated that the reliability of current technology is such that provisions for handlers to inspect and certify product after further processing could be established, and that such provisions would facilitate flow of product through processing facilities yet maintain a minimum standard of quality.

New walnut product forms are regularly requested by both domestic and foreign customers. In the last 20 years, the industry has become much more capable of producing at a considerably higher level quality and of developing more specific types of products that meet the differing needs of individual customers. To capitalize on this growing capability, a number of witnesses expressed the view that an important tool for increasing sales is the ability to establish standards for walnut products for which no USDA standards currently exist.

The order currently requires shelled product to be certified as merchantable, that is, meeting the minimum USDA requirements prior to further processing. When handlers are processing for end users that require further processing, this certification represents a costly extra step. After the initial shelled walnut certification, the handlers employ their own quality control procedures to meet the higher customer specifications. This proposal would allow a single inspection at the end of the process that would serve both purposes. If implemented, this proposal would allow the Board to recommend modifications to allow certification of product after it has been modified or chopped, leading to cost savings in the handling process.

According to the hearing record, the proposed language would allow for walnuts to be sliced, chopped, ground or in any other manner altered if quality for such walnuts were established under § 984.50(d), Additional grade, quality and size regulation, as discussed in Material Issue No. 12(a), above. This amendment would also establish a new paragraph (c) to § 984.52, Processing of shelled walnuts, that would provide authority for the Board to establish any procedures as deemed necessary to insure that all walnuts are inspected prior to being placed into the stream of commerce. The proposed language would allow the Board to create guidelines that would ensure that processed walnut product would meet a

minimum standard, and that it would be certified as compliant with the regulation in effect under the order. Implementation of this authority would allow these changes to be pursued through the informal rulemaking process.

Given the changes that the California walnut industry has seen over time, flexibility to recommend regulation regarding the further processing of shelled walnuts prior to inspection and certification would be an important tool. Witnesses explained that as consumer demands for further processed product grows, increases in efficiency of product flow through the processing facilities would enable handlers to handle product more quickly, better satisfy their customers, as well as potentially reduce costs.

Record evidence supports amending the order to add authority to allow for shelled walnuts to be inspected after having been sliced, chopped, ground, or in any other manner changed from shelled walnuts. The record also supports amending the language to provide authority for the Board to recommend any necessary testing, certification or minimum quality standards for such product to ensure that the integrity of any California walnut product entering the stream of commerce is kept.

There was no opposition to the proposed amendment offered at the hearing. For the reasons outlined above, Section 984.52, Processing of shelled walnuts, should be amended as proposed.

#### *Material Issue Number 13—Paid Advertising and Promotion*

Amend the order by adding authority for marketing promotion and paid advertising. This proposal would amend § 984.46, Research and development. This order provision currently authorizes only production research, marketing research and development activities.

This authority would enable the Board to develop more efficient marketing and distribution techniques for walnuts produced in the production area. Promotional activities, including paid advertising, could lead to greater market exposure and consumer demand for California walnuts, thereby supporting increased returns for growers.

According to the record, this authority would enable the Board to fund promotion efforts. Such activities could be conducted by the Board itself or be contracted out to other parties. Witnesses stated that it is important to include promotion and paid advertising

under the Federal marketing order, as these activities are vital to increasing demand for walnuts which promotes the long-term health of the industry.

The record evidence shows that walnut acreage in California has increased from 193,000 acres in 1997 to an estimated 219,000 acres in 2005. In that same time period, overall tonnage of California walnuts increased from 269,000 tons to 355,000 tons, or an increase in average yield from 1.39 tons per acre to 1.62 tons per acre. Witnesses testified that acreage and production will continue to increase, making promotion and paid advertising all that more important.

Witnesses explained that the California Walnut Commission (Commission), and other entities within the industry, has been responsible for past promotion and paid advertising activities. Demonstrated success of these promotion activities has led to industry support for adding this authority to the order. Testimony indicated that current marketing and promotion activities range from in-store promotion activities, to featured articles in magazines, inclusion of walnuts in cooking shows and promotion by celebrity chefs, and paid advertising.

A representative of the Board testifying at the hearing stated that, since 2001, both volume and prices of California walnuts have shown annual increases. Increased market demand can be tied to the Commission's success in working with the market outlets, the retail sector and consumers, with domestic consumption increasing by over 34 percent in the past 5 years. Witnesses attribute the industry's ability to successfully meet the challenge of increasing production to these promotion activities.

Witnesses explained that the industry wants to further its ability to conduct these activities by adding promotion authority to the order. According to the hearing record, authority to conduct promotion and paid advertising under the order would ensure that those activities continue in a consistent manner. Board member input into the development of promotional programs would also ensure that these activities, and the use of assessment funds to support them, would remain responsive to industry needs. Witnesses also indicated that this authority would be equally beneficial to small and large grower and handler entities.

According to the record, adding this authority to the order would provide the Board with the flexibility to use promotional activities, including paid advertising, to assist and improve the marketing, distribution and

consumption of California walnuts. The use of assessments for such promotion would be an important component to increasing demand and consumption of California walnuts, and would be beneficial to all members of the industry. The industry does not contemplate using this provision immediately. However, it wants to have the ability to consider these activities in the future. The impacts of any increased assessments resulting from implementing any program would be considered before a recommendation is made.

There was no opposition testimony on this issue. The record supports adding authority for promotion and paid advertising to § 984.46, Research and development.

#### *Material Issue Number 14—Updating Order Terminology*

Section 984.21, Handler carryover, and § 984.67, Exemptions, should be amended to replace the terms "carryover" with "inventory," and "mammoth" with "jumbo," respectively, to reflect current day industry nomenclature. Conforming changes should also be made to § 984.48, Marketing estimates and recommendations, and § 984.71, Reports of handler carryover.

Section 984.21, Handler carryover, defines the amount of California walnuts (both merchantable as well as the estimated quantity of merchantable walnuts to be produced from shelling stock and unsorted material), wherever located, held by California walnut handlers at any given time. Witnesses explained that the current term "carryover" is misleading in that the term implies the amount of inventory held by handlers from one marketing year to the next. Witnesses stated that the term "inventory" would more accurately convey the intent of this definition, and would also reflect current day calculations of walnut availability.

According to the record, conforming changes should also be made to § 984.48, Marketing estimates and recommendations, and § 984.71, Reports of handler carryover. Both of these sections make references to handler "carryover." In order to provide consistency in the order's terminology, witnesses stated that these sections should incorporate the updated term "inventory."

Section 984.67, Exemptions, of the order provides for situations under which California walnuts may be exempted from complying with order regulations. One exemption is applicable to lots of merchantable

inshell walnuts that are mammoth size or larger, as defined by the United States Standards for Walnuts in the Shell.

Witnesses stated that given the new varieties currently being produced in the industry, the term "mammoth" no longer applies. New walnut varieties do not produce walnuts that fit this size description. According to record evidence, the current production's equivalent to "mammoth" size is "jumbo" size, as defined by the United States Standards for Walnuts in the Shell. Thus, witnesses stated that the order language should be updated to reflect the industry's current terminology and size of walnuts being produced.

Record evidence supports this proposed change. The term "carryover" should be changed to "inventory", and the term "mammoth" should be changed to "jumbo." No opposition to this proposed amendment was presented at the hearing. For the reasons outlined above, § 984.21, Handler carryover, and § 984.67, Exemptions, should be amended. Conforming changes should also be made to § 984.48, Marketing estimates and recommendations, and § 984.71, Reports of handler carryover.

#### *Material Issue Number 15a— Interhandler Transfers*

Section 984.59, Interhandler transfers, should be amended to clarify the interhandler transfer provision of the order, and to add authority for the Board to recommend to USDA regulations, including necessary reports, for administrative oversight of such transfers.

According to the hearing record, current order language specifies two scenarios under which certain provisions relating to interhandler transfers are regulated. These include: (1) Transfers of inshell walnuts for the purpose of packing or shelling; or, (2) interhandler transfers that are made to meet reserve obligations. In both scenarios, the receiving handler must comply with regulations that are in effect under the order. The order further provides that any interhandler transfers that is not included under the above two scenarios, the first handler of such walnuts shall comply with any regulations in effect under the order.

Witnesses stated that it would be beneficial to simplify current order language so that all interhandler transfers were considered a "sale of inshell and shelled walnuts within the area of production by one handler to another." Witnesses explained that the proposed language restated the current

application of this provision in walnut transactions in simpler terms.

Witnesses also explained that authority for the Board to recommend rules and regulations, including necessary reports for such transfers, should be added to the order. This proposed authority would provide the Board with flexibility to adapt interhandler transfer rules and regulations as needed.

Concurrent with the proposal to add this authority, witnesses stated that the sentence, "The receiving handler shall comply with the regulations made effective to this part," as published in the Notice of Hearing, should be removed. Witnesses stated that the intent of this proposal was to replace the above sentence with the proposed authority for the Board to recommend such regulations. For this reason, USDA is recommending that this sentence be removed.

No opposition to this proposed amendment was presented at the hearing. Record evidence supports this proposed change. The order provisions regarding interhandler transfers should be simplified, as proposed. The authority for the Board to make recommendations to establish methods and procedures, including reporting requirements, for overseeing interhandler transfers should also be added. The proposed language for this section should be modified as recommended by USDA.

#### *Material Issue Number 15b—Reporting Requirements*

Section 984.73, Reports of walnut receipts, should be amended to clarify that the Board may require reports from handlers or packers that involve placing California walnuts into the stream of commerce.

According to the hearing record, current authority provided in this section only applies to the reporting of handler walnut receipts from growers. Witnesses stated that this authority should be broadened to include interhandler transfer receipts, or any other entity as recommended by the Board and approved by the Secretary.

Witnesses explained that this proposal is intended to support other proposed amendments to the order, such as the proposed clarification of interhandler transfer provisions discussed under Material Issue No. 15(a), above, by further clarifying the Board's authority to recommend reporting provisions necessary to obtain accurate tracking information of California walnuts.

No opposition to this proposed amendment was presented at the

hearing. Record evidence supports this proposed change. The authority for the Board to request handler reports of walnut receipts should be broadened to include receipts from other handlers, entities or activities that involve placing California walnuts into the stream of commerce.

#### *Material Issue Number 16—Trade Demand*

Section 984.22, Trade demand, should be amended to change the order language to state "United States and its territories," rather than name "Puerto Rico" and "The Canal Zone".

Under the marketing order, the Board is required to calculate a trade demand for all inshell and shelled walnuts. Calculation of domestic trade demand, or the anticipated amount of California inshell and shelled walnuts that are needed to satisfy the domestic market, is important in determining the need for volume regulation, and the amount of free versus reserve tonnage if volume regulation is in effect.

Witnesses explained that the reference to "Puerto Rico" and "The Canal Zone" in the order is outdated. According to the record, this terminology was incorporated into the order at the time of promulgation. Witnesses stated that the order language should be updated to reference "United States and its territories".

According to record evidence, this amendment would not impact trade demand calculations under the order since the purpose of the reference is to accurately identify the amount of shelled or inshell walnuts demanded by the United States, including its territories. Thus, while the terminology identifying the geographic regions included in the calculation would change, the intent of the original language would remain unchanged.

Record evidence supports this proposed change. No opposition to this proposed amendment was presented at the hearing. For the reasons outlined above, § 984.22, Trade demand, should be amended.

#### *Material Issue Number 17— Relationship With the California Walnut Commission*

Witnesses supported the addition of § 984.91, Relationship with the California Walnut Commission, by stating that the Board should have authority to deliberate, consult, cooperate and exchange information with the California Walnut Commission (CWC). Any sharing of information between the two organizations would be kept confidential in accordance with the provisions of section 10(i) of the Act.

Record evidence indicates the CWC and the Federal marketing order program are currently administered out of the same office location and employ the same staff. Thus, this proposal, if implemented, would formalize the relationship that currently exists between the two entities. Witnesses stated that collaboration between the two programs leads to reduced administrative costs, as much of the information collected by each entity can be shared.

For the reasons stated above, a new § 984.91, Relationship with the California Walnut Commission, should be added. No opposition to this proposal was presented at the hearing.

#### *Material Issue Number 18—Term Limits*

Section 984.36, Term of office, should be revised to establish a limit on the number of consecutive terms a person may serve as a member of the Board. Currently, the term of office of each member and alternate member of the Board is 2 years. There are no provisions related to term limits in the marketing order. Members and alternates may serve on the Board until their respective successors are selected and have qualified.

The record evidence suggests that term limits for Board members could increase industry participation on the Board, provide for more diverse membership, provide the Board with new perspectives and ideas, and increase the number of individuals in the industry with Board experience.

At the hearing, USDA proposed a period of 8 years as an appropriate limit to the number of years a member may serve consecutively. However, in other instances concerning Federal marketing orders containing term limit provisions, USDA has determined that a period of 6 years would be more appropriate. Accordingly, a limit of six years as the number of years that a member may serve consecutively would be in conformance with other marketing orders containing this provision and with established USDA practices regarding term limits. The proposed regulatory text has been modified to reflect this change.

Since the current term of office for members and alternates is 2 years, USDA is proposing that members serve no more than 3 consecutive two-year terms, or a total of 6 years. This proposal for term limits would not apply to alternate members. Once a member has served on the Board for 3 consecutive terms, or 6 years, the member could not serve as a member for at least one year before being eligible to serve again. However, the individual

could immediately begin serving as an alternate member after completing 3 consecutive terms as a member.

Industry witnesses presented testimony in opposition to this proposal. Although they agreed that increased industry participation in the program is desirable, witnesses stated that the application of term limits could be problematic. Testimony indicated that finding California walnut growers to serve on the Board is difficult. Witnesses noted that there have been times in the past when filling Board member positions has been difficult, and that recruiting new members is not easily done. Moreover, witnesses stated that industry members who currently serve on the Board bring knowledge and experience to the Board that would be difficult to replace.

USDA believes that any additional efforts necessary to find eligible growers and handlers who are willing to serve on the Board are offset by the benefits derived by broader industry participation in order operations. USDA recommends adding this requirement. Section 984.35, Term of office, should be amended to include tenure requirements. The proposed language should also be modified to reflect a proposed term limit of a total of six years, as discussed above.

#### *Material Issue Number 19—Continuance Referenda*

Section 984.89, Effective time and termination, should be amended to require that continuance referenda be conducted every six years to ascertain industry support for the order.

Currently, there is no requirement in the order that continuance referenda be conducted on a periodic basis. The USDA believes that growers should have an opportunity to periodically vote on whether a marketing order should continue. Continuance referenda provide an industry with a means to measure grower support for the program. Experience has shown that programs need significant industry support to operate effectively.

Under this proposal, USDA would consider termination of the order if continuance is not favored by at least two-thirds of those voting, or at least two-thirds of the volume represented in the referendum. This is the same as that for issuance and amendment of an order. Experience in recent years indicates that six years is an appropriate period to allow growers an opportunity to vote for continuance of the program. Therefore, the proposal sets forth that a referendum would be conducted six years after the year in which this

amendment is effective and every sixth year thereafter.

Several industry witnesses opposed periodic continuance referenda. They indicated that requiring unnecessary referenda would be costly and of little value to the industry or USDA.

The USDA believes, however, that growers should have an opportunity to periodically vote on whether the marketing order should continue, and that the minimal industry costs in time and money are well worth the periodic grower feedback afforded to the Board and the USDA by such referenda. Accordingly, USDA recommends adding a requirement that such referenda be conducted.

The USDA also proposed to make such changes as may be necessary to the order to conform to any amendment that may result from the hearing. All conforming changes have been identified and discussed in this document.

#### **Small Business Considerations**

Pursuant to the requirements set forth in the Regulatory Flexibility Act (RFA), the Agricultural Marketing Service (AMS) has considered the economic impact of this action on small entities. Accordingly, AMS has prepared this initial regulatory flexibility analysis.

The purpose of the RFA is to fit regulatory actions to the scale of business subject to such actions so that small businesses will not be unduly or disproportionately burdened. Marketing orders and amendments thereto are unique in that they are normally brought about through group action of essentially small entities for their own benefit. Thus, both the RFA and the Act are compatible with respect to small entities.

Small agricultural growers are defined by the Small Business Administration (SBA) (13 CFR 121.201) as those having annual receipts of less than \$750,000. Small agricultural service firms, which include handlers regulated under the order, are defined as those with annual receipts of less than \$6,500,000.

Interested persons were invited to present evidence at the hearing on the probable regulatory and informational impact on growers and handlers of the proposed amendments, and in particular the impact on small businesses. The record evidence shows that the proposed amendments are designed to enhance industry efficiencies and streamline administrative operations of the marketing order. The record evidence is that while some minimal costs may occur, those costs would be outweighed

by the benefits expected to accrue to the California walnut industry.

### Walnut Industry Background and Overview

According to the record, the California walnut industry currently has 44 handlers and approximately 5000 producers. The crop is produced in a region that spans approximately 400 miles in California's Central Valley.

Fifteen grower witnesses and 7 handler witnesses testified at the hearing. Using the SBA definition (\$750,000 in gross annual walnut sales), 7 of the grower witnesses identified themselves as large business entities and 6 as small business entities. All 7 handler witnesses identified themselves as being large business entities according to the SBA definition. Some of the handler witnesses were also growers. According to witnesses, 37 out of an industry total of 44 handlers would qualify as small business entities under the SBA definition. Also, under the order amendments contained herein, it is estimated that five packers would be considered handlers, the majority of whom would be considered small entities.

Based on information presented at the hearing, calculations describing an average California walnuts producer provide the following: Dividing 5000 producers by 219,000 bearing acres in 2005 indicates an average of 44 bearing acres per producer. Dividing 5000 producers by the two-year average crop value for 2003 and 2004 (\$414,950) yields an average walnut revenue per producer estimate of about \$83,000. According to the hearing record, more than 70 percent of California walnut producers would be classified as small producers according to the SBA definition.

According to a study presented at the hearing, entitled "Cost to Produce Walnuts in California" (prepared by Dr. Karen Klonsky, Department of Agriculture and Resource Economics, University of California Davis, 2006), typical average costs for a walnut orchard in the Sacramento Valley are \$2,460 per acre in full production. The costs are broken down as follows: (a) Land and trees, \$678 (28 percent), (b) cultural costs, \$667 (27 percent), (c) harvest, \$538 (22 percent), (d) equipment and buildings, \$302 (12%), and (e) cash overhead, \$275 (11 percent).

At an average grower price in recent years of \$0.62 per pound, a grower would need a yield of 2 tons per acre to break even, according to the study. The breakeven price at the State average yield of 1.5 tons per acre is about \$0.70

per pound, which is above the actual price received in most recent years, but equal to the 2004 average price received by growers.

Individual grower costs can vary considerably due to such variables as horticultural practices and varieties grown, and also due to orchard location and year of acquisition, and water availability and cost.

Although a majority of producers are considered small business entities, record evidence also indicates that producer revenue has increased over time. The National Agricultural Statistical Service (NASS) crop value estimate for 2004, \$451.75 million, was 38 percent higher than in 1995, and was the sixth successive yearly increase. Average revenue per acre in 2004 reached a record \$2,082.

Record evidence also indicates that acreage and production are trending upward. Production did not exceed 300,000 tons until 2001, but has exceeded that level for 4 out of the last 5 years. Witnesses stated that the five-year average production for 1996–2000 was 244,000 tons, compared to the five-year average production (2001–2005), which was 318,600 inshell tons.

According to the hearing record, a number of factors have contributed to increased production in recent years. New acres have been planted at a rate of three to five thousand acres per year, some of which are new varieties with higher yields. Witnesses explained that older varieties may yield 1,500 to 3,000 pounds per acre, due to both planting patterns and the typical yield of the variety. New varieties, such as the Chandler, will yield up to 6,000 pounds per acre. Newer plantings have led to a reduction in the cyclical peaks and valleys associated with the alternate-bearing characteristic of tree nuts. This, in turn, has facilitated better inventory management and has made the walnut industry a more reliable ingredient supplier to the food-processing industry.

According to the hearing record, the growing season commences in March of each year with harvest occurring between September and November, depending upon the variety. Inshell California walnuts are a seasonal item with 95 percent of the volume shipped between the months of September and December. This represents roughly 25 percent of the industry's production. Inshell walnuts are marketed primarily as a winter holiday food. According to the hearing record, the purchase of significant quantities of inshell walnuts occurs due to the tradition in many markets of displaying them with other

inshell nuts as part of winter holiday décor.

Shelled walnuts are marketed on a year-round basis, and represent about 75 percent of utilization. Large handler infrastructure investments have contributed substantially to the growth of the year-round shelled business, as well as the inshell business.

Over the past ten years sophisticated laser-sorting equipment and new varieties such as the Chandler have contributed to improved quality. Higher customer expectations have accompanied the improvements in technology and quality, with more demand for high-quality, high-specification California walnuts. Marketing success in Japan is cited as a prime example of this trend.

According to the hearing record, shelled walnuts are utilized in a variety of ways, with commercial baking believed to be the single largest utilization category. Retail consumption of walnuts packaged for use in the home has increased dramatically over the past several years. Shelled walnuts may be sold in packages ranging from 2.75 ounce retail packages to large bulk containers of 25 pounds or more for industrial users, wholesalers, and distributors. The last 12 years have seen substantial increases in snack food uses of walnuts, in addition to expansion of ingredient use beyond baking and confectionery items to include usage with salads, rice, and pasta.

A high degree of mechanization in the harvest has reduced the deleterious impact on nut quality from rain and other weather conditions. Once harvested, walnuts are taken to holding stations where a fibrous husk is removed, and the walnuts are then dried to approximately eight percent moisture. They are delivered to handlers for further processing, which includes cleaning, sorting, and shelling.

According to the hearing record, California walnuts rank eighth in exports over all the commodities grown in the state. The top three inshell export markets are Spain, Italy, and Germany. Five-year average export value (2000/01–2004/05) is approximately \$52 million, representing 63 percent of total export value for that five-year period. The key export markets for shelled-walnut utilization are: Japan, Germany, Spain, Israel, Korea, and Canada. Five-year average export value for those six countries is \$91.8 million, which is about 76 percent of the total value of shelled walnut exports.

California walnuts compete with walnuts grown in China, Turkey, France, Italy, Chile, North Korea, India, Vietnam, Argentina, Brazil, and many

areas within the former Soviet Union including Kazakhstan, Ukraine, Hungary, and Moldova. Within the European Union the major competition comes from France and Eastern Europe. In the Pacific Rim, major competitors include China and India.

**Material Issues**

The amendments included in this recommended decision would: change the marketing year; include “pack” as a handler function; restructure the Board and revise nomination procedures; rename the Board and add authority to change Board composition; modify Board meeting and voting procedures; add authority for marketing promotion and paid advertising; add authority to accept contributions, and to carry over excess assessment funds; broaden the scope of the quality control provisions and add the authority to recommend different regulations for different market destinations; add authority for the Board to designate more than one inspection service; replace outdated order language with current industry terminology; and other related amendments.

The USDA proposed three additional amendments: To establish tenure limitations for Board members, to require that continuance referenda be conducted on a periodic basis to

ascertain producer support for the order, and to make any changes to the order as may be necessary to conform with any amendment that may result from the hearing.

All of the proposals are intended to streamline and improve the administration, operation, and functioning of the program. Many of the proposed amendments would up-date the language of the order, thus better representing and conforming to current practices in the industry. The proposed amendments are not expected to result in any significant cost increases for growers or handlers. More efficient administration of program activities may result in cost savings for the Board. A description of the proposed amendments and their anticipated economic impact on large and small entities is outlined below:

**Designation of More Than One Inspection Service**

Proposal 11 would amend the order to add authority for the Board to designate more than one inspection service, as long as the functions performed by each service are separate and do not conflict with each other.

To ensure that walnuts are properly graded and meet marketing order minimum standards, the Board

currently arranges for inspection of walnuts prior to shipping for all walnut handlers. The marketing order currently authorizes contracting with one agency, the California-based Dried Fruit and Nut Association (DFA).

DFA inspects all walnuts that leave California to certify that they meet marketing order minimum standards. Operating as an out-going inspection service, samples of packed walnuts are examined and certified by licensed DFA inspectors at the end of the handling and packing process.

The following data representing current inspection costs, summarizing actual inspection cost data for 2004–05 for the entire industry (44 handlers), was presented at the hearing by Board representatives. According to the record, the 2004–05 cost to serve the 44 handlers was \$1.857 million, which is an average cost of just over \$42,000 per handler.

Since inspection costs depend largely on volume handled, the four largest handlers account for \$1.282 million, or 69% of total inspection expenditure in the 2004–05 crop year. The 37 smaller handlers account for \$412,172 in expenditure, about 22 percent of the total, averaging about \$11,000 per handler.

ANNUAL WALNUT INSPECTION COSTS USING DFA, 2004–05 CROP YEAR

	DFA cost	Number of handlers	Average per handler
Largest Handlers .....	\$1,282,362	4	\$320,591
Additional Large Handlers .....	162,487	3	54,162
Other Handlers .....	412,172	37	11,140
All Handlers .....	1,857,021	44	42,205

Source: Walnut Marketing Board.

The Federal-State Inspection Service (FSIS) has developed effective, less costly alternative inspection programs which do not require the continuous presence of a third party inspector at the end of the packing lines.

The PIQ program is a documented quality assurance system. Under this program, individual handlers must demonstrate and document their ability to handle and pack product that meets all relevant quality requirements. Effectiveness of the program is verified through periodic, unannounced audits of each handler’s system by USDA-approved auditors.

Under the Customer Assisted Inspection Program, or CAIP, USDA inspectors oversee the in-line sampling and inspection process performed by trained company staff. USDA oversight ranges from periodic visits throughout

the day to a continuous on-site presence.

DFA does not offer inspection services that operate similarly to the PIQ and CAIP programs.

Cost savings would occur by reducing the prevalence of double inspections under the current system. Currently, one inspection is undertaken to meet minimum USDA quality requirements specified in the marketing order. A second inspection is often required to meet the considerably higher standards of specific customers. Moving to a PIQ or CAIP program would greatly reduce inspection costs, because meeting higher standards under PIQ or CAIP would also ensure that an inspected lot met minimum marketing order standards.

Witnesses at the hearing testified that the California walnut industry should

allow handlers to take advantage of USDA’s alternative inspection programs such as the CAIP and the PIQ. Handlers who do not wish to use the alternative inspection services offered by USDA would continue to use the services of the DFA for traditional inspection services, such as end-line and lot inspections.

The proposal also specifies that “each service shall be separate so as to not conflict with each other”, meaning that each inspection service would offer distinct and different services (i.e. PIQ vs. lot inspections) so that the integrity of both programs can be maintained.

Witnesses speaking in favor of this proposal explained the importance of a handler’s ability to take advantage of inspection services that would most economically fit the size and functions of his or her operation. Currently, all

walnut product is inspected by DFA. While this inspection service has worked well for the industry for many years, the DFA inspection service does not accommodate inspection procedures that support larger handler economies of scale. Witnesses stated that USDA programs, such as PIQ and CAIP, are designed to fit larger scale handling operations, and therefore offer cost saving advantages that the DFA service

does not. This proposal, if implemented, would allow handlers to use the alternative inspection programs offered by USDA.

Several witnesses indicated that lowering costs to handlers would benefit growers because they expect that the cost reduction would be reflected in increased payments to growers.

Financial impact calculations provided by the Board (shown in the

table below) indicate that introducing the option of using PIQ or CAIP programs could result in savings of \$1.09 million, an average per handler savings of \$156,067 for the industry's seven largest handlers. Due to the high volumes handled, most of the savings accrue to the four largest handlers, estimated at \$1.05 million, or an average per handler of \$263,169.

#### WALNUT INSPECTION COST COMPARISON: DFA VS USDA FOR TOP 7 HANDLERS

	DFA	USDA PIQ/CAIP	Cost savings	
			Total	Per handler
Largest 4 Handlers .....	\$1,282,362	\$229,688	\$1,052,674	\$263,169
Additional 3 large handlers .....	162,487	122,692	39,795	13,265
Largest 7 Handlers .....	1,444,849	352,380	1,092,469	156,067

Source: Walnut Marketing Board.

Data from NASS indicate that the two-year average value of the 2003 and 2004 crops was about \$415 million. The current DFA inspection cost (\$1.857 million) represents a very small proportion of crop value, about 0.4 percent. If the largest 7 handlers used USDA for inspection at a cost of \$352,380 and the remaining 37 handlers continue to work with DFA at an estimated cost of \$412,172, then the combined cost of \$764,552 would represent 0.2 percent of the recent-year crop value.

Witnesses emphasized the cost effectiveness of having an additional inspection agency. If implemented, this proposal would facilitate the streamlining of handler operations to utilize the inspection service best suited to their operations.

Since potential savings are correlated with economies of scale, record evidence indicates that PIQ and CAIP programs would be most beneficial for large handlers. It is unlikely that the smaller handlers would initially opt for these programs. Smaller handlers that expand their operations in the future may realize benefits from switching to PIQ or CAIP. Witnesses stated that no change in inspection costs is expected for handlers remaining with traditional DFA inspection services. Therefore, no financial disadvantages are expected to result from this proposed amendment. If implemented, this proposal may result in an overall decrease in costs of inspection to the industry.

#### Inspection of Sliced, Chopped or Ground Shelled Walnuts

Proposal 12b would add authority for shelled walnuts to be inspected after having been sliced, chopped, or ground

or in any manner changed from shelled walnuts, if regulations for such walnuts are in effect.

New walnut product forms are regularly requested by both domestic and foreign customers. In the last 20 years, the industry has become much more capable of producing at a considerably higher level of quality and of developing more specific types of products that meet the differing needs of individual customers. To capitalize on this growing capability, a number of witnesses expressed the view that an important tool for increasing sales is the ability to establish standards for these walnut products.

The order currently requires shelled product to be certified as merchantable, that is, meeting the minimum USDA requirements prior to further processing. When handlers are processing for end users that require further processing, this certification represents a costly extra step. After the initial shelled walnut certification, the handlers employ their own quality control procedures to meet the higher customer specifications. This proposal would allow a single inspection at the end of the process that would serve both purposes. If implemented, this proposal would allow the Board to recommend modifications to allow certification of product after it has been modified or chopped, leading to cost savings in the handling process.

Witnesses contended that current standards focus on visually observed characteristics that are significant for consumer acceptance, but often do not adequately address specific quality concerns important to various export markets, including Europe. Such concerns include, for example, moisture

content or aflatoxin tolerances. If implemented, this proposal would allow the Board to review scientific data and develop inspection procedures for recommendation and approval by USDA to assure customers that walnuts meet their specified criteria.

Any new quality standards recommended by the Board would be subject to thorough review prior to seeking approval from USDA. Witnesses supported this amendment as it would give the Board authority to pursue quality regulations in addition to existing grade standards, both of which are important to industry customers.

Witnesses emphasized that this proposal would grant authority to the Board to recommend quality standards that could exceed current standards or to develop new standards for product characteristics not currently covered. Witnesses also stated that no specific modifications are currently requested, just flexibility to create them in the future.

While this proposed amendment may result in some cost increases associated with administration and oversight of new quality regulations, it is also expected that some handlers may benefit from lower inspection costs if the inspection requirements for specific markets were modified. Any costs associated with the implementation of this proposal are expected to be outweighed by the overall benefits accrued to the industry.

#### Marketing Promotion and Paid Advertising

Proposal 13 would amend the order by adding authority for marketing promotion and paid advertising.

Current promotional activities for California walnuts are undertaken by

the California Walnut Commission (CWC). Witnesses stated that the CWCs activities have led to considerable success in increasing demand for the industry's product.

Witnesses explained that with price inelastic demand for walnuts, recent increases in production could have driven down prices and total grower revenue. The CWCs successful promotional activities has helped mitigate that potential impact, keeping average grower prices and grower revenue steady or increasing for several years.

According to the hearing record, adding authority for paid advertising and promotion under the order would benefit the industry by allowing the Board to engage in activities that are currently supported by the Commission. Small businesses would be the greatest beneficiaries of an expanded generic advertising program, because they have the least financial resources to devote to selling their products, according to a witness.

While an increase in advertising and promotional activities may result in Board expenditures, witnesses were confident that the positive results of the Board's promotional activities on consumer demand for California walnuts would more than outweigh any increases in costs to the industry.

#### **Impact of Remaining Amendment Proposals**

Remaining amendment proposals are largely administrative in nature and would impose no new significant regulatory burdens on California walnut growers or handlers. They should benefit the industry by improving the operation of the program and making it more responsive to industry needs.

#### *Marketing Year*

Proposal 1 would amend the order to change the marketing year from August 1 through July 31 to September 1 through August 31. Under the current definition of the order, the California walnut marketing year begins August 1 and continues through July 31. Witnesses explained that, over time, new varieties of walnuts have been introduced, and the areas in which walnuts are cultivated have shifted. The newer varieties mature later than the varieties grown at the time of the program's inception. At the same time, cultivation has slowly moved into areas that previously were not suited for walnut production. With differences in climate, soil, and water, witnesses explained that these new production areas have slightly later growing cycles. The proposed change in the marketing

year would better reflect current crop cycles.

Proposed conforming changes would ensure that Board member terms of office and marketing estimates calculated by the Board would conform to the modified marketing year. This amendment is not expected to result in any increases in costs to growers or handlers.

#### *Definition of Pack*

Proposal 2 would amend the order by specifying that the act of packing walnuts is considered a handling function. In addition, the term "pack" would be amended to include shelling, and would be modified so that packing is applicable to both inshell and shelled walnuts.

According to the hearing record, the order currently defines "to handle" as to "sell, consign, transport, or ship, or in any other way, to put walnuts into the current of commerce". The definition does not include the specific act of packing. "To pack", as currently defined in the order means, "to bleach, clean, grade or otherwise prepare inshell walnuts for market". Pack is not currently applicable to shelled walnuts. Witnesses stated that the proposed amendments to the definitions of "handle" and "pack" would more accurately reflect current industry operations.

This amendment is not expected to result in any increases in costs to growers. If implemented, this proposal may result in some packing entities previously not considered to be handlers under the order to be redefined as handlers. According to witnesses, there are roughly five packer entities that would qualify as handlers under the new definition. While some increases in administration costs on the part of handlers could arise as a result of reporting requirements, record evidence indicates that the benefit of more accurate industry information would merit that expense.

#### *Restructuring of the Board*

Proposal 3(a) seeks to amend all parts of the order that refer to cooperative seats on the Board, to redistribute member seats among districts, and to provide designated seats for a major handler, if such handler existed. A major handler would have to handle 35 percent or more of the crop.

According to the hearing record, the recent transition of the industry's largest cooperative from a cooperative entity to a publicly held company was the impetus for this proposal. Witnesses expressed the need to modify the Board structure to provide for representation

that accurately reflects the current industry. Witnesses advocated that the Board structure should maintain the current number of Board members and alternates, and that the allocation of member seats between grower and handler positions should remain the same (meaning 4 handler member seats, five grower member seats and one public member).

Witnesses also recommended modifying the allocation of Board representation according to two possible scenarios. The two scenarios include: (1) Membership allocation that acknowledges the existence of a handler handling 35 percent or more of production and, (2) membership allocation in the absence of such handler. According to record evidence, these proposed amendments would not result in any increases in costs.

#### *Nominations*

Proposal 3(b) would amend the Board member nomination process to reflect proposed changes in the Board structure, as outlined in 3(a). Current nomination procedures allow for all cooperative seat nominees to be selected by the cooperative and forwarded to the Secretary for approval and appointment. The cooperative nominee selection process is independent of the Board. All non-cooperative seat nominees are selected through a ballot nomination process overseen by the Board staff, and forwarded to the Secretary for approval and appointment.

According to the hearing record, the revised nomination procedures would allow a handler who handles 35 percent or more of the crop to nominate persons to fill its designated seats (as described in 3(a)) and to forward them to the Secretary for approval and appointment. Nomination of persons to fill all other seats would be conducted by the Board staff.

In the event a handler handling 35 percent or more of the crop does not exist, all Board nominees would be selected through a ballot nomination process conducted by the Board staff.

While some increases in administration costs could arise as a result of an increased number of ballots to be mailed by the Board if a major handler does not exist, record evidence indicates that the expense would be minor and would not directly burden growers or handlers.

#### *Qualify by Acceptance*

Proposal 4 would require Board nominees to submit a written qualification and acceptance statement prior to selection by USDA. Currently, the acceptance procedure for persons

nominated and selected to serve on the Board involves a two-step process. If this amendment were implemented, the two steps could be combined into one, thus resulting in less paperwork, a shorter acceptance procedure and improved efficiency in the acceptance process. This amendment is not expected to result in any increases in costs to growers or handlers.

#### *California Walnut Board*

Proposal 5 would change the name of the Walnut Marketing Board to the California Walnut Board. Witnesses stated that the proposed name of "California Walnut Board" would more accurately represent the Board's responsibilities. This amendment is not expected to result in any significant increases in costs to growers or handlers.

#### *Authority To Reestablish Districts and Board Structure*

Proposal 6 would add authority to reestablish districts, to reapportion members among districts, and to revise groups eligible for representation on the Board. The intent of this proposal is to provide the Board with a tool to more efficiently respond to the changing character of the California walnut industry. In recommending any such changes, the following would be considered: (1) Shifts in acreage within districts and within the production area during recent years; (2) the importance of new production in its relation to existing districts; (3) the equitable relationship between Board apportionment and districts; (4) changes in industry structure and/or the percentage of crop represented by various industry entities resulting in the existence of two or more handlers handling 35 percent or more of the crop; and (5) other relevant factors. This amendment is not expected to result in any increases in costs to growers or handlers.

#### *Voting Procedures*

Proposal 7 would amend Board quorum and voting requirements to add percentage requirements, add authority for the Board to vote by "any other means of communication" (including facsimile) and add authority for Board meetings to be held by telephone or by "any other means of communication".

Witnesses stated that references to the meeting quorum requirements should be amended to include a percentage equivalent of the current six-out-of-10-member minimum, or sixty percent. In addition, witnesses supported modifying the order language regarding voting requirements to state that a sixty-

percent super-majority vote of the members present at a meeting should be required of all Board decisions, except where otherwise specifically provided. The order currently states that a majority vote is needed, with no percentage equivalent specified.

According to the record, the order currently requires that all Board meetings be held at a physical location. Witnesses stated that the order should be amended to allow for some meetings to be held using "other means of communication", such as telephone or videoconferencing. Witnesses stated that use of new communication technology would result in timesavings while still allowing the Board to conduct its business. Witnesses stated that it is the intent of the Board that voting procedures for all types of non-traditional meetings can be recommended and adopted as appropriate for each type of technology used.

Amendments proposed under this material issue are not expected to result in any significant changes in costs to growers or handlers.

#### *Carryover of Excess Assessment Funds*

Proposal 8 would amend the order to add authority to carry over excess assessment funds. According to the hearing record, the order currently states that any assessment funds held in excess of the marketing year's expenses must be refunded to handlers. Refunds are returned to handlers in accordance with the amount of that handler's pro rata share of the actual expenses of the Board.

This proposed amendment would allow the Board, with the approval of the Secretary, to establish an operating monetary reserve. This would allow the Board to carry over to subsequent production years any excess funds in a reserve, provided that funds already in the reserve do not exceed approximately two years' expenses. If reserve funds do exceed that amount, the assessment rate could be reduced so as to cause reserves to diminish to a level below the two-year threshold.

According to the record, reserve funds could be used to defray expenses during any production year before assessment income is sufficient to cover such expenses, or to cover deficits incurred during any fiscal period when assessment income is less than expenses. Additionally, reserve funds could be used to defray expenses incurred during any period when any or all of the provisions of the order are suspended, or to meet any other such costs recommended by the Board and approved by the Secretary. This

proposal is not expected to result in any significant increases in costs to growers or handlers.

#### *Contributions*

Proposal 9 would amend the order by adding authority to accept contributions. If implemented, this proposed amendment would grant authority to the Board to accept voluntary contributions. Contributions could only be used to pay for research and development activities, and would be free from any encumbrances by the donor. According to the hearing record, the Board would retain oversight of the application of such contributions.

Witnesses supported this proposal by stating that it would provide the Board and the industry with valuable resources to enhance research and development activities. It is not expected that this proposal would result in any additional costs to growers or handlers.

#### *Reimbursement of Expenses*

Proposal 10 would amend the order to clarify that members and alternate members may be reimbursed for expenses incurred while performing their duties and that reimbursement includes per diem. According to the hearing record, this proposed amendment would not have any impact on the current expense reimbursement activities of the Board. Rather, it would clarify and update order language to more clearly state that while Board members and alternates serve without compensation, expenses incurred while performing the duties of a Board member that have been authorized by the Board will be incurred. It is not expected that this proposal would result in any additional costs to growers or handlers.

#### *Quality Regulations*

Proposal 12a would broaden the scope of the quality control provisions by adding authority to recommend different regulations for different market destinations. Witnesses emphasized the usefulness in terms of market development of being able to establish different regulations for individual markets and/or regions. Witnesses stated that allowing the Board to make such recommendations would help the walnut industry adapt to changing international market conditions.

#### *Updating Order Terminology*

Proposal 14 would amend the order by replacing the terms "carryover" with "inventory," and "mammoth" with "jumbo," to reflect current day industry procedures. This proposal would also

result in conforming changes being made to the "Marketing estimates and recommendations" and "Reports of handler carryover" sections of the order.

Handler carryover, defines the amount of California walnuts (both merchantable as well as the estimated quantity of merchantable walnuts to be produced from shelling stock and unsorted material), wherever located, held by California walnut handlers at any given time.

Witnesses explained that the current term "carryover" is misleading in that the term implies the amount of inventory held by handlers from one marketing year to the next. Witnesses stated that the term "inventory" would more accurately convey the intent of this definition, and would also reflect current day calculations of walnut availability.

Section 984.67, Exemptions, of the order provides for situations under which California walnuts may be exempted from complying with order regulations. One exemption is applicable to lots of merchantable inshell walnuts that are mammoth size or larger, as defined by the United States Standards for Walnuts in the Shell.

Witnesses stated that given the new varieties currently being produced in the industry, the term "mammoth" no longer applies. According to record evidence, the current production's equivalent to "mammoth" size is "jumbo" size, as defined by the United States Standards for Walnuts in the Shell. Thus, witnesses stated that the order language should be updated to reflect the industry's current terminology and size of walnuts being produced. This proposal is not expected to result in any increases in costs to growers or handlers.

#### *Interhandler Transfers*

Proposal 15(a) would amend the order to clarify the term "transfer" and to add authority for the Board to recommend methods and procedures, including necessary reports, for administrative oversight of such transfers.

Witnesses stated that it would be beneficial to simplify current order language so that all interhandler transfers were considered a "sale of inshell and shelled walnuts within the area of production by one handler to another." Witnesses explained that the proposed language restated the current application of this provision in walnut transactions in simpler terms. This proposal is not expected to result in any increases in costs to growers or handlers.

#### *Reporting Requirements*

Proposal 15(b) would amend the order to clarify that the Board may require reports from handlers and packers to include interhandler transfers or any other activity that involves placing California walnuts into the stream of commerce.

According to the hearing record, current authority provided in this section only applies to the reporting of handler walnut receipts from growers. Witnesses stated that this authority should be broadened to include interhandler transfers, or receipts from any other entity as recommended by the Board and approved by the Secretary. This proposal is not expected to result in any increases in costs to growers or handlers.

#### *Trade Demand*

Proposal 16 would update and simplify the language in § 984.22, Trade demand, to state "United States and its territories," rather than name "Puerto Rico" and "The Canal Zone". Witnesses explained that the reference to "Puerto Rico" and "The Canal Zone" in the order is outdated and should be updated to reference "United States and its territories".

According to record evidence, this amendment would not impact trade demand calculations under the order since the purpose of the reference is to accurately identify the amount of shelled or inshell walnuts demanded by the United States, including its territories. Thus, while the terminology identifying the geographic regions included in the calculation would change, the intent of the original language would remain unchanged. This proposal is not expected to result in any increases in costs to growers or handlers.

#### *Relationship With California Walnut Commission*

Proposal 17 would amend the order by adding language that would acknowledge that the Board may deliberate, consult, cooperate and exchange information with the California Walnut Commission (CWC). Any information sharing would be kept confidential.

Record evidence indicates the CWC and the Federal marketing order program are currently administered out of the same office location and employ the same staff. Thus, this proposal, if implemented, would formalize the relationship that currently exists between the two entities. Witnesses stated that collaboration between the two programs leads to reduced

administrative costs, as much of the information collected by each entity can be shared. This amendment is not expected to result in any increases in costs to growers or handlers.

In addition, USDA proposed adding two provisions that would help assure that the operation of the program conforms to current Department policy.

Proposal 18 would establish tenure requirements for Board members. Currently, the term of office of each member and alternate member of the Board is 2 years. There are no provisions related to term limits in the marketing order.

The record evidence suggests that term limits for Board members could increase industry participation on the Board, provide for more diverse membership, provide the Board with new perspectives and ideas, and increase the number of individuals in the industry with Board experience. This amendment is not expected to result in any increases in costs to growers or handlers.

Proposal 19 would require that continuance referenda be conducted on a periodic basis to ascertain industry support for the order and add more flexibility in the termination provisions.

Currently, there is no requirement in the order that continuance referenda be conducted on a periodic basis. The USDA believes that growers should have an opportunity to periodically vote on whether a marketing order should continue. Continuance referenda provide an industry with a means to measure grower support for the program. Experience has shown that programs need significant industry support to operate effectively. This amendment is not expected to result in any increases in costs to growers or handlers.

The proposals put forth at the hearing would streamline program organization, but are not expected to result in a significant change in industry production, handling or distribution activities. In discussing the impacts of the proposed amendments on growers and handlers, record evidence indicates that the changes are expected to be positive because the administration of the programs would be more efficient, and therefore more effective, in executing Board duties and responsibilities. There would be no significant cost impact on either small or large growers or handlers.

Interested persons were invited to present evidence at the hearing on the probable regulatory and informational impact of the proposed amendments to the order on small entities. The record evidence is that most of the

amendments are designed to increase efficiency in the functioning of the orders.

Current information collection requirements for Part 984 are approved by OMB under OMB number 0581-0178, Vegetable and Specialty Crops. Any changes in those requirements as a result of this proceeding would be submitted to OMB for approval. Witnesses stated that existing forms could be adequately modified to serve the needs of the Board. While conforming changes to the forms would need to be made (such as changing the name of the Board), the functionality of the forms would remain the same.

As with other similar marketing order programs, reports and forms are periodically reviewed to reduce information requirements and duplication by industry and public sector agencies.

USDA has not identified any relevant Federal rules that duplicate, overlap or conflict with this proposed rule. These amendments are designed to enhance the administration and functioning of marketing order 984 to the benefit of the California walnut industry.

Board meetings regarding these proposals as well as the hearing dates were widely publicized throughout the California walnut industry. All interested persons were invited to attend the meetings and the hearing and participate in deliberations on all issues. All Board meetings and the hearing were public forums and all entities, both large and small, were able to express views on these issues. Finally, interested persons are invited to submit information on the regulatory and informational impacts of this action on small businesses.

A 20-day comment period is provided to allow interested persons to respond to this proposal. Twenty days is deemed appropriate so that this rulemaking may be completed and nominations can be conducted prior to the beginning of the next crop year. All written exceptions timely received will be considered and a grower referendum will be conducted before these proposals are implemented.

AMS is committed to complying with the E-Government Elimination Act, to promote the use of the Internet and other information technologies to provide increased opportunities for citizen access to Government information and services, and for other purposes.

Further, the public hearing held on May 17 and 18, 2006, in Modesto, California, was widely publicized throughout the California walnut industry and all interested persons were invited to attend and all entities, both

large and small, were able to express their views on this issue.

Finally, interested persons are invited to submit information on the regulatory and informational impacts of this action on small businesses.

A small business guide on complying with fruit, vegetable, and specialty crop marketing agreements and orders may be viewed at: <http://www.ams.usda.gov/fv/moab.html>. Any questions about the compliance guide should be sent to Jay Guerber at the previously mentioned address in the **FOR FURTHER INFORMATION CONTACT** section.

#### Civil Justice Reform

The amendments to Marketing Order No. 984 proposed herein have been reviewed under Executive Order 12988, Civil Justice Reform. They are not intended to have retroactive effect. If adopted, the proposed amendments would not preempt any State or local laws, regulations, or policies, unless they present an irreconcilable conflict with this proposal.

The Act provides that administrative proceedings must be exhausted before parties may file suit in court. Under section 608c(15)(A) of the Act, any handler subject to an order may file with USDA a petition stating that the order, any provision of the order, or any obligation imposed in connection with the order is not in accordance with law and request a modification of the order or to be exempted therefrom. A handler is afforded the opportunity for a hearing on the petition. After the hearing, USDA would rule on the petition. The Act provides that the district court of the United States in any district in which the handler is an inhabitant, or has his or her principal place of business, has jurisdiction to review USDA's ruling on the petition, provided an action is filed not later than 20 days after the date of the entry of the ruling.

#### Rulings on Briefs of Interested Persons

Briefs, proposed findings and conclusions, and the evidence in the record were considered in making the findings and conclusions set forth in this recommended decision. To the extent that the suggested findings and conclusions filed by interested persons are inconsistent with the findings and conclusions of this recommended decision, the requests to make such findings or to reach such conclusions are denied.

#### General Findings

The findings hereinafter set forth are supplementary to the findings and determinations which were previously made in connection with the issuance of

the marketing agreement and order; and all said previous findings and determinations are hereby ratified and affirmed, except insofar as such findings and determinations may be in conflict with the findings and determinations set forth herein.

(1) The marketing agreement and order, as amended, and as hereby proposed to be further amended, and all of the terms and conditions thereof, would tend to effectuate the declared policy of the Act;

(2) The marketing agreement and order, as amended, and as hereby proposed to be further amended, regulate the handling of walnuts grown in the production area (the State of California) in the same manner as, and are applicable only to, persons in the respective classes of commercial and industrial activity specified in the marketing agreements and orders upon which a hearing has been held;

(3) The marketing agreement and order, as amended, and as hereby proposed to be further amended, are limited in their application to the smallest regional production areas which is practicable, consistent with carrying out the declared policy of the Act, and the issuance of several orders applicable to subdivisions of the production areas would not effectively carry out the declared policy of the Act;

(4) The marketing agreement and order, as amended, and as hereby proposed to be further amended, prescribe, insofar as practicable, such different terms applicable to different parts of the production area as are necessary to give due recognition to the differences in the production and marketing of walnuts grown in the production area; and

(5) All handling of walnuts grown in the production areas as defined in the marketing agreement and order, is in the current of interstate or foreign commerce or directly burdens, obstructs, or affects such commerce.

#### List of Subjects in 7 CFR Part 984

Marketing agreements, Nuts, Reporting and recordkeeping requirements, and Walnuts.

#### PART 984—WALNUTS GROWN IN CALIFORNIA

1. The authority citation for 7 CFR part 984 continues to read as follows:

**Authority:** 7 U.S.C. 601-674.

2. Revise § 984.6 to read as follows:

##### § 984.6 Board.

Board means the California Walnut Board established pursuant to § 934.35.

3. Revise § 984.7 to read as follows:

**§ 984.7 Marketing year.**

Marketing year means the twelve months from September 1 to the following August 31, both inclusive, or any other such period deemed appropriate and recommended by the Board for approval by the Secretary.

4. Revise § 984.13 to read as follows:

**§ 984.13 To handle.**

To handle means to pack, sell, consign, transport, or ship (except as a common or contract carrier of walnuts owned by another person), or in any other way to put walnuts, inshell or shelled, into the current of commerce either within the area of production or from such area to any point outside thereof, or for a manufacturer or retailer within the area of production to purchase directly from a grower: The term "to handle" shall not include sales and deliveries within the area of production by growers to handlers, or between handlers.

5. Revise § 984.14 to read as follows:

**§ 984.14 Handler.**

Handler means any person who handles inshell or shelled walnuts.

6. Revise § 984.15 to read as follows:

**§ 984.15 Pack.**

Pack means to bleach, clean, grade, shell or otherwise prepare walnuts for market as inshell or shelled walnuts.

7. Revise § 984.21 to read as follows:

**§ 984.21 Handler inventory.**

Handler inventory as of any date means all walnuts, inshell or shelled (except those held in satisfaction of a reserve obligation), wherever located, then held by a handler or for his or her account.

8. Revise § 984.22 to read as follows:

**§ 984.22 Trade demand.**

(a) *Inshell.* The quantity of merchantable inshell walnuts that the trade will acquire from all handlers during a marketing year for distribution in the United States and its territories.

(b) *Shelled.* The quantity of merchantable shelled walnuts that the trade will acquire from all handlers during a marketing year for distribution in the United States and its territories.

9. Revise § 984.35 to read as follows:

**§ 984.35 California Walnut Board.**

(a) A California Walnut Board is hereby established consisting of 10 members selected by the Secretary, each of whom shall have an alternate nominated and selected in the same way and with the same qualifications as the member. The members and their alternates shall be selected by the Secretary from nominees submitted by

each of the following groups or from other eligible persons belonging to such groups:

- (1) Two handler members from District 1;
- (2) Two handler members from District 2;
- (3) Two grower members from District 1;
- (4) Two grower members from District 2;
- (5) One grower member nominated at-large from the production area; and,
- (6) One member and alternate who shall be selected after the selection of the nine handler and grower members and after the opportunity for such members to nominate the tenth member and alternate. The tenth member and his or her alternate shall be neither a walnut grower nor a handler.

(b) In the event that one handler handles 35% or more of the crop the membership of the Board shall be as follows:

(1) Two handler members to represent the handler that handles 35% or more of the crop;

(2) Two members to represent growers who market their walnuts through the handler that handles 35% or more of the crop;

(3) Two handler members to represent handlers that do not handle 35% or more of the crop;

(4) One member to represent growers from District 1 who market their walnuts through handlers that do not handle 35% or more of the crop;

(5) One member to represent growers from District 2 who market their walnuts through handlers that do not handle 35% or more of the crop;

(6) One member to represent growers who market their walnuts through handlers that do not handle 35% or more of the crop shall be nominated at large from the production area; and,

(7) One member and alternate who shall be selected after the selection of the nine handler and grower members and after the opportunity for such members to nominate the tenth member and alternate. The tenth member and his or her alternate shall be neither a walnut grower nor a handler.

(c) Grower Districts:

(1) *District 1.* District 1 encompasses the counties in the State of California that lie north of a line drawn on the south boundaries of San Mateo, Alameda, San Joaquin, Calaveras, and Alpine Counties.

(2) *District 2.* District 2 shall consist of all other walnut producing counties in the State of California south of the boundary line set forth in paragraph (c)(1) of this section.

(d) The Secretary, upon recommendation of the Board, may

reestablish districts, may reapportion members among districts, and may revise the groups eligible for representation on the Board as specified in paragraphs (a) and (b) of this section: Provided, That any such recommendation shall require at least six concurring votes of the voting members of the Board. In recommending any such changes, the following shall be considered:

(1) Shifts in acreage within districts and within the production area during recent years;

(2) The importance of new production in its relation to existing districts;

(3) The equitable relationship between Board apportionment and districts;

(4) Changes in industry structure and/or the percentage of crop represented by various industry entities resulting in the existence of two or more major handlers;

(5) Other relevant factors.

10. Revise § 984.36 to read as follows:

**§ 984.36 Term of office.**

The term of office of Board members, and their alternates shall be for a period of two years ending on August 31 of odd-numbered years, but they shall serve until their respective successors are selected and have qualified. Board members may serve up to three consecutive, two-year terms of office. In no event shall any member serve more than six consecutive years on the Board. For purposes of determining when a Board member has served three consecutive terms, the accrual of terms shall begin following any period of at least twelve consecutive months out of office. The limitation on tenure shall not apply to alternates.

11. Revise § 984.37 to read as follows:

**§ 984.37 Nominations.**

(a) Nominations for all grower members shall be submitted by ballot pursuant to an announcement by press releases of the Board to the news media in the walnut producing areas. Such releases shall provide pertinent voting information, including the names of candidates and the location where ballots may be obtained. Ballots shall be accompanied by full instructions as to their markings and mailing and shall include the names of incumbents who are willing to continue serving on the Board and such other candidates as may be proposed pursuant to methods established by the Board with the approval of the Secretary. Each grower, regardless of the number and location of his or her walnut orchard(s), shall be entitled to cast only one ballot in the nomination and each vote shall be given

equal weight. If the grower has orchards in both grower districts, he or she shall advise the Board of the district in which he/she desires to vote. The person receiving the highest number of votes for each grower position shall be the nominee.

(b) Nominations for handler members shall be submitted on ballots mailed by the Board to all handlers in their respective Districts. All handlers' votes shall be weighted by the kernelweight of walnuts certified as merchantable by each handler during the preceding marketing year. Each handler in the production area may vote for handler member nominees and their alternates. However, no handler with less than 35% of the crop shall have more than one member and one alternate member. The person receiving the highest number of votes for each handler member position shall be the nominee for that position.

(c) A calculation to determine whether or not a handler who handles 35 percent or more of the crop shall be made prior to nominations. For the first nominations held upon implementation of this language, the 35 percent threshold shall be calculated using an average of crop handled for the year in which nominations are made and one year's handling prior. For all future nominations, the 35 percent handling calculation shall be based in the average of the two years prior to the year in which nominations are made. In the event that one handler handles 35% or more of the crop the membership of the Board, nominations shall be as follows:

(1) Nominations of growers who market their walnuts to the handler that handles 35% or more of the crop shall be conducted by that handler and the names of the nominees shall be forwarded to the Board for approval and appointment by the Secretary.

(2) Nominations for the two handler members representing the major handler shall be conducted by the major handler and the names of the nominees shall be forwarded to the Board for approval and appointment by the Secretary.

(3) Nominations on behalf of all other grower members (Groups (b) (4), (5) and (6) of § 984.35) shall be submitted after ballot by such growers pursuant to an announcement by press releases of the Board to the news media in the walnut producing areas. Such releases shall provide pertinent voting information, including the names of candidates and the location where ballots may be obtained. Ballots shall be accompanied by full instructions as to their markings and mailing and shall include the names of incumbents who are willing to continue serving on the Board and such

other candidates as may be proposed pursuant to methods established by the Board with the approval of the Secretary. Each grower in Groups (Groups (b) (4), (5) and (6) of § 984.35), regardless of the number and location of his or her walnut orchard(s), shall be entitled to cast only one ballot in the nomination and each vote shall be given equal weight. If the grower has orchard(s) in both grower districts he or she shall advise the Board of the district in which he or she desires to vote. The person receiving the highest number of votes for grower position shall be the nominee.

(4) Nominations for handler members representing handlers that do not handle 35% or more of the crop shall be submitted on ballots mailed by the Board to those handlers. The votes of these handlers shall be weighted by the kernelweight of walnuts certified as merchantable by each handler during the preceding marketing year. Each handler in the production area may vote for handler member nominees and their alternates of this subsection. However, no handler shall have more than one person on the Board either as member or alternate member. The person receiving the highest number of votes for a handler member position of this subsection shall be the nominee for that position.

(d) Each grower is entitled to participate in only one nomination process, regardless of the number of handler entities to whom he or she delivers walnuts. If a grower delivers walnuts to more than one handler entity, the grower must choose which nomination process he or she participates in.

(e) The nine members shall nominate one person as member and one person as alternate for the tenth member position. The tenth member and alternate shall be nominated by not less than 6 votes cast by the nine members of the Board.

(f) Nominations in the foregoing manner received by the Board shall be reported to the Secretary on or before June 15 of each odd-numbered year, together with a certified summary of the results of the nominations. If the Board fails to report nominations to the Secretary in the manner herein specified by June 15 of each odd-numbered year, the Secretary may select the members without nomination. If nominations for the tenth member are not submitted by September 1 of any such year, the Secretary may select such member without nomination.

(g) The Board may recommend, subject to the approval of the Secretary, a change to these nomination

procedures should the Board determine that a revision is necessary.

12. Revise § 984.38 to read as follows:

**§ 984.38 Eligibility.**

No person shall be selected or continue to serve as a member or alternate to represent one of the groups specified in § 984.35(a)(1) through (6) or § 984.38(b)(1) through (6), unless he or she is engaged in the business he or she is to represent, or represents, either in his or her own behalf or as an officer or employee if the business unit engaged in such business. Also, each member or alternate member representing growers in District 1 or District 2 shall be a grower, or officer or employee of the group he or she is to represent.

13. Revise § 984.39 to read as follows:

**§ 984.39 Qualify by acceptance.**

Any person nominated to serve as a member or alternate member of the Board shall, prior to selection by USDA, qualify by filing a written qualification and acceptance statement indicating such person's willingness to serve in the position for which nominated.

**§ 984.40 [Amended]**

14. Amend § 984.40 by removing the word "his" and adding the phrase "his or her" in its place in 2 places in paragraph (a) and 3 places in paragraph (b), and by removing the last sentence in paragraph (b).

15. Revise § 984.42 to read as follows:

**§ 984.42 Expenses.**

The members and their alternates of the Board shall serve without compensation, but shall be allowed their necessary expenses incurred by them in the performance of their duties under this part.

16. Amend § 984.45 by revising paragraphs (b) and (c) and adding paragraph (d) to read as follows:

**§ 984.45 Procedure.**

(a) \* \* \*

(b) All decisions of the Board, except where otherwise specifically provided (see § 984.35(d)), shall be by a sixty-percent (60%) super-majority vote of the members present. A quorum of six members, or the equivalent of sixty percent (60%) of the Board, shall be required for the conduct of Board business.

(c) The Board may vote by mail or telegram, or by any other means of communication, upon due notice to all members. The Board, with the approval of the Secretary, shall prescribe the minimum number of votes that must be cast when voting is by any of these methods, and any other procedures

necessary to carry out the objectives of this paragraph.

(d) The Board may provide for meetings by telephone, or other means of communication and any vote cast at such a meeting shall be confirmed promptly in writing: Provided, That if any assembled meeting is held, all votes shall be cast in person.

17. Revise § 984.46 to read as follows:

**§ 984.46 Research and development.**

The Board, with the approval of the Secretary, may establish or provide for the establishment of production research, marketing research and development projects, and marketing promotion, including paid advertising, designed to assist, improve, or promote the marketing, distribution, and consumption or efficient production of walnuts. The expenses of such projects shall be paid from funds collected pursuant to § 984.69 and § 984.70.

18. Amend § 984.48 by revising paragraphs (a) introductory text, (a)(2), (4), and (5) to read as follows:

**§ 984.48 Marketing estimates and recommendations.**

(a) Each marketing year the Board shall hold a meeting, prior to October 20, for the purpose of recommending to the Secretary a marketing policy for such year. Each year such recommendation shall be adopted by the affirmative vote of at least 60% of the Board and shall include the following, and where applicable, on a kernelweight basis:

(1) \* \* \*

(2) Its estimate of the handler inventory on September 1 of inshell and shelled walnuts;

(3) \* \* \*

(4) Its estimate of the trade demand for such marketing year for shelled and inshell walnuts, taking into consideration trade inventory, imports, prices, competing nut supplies, and other factors;

(5) Its recommendation for desirable handler inventory of inshell and shelled walnuts on August 31 of each marketing year;

\* \* \* \* \*

19. Amend § 984.50 by revising the heading and paragraph (d) to read as follows:

**§ 984.50 Grade, quality and size regulations.**

\* \* \* \* \*

(d) *Additional grade, size or other quality regulation.* The Board may recommend to the Secretary additional grade, size or other quality regulations, and may also recommend different regulations for different market

destinations. If the Secretary finds on the basis of such recommendation or other information that such additional regulations would tend to effectuate the declared policy of the Act, he or she shall establish such regulations.

\* \* \* \* \*

20. Amend § 984.51 by revising paragraph (a) to read as follows:

**§ 984.51 Inspection and certification of inshell and shelled walnuts.**

(a) Before or upon handling of any walnuts for use as free or reserve walnuts, each handler at his or her own expense shall cause such walnuts to be inspected to determine whether they meet the then applicable grade and size regulations. Such inspection shall be performed by the inspection service or services designated by the Board with the approval of the Secretary; Provided, That if more than one inspection service is designated, the functions performed by each service shall be separate, and shall not duplicate each other. Handlers shall obtain a certificate for each inspection and cause a copy of each certificate issued by the inspection service to be furnished to the Board. Each certificate shall show the identity of the handler, quantity of walnuts, the date of inspection, and for inshell walnuts the grade and size of such walnuts as set forth in the United States Standards for Walnuts (*Juglans regia*) in the Shell. Certificates covering reserve shelled walnuts for export shall also show the grade, size, and color of such walnuts as set forth in the United States Standards for Shelled Walnuts (*Juglans regia*). The Board, with the approval of the Secretary, may prescribe procedures for the administration of this provision.

\* \* \* \* \*

21. Amend § 984.52 by revising paragraph (a) and adding a new paragraph (c) to read as follows:

**§ 984.52 Processing of shelled walnuts.**

(a) No handler shall slice, chop, grind, or in any manner change the form of shelled walnuts unless such walnuts have been certified as merchantable or unless such walnuts meet quality regulations established under § 984.50(d) if such regulations are in effect.

\* \* \* \* \*

(c) The Board shall establish such procedures as are necessary to insure that all such walnuts are inspected prior to being placed into the current of commerce.

22. Revise § 984.59 to read as follows:

**§ 984.59 Interhandler transfers.**

For the purposes of this part, transfer means the sale of inshell and shelled

walnuts within the area of production by one handler to another. The Board, with the approval of the Secretary, may establish methods and procedures, including necessary reports, for such transfers.

**§ 984.67 [Amended]**

23. Amend § 984.67 by removing the word "mammoth" and adding the word "jumbo" in its place in paragraph (a).

24. Amend § 984.69 by revising paragraph (c) to read as follows:

**§ 984.69 Assessments.**

\* \* \* \* \*

(c) *Accounting.* If at the end of a marketing year the assessments collected are in excess of expenses incurred, such excess shall be accounted for in accordance with one of the following:

(1) If such excess is not retained in a reserve, as provided in paragraph (c)(2) or (c)(3) of this section, it shall be refunded to handlers from whom collected and each handler's share of such excess funds shall be the amount of assessments he or she has paid in excess of his or her pro rata share of the actual expenses of the Board.

(2) Excess funds may be used temporarily by the Board to defray expenses of the subsequent marketing year: Provided, That each handler's share of such excess shall be made available to him or her by the Board within five months after the end of the year.

(3) The Board may carry over such excess into subsequent marketing years as a reserve: Provided, That funds already in reserve do not exceed approximately two years' budgeted expenses. In the event that funds exceed two marketing years' budgeted expenses, future assessments will be reduced to bring the reserves to an amount that is less than or equal to two marketing years' budgeted expenses. Such reserve funds may be used:

(i) To defray expenses, during any marketing year, prior to the time assessment income is sufficient to cover such expenses;

(ii) To cover deficits incurred during any year when assessment income is less than expenses;

(iii) To defray expenses incurred during any period when any or all provisions of this part are suspended;

(iv) To meet any other such costs recommended by the Board and approved by the Secretary.

\* \* \* \* \*

25. Add a new § 984.70 to read as follows:

**§ 984.70 Contributions.**

The Board may accept voluntary contributions but these shall only be used to pay expenses incurred pursuant to § 984.46, Research and development. Furthermore, such contributions shall be free from any encumbrances by the donor and the Board shall retain complete control of their use.

26. Revise § 984.71 to read as follows:

**§ 984.71 Reports of handler inventory.**

Each handler shall submit to the Board in such form and on such dates as the Board may prescribe, reports showing his or her inventory of inshell and shelled walnuts.

27. Revise § 984.73 to read as follows:

**§ 984.73 Reports of walnut receipts.**

Each handler shall file such reports of his or her walnut receipts from growers, handlers, or others in such form and at such times as may be requested by the Board with the approval of the Secretary.

28. Amend § 984.89 by redesignating paragraph (b)(4) as (b)(5) and adding a new paragraph (b)(4) to read as follows:

**§ 984.89 Effective time and termination.**

\* \* \* \* \*

(b) \* \* \*

(4) Within six years of the effective date of this amendment the Secretary shall conduct a referendum to ascertain whether continuance of this part is favored by producers. Subsequent referenda to ascertain continuance shall be conducted every six years thereafter. The Secretary may terminate the provisions of this part at the end of any fiscal period in which the Secretary has found that continuance of this part is not favored by a two-thirds ( $\frac{2}{3}$ ) majority of voting producers, or a two-thirds ( $\frac{2}{3}$ ) majority of volume represented thereby, who, during a representative period determined by the Secretary, have been engaged in the production for market of walnuts in the production area. Such

termination shall be announced on or before the end of the production year.

\* \* \* \* \*

29. Add a new § 984.91 to read as follows:

**§ 984.91 Relationship with the California Walnut Commission.**

In conducting Board activities and other objectives under this part, the Board may deliberate, consult, cooperate and exchange information with the California Walnut Commission, whose activities compliment those of the Board. Any sharing of information gathered under this subpart shall be kept confidential in accordance with provisions under section 10(i) of the Act.

Dated: March 19, 2007.

**Lloyd C. Day,**

*Administrator, Agricultural Marketing Service.*

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