

**Clarifications and Additional Information
as requested at the May 18, 2006 Prehearing Workshop**

On May 18, 2006, the Department held a prehearing workshop for the June 1 hearing on Class 2, 3, 4a and 4b pricing formulas. The Department received requests for clarification and additional information regarding some of the documents presented. This is the Department's response to those requests.

The enclosed *Tables 2a* and *2b* expands the information given in *Table 2* as presented at the workshop. *Table 2* presented only five-year averages for 2001 through 2005; *Table 2a* (for Class 4a) and *Table 2b* (for Class 4b) present both annual and five-year averages for 2001 through 2005.

At the workshop, information was presented on costs associated with the making of butter, NFDM, Cheddar cheese and SWP. The costs were presented in a number of categories, including "processing nonlabor". *Table 7* gives additional information on the energy components of "processing nonlabor".

At the workshop, a question arose about the moisture test of the block Cheddar cheese; specifically that the value of 39.26% for 2004 exceeded the maximum moisture value for Cheddar. Further checking showed that both the moisture and yield values had been misentered. *Table 8* gives the corrected information in blue. Following *Table 8* is a revision of the "Cheddar cheese processing costs for the period of January through December 2004, amended January 2006" with the corrected moisture and yield information shown in blue.

Table 2a - Supplement to Table 2
For Class 4a, Estimates of Impact of Proposals (Proposed less Current Class and Pool Prices)
 By factors in the formulas

Using historic commodity prices, estimates assume that the current and alternative formulas
 had been in effect from January 2001 through December 2005

Excludes Institute proposals as their impacts are uniform over the entire five years

Annual and Five-Year Averages: 2001-2005

(Dollars per Hundredweight)

	MCA	f.o.b. Adjusters	Other	Total w/o Variable	Variable Component	Total with Variable
WUD						
2001		\$0.06		\$0.06		\$0.06
2002		\$0.06	\$0.00	\$0.06		\$0.06
2003		\$0.06	\$0.00	\$0.06		\$0.06
2004		\$0.06		\$0.06		\$0.06
2005		\$0.06		\$0.06		\$0.06
5-Year Average		\$0.06	\$0.00	\$0.06		\$0.06
CDC						
2001	\$0.07	\$0.12		\$0.19	-\$0.44	-\$0.24
2002	\$0.07	\$0.12	\$0.00	\$0.19	\$0.07	\$0.27
2003	\$0.07	\$0.12	\$0.00	\$0.19	\$0.18	\$0.38
2004	\$0.07	\$0.12		\$0.19	-\$0.21	-\$0.01
2005	\$0.07	\$0.12		\$0.19	-\$0.18	\$0.01
5-Year Average	\$0.07	\$0.12	\$0.00	\$0.19	-\$0.11 2/	\$0.08
CDI						
2001	-\$0.13	\$0.01		-\$0.13		-\$0.13
2002	-\$0.13	\$0.01	\$0.00	-\$0.13		-\$0.13
2003	-\$0.13	\$0.01	\$0.00	-\$0.13		-\$0.13
2004	-\$0.13	\$0.01		-\$0.13		-\$0.13
2005	-\$0.13	\$0.01		-\$0.13		-\$0.13
5-Year Average	-\$0.13	\$0.01	\$0.00	-\$0.13		-\$0.13
ALLIANCE						
2001	-\$0.13	\$0.01		-\$0.13		
2002	-\$0.13	\$0.01	\$0.00	-\$0.13		
2003	-\$0.13	\$0.01	\$0.00	-\$0.13		
2004	-\$0.13	\$0.01		-\$0.13		
2005	-\$0.13	\$0.01		-\$0.13		
5-Year Average	-\$0.13	\$0.01	\$0.00	-\$0.13		3/

1/ Elimination of whey factor.

2/ Base manufacturing cost allowances vary with ratio of CRP/PCC.

3/ Base manufacturing cost allowances vary with natural gas factor which was unavailable for analysis.

4/ Base cheese manufacturing cost allowance varies with cheese price.

5/ Base whey manufacturing cost allowance varies with whey price.

Table 2b - Supplement to Table 2
For Class 4b, Estimates of Impact of Proposals (Proposed less Current Class and Pool Prices)
By factors in the formulas
Using historic commodity prices, estimates assume that the current and alternative formulas
had been in effect from January 2001 through December 2005
Annual and Five-Year Averages: 2001-2005
(Dollars per Hundredweight)

	MCA	f.o.b. Adjusters	Other	Total w/o Variable	Variable Component	Total with Variable
INSTITUTE						
2001	-\$0.51	\$0.04	-\$0.16	-\$0.63	\$0.09	-\$0.53
2002	-\$0.51	\$0.04	-\$0.14	-\$0.61	\$0.48	-\$0.13
2003	-\$0.51	\$0.04	-\$0.16	-\$0.63	\$0.62	-\$0.01
2004	-\$0.51	\$0.04	-\$0.19	-\$0.66	\$0.31	-\$0.35
2005	-\$0.51	\$0.04	-\$0.18	-\$0.64	-\$0.13	-\$0.78
5-Year Average	-\$0.51	\$0.04	-\$0.16	-\$0.63	\$0.27 1/	-\$0.36
WUD						
2001		\$0.06	\$0.02	\$0.08		\$0.08
2002		\$0.06	\$0.09	\$0.15		\$0.15
2003		\$0.06	\$0.07	\$0.13		\$0.13
2004		\$0.06	\$0.00	\$0.06		\$0.06
2005		\$0.06	\$0.00	\$0.06		\$0.06
5-Year Average		\$0.06	\$0.04	\$0.10		\$0.10
CDC						
2001	\$0.03	\$0.29	\$0.02	\$0.34	-\$0.22	\$0.12
2002	\$0.03	\$0.29	\$0.20	\$0.52	\$0.13	\$0.64
2003	\$0.03	\$0.29	\$0.27	\$0.59	-\$0.01	\$0.58
2004	\$0.03	\$0.29	\$0.05	\$0.37	-\$0.40	-\$0.04
2005	\$0.03	\$0.29	\$0.00	\$0.32	-\$0.25	\$0.06
5-Year Average	\$0.03	\$0.29	\$0.11	\$0.43	-\$0.15 2/	\$0.27
ALLIANCE						
2001	-\$0.18	\$0.12	\$0.02	-\$0.05		
2002	-\$0.18	\$0.12	\$0.23	\$0.17		
2003	-\$0.18	\$0.12	\$0.33	\$0.26		
2004	-\$0.18	\$0.12	\$0.06	-\$0.01		
2005	-\$0.18	\$0.12		-\$0.07		
5-Year Average	-\$0.18	\$0.12	\$0.13	\$0.06	3/	
MPC						
2001		\$0.17	\$0.41	\$0.58	-\$0.08	\$0.51
2002		\$0.17	\$0.48	\$0.65	-\$0.02	\$0.63
2003		\$0.17	\$0.54	\$0.71	-\$0.05	\$0.66
2004		\$0.17	\$0.36	\$0.54	-\$0.13	\$0.41
2005		\$0.17	\$0.32	\$0.49	-\$0.09	\$0.40
5-Year Average		\$0.17	\$0.42	\$0.59	-\$0.07 4/	\$0.52
LOL						
2001	-\$0.43			-\$0.43	\$0.05	-\$0.38
2002	-\$0.43			-\$0.43	\$0.24	-\$0.18
2003	-\$0.43			-\$0.43	\$0.31	-\$0.12
2004	-\$0.43			-\$0.43	\$0.15	-\$0.27
2005	-\$0.43			-\$0.43	-\$0.07	-\$0.49
5-Year Average	-\$0.43			-\$0.43	\$0.14 5/	-\$0.29

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4/ Base cheese manufacturing cost allowance varies with cheese price.

5/ Base whey manufacturing cost allowance varies with whey price.

**Table 7 - Estimated Analysis of the
Processing Cost of a Pound of Product
Associated with the Cost of Natural Gas**

Estimate A

- The 2004 manufacturing cost study served as the model for preparing the estimated costs.
- All other variables/factors in the 2004 cost study were held constant.

Study Period	Average Natural Gas Prices Time Period Used	Natural Gas Costs, For Each Commodity In Dollars Per Pound			
		Butter	NFDM	Cheddar Cheese	SWP
January-December 2004	Jan. to Dec. 2004	\$0.0018	\$0.0244	\$0.0068	\$0.0232

Estimate B

- The 2004 manufacturing cost study served as the model for preparing the estimated costs.
- The labor and utility rates that were incorporated in the 2004 cost study were replaced by the nine-month average (January-September 2005) labor and utility rates, including natural gas rates.

Study Period	Average Natural Gas Prices Time Period Used	Natural Gas Costs, For Each Commodity In Dollars Per Pound			
		Butter	NFDM	Cheddar Cheese	SWP
January-December 2004 Utility & Labor Rates for January-September 2005	Jan. to Sep. 2005	\$0.0020	\$0.0277	\$0.0076	\$0.0286

Estimate C

- The 2004 manufacturing cost study served as the model for preparing the estimated costs.
- The labor and utility rates that were incorporated in the 2004 cost study were replaced by September 2005 labor and utility rates, including natural gas rates.

Study Period	Average Natural Gas Prices Time Period Used	Natural Gas Costs, For Each Commodity In Dollars Per Pound			
		Butter	NFDM	Cheddar Cheese	SWP
January-December 2004 Utility & Labor Rates for September 2005	September 2005	\$0.0025	\$0.0330	\$0.0095	\$0.0415

*Table 8 - California Yield and Vat Information
Separately for Block and Barrel Cheddar Cheese Plants
January-December 2003; January-December 2004
Revised May 23, 2006 (Revisions in Blue)*

	Finished Moisture	Vat Fat	Vat SNF	Yield * (lbs./cwt.)
January-December 2003				
Six Block Plants	37.98%	3.88%	8.85%	10.90
Three Barrel Style Plants	35.45%	4.06%	9.16%	10.97
All Nine Plants	37.12%	3.94%	8.95%	10.92
January-December 2004				
Four Block Plants	38.09%	3.94%	8.95%	11.55
Three Barrel Style Plants	34.76%	4.17%	9.28%	11.49
All Seven Plants	37.04%	4.02%	9.05%	11.53

**Increases in the yield percentages compared to previous years, mostly reflect fortification.*

Cheese Processing Costs

Amended January 2006

May 2006 Amendments in Blue

1. Manufacturing cost data were collected and summarized from seven California cheese plants. The seven plants processed 817 million pounds of cheese during the study period, representing 98.5% of the Cheddar and Monterey Jack cheese processed in California.
2. The processing costs summarized in this study were incurred during a 12-month period, starting in January 2004 and concluding in December 2004.
3. The "Processing Non-Labor" category includes costs such as utilities, repairs and maintenance, supplies, depreciation and rent.
4. The volume total includes both Cheddar and Monterey Jack cheeses, but the costs reflect only costs for 40 lb. blocks of Cheddar.
5. Three plants processed 500-lb. barrels or 640-lb. blocks. Packaging costs and packaging labor for 40 lb. blocks were substituted for these plants.
6. To obtain the weighted average, individual plant costs were weighted by their cheese processing volume relative to the total volume of cheese processed by all plants involved in the cost study.
7. The current manufacturing cost allowance for cheese is \$0.171 per pound. About 62% of the cheese was processed at a cost less than the manufacturing cost allowance.
8. **The weighted average yield was 11.53 lbs. of cheese per hundredweight of milk. The weighted average moisture was 37.04%, and weighted average vat tests were 4.02% fat and 9.05% SNF.**

<u>Cost Groups</u>	<u>Number of Plants</u>	<u>Processing Labor</u>	<u>Processing Non-Labor</u>	<u>Package</u>	<u>Other Ingredient</u>	<u>General & Administrative</u>	<u>Return on Investment</u>	<u>Total Cost</u>	<u>Volume in Group</u>	<u>Percent in Group</u>
<i>dollars per pound of cheese</i>										
Low Cost	3	\$0.0397	\$0.0759	\$0.0180	\$0.0089	\$0.0191	\$0.0094	\$0.1710	628,560,303	76.9%
High Cost	4	\$0.0709	\$0.0584	\$0.0206	\$0.0179	\$0.0243	\$0.0042	\$0.1963	188,508,025	23.1%
<u>Summary Statistics</u>										
<u>Weighted Average</u>		\$0.0469	\$0.0719	\$0.0186	\$0.0110	\$0.0203	\$0.0082	\$0.1769		
Range	Minimum	\$0.0340	\$0.0518	\$0.0146	\$0.0066	\$0.0077	\$0.0024			
	Maximum	\$0.0852	\$0.0795	\$0.0281	\$0.0289	\$0.0299	\$0.0128			
Total									817,068,328	100%