— HEARING PANEL REPORT —

ADDRESSING MILK MOVEMENT ISSUES CONTAINED IN THE
MILK POOLING PLAN FOR MARKET MILK
BASED UPON PUBLIC HEARINGS HELD ON JUNE 28 AND JULY 2, 2001

This Report of the Hearing Panel regarding proposed amendments to the Milk Pooling Plan for Market Milk is based on evidence received into the Department of Food and Agriculture's hearing folder. The folder includes the Departmental exhibits, written statements and comments received from interested parties, written and oral testimony received at two public hearings held June 28, 2001 and July 2, 2001 and written post–hearing briefs.

The analyses, discussions and recommendations contained in this report are limited to the proposed amendments to the Milk Pooling Plan. For analyses, discussions and recommendations pertaining to proposed amendments to the Stabilization and Marketing Plans for Northern and Southern California, please refer to the associated Panel report.

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INTRODUCTION

The Department held public hearings on Thursday, June 28, 2001 in Ontario and on Monday July 2, 2001 in Sacramento. The hearings considered amendments to milk movement incentives, namely, transportation allowances, transportation credits and call provisions, as provided in the Milk Stabilization and Marketing Plans for Market Milk and the Pooling Plan for Market Milk (Plans). The Department called the hearings after receiving a petition from the Imperial County's Agricultural Commissioner Office (IC). Subsequent to the receipt of that petition, alternative proposals were received by California Dairies, Inc. (CDI), Land O'Lakes (LOL), Milk Producers Council (MPC) and Producers Dairy Foods, Inc. (PDF).

Hearing Witnesses:

A total of sixteen witnesses testified including the Department's witness.

1. Candace Gates — CDFA
2. Stephen Birdsall — Imperial County Agricultural Commissioners Office
3. Gary Korsmeier — California Dairies, Inc.
4. Jay Goold — Western United Dairymen
5. Tiffany LaMendola — Western United Dairymen
6. Edward McGrew — Dairy Attraction Committee for Imperial County
7. William Schiek — Dairy Institute of California
8. James Dolan — Driftwood Dairy
9. Kevin McLaughlin — Security Milk Producers
10. Richard Shehadey — Producers Dairy Foods, Inc.
11. Geoffrey Vanden Heuvel — Milk Producers Council
12. James Gruebele — Land O' Lakes
13. Richard Sturgeon — Suiza Foods, Inc.
14. Charles English — Suiza Foods, Inc.
15. Robert Ham — representing Assemblyman David Kelly
16. Sharon Hale — Crystal Cream and Butter

In addition, written submissions were received from six people who did not give oral testimony:

17. David L. Parrish — Dairy Farmers of America
18. Clifford Caldwell — El Centro Chamber of Commerce
19. Duncan Hunter — U.S. House of Representatives
20. Lauren S. Grizzle — Imperial Valley Vegetable Growers Association and Imperial County Farm Bureau
21. Donald P. Glud — Valley Independent Bank
22. Gary Stueve — Dean Foods Company

Discussion and Analysis of Proposed Amendments

Background

During 2000, the Department held a series of four industry workshops that attempted to review fully all aspects of milk movement incentives. A primary objective of the workshops was to try to reach a consensus on potential changes to the structure and scope of the milk movement incentive program. The workshops concluded without industry consensus; rather, the participants urged the Department to consider reviewing the unresolved issues in a public hearing format.

The last hearing to make any changes to the transportation allowance system was held July 19, 1994 with the amendments effective September 1, 1994. The last hearing to make any changes to the transportation credit system and the call provisions was held October 9, 1996 with the amendments effective December 1, 1996.

Transportation Allowances

What they are and how they work — When the Milk Pooling Plan was instituted in 1969, location differentials were established to provide producers with economic signals to move milk to designated counties. Location differentials were added to or deducted from quota payments to producers and were determined by the location of the plant that first received the milk. When milk was moved to designated counties, favorable location differentials offset the added cost of transporting milk.

As California milk production began to increase, overbase milk became increasingly larger share of the total milk production. As a result, location differentials based solely on quota milk were no longer an efficient means of ensuring that adequate milk supplies would be made available to Class 1 plants. Consequently, location differentials were discontinued and a system of "transportation allowances" and "regional quota adjusters" (RQAs) were used as a means of ensuring the Class 1 plants were served.

Transportation allowances partially compensate producers for the cost of hauling milk from a producer's ranch to qualified plants. These allowances apply to all market (grade A) milk moving from dairy farms to plants in qualifying areas that process more than 50 percent of the milk received into Class 1, Class 2, and/or Class 3 products. In addition, cooperative organizations receive transportation allowances on shipments to their plants if the plant is located in a deficit area and if the plant supplies 40 percent of its receipts for Class 1 usage. A more complete discussion of transportation allowances can be found in the Departmental publication, *"Options to Facilitate Orderly Movement of Milk to California's Fluid Markets"*.

Introduction of Proposals — Six organizations proposed changes to the transportation allowance system. The suggested amendments are summarized below.

Imperial County

1) Southern California Receiving Area
    a) Add Imperial County to the list of counties eligible to receive transportation allowances for milk shipped into the Southern California Receiving Area at the same rate as Fresno, Kings, Kern and Tulare Counties
    b) Add San Diego County to the Southern California Receiving Area

California Dairies, Inc.

1) Bay Area Receiving Area
    a) Increase rate for the 0 to 99 miles zone from $0.20 to $0.24 per cwt.
2) Southern California Receiving Area
    a) Set mileage zone from 0 to 119 miles with a rate of $0.00 per cwt.
    b) Set mileage zone from 119.1 to 149 miles with a rate of $0.46 per cwt.
    c) Set mileage zone for more than 149 miles with a rate of $0.58 per cwt.
    d) Establish Tulare, Kings, Kern and Santa Barbara as the only counties eligible to receive transportation allowances for milk shipped into the Southern California Receiving Area

Dairy Farmers of America

1) Bay Area Receiving Area
    a) Increase rate for the 0 to 99 miles zone from $0.20 to $0.24 per cwt.
    b) Increase rate for the 99 to 199 miles zone from $0.24 to $0.28 per cwt.
2) Solano Receiving Area
    a) Increase rate for the 0 to 44 miles zone from $0.11 to $0.15 per cwt.
    b) Increase rate for the 44 to 99 miles zone from $0.16 to $0.20 per cwt
    c) Increase rate for the over 99 miles zone from $0.21 to $0.25 per cwt.

Producers Dairy

1) Statewide
    a) Eliminate the concept of receiving areas and designate all Class 1 plants as qualified plants for transportation allowances
    b) No transportation allowances for hauls less than 15 miles
    c) Set mileage brackets every 25 miles with a shortfall in the rate for milk that is hauled longer distances.

Land O'Lakes

1) Southern California Receiving Area
    a) Set mileage zone from 0 to 75 miles with a rate of $0.00 per cwt.
    b) Set mileage zone from 75 to 125 miles with a rate of $0.4525 per cwt.
    c) Set mileage zone from 125.1 to 160 miles with a rate of $0.575 per cwt.
    d) Set mileage zone for more than 160 miles with a rate of $0.645 per cwt.

Milk Producers Council

1) Statewide
    a) Eliminate the concept of receiving areas and designate all Class 1 plants as qualified plants for transportation allowances

b) Make all grade A milk production eligible
c) No transportation allowances for hauls less than 15 miles
d) Set mileage brackets approximately every 25 miles with a shortfall in the rate for milk that is hauled longer distances.

Impact of Proposals

The proposals were assessed using static analyses with monthly data from 2000. No assumptions were made regarding changes in milk movement patterns. The "templates" generated by each proposal were overlaid on the milk movements that occurred in 2000, and costs were calculated accordingly. The cost of each proposal was compared to the cost generated by the current system on identical milk movements. The impacts of the PDF and MPC proposals were collapsed into a single analysis because of the common elements that they share. Table 1 shows that the proposals by LOL and by MPC result in significant cost increases to the pool while the other proposals have more moderate effects.

Table 1. Monthly Average Impacts for Various Proposed Changes to the Transportation Allowance System Using 2000 Data

	Current	Proposed	Difference
CDI, Bay Area	$186,439	$215,181	$28,742
DFA, Bay Area	$186,439	$221,346	$34,907
DFA, Solano	$31,145	$38,354	$7,209
IC, Southern California	$432,258	$434,180	$1,922
LOL, Southern California	$432,258	$533,365	$101,108
CDI, Southern California	$432,258	$482,007	$49,749
MPC, Statewide	$700,900	$1,241,968	$541,068

Analyses

Why Milk Movement Incentives are Needed — In the first of the four Departmental workshops on milk movement incentives, the consensus of the participants is that a regulated system to move milk to the higher usages needs to continue to be in place. The group conceded that milk may move without a regulated system. However, one of the underlying tenets of instituting a pooling program in California was to ensure that Class 1 plants continue to be served in the absence of direct incentives for producers to ship their milk to those plants.

Since the inception of the pooling program, few significant changes have been implemented in the mechanisms used to compensate those dairy farmers who supply milk to Class 1 plants. Consequently, there is no direct and compelling economic reason for a producer to ship milk to a fluid milk plant. In the late 1960s and early 1970s, this was not of concern because Class 1 utilization hovered near 65 percent of California's total milk production. Today, Class 1 utilization is less than 20 percent. More importantly, almost three–quarters of California's milk production is used to manufacture cheese, butter and nonfat dry milk.

To further compound the problem, many manufacturing plants pay premiums, and most cooperative plants distribute annual dividends. These monies are paid to producers in addition to regulated minimum prices and are not subject to pooling. The producers who ship milk to these manufacturing plants receive both the appropriate pool price (quota, overbase or a blend of the two) plus the associated premium or dividend. The availability of these economic incentives may cause some milk production that would have been shipped to fluid milk plants to be diverted to manufacturing plants.

The Southern California Milk Marketing Area exemplifies the changing nature of milk market structure. Although Southern California has been traditionally viewed as a deficit market, that may no longer be the case. The hearing record is replete with definitions of a “deficit market”. Not surprisingly, the descriptions of a “deficit market” not only reflected the positions of the witnesses, but supported them as well. The definition for the term “deficit market” is not precise, but for the task at hand, a precise definition is not needed. Most recognize “deficit market” as a general term used to describe the conditions of a market vis-à-vis a “surplus market”. Nonetheless, the Panel puts forth its working definition of a deficit market to make a point about the use of transportation credits.

In the strictest sense, a market that has enough locally produced milk to satisfy its *Class 1* needs plus a moderate reserve (20 to 25 percent) to account for fluctuations in demand and supply for Class 1 products is not deficit. In the case of the Southern California Milk Marketing Area, enough milk was produced in May 2001 to serve all of its Class 1 needs and maintain a 30 percent standby reserve. Nonetheless, dairy farmers incurred a cost of $805,688 in transportation allowances for May 2001 to bring milk from the South Valley to serve Southern California's Class 1 needs. During 2000, the cost to the pool was nearly $8.5 million. Furthermore, fluid milk processors in Southern California routinely support the annual implementation of call provisions as a standby mechanism for obtaining adequate milk supplies. This statement of fact merely underscores the point that milk produced locally does not necessary move to the fluid milk plants despite the quantity of milk that continues to be produced in the area.

Where the Panel is Coming From — The Panel recognizes that there are increasing incentives to obtain transportation allowances, particularly as milk production and marketing becomes market-oriented, and the level of competition among producers intensifies. Obtaining new or higher rates for transportation allowances may mean the difference between economic success or failure of a dairy. Consequently, the Department has been receiving a growing number of requests to establish new or higher transportation allowance rates. Moreover, there seems to be a growing perception that if some farmers receive transportation allowances then all farmers should be entitled to them. At the hearings, it was apparent that self–interest largely dictated the positions taken.

The Panel adopted the idea that producers who serve the Class 1 market ought to be rewarded as one of the basic criteria for evaluating the proposed amendments. Among the other criteria used were the idea that the closest milk to the market ought to move first and that any regulated system ought to attempt to minimize costs to the pool. Other factors were considered, but were given less weight than these primary factors.

Uniform Transportation Allowances Statewide — The proposal advanced by MPC was fully supported by two other hearing participants and supported in part by several other participants. The basic tenets of this proposal centered on equity for producers, designating all Class 1 plants as qualifying plants, designating all grade A milk production as eligible, and using a uniform mileage bracket and rate structure statewide. While this approach has some appeal, it also has several flaws. First, nearly all hearing participants agreed that Northern California and Southern California represented two entirely different marketing areas. As such, a "one–size–fits–all" transportation allowance system would be inadequate to reflect the specific needs of both marketing areas. Second, the blanket qualification standard for Class 1 plants ignores that there are distinct differences among plants in their ability to attract adequate supplies of milk. For example, fluid milk plants located in the Central Valley are relatively close to local milk supplies while fluid milk plants in the Bay Area and Southern California may have to draw milk from as far away as 200 miles. Departmental data show that over 90 percent of the milk processed at fluid milk plants in Fresno, Stanislaus and Merced counties is located no further than 40 miles from the plants, and nearly 40 percent of milk is located within 20 miles of the plants. Conversely, 35 percent of the milk shipped to Southern California fluid milk plants and 82 percent of the milk shipped to Bay Area fluid milk plants travels at least 70 miles. Third, the proposal seems to focus too narrowly on what MPC perceives as producer equity. As stated in MPC's testimony,

> "In our view, if the government is going to use its power of regulation to subsidize certain milk movements, the equity is the major criterion that should be used to determine whether or not changes should be made to the current transportation subsidy system."

The Panel recognizes the importance of producer equity in all dairy related issues. However, MPC seems to suggest that equity means "equal" and that all producers should have equal access to transportation allowances. In the Panel's view, equity does not necessarily mean "equal". To use "equal" as the major criterion clearly misses the point of a milk movement incentive system. As stated earlier, the system exists to facilitate movement of milk from supply areas to deficit areas, and as such, criteria to assess the efficacy of the system should include cost and resource efficiency, orderliness of milk movement patterns, minimization of unequal raw product costs among processors, and adaptability of the system to keep pace with a dynamic industry. In the Panel's view, a transportation allowance system resulting from consideration of all these factors will be equitable to producers.

Panel Recommendation — Do not adopt the MPC proposal to extend transportation allowances to all Class 1 plants and all grade A milk.

Eligibility of Imperial County for Transportation Allowances — The petition by Imperial County received mixed support from other hearing witnesses. In general, those in support saw the Imperial County proposal as a step toward minimizing perceived producer inequities being perpetuated by the transportation allowance system. Those witnesses opposed to the concept of granting the petition were unified in stating that transportation allowances were never intended to be used as a tool to assist in developing stronger dairy industries for counties.
While the Panel may see the logic in both positions, it views the issue from a slightly different angle. Imperial County, as well as Los Angeles, Orange, Ventura, San Diego, Riverside, San

Bernardino, Inyo and Mono Counties, was originally exempted from receiving transportation allowances when milk was shipped into the Southern California Receiving Area. The reason the exemption was put in place was because there were very few shipping options other than the fluid milk plants located in the area. Ostensibly, there was no reason to offer incentives to producers to ship to fluid milk plants if that was the only practical option available. However, with the changing structure of the dairy industry, that logic no longer seems applicable. The presence of other processing plants in the area, particularly the cheese plant in Corona, has given shipping options to producers where there once were virtually none. As such, the Panel finds no reason to continue a regulation that does not serve its original purpose, and in fact, may be inhibiting the objectives of the milk movement incentives program.

Panel Recommendation — Delete Section 921.2 (e) (1) from the Milk Pooling Plan, which specifically exempts Imperial, Los Angeles, Orange, Ventura, San Diego, Riverside, San Bernardino, Inyo and Mono Counties from receiving transportation allowances for milk shipped into the Southern California Receiving Area.

Inclusion of San Diego as part of the Southern California Receiving Area — Imperial County's petitioner, among other things, would include San Diego County as part of the Southern California Receiving Area, which would make milk shipped to qualifying plants eligible for transportation allowances. This would create an incentive for milk produced in Imperial County to be shipped into Class 1 plants in San Diego, rather than the more distant haul into the Los Angeles area. The Panel agrees with the logic of this supposition. The Panel also notes that San Diego is the largest metropolitan area in California not covered by a transportation allowance program.

While the petitioner proposed that San Diego be incorporated into the Southern California Receiving Area, the Panel recommends that San Diego County be made a separate receiving area. The San Diego market differs substantially from that of what principally is the Los Angeles market. However, both of these areas will most likely see significant changes in the years to come particularly regarding production of milk. While adopting the Southern California brackets and rates for now and by making San Diego a separate receiving area, the Department will have greater latitude to adjust allowance mileage brackets and/or rates that are different from the Southern California area at some point in the future.

Panel Recommendation — Amend Section 921.2 to add a subsection (f) to the Milk Pooling Plan, which specifies that San Diego County is a receiving area. The transportation allowance rates and mileage brackets are as follows:

From 0 through 90 miles	\$0.00 per cwt.
Over 90 through 140 miles	\$0.43 per cwt.
Over 140 miles	\$0.58 per cwt.

Adjustments to Allowances for Southern California Receiving Area — The most detailed proposals regarding milk movement incentives dealt directly with the Southern California Receiving Area. Two dairy cooperatives that receive transportation allowances from the Southern

California Receiving Area presented the two proposals that sought to alter the current structure of the rates, mileage brackets and other associated features of the receiving area. While the two proposals differed slightly in the details, the major difference was philosophical — should the allowance provide for full coverage of transportation costs (excluding the cost of the local haul) or should the allowance contain a shortfall? The proposal submitted by LOL suggests that the current allowance should be increased so that there is no shortfall or a very minimal shortfall. The proposal submitted by CDI recognizes the need for a shortfall and stated,

> "…disincentives should exist to discourage this movement, and transportation allowances should be set to attract milk from Kern County, which has sufficient milk to cover the shortfall needs of the Southern California marketplace."

The Panel agrees with this assessment. A shortfall should continue exist in the structure of any area receiving a transportation allowance to encourage the closest milk to move first.

The proposals submitted by LOL and CDI attempted adjust the mileage brackets materially. The proposal from LOL added one additional mileage bracket (a total of four) and altered the "length" of the middle zones. The apparent intent of using more mileage brackets was to facilitate the movement of milk located closer to the market first. The proposal from CDI maintains three mileage brackets, but increased the "length" of the zone that currently receives an allowance of $0.00. CDI testified that the zones they proposed are based on the location of their members and would defer to Departmental data if more appropriate mileage brackets were suggested by the analysis. The rate structures suggested by both LOL and CDI were similar for the lower mileage brackets. Both organizations agreed that the transportation allowance for milk closer than 149 miles was woefully short of current hauling costs. Different philosophies regarding shortfalls explains the large difference in rates suggested by the two organizations for more distant milk.

Departmental analysis suggests that changes need to be made to the mileage brackets. Whereas the current zones of 0 to 74 miles and 74 to 149 miles zones fit well with the location of producers at the time the zones were implemented, they no longer continue to make logical sense. For milk shipped into Southern California, there are four clear milk production zones defined by breaks in the data: less than 65 miles, 65 to 90 miles, 90 to 140 miles and over 140 miles. These breaks in the data reflect the notion that dairy farms locations are selected such that clusters are formed; dairy farm locations are not chosen randomly. While there is a natural at 65 miles, only about 5 percent of the milk shipped to Southern California lies within the 65 to 90 mile zone. Thus, the Panel recommends combining the two shorter distance zones to form one zone that ranges from 0 to 90 miles. The Panel further recommends that this zone be used with the other two naturally occurring zones as the basis for a revised set of three transportation allowance mileage brackets. For the purposes of assigning transportation allowances, the Panel verified, through the Department's hauling cost surveys, that hauling costs have increased. However, the Panel suggests a small shortfall in the middle bracket of $0.03 per cwt. such that a small disincentive will exist for milk moving more than 90 miles.

One remaining issue regarding the Southern California Receiving Area addresses the eligibility of counties for receipt of a transportation allowance. An earlier section of this report removed the exempt status from the nine Southern California counties. However, Kings, Kern, Fresno and

Tulare Counties currently are eligible for significantly higher transportation allowances than all other counties, particularly for distances over 149 miles. CDI proposed that Santa Barbara County as a substitute for Fresno County as one of the four counties eligible to receive higher transportation allowances. CDI also proposed eliminating the eligibility of all other counties because the historical shipments of milk into Southern California have come from Tulare, Kings, Kern and, more recently, Santa Barbara Counties. The Panel does not question the accuracy of this statement, but it is not willing to exclude other counties from the available transportation rate. To do so discriminates against producers who may wish to ship milk into Southern California based strictly on the location of their dairies. Furthermore, designating eligible and ineligible counties may actually decrease the supply of milk available to Class 1 plants, a result which does not work toward the principles previously outlined by the Panel. As such, the Panel sees no compelling reason to exclude other counties from receiving the same rates as are available to the counties that have historically supplied milk to the Southern California market.

Panel Recommendation — Delete Sections 921.2 (2) and (3) from the Milk Pooling Plan. Add a new Section 921.2 (e) (1), which specifies the transportation allowance rates available for milk shipped into qualifying plants within the Southern California Receiving Area. The amended rates are:

0 to 90 miles	$0.00 per cwt.
Over 90 to 140 miles	$0.43 per cwt.
Over 140 miles	$0.58 per cwt.

Adjustments to Allowances for Bay Area Receiving Area — Although it may be limited, the hearing record contains adequate testimony and evidence for changes to the transportation allowance system operating in the Bay Area Receiving Area. The proposals submitted by CDI and DFA both requested increases in rates without any changes to the existing mileage brackets or adjustments to receiving areas. The proposal from CDI requested a four–cent increase in the “0 through 99 miles” bracket but did not make any additional adjustments, ostensibly because CDI does not ship milk into the Bay Area Receiving Area from beyond 99 miles. The proposal from DFA requested four–cent increases in the “0 through 99 miles” bracket and in the “Over 99 through 199 miles” bracket. Like CDI, DFA did not propose any adjustments to the bracket covering shipments over 199 miles because DFA does not have milk moving into Bay Area Receiving Area from that distance. No organization opposed the hauling rate increases proposed by either CDI or DFA, although CDI did recommend to the Panel that any adjustments made should be cost–justified.

Using Departmental hauling cost survey data, the Panel was able to verify that hauling costs have increased by the amounts to which the organizations testified. It appears that a four–cent adjustment to both the “0 through 99 miles” bracket and the “Over 99 through 199 miles” bracket are warranted. As such, the new rates would be $0.24 per cwt. and $0.28 per cwt., respectively. Furthermore, the Panel recommends no change in the over 199 miles bracket, which shall remain at $0.30 per cwt. There was no testimony that suggested that a rate increase for this more distant mileage bracket was warranted.

Panel Recommendation — Amend Section 921.2 (a) (1) from the Milk Pooling Plan, which specifies the transportation allowance rates available for milk shipped into qualifying plants within the Bay Area Receiving Area. The amended rates are:

From 0 through 99 miles	$0.24 per cwt.
Over 99 through 199 miles	$0.28 per cwt.
Over 199 miles	$0.30 per cwt.

Adjustments to Allowances for Solano Receiving Area — Like the Bay Area Receiving Area, the hearing record contains limited but adequate testimony and evidence for changes to the transportation allowance system operating in the Solano Receiving Area. The proposal submitted by DFA requested increases in allowance rates without any further adjustments to allowance system. The proposal requested four–cent increases in all three mileage brackets. No organization opposed the hauling rate increases proposed by DFA, although CDI did recommend to the Panel that any adjustments made should be cost–justified.

Using Departmental hauling cost survey data, the Panel was able to verify that hauling costs have increased. A four–cent adjustment to all three mileage brackets is warranted. As such, the new rates would be $0.15 per cwt., $0.20 per cwt. and $0.25 per cwt., respectively.

Panel Recommendation — Amend Section 921.2 (d) (1) from the Milk Pooling Plan, which specifies the transportation allowance rates available for milk shipped into qualifying plants within the Solano Receiving Area. The amended rates are:

From 0 through 44 miles	$0.15 per cwt.
Over 44 through 99 miles	$0.20 per cwt.
Over 99 miles	$0.25 per cwt.

Concluding Remarks — After reviewing all of the matters during the process of developing this report, the Panel is more aware than ever that all of the regulations encompassed by the milk movement incentive program are linked. Changing one regulation necessarily has a ripple effect and affects other milk movement regulations directly or indirectly.

The Panel notes that individual interests appeared to dictate the types and scopes of proposals submitted and the positions taken in the matters affecting milk movement incentives. The Panel recommends moving forward on milk movement incentive policy and cites three basic criteria as guidelines — most efficient milk movements promoted or rewarded, encourage the closest milk to Class 1 plants to move first and minimize costs to the pool. The Panel was disappointed in the lack of testimony or evidence submitted into the hearing record that dealt directly with these three basic criteria. The Panel sees a need for more focus on the long term implications of changes and exhorts the industry to work toward a compromising solution that is in the best interest of the industry and of the public.

ATTACHMENT A–1

Summary of Panel Recommendation

Recommendation: Do not adopt a uniform transportation allowance system statewide.

Arguments in Favor of Panel Recommendation

1. Milk markets have too variegated to implement successfully a "one–size–fits–all" system.
2. May give a financial reward to move milk where none is needed
3. Potentially costs the pool hundreds of thousands of dollars in new transportation allowances
4. May lead to unequal raw product costs among Class 1 handlers

Arguments Opposed to Panel Recommendation

1. Does not address some producers' concerns that the current system is inequitable
2. Not all producers shipping to qualifying plants will be rewarded similarly
3. Only select plants (qualifying plants in designated deficit areas) will be able to use transportation allowances to attract milk.

Recommendation:

Remove exempt status of nine Southern California counties so that milk shipped to qualifying plants and travelling a specified distance will qualify for transportation allowances.

Arguments in Favor of Panel Recommendation

1. Removes an apparent inequity in the milk movement incentive system
2. May give processors ability to attract milk locally

Arguments Opposed to Panel Recommendation

1. May cost the pool thousands of dollars in new transportation allowances
2. May create unanticipated and inefficient milk movements

Recommendation:

Establish San Diego as a receiving area

Arguments in Favor of Panel Recommendation

1. Gives a transportation allowance system to a large metropolitan area that has a shrinking local milk supply.
2. Rewards producers who ship into the Class 1 handlers

3. Gives the Department the ability to adjust transportation allowances separate from the Southern California Receiving Area.

Arguments Opposed to Panel Recommendation

1. May cost the pool thousands of dollars in new transportation allowances
2. May create unanticipated and inefficient milk movements

Recommendation:

Adjust rates, mileage brackets and county designations for the Southern California Receiving Area

Arguments in Favor of Panel Recommendation

1. Adjusts rates according to actual hauling costs
2. Adjusts mileage brackets to match with current industry structure
3. Removes discriminatory rates that have historically applied to some counties

Arguments Opposed to Panel Recommendation

1. Structure of allowance system is current with industry and not forward looking
2. May create unanticipated and inefficient milk movements

Recommendation:

Adjust rates for the Bay Area and Solano Receiving Areas

Arguments in Favor of Panel Recommendation

1. Rate adjustments reflect increases in actual hauling costs

Arguments Opposed to Panel Recommendation

1. Structure of allowance system is current with industry and not forward looking
2. May create unanticipated and inefficient milk movements
3. All other things kept constant, the higher rates will cost the pool more money

ATTACHMENT A-2

Summary of Evidence, Testimony and Post Hearing Briefs

William Schiek — *Dairy Institute of California*

Testimony:

- ✓ Historically the transportation credits have been set at levels that do not fully compensate handlers for their shipment costs.
- ✓ Shortfalls are supported by Dairy Institute
- ✓ Continues to believe that some type of milk movement incentive system is necessary
- ✓ Milk should be attracted to Class 1 plants at order prices, i.e., premiums should not be a necessary part of attracting adequate supplies of milk.
- ✓ Some producers held incorrect views that the sole purpose of the Class 1 price differential is to enhance producer income rather than recognizing that it was designed to assure that Class 1 markets are served.
- ✓ Existing order prices paid by procesors are high enough to provide more than enough revenue to attract milk for Class 1 and mandatory Class 2 purposes.
- ✓ Dairy Institute continues to believe that a system which provides positive incentives for producers to ship to Class1 and Class 2 plants is appropriate but support a much more modest amendments to the existing program.
- ✓ Continue to support the establishment of a subcommittee to look at all existing plants milksheds, and transportation costs and hauling rates for producers shipping to those plants to determine the appropriate allowance and credit rates for various locations.
- ✓ Without a comprehensive and disaggregate review of hauling costs, uncomfortable with making more than modest changes to the milk movement incentives at this time.
- ✓ Dairy Institute continues to support the principle that transportation allowances rates should be set equal to the difference between the cost of the local haul and the cost of the haul to fluid plants in metropolitan markets.
- ✓ Support adjustments to the allowance rates for shipments from the South Valley to Southern California.
- ✓ Current rates seem to create an incentive for inefficient milk movement.
- ✓ CDI and LOL proposals regarding transportation allowances do much to improve the current situation.
- ✓ Favors the LOL proposal of creating more mileage zones, it has the potential to promote more efficient movement.
- ✓ Dairy Institute opposes the petition from Imperial County because the current milk supply appears inadequate to warrant its inclusion in the counties eligible to receive transportation allowances.
- ✓ The transportation allowance has not been used in the past as an economic development tool to encourage the relocation of dairies to a particular area.
- ✓ Opposes MPC's proposal in that nearby milk should be encouraged to move to Class 1 uses ahead of more distant milk.

- ✓ Opposes any changes to the transportation credits into Southern California from Tulare at this time.
- ✓ CDFA should leave transportation credit rates unchanged to stabilize the existing supply relationships within the industry.
- ✓ Supports the continuation of the call provisions. Under these provisions handlers are given an incentive to voluntarily supply milk for fluid uses if call provisions are implemented.
- ✓ Call provisions are necessary as a standby mechanism.
- ✓ Oppose any changes to the Class 1 area differential at this time.
- ✓ They have not been subject to industry study and review.
- ✓ Supports continuation of the RQA's that quota holders have an obligation to ensure that Class 1 markets are served. No changes at this time.
- ✓ Supports adjustments to the allowance rates for shipments from Central Valley to the Bay Area.
- ✓ Supports the proposal by CDI for a 4 cent per hundredweight increase in the allowance rate.
- ✓ The increase needed for the greater than 199 miles zone should be somewhat less than 4 cents to encourage the milk in the closer brackets to move first.
- ✓ Opposes the proposal of Producers Dairy.
- ✓ Maintains that milk movement incentives are needed to encourage shipments to deficit metropolitan area fluid milk plants at order prices.
- ✓ Does not believe there is a credible reason to establish a receiving area for Fresno.

Post Hearing Brief:

- ✓ Opposes any changes to the transportation credit rates at this time.
- ✓ If CDI's concerns have merit, prefer that the Department take a pro-competitive approach by giving CDI – Artesia a transportation credit rather than reducing the credit for Tulare as CDI proposes.
- ✓ Believes that the Department's published data on plant to plant and ranch to plant hauling rates indicate the modest changes in transportation allowance sin specific areas are warranted.
- ✓ A thorough and detailed study of all hauling rates should be completed before making changes.
- ✓ Class 1 price differential is intended to reflect the cost of moving milk to Class 1 plants.
- ✓ From the South Valley the highest incentive needed for plant to plant movement is about $0.67 per hundredweight.
- ✓ The Southern California Class 1 differential of $2.27 to $2.34 per hundredweight provides more than enough revenue to reflect the cost of Grade A conversion and Class 1 milk movements.
- ✓ Northern California Class 1 differential of $1.99 to $2.07 per hundredweight is much more than adequate to fund the extra costs of market grade milk production and the cost of attracting milk to the deficit areas.

Gary L. Korsmeier — *California Dairies Inc.*

Alternative Proposal:

- ✓ Propose changes on transportation allowances and credits include Section 921.2 for plants located in the Bay Area receiving area, zero to 99 miles $0.24 per cwt.
- ✓ For plants located in Southern California receiving area from Kern, Kings, Santa Barbara and Tulare Counties (not Fresno) zero to 119 $0.00, Over 119 to 149 $0.46 per cwt and over 149 miles $0.59 per cwt.
- ✓ Subsection (3) should be deleted
- ✓ Section 300.2 Tulare County $0.30 cwt to Los Angeles, Orange and Riverside not San Diego or Ventura Counties.
- ✓ The proposed changes are reflective of current hauling costs and changes in supply arrangements in the Southern California marketplace.

Testimony:

- ✓ CDI opposes the expansion of transportation allowances for Imperial County.
- ✓ Transportation allowances should not be used as a business development tool.
- ✓ Opposes Producers Dairy proposal in that Fresno County is not a deficit area
- ✓ Support LOL, the need to adjust transportation allowances into Southern California because of escalating costs is the basis for their alternative proposal.
- ✓ Opposes LOL recommended changes to transportation credits.
- ✓ Do not support MPC's proposal.
- ✓ CDI proposes to increase the rate from $0.20 per cwt $0.24 per cwt for mileage 0 to 99.
- ✓ Request a change to 921.2(e)(2) by adding Santa Barbara County as an area that can obtain transportation allowances to the Southern California receiving area and deleting Fresno County.
- ✓ With inclusion of Santa Barbara County there is no need for the continuance of Section 921.2(e)(3) and therefore should be deleted.
- ✓ Recommend changes are to Section 921.2(e)(2)(10 in both mileage brackets and rates.
- ✓ From Kern, Kings, Santa Barbara and Tulare Counties, 0 to 119 miles $0.00, over 119 to 149 miles $0.46 per cwt and over 149 miles $0.58 per cwt.
- ✓ Have historically supported a slight shortfall from milk movement from Tulare County.
- ✓ Propose a reduction in the transportation credit to $0.30 per cwt for shipments from Tulare County to Los Angeles, Orange and Riverside Counties.
- ✓ Not recommending total elimination of transportation credits; just equalization among suppliers.
- ✓ Transportation credits to the Southern California marketplace today charge most of the second haul to the Statewide producer pool.
- ✓ Proposal increases the shortfall to $0.39 per cwt to allow for a local processor in Southern California to be competitive with an out of area processor.
- ✓ The current system penalizes an available local supplier.
- ✓ Remove the inequity and reduce the transportation credit from Tulare to Southern California from $0.50 per cwt to $0.30 per cwt.

Post Hearing Brief:

- Basic principles of transportation allowances are to encourage milk movement from closer distances and build in a disincentive from further locations.
- CDI's proposal incorporates new mileage brackets and rates, which adequately accomplishes the objectives of transportation allowances.
- CDI's proposal will leave a $.065/cwt. disincentive from Tulare County and will cover the current movement costs from the county of Kern.
- With regards to milk movement from less than 119 miles to Southern California, CDI is not aware of testimony supplying cost-justified data to support a reduced mileage bracket.
- Land O' Lakes opposed the addition of Santa Barbara County in receiving an allowance, while CDI believes the actual mileage distance of the dairies to even Ventura County is more than the 149 mileage bracket that would receive the maximum allowance of $.58/cwt. in CDI's proposal. If the distance is less than 149 miles, then this movement would receive the lower allowance of $.46/cwt.
- CDI supports the elimination of Section 921.2(e)(3) because the mileage brackets should be the same for Kern, Kings, Santa Barbara and Tulare Counties.
- Regarding transportation credits accepting Land O' Lakes recommendation of $.695 CDI would be disadvantaged to the level of almost $.40/cwt.
- There will be no options for Southern California processors that desire tailored products without a reduction in transportation credits.
- Land O' Lakes will be the only player; cannot imagine how that will benefit anyone other than Land O' Lakes in the long term.
- CDI has a long history in supplying the needs of Class I processors, especially in Southern California.
- CDI does not accept the argument that reducing credits will encourage out of state milk movement.
- The concern for transporting cream back to Tulare if tailored products in not purchased from Tulare is a weak argument.
- The argument of institutional factors also no longer exists today because it all boils down to economics.
- CDI has requested to reduce transportation credits to $.30/cwt. into Southern California only to make it an equal playing field. CDI should be afforded the opportunity to be competitive.

Geoffrey Vanden Heuvel — *Milk Producers Council*

Alternative Proposal:

✓ The current transportation subsidy system is inequitable.
✓ Rules and mileage brackets have no logical consistency between regions and certain producers and certain plants are discriminated against for no justifiable reason.
✓ All Class 1 plants in California should qualify for milk movement incentives.
✓ All California Grade A milk production is eligible.

- ✓ The allowance starts at some mileage greater than zero and the starting point is the same throughout the State.
- ✓ The allowance zones out in logical increments with a slight shortfall applied progressively to each mileage increment.
- ✓ Transportation credits continue but shall not exceed the rate for the distance traveled.
- ✓ MPCs proposal eliminates the current county based discrimination against fluid plants and producers and establishes consistent statewide mileage criteria to the system.
- ✓ The inclusion of all Class 1 plants and all production addresses the discrimination issues and allows for the shifts in milksheds and population centers that have taken place and will continue to take place.
- ✓ Reevaluate the standard for "constructive miles" to assure that it still is effective in normalizing the difference between open highway miles and congested urban miles.

Testimony:

- ✓ MPC has held the position that the transportation allowance and credit system is unnecessary.
- ✓ The Call Provisions contained in the various plans are all that is needed in the way of State imposed regulations.
- ✓ It is the consensus of the industry that the state must provide within the regulated Plans, specific Class 1 incentives to ensure that milk moves to Class 1 handlers.
- ✓ The current system is not equitable.
- ✓ The system assumes milk has a location value.
- ✓ It assumes it is more efficient to haul milk in bulk form from a production area to a bottling plant in an urban area that it would be to bottle milk in the production are and transport it in packaged form.
- ✓ The current system also assumes that there are distinct urban receiving areas that are separate and different from rural "supply" areas.
- ✓ The current system provides incentives in the form of transportation subsidies to move bulk milk to Sacramento and San Francisco and no incentives to move milk to bottlers in Modesto and Fresno.
- ✓ Southern California producers located in the Inland area must pay the full cost of transporting milk to the Los Angeles and Orange County bottling facilities.
- ✓ Results in South Valley producers hauling rate being significantly lower than the Southern California produceres hauling rate.
- ✓ The Department's own analysis shows that there are significant cost savings that accrue to the bottling facility in the plant to plant arrangement.
- ✓ Transportation credit from Tulare to So. California is so generous that it makes it virtually impossible for standardized So. California produced milk to be price competitive in So. California.
- ✓ MPC proposes to make all Class 1 plants eligible for milk movement incentives.
- ✓ Only drop the county criterion.
- ✓ Make all grade A milk production eligible.
- ✓ Establish constructive mileage brackets that are consistent for every Class 1 plant in the state.
- ✓ Have no subsidy available for milk located within 15 miles of the plant.

- ✓ Continuation of the transportation credit system with the requirement that the combination of the area Class 1 differential and the transportation credit shall not exceed rate for the distance that milk travels.
- ✓ Not proposing to change the definition of constructive mileage.
- ✓ Imperial County production would be eligible for transportation allowances.
- ✓ Non producer-distributor milk shipped to the Producers Dairy, Fresno bottling plant would be eligible to receive an allowance.
- ✓ MPC proposal similar to CDI's reducing transportation credit from $0.50 to $0.30.
- ✓ Strongly support the concept of a shortfall.
- ✓ LOL seeks to enhance their competitive position with regards to transportation credits.
- ✓ It is true that quota held by producers in the Southern California region is not subject to a negative Regional Quota Adjusted.
- ✓ RQA's are not class 1 incentives but are recognition of the location differences in the value of milk and the cost of production.
- ✓ MPC proposal by starting the allowance at 15 miles distant restores the incentive in Southern California.
- ✓ The current system makes all producers pay, but picks and chooses rather arbitrarily who may take advantage of the program.
- ✓ Discrimination is cheaper, but it is not the right thing to do.

Post Hearing Brief:

- The MPC program was designed to meet the primary criteria identified at the Department's Transportation Workshops.
- MPC supports moving the closest milk first; moving milk at least cost and providing those people who serve the class 1 market some compensation or assistance in their transportation cost.
- MPC proposes moving the closest milk first by starting the transportation allowance at 15 miles.
- The current program discourages rather than encourages the closest milk to move to the class 1 handlers in the Southern California receiving area.
- Moving the mileage bracket to 15 miles statewide makes eligible for transportation incentives, significant amounts of milk that is located much closer to the Southern California class 1 bottlers than is currently the case.
- It is rational to assume that producers who have a local haul to a Class 1 plant of less than 15 miles should be paying a haul rate that is lower than the $.23/cwt.
- The current transportation allowance system is unnecessarily inflating costs because it subsidizes producers who need no subsidy.
- MPC proposal makes the vast majority of the milk that serves the Class 1 market eligible for transportation incentives.
- Corona and the Sorrento plant suppliers are subject to the call provisions, which by definition makes them part of the available reserve supply.
- The current milk movement patterns in Southern California are a creation of the current transportation program.
- If MPC's proposal adopted the incentive to haul the local milk to the class 1 handlers will be created.

- MPC notes that a positive response to that policy may make milk procurement more difficult for manufacturing plants. But the purpose of the transportation subsidy program is "to attract milk to fluid plants in metropolitan areas at order prices."
- MPC's proposal does not significantly change the rates or general mileage brackets currently in place. It expands the program with built in shortfalls to the structure, which limits the abuse of the system.
- Constructive miles take into account "elements of highway traffic, such as congestion and controls."
- MPC's plan would still have Crystal as a qualified receiving plant and in fact would see an increase in the allowance available to producers located 15 or more constructive miles from their plant.
- MPC's plan includes significant shortfalls for far away milk from fluid plants.
- Puts into place an incentive to actually move the close in milk first.
- Fresno is located in the middle of the largest surplus area in the country.
- Land 'O Lakes points out "The area differential according to Ag Economists should reflect the difference in freight costs from an area of surplus to a deficit market."
- Fresno is a surplus area so Class 1 price should be lower in Fresno than it is in Sacramento and Bay area. There is no reason to exclude Fresno or Modesto.
- No difference between the Santa Barbara circumstance and the Imperial County situation.
- No rational reason to oppose the Imperial County request.
- MPC proposes using constructive miles to address the congestion issues faced by the various regions and the mileage brackets and rates are consistent with the current program.
- MPC proposal does indicate that if nothing were to change, the proposal would cost a few cents per cwt. more than the current program.
- They emphasized at the hearing that the current program is unfair and inequitable.

James W. Gruebele, Consultant — *Land O' Lakes*

Alternative Proposal:

- ✓ LOL opposes the proposal by Milk Producers Council and the proposal by Imperial County.
- ✓ The pool does not need to be used for economic development for the Imperial Valley.
- ✓ Milk movement information suggests that Southern California is a deficit market and that the transportation credit and allowance programs are needed to ensure adequate supplies of pure and wholesome milk for Class 1 purposes in Southern California.
- ✓ Southern California market area is losing producers and milk production.
- ✓ Recommend adjustment to the current transportation allowance in Article 9.2, Section 921.2.
- ✓ The current transportation allowance is inadequate to cover the cost of moving milk from the South Valley to Southern California Class 1 milk plants.
- ✓ If milk is needed for Class 1 purposes then the transportation allowance should be adequate to cover that cost so as to not disadvantage a producer from serving the Class 1 market.
- ✓ LOL recommends that the transportation credit be increased from \$.50 to \$.695.
- ✓ This is needed to make up the difference between the freight cost and the area differential between the South Valley and Southern California for plant to plant movement.

- ✓ The remainder of schedule remains unchanged.
- ✓ CDFA published data which showed more efficient to utilize plant to plant milk than when using ranch to plant milk movement.
- ✓ The demand for low fat products continues to be strong.
- ✓ To maintain equal raw product costs for California fluid milk operations it is necessary to update the transportation credit to reflect the cost of moving the milk.
- ✓ Transportation credits would compensate for some of the cost differences in moving milk from an area of surplus in the South Valley to deficit markets in Southern California.
- ✓ Data clearly shows Southern California's milk production is declining.
- ✓ Milk is needed in Southern California.
- ✓ The milk shipped to Southern California is primarily used for Class 1 purposes.
- ✓ Most of the milk moved to Southern California is tailored milk.

Testimony:

- ✓ LOL opposes the proposal by MPC and the proposal by Imperial County.
- ✓ The pool does not need to be used for economic development for Imperial County.
- ✓ Opposes the proposal by CDI to reduce the transportation credit from $0.50 to $0.30 per cwt.
- ✓ LOL opposes the proposal by Western United Dairymen.
- ✓ A market which has less than 30 to 35 percent reserve is termed a "deficit market".
- ✓ The percent of fat in Class 1 in Southern California in 1999 was 2.37 percent and the solids not fat percentage was 9.61 percent.
- ✓ A decision was made to introduce a transportation credit program to replace the area differential in part.
- ✓ The Department can used call provisions to ensure that milk will be released for Class 1 uses if needed.
- ✓ LOL strongly supports the continued uses of programs to ensure that adequate supplies of milk be made available for Class 1 uses.
- ✓ For plants located in the Southern California receiving area, which shall consist of the counties of Los Angeles, Orange and Ventura:

    (1) From Imperial, Inyo, Los Angeles, Mono, Orange, Riverside, San Bernardino San Diego, and Ventura Counties $0.00

    From Fresno, Kern, Kings, and Tulare Counties:

From zero through 75 miles	$0.00
Over 75 miles – 125 miles	$.4525 cwt
Over 125 miles – 160 miles	$.575 cwt
Over 160 miles	$.645 cwt

- ✓ LOL recommends Stabilization and Marketing plan be increased from $0.50 to $0.695 or an increase of $.195 per cwt for milk shipped to the Riverside plant.
- ✓ Recommends that the remainder of the schedule remain unchanged.
- ✓ LOL has served plants in So. Cal on a plant to plant basis for about 40 years.

- ✓ Proposed that the Swiss account have a separate transportation credit because of the additional distance involved.
- ✓ Have argued in the past that plant to plant milk shipments are an efficient means of supplying the Southern California markets with milk.
- ✓ CDFA published data which showed that it is more efficient to utilize plant to plant milk.
- ✓ The demand for low fat products continues to be strong.
- ✓ To maintain equal raw product costs for California fluid milk operations it is necessary to update the transportation credit to reflect the cost of moving milk into the Swiss plant and to other Class 1 plants from the LOL plant in Tulare.
- ✓ A shortfall should be eliminated by increasing the transportation credit from \$0.50 to \$0.695 per cwt.
- ✓ There is no transportation credit for the milk in lower classes. This provides an additional shortfall for milk moved on a plant to plant basis.
- ✓ LOL is not opposed to the utilization of both the transportation credit and the area differential.
- ✓ Recommend that there be two transportation rates established, one for San Diego and Riverside counties and another for Los Angeles, Ventura and Orange counties.
- ✓ There is a significant quantity of milk shipped to Class 1 milk plants on a plant to plant basis as well as on a ranch to plant basis from the South Valley to Southern California.
- ✓ One of the big advantages of the plant to plant system is that milk can be tailored and the unneeded fat is not shipped to Southern California in the first place.
- ✓ Volumes of milk shipped vary from season to season.
- ✓ The fat test is significantly less than one would find with producer milk.
- ✓ The solids not fat tests are higher than one would find with producer milk.
- ✓ The shortfall places LOL and its customers at an immediate disadvantage.
- ✓ Our recommendation is that the Secretary grant an increase in the transportation credits so that the shortfall is totally eliminated.
- ✓ Opposes the proposal by California Dairies Inc. to reduce the credit from \$0.50 to \$0.30 per cwt.
- ✓ The elimination of competition in Southern California is going to reduce the overall market performance in that deficit market.
- ✓ A reduction in the transportation credit could encourage operations to bring in out of state milk instead of paying the shortfall amount.
- ✓ If Ventura County is a deficit county one would think that it would make sense to move the milk from Santa Barbara producers to the Class 1 plants in Ventura County.
- ✓ Strongly opposes the Producers Dairy position.
- ✓ Fresno is located in on of the largest surplus milk producing areas in the nation. A transportation allowance is not needed to move milk into a Class 1 plant in this area.
- ✓ Opposed the elimination of the Area differential with respect to Class 1 milk and opposed the elimination of the differences in Class 2 and 3 prices as well.
- ✓ Opposes the proposal by Imperial County. There are only two producers and the pool should not be used for economic development.
- ✓ Opposes the MPC proposal.
- ✓ The MPC proposal would simply apply a transportation allowance for anyone located anywhere if the milk was shipped to a Class 1 plant.
- ✓ Opposes the addition of the transportation credit to producers located in Southern California.

Post Hearing Brief:

- In Land O' Lakes testimony the last paragraph on pg 12 should read "In conclusion we urge the Secretary to deny the requests of CDI regarding Transportation Credits, the MPC proposal regarding allowances and imperial county proposal with respect to allowances for Imperial County and adopt the proposals presented by LOL on transportation allowances and credits".
- Table 2 has been revised the volumes of milk shipped were somewhat larger than the original table submitted.
- Milk production for Southern California is significantly lower for 2001 compared to 2000.
- Southern California is becoming a deficit area.
- Ask that there be no shortfall in the transportation credit or allowance rates.
- CDI has an advantage over LOL.
- It would be a mistake to grant a transportation credit from Artesia to Riverside because Artesia is located in a SNF deficit area.
- It makes sense to utilize the Southern California milk from the ranch to a Class 1 milk plant and to supplement additional Class 1 milk needs with tailored milk from the South Valley.
- LOL has provided milk on a plant-to-plant basis for 40 years.
- Because of mileage under the current system CDI has and would have a competitive advantage over LOL in supplying Riverside with tailored milk.
- Our proposal does not eliminate competition it would have a competitive advantage over LOL in supplying tailored product to the Riverside Class 1 plant because of the proximity of the manufacturing operations for the respective cooperatives.
- LOL recommended a transportation credit from Tulare to Riverside of $0.695 and LOL recommended a transportation allowance of $0.645 over 160 miles.
- The only way to serve Riverside plant is local sources on a ranch to plant basis and from plant to plant from the South Valley.
- The area differential should reflect the freight cost for milk moved from an area of surplus into a deficit market.
- The request of $0.695 for a transportation credit represents the difference in the freight rate from Tulare to Riverside County minus the area differential of $0.27 per cwt.
- The net cost of the plant-to-plant requested credit is lower than the requested ranch to plant allowance from the same geographic area.
- In Federal Orders transportation credits are larger for plant-to-plant shipments for the same mileage than the credits for milk shipped ranch to plant.
- By tailoring the milk the SNF are shipped in a very efficient manner. Plant to plant program makes sense.
- The CDI proposal would not only discourage plant-to-plant shipments from Tulare it would also have the same effect on shipments from Tipton.

Stephen L. Birdsall — *Imperial County Agricultural Commissioner*

Proposal:

- ✓ San Diego County be included as a receiving area for Southern California.
- ✓ Imperial County be removed from the list that specifies counties that are to receive no transportation allowance.
- ✓ Imperial County be added to (e)(2) as a county to receive a transportation allowance.
- ✓ Makes no recommendations to change the rates of the mileages and the amounts that apply currently.

Testimony:

- ✓ Milk plants in deficit areas have favored purchases from producers and plants in areas that receive a transportation allowance.
- ✓ The fact that Imperial County does not receive a transportation allowance puts future producers in the Imperial County at a considerable competitive disadvantage in selling to current and future deficit area plants.
- ✓ The economic feasibility of dairying in the Imperial Valley; however, is importantly determined by profitability which in turn is largely influenced by transportation costs.
- ✓ Imperial County is NOT new in the dairy industry.
- ✓ Milk can be produced on a dairy farm in the Imperial Valley at least as efficiently and cheaply as in the Southern San Joaquin Valley.
- ✓ Imperial County is planning to use transportation and allowance subsidy as business development tools to attract dairies to relocate to Imperial County.
- ✓ There is a Southern California dairy that has land in escrow in Imperial County.
- ✓ Once this dairy reaches full production, Imperial County will then be in an oversupply situation.
- ✓ Recognizes that at this point in time Imperial has no need for a transportation allowance.

James E. Dolan — *Driftwood Dairy, El Monte, CA*

Testimony:

- ✓ Has historically purchased our milk from the Southern San Joaquin Valley up until the Marketing Association was formed.
- ✓ The Marketing Association has now partially disbanded; wish to re-establish ties with previous supplier in the South Valley.
- ✓ Testifies against the disincentive to ship milk into plant.
- ✓ The Chino Basin milk supply is decreasing while the overall demand is increasing.
- ✓ Production in the Southern California basin is going to continue to decline.
- ✓ LOL is asking for an increase in the transportation credit; support their testimony completely.

Post Hearing Brief:

- Have had unpredictable service with unknown sources of milk supply.
- If Tulare milk is made to be noncompetitive there will be no reason for the local supplier to solve these services problems.

Kevin McLaughlin — *Security Milk Producers Association*

Testimony:

- ✓ Transportation subsidy program should provide equity in costs and values, insure the Class 1 market gets served; encourage efficient and orderly marketing; and anticipate the relocation of milk sheds.
- ✓ SMPA supports the principles detailed in the MPC proposal.
- ✓ The transportation allowance must represent the difference of a local haul rate and a long distance haul rate.
- ✓ The most recent data for January 2001 indicates increased hauling costs, over January 2000 levels.
- ✓ The effective cost to supply LA for a producer located closer to LA, in Bakersfield, is greater than the effective cost to supply LA from Tulare.
- ✓ Believes that this is contrary to the intent of the Plans.
- ✓ We feel that even eight cents per hundredweight creates too large of a shortfall.
- ✓ The MPC proposal also allows for the shifts in milk sheds and population centers that have happened, and will continue to happen.
- ✓ The principle seems clear to us that discrimination against certain counties should end.
- ✓ All counties should be designated eligible supply counties.
- ✓ All Class 1 plants should qualify.
- ✓ We ask that you remove the “receiving area” and “supply county” stigmas.

Post Hearing Brief:

- SMPA believes the Milk Producers Council proposal to be the only true concerted effort to correct the inequities and discrimination in the current Milk Movement Incentives.
- The Department has the opportunity correct the inequities, remove the outdated discriminating stigmas and include all plants with more than 50% Class 1, 2 and 3 usage.
- Include milk produced in any county within the State.

David L. Parrish, Vice President — *Dairy Farmers of America, Inc.*

Testimony:

- ✓ In addition to our own plants DFA supplies significant amounts of bulk milk to Class 1 handlers and other customers.
- ✓ We wish to recommend some changes to the transportation allowance program in the Northern California marketing area.

- ✓ Section 921.2 (a) for plants located in the Bay Area receiving area, which shall consist of the counties of Alameda, Contra Costa, Santa Clara, San Francisco, and San Mateo:
  - (1) From zero through 99 miles $0.24 per CWT
  - (2) From 99 through 199 miles $0.28 per CWT

- ✓ Section 921.2 (b) for plants located in the Solano receiving area, which shall consist of the County of Solano:
  - (1) From zero through 44 miles $0.15 per CWT
  - (2) Over 44 miles through 99 miles $0.20 per CWT
  - (3) Over 99 miles $0.25 per CWT

- ✓ Has milk moving within the mileage bracket over 99 miles through 199 miles to the Bay Area Class 1 plants.
- ✓ Does not have any milk being shipped from more than 199 miles and cannot recommend a change to that mileage bracket.
- ✓ Proposes a change to accommodate the increases in the haul rate to the Class 1 plant in Solano County.

Gary M. Stueve, California Regional Director — *Dean Foods Company*

Testimony:

- ✓ Approximately 90% of milk is purchased directly from independent producers.
- ✓ Supports the original petition by the Imperial County Agricultural Commissioner's Office.
- ✓ Supports in concept the alternative proposal submitted by Milk Producers Council.
- ✓ Believes that transportation allowances should meet the two basic sets of criteria, move adequate, regular and competitive milk supplies to non-Class 4 plants, and be equitable in participation opportunities across all supply and receiving areas.
- ✓ Because plants in San Diego County are currently excluded, attracting California milk to our Escondido plant is difficult and/or costly.
- ✓ Plants located in San Diego County should be treated no differently than those in other Southern California counties.
- ✓ Tulare and Imperial Counties are equal distances to the Los Angeles market, both are viable agricultural areas, both can profitably produce milk and both have alternatives other than supplying the California Class 1 market.
- ✓ Supports an enhancement of transportation allowances as proposed by LOL but we are opposed to the suggested increase in transportation credit.
- ✓ The CDI proposal leaves unanswered the question of Imperial County and other potential milk production areas.

Richard Shehadey, President — *Producers Dairy Foods in Fresno, CA*

Testimony:

- ✓ Are a producer-distributor for a small portion of our milk sales.
- ✓ The current transportation allowance system is unfair and not equitable.
- ✓ Feels that either all Class 1 plants should receive the transportation allowance on a uniform mileage scale or no one should receive it.
- ✓ Does not believe that raw milk located within 15 miles of a processing plant should receive a subsidy.
- ✓ The brackets could be set a 25 mile increments with a shortfall built into the rates for milk that is hauled longer distances.
- ✓ It makes more sense to include all Class 1 processing plants as "receiving plants" instead of by geographic "receiving areas".

Rick Sturgeon, Vice President Western Region — *Suiza Foods Corporation*
Charles English, Consultant — *Suiza Foods Corporation*

Testimony:

- ✓ Give modified support to the LOL proposal and in opposition to the proposal of CDI and MPC proposals.
- ✓ Oppose Western United's Proposal.
- ✓ Southern California is a deficit market.
- ✓ A reasonable reserve must also be an **available** reserve.
- ✓ The volume of milk committed to Corona Cheese plant and to the Sorrento plant also in Southern California cannot be expected to be part of the reasonable available reserve.
- ✓ Southern California is most certainly a deficit market with respect to SNF.
- ✓ Call provisions were used last year with respect to Southern California.
- ✓ Disagree with CDI in that milk purchased by us is available at a cheaper "cost" than they can provide.
- ✓ Why effectively increase the cost of milk to the Class 1 bottler when the Class 1 bottler is paying the Class 1 price for the privilege of receiving a milk supply.
- ✓ Suggest that CDI's request for a reduction in transportation credit has less to do with the claimed competitive disadvantage and more to do with its over-order pricing intentions should the Department adopt their proposal.
- ✓ Does not believe that there is a cost advantage for South Valley tailored milk.
- ✓ Department's own analysis from last year demonstrate that plant to plant movements are actually more efficient than ranch to plant movements.
- ✓ The 5 cent per cwt shortfall maintained by CDFA should be retained.
- ✓ This is no justification to increase that shortfall.
- ✓ The transportation credit should be increased to a level leaving only the $0.05 shortfall for Riverside or 64.5 cent per cwt.

Post Hearing Brief:

- There was no philosophical support for an open revolution regarding these milk movements provisions, except for Milk Producers Council's official position that they should be abolished.
- Equity is an important factor in any regulatory system.
- Suiza rejects the concepts advanced by MPC and CDI that everyone must be treated alike and that credits and allowances should be equal.
- Equity does not move milk, it takes money to move milk.
- Suiza endorses the LOL transportation credit proposal with a modest shortfall.
- We endorse the concept of including Imperial County as a surplus supply county and San Diego as a deficit county.
- Suiza rejects the concept of CDI's proposal to significantly reduce the transportation credit from the South Valley to Riverside and instead would endorse a proposal to widen the credit's use by applying credits from Artesia to Riverside.
- The need to move milk to Class 1 market remains.
- Southern California has been and remains a deficit market in terms of milk available for the fluid market.
- Southern California and Northern California must be treated differently for transportation credits and allowances.
- LOL transportation credit proposal is fair and equitable.
- LOL's proposal should be modified for a modest shortfall, Imperial and San Diego counties and potential credit from Artesia to Riverside is fair and equitable.
- The industry saves 6.2 cents per cwt on the milk moved.
- The idea that transportation allowances and credits should be equal has merit.
- A modest shortfall, in the applicable federal orders 2 cents per cwt, is established to encourage efficient movements.
- Allowances and credits should both be increased and milk movements from the surplus South Valley region to Southern California need to be encouraged not discouraged.
- Suiza urges rejection of the CDI and MPC proposals.

Sharon Hale, Vice President — *Crystal Cream and Butter Company*

Testimony:

- ✓ The proposal put forth by MPC we are pleased with their recognition of the need for milk movement incentives.
- ✓ Our appreciation however is not sufficient to prevent opposition to this proposal.
- ✓ The proposal fails to consider the differences between markets.
- ✓ We are also opposed to starting allowances at some mileage greater than zero.
- ✓ Our final comment about MPC involves the cost. To us this is an equity issue among participants in the pool and it should be confined to that same group.
- ✓ Opposed to Producers Dairy proposal

- ✓ Believes population growth of this magnitude is sufficient to conclude demand in the Sacramento area remains strong.
- ✓ Sufficient justification for retaining transportation allowances in Northern California has been given.
- ✓ Option II of Producers Dairy's proposal does not appear to be necessary.
- ✓ Transportation allowances apply to all market milk moving from dairy farms to processing plants which process more than 50 percent of their production into Class 1, 2, or 3 products.
- ✓ This is an important component of any milk movement plan.
- ✓ Believes a review of milk movement issues on a periodic basis is warranted.
- ✓ Believes the system should focus on hauling differences between deficit and alternative markets.

Jay Goold and Tiffany LaMendola — *Western United Dairymen*

Testimony:

- ✓ Oppose the proposal to include Imperial County in the list of supply counties for Southern California.
- ✓ The inclusion of San Diego on the list of receiving counties in Southern California seems to be nothing more than a "good neighbor" gesture.
- ✓ If San Diego were included on the list of receiving counties, it would then make them eligible to receive milk from counties in the South Valley.
- ✓ San Diego County is already adequate to meet the needs of that county.
- ✓ See no reason to support Imperial County's proposal to include them.
- ✓ No reason for producers throughout the state to absorb additional transportation costs for the sole purpose of Producers Dairy being able to compete in distant retail markets where milk supplies already exist.
- ✓ Due to lack of sound justification, oppose both options included in the proposal from Producers Dairy.
- ✓ The single rate allowances proposed do not provide adequate disincentives to prevent far out milk from being shipped in at additional cost to all producers.
- ✓ In order to maintain incentives in place to use the least cost approach of hauling the closest milk to the plant, we oppose all components of MPC's proposal.
- ✓ The smaller increase of approximately $0.14 cwt requested by CDI is in keeping with our policy seeking the most efficient movement and is supported by our Board.
- ✓ Oppose to the proposal for credit modification of this magnitude.
- ✓ Support CDI in their proposal to modify the allowance rate to the Bay Area.
- ✓ Support adding Riverside County to the list of Counties indicated in Section 921.2(e) of the Pooling Plan as a receiving area for Southern California.
- ✓ Support adding Santa Barbara to the list of shipping counties in Subsection (e)(2) and deleting Fresno County.
- ✓ Support amending the mileage area to less than 119 miles.
- ✓ Support amending Section 300.2 of the Stabilization and Marketing Plan as proposed by CDI.
- ✓ Conclude that now is the time for the industry to propose that all area differentials be reduced to zero.

- ✓ Final goal will be to eliminate the economic basis for the need to maintain regional quota adjusters.
- ✓ Our point of view relative to the purpose of regional quota adjusters, was developed over an extended period of time during the development of modifications to the California Pooling Plan in 1984. During this time, plant location differentials were replaced by RQA's.
- ✓ RQA's were developed as a means to allocate producer income out of the pool based upon unequal are Class 1 price income into the pool.
- ✓ Again, it is our intention to continue discussions pertaining to Class 1 price differentials and regional quota adjusters and to submit a petition for an additional hearing to the Department.

Jim Battin, Senator — *Thirty–Seventh Senatorial District*

Testimony:

- ✓ In full support of the request submitted by the Imperial County Ag Commissioner.
- ✓ To receive a transportation allowance for dairies, and also to include San Diego County in the Southern California receiving area.
- ✓ It is essential that we provide incentives in Imperial County to enhance growth of the dairy industry.

Exhibits 46 through 49 and 55 — Letters in Support of Imperial County Proposal

46 – Clifford Caldwell, President – El Centro Chamber of Commerce & Visitors Bureau
47 - Duncan Hunter, Member of Congress – U.S. House of Representatives, Washington, DC
48 - Lauren S. Grizzle, Executive Director – Imperial Valley Vegetable Growers Association
49 - Lauren S. Grizzle, Executive Director – Imperial County Farm Bureau
55 - Donald P. Glud, Vice President – Valley Independent Bank