

# **Hearing Panel Report**

*Based on a Public Hearing Held  
July 1, 2008*

Addressing Technical Changes to the  
Pooling Plan for Market Milk

and

Addressing the Milk Movement Issues  
Contained in the  
Pooling Plan for Market Milk and the  
Stabilization and Marketing Plans  
for Market Milk for the  
Northern and Southern California Marketing Areas

— HEARING PANEL REPORT —

JULY 1, 2008 PUBLIC HEARING

ADDRESSING TECHNICAL CHANGES TO THE  
MILK POOLING PLAN FOR MARKET MILK

and

ADDRESSING MILK MOVEMENT ISSUES CONTAINED IN THE  
MILK POOLING PLAN FOR MARKET MILK AND THE  
STABILIZATION AND MARKETING PLANS FOR MARKET MILK  
FOR NORTHERN AND SOUTHERN CALIFORNIA

This report of the Hearing Panel (Panel) regarding proposed amendments to the Milk Pooling Plan for Market Milk (Pool Plan) and to the Stabilization and Marketing Plans for Market Milk for Northern California and Southern California (Stab Plans) is based on the July 1, 2008, hearing record. The record includes the exhibits prepared by the California Department of Food and Agriculture (Department), written statements and comments received from interested parties, written and oral testimony received, and written post hearing briefs.

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## INTRODUCTION, SUMMARY OF PROPOSALS AND LIST OF WITNESSES

California Food and Agricultural Code Section 61801, *et sec.*, provides the authority, procedures and standards for establishing minimum farm prices by the Department for the various classes of milk that processors (handlers) must pay for milk purchased from dairy farmers (producers). These statutes provide for the formulation and adoption of Stab Plans.

The Gonsalves Milk Pooling Act, California Food and Agricultural Code Section 62700, *et sec.*, authorizes the Secretary to operate a statewide pooling system under specified guidelines. These statutes provide for the formulation and adoption of Pool Plans.

On April 25, 2008, the Department called a hearing on its own motion to consider three proposed technical amendments to the Pooling Plan. The technical amendments were being offered by the Department for consideration.

Subsequently, a hearing petition was submitted by:

- California Dairies, Inc. (CDI)

On May 9, 2008, the Department issued a revised hearing notice that broadened the call of the hearing to include consideration of amendments to the transportation allowance and credit system.

Three alternative proposals were submitted:

- Humboldt Creamery Association (Humboldt)
- Dairy Institute of California (Institute)
- Dairy Farmers of America (DFA)

### Hearing Witnesses:

A total of 13 witnesses testified including the Department's witnesses:

Tom Gossard - Department

Donald Shippelhoute - Department

Gary Korsmeier – CDI

\*Rich Ghilarducci – Humboldt

\*Len Mayer – Humboldt

\*William Schiek – Institute

\*Gary Stueve – DFA

Robert VandenHeuvel – Milk Producers Council (MPC)

Dennis Brimhall – Super Store Industries (Super Store)

William Van Dam – Alliance of Western Milk Producers (Alliance)

Mkulima G. Britt - Clover Stornetta Farms, Inc. (Clover)

Michael Marsh – Western United Dairymen (WUD)

Kevin Abernathy – California Dairy Campaign (CDC)

An “\*” indicates witness/organization who submitted a post hearing brief.

Written statements were received and entered into the hearing record from Land O'Lakes (LOL) and Security Milk Producers (Security).

## **BACKGROUND**

### **Program**

Minimum producer price regulation established in the mid-1930s brought some stability to the marketing of milk, but did not guarantee all producers the same price. The price producers received depended on the utilization of the processing plant they shipped (sold) their milk to (under a contract system that depended upon plant pooling). Thus, producers shipping to a plant with high Class 1 usage received more revenue than producers shipping to a plant with high Class 4 usage. There was competition among producers for Class 1 contracts (the legal rights to market a producer's milk production to a processor that had significant Class 1 usage). In addition, there was an imbalance of market power between the relatively small number of processors and the large number of producers. Dairy farmers were relatively small in size and generally operated very independently/autonomously. These factors created market instability and price inequity among producers.

Passage of the Gonsalves Milk Pooling Act in 1967, with its implementation in 1969, corrected many of these problems. In doing so, however, it removed the economic incentive that existed under the old contract system for producers to ship their milk to a Class 1 plant. Instead, the typical producer had an incentive to ship to a local plant, which for most producers is a manufacturing plant.

Under the California milk pooling program, most California dairy farm revenues generated from milk sales by dairy farmers to California processors are combined into a central Pool. The Pool redistributes the total Pool revenues to dairy farmers in the form of two blend prices. While the Pool Plan specifies that dairy farmers are paid based upon their allocated quota, base, and overbase prices, which reflect the pool-wide usage of all class prices, the base and overbase prices have been the same value since 1994. The monthly quota and base amounts are computed for each producer to the extent these amounts are produced. The current quota allocation determines the maximum monthly quota amount, and the balance in the Pool is paid out in the form of base and overbase prices.

Revenue from processors is distributed to dairy farmers via two prices: the quota price; and the base/overbase price. From the inception of statewide milk pooling in 1969 until 1993, Class 1, 2 and 3 farm prices were the primary determinants of the quota price, and Class 4a and 4b farm prices the primary determinants of the overbase price. This was changed by statute, and beginning in January 1994 a fixed differential was established so that the quota price is always \$1.70 per hundredweight (cwt.) greater than the base/overbase price. Historically from 1969 through 1993, the difference between the announced quota and overbase prices ranged from \$1.06 to \$2.26 per cwt. on an annual average basis. Currently, revenue above that range needed to maintain the \$1.70 differential is shared equally among quota, base and overbase production. The announced quota price is adjusted based on farm location by regional quota adjusters (RQAs). Prices paid to an individual producer depend upon their farm location and their blend of quota, base and overbase holdings.

### **Administrative Operational Background**

When the Milk Pooling Program was first made effective in 1969, a sophisticated computer system was critical in performing the significant number of calculations necessary to account for the then four minimum class prices and the monthly sales of each classified price in order to determine the three monthly Pool prices for each of the state's over 2,000+ producers. In 1969, the Milk Pooling Branch contracted with the State of California

Franchise Tax Board (FTB), one of the few organizations that had a computer system capable of performing the essential computations necessary to run the monthly Pool. This same FTB hardware and software system is still performing the monthly Pool calculations today, almost 40 years later. This system has not undergone a significant update since its inception. The monthly Pool calculations are increasingly dependent upon a growingly outdated system. Moreover, FTB has provided notice to the Department that it will be unable to provide the professional expertise needed to make adjustments to the system in the long term. As newer technologies and software systems become more commonplace, finding people with knowledge of the current system will become more problematic.

Since the Pooling Program became effective, the computer program has accounted for the solids-not-fat (SNF) test differently for handlers who purchased their milk directly from producers versus handlers who obtained their milk from cooperatives or other handlers. For handlers who do not purchase milk directly from farmers, the SNF is accounted for by using a statewide average SNF factor (.08934715) to skim. For proprietary handlers who purchase directly from producers, the SNF accounting in the Pool is determined by the actual SNF test of the producer's milk acquired during the month. These accommodations were in part necessary because of the limited capability within the existing computer technology at the time. In addition, there were numerous relatively small cooperative organizations that had limited ability to obtain and administer the reporting of the actual SNF fat tests for their cooperative membership within the available time constraints.

The pending implementation of a new pooling software system and the improvements in accounting systems, however, eliminate both these prior limitations. Implementation of the upgraded Dairy Accounting System (DAS) will enable the Department to account for SNF by handlers in a more precise manner, using actual SNF pounds as determined by tests on milk. The improvements in computer technology and the relatively large size of a handful of very capable California cooperative operations would suggest that using the actual SNF test is now attainable.

The Department's work to replace the current system is nearing completion. The newly created and more sophisticated system no longer will depend upon batch processing. It provides significant enhancement and more flexibility over the current system. It will facilitate the Department's ability to organize and compile aggregate details that are currently not readily available. The new DAS has been tested while the current FTB system is operating. Based on the positive test results, implementation of the new DAS can occur within the next few months.

## SUMMARY OF PROPOSALS

**Transportation Allowances.** The proposed changes to transportation allowance rates and mileage brackets are summarized in Table 1.

**Table 1: PROPOSED CHANGES TO  
TRANSPORTATION ALLOWANCES: *Ranch-to-Plant***

|  | CONSTRUCTIVE<br>MILES | Current<br>since<br>September<br>2006 | CDI<br>Proposal            | Dairy<br>Institute<br>Proposal | Humboldt<br>Proposal | DFA<br>Proposal | Clover<br>Testimony |
|--|-----------------------|---------------------------------------|----------------------------|--------------------------------|----------------------|-----------------|---------------------|
|  | <i>In Miles</i>       | <i>In Dollars Per Hundredweight</i>   |                            |                                |                      |                 |                     |
| <b>Bay Area Receiving Area</b> <sup>1/</sup>   | 0 to 99               | \$0.27                                | <b>\$0.36<sup>5/</sup></b> | <b>\$0.37</b>                  | \$0.27               | <b>\$0.37</b>   |                     |
|  | 99 to 199             | \$0.34                                | <b>\$0.43</b>              | <b>\$0.45</b>                  | \$0.34               | <b>\$0.45</b>   |                     |
|  | 199 +                 | \$0.36                                | <b>\$0.45</b>              | <b>\$0.47</b>                  | \$0.36               | <b>\$0.47</b>   |                     |
| <b>North Bay Receiving Area</b> <sup>2/</sup>  | 0 to 44               | \$0.19                                | \$0.19                     | \$0.19                         | \$0.19               | \$0.19          | <b>\$0.29</b>       |
|  | 44 to 99              | \$0.29                                | \$0.29                     | <b>\$0.35</b>                  | \$0.29               | <b>\$0.35</b>   |                     |
|  | 99 +                  | \$0.34                                | \$0.34                     | <b>\$0.44</b>                  | \$0.34               | <b>\$0.44</b>   |                     |
| <b>Sacramento Receiving Area</b>   | 0 to 59               | \$0.15                                | \$0.15                     | \$0.15                         | \$0.15               | \$0.15          |                     |
|  | 59 +                  | \$0.20                                | \$0.20                     | <b>\$0.25</b>                  | \$0.20               | <b>\$0.25</b>   |                     |
| <b>Shasta Receiving Area</b> <sup>3/</sup>   | 0 to 29               | \$0.13                                | \$0.13                     | \$0.13                         | \$0.13               | \$0.13          |                     |
|  | 29 to 49              | \$0.16                                | \$0.16                     | \$0.16                         | \$0.16               | \$0.16          |                     |
|  | 49 +                  | \$0.19                                | \$0.19                     | \$0.19                         | \$0.19               | \$0.19          |                     |
| <b>San Diego Receiving Area</b>  | 0 to 89               | \$0.11                                |                            |                                | \$0.11               | \$0.11          |                     |
|  | 89 to 139             | \$0.43                                |                            |                                | \$0.43               | \$0.43          |                     |
|  | 139 +                 | \$0.70                                |                            |                                | \$0.70               | \$0.70          |                     |
|  | <b>0 to 79</b>        |                                       | <b>\$0.15</b>              | <b>\$0.15</b>                  |                      |                 |                     |
|  | <b>79 to 119</b>      |                                       | <b>\$0.46</b>              | <b>\$0.46</b>                  |                      |                 |                     |
|  | <b>119 +</b>          |                                       | <b>\$0.84</b>              | <b>\$0.84</b>                  |                      |                 |                     |
| <b>Southern California Receiving Area</b> <sup>4/</sup><br>from San Bernardino<br>and Riverside counties | 0 to 89               | \$0.11                                |                            |                                | \$0.11               |                 |                     |
|  | 89 +                  | \$0.37                                |                            |                                | \$0.37               |                 |                     |
|  | <b>0 to 79</b>        |                                       | <b>\$0.15</b>              | <b>\$0.15</b>                  |                      | <b>\$0.15</b>   |                     |
|  | <b>79 +</b>           |                                       | <b>\$0.46</b>              | <b>\$0.46</b>                  |                      | <b>\$0.46</b>   |                     |
| <b>From Humboldt and<br/>Del Norte counties</b>  | All distances         | \$0.70                                | <b>\$0.84</b>              | <b>\$0.84</b>                  | <b>\$3.50</b>        | <b>\$0.84</b>   |                     |
| from all other counties  | 0 to 89               | \$0.11                                |                            |                                | \$0.11               |                 |                     |
|  | 89 to 109             | \$0.37                                |                            |                                | \$0.37               |                 |                     |
|  | 109 to 139            | \$0.56                                |                            |                                | \$0.56               |                 |                     |
|  | 139 +                 | \$0.70                                |                            |                                | \$0.70               |                 |                     |
|  | <b>0 to 79</b>        |                                       | <b>\$0.15</b>              | <b>\$0.15</b>                  |                      |                 |                     |
|  | <b>79 to 99</b>       |                                       | <b>\$0.46</b>              | <b>\$0.46</b>                  |                      |                 |                     |
|  | <b>99 to 119</b>      |                                       | <b>\$0.67</b>              | <b>\$0.67</b>                  |                      |                 |                     |
|  | <b>119 +</b>          |                                       | <b>\$0.84</b>              | <b>\$0.84</b>                  |                      |                 |                     |
|  | <b>0 to 87</b>        |                                       |                            |                                |                      | <b>\$0.15</b>   |                     |
|  | <b>87 to 108</b>      |                                       |                            |                                |                      | <b>\$0.46</b>   |                     |
| <b>107 to 127</b>  |                       |                                       |                            |                                | <b>\$0.67</b>        |                 |                     |
| <b>127 +</b>   |                       |                                       |                            |                                | <b>\$0.84</b>        |                 |                     |

1/ Alameda, Contra Costa, San Francisco, San Mateo, Santa Clara, and Santa Cruz counties.

2/ Marin, Solano and Sonoma counties.

3/ Transportation Allowances for the Shasta Receiving Area have not been used since mid-1996.

4/ Los Angeles, Orange, Riverside, San Bernardino, and Ventura Counties.

5/ Numbers in bold represent proposed changes

**Transportation Credits.** The proposed changes to transportation credit rates are summarized in Table 2.

**Table 2 - Proposed Changes to Transportation Credits: *Plant-to-Plant***  
*CDI and DFA proposals would not affect transportation credits.*

Area differentials based on whole milk \$0.27 = \$0.0031 x 87.8;  
 for skim the differential would be \$0.28 = \$0.0031 x 90.9;  
 for condensed skim \$0.21 = \$0.0031 x 68.0

| SUPPLY COUNTIES                           | DEFICIT COUNTIES  |              | CURRENT SINCE Sept 2006 | Institute Proposal       | Humboldt Proposal | Clover testimony |
|---|---|--------------|-------------------------|--------------------------|-------------------|------------------|
| Los Angeles                               | Orange, Riverside, San Bernardino, San Diego and Ventura          | Differential | 0.00                    | 0.00                     |                   |                  |
|   |   | Credit       | 0.37                    | <b>0.50<sup>1/</sup></b> |                   |                  |
|   |   | Total        | \$0.37                  | <b>\$0.50</b>            |                   |                  |
| Tulare                                    | Los Angeles, Orange, and Ventura                                  | Differential | 0.27                    | 0.27                     |                   |                  |
|   |   | Credit       | 0.73                    | <b>0.94</b>              |                   |                  |
|   |   | Total        | \$1.00                  | <b>\$1.21</b>            |                   |                  |
|   | Riverside, San Bernardino and San Diego                           | Differential | 0.27                    | 0.27                     |                   |                  |
|   |   | Credit       | 0.81                    | <b>1.02</b>              |                   |                  |
|   |   | Total        | \$1.08                  | <b>\$1.29</b>            |                   |                  |
| Kings and Fresno                          | Los Angeles, Orange, and Ventura                                  | Differential | 0.27                    | 0.27                     |                   |                  |
|   |   | Credit       | 0.76                    | <b>0.94</b>              |                   |                  |
|   |   | Total        | \$1.03                  | <b>\$1.21</b>            |                   |                  |
|   | Riverside, San Bernardino and San Diego                           | Differential | 0.27                    | 0.27                     |                   |                  |
|   |   | Credit       | 0.84                    | <b>1.02</b>              |                   |                  |
|   |   | Total        | \$1.11                  | <b>\$1.29</b>            |                   |                  |
| Sonoma                                    | Alameda, San Francisco and Santa Clara                            | Differential | 0.00                    |                          |                   |                  |
|   |   | Credit       | 0.27                    |                          |                   |                  |
|   |   | Total        | \$0.27                  |                          |                   |                  |
| <b>Merced and Stanislaus<sup>2/</sup></b> | Alameda, San Francisco and Santa Clara                            | Differential | 0.00                    | 0.00                     |                   |                  |
|   |   | Credit       | 0.38                    | <b>0.80</b>              |                   |                  |
|   |   | Total        | \$0.38                  | <b>\$0.80</b>            |                   |                  |
| <b>Merced and Stanislaus<sup>2/</sup></b> | Sacramento  | Differential | 0.00                    | 0.00                     |                   |                  |
|   |   | Credit       | 0.20                    | <b>0.73</b>              |                   |                  |
|   |   | Total        | \$0.20                  | <b>\$0.73</b>            |                   |                  |
| <b>Merced and Stanislaus</b>              | <b>Solano and Sonoma</b>  | Differential | 0.00                    | 0.00                     |                   |                  |
|   |   | Credit       | 0.00                    | <b>0.79</b>              |                   | <b>0.79</b>      |
|   |   | Total        | \$0.00                  | <b>\$0.79</b>            |                   |                  |
| Humboldt                                  | <b>Orange, Riverside, San Bernardino, Los Angeles and Ventura</b> | Differential | 0.27                    |                          | 0.27              |                  |
|   |   | Credit       | 0.00                    |                          | <b>3.50</b>       |                  |
|   |   | Total        | \$0.27                  |                          | <b>\$3.77</b>     |                  |

<sup>1/</sup> Values in bold represent proposed changes

<sup>2/</sup> The Dairy Institute proposal includes all of Stanislaus County

## GENERAL POLICY CONSIDERATIONS

The economic and marketing factors listed in the Panel Report for the July 2006 hearing remain important considerations for this July 1, 2008 hearing. They help to establish the basic parameters through which proposed changes to the transportation allowances and credits will be reviewed and considered. They include:

- *“Prior to the establishment of milk pooling, a dairy producer’s income was directly related to the actual processing plant that the producer sent their milk. If the plant had a high Class 1 usage, then the producer’s income reflected the higher Class 1 price. If the receiving plant made Class 4 products, then the producer’s income reflected the Class 4 prices. . .*
- *After the establishment of milk pooling: A dairy farm’s revenues do not increase when the farm ships their milk to the highest usage (Class 1, 2, 3) plants. . . Since manufacturing plants are typically operated in rural locations in closer proximity to dairy farms, dairy farms can normally minimize their hauling costs by shipping to these plants. . . [Thus] the cost of hauling milk from the farm to the processing plant becomes a governing factor for determining the destination of the farm milk shipments. . .*
- *The total cost of the transportation allowance and credit system is borne by the Pool.*
- *All producers that share in Pool revenues benefit from higher revenues of Class 1, 2, and 3. – even if their farm milk sales are not shipped to the higher usage plants.*
- *Many producers are paid premiums outside the Pool revenues by manufacturing plants. The availability of these premiums provide additional economic incentives to farms to ship their milk supply to manufacturing plants instead of fluid plants.*
- *As the dairy farms relocate away from metropolitan markets, the annual cost of the milk transportation allowance and credit system will continue to increase.*

Based on the above, the Panel is of the opinion that the following general conclusions made in the Panel Report for the July 2006 hearing are still appropriate to this July 1, 2008 hearing:

- *“California producers have the responsibility to ensure that the higher valued usages are supplied. The cost of the transportation allowance and credit system is the producers’ obligation to finance this responsibility. In return, all producers that participate in the Pool revenues get the opportunity to share in the blended revenues of the higher priced class usage.*
- *California manufacturing plants that satisfy the California Pool qualification requirements and thereby enable the producers that ship farm milk to their plants to participate in the Pool revenues also have the responsibility to make milk supplies available to the higher value usages when needed.*
- *The transportation allowances, which represent the bulk of the milk movement expenses, reimburse the farmer’s hauling costs for their milk shipments to the more distant class 1, 2, 3 usages in the populated urban regions.*
- *Failure to provide adequate reimbursement of transportation allowances and credits, creates an unnecessary financial expenses on those farmers who serve the higher class usage with milk supplies, compared to producers transport their milk supplies to local manufacturing plants.*
- *Inadequate transportation allowance and credit rates will over time tend to encourage all dairy farmers to send their milk to local manufacturing plans, rather than serving the higher valued Class 1, 2, 3 market.*

- *Costs for diesel fuel have continued to increase over the past few years (Hearing Exhibit #7d). As a result, the cost for hauling milk to fluid plants in metropolitan markets has increased since the last public hearing on this subject matter, in July 2006.*

The Panel also believes that the following principles provide sound general criteria for establishing appropriate transportation allowance and credit rates:

1. *The pooling system should seek to make available sufficient milk supplies to the highest classified usages (Class 1, 2, 3).*
2. *The pooling system should only provide transportation/hauling cost reimbursement via transportation allowances and credits to those producers closest to the market that are needed to supply the deficit fluid markets.*
3. *The pooling system should only provide the necessary added transportation costs for serving the higher valued usage of the higher classified usage.*
4. *The system should attempt to minimize costs to the Pool.*
5. *The system of transportation allowance and credits should be reasonably consistent throughout the state.*
6. *When establishing the allowances and credits, there should be equity among competing Class 1 plants.*
7. *It is important that the established transportation allowance and credits are designed to preserve fair competition among supplying producer organizations, and not to promote or encourage monopoly power to a supplying producer organization.*

# **DISCUSSION AND RECOMMENDATIONS FOR TECHNICAL AMENDMENTS TO THE POOLING PLAN**

## **Incorporation of Dairy Accounting System**

### **Issue**

The current Milk Pooling system, utilized by the Milk Pooling Branch, is responsible for the calculation and redistribution of class price revenues to dairy producers. Since the inception of Pooling, the Department has used the same data processing system which is becoming obsolete and is housed on a mainframe computer at the FTB.

While the current Milk Pooling system is functioning, it is very rigid and not easily adaptable to changes. The current system is complex containing over one hundred programs and 110,000 lines of code. The complexity of the code makes it difficult to maintain or enhance, thus limiting changes or enhancements related to pricing and pooling.

The above factors have created a significant need to develop an improved computer program to calculate the Pool. It is the Department's proposal to amend the Pool Plan by inserting a definition for the new DAS. This will allow for the replacement of the aging system with the new DAS.

### **Discussion**

The new DAS has been under development through a joint effort between the Department and the National Agricultural Statistics Service (NASS) under the United States Department of Agriculture (USDA). For decades, NASS has partnered in many projects with the Department to acquire, analyze and share agricultural data. Based upon this relationship, in 2004, the Department began discussions and finalized an agreement with NASS to upgrade/replace the current system. Since then, Department staff and the NASS programming team have worked together in planning and establishing the requirements for this system. Starting in 2006, staff have been testing the new DAS with the existing system successfully.

Except for changes that will occur from transportation allowance mileage calculations and calculations using actual SNF, the new DAS has been developed to mirror the current system. It is expected that the transition from the old system to the new DAS will be relatively seamless, since the current reporting requirements of the industry will not change under the new DAS. The new system should be fully operational by the end of 2008.

All the testimony that addressed this issue at the hearing supported implementation of the new DAS system. There was no opposition expressed at the hearing over implementation.

### **Panel Recommendation**

Amend the Pooling Plan by adding a definition for the Dairy Accounting System.

## **Implementation of Actual Solids-Not-Fat Values For Pool Reporting and Accounting**

### **Issue**

Since the implementation of the Pooling System, the accounting for each handler's SNF has been based on who they purchased their milk from. For handlers who do not purchase farm milk but purchased milk from co-operatives and other handlers, their SNF is accounted for in all classes processed and the milk received using the statewide average SNF factor (.08934715) to skim. For proprietary handlers who purchase from producers (non co-op), their SNF accounting in the Pool is determined by the actual SNF test of the producer's milk acquired during the month.

In the past, milk processors did not have the technology available to economically test for SNF content in milk. The Pooling Plan required that milk processors report the fat content and the skim milk content of the milk received and processed each month. Therefore, the current computer program accounts for the SNF content in the milk based on applying the average solids test to skim pounds to arrive at its SNF pounds. Now, almost all milk handlers test incoming milk for fat and SNF composition and are able to report this data to the Department.

Based upon the widespread testing of actual SNF pounds for incoming milk at processing facilities, the Department proposal would require handlers to report actual SNF pounds, in order to capture the SNF component value based on the application of actual SNF tests to skim.

### **Discussion**

Together with the implementation of the upgrade of the new DAS, the Department will be able to begin accounting for SNF by handlers in a more precise manner, using actual SNF pounds as determined by tests on milk. Thus the proposed amendment to the Pool Plan would account for handlers in the Pool, the actual SNF contained in the milk received from all sources and account for the SNF in the milk utilized on an actual basis, rather than the averages used in the current system.

Prior to proposing the use of actual SNF pounds by handlers, the Department contacted the dairy producer and processor community in order to obtain the stakeholder input for moving away from using average SNF pounds for Pool calculations. The Department received a positive response for the proposal. With the July 2006 Pool month, the Department asked all handlers to report the actual SNF component for bulk milk received and utilized in their plants, including bulk milk shipped out of their plants to other handlers.

While the Department has collected actual SNF tests on utilization and non-farm milk received from handlers since July 2006, the Department has not officially implemented those values in the Pool calculations. However, having the actual solids data reported by the handlers has been crucial for testing the Pool calculations under the new DAS. Without this data, there would be no guarantee the calculations would have been correct once the DAS was ready for official operation.

Though the proposed change requires greater attention by handlers in determining SNF pounds to be reported, any monetary differences in Pool obligations to the handler will be minimal. Furthermore, with the improved DAS and the new process for reporting SNF pounds, a more precise reporting of milk composition is expected. This should not only result in a more accurate valuation of milk produced and utilized within the state, but more accurate Pool accounting as well.

All the testimony that addressed this issue at the hearing supported the implementation of the new DAS system. There was no opposition expressed at the hearing over implementation.

### **Panel Recommendation**

Amend the Pooling Plan by implementing the proposal to account for the actual SNF pounds in calculating the Pool.

## **Replacement of Public Utilities Mileage Table with PC Miler® Program for Distance Measurement in Transportation Allowances**

### **PUC Option versus PC Miler®**

In order to account for the distance that milk travels from a farm to a processing plant, a frame of reference was incorporated into the computer programming system. At the time the transportation allowance system was implemented, the best available reference was a set of mileage tables called "Optional All Points to All Points Table" created by the Public Utilities Commission (PUC). The PUC established the tables in their regulation of transportation and hauling fees that could be charged in California. The state regulation of the trucking industry was later significantly reduced, and unfortunately the PUC ceased updating these mileage tables.

Dairy industry members that frequently rely on truck transportation to ship their commodities/products did advise the Department of the option of replacing the PUC tables with PC Miler®. PC Miler® is used extensively by the trucking industry to establish mileage and rates for hauling commercial cargo. PC Miler® is based on Global Positioning System (GPS) and could be integrated into a relational database.

### **Issue**

An essential component of the Pooling Program is the transportation allowance system. Transportation allowances are based in part on the distance that milk travels from a farm to a processing plant. The current Pooling system utilizes the PUC tables that took into consideration among other things, traffic patterns, road alignment, and toll bridges. The PUC discontinued updating the tables in approximately 1980 when their regulation of the trucking industry was significantly amended. Since 1980, additional people have moved into California, new roads have been built, and existing ones improved. All of these changes have left the PUC tables less relevant to current driving conditions and appropriate mileage calculating.

The Department has recognized that the PUC table was becoming outdated for some time. Despite this fact, the PUC table worked reasonably well in the transportation allowance

system. More importantly, there were no readily available mechanisms that would serve as a better replacement. Consequently, there has been very little interest in replacing the PUC table in the Milk Pooling Plan until now.

Given the Department's efforts to improve and enhance the system that calculates the monthly Milk Pool, staff reviewed several replacement options. Based on the suggestions and recommendations from dairy stakeholders, the Department concluded that the PC Miler® program should be proposed as a replacement for the PUC table.

## **Discussion**

PC Miler® is a program utilized by many trucking firms in California. PC Miler® uses GPS that can be integrated into a relational database. The mileage data that are generated in this system are based on the distance between GPS coordinates of farms and processing plants. GPS coordinates can be readily determined by use of Google Earth, or similar internet based mapping and/or satellite photo services.

Adopting PC Miler® would improve the accuracy of mileage computations, and increase the transparency of those computations. Producers and handlers would be able to more accurately estimate their own mileages, without relying on the Department to look up miles when they are considering changing shipping patterns.

The new mileages that are derived from the PC Miler® data typically are lower in magnitude than the comparable numbers generated by the PUC Tables (see Table 3). If the Department were to adopt the use of the new mileage computations without any other adjustments, the cost of transportation allowances would drop \$86,562 for the month of January 2008, \$73,363 in February 2008 and \$83,371 in March 2008.

The Alliance, CDI, Institute, DFA, and WUD through their testimony/written statements support the implementation of PC Miler® Program as a replacement for the PUC Mileage Table. With the support of other industry organizations, CDI addressed the issue of the need to adopt adjustments to the mileage brackets on distances calculated using PC Miler®. This was to maintain the current transportation allowance values that are in place today supporting the need to move milk to deficit areas.

## **Panel Recommendation**

Amend the Pooling Plan by implementing the PC Miler® Program for calculating distances for transportation allowances.

**Table 3: PC Miler® and PUC Table Distance Between Points Comparison**

**Southern California**

PCMiler and PUC Table Distance Between Points (PUC / PCMiler)

| Place Name   |                   |                            | Artesia              | Buena Park                   | Commerce                      | Compton                  | Downey              | Industry              | Los Angeles             | Riverside           |
|--------------|-------------------|----------------------------|----------------------|------------------------------|-------------------------------|--------------------------|---------------------|-----------------------|-------------------------|---------------------|
|              | GPS Coordinates   | Physical location          | 33.8603<br>118.1251  | 33.8567<br>118.0286          | 33.9951<br>118.1193           | 33.9033<br>118.2212      | 33.9171<br>118.1254 | 34.0748<br>118.0350   | 33.9891<br>118.2915     | 33.9934<br>117.3573 |
|              |                   |                            | South St. Bellflower | Artesia Blvd Valley View Ave | Washington Blvd Greenwood Ave | Rosecrans Ave Alameda St | Imperial Bellflower | Valley Blvd Tyler Ave | Slauson Ave Vermont Ave | Hwy 60 Frwy 215     |
|              |                   |                            | PUC/PCMiler          | PUC/PCMiler                  | PUC/PCMiler                   | PUC/PCMiler              | PUC/PCMiler         | PUC/PCMiler           | PUC/PCMiler             | PUC/PCMiler         |
| Alpaugh      | 35.8877, 119.4873 | Tule Rd & Ave 54           | 194 / 184            | 199 / 185                    | 183 / 174                     | 183 / 176                | 183 / 179           | 194 / 178             | 183 / 169               | 225 / 220           |
| Arvin        | 35.2090, 118.8332 | Bear Mnt Blvd Campus Rd    | 139 / 128            | 144 / 129                    | 128 / 118                     | 128 / 120                | 128 / 123           | 126 / 121             | 128 / 112               | 170 / 189           |
| Buttonwillow | 35.3993, 119.2705 | Hwy 58 & Buttonwillow DR   | 159 / 138            | 164 / 139                    | 148 / 128                     | 148 / 130                | 148 / 132           | 146 / 131             | 148 / 122               | 190 / 173           |
| Conner       | 35.1806, 119.1101 | Old River Rd & Millux Rd   | 133 / 119            | 138 / 120                    | 122 / 109                     | 122 / 111                | 122 / 114           | 120 / 112             | 120 / 104               | 186 / 155           |
| Corcoran     | 36.0981, 119.5566 | Whitley Ave at RR crossing | 207 / 193            | 212 / 194                    | 196 / 183                     | 196 / 185                | 196 / 188           | 194 / 187             | 196 / 178               | 238 / 229           |
| Hanford      | 36.3214, 119.6551 | Hwy 198 & South 11th Ave   | 225 / 216            | 230 / 217                    | 214 / 206                     | 214 / 208                | 214 / 210           | 212 / 209             | 214 / 201               | 256 / 252           |
| Hinkley      | 34.9329, 117.1890 | Sante Fe Ave & Hinkley Rd  | 147 / 123            | 124 / 120                    | 135 / 116                     | 135 / 125                | 135 / 119           | 126 / 107             | 126 / 126               | 87 / 84             |
| Old River    | 35.2672, 119.1097 | Old River RD & Taft Hwy    | 140 / 126            | 145 / 127                    | 129 / 117                     | 129 / 118                | 129 / 121           | 127 / 120             | 127 / 111               | 171 / 162           |
| Ontario      | 33.9977, 117.6281 | Grove & Edison             | 41 / 39              | 34 / 34                      | 34 / 35                       | 45 / 44                  | 37 / 38             | 26 / 28               | 26 / 45                 | 18 / 18             |
| Rio Bravo    | 35.3983, 119.2876 | Mayer Ave & Hwy 58         | 153 / 139            | 158 / 140                    | 142 / 129                     | 142 / 130                | 142 / 133           | 140 / 132             | 140 / 123               | 184 / 174           |
| San Jacinto  | 33.7839, 116.9589 | Main St & San Jacinto Ave  | 81 / 75              | 74 / 70                      | 81 / 81                       | 88 / 83                  | 80 / 77             | 75 / 76               | 75 / 90                 | 32 / 32             |
| Semitrpic    | 35.6010, 119.5091 | Hwy 46 & Gun Club Rd       | 172 / 170            | 177 / 171                    | 161 / 160                     | 161 / 162                | 161 / 165           | 159 / 163             | 161 / 154               | 203 / 205           |
| Shafter      | 35.4998, 119.2705 | East Lerdo Hwy & Hwy 43    | 159 / 144            | 164 / 145                    | 159 / 134                     | 148 / 136                | 148 / 139           | 146 / 137             | 146 / 128               | 190 / 179           |
| Tipton       | 36.0659, 119.3146 | Ave 152 & Hwy 99           | 198 / 181            | 203 / 182                    | 187 / 171                     | 187 / 173                | 187 / 176           | 185 / 175             | 185 / 166               | 229 / 217           |
| Tulare       | 36.2052, 119.3471 | W Inyo Ave & South J St    | 210 / 192            | 215 / 194                    | 199 / 183                     | 199 / 185                | 199 / 188           | 197 / 186             | 199 / 177               | 241 / 228           |
| Visalia      | 36.3269, 119.2923 | Hwy 198 & S Court St       | 218 / 202            | 223 / 203                    | 207 / 192                     | 207 / 194                | 207 / 196           | 205 / 195             | 205 / 186               | 249 / 237           |
| Wasco        | 35.6014, 119.3337 | Hwy 46 & Hwy 43            | 168 / 155            | 173 / 156                    | 157 / 145                     | 157 / 147                | 157 / 150           | 155 / 149             | 157 / 140               | 199 / 191           |

**Northern California**

PCMiler and PUC Table Distance Between Points (PUC / PCMiler)

| Place Name  |                   |                           | San Leandro            | Cordelia           | Rancho Cordova      | Petaluma                  |
|-------------|-------------------|---------------------------|------------------------|--------------------|---------------------|---------------------------|
|             | GPS Coordinates   | Physical location         | 37.7239 122.1614       | 38.2077 122.1506   | 38.5910<br>121.2874 | 38.2339<br>122.6404       |
|             |                   |                           | San Leandro B Davis St | Int 80 Cordelia Rd | US 50 Zinfandel     | Petaluma Blvd Western Ave |
|             |                   |                           | PUC/PCMiler            | PUC/PCMiler        | PUC/PCMiler         | PUC/PCMiler               |
| Los Banos   | 37.0569, 120.8352 | SR 33 & SR 152            | 118 / 103              | 139 / 129          | 124 / 127           | 168 / 156                 |
| Turlock     | 37.4947, 120.8460 | Old 99 & E Main           | 97 / 87                | 108 / 113          | 89 / 89             | 147 / 140                 |
| Modesto     | 37.6363, 121.0034 | SR 99 & I St              | 83 / 73                | 94 / 99            | 75 / 75             | 133 / 126                 |
| Schellville | 38.2460, 122.4385 | Fremont @ old RR crossing | 71 / 55                | 23 / 18            | 83 / 77             | 16 / 15                   |
| Two Rock    | 38.2581, 122.7811 | Valley Ford Rd & Tomales  | 84 / 65                | 50 / 44            | 110 / 112           | 11 / 15                   |
| Artois      | 39.6242, 122.1954 | SR 99 & County Rd 33      | 154 / 151              | 106 / 108          | 107 / 105           | 145 / 140                 |
| Galt        | 38.2523, 121.3056 | 4th St & C ST             | 93 / 88                | 63 / 73            | 28 / 39             | 102 / 105                 |
| Novato      | 38.0807, 122.5455 | US 101 & Sr 37            | 57 / 39                | 31 / 27            | 91 / 86             | 16 / 16                   |

This table is a comparison illustrating distances using PUC tables and the PCMiler program.

## INTRODUCTION: TRANSPORTATION ALLOWANCES AND CREDITS

Transportation allowances and credits were established as a means of providing incentive to supply milk to Class 1 markets in deficit market areas. Transportation allowances partially reimburse those producers who supply milk to higher valued usage (Class 1, 2 and 3) for the higher transportation (hauling) cost to ship their milk supplies (usually produced in California's rural production regions) to California's highly populated urban regions (where fluid plants are typically located). These allowances are provided to dairy farms that transport their market (Grade A) milk from their farms to qualifying plants in deficit areas (qualifying plants process more than 50 percent of the milk received into Class 1, 2, and/or 3 products). Transportation credits offset some of the cost of hauling milk assigned to Class 1 usage from processing plants in designated supply counties to processing plants in designated deficit counties. The cost of these transportation allowances and credits are shared by all producers through the Pool.

Since producers share revenues under the Milk Pooling Plan regardless of the location of the plant where their milk is shipped or the usage of that plant, producers have the incentive to ship milk to the plant located closest to their ranch. Because manufacturing plants tend to be located in rural areas close to ranches, producers are most likely to ship to them as a way to minimize haul costs. With the advent of the Milk Pooling Plan, the dairy stakeholders recognized that serving the needs of the higher valued usages for milk was important, and the dairy producers agreed to serve the needs of the plants with higher value usages. The transportation system was borne from the agreement to serve the needs of the higher value usages, with transportation allowances providing the incentive for producers to ship milk to qualifying plants and transportation credits providing the incentive for milk to move plant-to-plant to deficit areas.

Transportation credits serve as an incentive to move milk from one plant to another in order to more effectively serve the specific needs of bottling plants. Ranch milk closely resembles the composition of whole milk. However, presently whole milk represents only about 33 percent of fluid milk sales in California compared to about 66 percent for non-fat and reduced fat milks, which have grown in popularity over time. In order to create non-fat and reduced fat milks, a bottling plant has to remove fat and also add additional SNF (fortification) in order to meet California fluid milk standards. Bottling plants then have to ship their excess fat to manufacturing plants and obtain extra milk for fortification purposes. In order to more efficiently handle this situation, bottling plants can receive condensed skim milk from other plants for use in the fortification process. Since not all bottlers have the equipment available to effectively handle their needs for additional SNF fortification, it is often more efficient to purchase condensed skim milk from other plants. Overall, cost savings can be achieved by the receipt of condensed skim milk at the bottling plant; therefore, the transportation credits provide the incentive for milk shipments plant-to-plant to serve this need.

Traditionally, Southern California has been the major deficit area of the state needing shipments of milk to meet its needs and this continues today. The vast majority (95 percent) of the milk shipped under the transportation system is shipped ranch-to-plant, with 75 percent of that going to Southern California, as evidenced by the following table. Plant-to-plant shipments pale in magnitude when compared to ranch-to-plant shipments, but the majority of these shipments (93 percent) go to Southern California as well. Ultimately, the milk movement incentives provided by transportation allowances and credits are important, especially the incentives moving milk to Southern California. Therefore we will discuss

these incentives beginning with the areas of greatest magnitude, the transportation allowances to Southern California.

**Table 4: Historic Volumes of Milk Using Transportation Allowances and Credits and the Impact to the Pool For the Period May 2007 to April 2008**

**Monthly Average Pounds of Milk Using Transportation Allowances and Credits for May 2007 to Apr 2008**

| <b>For Milk Going to:</b> | <b>Allowances: Ranch-to-Plant</b> | <b>Credits: Plant-to-Plant</b> | <b>Total</b>       |
|---------------------------|-----------------------------------|--------------------------------|--------------------|
| <b>Sacramento</b>         | 13,960,833                        | 0                              | 13,960,833         |
| <b>North Bay</b>          | 48,913,083                        | 0                              | 48,913,083         |
| <b>Bay Area</b>           | 86,793,000                        | 2,041,842                      | 88,834,842         |
| <b>San Diego</b>          | 1,822,333                         | 0                              | 1,822,333          |
| <b>So. Calif.</b>         | 403,869,667                       | 27,004,646                     | 430,874,313        |
| <b>TOTAL</b>              | <b>555,358,917</b>                | <b>29,046,488</b>              | <b>584,405,405</b> |

**Monthly Average Estimated Impact to the Pool for May 2007 to April 2008**

| <b>For Milk Going to:</b> | <b>Allowances: Ranch-to-Plant</b> | <b>Credits: Plant-to-Plant</b> | <b>Total</b>       |
|---------------------------|-----------------------------------|--------------------------------|--------------------|
| <b>Sacramento</b>         | \$22,635                          | \$0                            | \$22,635           |
| <b>North Bay</b>          | \$122,208                         | \$0                            | \$122,208          |
| <b>Bay Area</b>           | \$249,891                         | \$7,759                        | \$257,650          |
| <b>San Diego</b>          | \$5,689                           | \$0                            | \$5,689            |
| <b>So. Calif.</b>         | \$2,100,361                       | \$102,997                      | \$2,203,358        |
| <b>TOTAL</b>              | <b>\$2,500,784</b>                | <b>\$110,756</b>               | <b>\$2,611,540</b> |

## **DISCUSSION AND RECOMMENDATIONS FOR TRANSPORTATION ALLOWANCES SOUTHERN CALIFORNIA**

### **Transportation Allowances for the Southern California and San Diego Receiving Areas**

#### **Issue**

Increases in diesel fuel and related energy costs have raised the transportation cost to haul milk from dairy farms to processing plants in major urban markets. The relocation of dairy farms away from the urban centers of Southern California to the southern San Joaquin Valley, creates additional difficulty in ensuring adequate milk supplies are made available for fluid plants located in the Southern California receiving area.

The proposed adoption of the PC Miler® software program in place of the PUC table by the Department to measure distances will result in changes in the amount of transportation allowances given for milk movement to deficit areas in some situations. Data resulting from using PC indicates that it tends to give lower mileages than what was determined using the PUC tables. Overall, this results in less transportation allowances given to producers under current milk supply movements to deficit areas. The proposed transportation allowance increases proposed by dairy stakeholders would address these issues.

Humboldt, a co-operative association located in Humboldt County is requesting that Humboldt and Del Norte counties become new supply counties for milk received in the Southern California receiving area. In addition, Humboldt has asked for a transportation allowance rate change of \$0.70/cwt. to \$3.50/cwt. for milk transported to the Southern California receiving area.

### **Transportation Allowances for Southern California Receiving Area from all Counties other than Riverside and San Bernardino.**

#### **Discussion**

A summary of the current and proposed transportation allowance rates is presented in Table 1. During the hearing, witnesses for CDI, Institute, and WUD reiterated the following precepts for implementing transportation allowances:

- Transportation allowances contribute to the orderly marketing of milk.
- Producers should be responsible for local hauls, and transportation allowances should compensate producers/co-ops that service Class 1, 2 and 3 markets from outside local areas.
- Allowance rates should be cost justified.
- Incentives should be implemented from the closest production area, discouraging milk movement from distant locations, and minimizing the cost to the Pool.
- In setting rates and brackets consider existing milk movement patterns

To these the Institute added:

- Due to the necessity of moving milk longer distances, a shortfall should be limited to the most distant milk supplies only.
- Should consider future milk movement patterns.

Most testimony concurred that the cost of transporting milk has increased significantly and should be recognized by increasing rates for transportation allowances.

CDI, DFA, Institute, Alliance and LOL also testified that mileage brackets used in determining distances for transportation allowances should be adjusted for the proposed adoption of PC Miler®. CDI testified that these bracket changes for PC Miler® “will not be disruptive to current milk movement patterns or cause windfalls or hardships to producers.”

CDI testified that the adoption of PC Miler® under the current mileage brackets would disadvantage several producers who are shipping from southern Kern County to the Los Angeles area. CDI indicated an adjustment for PC Miler® is necessary from Tulare and Kern counties to supply the Southern California Class 1 market. They requested a bracket of 99 to 119 miles be implemented to recover costs in moving milk from southern Kern County to the Southern California receiving area.

In addition, CDI requested bracket changes and increased mileage rate of \$0.67/cwt. for the 99 to 119 mileage bracket. A recent notice submitted by CDI from Kings County Trucking indicated a cost of \$0.33/cwt. for local deliveries in the Kings, Tulare, and Kern counties and a cost of \$1.005/cwt. for shipments to the Los Angeles area. The March 2008 Department haul survey confirms this data, \$1.04/cwt. Kern County to Los Angeles and a local southern San Joaquin Valley rate of \$0.33/cwt. The suggested rates by CDI were supported by testimony and documentation from other hearing witnesses.

While the Institute agreed with CDI bracket and rate amendments, they also testified that while transportation allowances address the problem of attracting milk to fluid plants, they indicated concern over competition among Class 1 plants: “However, when setting both allowances and credit rates, equity among Class 1 plants in attracting milk supplies is something that needs to be considered.”

DFA, in their post hearing brief, agreed with CDI bracket amendments and indicated their support of CDI mileage rates in their testimony.

Humboldt testified in favor of increasing the transportation allowance for milk shipments from the Humboldt and Del Norte counties into the Southern California receiving area from \$0.70/cwt. to \$3.50/cwt. They stated in their alternative proposal dated, June 2, 2008, “We have a long term commitment to supply organic milk to our customers but rising fuel costs are putting us at a further disadvantage with each passing day.”

Humboldt testified that seventy percent (70%) of the organic milk producers in California are located in the Humboldt and Del Norte counties. Humboldt stated that with a majority of the organic milk supply located in the northwest corner of California, they believe there is a need to move organic milk to processors who process Class 1 products in deficit areas such as the Bay Area and Southern California.

In their testimony, CDI was concerned that the Humboldt proposal did not meet the requirements for receiving transportation allowances. CDI cited the long-standing position that the milk closest to the market should be adequately compensated for transportation

credits or allowances and disincentives should be incorporated for more distant locales. CDI testified that while the proposal addresses a small amount of organic milk and milk entering the state, it would provide an opportunity for milk to be transported, at producer expense, from one of the most northern counties in California to Southern California. DFA and the Institute also opposed the concept of having Humboldt and Del Norte counties designated as supply areas for transportation allowances.

In support of their opposition, the Institute stated that the California Food and Agricultural Code governing pooling and pricing makes no distinction between organic and conventional milk. From a “conventional” point of view, there is no reason for the Pool to subsidize milk movements from Humboldt County to the Los Angeles market because milk is available from closer sources. Furthermore, the Institute testified that, while out-of-state organic milk may supplant California organic milk in this market, Humboldt’s proposal would apply to all milk moving that long distance.

MPC testified that they strongly opposed the Humboldt transportation allowance proposal. They stated that since organic milk receives a premium in the marketplace over conventional milk, the Pool should not subsidize any transportation since other producers in the Pool would not be sharing those premiums received by Humboldt.

The Panel analyzed the proposed rate increases using the Department March 2008 haul survey and U.S. Dept. of Energy diesel fuel prices to perform a margin analysis. For the last two years, on a six month basis, the Department has released its haul survey that shows the actual hauling rates charged for both ranch-to-plant and plant-to-plant milk shipments. The latest survey was released in June 2008 for the hauling costs of March 2008. Using this haul cost as a basis, the Panel reviewed the additional haul cost one would expect based on the increase in diesel fuel prices from March to June 2008 from the U.S. Department of Energy and the average hundredweight load and miles per gallon of a truck making a roundtrip between the ranch and the plant of first receipt. By adding this additional cost to the base haul rate released by the Department, the Panel could estimate an expected range of rates that would seem reasonable for hauling costs for June 2008. Using this expected range of rates, coupled with other Department data and analysis, the Panel found the proposed rate increases were reasonably related to the current hauling costs.

When considering proposed mileage bracket changes, the Panel reviewed the lists of individual producers shipping to each of the receiving areas with their corresponding volumes and ranch-to-plant distances in miles from both the PUC table and PC Miler®. In analyzing each specific receiving area, the Panel sought to minimize costs to the Pool and also maintain the same level of milk movement incentives by keeping individual producers in the same mileage bracket after the adoption of PC Miler®. The Panel was cognizant that if an individual producer moves to a shorter distance mileage bracket, the rate will decrease and the incentive for that producer to continue to ship to the Class 1 market decreases. On the other hand, if a producer moves to a longer mileage bracket, the opposite occurs. The Panel recognizes that when recommending new mileage brackets, it is not possible to keep all producers in the same mileage bracket. The Panel also recognized that it was important to minimize the number of producers moving to a lower mileage bracket so that the adoption of PC Miler® does neither significantly change the current incentives of the transportation allowances nor significantly change the current movement of milk.

In reviewing the amount of producer milk available for serving the Class 1 market, the Panel determined the amount that is closest to the deficit receiving area. The Panel analyses indicate that sufficient milk was available from many sources that are closer than Humboldt and Del Norte counties to serve the needs of the Southern California receiving area. While this supply may not be under the control of Humboldt Creamery it would be inappropriate to have transportation allowances expanded to a new supply area, while there are sufficient milk supplies that are much closer. With this in mind, the need to establish Humboldt and Del Norte counties as a supply area would not be appropriate and not cost effective. After reviewing the testimony and letters received from the industry, the Panel was in agreement with the concerns expressed by CDI, DFA, Institute, and MPC. The Panel finds that the Humboldt proposal is contrary to the criteria that have been applied to establishing transportation allowances.

The cost of transporting milk has increased as indicated by the testimony and available energy data. The Department haul survey for March 2008 indicated higher transportation rates being charged for all movements of milk as compared with data established in prior surveys which were used in the last transportation allowance hearing of July 2006. The need to move producer milk from supply areas to deficit Class 1 markets in Southern California remains. The Southern San Joaquin Valley is one of the major supply areas of producer milk for facilities processing Class 1 products in Southern California. The volume of milk from this area continues to increase as milk production decreases in Southern California. With the current increases in transportation costs for transporting producer milk from supply areas, an increase in rates and adjustments to mileage brackets to address milk movement concerns is justified.

## **Panel Recommendation**

### **For the Southern California Receiving Area:**

From all counties other than Riverside and San Bernardino counties:

- Increasing the rate from \$0.11/cwt. to \$0.15/cwt.; change the mileage bracket from 0-89 miles to 0-79 miles
- Increasing the rate from \$0.37/cwt. to \$0.46/cwt.; change the mileage bracket from over 89-109 miles to over 79-99 miles
- Increasing the rate from \$0.56/cwt. to \$0.67/cwt.; change the mileage bracket from over 109-139 miles to over 99-119 miles
- Increasing the rate from \$0.70/cwt. to \$0.84/cwt.; change the mileage bracket from over 139 to over 119 miles

### **Transportation Allowances for Southern California Receiving Area from Riverside and San Bernardino Counties**

## **Discussion**

A summary of the current and proposed transportation allowance rates is presented in Table 1. Producers located in Riverside and San Bernardino counties continue to service the needs for the Class 1 market in Southern California.

CDI proposed that transportation allowance rates be increased and mileage brackets adjusted for producer milk serving the Southern California receiving area to compensate for

increased hauling costs. The Institute and DFA both testified in support of CDI rate increases and bracket changes.

In addition, CDI also testified that San Bernardino and Riverside supply areas be maintained as a separate supply area from the other 56 counties to provide sufficient allowances for the dairies located in the High Desert serving the Southern California market. In their testimony, DFA supported CDI in the importance of maintaining the San Bernardino and Riverside counties.

The Panel reviewed the current mileage brackets to determine whether changes were necessary to implement PC Miler® and maintain adequate transportation allowances. The Panel is recommending that the first mileage bracket to be 0-93 miles changed from 0-89 miles, to ensure that revised mileage brackets for PC Miler® minimize the impact to producers and to Pool revenue. The producer milk shipments from this supply area to Southern California indicated a need to amend the current brackets and rates to reflect the increases in hauling and transportation costs.

### **Panel Recommendation**

#### **For the Southern California Receiving Area:**

For the Riverside and San Bernardino Supply Areas:

- Increasing the rate from \$0.11/cwt. to \$0.15/cwt.; change the mileage bracket from 0-89 miles to 0-93 miles
- Increasing the rate from \$0.37/cwt. to \$0.46/cwt.; change the mileage bracket from over 89 miles to over 93 miles

### **Transportation Allowances for the San Diego Receiving Area**

#### **Issue**

A summary of the current and proposed transportation allowance rates is presented in Table 1. CDI testified that the mileage brackets and mileage rates for the San Diego receiving area should be amended due to the higher transportation costs incurred while moving producer milk to this area.

#### **Discussion**

The Institute supported the CDI proposal. The hearing of July 6, 2006 addressed the milk movement issues for San Diego County. At that time the concern was the number of producers located in San Diego had continued to decline and the availability of local milk for the remaining plant with Class 1 processing in San Diego County was diminishing. In addition, the San Diego receiving area is in competition for milk from the Southern California receiving area. In 2008 these concerns still remain.

The Panel analyses concur that the CDI and Institute proposed rates and bracket changes had merit considering the need for bracket changes due to implementing PC Miler® and increases in hauling costs as indicated in the Department March 2008 haul survey.

### **Panel Recommendation**

#### **For the San Diego Receiving Area:**

- Increasing the rate from \$0.11/cwt. to \$0.15/cwt.; change the mileage bracket from 0-89 miles to 0-79 miles
- Increasing the rate from \$0.43/cwt. to \$0.46/cwt.; change the mileage bracket from over 89-139 miles to over 79-119 miles
- Increasing the rate from \$0.70/cwt. to \$0.84/cwt.; change the mileage bracket from over 139 miles to over 119 miles

## **DISCUSSION AND RECOMMENDATIONS FOR TRANSPORTATION ALLOWANCES NORTHERN CALIFORNIA**

### **Issue**

Many of the issues raised regarding transportation allowances in Southern California were also raised in Northern California. Transportation allowance proposals for milk supplied to the Bay Area, North Bay, and Sacramento deficit areas presented minimal diversity among petitioners at this hearing. The majority of the witnesses supported the notion that transportation allowances should make the producers indifferent between shipping milk to a distant Class 1, 2 or 3 processing plant versus a closer manufacturing plant. For these three areas, the volume of milk movement is much less when compared to Southern California.

Witnesses that proposed changes to specific allowance rates focused their testimony on areas in which they supplied milk. All the proposals appeared to be reasonable relative to recent hauling and fuel cost increases, and were fairly consistent among witnesses.

The Department also proposed the adoption of the PC Miler® software program in place of the PUC table to measure ranch-to-plant distances which would result in changes to transportation allowances for milk moving to these deficit areas. PC Miler® would tend to give lower mileages than what has been determined using the PUC tables, resulting in less transportation allowances given to some producers compared to the current PUC mileage system. While proponents addressed these issues in Southern California areas, they made no specific proposals for mileage bracket changes in Northern California. Several witnesses did mention that the move from the PUC tables to PC Miler® might require adjustments to the mileage brackets.

### **Discussion**

A summary of the current and proposed transportation allowance rates is presented in Table 1. In general, CDI proposed to increase the rates for the Bay Area receiving area in all mileage brackets, while leaving North Bay and Sacramento unchanged as they had no deliveries into these areas. CDI supplies the Bay Area from Marin, Sonoma, Merced, Stanislaus and San Joaquin counties. They testified that the local haul rate is \$0.34/cwt. and the cost to deliver to the Bay Area is \$0.70/cwt. resulting in a difference of \$0.36/cwt. Therefore, they have proposed a change for the zero to 99 mile range. CDI testified that they do not regularly supply the Bay Area from outside the 99 mile range, but requested corresponding adjustments to the higher mileage brackets.

In regards to the CDI proposal for changes to the rate for transportation allowances, rate increases and subsequent changes made by Kings County Truck Lines, California Milk Transport and Orozco Trucking were submitted to substantiate the increases in hauling and fuel costs.

DFA presented a proposal to change the rates in all three active Northern California receiving areas. For the Bay Area, DFA called for cost related increases but also argued that in recent years the Bay Area has lagged behind other areas, in terms of the transportation allowance levels. They contended that the haul rates to the Bay Area, up to

99 miles, run approximately \$0.70-\$0.90/cwt., but currently capture only a \$0.27/cwt. allowance. DFA provided documentation with their testimony to support their statements.

The Institute testimony favored adopting the transportation allowance rate changes attested to by DFA. They expressed that when setting both allowances and credit rates, equity among competing Class 1 plants in attracting milk supplies is something that needs to be considered. The Institute position was that fluid milk plants operating within a market should not be disadvantaged relative to each other in the procurement of nearby milk supplies.

The Panel recognizes the need to ensure Class 1 plants have an adequate milk supply. It also recognizes that there is a need to increase the transportation allowances taking into consideration the increased costs of fuel and overall hauling charges. All proponents of rate increases expressed this same concern. Testimony, supporting documentation, and the Department's March 2008 haul survey evidenced the need to make adjustments in the Northern California allowances. Additional analysis of increased fuel costs between March and June 2008 further justifies the need for increases in the rates for transportation allowances. The Panel used the same approach as was used for Southern California and believes there is sufficient justification increasing the allowances.

The Panel recommended increases in rates for the Bay Area either mirror or stay within the amounts proposed in the CDI and DFA proposals. There are, however, a few exceptions for the other areas.

CDI made no mention of North Bay or the Sacramento area. DFA and the Institute kept the lowest mileage bracket rates unchanged for North Bay and Sacramento. However, testimony was given by Clover that requested consideration for the North Bay lowest bracket be increased \$0.10/cwt. from \$0.19/cwt. to \$0.29/cwt. Again rising fuel costs were the indicators for Clover's request.

For the Sacramento area, DFA and the Institute proposed changes to the over 59 mileage bracket, an increase of \$0.05/cwt. from \$0.20/cwt. to \$0.25/cwt. The Panel agreed that there was justification for an increase due to high fuel costs across the state; however given that there was currently no milk movement in Sacramento within that mileage bracket, the need for the full requested increase of \$0.05/cwt. was not substantiated. However a \$0.03/cwt. increase would be an appropriate adjustment to reflect the relative cost issues.

Although there were no proposed mileage bracket changes for the Bay Area, North Bay or Sacramento Area, the Panel reviewed the current mileage brackets to determine whether changes were necessary to implement PC Miler® and maintain adequate transportation allowances. The Panel is recommending that the mileage brackets be changed to ensure that revised mileage brackets for PC Miler® have minimal impact on individual producers and Pool costs. The producer milk shipments from these areas indicated a need to amend the current brackets and rates to reflect the increases in hauling and transportation costs.

### **Panel Recommendations**

For the Bay Area Receiving Area:

- Increasing the rate from \$0.27/cwt. to \$0.36/cwt.; change the mileage bracket from 0-99 miles to 0-78 miles

- Increasing the rate from \$0.34/cwt. to \$0.45/cwt.; change the mileage bracket from over 99-199 miles to over 78-199 miles
- Increasing the rate from \$0.36/cwt. to \$0.47/cwt.; no change in the over 199 mileage bracket

For the North Bay Receiving Area:

- Increasing the rate from \$0.19/cwt. to \$0.23/cwt.; change the mileage bracket from 0-44 miles to 0-45 miles
- Increasing the rate from \$0.29/cwt. to \$0.35/cwt.; change the mileage bracket from over 44-99 miles to over 45-96 miles
- Increasing the rate from \$0.34/cwt. to \$0.44/cwt.; change the mileage from over 99 miles to over 96 miles

For the Sacramento Receiving Area:

- Increasing the rate from \$0.20/cwt. to \$0.23/cwt.; no change in the 59+ mileage bracket

## **DISCUSSION AND RECOMMENDATIONS FOR TRANSPORTATION CREDITS**

### **Transportation Credits for Southern California**

#### **Issue**

Many dairy stakeholders testified that during the past few years, the cost of diesel fuel has significantly increased in California. Specifically, it has risen to unprecedented levels in the past few months, thus changing the cost of milk movement across the state. CDI, the Institute, DFA and Clover all explicitly testified to the increases in hauling rates by submitting documentation on fuel rates and trucking costs.

Additionally, there are no supply counties for transportation credits to Southern California from counties north of Kings and Fresno. While Humboldt and Del Norte counties are eligible for transportation allowances, they are not designated as supply counties, thus ineligible to receive transportation credits. Humboldt requested that the designated supply counties for eligible transportation credits include Humboldt and Del Norte counties for shipments to Southern California.

#### **Discussion**

In addition to San Diego County, five counties in the Southern California area are deficit in available milk production and have been designated as being eligible for transportation credits. The Institute proposed to increase all the transportation credit rates into Southern California. Humboldt proposed to add Humboldt and Del Norte counties as designated supply counties for shipments to the deficit counties of Los Angeles, Riverside, San Bernardino, Orange and Ventura counties. A summary of the current and proposed rates is presented in Table 2.

With the increase in diesel fuel costs and subsequent hauling costs associated with milk shipments, the Panel has concluded that increases in the rates for transportation credits are warranted in order to assure the needs of the Class 1 market continue to be met. Except for WUD and CDC, who opposed increases in the rates of transportation credits in general, there was no opposition to any of the specific rates proposed by the Institute. It appears the Institute's proposed rate increases correspond exactly with the March 2008 plant-to-plant haul rates as released by the Department in June 2008. The Institute testified that credit rates should be equal to the haul cost minus any area differential for all but the most distant milk in order to encourage competition in supplying the Class 1 market.

The Panel agrees that credit rates should be cost-justified and related to actual haul costs, and that a shortfall of \$0.05/cwt. is warranted. Furthermore, there are additional factors of importance that must be considered when establishing rates including, but not limited to, equity and competition among Class 1 processors, competition among all possible suppliers of milk, relative comparison of transportation credit rates to the transportation allowance rates for milk moving similar distances, minimizing costs to the Pool, and Department data and analyses. Therefore, when setting its recommended credit rate increases, the Panel considered a myriad of factors.

Moreover, the Panel considered other factors that are specific to certain supply/deficit county combinations when determining its recommended rate increases. Currently, there is enough milk in the supply counties of Los Angeles and Tulare to meet the regular plant-to-plant needs of the Southern California deficit counties. Therefore, the rates to the Southern California deficit counties should provide incentives such that qualifying milk movements primarily originate from Los Angeles and Tulare counties. Since potential supply plants in Fresno and Kings counties are approximately 50 to 60 miles further north than those in Tulare County, the credit for these counties should not provide a great enough incentive to supplant closer milk from Tulare County.

Department data show that over the last few years, the vast majority of qualifying milk originated from Los Angeles and Tulare counties. The relative comparison between the current rate for the supply counties of Fresno and Kings is such that the closer milk from the supply counties of Los Angeles and Tulare is regularly moving to meet the needs of the Class 1 market and should continue in the future.

Humboldt proposed adding Humboldt and Del Norte counties as designated supply counties for shipments to Southern California. MPC, DFA, Institute, WUD and CDI opposed the proposal. When the Department analyzes milk movement incentives, it must encourage the closest supply areas to serve to the deficit markets first. In this case, Department data shows that an adequate amount of milk is already being shipped to Southern California from counties between Humboldt/Del Norte and Southern California. This available milk supply is closer to Southern California than Humboldt/Del Norte, hence there is no need to subsidize milk from further away. Moreover, some milk shipped to Southern California comes from counties in Northern California not designated as supply counties, thus not qualified for transportation credits. The Panel has concluded that the milk movement into the Southern California receiving area from Northern California plants is already responding to economic and market incentives that are external to the transportation credit system.

The Panel also needs to take into consideration the competition among milk suppliers and ensure the transportation credit system does not result in inequitable competition. The credits should not encourage unfair advantages to supplying organizations. Allowing transportation credits from Humboldt/Del Norte would reduce their cost of milk shipments to Southern California. This would give a competitive advantage to suppliers in Humboldt/Del Norte over suppliers located closer to Southern California that are not part of a supply county.

### **Panel Recommendation**

- Increasing the transportation credit from Los Angeles County to Orange, Riverside, San Bernardino, San Diego, and Ventura counties from \$0.37/cwt. to \$0.45/cwt.;
- Increasing the transportation credit from Tulare County to Los Angeles, Orange, and Ventura counties from \$0.73/cwt. to \$0.89/cwt.;
- Increasing the transportation credit from Tulare County to Riverside, San Bernardino, and San Diego counties from \$0.81/cwt. to \$0.97/cwt.;
- Increasing the transportation credit from Fresno and Kings counties to Los Angeles, Orange, and Ventura counties from \$0.76/cwt. to \$0.89/cwt.;
- Increasing the transportation credit from Fresno and Kings counties to Riverside, San Bernardino, and San Diego counties from \$0.84/cwt. to \$0.97/cwt.;
- Not designating Humboldt and Del Norte counties as supply counties for shipments to deficit counties in Southern California.

## **Transportation Credits for Northern California**

### **Issue**

Similar to Northern California, many interested stakeholders testified that during the past few years, the costs of diesel fuel have significantly increased in California, thus changing the costs of milk movement across the state. CDI, the Institute, DFA and Clover all explicitly testified to the increases in hauling rates by submitting documentation on fuel prices or trucking costs.

While Solano and Sonoma counties are eligible for transportation allowances, they are not designated as deficit counties under the transportation credit system. The Institute testified that in recent years the industry has evolved and undergone structural changes that have changed milk production and distribution patterns. As a result, the Institute proposed to establish a transportation credit for milk shipped from Merced and all of Stanislaus counties to Solano and Sonoma counties.

Only a portion of Stanislaus County is currently designated as a supply county shipping to the Bay and Sacramento areas. Super Store testified that the boundaries of all the other areas of the state that are designated as supply or deficit counties follow county lines. The Institute and Super Store supported changing the definition of Stanislaus County to include the entire county in order to allow all major processing plants located in the designated counties to qualify for transportation credits.

### **Discussion**

In Northern California, transportation credits currently are established for the Bay Area and the Sacramento Area receiving areas. The Institute proposed to increase all the transportation credit rates in Northern California except for the designated supply county of Sonoma to the deficit counties of Alameda, San Francisco and Santa Clara. A summary of the current and proposed rates is presented in Table 2. The Institute also proposed to include the entire county of Stanislaus as a supply county (instead of that portion of Stanislaus County lying south of the standard parallel between Township 3 South and Township 4 South, Mount Diablo Meridian as it currently is designated) and to make credits available to the North Bay Area (Solano and Sonoma counties).

The Panel considered the same type of factors when analyzing what rate changes would be adequate in Northern California as previously mentioned in the discussion of Southern California. More specifically, the Panel looked at the March 2008 haul survey that was released by the Department in June 2008, again including a shortfall of \$0.05/cwt.

Currently, there are no milk shipments from Sonoma County plants to plants in the Bay area. However, in order to maintain equity and proper competition between Class 1 processors, the incentive should continue to exist for the future, with a credit in the same magnitude as the credit for the supply county of Los Angeles moving to the deficit counties within Southern California. The Panel recognized the credits for Merced and Stanislaus counties and Sonoma County to the Bay area have not been updated for 17 years, so the increase in these credits needs to be large enough to bring the rates back into alignment with hauling costs. The credit for Merced and Stanislaus counties to Sacramento is drastically below current hauling costs and must be increased to a level that is more closely

related to actual hauling costs in order to maintain equitable credit rates across different supply/deficit county combinations.

Regarding the Institute proposal to include all of Stanislaus County as a designated supply county and the establishment of a new credit from Merced and Stanislaus counties to Sonoma and Solano counties, there was no specific opposition in the hearing record. DFA, Clover, and Super Store all specifically supported these changes. Clover testified that these changes would resolve inequity issues that currently exist in the Bay and North Bay areas. Clover stated that milk routinely moves from Merced and Stanislaus counties to Sonoma and Solano counties, and due to the close proximity of the Bay and North Bay areas, milk moves in similar fashion to both areas. Since the Bay area currently receives credits and the North Bay does not, there are inequities among Class 1 processors in these areas. Department data confirm this trend. The Panel agrees that if a need exists to move qualifying milk from Merced and Stanislaus counties to Sonoma and Solano counties, then the proposed credit could be implemented. Also, except for Stanislaus, the designated areas for credits follow county lines. The Panel concurs that designated areas should all be defined by the entire county in order to include all major processing plants for competition and equity sake.

### **Panel Recommendation**

- Designating the entire county of Stanislaus as a supply county for purposes of transportation credits;
- Increasing the credit from Sonoma County to Alameda, San Francisco, and Santa Clara counties from \$0.27/cwt. to \$0.45/cwt.;
- Increasing the credit from Merced and all of Stanislaus counties to Alameda, San Francisco, and Santa Clara counties from \$0.38/cwt. to \$0.75/cwt.;
- Increasing the credit from Merced and all of Stanislaus counties to Sacramento from \$0.20/cwt. to \$0.68/cwt.;
- Establishing a credit from Merced and all of Stanislaus counties to Solano and Sonoma counties at a rate of \$0.74/cwt.

This Hearing Panel Report has been prepared and submitted by:

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## SUMMARY OF PANEL RECOMMENDATIONS

### DISCUSSION AND RECOMMENDATIONS FOR TECHNICAL AMENDMENTS TO THE POOLING PLAN

#### Panel Recommendation

- Amend the Pooling Plan by adding a definition for the Dairy Accounting System.
- Implement the proposal to account for the actual SNF pounds in calculating the Pool.
- Amend the Pooling Plan by implementing the PC Miler® Program for calculating distances for transportation allowances.

### DISCUSSION AND RECOMMENDATIONS FOR TRANSPORTATION ALLOWANCES FOR SOUTHERN CALIFORNIA

#### Panel Recommendation

##### For the Southern California Receiving Area:

From all counties other than Riverside and San Bernardino counties:

- Increasing the rate from \$0.11/cwt. to \$0.15/cwt.; change the mileage bracket from 0-89 miles to 0-79 miles
- Increasing the rate from \$0.37/cwt. to \$0.46/cwt.; change the mileage bracket from over 89-109 miles to over 79-99 miles
- Increasing the rate from \$0.56/cwt. to \$0.67/cwt.; change the mileage bracket from over 109-139 miles to over 99-119 miles
- Increasing the rate from \$0.70/cwt. to \$0.84/cwt.; change the mileage bracket from over 139 to over 119 miles

For the Riverside and San Bernardino Supply Areas:

- Increasing the rate from \$0.11/cwt. to \$0.15/cwt.; change the mileage bracket from 0-89 miles to 0-93 miles
- Increasing the rate from \$0.37/cwt. to \$0.46/cwt.; change the mileage bracket from over 89 miles to over 93 miles

##### For the San Diego Receiving Area:

- Increasing the rate from \$0.11/cwt. to \$0.15/cwt.; change the mileage bracket from 0-89 miles to 0-79 miles
- Increasing the rate from \$0.43/cwt. to \$0.46/cwt.; change the mileage bracket from over 89-139 miles to over 79-119 miles
- Increasing the rate from \$0.70/cwt. to \$0.84/cwt.; change the mileage bracket from over 139 miles to over 119 miles

Most producers serving the fluid market will receive increased compensation of \$0.03/cwt. to \$0.14/cwt. As an example, for March 2008, this increased compensation would result in redistributing an approximate additional \$500,591/month of Pool revenues. (This estimated funding increase assumes that these rates had been in place during the month of March 2008).

## **DISCUSSION AND RECOMMENDATIONS FOR TRANSPORTATION ALLOWANCES FOR NORTHERN CALIFORNIA**

### **Panel Recommendation**

For the Bay Area Receiving Area:

- Increasing the rate from \$0.27/cwt. to \$0.36/cwt.; change the mileage bracket from 0-99 miles to 0-78 miles
- Increasing the rate from \$0.34/cwt. to \$0.45/cwt.; change the mileage bracket from over 99-199 miles to over 78-199 miles
- Increasing the rate from \$0.36/cwt. to \$0.47/cwt.; no change in the over 199 mileage bracket

For the North Bay Receiving Area:

- Increasing the rate from \$0.19/cwt. to \$0.23/cwt.; change the mileage bracket from 0-44 miles to 0-45 miles
- Increasing the rate from \$0.29/cwt. to \$0.35/cwt.; change the mileage bracket from over 44-99 miles to over 45-96 miles
- Increasing the rate from \$0.34/cwt. to \$0.44/cwt.; change the mileage from over 99 miles to over 96 miles

For the Sacramento Receiving Area:

- Increasing the rate from \$0.20/cwt. to \$0.23/cwt.; no change in the over 59 mileage bracket

Most producers serving the fluid market will receive increased compensation of \$0.03/cwt. to \$0.11/cwt. As an example, for March 2008, this increased compensation would result in redistributing an approximate additional \$131,773/month of Pool revenues. (This estimated funding increase assumes that these rates had been in place during the month of March 2008).

## **DISCUSSION AND RECOMMENDATIONS FOR TRANSPORTATION CREDITS FOR SOUTHERN CALIFORNIA**

### **Panel Recommendation**

- Increasing the transportation credit from Los Angeles County to Orange, Riverside, San Bernardino, San Diego, and Ventura counties from \$0.37/cwt. to \$0.45/cwt.;
- Increasing the transportation credit from Tulare County to Los Angeles, Orange, and Ventura counties from \$0.73/cwt. to \$0.89/cwt.;
- Increasing the transportation credit from Tulare County to Riverside, San Bernardino, and San Diego counties from \$0.81/cwt. to \$0.97/cwt.;

- Increasing the transportation credit from Fresno and Kings counties to Los Angeles, Orange, and Ventura counties from \$0.76/cwt. to \$0.89/cwt.;
- Increasing the transportation credit from Fresno and Kings counties to Riverside, San Bernardino, and San Diego counties from \$0.84/cwt. to \$0.97/cwt.;
- Not designating Humboldt and Del Norte counties as supply counties for shipments to deficit counties in Southern California.

Processors, mainly producer cooperatives, serving the fluid market will receive increased compensation of \$0.08/cwt. to \$0.16/cwt. As an example, for March 2008, this increased compensation would result in redistributing an approximate additional \$22,382/month of Class 1 revenues. (This estimated funding increase assumes that these rates had been in place during the month of March 2008).

## **DISCUSSION AND RECOMMENDATIONS FOR TRANSPORTATION CREDITS FOR NORTHERN CALIFORNIA**

### **Panel Recommendation**

- Designating the entire county of Stanislaus as a supply county for purposes of transportation credits;
- Increasing the credit from Sonoma County to Alameda, San Francisco, and Santa Clara counties from \$0.27/cwt. to \$0.45/cwt.;
- Increasing the credit from Merced and all of Stanislaus counties to Alameda, San Francisco, and Santa Clara counties from \$0.38/cwt. to \$0.75/cwt.;
- Increasing the credit from Merced and all of Stanislaus counties to Sacramento from \$0.20/cwt. to \$0.68/cwt.;
- Establishing a credit from Merced and all of Stanislaus counties to Solano and Sonoma counties at a rate of \$0.74/cwt.

Processors, mainly producer cooperatives, serving the fluid market will receive increased compensation of \$0.18/cwt. to \$0.48/cwt. As an example, for March 2008, this increased compensation would result in redistributing an approximate additional \$21,320/month of Class 1 revenues. (This estimated funding increase assumes that these rates had been in place during the month of March 2008).

## PROS AND CONS OF THE RECOMMENDATIONS

### AMENDMENTS TO THE POOLING PLAN

#### Incorporation of Dairy Accounting System

##### Pros

- The FTB is unable to provide support the current system
- DAS is designed and built using relational database, which is more widely used and efficient for data processing and calculations
- DAS is more straightforward in use, amendments to pricing and pooling would be easier to incorporate and program upkeep is relatively easy
- DAS was developed to mirror the current program, except for SNF and transportation allowance mileages calculations, which will result in a relatively seamless transition
- All witnesses either supported using the new DAS or were silent on this issue

##### Cons

- While the Department has tested the DAS against the current Pooling system, there is always the chance of an undetected error

#### SNF Implementation of Actual Solids-Not-Fat Values for Pool Reporting and Accounting

##### Pros

- Almost all milk handlers test incoming milk for fat and SNF and the new DAS enables full accounting and testing of SNF
- More accurate accounting of milk receipts and usage
- Two year trial of reporting actual SNF pounds was successful
- All witnesses either supported using actual SNF or were silent on this issue

##### Cons

- Differences between actual SNF testing versus skim equivalent calculations could occur so that some producers/processors might be better off or worse off
- Should the Pool Plan be amended to account for actual solids, handlers may need assistance with comprehending the calculations used for actual solids compared to average solids

#### Replacement of Public Utilities Mileage Table with PC Miler® Program for Distance Measurement in Transportation Allowances

##### Pros

- PUC table was once an appropriate option, but the regulation of the trucking industry significantly declined, and PUC ceased updating the tables in 1980
- Since 1980, additional people have moved into California, new roads have been built, and existing ones improved changing trucking routes
- Industry recommended replacing the PUC tables with PC Miler®
- Utilized by many trucking firms in California to establish mileage and rates
- Based on GPS, which coordinates can be readily determined

- Can be integrated into a relational database
- Improve accuracy and transparency of mileage computations
- Easier for producers and handlers to estimate their own mileages
- All witnesses either supported using PC Miler® or were silent on this issue

### **Cons**

- Hard to verify if trucks actually follow the routes
- Does not take into account high traffic areas in mileage calculations

## **TRANSPORTATION ALLOWANCES for NORTHERN and SOUTHERN CALIFORNIA**

### **Mileage Brackets**

#### **Pros**

- PC Miler® tends to give lower mileages than the old PUC tables
- Minimizes impact both to individual producers and to total Pool costs
- PC Miler® will not significantly change the current incentives and will not significantly change the current patterns of milk movement
- Sufficient milk is available from many sources that are closer than Humboldt/Del Norte Counties to serve the needs of the Southern California receiving area.
- Most witnesses supported changes to the brackets with the change to PC Miler® or were silent on the issue

#### **Cons**

- Some bracket changes will result in producers being in lower brackets than they were before, increasing total Pool revenues
- Some bracket changes will result in producers being in higher brackets than they were before, decreasing total Pool revenues

### **Allowance Rates**

#### **Pros**

- Significant increases in diesel fuel and other related transportation costs were supported by the March 2008 haul cost survey and were higher than the cost survey results used at the last hearing in July 2006
- Diesel prices increased significantly from March to June 2008
- Two witnesses documented their own hauling cost increases
- Most witnesses supported changes to the rates or were silent on the issue
- Declining milk production in Southern California has limited the milk available for the needs of the fluid market and transportation allowances are required to encourage milk production in more distant areas (outside Southern California) to be shipped into the area.
- Reimburse those producers who incur added hauling costs for supplying the Class 1 plants over what they would have incurred if they had supplied manufacturing plants.

#### **Cons**

- Rate increases will lower overbase prices in times of increasing cost of production

## **TRANSPORTATION CREDITS for NORTHERN and SOUTHERN CALIFORNIA**

### **Transportation Credit Areas**

#### **Pros**

- North Bay is the only active area receiving transportation allowances but no transportation credits
- Including all of Stanislaus County increases the number of plants that can supply the Class 1 market
- More condensed skim milk moving from plant-to-plant is more efficient to the entire system
- Sufficient milk is available from many sources that are closer than Humboldt/Del Norte Counties to serve the needs of the Southern California receiving area.

#### **Cons**

- Area increases will result in decreased Pool revenues

### **Credit Rates**

#### **Pros**

- Significant increases in diesel fuel and other related transportation costs were supported by the March 2008 haul cost survey and were higher than the cost survey results used at the last hearing in July 2006
- Diesel prices increased significantly from March to June 2008
- Shortfall helps insure closest milk first
- Balance competition among milk suppliers and users
- Declining milk production in Southern California has limited the milk available for the needs of the fluid market and transportation credits are required to encourage milk production in more distant areas (outside Southern California) to be shipped into the area.
- Most witnesses supported changes to the rates or were silent on the issue

#### **Cons**

- Rates increase will lower overbase prices in times of increasing cost of production

## ATTACHMENT A-3

### SUMMARY OF TESTIMONY AND POST-HEARING BRIEFS

#### CALIFORNIA DAIRIES, INC. – Gary Korsmeier

##### Testimony

- Transportation allowance principals
  - Part of orderly milk movement
  - Producers absorb costs
  - Rates cost justified
  - Rates equal cost of distant haul less cost of local haul
  - Encourage local milk, discourage distant milk
  - Encourage efficiency and minimize cost to the Pool
  - Base on existing milk movement patterns
- Proposal only addresses transportation allowances
- Requested rate increases due to increases in diesel fuel prices
  - Important to consider increases in diesel prices and hauling rates since the Department's March 2008 hauling survey
- Requested mileage bracket changes predicated on replacement of PUC tables by PC Miler®
  - Adopting PC Miler® and not changing mileage brackets will disadvantage milk in southern Kern County
- Requesting changes for the Bay Area, but main focus on Southern California
- Important that milk to Southern California comes from Kern County and southern Tulare County rather than further north
  - Adequate milk supply in Kern and southern Tulare
- Oppose Humboldt proposal because runs counter to principal of attracting closest milk first
- Support Institute proposal regarding transportation credits if
  - Cost justified
  - Rate increases are comparable to rate increases for comparable allowances

#### HUMBOLDT CREAMERY – Rich Ghilarducci and Len Mayer

##### Testimony

- For organic milk, Southern California is a deficit area, while Del Norte and Humboldt counties are the only surplus areas in California
- Requested a transportation credit for milk coming from Humboldt County to Southern California at a rate
  - Based on actual hauling costs, or
  - That is at least the same as the rate for milk coming from Fresno and King counties into Southern California
- Requested a transportation allowance for milk coming from Del Norte and Humboldt counties to Southern California at a rate based on actual hauling costs
  - The actual rate paid is less than the requested credit rate

##### Post-Hearing Brief

- As a percent of actual cost, their credit request is comparable to other hauling costs and credit rates
- Reiterated that at least the credit rate should be the same as the rate for milk coming from Fresno and King counties into Southern California

## **DAIRY INSTITUTE OF CALIFORNIA – William Schiek**

### **Testimony**

- Transportation allowance and credit principals
  - Producers absorb costs
  - Since Class 1, 2 and 3 differentials fund allowances and credits, the allowance and credit rates should not be so low as to encourage excessive over order premiums
  - Rates cost justified
  - For allowances, rates equal net cost of distant haul less cost of local haul, with a shortfall only for most distant milk (in this context, shortfall means the rate is less than the net cost)
  - For credits, rates equal cost of haul less any Class 1 differential, with a shortfall only for most distant milk
  - Encourage efficiency
  - Consider existing milk movement patterns that resulted from past Departmental decisions
  - Ensure an adequate supply to plants utilizing milk in higher uses
  - Incentivize producers to supply plants utilizing milk in higher uses
  - Ensure equity among competing plants in setting both allowances and credits and the combination of the two, this is especially important regarding a plant's local supply
  - The Department should be cognizant of potential future milk movement patterns as well as current patterns
- A review of allowance and credit rates is timely given recent structural changes
  - Declining milk production in Southern California
  - Increasing milk production in Kern County
  - Unprecedented increases in diesel fuel prices
- In setting rates for both allowance and credits, it is important to consider increases in diesel prices and hauling rates since the Department's March 2008 hauling survey
- Transportation credits for North Bay
  - Except for the North Bay Area, all plants eligible for allowances are also eligible for credits
  - North Bay plants are only eligible for allowances
  - North Bay plants are at a competitive disadvantage relative to plants in the Bay Area and in Sacramento
- Proposed rate increases for credits are important to ensure movement of condensed skim to Class 1 plants
- Support current system of call provisions
- Support CDI proposal
  - Appears cost justified
  - However, there needs to be competitive increases for all credit rates and for allowance rates in areas not addressed by CDI
- Support DFA proposal
  - Appears cost justified

- Given current volatile diesel fuel prices, their proposal from a previous hearing on indexing needs to be reviewed
- Oppose Humboldt proposal because runs counter to principal of attracting closest milk first
  - May be some justification for a credit rate equal to the rate for milk coming from Fresno and King counties into Southern California
- Support the Department proposal to adopt a new dairy accounting system
  - More flexible to accommodate a changing industry structure
- Support the Department proposal to replace the remaining skim equivalents by a strictly SNF based system
  - More accurate accounting of milk utilization
  - Possible need to insure each individual processor has a smooth transition to new system
- Support the Department proposal to replace the PUC tables with PC Miler®
  - More accurate accounting of distances
  - Possible need to adjust the current mileage brackets for transportation allowances to reflect the changes from PUC to PC Miler®

### **Post-Hearing Brief**

- All Grade-A milk should be treated the same
- Conventional utilization is an outlet for surplus organic milk

### **DAIRY FARMERS OF AMERICA – Gary Stueve**

#### **Testimony**

- Requested rate increases due to increases in diesel fuel prices
  - diesel prices up significantly since the last hearing on allowances and credits
- Requesting bigger increases for allowances into the Bay Area as prior increases have made this area less competitive with competing plants in other areas
- Adjustment to mileage brackets are needed with adoption of PC Miler®
- Oppose Humboldt proposal
  - Not the purpose of allowances and credits
- Institute proposal
  - No objection to credit rates
  - Support creation of credit going into North Bay
  - Support inclusion of all of Stanislaus County for credits into the three Northern California receiving areas
- Support Department proposed adoption of PC Miler®

#### **Post-Hearing Brief**

- For the 0 to 99 mileage bracket going into the Bay Area, most of the milk is moving over 50 miles, hence the relative high allowance rate requested
- For the mileage brackets going into Southern California, DFA is comfortable with the brackets proposed either by DFA or by CDI
- Reaffirm opposition to rate increases for the 0 to 44 mileage bracket going into the North Bay area

### **MILK PRODUCERS COUNCIL – Robert VandenHeuvel**

#### **Testimony**

- Increased hauling costs are also affecting dairy farmers especially for incoming feed and for the outgoing milk
- Would like a “transportation surcharge” to be added to the Class 1 price to cover cost of future increases in transportation subsidies
  - This would pass the cost of the transportation subsidies onto the consumers where it belongs
- No position on specifics of any increase in transportation subsidies
  - But ask that the Department also consider the increasing cost of production
- Oppose Humboldt proposal
  - Not the purpose of transportation subsidies

## **SUPER STORE INDUSTRIES – Dennis Brimhall**

### **Testimony**

- As a member, supports the Institute proposal
  - The broader perspective makes their proposal more equitable than other, narrower proposals
  - North Bay is the only area eligible for allowances but not for credits
  - The current split of Stanislaus County is a form of gerrymandering
  - Their credit proposal will encourage efficient movement of condensed skim to Class 1 plants

## **ALLIANCE OF WESTERN MILK PRODUCERS – William Van Dam**

### **Testimony**

- Support the proposals made by the Department
  - Adoption of a new dairy accounting system
  - Replacement of remaining skim equivalents by a strictly SNF based system
  - Replacement of the PUC tables with PC Miler®, but possibly need to adjust the current mileage brackets for transportation allowances to reflect the changes from PUC to PC Miler®

## **CLOVER STORNETTA FARMS, INC. – Mkulima G. Britt**

### **Testimony**

- Allowances and credits needed to encourage closest milk to Class 1 plants
- If allowance and credit rates are too low, excessive over-order premiums will be charged, this results in higher retail prices and decreased sales
- Institute proposal
  - General support for all rate increases
  - Specific support for allowance rate increase for North Bay
  - Specific support for making North Bay eligible for credits
- Requested rate increases result from increased hauling cost
  - Mainly a result of increases in diesel fuel prices
- In setting rates for both allowances and credits, it is important to consider increases in diesel prices and hauling rates since the Department March 2008 haul survey
- Changes in allowances will maintain equity with competitors
- Clover has always needed to buy condensed skim, but now Clover must go farther for it; this puts Clover in an inequitable position compared to competitors who do get credits

## **WESTERN UNITED DAIRYMEN – Michael Marsh**

### **Testimony**

- Transportation allowance principals
  - Rates should equal cost of distant haul less cost of local haul, with a shortfall
  - The closest milk should be utilized first
  - Costs should be minimized
  - With introduction of Pooling, producers made a commitment to supply milk to Class 1 plants
- WUD supports allowances because
  - It redistributes money among the producers within the Pool
  - Protects the Class 1 revenues that are shared by all producers
  - It rewards producers serving the Class 1 market
  - Without allowances,
    - o Overorder premiums will decrease Class 1 sales
    - o Processors may opt to buy out-of-state milk
    - o Processors may opt to relocate out-of-state
- It will be an ongoing challenge to minimize costs as more producers leave Southern California
- Support CDI proposal
  - Assuming it is cost justified
- Does not support the other proposals
- Cannot support any changes to credit system
- Support proposal made by the Department which will improve accuracy and efficiency
  - Adoption of a new dairy accounting system
  - Replacement of remaining skim equivalents by a strictly SNF based system
  - Replacement of the PUC tables with PC Miler®

## **CALIFORNIA DAIRY CAMPAIGN – Kevin Abernathy**

### **Testimony**

- Support MPC proposal for a “transportation surcharge” to be added to the Class 1 price to cover cost of future increases in transportation subsidies
- Oppose all other proposals
- Increased hauling costs are also effecting dairy farmers especially for incoming feed and for the outgoing milk
- Transportation subsidies eliminate any incentives for efficient milk transport