

Mr. Hearing Officer and Members of the Panel,
My name is Geoffrey Vanden Heuvel and I am testifying today on behalf of Milk Producers Council.

I respectfully request that my testimony on behalf of Milk Producers Council, which I read into the record in Sacramento on May 3, 2005, be included in the record of today's hearing as if it had been read.

The Dairy Institute (DI) makes a number of points in their testimony of the May 3 hearing, which we would like to comment on.

DI makes the claim that the class 1 price relationship with manufacturing prices is not economically sound or reasonable because of three reasons: reductions in class 1 utilization, low California production costs in relation to other areas and excess price enhancement on top of the traditional cost-based justifications for class 1 price differentials.

There are a couple of flaws in DI's argument: First, The utilization's DI uses in their Table 1 do not take into consideration the de-pooling of class III milk in some federal orders which has occurred quite often in the last several years. This fact inflates the class 1 utilization percentages for those orders. Secondly, and more importantly, DI's argument ignores the substantial class 1 premiums that exist in the rest of the country, even in some of the lower class 1 utilization federal orders. For example, the class 1 premium in Chicago and Milwaukee is \$2.27 per cwt. Low class 1 utilization means there are other competing uses for the milk. Class 1 prices need to be sufficiently high to attract an adequate supply to class 1 uses. Historically, class 1 premiums in California have been very modest in comparison to class 1 premiums in the rest of the country. The basic philosophy of the California regulatory system has been to not rely on a premium structure outside the pool to get milk to move to class 1. In fact, producers have supported a transportation subsidy system precisely for the purpose of facilitating the service of the class 1 market without the use of large premiums.

The cost of production has been removed as a specific factor in the setting of class 1 prices in California. One of the reasons a change was made was to create a constant relationship between the various classes of milk. There are times when this has worked both for and against producer interest. But the decision was made to establish milk prices in California based on the market values of manufactured dairy products. DI Table 2 uses a very misleading class 1 differential for California of \$2.36 per cwt. CDFA does a much more credible comparison in Table 5 of the Hearing Background paper, which shows an average California class 1 differential of \$1.57 per cwt. If the more accurate \$1.57 were used in DI's Table 2 then of course their point completely falls apart.

Geoffrey Vanden Heuvel Testimony on behalf of Milk Producers Council
May 6, 2005 Class 1 Hearing

DI's claim that there is too much price enhancement in the class 1 price ignores the fact that one of the main purposes of the entire classified pricing system is to make sure that there is an adequate incentive to serve the class 1 market. Simply covering the increased costs DI has identified, namely the added cost of maintaining grade A status and the compensation of the apparent extra freight costs, is insufficient to provide an incentive to serve the class 1 market. Price enhancement for class 1 is an absolute necessity if the classified pricing system is to be successful in making sure that the class 1 market is adequately supplied.

DI's charge that milk prices to consumers are not fair and reasonable would be funny if it were not so serious. By consumer prices DI must be talking about retail milk prices. Section 61802 (h) specifically talks about retail milk prices and the fact that many factors that are not in the department's control influence the retail prices and that minimum producer prices "... should not be unreasonably depressed because other factors have affected the levels of retail milk prices paid by consumers." Just looking at Table 18 of the monthly Dairy Information Bulletin reveals the truth of Section 61802 (h). In December of 2004, according to the AC Nielson survey the cheapest gallon of whole milk in the nation was in Phoenix, Arizona, and sold for an average price of \$2.30. The December 2004 Phoenix class 1 price was \$16.78 per cwt. On the other hand, the price for a gallon of whole milk in Los Angeles in December of 2004 was \$2.80. \$0.50 per gallon higher. The class 1 price in Los Angeles for December 2004 was \$16.38, \$0.40 per cwt. less than the Phoenix class 1 price. Producers can not be held responsible for the extra \$0.50 per gallon cost of "consumer" milk in Los Angeles. If anyone is to blame for "heavily taxing" families with children who consume a lot of milk, it is the Dairy Institute's members who are clearing taking more margin on the sale of milk than their counterparts in Phoenix.

DI makes the point that Section 62062.1 does not mean that the California class 1 price needs to be "equal" to the class 1 price in contiguous states. We agree. But neither does it mean that California class 1 prices can be significantly lower than the class 1 price in contiguous states. The Dairy Institute proposal is radical and if adopted would require a new definition of reasonable in the dictionary.

DI drags up their most long standing and tired complaint about the alleged California P-D advantage. It is important to remember that P-D's existed from the beginning of milk pooling in California. Their presence in the marketplace has been a reality for many decades. They are not very large group and their P-D milk supply is not growing. As urbanization takes place in Southern California and the P-D's are forced to relocate their herds further away from their bottling plants, the P-D advantage is significantly diminished, because P-D milk is not eligible for the transportation subsidies that other handlers enjoy.

Geoffrey Vanden Heuvel Testimony on behalf of Milk Producers Council
May 6, 2005 Class 1 Hearing

DI quotes the Statement of Determinations from the February 1997 hearing to back up their point, that class 1 prices should be dramatically reduced to eliminate incentives for economic waste. It is important to note that the department did, as a result of that hearing, significantly reduce the California class 1 price to a level that is now lower than the class 1 price in the states contiguous to California. The reduction sought in that hearing already happened.

Finally, DI criticizes the use of transportation models to determine class 1 price levels. It is true that models are indicators of relative value across space and not determiners of absolute value. However, Federal Order reform did establish absolute values that can not be ignored. Federal Order rules enforce the efficacy of those values in enforcing compensatory payments for out of order milk shipped into federal order areas. And California law requires the department to monitor the prices in the states contiguous to California to see to it that California class 1 prices are in a reasonable relation with them. The Dairy Institute may wish the law did not exist, but it does. We urge the department to either make no change to the existing class 1 formulas or adopt either the Alliance or the CDC proposal.

We respectfully request that these comments be also incorporated into the hearing record of the May 3, 2005 hearing. We also request the opportunity to provide a post-hearing brief.

Table 18: U.S. Retail Average Prices for Whole, Reduced Fat, Lowfat, and Skim Milk
(Weighted Average Prices in Dollars Per Gallon)

City	December 2004				January 2005				February 2005			
	Whole	Reduced Fat	Lowfat	Skim	Whole	Reduced Fat	Lowfat	Skim	Whole	Reduced Fat	Lowfat	Skim
<i>Weighted Average Prices in Dollars Per Gallon</i>												
Albany	3.04	2.97	2.99	2.91	3.20	3.15	3.17	3.11	2.89	2.82	2.84	2.76
Atlanta	3.12	2.98	2.85	2.96	3.29	3.22	3.11	3.21	3.40	3.36	3.23	3.29
Baltimore	3.22	3.19	3.06	2.99	3.31	3.26	3.16	3.09	3.26	3.19	3.07	3.05
Birmingham	3.34	3.24	3.25	3.24	3.41	3.31	3.25	3.26	3.45	3.36	3.38	3.38
Boston	3.04	3.01	3.06	3.08	3.12	3.07	3.13	3.16	2.98	2.96	3.02	3.01
Buffalo/Rochester	2.90	2.40	2.27	2.20	2.84	2.39	2.26	2.20	2.80	2.31	2.13	2.03
Charlotte	3.58	3.60	3.71	3.67	3.67	3.68	3.78	3.71	3.59	3.63	3.75	3.68
Chicago	2.70	2.55	2.56	2.66	2.88	2.76	2.75	2.70	2.78	2.67	2.76	2.67
Cincinnati	2.48	2.33	2.25	2.23	2.58	2.40	2.29	2.27	2.34	2.26	2.27	2.22
Cleveland	2.76	2.59	2.58	2.55	3.05	2.82	2.75	2.72	2.81	2.58	2.55	2.55
Columbus	2.49	2.47	2.49	2.51	2.33	2.33	2.23	2.24	2.51	2.45	2.42	2.43
Dallas	2.99	2.98	2.97	2.94	2.96	2.96	2.96	2.97	2.78	2.77	2.76	2.76
Denver	3.35	3.21	3.01	2.92	3.42	3.27	3.10	2.99	3.14	3.01	2.88	2.76
Des Moines	3.01	2.75	2.55	2.36	3.13	2.86	2.65	2.45	3.12	2.84	2.62	2.46
Detroit	2.75	2.66	2.66	2.70	2.57	2.50	2.31	2.49	2.74	2.71	2.65	2.72
Grand Rapids	2.52	2.43	2.44	2.44	2.48	2.32	2.12	2.28	2.55	2.41	2.41	2.38
Hartford-New Haven	3.72	3.69	3.72	3.73	3.82	3.83	3.77	3.87	3.70	3.74	3.68	3.71
Houston	3.34	3.20	2.97	2.84	3.24	3.15	2.98	2.81	3.30	3.20	3.04	2.86
Indianapolis	2.55	2.43	2.37	2.38	2.77	2.61	2.54	2.56	2.52	2.45	2.40	2.40
Jacksonville	3.37	3.36	3.34	3.34	3.39	3.32	3.25	3.25	3.45	3.44	3.42	3.43
Kansas City	3.22	2.98	2.88	2.67	3.34	3.10	2.99	2.81	3.34	3.10	3.00	2.81
Las Vegas	2.68	2.44	2.32	2.25	2.85	2.57	2.47	2.35	2.80	2.57	2.47	2.41
Little Rock	3.10	3.01	2.95	2.91	3.06	2.95	2.87	2.85	2.92	2.80	2.69	2.69
Los Angeles	2.83	2.60	2.68	2.27	3.01	2.78	2.84	2.37	2.88	2.63	2.68	2.27
Louisville	2.80	2.67	2.45	2.47	2.92	2.78	2.50	2.50	2.88	2.74	2.51	2.51
Memphis	3.10	2.85	2.57	2.62	3.21	2.98	2.65	2.72	3.13	2.93	2.66	2.72
Miami	3.40	3.42	3.31	3.35	3.53	3.55	3.44	3.47	3.50	3.56	3.44	3.48
Milwaukee	3.27	2.97	2.85	2.75	3.30	3.01	2.91	2.79	3.42	3.09	2.95	2.84
Minneapolis	3.46	3.54	3.49	3.48	3.55	3.60	3.56	3.54	3.56	3.66	3.60	3.56
Nashville	3.26	3.02	2.85	2.91	3.51	3.28	3.13	3.14	3.43	3.21	3.05	3.09
New Orleans-Mobile	3.55	3.51	3.54	3.46	3.60	3.55	3.57	3.48	3.65	3.60	3.62	3.54
New York	3.43	3.23	3.36	3.32	3.62	3.50	3.50	3.48	3.45	3.37	3.38	3.35
Oklahoma City-Tulsa	3.05	2.95	2.83	2.78	3.13	3.07	2.96	2.87	3.12	3.03	2.93	2.89
Omaha	3.04	2.76	2.58	2.39	3.11	2.83	2.64	2.47	3.00	2.79	2.60	2.45
Orlando	3.32	3.32	3.32	3.32	3.32	3.28	3.21	3.20	3.42	3.41	3.40	3.40
Philadelphia	3.28	3.08	2.95	2.84	3.43	3.20	3.06	2.95	3.34	3.15	3.04	2.91
Phoenix	2.30	2.12	2.12	2.08	2.52	2.56	2.53	2.48	2.51	2.20	2.24	2.25
Pittsburgh	3.07	2.89	2.81	2.73	3.16	2.98	2.87	2.77	3.05	2.90	2.83	2.77
Portland	2.78	2.43	2.44	2.38	2.70	2.37	2.40	2.33	2.78	2.40	2.41	2.39
Raleigh-Durham	3.61	3.61	3.66	3.65	3.79	3.79	3.82	3.80	3.78	3.77	3.78	3.70
Richmond-Norfolk	3.53	3.49	3.35	3.27	3.72	3.65	3.46	3.39	3.67	3.59	3.41	3.33
Sacramento	3.00	2.88	3.06	2.31	3.23	3.06	3.21	2.46	3.02	2.85	3.00	2.36
Salt Lake City-Boise	2.34	2.27	2.07	2.13	2.58	2.54	2.32	2.40	2.78	2.51	2.35	2.39
San Antonio	3.38	3.25	2.98	2.87	3.48	3.36	3.08	2.98	3.46	3.32	3.08	2.97
San Diego	2.77	2.53	2.67	2.32	2.94	2.70	2.83	2.42	2.83	2.58	2.70	2.36
San Francisco	3.00	2.78	3.36	2.34	3.26	3.01	3.58	2.52	3.05	2.82	3.37	2.43
Seattle	3.11	2.77	2.74	2.71	3.33	2.87	2.87	2.85	2.94	2.63	2.61	2.55
St Louis	3.00	2.81	2.65	2.59	3.18	2.98	2.79	2.69	3.15	2.85	2.74	2.61
Syracuse	2.88	2.53	2.52	2.51	2.98	2.63	2.58	2.56	2.82	2.49	2.42	2.39
Tampa	3.31	3.31	3.31	3.31	3.43	3.42	3.42	3.42	3.40	3.38	3.38	3.40
Washington DC	3.27	3.13	3.04	2.99	3.33	3.21	3.13	3.11	3.19	3.11	3.01	3.01
West Texas	3.03	2.95	2.83	2.81	2.93	2.89	2.79	2.77	3.11	2.94	2.86	2.78
Total US	3.07	2.93	2.88	2.80	3.16	3.02	2.95	2.87	3.11	2.96	2.91	2.83

Source: AC Nielsen Scantrack Reports on Refrigerated Milk. The average price per gallon represents the weighted averages for specific brands of milk within the specified market. Data includes organic milk. Data subject to revision. February data through the week ending 2/19/05.

ANNOUNCED COOPERATIVE CLASS I PRICES FOR SELECTED CITIES IN FEDERAL MILK ORDERS, MAY 2005, WITH COMPARISONS ^{1/}

For May 2005, the all-city average announced cooperative Class I price was \$18.80 per cwt., \$1.47 higher than the Federal milk order Class I price average for these cities. The May cooperative Class I price was \$.60 higher than the April price, while the Federal order price was \$.67 higher. On an individual city basis, the difference between the Federal order and announced cooperative Class I price ranged from \$.15 in Phoenix, AZ, to \$2.68 in Miami, FL. For May 2004, the all-city average announced cooperative Class I price was \$23.68, \$1.50 higher than the Federal order Class I price average for these cities.

City	May 2005		
	Announced Cooperative Class I Price	Federal Milk Order Class I Price	Difference
	Dollars per hundredweight, 3.5% butterfat		
Atlanta, GA	19.51	17.90	1.61
Baltimore, MD	19.60	17.80	1.80
Boston, MA	19.75	18.05	1.70
Charlotte, NC	19.51	17.90	1.61
Chicago, IL	18.87	16.60	2.27
Cincinnati, OH	18.71	17.00	1.71
Cleveland, OH	18.51	16.80	1.71
Dallas, TX	18.30	17.80	0.50
Denver, CO	18.20	17.35	0.85
Des Moines, IA	18.34	16.60	1.74
Detroit, MI	18.26	16.60	1.66
Hartford, CT	19.65	17.95	1.70
Houston, TX	18.90	18.40	0.50
Indianapolis, IN	18.51	16.80	1.71
Kansas City, MO	18.03	16.80	1.23
Louisville, KY	18.61	17.00	1.61
Memphis, TN	19.01	17.60	1.41
Miami, FL	21.78	19.10	2.68
Milwaukee, WI	18.82	16.55	2.27
Minneapolis, MN	18.52	16.50	2.02
New Orleans, LA	19.81	18.40	1.41
Oklahoma City, OK	17.95	17.40	0.55
Omaha, NE	18.09	16.65	1.44
Philadelphia, PA	19.89	17.85	2.04
Phoenix, AZ	17.30	17.15	0.15
Pittsburgh, PA	18.83	16.90	1.93
St. Louis, MO	18.35	16.80	1.55
Seattle, WA	17.12	16.70	0.42
Springfield, MO	17.55	17.00	0.55
Washington, DC	19.60	17.80	1.80
Simple Average	18.80	17.33	1.47

^{1/} This table contains information obtained from the Class I price announcements sent by the major cooperative in each city market to all handlers who buy milk from them. These over-order prices include charges for various services performed by the cooperative. In some instances, these over-order prices may not include all credits that may be allowed. These prices have not been verified as having been actually paid by handlers.