Hearing Panel Report

Based on a Public Hearing Held On
June 3, 2015

Addressing the Class 4b Pricing Formula
Contained in the
Stabilization and Marketing Plans
for Market Milk for the
Northern and Southern California Marketing Areas

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Addressing the Class 4b Pricing Formula
Based Upon a Public Hearing Held on June 3, 2015

This Report of the Hearing Panel regarding proposed amendments to the Stabilization and Marketing Plans for Market Milk for Northern California and Southern California (Plans) is based on evidence received and entered into the Department of Food and Agriculture's hearing record. The evidence includes the Departmental exhibits, written statements and comments received from interested parties, written and oral testimony received at a public hearing held on June 3, 2015, and written post-hearing briefs.

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INTRODUCTION/WITNESSES

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

Two alternative proposals were submitted by:
1. California Dairy Campaign (CDC), Milk Producers Council (MPC), and Western United Dairymen (WUD)
2. Dairy Institute of California (Institute)

A total of 31 witnesses testified including the Department's witness:
CDFA, Mike Francesconi
*CDC/MPC/WUD, Annie AcMoody, Lynne McBride, Rob Vandenheuvel
*Institute, Bill Schiek
*Sacramento Advocates, Inc. for Kraft Foods (Kraft), Barry Brokaw
*Cacique, Inc. (Cacique), Antonio de Cardenas
Joseph Gallo Farms (Gallo), Joe E. Paris
*California Dairies Inc. (CDI), Eric Erba
*Saputo Cheese USA Inc. (Saputo), Greg Dryer
*CDC, Lynne McBride
*Pacific Cheese, Alan Zolin
Farmdale Creamery, Inc. (Farmdale), Scott Hofferber
BESTWHEY, LLC, Barry Murphy
*Hilmar Cheese Company, Inc. (Hilmar), David Ahlem and John Jeter
*Dairy Farmers of America, Inc. (DFA), Elvin Hollon
Pacific Gold Milk Producers, Leonard Vandenburg
*Land O'Lakes, Inc. (LOL), Pete Garbani
Dairy Producer, Xavier Avila
Rizo Lopez Foods, Ivan Rizo
Dairy Producer, Cornell Kasbergen
Alouette Cheese, John Rutherford
R. Doornenbal Dairy, Rien Doornenbal
MPC, Rob Vandenheuvel
Rumiano Cheese Co. (Rumiano), John Rumiano
*Leprino Foods Company (Leprino), Sue Taylor

Special 3-Minute Testimony Given:
Van Warmerdan Dairy, Peter Van Warmerdan
Deniz Dairy, Lucas Deniz
Corda Family Dairy, Jerry Corda
Duarte Dairy, Antoinette Duarte
T-Bar Dairy, Tom Barcellos
FM Ranch, Frank Mendonsa
Los Altos Foods, Adolfo Sanchez
*Agricultural Council of California (Ag Council), Emily Rooney

A total of four witnesses submitted written comments that were entered into the hearing record:
Tony P. Cardoza, Inc., Tony Cardoza
Sierra Nevada Cheese Company, Ben Gregersen
Seifert Dairy, L.P., Joy Seifert
Marquez Brothers International, Inc. (Marquez), Jose T. Maldonado

* Indicates submission of a Post Hearing Brief

THE ALTERNATIVE PROPOSALS

CDC/MPC/WUD

For the period August 1, 2015 to July 31, 2017: Change the dry whey value based on the following schedule (corresponding to the monthly average Dairy Market News (DMN) dry whey price):

Average Western Monthly Dry Whey per lb			Whey Value per cwt
Less than $0.2000			$0.0000
$0.2000	to	$0.2099	$0.0360
$0.2100	to	$0.2199	$0.0968
$0.2200	to	$0.2299	$0.1575
$0.2300	to	$0.2399	$0.2183
$0.2400	to	$0.2499	$0.2791
$0.2500	to	$0.2599	$0.3398
$0.2600	to	$0.2699	$0.4006
$0.2700	to	$0.2799	$0.4614
$0.2800	to	$0.2899	$0.5222
$0.2900	to	$0.2999	$0.5829
$0.3000	to	$0.3099	$0.6437
$0.3100	to	$0.3199	$0.7045
$0.3200	to	$0.3299	$0.7652
$0.3300	to	$0.3399	$0.8260
$0.3400	to	$0.3499	$0.8868
$0.3500	to	$0.3599	$0.9475
$0.3600	to	$0.3699	$1.0083
$0.3700	to	$0.3799	$1.0691
$0.3800	to	$0.3899	$1.1299
$0.3900	to	$0.3999	$1.1906
$0.4000	to	$0.4099	$1.2514
$0.4100	to	$0.4199	$1.3122
$0.4200	to	$0.4299	$1.3729
$0.4300	to	$0.4399	$1.4337
$0.4400	to	$0.4499	$1.4945
$0.4500	to	$0.4599	$1.5552
$0.4600	to	$0.4699	$1.6160
$0.4700	to	$0.4799	$1.6768
$0.4800	to	$0.4899	$1.7376
$0.4900	to	$0.4999	$1.7983
$0.5000	to	$0.5099	$1.8591
$0.5100	to	$0.5199	$1.9199
$0.5200	to	$0.5299	$1.9806

Average Western Monthly Dry Whey per lb			Whey Value per cwt
$0.5300	to	$0.5399	$2.0414
$0.5400	to	$0.5499	$2.1022
$0.5500	to	$0.5599	$2.1629
$0.5600	to	$0.5699	$2.2237
$0.5700	to	$0.5799	$2.2845
$0.5800	to	$0.5899	$2.3453
$0.5900	to	$0.5999	$2.4060
$0.6000	to	$0.6099	$2.4668
$0.6100	to	$0.6199	$2.5276
$0.6200	to	$0.6299	$2.5883
$0.6300	to	$0.6399	$2.6491
$0.6400	to	$0.6499	$2.7099
$0.6500	to	$0.6599	$2.7706
$0.6600	to	$0.6699	$2.8314
$0.6700	to	$0.6799	$2.8922
$0.6800	to	$0.6899	$2.9530
$0.6900	to	$0.6999	$3.0137
$0.7000	to	$0.7099	$3.0745
$0.7100	to	$0.7199	$3.1353
$0.7200	to	$0.7299	$3.1960
$0.7300	to	$0.7399	$3.2568
$0.7400	to	$0.7499	$3.3176
$0.7500	to	$0.7599	$3.3783
$0.7600	to	$0.7699	$3.4391
$0.7700	to	$0.7799	$3.4999
$0.7800	to	$0.7899	$3.5607
$0.7900	to	$0.7999	$3.6214
$0.8000	to	$0.8099	$3.6822
$0.8100	to	$0.8199	$3.7430
$0.8200	to	$0.8299	$3.8037
$0.8300	to	$0.8399	$3.8645
$0.8400	to	$0.8499	$3.9253
$0.8500	to	$0.8599	$3.9860
More than $0.86			$4.0000

Institute

For the period beginning on July 1, 2015 and ending on December 31, 2015: Change the price per hundredweight (cwt.) for the whey factor value, corresponding to the monthly average whey protein concentrate 34% (WPC34) price, based on the following schedule:

Monthly Average WPC34 Price ($/lb.)	***Whey Factor Value ($/cwt.)***
< $0.75	*$0.2500*
≥ $0.75 and < $0.80	*$0.3210*
≥ $0.80 and < $0.85	*$0.4013*
≥ $0.85 and < $0.90	*$0.4816*
≥ $0.90 and < $0.95	*$0.5618*
≥ $0.95 and < $1.00	*$0.6421*
≥ $1.00 and < $1.05	*$0.7224*
≥ $1.05 and < $1.10	*$0.8026*
≥ $1.10 and < $1.15	*$0.8829*
≥ $1.15 and < $1.20	*$0.9631*
≥ $1.20 and < $1.25	*$1.0434*
≥ $1.25 and < $1.30	*$1.1237*
≥ $1.30 and < $1.35	*$1.2039*
≥ $1.35	*$1.2500*

ESTIMATED IMPACTS OF THE ALTERNATIVE PROPOSALS ON CALIFORNIA CLASS AND POOL PRICES

The table below shows the impacts of the proposed amendments on Class 4b and Pool prices relative to current prices from April 2010 through March 2015. The analysis assumes that the alternative proposals and current formulas were in effect throughout the entire period. When a change is a "plus," the proposal would have increased the price and when a change is a "minus," the proposal would have decreased the price.

Table 1 - Estimates of Proposals less Current Class 4b and Pool Prices
12-Month Averages: April-March and 5-Year Averages: April 2010 - March 2015
(Dollars per Hundredweight)

CLASS 4b PRICES	**2010-11**	**2011-12**	**2012-13**	**2013-14**	**2014-15**	**5-Year Average**
CDC/MPC/WUD	$0.76	$1.69	$1.51	$1.64	$1.68	$1.46
Institute	$0.20	$0.55	$0.37	$0.51	$0.42	$0.41
POOL PRICES: QUOTA & OVERBASE						
CDC/MPC/WUD	$0.33	$0.76	$0.69	$0.76	$0.80	$0.67
Institute	$0.09	$0.25	$0.17	$0.24	$0.20	$0.19

Please Note: Historic Prices are not necessarily a good predictor of future prices.

SUMMARY AND IMPACT OF THE ALTERNATIVE PROPOSALS

There were two alternative proposals presented at the current hearing to change the methodology of determining the whey factor in the Class 4b pricing formula. The first, representing producer interests, was submitted by CDC, MPC, and WUD. The second, representing processor interests, was submitted by the Institute. (See pages 5 and 6 for specifics of these proposals)

The producer proposal would replace the current dry whey sliding scale with a scale that closely models the values resulting from the variable factor in the federal order Class III pricing formula. Their proposed scale introduces one-cent steps for the dry whey commodity price and establishes corresponding whey factor values for each step. The scale imposes a floor of $0.00/cwt. on the whey value incorporated into the pricing formula when the DMN dry whey commodity price is less than $0.20 per pound and caps the whey value at $4.00/cwt. when the dry whey commodity price is $0.86 per pound or higher. The producer proposal is constructed in the form of a sliding scale. The effect of the scale is similar to reinstituting a variable factor that models the federal order Class III price, which resembles the type of factor that was in the Class 4b pricing formula from April 2003 to November 2007.

The processor proposal would replace the current dry whey sliding scale with a scale based on the price of whey protein concentrate (WPC) consisting of 34 percent protein (WPC34), as reported by the DMN. Their proposed scale introduces five-cent steps for the WPC34 price and establishes corresponding whey factor values for each step. The scale imposes a floor of $0.25/cwt. on the whey value incorporated into the pricing formula when the WPC34 price is less than $0.75 per pound and caps the whey value at $1.25/cwt. when the WPC34 price is $1.35 per pound or higher. This proposal consists of 14 steps, while the producer proposal consists of 68 steps. Both proposals increase the number of steps compared to the current whey table, which consists of nine steps.

Impact of Proposals

To estimate the impact to the current Class 4b and California Pool prices, the Department analyzed the two proposals assuming that the proposals had been in effect from April 2010 through March 2015. The producer proposal would have resulted in a five-year monthly average increase of $01.46/cwt. in the Class 4b price and a $0.67/cwt. increase in the Pool prices. The processor proposal would have resulted in a five-year monthly average increase of $0.41/cwt. in the Class 4b price and an increase of $0.19/cwt. in the Pool prices. The estimated annual and five-year average price impacts to the current Class 4b and Pool prices are summarized in "*Table 1 – Estimate of Proposals less Current Class 4b and Pool Prices*" found on page 7 of this Panel Report.

INTRODUCTION

The Department called the June 3, 2015 public hearing on its own motion because of concern that current conditions impacting the production of milk and the marketing of dairy products may warrant short-term adjustments to the current pricing levels.

Since 2011, the Department has held six public hearings, including the hearing in question, that have addressed the Class 4b pricing formula and the valuation of whey. The hearing records of each underscore various issues and difficulties faced by the Department when establishing the regulated Class 4b price, which is the price of farm milk utilized for the manufacture of cheese and whey products. The modification and serviceability of different aspects of the Class 4b pricing formula are problematic because of the lack of transparent data. The data the Department used historically to modify the pricing formula are no longer published due to confidentiality. In addition, it is difficult to balance the needs of producers and processors partly because they find themselves on opposite ends of the financial transaction of the sale of the milk and also because they are affected differently by changes in the Class 4b price. These issues and others have been and continue to be at the forefront of Class 4b pricing.

Besides participating in public hearings, dairy stakeholders and the Department have been engaged in industry meetings to find long-term reforms to address issues related to Class 4b pricing and other structural issues related to the milk pricing system in California. In August 2012, the Secretary created the California Dairy Future Task Force (Task Force) that consisted of producers, processors, and representatives of dairy organizations. The Task Force came together with the purpose of working in a collaborative manner to reform the California milk pricing system, in order to create the opportunity for growth and prosperity for both producers and processors in California. Many meetings were held with large and small work groups to identify, analyze, and work towards solutions to the issues facing the industry. During these meetings, both producers and processors recognized that each side was confronted by issues related to the pricing system and worked collaboratively to improve the pricing system for all stakeholders.

By 2014, the work and efforts of the Task Force resulted in a proposed legislative bill that would have provided the foundation to amend the California milk pricing system to address some of the structural issues confronting the dairy industry. Some of these structural issues included: providing flexibility, both inside and outside of the regulated milk pricing system; allowing for milk pricing to be better related to global marketing conditions and the product mix manufactured by California stakeholders; and increased revenue to producers to offset the increased costs associated with feed, environmental regulations, and competing uses for resources. However, the proposed legislation did not move forward or result in the implementation of improvements to the pricing system to address these issues, including those related to Class 4b pricing. Because certain issues continue to affect dairy industry stakeholders, this hearing was held in order to address those issues specifically related to Class 4b pricing.

Similar to previous hearings, the June 3, 2015 hearing record contains opposing testimony regarding the appropriate level of the California Class 4b price. Testimony supporting the producer proposal advocated for increasing the Class 4b price for reasons of producer equity and to narrow the gap between the Class 4b price and the federal order Class III price, which is the price of milk paid by regulated handlers for farm milk used in making cheese and whey products in areas of the U.S. regulated by the United States Department of Agriculture (USDA). Testimony supporting the

processor proposal advocated increasing the Class 4b price in a more modest manner using a new WPC34 price series, which could be more representative of manufacturing conditions faced by California cheese plants than the current price series based on dry whey. Some witnesses at the hearing advocated for not making any changes to the formula, citing current industry conditions do not indicate that changes are warranted.

The hearing record showed that 35 organizations and businesses participated in the hearing. Interested parties testified at the hearing on behalf of 31 organizations and businesses, while four businesses submitted written correspondence that was included in the record. The majority of those entities that participated in the hearing (25) supported one of the two proposals considered at the hearing, both of which increase the level of the Class 4b price. Consistent with previous hearings on the subject, the 17 entities supporting the producer proposal include individual dairy producers, representatives of producer cooperative organizations, representatives of producer trade organizations, and an organization representing California farmers.

The entities supporting the processor proposal included the Institute, an organization representing California processors, and seven proprietary cheese processors. There were five proprietary cheese processors that advocated for no change. Their testimony reflected a lack of support for either of the proposals. Additionally, there were four proprietary cheese processors and one consultant in the whey processing industry that also advocated for no change in the Class 4b price. This last group of witnesses stated, however, that if changes were to be made, they would support changes to the Class 4b pricing formula consistent with the processor proposal that would increase the price level more modestly, compared to the producer proposal.

Generally speaking, most of the topics discussed during the hearing in question were the same as those discussed in previous Class 4b hearings, and much of the testimony provided by witnesses was similar, if not the same. As a result, some discussion of various topics contained in this Panel report will echo the discussion contained in the Panel reports of previous hearings.

When considering the appropriate level of the Class 4b price, the Secretary must take into consideration various relevant factors; such as, those cited in the *"Economic Considerations of the Proposed Changes to the Pricing Formulas"* (see Appendix A), relevant Code sections, relevant economic factors, analysis, public and Department information, and testimony contained in the hearing record. These important considerations are discussed within the following sections of this Panel Report, which examine: how to determine the whey factor; whether to increase the Class 4b price; the appropriate level of an increase to balance the impact to producers and processors; and the duration of an increase.

DETERMINING THE WHEY FACTOR

Issue

Previous hearings held to consider adjustments to the Class 4b pricing formula have illustrated the difficulties faced by the Department while administering and updating the whey factor. The outcomes of these hearings have resulted in various modifications to the manner in which whey is valued in the pricing formula. These hearings have also highlighted the concerns the Department has had with establishing a whey factor that balances the differing needs of industry stakeholders, while meeting statutory directives to promote the orderly marketing of milk and dairy products. This hearing focused on many of these same difficulties and concerns.

In order to balance the differing needs of the industry, the Department has endeavored to utilize the best objective information and data available to connect the value of whey with the relevant economic factors and conditions specific to the California dairy industry. However, certain issues related to the whey factor have consistently created difficulties and challenges in valuing whey. These issues include: limitations of data directly relatable to the actual manufacturing and marketing conditions of California's diverse cheese manufacturers; lack of transparent, California-specific data related to the product prices, yields and manufacturing costs of whey products; and data that the Department cannot publish due to confidentiality. In order to overcome some of these issues of the whey factor, the processor proposal suggested changing the basis of the value of whey in the Class 4b pricing formula from dry whey to WPC34. A review of this proposed methodology, compared with the current one, is warranted in order to determine how best to objectively modify the current whey factor.

Data Related to California Manufacturing and Marketing Conditions

One consistent concern related to the whey factor, and the entire Class 4b pricing formula, is whether each component or factor of the pricing formula relates well to the actual manufacturing processes that occur in processing plants and the marketing conditions of dairy products manufactured in California. By relating the pricing formulas to the actual conditions observed in California plants, the resulting milk prices should be commensurate with the dairy products made from that milk, thus providing a better opportunity for California manufacturers to compete in statewide, national, and international markets. Previous hearing records show that the Department has expressed concern about the efficacy of the whey factor to relate to the actual manufacturing and marketing conditions of California cheese and whey products. The Panel believes that basing the whey factor on WPC34 could potentially improve how the whey factor relates to some, but not all, of the California cheese processors.

Since its inclusion in the Class 4b pricing formula in 2003, the whey factor has used dry whey as the basic commodity. However, since dry whey is produced consistently by only one of approximately 57 California cheese plants, a whey factor based on dry whey does not appear to accurately represent the manufacturing conditions of most California cheese plants. There are 10 California cheese plants that make WPC ranging from 25.0 percent to 89.9 percent protein content. As a group, these 10 plants represent a significant percentage of California cheese production: 96.5 percent, 72.3 percent, and 57.5 percent of California's Cheddar, Mozzarella, and total cheese, respectively. Additionally, testimony indicates that there are some plants that do not make a dried WPC product, but do concentrate their wet whey stream. The revenue derived from selling the concentrated wet whey stream is based on the

WPC34 price, albeit at a reduced rate. Compared to dry whey, it appears that a whey factor based on WPC34 could relate better to a larger portion of California cheese plants.

Despite relating better to some California cheese plants, there are concerns regarding a whey factor based on WPC34. First, the majority of California cheese plants do not recover a value-added product from their whey stream. Some plants sell their wet whey stream for the purpose of animal feed, which may result in some net revenue. Others simply pay a fee to dispose of their whey steam without receiving any revenue in return. In both of these cases, the cheese plant may be financially stressed because an assumed whey value based on either dry whey or WPC34 would not relate well to their actual manufacturing conditions. Even though the hearing record shows that some California and U.S. cheese processors support the concept of the whey factor based on WPC34, various witnesses recognized that this whey factor methodology would not relate well to those plants that recover little or no value from their whey stream.

Second, a whey factor based on WPC34 may not track a whey factor based on dry whey when comparing cheese-milk prices paid by California's out-of-state competitors with California prices. A review of the dry whey price series and WPC34 price series quoted from USDA's DMN, shows the two price series tend to trend up and down together; however, there are occurrences when the two price series will move in opposite directions or when one price series will be relatively constant, while the other is moving. Moreover, a comparison of the per-pound protein price of WPC34 with that of dry whey shows that their price movements are highly correlated, but not perfectly correlated. This indicates that there may be occasions when a whey factor based on WPC34 may move differently than a whey factor based on dry whey. If this led to California milk prices rising at a time when milk prices outside California were decreasing, a competitive disadvantage for California cheese processors could result.

California-Specific Product Price, Yield, and Manufacturing Cost Data

First implemented in 2003, the whey factor followed the typical end-product pricing construct consisting of: a product price, minus a manufacturing cost allowance, times a yield factor. This is still the standard methodology that serves as the foundation for all the California class pricing formulas. The servicing of this end-product pricing construct relies on the annual manufacturing cost studies performed by the Department on California manufacturing plants. These manufacturing cost studies detail the most current data available regarding the actual manufacturing costs and yields observed in California plants that manufacture butter, nonfat dry milk, and Cheddar cheese (studies also included dry whey from 2004-2007 only). These cost studies are key to determining the milk price established by the class pricing formulas.

The Department performed audited manufacturing cost studies on dry whey and publicly released such studies annually from 2004 to 2007. These studies provided the California-specific data needed to adjust the whey factor during these years, based on the actual manufacturing cost and yield data observed in these plants during this time period. However, by 2007, the number of California plants manufacturing dry whey decreased from four to two, with the second plant only intermittently manufacturing dry whey. The Department was unable to continue releasing the manufacturing cost study data because of confidentiality rules regarding the public release of proprietary data. Objectively servicing the whey factor has been difficult since then because the Department has not had access to verifiable, California-specific data, representative of California plants.

The whey factor based on WPC34 appears to have merit, but the concept needs to be vetted further in order to verify and validate the commodity price and manufacturing cost factors that will be associated with the proposed whey factor. The Department needs to examine the proposed DMN WPC34 price series to determine if it will function well as a commodity price series for California. This price series is based on the Western and Central parts of the U.S. Although various witnesses supported this concept, it is prudent to determine if this price series is representative of the price received by California plants. Further, it is unclear if plants making WPC of higher protein concentrations receive a similar price or a price related to the WPC34 price series. If the DMN WPC34 price series is indeed representative, then this concern would be resolved. If not, other alternatives such as a California price survey or other price discovery method would need to be established.

Additionally, the Department is not currently performing any cost studies and is not aware of any cost studies recently completed for plants making WPC34. Before implementing a whey factor based on WPC34, any explicit or implied manufacturing cost allowance and yield factor incorporated into the whey factor should be confirmed and verified as representative of California plants. The Panel is concerned with implementing a new whey factor based on WPC34 that is not accurate and consistent with actual manufacturing conditions of California plants making all types of WPC, including WPC34. Prior to implementing a whey factor based on a new methodology, there should be a thorough examination of this issue in order to ensure it balances the needs of both producers and processors adequately.

Confidential Data Issues

The California dairy industry has been consolidating in both number of dairy farms and dairy manufacturing facilities. The number of manufacturing facilities has been decreasing, while the size of the manufacturing facilities has been increasing. One consequence of this industry consolidation is that in many instances, statistical data on manufactured dairy products and manufacturing costs that were historically published for public use now must be held confidential.

In the case of manufacturing facilities, the statistical data regarding the quantity of dairy products manufactured and manufacturing costs of certain dairy products can no longer be published because there are too few plants manufacturing certain dairy products, or there are dominant manufacturers whose output represents a significant percentage of the total output for the whole state. In either case, the data is considered proprietary to the California manufacturer in question and cannot be released publicly.

The issue with confidentiality currently applies to the Class 4b pricing formula with Cheddar cheese and dry whey. This would also be true with WPC. WPC tends to be categorized into two groups by protein content, with WPC Low (protein content 25.0 to 49.9 percent) and WPC High (protein content 50.0 to 89.9 percent). WPC Low data is confidential due to one dominant manufacturer, while WPC High data is not confidential at this time. In order to overcome the issue of confidentiality, there would probably need to be some sort of cost survey implemented that combines all the California plants making both WPC Low and WPC High. Further evaluation and input from industry stakeholders would be needed to determine the best manner in which to set up such a cost study or obtain usable cost data.

Panel Recommendation

The whey factor has been challenging to administer since its inclusion in the Class 4b pricing formula in 2003, especially after 2007, when verifiable, objective data became limited due to confidentiality. There is merit to the concept of establishing a whey factor based on WPC because it appears more representative of California manufacturing conditions. The Panel believes, however, that further industry discussion and input is required in order to remedy the above-mentioned concerns regarding verifiable cost study information and data confidentiality associated with a whey factor based on WPC.

In addition, the Panel is concerned with the other portions of the Class 4b pricing formula that continue to be affected by data confidentiality and lack of transparent manufacturing cost data. This has been the case since the end of 2011 and has been a topic discussed in the numerous industry meetings held since then. Because of the issues surrounding the entire Class 4b pricing formula, the Task Force considered other methods to pricing cheese-milk as a comprehensive solution. Before investing time and resources into vetting a whey factor based on WPC, the industry needs to not lose sight of the continuing issues with the entire Class 4b formula and whether it may be prudent to create a better pricing alternative altogether.

The Panel recommends continuing to use dry whey as the basis of the whey factor.

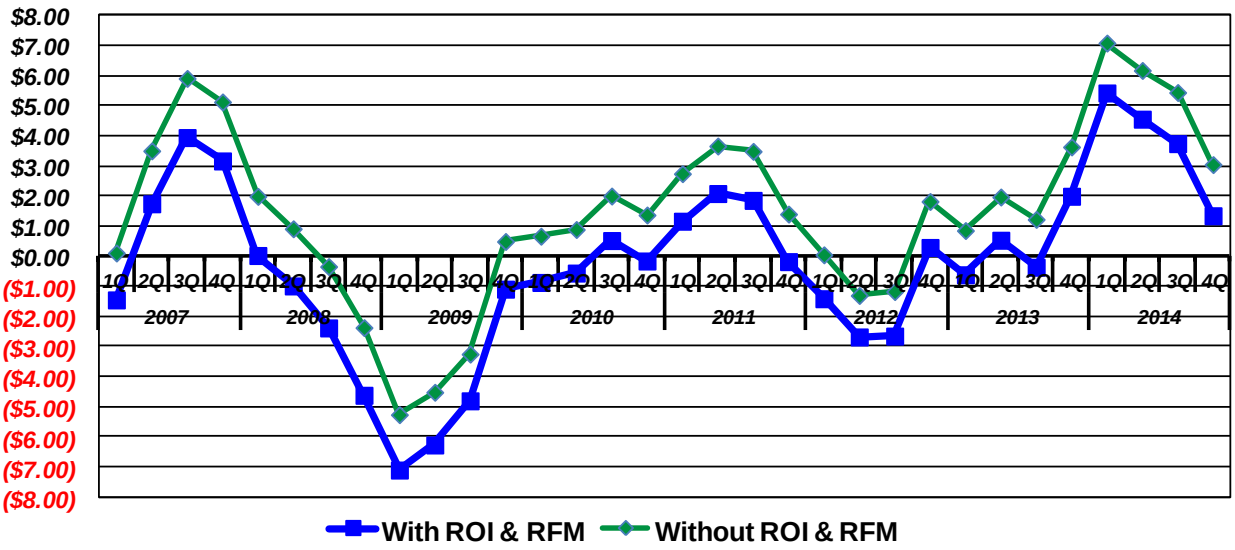
INCREASING THE CLASS 4B PRICE

While there was testimony advocating for no change in the Class 4b price, the majority of the entities that participated in the hearing supported some level of increase in the price. The support for some level of increase came from both the producer and processor sides of the industry. Moreover, the hearing itself was called by the Secretary, on her own motion, to consider changes to the current Class 4b pricing formula that would continue the balancing of opposing interests of producers and processors. Ultimately, when determining whether to increase prices to provide more income to producers, the Department must address certain issues affecting producers and the state's milk supply. Discussion regarding the issues affecting California milk production includes: margins on the dairy; the decreasing number of dairy farms; current milk supplies; and the outlook for future milk production.

Dairy Margins

One principle indicator of the state of milk production is the comparison of the cost of producing milk in relation to the income or price received for milk. This comparison, or margin, provides an indication of the financial conditions facing producers. Like much of agriculture, dairy financial conditions tend to exhibit fluctuations as they cycle through periods of positive and negative margins.

Figure 1: **Difference between California Mailbox Milk Price Less California Cost of Production**
Based on the California Production Cost Survey, with Allowances
January 2007 through December 2014
(In Dollars per Hundredweight)



ROI - Return on Investment
RFM - Return For Management

Data Source: CDFA Dairy Marketing Branch

For each quarter beginning with the first quarter of 2007 to the fourth quarter of 2014, *Figure 1* utilizes the Department's Cost of Production Survey to estimate the difference between mailbox milk prices received for milk and the cost of producing milk, which is a measurement of margins on the dairy. Both the mailbox milk price and the cost of production are based on the dairies participating in the survey. The mailbox milk price consists of quality payments,

component and yield premiums, bonuses, and monthly distribution of cooperative earnings. It is a measurement of the actual income received by producers participating in the Cost of Production Survey. It has been adjusted to account for marketing costs, which are included in the estimated cost of production. The cost of production estimate takes into account allowances for return on investment and return for management.

Figure 1 illustrates the cyclical nature of financial conditions on the dairy. During 2007, 2011, and 2014, dairy margins were positive, with 2014 being a year considered to be one of the best in recent history due primarily to record milk prices. Margins were negative in 2008-2010, 2012, and parts of 2013, with 2008 and 2009 considered two of the worse years in recent history, primarily due to low milk prices caused by global recession.

Increasing the Class 4b price would provide extra producer income and may shift margins upward so that downturns would not extend as low. However, a price increase would not be sufficient for dairies to make up for past losses or recoup lost equity that occurred during past periods of negative margins. Additionally, it is not possible to counteract the influences of key determinants of milk prices and costs of production that contribute to dairy producer margins. The supply and demand conditions of farm milk and dairy products, both domestically and globally, influence the income derived from the sale of farm milk in California. The movements in supply and demand generally transpire independent of milk pricing regulations and are not conditions that can be controlled by milk pricing regulations. The key determinants of the cost of production on the dairy are also determined independent of milk pricing regulations. As a result, the cyclical movements of margins on the dairy cannot be remedied through regulated price increases.

The Loss of Dairies

The total number of California dairies has been a topic frequently discussed for many years, especially since the time period from 2008 to 2010 when negative margins on the dairy were financially devastating. Testimony indicated that many dairies went out of business as a result of negative operating margins and loss of equity, experienced during the last few downward cycles. Anecdotal evidence available to the Department supports the concept that there are dairies that were unable to weather the downturn in dairy margins and have closed down.

In addition to dairy closure caused by financial stress, the Panel is aware that there are other factors contributing to the loss of dairies in California, which include consolidation of the industry and retirement. Department data show that there has been a constant consolidation of California dairies that has been occurring for decades. Over the years dairies have become larger, have milked more cows, and developed economies of scale, which often create per unit cost advantages over smaller dairies. Over time, smaller dairies are not able to compete and as a result, exit the industry. This phenomenon is exacerbated during periods of financial stress, and the Panel believes that the consolidation trend has continued during the last few years, albeit accelerated by the last few downturns in dairy margins.

Furthermore, the Panel is aware that some producers have exited the industry due to timing and retirement. USDA and Department data show that from early spring 2014 to the present, replacement cow, replacement springers, cull beef, and calf prices have all risen to relatively high levels compared with previous years. These high prices have proven to be advantageous for producers seeking to retire or leave the dairy business because the monies obtained through the sale of these animals have allowed some producers to pay off debt

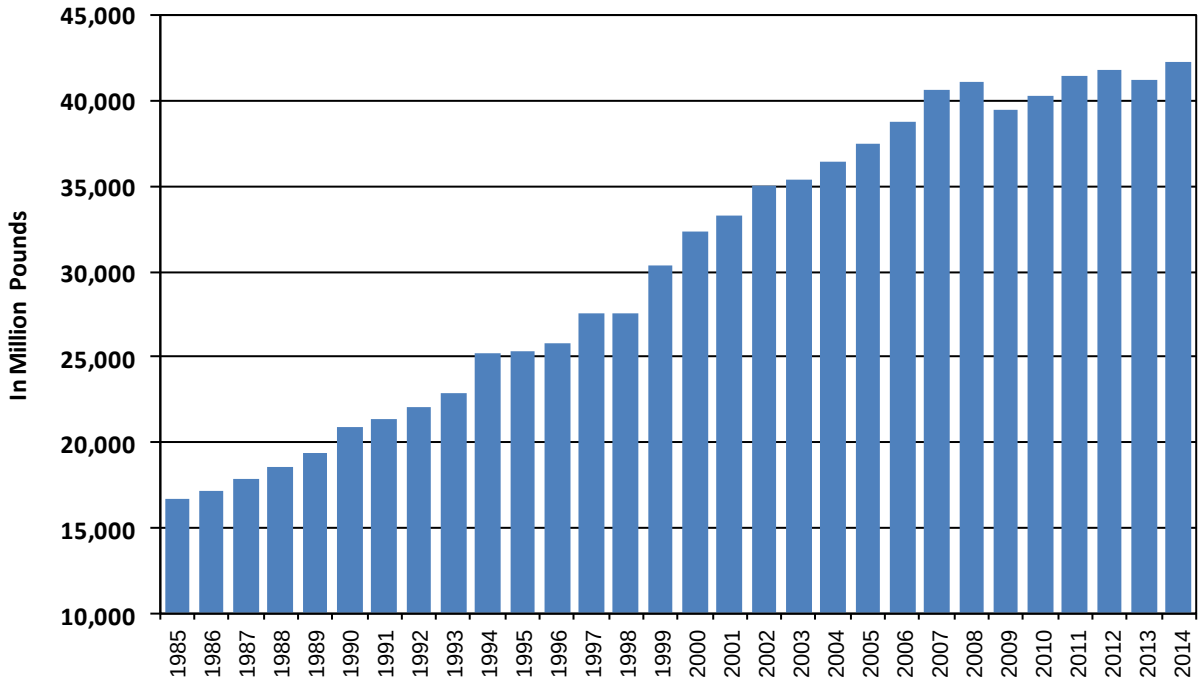
and/or have the funds necessary to retire. The high price of farmland and the value obtained from the dairy infrastructure, have also contributed to these trends.

The number of operating dairies in California, and throughout the U.S., has been declining for many years and continues to decline. The Panel recognizes that one reason for the decline had been financial stress when margins were squeezed and the subsequent loss of equity incurred as a result. The Panel also believes that the continuing trend of consolidation and dairies leaving the industry have also contributed to the decline of dairies. An important economic implication from the loss of dairies is the effect that this has had on the state's historic and current milk supplies, and more importantly, the effect it will have on future milk supplies.

Present and Future Milk Production

Even though dairy numbers have steadily declined for decades, both the size of dairies and the average number of cows being milked on dairies have steadily grown. The hearing record shows that milk production grew at an average rate of approximately three to four percent over the few decades leading up to the year 2008. During this time, cow numbers were increasing and the California milk trend outlook was one of consistent annual increases. Since 2008, this ever-increasing trend in milk production appears to have changed: California milk production has deviated from an upward trend by exhibiting more cyclical movements as evidenced by more frequent upward and downward movements in annual milk production, and a generally flat trend since 2008.

Figure 2: **California Milk Production, 1985-2014**



Source: CDFA Dairy Marketing Branch

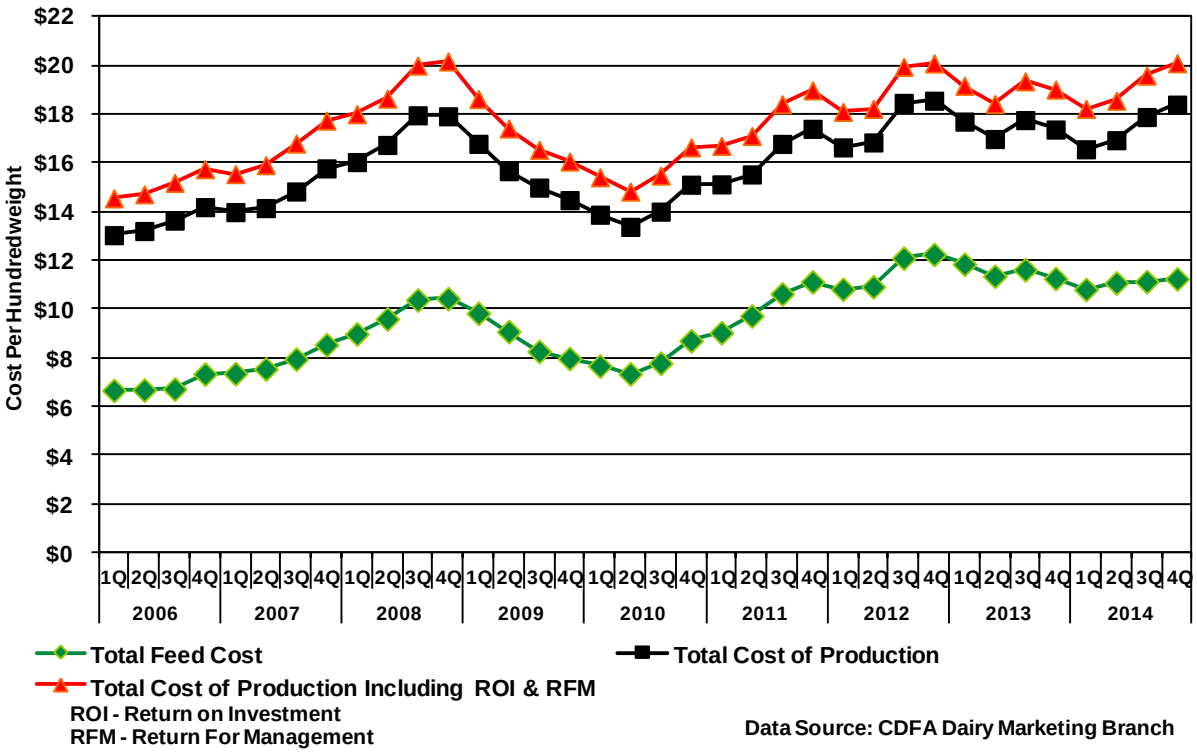
Figure 2 shows total California milk production from 1985 to 2014 and illustrates this new movement in milk production. Starting in 2008, milk production declined in 2009, increased in 2010-2012, decreased again in 2013, only to be followed by an increase in 2014. For every

month in 2015 so far, year-over-year milk production has been declining and is expected to continue to decline, with year-to-date 2015 milk production levels comparable to those of 2008. It appears that the trend in the state's milk production has changed course since 2008 and the outlook for future milk production appears to be the same. This new outlook is supported by the combined effects of structural changes in the cost of feed, environmental regulations and costs, competition for land use, and more recently, the effects of drought.

Feed Costs

Based on the Department's Cost of Production Survey prior to 2008, average statewide feed costs generally fluctuated in a range from $6 to $8 per cwt., with average statewide total cost of production ranging from $13 to $15 per cwt. However, after 2008, statewide average feed costs rose to a new plane, fluctuating from $10 to $12 per cwt., causing statewide average total cost of production to also rise to a new plane, fluctuating from $18 to $20 per cwt. *(see Figure 3).* Although these costs do move up and down according to conditions affecting feed markets, these fluctuations have occurred in a higher plane compared with pre-2008 years. This trend is likely to continue, as evidenced by the records of previous hearings and the current hearing. Because feed costs are the principle cost of producing milk, one of the main drivers of milk production decisions and the total cost to produce milk are feed costs. Ultimately, this structural change in the level of feed costs, and its associated affect on total cost of production, has recently limited the growth potential in milk production and is expected to continue to limit it.

Figure 3: **California Cost of Production, by Quarter**
Based on California Cost of Production Survey
January 2006 through December 2014



Environmental Costs and Regulations

Another factor contributing to the changing milk production trend is environmental regulations and their costs. Over the last decade, the explicit costs to comply with environmental (air and water) regulations have increased. Besides explicit costs, the time and resources needed to comply with such regulations have also increased. Environmental regulations require costly economic impact reports to be generated when establishing a new dairy or to reactivate an existing, idle dairy with lapsed permits. Regulations and permitting also create caps on the number of cows that can be milked on existing and new dairies and impede the process of re-permitting an existing dairy to add more cows.

All of these environmental costs and regulations have limited the ability of producers to expand their production. Historically, producers seeking to increase production built new dairies and expanded the number of cows on existing facilities. Conversely, environmental costs and regulations have severely limited the building of new dairies, the reactivation of dormant dairies, and reduced the re-permitting of existing dairies. Because current environmental costs and regulations are expected to remain in place, if not intensify, they are expected to limit the ability of production to grow in the future through the traditional method of adding dairies or adding a significant number of cows to the milking herd.

Land Use Competition and Drought

Over the last number of years, the amount of farmable land in California utilized in the production of agricultural products not associated with milk production, particularly tree nuts and grapes, has grown. Over the recent past, the net return for these agricultural products has increased dramatically and eclipsed the return available for other agricultural products, including feed grown for milk cows. As a result of the return and profitability of tree nuts and grapes, land use has shifted out of the production of milk cow feed and even milk production facilities. Testimony provided at the hearing indicated that land previously used to grow feed, such as alfalfa hay and corn silage, has been changed to grow tree nuts and grapes. Further testimony indicated that some dairy facilities have been removed in order to utilize the land for tree nuts. The incentive to use farmable land for these other agricultural products creates competition with the inputs to milk production that appear likely to continue in the future.

In addition to land use competition, drought in California also impacts the inputs needed for milk production. As California enters its fourth year of drought, its effects on the dairy industry seem to be intensifying. Reduced water supplies in the state are influencing feed availability and costs. Testimony indicated that the cost of water and the lack of water are causing farmable land acres used for corn silage and alfalfa to be reduced, left fallow, or switched to the production of other feed, like sorghum that uses less water, but contains lower nutritional qualities. Costs to obtain underground water are also rising. As surface water has diminished, farmers have drilled new wells to access underground water. Additionally, the water table level has been declining in California, forcing new and existing wells to be drilled deeper, which are more costly and bring high utility costs associated with the pumping of groundwater from further below the surface.

In the end, the effects of drought and land use competition are similar. Both of these factors reduce the availability or access to locally grown feed. When less feed is grown locally, it must be purchased from regional, more-distant areas at a higher cost. These higher costs are associated with transportation to California. Testimony at the hearing provided evidence that these higher costs affect dairies more severely when margins are reduced, which currently

appears to be the case. Preliminary Department data point to declining margins in the first quarter of 2015 and into the second quarter.

The Decision to Increase the Class 4b Price

When reviewing the combined effects of elevated feed costs, environmental regulations, land use competition, and drought, it appears that future milk production conditions in California will resemble those observed since 2008. The Panel believes that large increases in milk production will be limited and that milk production increases will be primarily achieved through increases in milk per cow output, which is influenced by feed quality and management practices. The milk production increase of 2014 provides evidence of this. Department data show that this production increase occurred primarily through milk per cow increases rather than through an increase in cows, even though producers were responding to a year with record milk prices and revenue. Prior to 2008, producers generally increased production during years of high milk prices through the addition of cows. It seems likely that milk production will continue to cycle though periods of higher and lower production, in which production is relatively flat, and stable, but fluctuating within the range observed since 2008. Testimony by two witnesses from organizations receiving milk from large numbers of dairy producers, support the view that the state's future milk supply should be stable and sustainable, will probably not return to an environment of significant increases observed prior to 2008, and will probably be vulnerable or susceptible to above mentioned factors currently affecting production.

By the time of this hearing, a clear track record of milk production conditions has been established that shows the milk production response has been different over the course of the last six-to-seven years. Over this time, producers have experienced a complete spectrum of financial conditions on the dairy, ranging from large negative margins to large positive margins. However, even the large positive margins of 2014 were not enough to invoke production growth similar to the pre-2008 time frame, based on expansion rather than milk per cow increases. In light of this new track record of milk production, which appears influenced by the factors examined above, the Panel believes an increase in the Class 4b price to provide more income to producers is warranted. The level and duration of the increase to the Class 4b pricing formula is discussed in the following section that examines: price alignment between the Class 4b and Class III pricing formulas; the impact of price increases to industry stakeholders; and setting the level and duration of the price increase.

The Panel recommends increasing the Class 4b price.

LEVEL AND DURATION OF ADJUSTMENT TO THE CLASS 4B PRICE

Issue

Previous hearings held to consider adjustments to all class pricing formulas, especially the Class 4b pricing formula, have illustrated the difficulties confronting the Department while administering and updating these pricing formulas. Because producers and processors find themselves on opposite ends of the financial transaction of the sale of the milk, any change to the pricing formulas will inevitability affect one side of the industry negatively while positively affecting the other. Furthermore, individual cheese processor operations are affected differently by Class 4b price changes because they vary in regards to size, efficiency, and whey processing investment. Producer operations are also affected differently by Class 4b price changes depending on whether or not they ship milk to a cheese processor that pays premiums for quality or high milk component tests.

When determining the appropriate level of a Class 4b price increase, the Department must consider various factors to balance the needs of producers and processors while maintaining an adequate milk supply in relation to the demand for milk. Many of these factors have been discussed at length in previous hearings and will be examined again in this section of this Panel Report. These factors are related to: the price alignment observed between the Class 4b price and the federal Order Class III price; the varied impact to dairy stakeholders from an increase in the Class 4b price; the appropriate level of price increase; and the duration of the price increase.

Price Alignment between the Class 4b and Class III Prices

One consistent topic discussed at Class 4b pricing hearings is that of the alignment of the California Class 4b price and the federal Order Class III price. In general, witnesses supporting producer interests have argued that the Class 4b price should be set at a level equal to the Class III price or as close as possible to it. They assert that this argument is supported by the Code, specifically Section 62062. Witnesses supporting processor interests have argued that there are a number of economic factors that should be considered when determining the appropriate level of the Class 4b price, not just the comparison between the Classes 4b and Class III prices. As cited in previous hearings, the Panel continues to believe that a number of factors should be considered when establishing an appropriate Class 4b price level. These factors are associated with the mandates of the Code, the difference between the California and federal order systems, and California-specific marketing conditions.

The Code

Witnesses supporting producer interests have consistently asserted that Code Section 62062 provides the main directive when establishing the appropriate level of the Class 4b price. These witnesses have cited a portion of Section 62062 that states, “If the director adopts methods or formulas in the Plan for designation of prices, the methods or formulas shall be reasonably calculated to result in prices that are in a reasonable and sound economic relationship with the national value of manufactured milk products.” They assert that the Class III price is a national benchmark price for cheese milk, making it synonymous with the national value of cheese milk sold for manufactured milk products. They further argue that setting the Class 4b price equal to the Class III prices will establish a reasonable and sound economic relationship as outlined in Section 62062, even though this Code section

references a relationship with the value of “manufactured milk products” not any specific milk price, such as the Class III Price.

The Panel continues to believe that the language quoted by producer witnesses from Code Section 62062 provides the Secretary with an important directive to consider when setting milk prices. However, there are other portions of Section 62062 and other Code sections that provide the Secretary with additional, essential directives to consider when setting prices. These further directives include relevant economic factors and high-level, overarching mandates to ensure stability in the California marketplace for farm milk and dairy products. A more detailed review of these other directives from the Code is found in Appendix B, which mainly consists of excerpts from the Panel Report from the hearing held on May 31 and June 1, 2012. Although a reasonable and sound economic relationship with the national value of manufactured milk products is one factor to consider when establishing milk prices, there are many other specifically cited factors, other relevant economic factors, and statutory directives that the Secretary must consider when determining the appropriate level of milk prices to balance the needs of stakeholders. One of these other considerations is the difference in the minimum pricing regulations in California and federal orders.

Pricing Regulations in California and Federal Orders

Another recurring topic discussed in Class 4b pricing hearings is whether a direct comparison between the Class 4b and Class III prices is appropriate. Witnesses supporting producer interests have stated that the minimum pricing and pooling regulations of California and federal orders are similar enough to support the concept that the Class 4b and Class III prices should be directly comparable. While they admit that the two systems are not identical, they argue that the similarities are great enough to warrant direct comparison. Witnesses supporting processor interests generally argue that the ability for milk to escape minimum pricing regulations in federal orders, but not in California, creates a key difference in the two systems that make direct comparisons unwarranted.

One principle difference between the California and federal order systems is the ability in federal orders to ‘escape’ regulated minimum prices by paying a lower price for milk than the announced class prices for milk used to make manufactured products (milk used to manufacture cultured and frozen dairy products, butter, dry milk powders, cheese, and whey products). Although it appears that much of the milk marketed in federal order areas is priced at least at the announced class price, there is evidence that a significant percentage of milk in federal order areas is marketed outside of the regulated price. A representative of a producer organization cited USDA data from 2014 showing that 79 percent, 129.4 billion pounds out of the 163.7 billion pounds, of the milk produced outside of California was sold to regulated handlers in the federal order system. Correcting for the estimated quantity of milk from states outside of California not regulated by federal orders, an estimated 7 to 10 percent of the milk produced in federal order areas appears to be marketed outside of the regulated price. The Panel believes that this percentage of unregulated milk is significant and important to the overall marketing of milk in those areas.

The records from previous hearings and the current hearing show that there are circumstances in federal orders that lead to milk being purchased below the announced class price. Some milk is not pooled based on monthly decisions by handlers due to pricing considerations. Although data is not available showing at what price this milk was sold, this milk is not required to be sold at the announced class price. Some plants in federal orders are non-Pool plants that regularly purchase milk below the announced class price. Some milk is

sold below announced class prices under temporary circumstances, such as over weekends or holidays, when milk is diverted from bottling plants to manufacturing plants in order to be processed. Additionally, some milk is sold below announced class during periods when milk supplies exceed the demand for milk by manufacturers in the area. This often occurs during the spring flush when milk production is at cyclical highs. Evidence in the hearing record indicates this has occurred in past years and has been occurring this year. The opportunity to market milk below announced class prices provides flexibility in the federal order system to allow the market to clear when the announced class price for milk would be too high to provide an incentive for manufacturers to purchase such milk.

While the federal order system provides circumstances that allow milk to be sold below announced class prices, California statutes do not. In California, manufacturers must pay at least the regulated minimum class price for Grade A milk, regardless of their Pool status. There is no flexibility in the California system that allows for California milk to be sold below the minimum class price, even when conditions exist that would cause milk to be sold below the announced class price in order to clear the market, such as in federal orders. Because there are quantities of milk purchased below announced class prices in federal orders under circumstances not permitted in the California system, a strict comparison of the Class 4b and Class III prices is not appropriate. The Panel believes that the price alignment between the two prices can serve as a starting point when determining the appropriate level of the Class 4b price. However, the two prices should not be set equal to each other because of the differences in the California and federal order systems regarding how milk clears the market, and because of California-specific marketing conditions, discussed in the next section.

California Marketing Conditions

As discussed previously in this Panel Report, California has experienced a long-term growth trend in milk production and has been the largest milk producing state since the early 1990s. The majority of the state's milk production growth has been directed to the production of Class 4a and 4b manufactured products. Because the large quantities of manufactured dairy products produced in the state eventually exceeded the demand for such products within the state, California transformed into a net exporter of dairy products. The marketing of these products is now predicated on them being sold in U.S. and global markets. The growth of California's milk supply and subsequent growth in manufactured dairy products create the need to examine certain economic factors that should be considered when increasing the regulated price. Two of these economic factors that warrant an examination are the state's plant capacity and the marketing of dairy products to distant markets outside California.

As the state's milk supplies steadily increased, new manufacturing plants were built in order to process the growing supply. However, the growth in new manufacturing capacity did not always correspond exactly with that of the milk production growth. This caused time periods when the milk supply exceeded plant capacity. Department data and previous hearing records show this was a concern in the early 1980s, in 2007 and 2008, and finally in 2011 and 2012. When the state's milk supply exceeds plant capacity, disorderly marketing conditions can occur that negatively affect the industry. For this reason, plant capacity has been a reoccurring issue evaluated during previous hearings.

Presently, it appears that the state's milk supply in the aggregate, is in relative balance with the state's processing capacity. Although milk production is cyclically high in the spring causing temporary excess milk supplies and low in the fall causing temporary shortfalls, consistent surplus and shortages of milk supplies outside of these times of the year are an

indication of an imbalance. Department data and hearing testimony suggest that the overall balance of the state's milk supplies with plant capacity has not been problematic and is not anticipated to become problematic because milk production is not expected to increase dramatically. However, this issue should be continually monitored because conditions can always change in the future.

Besides plant capacity, the marketing conditions facing the California industry, as it sells its products across the U.S. and to the world, create a certain marketing reality. As a net exporter of dairy products, California manufacturers must be able to compete with other manufacturers for buyers in distant markets. In order to do so, transportation costs to ship product to distant markets must be considered when setting regulated prices. Hearing testimony indicates that California products are sold across the U.S., including the East Coast. In order to compete with other U.S. dairy manufacturers that are situated east of California and closer to these markets, there must be transportation cost considerations accounted for in the price manufacturers pay for milk. Because California is situated on the West Coast, basic economic theory would suggest that the regulated price for milk used in products sold in the Eastern U.S. would need to be lower than the regulated price of milk paid by manufacturers situated closer to these markets.

Besides transportation costs, the marketing conditions of California dairy products have been evolving. The California dairy industry markets a significant quantity of its products globally. Factors influencing the global marketplace include changes in the global demand of dairy products, global milk production, competition from global competitors, extreme weather events, etc. These economic factors are becoming increasingly important to the California dairy industry. The Panel believes they must be considered when establishing California milk prices; even though, there currently are no factors in the current pricing formula that explicitly account for these economic conditions. In the end, it is necessary for California milk prices to be somewhat lower than other areas of the country due to California specific marketing conditions and as well as the difference in how regulated prices in other parts of the U.S. are determined. Both of these factors and others make strict price alignment between California and other areas of the country inappropriate.

Impact of Price Increase to Industry Stakeholders

An increase to the Class 4b price would result in direct financial impacts to both producers and processors. In general, producers would receive higher Pool prices and income through the Pool. Generally, cheese processors would have their current margins reduced due to higher milk costs, which represents the largest portion of the cost to produce cheese. Despite these predictable financial outcomes, an increase in the Class 4b price would impact dairy stakeholders differently.

The size, efficiency, and whey processing investments of cheese processors influence how cheese processors would be able to adjust to Class 4b price increases. Cheese processors can be segmented based primarily on the size of the operation and whether they have invested in equipment to process their whey stream. There are a few large cheese processors in the state that have invested in whey processing equipment to manufacture value-added, dry whey products. These processors will be better able to adjust to price increases. Hearing testimony and Department data indicate that these large processors have a sufficient margin to pay premiums on top of the regulated price, with the premium payments based primarily on quality and milk component tests. Assuming any Class 4b price increase is smaller than the premiums paid for milk, it is anticipated that these cheese processors will

simply allocate the money normally paid in premiums to the Class 4b price increase. There may not be a net change to these processors.

Some cheese processors that are smaller in scale have also invested in equipment to process their whey stream and manufacture value-added, dried whey products. These processors do not necessarily pay quality and component test premiums like larger processors. An increase in the Class 4b price will simply reduce their profit margin. Their ability to adjust to the price increase will depend on the combined margins resulting from both their cheese and whey processing operations. Still other cheese processors have invested in equipment to condense their whey stream into a liquid whey concentrate product. The revenue generated from this liquid product is lesser in comparison to the revenue generated from a dried product, if revenue is generated at all by the sale of the whey stream. The impact of a price increase to these cheese processors is greater because it is likely that the margin observed from the liquid whey processing operation is lower.

Finally, the small or medium-sized cheese processors that do not process their whey stream at all are likely the most vulnerable to Class 4b price increases. Like prior hearings, there has been much debate regarding the impact to these cheese processors. Because these cheese processors generally receive no revenue from their whey stream, or a minimal amount if they sell it for animal feed, they most likely incur a net cost to dispose of it. Any increase in the Class 4b price simply increases the cost to these processors that could impact the margin on their cheese making operation. Testimony submitted at the hearing indicate that the margins faced by these processors may not be large enough to offset the increased cost, which may be problematic.

The Panel is cognizant that cheese processors are impacted in different ways by increases in the Class 4b price. Cheese processors are impacted based on various factors, such as: whey processing investments as described above; price and income sensitivity of the consumers purchasing different types of cheeses; how well the actual manufacturing conditions of different processors relate to the current Class 4b pricing formula in its entirety; and whether cheese processors have multiple manufacturing facilities inside and outside of California. These factors, and others, make it difficult to predict exactly how each individual processor will be impacted, but economic theory would suggest milk procurement and cheese production would inevitability decrease for some processors.

It is likely that a price increase will cause some cheese processors to reduce their milk intakes and produce less cheese as their margins are reduced and their competitive position in the marketplace changes. From 2007-2014 (a time period of increasing Class 4b prices resulting from hearings), Department data show that total cheese production by processors that do not process whey decreased by 14.3 percent over the 7 year period. It is possible that this group of cheese processors will procure less milk and make less cheese in the face of a Class 4b price increase. During this same 2007-2014 period, cheese production by processors that currently process whey increased by approximately 28.6 percent over the 7 year period. However, it is unclear if the milk intake and subsequent cheese production by this group will continue to increase, remain constant at current levels, or decline in the aggregate. This may be dependent on the level and duration of the increase, which are examined in a subsequent section of this Panel Report.

While cheese processors are impacted differently by Class 4b price increases, producers will also be impacted differently depending on where they ship their milk. An increase in the Class 4b price will lead to increased Pool prices for producers that participate in the Pool.

However, there are some producers that may experience a decrease in income as a result of a Class 4b price increase. Some producers that ship to certain cheese processors receive individualized premiums based on the quality and milk component tests of their milk. If the Class 4b price increase were to result in decreased premium payouts from these cheese processors in an amount equal to or greater than the Class 4b price increase, then these producers would experience lower incomes. The reason these producers would receive lower income is because they would lose the premium payout and receive in return the higher Pool price payout. However, the Pool price increase will be less than the lost premium, which would lower income.

In the end, any Class 4b price increase will end up affecting cheese processors and producers differently. The different impacts to different stakeholders make balancing the needs of the industry difficult. These differing impacts are unavoidable because current California statutes require processors to pay the same regulated, minimum price for California Grade A milk utilized for the same purpose and require revenue to be shared in a certain manner in the statewide Pool. As long as California statutes continue in their current form, the balancing of stakeholder needs will be difficult, with variable impacts to California's diverse stakeholders. These variable impacts to stakeholders may be remedied by structural reforms to the pricing system to allow for greater milk pricing flexibility.

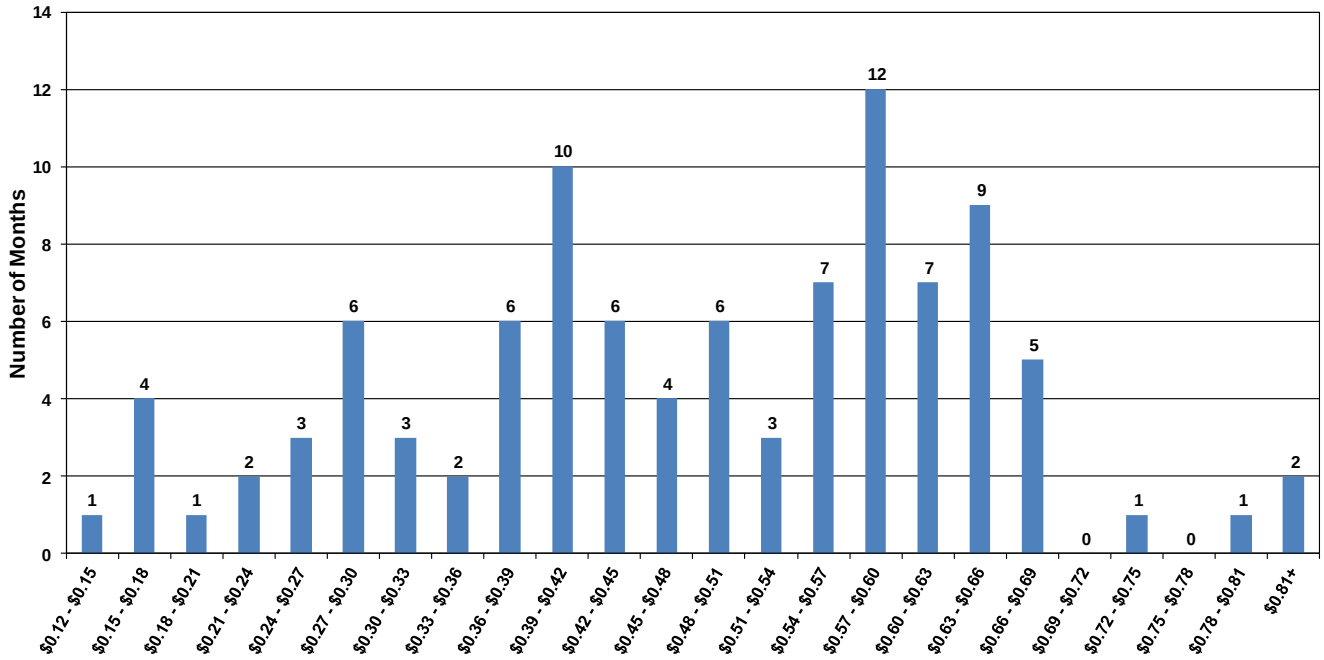
Level of Price Increase – Modification to the Whey Scale

As reviewed previously in this Panel Report, two different proposals that increase the Class 4b price, for a temporary time period, were submitted at the hearing. Each proposal recommended modifications to the current dry whey scale in order to balance the needs of producers and processors. In reviewing the construct of each proposal, the Panel believes that the whey scales recommended in the two alternative proposals cannot be accepted and implemented in their proposed forms. The processor dry whey scale, based on WPC34, appears to have merit but requires further vetting in order to appropriately implement it in the future, if found suitable. The producer dry whey scale essentially uses a strict price alignment approach to establishing a whey value similar to the federal order whey value incorporated in the Class III pricing formula. As discussed previously, strict price alignment is not appropriate. Although the Panel believes the two proposals should not be implemented as proposed, there are aspects of each proposal that can be used to modify the current dry whey scale.

To begin with, each proposal suggested increasing the number of steps of the scale. Increasing the number of steps allows for a smoother change in the whey value as the dry whey commodity price moves with the market. In general, this allows the whey factor to be more responsive to changes in the dry whey market. The Panel reviewed a few options for increasing the number of steps in the dry whey scale that would allow for a desired increase in the Class 4b price. An option that appeared appropriate was a dry whey scale based on three-cent steps.

Figure 4 shows the distribution of monthly DMN dry whey prices used in the Class 4b pricing formula across three-cent steps starting at $0.12 and ending at $0.81. The majority of the monthly prices from January 2007 to May 2015 (75 out of 101) seem to fall in the steps between $0.30 and $0.66, which may indicate the range where future monthly prices may fluctuate. Although it is difficult to foresee what the value of the dry whey price may be in the future, the numbers of historic monthly prices that fall within the three-cent steps in this range appear somewhat evenly distributed and may allow for a smoother transition between the steps of this dry whey scale compared with the current table based on five-cent steps.

Figure 4: **Distribution of Monthly DMN Dry Whey Prices by Specified Ranges, January 2007-May 2015**



Besides the construct of the steps of the dry whey scale, a cap and floor that limit whey values on the upper and lower ends of the scale, respectively, are important. The current dry whey scale has a cap and floor and the two proposals suggest maintaining caps and floors, albeit at different levels. A further review of *Figure 4* shows that the monthly dry whey prices below $.30 correspond to periods of very low prices in 2008 and 2009 when the dry whey market was at historically low values. Many of the monthly dry whey prices above $0.60 correspond to periods of very high prices in the years 2007 and 2014. Because these periods of very low and high prices tend to occur infrequently and do not appear to be the norm, the Panel believes that the dry whey scale should maintain a cap and floor directed at these very high and low prices, albeit with a slight modification to the floor. While the cap appears to be appropriate at $0.60, the floor requires being changed from a dry whey price of $0.25 to a different level because the Panel's recommended dry whey scale will have steps in increments of three cents. Using the producer proposed scale as a guide, the Panel recommends modifying the floor to a dry price below $0.21.

The final consideration of a modification to the dry whey scale is an adjustment to the level of whey values that correspond to each step. In order to increase the Class 4b price, the level of whey values that correspond to the steps must be increased. The Panel examined different scenarios and reviewed the estimated impact of each scenario to the Class 4b price, Pool prices, and the alignment between the Class 4b and Class III prices. A dry whey scale that seems to provide an appropriate balance, applying the economic factors cited in this Panel Report, has: a floor whey value of $0.00 per cwt. for dry whey prices below $0.21; a cap whey value of $1.55 per cwt. for dry whey prices above $0.60; and whey values ranging from $0.25 to $1.45 per cwt. for dry whey prices between the floor and cap. The recommended dry whey scale can be found in the Summary of Panel Recommendations section of this Panel Report.

In summary, the Panel-recommended dry whey scale modifies the current dry whey scale in three ways. First, it increases the number of steps to allow for a smoother transition between the steps as the monthly dry whey price moves with the market. Second, it increases the

whey value at the cap from $0.75 per cwt. to $1.55 per cwt. and increases the change in the whey values between the steps from $0.0625 per cwt. to $0.10 per cwt. This provides an increase in whey values corresponding to every step above a dry whey price of $0.25. Finally, it decreases the floor whey value from $0.25 per cwt. to $0.00 per cwt., which matches the floor whey value of the producer proposal. This floored whey value at $0.00 per cwt. seems to protect producers from negative whey values at the floor, while the cap protects processors from large, positive whey values.

Duration of Price Increase

When considering price changes, one important consideration is the sound, economic relationship between the production of milk and the marketing conditions of the products manufactured from milk. When a sound economic relationship exists, the Department is able to promote, foster, and encourage the intelligent production and orderly marketing of milk products, which is one overarching mandate from the Code. When this sound economic relationship deteriorates for any reason, disorderly marketing conditions may ensue, which would point to the Department taking action to respond to the situation. Because the relationship between milk production and the marketing of dairy products may change in the future, it appears prudent to implement a price increase of relatively short duration with the aim to also reevaluate the adequacy and viability of the increase as time passes.

It is difficult to predict how milk and dairy product markets may change in the future. As a result, it is prudent that the duration of the price change should not be so long that negative marketing conditions are likely to occur, but not so short that there is not data available to monitor how the industry responds to the new price. Milk production is cyclical and seems to go through one entire cycle over the course of a year. Milk production tends to build in the winter, peak in the spring, decline over the summer, and bottom out in the fall. Industry analysts tend to examine milk production based on its one year cycle. Analysts also tend to examine how milk procurement and how dairy product manufacturing and marketing conditions respond to the milk production cycle. Moreover, analysts evaluate current conditions based on observed conditions during the same period of the previous year. Since dairy data is analyzed on an annual basis, the Panel believes that a one year time period would be appropriate in order to evaluate how the markets respond to the price increase and how market conditions may change, based on other economic factors.

Although the Panel recommends a price change lasting one year, the Panel is cognizant that the conditions affecting milk production and the manufacturing and marketing of dairy products are volatile and can change rapidly. Unpredictable changes in the markets for milk production, milk procurement, and dairy products may occur independently of regulatory changes implemented by the Department. There simply are numerous economic factors that could lead to dramatic changes in the milk and dairy product markets that may cause a negative outcome, such as disorderly marketing conditions and milk supply to plant capacity imbalances. If the Class 4b price change or any other circumstance were to lead to deterioration in market conditions, then the Department and the industry would need to reevaluate the adequacy and viability of the Class 4b price.

Panel Recommendation

The Panel recommends modifications to the steps and values of the dry whey scale for a period of one year.

SUMMARY OF PANEL RECOMMENDATIONS

Because of the significant issues influencing the production of milk in California, the Panel recommends the following:

- The Panel recommends continuing to use dry whey as the basis of the whey factor.
- The Panel recommends temporary modifications to the steps and values of the dry whey scale for a period of one year, August 1, 2015 through July 31, 2016.
- The Panel recommends temporarily increasing the Class 4b price, replacing the current dry whey scale with the following dry whey scale based on dry whey:

Monthly Average Dry Whey Price ($/lb)	Whey Factor Value ($/cwt.)
< $0.21	$0.0000
≥ $0.21 and < $0.24	$0.2500
≥ $0.24 and < $0.27	$0.3500
≥ $0.27 and < $0.30	$0.4500
≥ $0.30 and < $0.33	$0.5500
≥ $0.33 and < $0.36	$0.6500
≥ $0.36 and < $0.39	$0.7500
≥ $0.39 and < $0.42	$0.8500
≥ $0.42 and < $0.45	$0.9500
≥ $0.45 and < $0.48	$1.0500
≥ $0.48 and < $0.51	$1.1500
≥ $0.51 and < $0.54	$1.2500
≥ $0.54 and < $0.57	$1.3500
≥ $0.57 and < $0.60	$1.4500
≥ $0.60	$1.5500

Analyzing the 5-year period April 2010-March 2015, the effect of these changes would have resulted in a five-year monthly average increase of $0.65/cwt. in the Class 4b price and $0.30/cwt. in the Pool prices.

In addition to the issues confronting California producers such as decreased margins on the dairy; higher feed costs; environmental costs and regulations; and land use competition and drought; the Panel recognizes that there are also issues that confront California's proprietary and cooperative processors of dairy products, including cheese. Some of the factors influencing California's processors include: differing size, efficiency, and marketing conditions of California's varied processors; growing influence of global supply and demand conditions for milk and dairy products; and lack of flexibility in the pricing of both contracted farm milk supplies and excess/surplus farm milk supplies. Some of these issues exist because current California statutes require processors to pay the regulated, minimum price for California Grade A milk based on the same pricing formulas, regardless of the factors that affect each individual processor.

The Panel is concerned with how the regulated pricing system and its pricing formulas relate to the factors influencing milk production and the manufacturing and marketing of dairy products. Many of these concerns are also held by industry stakeholders and were topics discussed and analyzed during Task Force meetings and other industry meetings. The Panel believes that it is imperative for industry stakeholders and the Department to collaboratively seek solutions to the problems facing the industry so that individual stakeholders may have more flexibility to establish milk prices that may correlate better to the factors influencing each individual stakeholder.

This Hearing Panel Report has been prepared and submitted by:

Original Signed by:

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John Lee, Branch Chief

Original Signed by:

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Original Signed by:

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Don Shippelhoute, Branch Chief

Appendix A

ECONOMIC CONSIDERATIONS OF THE PROPOSED CHANGES TO THE PRICING FORMULAS

Each and every public hearing involving the milk pricing formulas can impact the economic interest of dairy producers, producer cooperative organizations, dairy processors, distributors, retailers, and consumers. The careful consideration of each pricing issue and the implementation of appropriate policy require impartial balancing of all interests involved. At the same time, the Panel believes it is important to set as accurate a pricing formula as possible that reflects full consideration of all the key economic factors impacting the California milk market. To achieve this, the Panel considers relevant economic factors, including statutory requirements, for all of the issues covered in the Panel Report, some of which are listed below:

- Milk production costs;
- Milk supply;
- Manufacturing costs;
- Product yields in converting bulk milk into finished products;
- Markets for California commodities;
- Transportation costs;
- Price volatility and lags in the release of different datasets;
- The competitiveness of California commodities compared to other major supply regions;
- The prices received by California processors for their finished commodities;
- The differences in the Pool obligations for processors in the California order and the federal orders;
- The state's processing capacities;
- California's long-term history of milk expansion;
- Greater distance to domestic markets for finished dairy products compared to other regions;
- The relationship of California class prices and federal order class prices;
- The effectiveness of risk management tools;
- The supply/demand forces of the domestic and international markets;
- The reasonableness and economic soundness of market milk prices for all classes, giving consideration to combined income from those classes;
- Whether prices will insure an adequate and continuous supply, in relation to demand, of pure, fresh, wholesome market milk for all purposes, including manufacturing purposes, at prices to consumers which, when considered with relevant economic criteria, are fair and reasonable;
- Whether prices for the various classes of market milk bear a reasonable and sound economic relationship to each other; and
- Whether prices promote, foster and encourage the intelligent production and orderly marketing of milk.

CALIFORNIA FOOD AND AGRICULTURAL CODE

When reviewing the codified mandates and directives given to the Secretary by the Code, the Panel believes that the Secretary has been given the mandate to consider any and all economic factors available in order to set minimum prices in California. A review of the language found in Section 62062 and other Code sections support this view. The Panel believes that, as previously quoted, California prices shall be in reasonable and sound economic relationship with the national value of manufactured milk products. As further stated in Section 62062, when establishing prices, the Secretary also "shall take into consideration any relevant economic factors, including, but not limited to" other factors listed in this section. These other factors specifically listed in this section include the reasonable and economic soundness of market milk for all classes while considering the combined income from those classes in relation to the cost of producing milk (Section 62062(a)), the establishment of prices that ensure an adequate and continuous supply of milk in relation to the demand for milk for all purposes including consumer prices that are fair and reasonable when considering relevant economic criteria (Section 62062(b)), and the establishment of prices for the various classes of milk that bear a reasonable and sound economic relationship to each other (Section 62062(c)).

Furthermore, when establishing the appropriate level of prices in California, Section 62062 provides the Secretary with further directives and mandates. At the end of Section 62062, there is language stating that, "In establishing the prices, the director shall also take into consideration all the purposes, policies, and standards contained in Sections 61801, 61802, 61805, 61806, 61807, 62076, and 62077." These sections provide further mandates to insure an adequate and continuous supply of market milk for consumption, develop and maintain satisfactory marketing conditions, and other high-level mandates affecting the state in the aggregate.

Sections 61801 and 61802 provide a mandate that states that the production of milk is a business affected with a public interest, that milk is a necessary food for human consumption, and that health regulations alone are not sufficient to prevent economic disturbances in the production of milk; therefore, as stated in Section 61802(e), "It is the policy of this state to promote, foster, and encourage the intelligent production and orderly marketing of commodities necessary to its citizens, including market milk, and to eliminate economic waste, destructive trade practices, and improper accounting for market milk purchased from producers." Section 61805 states that the Secretary should determine prices based on varying factors like the cost to produce milk, health regulations, transportation, and other factors, and with the aid of the state, should enable the dairy industry to develop and maintain satisfactory marketing conditions while bringing about and maintaining a reasonable amount of stability and prosperity in milk production. These three sections provide the Secretary with (1) the authority and (2) the overarching mandate to promote overall stability in the marketplace by ensuring the intelligent production of milk at the farm level and a corresponding orderly marketing of dairy products made from farm milk.

Sections 61806 and 61807 seem to provide the Secretary with broad power in setting prices and the mandate to facilitate the state's milk supply. Section 61806 states that, "It is the intent of the Legislature that the power conferred in this chapter shall be liberally construed." Section 61806 is found in Chapter 2, Part 3, Division 21 of the Code along with Section 62062 and other sections of the Code mentioned above, which indicates that the Secretary

has been given liberal authority in establishing prices. Section 61807 states that prices should be established that, “under the varying conditions of production, ensure an adequate and continuous supply of pure, fresh, wholesome market milk to consumers of the market milk.” This indicates that prices should be set at levels that will allow for an adequate amount of milk to meet the needs of consumers of market milk.

Sections 62076 and 62077 provide factors for consideration in establishing prices that are associated with Class 2, 3, 4a and 4b milk and the minimum price laws of California. When establishing prices for Class 2, 3, 4a, and 4b milk, Section 62076 states that the Secretary “shall take into consideration any relevant economic factors” that include, but are not limited to the value of the various products manufactured from milk (Section 62076(a)), the price of other milk used for the same purposes in the respective classes listed above (Section 62076(b)), and the value of manufacturing milk while “giving consideration to any relevant factors including, but not limited to, product prices, product yields, and manufacturing costs of Class 4a or Class 4b” (Section 62076(c)). This section reiterates the concept of considering any relevant economic factors available in order to make appropriate pricing decisions. Additionally, this section mandates the consideration of the prices of the dairy products manufactured in the state along with the value of milk used in the various classes. Section 62077 states that handlers in California shall not pay any producer less than the regulated minimum prices for milk. This section cites current law that handlers must pay at least the regulated minimum price for market milk for the various classes, regardless of the dairy products manufactured from the milk or the Pool status of the handler.

Appendix C

SUMMARY OF TESTIMONY AND POST HEARING BRIEFS

WESTERN UNITED DAIRYMEN, Annie AcMoody

Testimony

- Supports the milk pricing proposal submitted by the producer trade organizations.
- Concern about the manner in which whey is valued by the California milk pricing system.
- Proposal is meant to adjust the whey scale to mirror the whey value in the federal order Class III formula.
- California milk price for 4b has trailed the federal order Class III price by $1.80/cwt. over the past five years.
- The current Class 4b formula fails to determine the cheese milk's value appropriately.
- Deviation between Class III and 4b prices are caused by several factors but the whey value creates the most variance between the two classes.
- Plants in the federal orders can avoid the minimum Class III price by depooling. The option to depool in California is not the same but there are options for a producer to go Grade B where no minimum price applies to that producer.
- Focuses on what the processor pays for milk not what the producer is getting paid, once it goes through the pooling process.
- The all milk price is a good barometer of what is paid by processors in an area dominated by Class III utilization. In Wisconsin the all milk price averaged $1.68/cwt. higher than the Class III price in 2014.
- In Idaho, plants pay a range from +12 cents over the Class III price to -50 cents below Class III, with some paying the Class III price.
- Clearly even when no regulation exists, the Class III price is used as a benchmark.
- Department data indicated that feed costs rose from just over 51 percent of total cost of production in 2003 to 60 percent in 2010, with a slowdown in feed costs in 2013.
- Department data for 2014 indicates that feed costs represent 61 percent of the total cost of production.
- Estimates for 2015 are that with fairly steady feed costs, and an average overbase price of $13.91 for the first four months, the current financial snapshot for producers is somber.
- Failure to capture the value of whey is hurting the competitiveness of dairy farmer further.
- There is no sign that milk prices will increase much above what they are now.
- The average overbase price for the second quarter of 2015 will likely be in the $14 range.
- A clear sign that the financial situation in California has deteriorated is the SDA milk production report that indicates milk production has average 2.8 percent below last year, in contrast milk production nationwide is up 1.7 percent over last year.
- Plant capacity issues are not a factor.
- Producers bear the cost of lack of plant capacity.
- The whey issue is one of fairness with prices observed in the rest of the country.
- In 2014 there were 1,470 dairies left in the state, down from 1,752 five years ago.
- No new plant capacity was built in the last five years.
- Two mid-size companies have built plant capacity, and one underway. Several small farmstead operations have also started. There are more handlers in operation than there were five years ago.
- According to a study by UC Davis the dairy industry generated $21 billion in economic activity (for a total of $65 billion of dairy related economic activity).It supported 55,000 milk production and processing jobs (for a total of 189,000 jobs related to the dairy industry).

- Various studies cited that the drought has had an impact on driving up feed costs with fallowed acres, water cuts, zero water and increased water costs. The hardest hit area is sighted at the Tulare Basin.
- With price volatility producers have turned to risk management to protect their operations.
- Futures contracts are tied to Class III prices, with the spread between Class III and 4b increasing, futures contracts do not perform as they are intended preventing dairymen from being able to determine their basis effectively.
- Banks find that dairy loans are increasingly undesirable, making it harder for dairy producers to secure funding when needed.
- The safety net that resulted from the latest Farm Bill is an issue for California producers due to the discrepancy between California prices and the rest of the country.
- It is widely recognized that the whey stream has generated considerable revenues for the cheese processing industry.
- The U.S. continues to produce and export whey products, which leads to the growing potential of whey and whey products. Producers and processors should benefit from higher prices in whey product markets.
- The narrow range of the sliding whey scale is problematic with a ceiling capping the whey value at 75 cents and a floor of 25 cents.
- There is no ceiling cap in federal orders.
- Opposes the Institute proposal.

Post-Hearing Brief

- Added to the record, 2015 milk price information for Wisconsin: Jan-April 2015 all milk price averaged $17.30/cwt. versus a Class III price of $16.29/cwt. challenging the processor argument that milk was being sold under the Class III price in the Upper Midwest order this year.
- Challenged the statement that the current loss of dairies in not abnormal: from 2012-14, 93 dairies were lost in contrast to 57 cheese plants remaining constant from 2012-15.

DAIRY INSTITUTE OF CALIFORNIA, William Schiek

Testimony

- Opposes the milk pricing proposal submitted by the producer trade organizations.
- 2014 was an outstanding year for dairy farm margins.
- While 2015 production is off slightly from last year, but that was a record year and not cause for concern.
- It is wrong for producer advocates to assume that plant margins are so large that cheesemakers can easily absorb and sustain big increases in the 4b milk price.
- Coops in California have sold off their cheese plants and opted for the profitability of butter-powder plants.
- In federal orders where dry whey end-product formula is used to calculate the Class III price, the regulated minimum price is optional.
- This last week milk sold for as much as $10 below class in the Upper Midwest order and multi-dollar discounts have been common this spring.
- Economics and basic logic reveal that the regulated price levels for milk used in cheese making in California and the federal orders are not and should not be the same.
- Producers fail to acknowledge the difference in location value of cheese, fail to consider the possibility that the federal order formula might overvalue milk to cheesemakers, or the differences in industry structure and costs in California necessitate a lower milk price.

- Most cheese plants receive no value from whey, about half receive some value, but less than what is assumed in the Class 4b formula, nor does the value track well with dry whey.
- Only one plant in the state produces dry whey.
- Small to medium plants have been investing in equipment to process liquid whey and liquid whey price is driven by the WPC-34 price.
- Most small to medium cheese plants if they ultrafilter their whey, still have a disposal cost, not a money making product. Thus it should not be included in the minimum price.
- Institute proposes adjusting the sliding scale and replacing the commodity of dry whey with WPC34 as published in the DMN.
- This proposed change better reflects the diverse types of cheese plants that operate in California- it is reflective of the value of whey to cheesemakers that concentrate liquid whey and sell it to plants for further processing.
- This proposal includes a discount of 15 cents per pound to dry liquid whey and turn it into a finished product, 35 cents per pound to make liquid WPC34, a yield of 1.8 and a 0.8918 adjustment for the portion of milk that ends up as skim whey in cheddar cheese making.
- The proposal increases the top of the whey scale significantly, thus limiting the duration of the proposed changes to six months.
- The current whey scale no longer represents the value of whey received by cheese plants operating in California.
- Cheese plants are experiencing their margins under pressure due to inadequate make allowances in the cheese formula, so a large increase in the whey contribution would likely lead cheesemakers to exit the industry.
- Appendix A: Statutory Directives, Legislative Intent and the Paramount Importance of Orderly Marketing of Milk
- Figure A-1: California Milk Production and Estimated Plant Capacity, 2006-2015 YTD
- Appendix B: Large Price Increases are Not Warranted by Economic Conditions
- Figure B-1: California Spot Feed Prices, August 2012-2015
- Table B1: California Feed Prices, August 2012-June 2015
- Figure B2: Cost Comparison Summary, 2014
- Figure B3: California Milk Income and Production Costs, 2003-Q3 2014
- Figure B4: California Dairy Farm Income Over Feed Costs, 2012-Q3 2014
- Figure B5: California Dairy Farm Income Over Production Costs, Per Hundredweight of Milk, Q1 2003-Q4 2014
- Figure B6: USDA Milk Production Cost by State, 2014
- Figure B7: Dairy Farm Numbers by State as a Percentage of 2003 Levels
- Appendix C: Attempting to Drive Regulated Prices Class 4b Prices in California toward the Level of Regulated Class III Prices in the federal orders is Without Economic Justification
- Figure C1: Population Density in the United States
- Figure C2: Milk Production, Top 5 States, 1997-2012
- Figure C3: Milk Production Costs 2012-2014
- Exhibit C1: America’s Top States for Business 2014
- Appendix D: Difficulties Associated with Using Whey to Price Milk Used in Cheese Making
- Figure D1: Dry Whey-WPC34 Price Inversion
- Figure D2: Western Dry Whey Mostly Price and Central/West WPC-34 Protein-Equivalent Price, 1991-2015
- Table D1: Pounds of Milk Processed into Cheese
- Exhibit E: Editorial Comment, Cheese Reporter, May 29, 2015

Post –Hearing Brief

- Believes any impact of their proposal on whey prices and whey market dynamics to be negligible.
- Very few cheese plants have whey revenue that is in direct proportion to the dry whey price.
- While it may seem that the dry whey prices track with WPC34, it could vastly overstate the whey values earned by plants making WPC or liquid whey. The equivalent value from dry whey overstates the revenue from attainable making WPC34 in most months since early 2009.
- It would be more keeping with the spirit and underlying meaning of the Code Section 62062 if we were to construct a formula based on WPC34 than dry whey.
- It is key that in FMMO regulation the option to pay less than the order minimum as an "escape valve" to allow for milk to clear the market when it exceeds demand at order prices.
- When distressed California milk ends up in cheese pants in other states at lower prices than those plants would ordinarily obtain their milk, the competitive position of California cheesemakers is put at risk. Thus, California regulated prices must be set at levels that clear the market to ensure orderly marketing of milk.
- Caps cooperatives place on milk supply through their base programs should be a temporary and not a long term solution to improve the state's competitiveness.

KRAFT FOODS, Barry Brokaw

Testimony

- Opposes the milk pricing proposal submitted by the producer trade organizations.
- Supports the milk pricing proposal submitted by Institute.
- Large plants in California manufacture WPC34 or WPC50 and lactose and dry whey permeate.
- The next size plants manufacture WPC but do not further process the permeate, creating a cost to dispose of the permeate.
- The next size pants recover some value from selling liquid whey concentrate, when possible, and pay to dispose of liquid whey when there is no buyer. Transportation costs are also paid further eroding the value.
- The smallest plants (two thirds of the cheese plants in California) pay to transport and dispose of the whey liquid and receive no value.
- Kraft sells a small amount of liquid condensed whey and processes the rest into sweet whey powder. Occasionally the sweet whey powder is sold as animal feed and does not receive the value from the whey that is achieved when sold as food grade.
- It does not calculate out to be financially feasible for Kraft to convert to a plant that processes value added whey products such as WPC34, WPC80 or WPI, nor is it cost justified to transport whey to another plant for processing.
- Kraft garners minimal value from processing sweet whey.
- Any increase in the cost of 4b milk would have negative impact on Kraft's margins.
- Cheese processors margins are small, as retail cheese is a commodity business and must compete with branded products.
- Storage, transportation, sales and marketing costs are inflationary and inelastic and plants must absorb any increases costs from their margin, they cannot charge the customer more.
- A long term fix to the pricing system should be the goal rather than short term fixes that result in higher milk costs for processors.

- If it is more profitable to manufacture cheese in other regions of the country then manufacturing investments will move to those regions and the milk supply will increase to meet the needs.

Post-Hearing Brief

- The source used to determine size and disposal of whey in testimony was by my industry and marketplace knowledge of California dairy manufactures.
- Outlined the mix of Kraft's nine plants.
- Cost of milk at Kraft's plants are confidential and contract prices cannot be disclosed, but all plants have contracts that include premiums.
- Areas where Kraft has plants that the milk supply is local, have flexible sourcing and pricing.
- Kraft periodically has excess capacity due to volume fluctuations and is able to purchase less expensive spot milk.
- Where there is more competition for milk (other areas of the nation) it keeps the premiums extremely competitive. In California, the lack of competition keeps prices stable and elevated.
- The milk costs (transportation, manufacturing and distribution) for Kraft plants in other locations, closer to customers are less than in its California plant.
- The estimated share of total cheese plant volume by plants that do not process whey is 5.3 percent as reported by CDFA's Background Materials Table.
- Explained processing issues that lower food grade whey to animal feed, garnering a lower price for the whey; standards for food grade whey such as flavor, appearance, bacteria, coliform count, moisture, etc.
- Elaborated on the analysis used in calculating the coefficient of dry whey and WPC34.

CACIQUE, Antonio De Cardenas

Testimony

- Whey was in the past an expense and had no practical use, although we concentrate whey into WPC and sell at market rates, the by-product of WPC, lactose is a zero-gain feed, at is a great cost to dispose of.
- The cost of doing business in California is higher that our competitors in the Upper Midwest, where their costs are much lower, it is hard to compete for market share as we must ship our products to the market outside of California.
- Supports no changes.

Post Hearing Brief

- Nearly half of Cacique's products are sold out of state with transportation costs of $0.30-$0.70/cwt., making it very hard to remain competitive.
- It is hard to compete with competitors east of the Rockies, with lower costs and in states that are more business friendly than California.
- Exhibit A: 2014 Oregon Worker's Compensation Premium Rate Ranking Summary
- Exhibit B: U.S. Energy Information Administration, Electric Power Monthly
- Exhibit C:Tax Foundation Background Paper, October 13, 2008 2014 State Business Tax Climate Index

JOSEPH GALLO FARMS, Joe Paris

Testimony

- Gallo Farms operates a cheese plant and two dairies, milking approximately 8,000 cows.

- Gallo concentrates whey for their plant and are a market for WPC from other small plants in the area. WPC is processed and dried into whey protein isolates.
- Most of the cheese processed is sold to grocery store chains, WalMart, Costco and exported to Mexico.
- Gallo invested in whey processing and a methane digester to improve efficiencies.
- Until Gallo invested in a whey processing facility, much of the whey was dumped or fed to cows.
- If Gallo had been required to pay the 4b price that is being proposed by the producer groups, none of the investment improvements would have taken place.
- Both dairy producers and processors are at the mercy of the market place and volatility can be the enemy of both.
- Long term planning and investment is needed in order to grow both the producer and processor segments of the industry.
- If the producer proposal is adopted, the cheese sector in California will stagnate almost immediately.
- Medium and small plants will no longer be able to sustain their processing plants.
- Producers will find themselves with fewer markets, mostly butter/power industry.
- If the producer proposal is adopted Gallo may respond by eliminating all outside suppliers of milk and reduce cheese sales to only Joseph Farms packaged cheese. May add cows to take advantage of higher milk prices. May look to diversify by planting permanent crops. Would eliminate premiums or handling charges they currently pay to suppliers.
- Producers should not look to the Midwest/East Coast milk prices and feel they are deprived of a fair price. We are in a different market, different location with transportation costs that demand higher prices. The export market (Mexico) does not pay greater than $1.90/pound for cheese, anything over $2.00/pound slows sales here in the West.
- Federal orders allow plants to depool and not pay minimum prices. Just recently milk has been purchased for $7.00/cwt. below the minimum regulated price. In contrast, California requires all processors to pay the regulated price.
- Many plants in the Upper Midwest have much lower overhead costs due to various regulations.
- Opposes the milk pricing proposal submitted by the producer trade organizations.
- Supports Institute proposal which adjusts the sliding scale and replaces the commodity of dry whey with WPC34 as published in the DMN.
- Regulated prices should be minimum prices based on the best market orientated criteria and should not be changed every few years.
- Producers should negotiate higher prices than the minimums based on individual plants ability to pay above the regulated price.

CALIFORNIA DAIRIES INC., Eric Erba
Testimony

- Disparity between the whey valuation in federal milk marketing and in California to large to ignore.
- Supports the milk pricing proposal submitted by the producer trade organizations as it has a foundation based on economics, logic and consistency consistent with the California federal milk marketing order effort that is being actively pursued.
- California producers need fair compensation for milk and its components by processors.
- The Class 4b formula has not tracked within a reasonable range of the federal order Class III for some time, it is past time for the appropriate adjustment to occur.

- Modifying the method of valuing whey will restore the equity in what processors in California are paying for milk with what processors in the rest of the country.
- Dairy is the leading agriculture industry in California.
- There are signs that the producer side of the industry is not faring well, milk sales dollars do not translate directly to on farm profitability.
- Over 480 dairies have exited the industry since 2007.
- Affiliated businesses are affected by the collapse of the milk production side of the dairy industry.
- Regions of the state where the dairy industry has flourished, have reported high unemployment numbers for the past several years.
- The drought has had, and will continue to have significant implications for dairy farms.
- Due to the drought, dairy farms are switching from growing alfalfa and corn, which take substantial amounts of water and cannot tolerate stress well, to sorghum which take less water but have a lower nutritional value than corn.
- With less corn available for silage, producers are changing their feed rations to more alfalfa, a fiber which is purchased from out of state sources, and very costly.
- The Department's concern regarding a sufficient milk supply to service processing plants and that establishing a higher minimum price will lead to more milk production is ineffective and inefficient.
- The major coops and proprietary plants have adopted programs that allocate milk production shares to producers based on the ability of the entity to handle its milk supply.
- These programs adjust with market conditions much faster than the Department can call a hearing and institute milk pricing changes.

Post-Hearing Brief

- Responding to a question from the Panel, how much more it will cost producers to buy alfalfa hay rather than growing it themselves, the cost to grow hay ranges from $140/ton to $170/ton, but the hay would not be the high quality required for dairy cows, more for dry cows.
- Few dairymen can purchase premium hay for $240-$275/ton, however most hay purchased to supplement dairy rations would have to be supreme, purchased from Nevada or the Imperial Valley for $300-$325/ton.

SAPUTO CHEESE, Greg Dryer

Testimony

- Supports Institute proposal which adjusts the sliding scale and replaces the commodity of dry whey with WPC34 as published in the DMN.
- The California 4b price is not a discounted price. It is based on California commodities FOB California, less the average cost of manufacture, independent of other regions and circumstances.
- California has the lowest milk price due to low Class I utilization, a low value of butter and powder and a lower fat percentage.
- In comparison, California grapefruit sold for 24 to 26 percent less than that of Texas and Florida and gas sold in California for $3.50/gallon is sold in the Midwest for $2.50/ gallon. Thus, it is normal for commodities to vary by region.
- The market for milk is regional, not national.
- California milk production increased more than any other state in 2014, and doubled since 1991, that would not have happened if the milk pricing system was detrimental to the participants.

- There is little local competition for milk, supplies have been more than adequate to fill existing capacity.
- According to USDA, California dairies produce 7.6 times the amount of milk than the average dairy farm in the nation and 10 times the amount produced by Wisconsin dairy farmers. This enormous scale gives California producers a substantial cost advantage.
- According to USDA, the percentage reduction in dairy farms numbers for California from 2013-2014 ranked 34th of the 50 states.
- California lost just 3.3 percent of its farms but 9.4 percent of its cheese plants.
- Available processing capacity has continually been stressed to keep pace with the growing supply of milk.
- Construction of very large plants producing bulk commodity products needed to accommodate the increasing milk flow command lower margins than those of smaller specialty plants that operate in other cheese producing areas such as WI, MN, NY, PA and VT.
- In the West where larger plants are more common, they are located in areas where the industry is either completely unregulated or most manufacturing is dominated by cooperatives, which have pooling and pricing flexibility to adjust to changing market conditions.
- California milk production has grown and vastly exceeds the demand for local dairy products and as a result most of the cheese produced is exported to other population centers.
- It costs 11 cents per pound to ship cheese from central California to Chicago and 16.5 cents/pound to ship to New York.
- 16.5 cents/pound equates to $1.67/cwt. according to the Class 4b formula.
- In addition to shipping costs, operating, Cap and Trade regulations and regulatory compliance costs contribute to a lower cheese milk value in California impeding the ability to pay a higher price for milk.
- California implemented a whey factor very similar to federal order whey factor in 2003.
- In 2007 dry whey prices surged and were out of proportion to the value derived from whey products made by most California cheese plants.
- An emergency hearing was called to address the issue which resulted in an arbitrary fixed value for whey giving higher milk prices to producers for 17 of the 19 months after its implementation.
- When dry whey prices again increased after 2009, the opposite has been the case.
- A variable whey value table was introduced in 2011 and increased in 2012.
- Since 2007 USDA did nothing to address the over valuation of whey in the federal order system, it became so cumbersome that participants resigned themselves rather than try and change the value in the federal order system.
- Many plants did not survive. The result was a decrease in cheese plants by 30 and non fat dry milk plants virtually disappeared. 91 of the remaining 127 cheese pants moved from producing commodity cheese top specialty cheese in order to survive.
- Losses were reported for 2014 by two large Midwestern coops.
- The fact that California addressed the whey problem and USDA didn't led to the price disparity between the two systems.
- It does not mean that California milk in underpriced. Federal order prices are significantly over priced.
- The overpriced value for whey was addressed in comments filed on the 610 Review of Federal Milk Order Docked ID: AMS-DA-009-0065 (Wisconsin Cheese Makers comments from April 13, 2015 entered into the record). Comments were made that dry whey is not

an appropriate basis for valuation and less than 6 percent of U.S. cheese plants producer dry whey.

- The answer for California is not to mirror the failed federal order system, especially without the ability to operate outside of the Pool, like in the federal order.
- Recent milk sales in the Midwest were reported at $7-$10 below class price.
- California producers do not want a federal order, they want higher prices for their milk.
- Setting milk prices above the market does not achieve its intended purpose.
- 2014 was a record year for milk prices, which resulted from demand not price intervention.
- The threat of CDFA intervention leads to uncertainty and discourages investment.
- It is very unlikely that any increase in the cheese price could be passed on to consumers.
- Memorandum: April 13, 2015, to Agricultural Marketing Services, USDA from Wisconsin Cheese Makers Association

Post-Hearing Brief

- Supply and demand should establish the price for milk.
- You can't make California producers more "competitive" by increasing the regulated price if that makes the rest of the supply chain (cheesemakers) uncompetitive.
- Increased demand for milk in CA will come only from investment in plant capacity and value added technology, products, and marketing.
- Entered in the record:
    - Freight rate document containing screen shots of queries made from Chainalytics.
    - A simple spreadsheet which summarizes the information they provided.
    - May 1, 2105 USDA ERS Cost of Milk Production by State Spreadsheet and the February 2015 USDA NASS Milk Production Report which provided most of the statistics I quoted in my testimony.
    - From the Milk Production Report, I prepared the spreadsheet, also attached, which enabled me to review and rank farm sizes, the growth in milk production, and losses in farm numbers.

CALIFORNIA DAIRY CAMPAIGN, Lynn McBride

Testimony

- Supports the milk pricing proposal submitted by the producer trade organizations as it has a foundation based on economics, logic and consistent with the California federal milk marketing order effort that is being actively pursued.
- There are 1470 dairies left in the state, 26 dairies went out of business in 2014 and economic conditions have led to the loss of 500 dairies since 2006.
- 2014 prices improved but dropped and did not last long.
- 2009 was the worst year with income lost averaging $5 per cwt. Conditions improved in 2010 and 2011. It deteriorated in 2012 and 2013.
- Currently income is not covering the cost of production.
- Believes that dairies have closed due to producers not receiving the same prices that other producers do in other areas of the nation.
- Several small dairies have closed and were converted to grind up operations (converted to tree farming) because it is more profitable and dairy cannot compete.
- Livestock sales in Turlock indicate that approximately half of the heifers sold are leaving the state.
- Milk production has been on the decline and expects the trend to continue.
- Believes that the disparity between the 4b price and equivalent federal order price is the reason for the decline in milk production.

- The average difference between the 4b price and equivalent federal order price is $1.80 per cwt.
- The latest cost of production data from CDFA for the fourth quarter of 2014 showed costs at $20.09 per cwt. Income according to the mailbox price for February 2015 was $14.49/ cwt., indicating that income was more than 25 percent below average production costs.
- The ongoing drought in California is creating challenges with feed costs and the uncertainty with feed availability.
- According to the CMAB report on the dairy industry "the economic health of the California dairy industry depends crucially on a healthy local forage industry to supply silage, hay and other forages that are too bulky to economically haul long distances."
- California dairy producers are paid on average $1 per cwt. less than dairy farmers in the federal milk marketing order system. Mailbox prices for January and February of 2015 show California prices $15.11 and $14.49/cwt., respectively, compared to federal order prices at $17.71 and $16.91/cwt., respectively.
- Consolidation and concentration does not allow for competition in the marketplace and producers cannot find new markets and change to a new buyer.
- Feels that under the new Farm Bill, California dairy producers are at a greater disadvantage due to the fact that prices are below prices paid in other states resulting in far less of an effective safety net for producers when margins decline.
- Oppose the Institute proposal because it would only increase the whey value by six cents and does not agree to move to using WPC34 to value whey.

Post-Hearing Brief

- Cites a June 3rd article from the U.S. Dairy Export Council explaining a statement in testimony regarding "demand continues to grow both domestically and overseas for whey products".
- Clarifies the term "grind up dairies." Grind up dairies today are different from the grind up dairies in the past in Southern California. Dairies today are different than closures back then because today they are permanent closures leading to the decline of milk production. When dairies in Southern California happened a decade ago, they used the proceeds of the sales to purchase and build dairies in other parts of the state.

PACIFIC CHEESE COMPANY, Al Zolin

Testimony

- Very concerned about proposals that would significantly increase the cost of milk to cheese suppliers and the cost of products that they source in the state.
- The cheese business is very competitive.
- Procurement decisions are not only about price, but quality, service and supplier relationships.
- California cheese suppliers will become less competitive on a price basis if the price is increased.
- Supports the Institute proposal.

Post Hearing Brief

- As of 2015, Pacific Cheese did not process milk into cheese in its facility in California.

FARMDALE CREAMERY, INC., Scott Hofferber

Testimony

- Supports no changes.

- Federal orders do not mandate the minimum prices paid for milk going into anything other than fluid milk.
- Currently Wisconsin cheese plant can purchase milk for $7 below federal order Class III.
- Producers make the assumption that certain features in the federal order system directly apply to our California regulatory model, they don't.
- The federal orders have a whey issue, as cited in the Cheese Reporter "It is a fundamental flaw in federal milk market order pricing-a built in discrimination against small and mid-sized cheese manufacturing businesses that cannot begin to afford the cost of dried whey manufacturing".
- Farmdale invested in whey processing with great risk.
- Before investing in the new whey processing Farmdale's old animal feed whey roller system resulted in a negative outcome of $0.012/pound of cheese produced, which was absorbed by the cheese operation.
- After investing in the new whey processing, the result was a positive outcome of $0.302/pound of cheese produced during the most recent 18 months (ending in April 2015). The final six months, ending in April 2015 resulted in a negative outcome of $0.0227/pound of cheese produced.
- The improvement of $0.423/ pound of cheese represents the return on investment needed to service the debt incurred on making the investment in the whey processing and can only remotely justify an increase in the whey stream of $0.3845/cwt. of the 4b milk.
- You cannot justify an increase of $1.46/cwt. that the producers are asking.
- Has concerns with the Institute proposed increase of $0.41/cwt. but is hopeful that by changing to WPC35 as the driver, the movements in milk costs will track more closely with the WPC80 market that Farmdale produces.
- If anything close to the producer proposal is implemented, it could have catastrophic results that may cause Farmdale to go out of the cheese business without ever recovering the debt incurred from investment into whey.
- Cheese processors are impacted by lower whey prices just as producers are.
- The Department's own costs show that the cheese make-allowance continues to run behind the actual costs in an ever-increasing amount- current make allowance $0.1988/pound with actual costs averaging $0.2291/pound.
- Wants to move from the term fair price to appropriate price for whey valuation.
- Let the market place determine the appropriate level of equilibrium in the price of 4b milk.
- Attachment: Cheese Reporter, May 8, 2015, John Umhoefer, "The Whey Problem and California's Solution."

BESTWHEY, LLC, Barry Murphy
Testimony

- Supports no change, but would support Institute if changes are made.
- Believes the whey factor should remain the same as is and allow market forces to determine 4b milk price premiums.
- Of the 57 cheese plants in California, one manufactures dry whey, three major plants process other whey products, ten process liquid reverse osmosis (RO) whey for sale as liquid animal feed to other whey processors and four of those plants as dried whey protein.
- All of these ten companies dispose of more than 85 percent of whey solids into animal feed at little or no value.
- 13 of the 57 plants in California can process whey to some degree.

- Using whey powder market value in 4b pricing formula does not make sense-assumes all plants utilize 100 percent of whey solids.
- RO whey solids are sold in liquid form by two plants in the state and achieve 50-70 percent of the whey powder value minus freight costs.
- WPC34 liquid solids are sold by three plants in the state to dryers at 20-30 cents under the WPC34 price, delivered.
- Small cheese plants representing 70 percent of the 57 cheese plants in the state have no ability or economies of scale to process whey and pay up to $1.00 per cwt. to dispose of whey.
- Institute's proposal to index whey value in 4b milk to the WPC34 market value makes more sense than using whey powder market value.
- Adopting the producer proposal will wipe out the smaller cheese plants and may result in reduced processing levels by larger cheese plants.
- The cheese business is a low margin business, with a few cents margin from cheese sales values.
- Private cheese plants cannot assess losses to producers like coops can.
- Coops have either sold their cheese plant operations or sold liquid whey below market to cheese plant dryers, but have not invested in whey operations due to the investment cost.

HILMAR CHEESE COMPANY INC., David Ahlem

Testimony

- Supports no changes.
- Does not believe economic conditions warrant additional increases in 4b minimum milk prices.
- Long term reform is what is needed.
- Increases in the minimum price put us at a competitive disadvantage to our primary competitors who are not subject to minimum prices.
- CDFA data makes the case for lower not higher minimum prices
- The 4b make allowance is $0.1988/lb where CDFA plant cost study shows the cost of manufacturing at 0.2291 percent.
- 2014 was a record year for dairy producers.
- Estimates of up to one billion dollars in income was deferred in 2014 by California dairy producers.
- 2015 brings lower milk prices and lower feed prices.
- Compared to other states, California's producer net margins are reasonable.
- California's dairy consolidation is not unique in the U.S. or the rest of the world.
- Minimum prices are just that, minimums, processors pay premiums to producers above the 4b price, Hilmar has paid over $120 million dollars over the past several years in premiums.
- The regulated minimum prices must be market clearing.
- Cooperatives who control 85 percent of the milk can charge more for milk.
- Increasing the 4b price takes money from many of our producers, it does not create more revenue for end products. It will only redistribute revenue among producers.
- Coops have exited the cheese business.
- This hearing is not about the economic situation of producers, it's about the inappropriate comparison of federal order Class III and California 4b prices.
- Comparing the two prices is like comparing apples and oranges, they are two different markets.

- Where Class III pricing is used it is not mandatory, it is optional. Processors regularly depool.
- Federal orders provide no guarantee that producers receive class pricing.
- The Class III formula is not a good way to value cheese.
- Dry whey is not an appropriate means to value milk.
- Dry whey is generally over valued for cheese makers receiving the WPC based price for their whey solids. It is a poor indicator of whey solids value.
- It is false that producers require a Class III price to make risk management effective.
- Frequent hearings create massive regulatory instability and drive investment elsewhere.
- Cheese plant closures over the years:
    - Suprema Specialties, Manteca - closed 2/2003
    - Sorrento, San Jose - closed 2/2003
    - DFA Cheddar Cheese Plant, Petaluma - closed 5/2004
    - Golden Cheese (DFA), Corona – closed 12/2007
    - Land O' Lakes Cheese Plant, Tulare – closed 9/2010
    - Gossner, Imperial Valley – closed 2013

- California cheese plants have invested outside of California.
- Long term reform is needed, not increasing the minimum price, which will further damage the industry and deter investment.
- Appendix:
    - Figure 1: Combined Milk Production Growth of Big 7 Exporters
    - Figure 2: California Milk Production
    - Figure 3: California Number of Cows
    - Figure 4: HCC Hilmar Milk Pounds per Day, March 2014-June 2015
    - Figure 5: California Cheese Decreasing Exports
    - Figure 6: California Feed Prices 5 Year Average
    - Figure 7: Number of Dairy Farms- U.S., EU-15, CA and NZ
    - Figure 8: Change in Milk Production, Licensed Dairies, CA, U.S. and WI
    - Figure 9: California Producer Margins
    - Figure 10: Milk Regularly Sold Under Class in FMMO's
    - Figure 11: Upper Midwest FMMO Depooled Milk percent
    - Figure 12: Pacific Northwest FMMO Class III Utilization
    - Figure 13: Southwest FMMO Class III Utilization
    - Figure 14: New Mexico Mailbox Price Over California
    - Figure 15: 2013 U.S. Cheese and Whey Production
    - Figure 16: 2013 U.S. Cheese and Whey Plants
    - Figure 17: Futures Price Correlation since 2011 to Milk Prices
    - Figure 18: WPC-34 and Lactose
    - Figure 19: Dairy Market News WPC-34 and Lactose verses NDPSR Dry Whey
    - Figure 20: U.S. and World Dry Whey Prices

Post Hearing Brief

- Higher cost of doing business in California over Texas, electricity and labor rates are higher by 100 and 20 percent, respectively.
- Ways you can pay below minimum in federal orders:
    - Spot milk purchases
    - By contract
    - Long term contractual arrangements
    - During the spring flush or other times of surplus through slotting allowances

    - Non-Pool plant buys directly from producers below class
- Cheese plants can use combinations of the above methods to pay producers below minimum
- Prior to the establishment of the Chobani plant in Idaho, Idaho had similar prices to California. Investment drives competition and prices up.
- Raising the 4b minimum price decreases the amount of premiums paid to high quality, high cheese yielding dairies.
- Hilmar receives 82 percent of its milk from independent dairy producers, not owners.
- New Mexico milk prices are a valid comparison to California milk prices, by default should have higher prices due to three times the Class I utilization, however they are still not paid the blend FMMO prices due to milk escaping the system.
- The whey market is extremely competitive, with no ability to pass on higher costs they may have to pay for milk.

DAIRY FARMERS OF AMERICA, INC., Elvin Hollon

Testimony

- Supports the milk pricing proposal submitted by the producer trade organizations.
- The support of this proposal aligns with our intentions in the federal order proposal.
- This proposal provides the best method for calculating the contribution of whey into the 4b formula.
- California's milk trend has veered off from the rest of the country.
- Overall, U.S. milk production increased in 2014 by 2.4 percent, in first quarter 2015, California shows a decrease in production, which is not the norm for California.
- California's all milk price consistently trails that of surrounding states prices and does not yield a comparable price.
- The difference ranges from $.91 cents/cwt. to $2.38/cwt., with the median difference of $1.50/cwt.
- Nine of the eleven largest states in terms of total cheese production, excluding California show a positive compound annual growth rate and produce 65 percent of the production of all types of cheese. They all operate where federal order Class III price is the minimum price for milk.
- There is continued plant investment in facilities in the Central, Mideast, Southwest and Upper Midwest orders, all where federal order pricing is the basis for minimum pricing, while California has slowed.
- The Institute proposal falls short of the needed adjustment to the 4b price.
- Does not support the change proposed by Institute to use WPC-34 instead of dry whey in the 4b formula.
- Producer's proposal provides significantly more revenues to meet the Secretary's hearing objective.
- Producer's proposal meets the requirements of section 62062.
- Map 1: Annual Milk Production
- Map 2: U.S. Milk Production Q1 2015 vs. Q1 2014
- Map 3: U.S. Milk Production April 2015 vs. April 2014
- Table 1: Milk Price, Selected Western States, 2012-2015
- Chart 1: Comparison all Milk Price Western States and U.S.
- Table 2: Total Cheese Production

Post Hearing Brief

- Submitted the t-statistic for each individual variable of the whey price projection equation.

- Table 3: Calculation of Improvement to the Producer Price From Each Proposal

PACIFIC GOLD MILK PRODUCERS, Leonard Vandenburg
Testimony

- Supports no change, but would support Institute if changes are made.
- A coop making specialty cheese started in 2008 when there was s surplus of milk and no one to ship to.
- Face increased cost of doing business from quality standards, regulatory standards to customer demands.
- Do not have higher premiums on specialty cheese, but have higher costs, moved to organic to make a profit.
- It is very common in federal orders for processors to pay one to two dollars under the federal order announced price.
- In the past 10 years, non-Pooled milk represented 14.83 percent, in 2014 16.66 percent.
- Class III average volumes equal 49 percent of Class III form non-Pooled milk.
- It is unreasonable to compare the 4b with Class III prices because approximately 50 percent of federal order Class III milk was severally underpriced compared to Pool milk.
- In federal orders over the last four to five months millions of pounds of milk have been sold to cheese plants for $7-10/cwt. under the announced price.
- Most cheese is sold at nearly break even or a loss while the dried whey products and ricotta cheese (which is what we make from our whey) subsidizes the cheese sales.
- Increasing the 4b price will be devastating to small/medium size cheese plants.
- Concern for unfairness happening when whey values are going down due to increased volumes entering the market and income being carved out from cheese plants on higher value products (whey), but not from higher value dried powders.
- Cannot understand why if the coops feel that there is so much money in cheese and whey, why coops aren't processing cheese and whey. Why do they want to take away the dollars invested and risked from cheese processors that earned it?
- Major plant investment in the past ten years has come in non-regulated areas.
- Oppose a production driven model that ultimately lowers prices and creates over supply.
- Exhibit A: Van Slyke Cheese Formula for Pacific Gold Creamery-90 percent fat and 78 percent protein
- Exhibit B: Van Slyke Cheese Formula for Pacific Gold Creamery-85 percent fat and 75 percent protein
- Exhibit C: Percent Milk Pooled/not Pooled in federal orders Annually
- Exhibit D: Federal Milk Order Marketing and Utilization Summary, annual 2013
- Exhibit E: Federal Milk Order Marketing and Utilization Summary, May 2014
- Federal order Class Prices January 2005-April 2015

LAND O' LAKES, INC, Pete Garbani
Testimony

- Supports the milk pricing proposal submitted by the producer trade organizations.
- The support of this proposal aligns with our intentions in the federal order proposal.
- Supports a period of no less than 24 months.
- Agrees that the overall marketing conditions support the adjustment to the 4b formula.
- Support updating the sliding scale to better reflect whey's recent market value.
- Recent heightened market value of whey indicates that the scale needs to be updated to allow additional sharing of these higher whey market values.
- Majority of producers favor using a sliding scale as a method to value whey.

- California milk production has slowed decreasing 0.1, 2.6, 3.5, 2.9 and 2.1 percent respectively from December 2014 through April 2015.
- LOL member production has decreased at a faster rate, 2.1, 4.6, 5.3, 5.3, and 4.7 percent respectively, from December 2014 through April 2015.
- LOL members' milk production appears to be responding to rapidly decreasing milk price and increasing production costs.
- Thus far in 2015 California producers have received far less for their milk than in 2014:
    - Statewide blend peaked at $23.67/cwt. in March of 2014 and declined to $14.72 in February of 2015.
    - Mailbox prices peaked at $23.36/cwt. in March of 2014 and declined to $14.49/cwt. in February of 2015.
    - The overbase price peaked at $22.47/cwt. in March of 2014 and declined to $13.82 in March 2015
    - During the first four months of 2014, the overbase price averaged $21.83/cwt., compared to an average of $13.91/cwt. for the first four months of 2015, a decrease of $7.92/cwt.
- These farm level decreases have had a huge impact on the cash flow position of our state's dairy farmers.
- Feed costs have increased for dry and wet roughages.
- The estimated drought impact on quality forages, such as alfalfa, is likely to be 11 percent higher when compared to 2014.
- Increased hired labor costs increased 2.7 percent, operating costs increased 3.9 percent and herd replacement costs increased 26.6 percent summing up estimated total costs of production for 2014 at $19.08 per cwt.
- Comparison of California farm level milk prices with 2014 cost of production:
    - February 2015 mailbox price was $14.49/cwt. which was lower by $4.59/cwt. than the $19.08 cost of production in 2014.
    - Statewide blend of $14.72 in March of 2015 was $4.36/cwt. lower than the $19.08 cost of production in 2014.
    - The overbase price averaged $13.91/cwt. for the first four months of 2015, 5.17/cwt. lower than the $19.08/cwt. cost of production in 2014.
- Income over feed costs has narrowed to $2.86/cwt., a catastrophic margin level when compared to the Dairy Margin Protection Program (DMPP) base insurance level of $4.00/cwt.
- It is estimated that 69 percent of California producers enrolled in the DMPP for 2015, with 95 percent of LOL members enrolled.
- The DMMP benefit is reduced when the California all-milk price falls below the U.S. all milk price.
- Thirty-seven LOL members have exited the business or changed their operations since August 2012 representing a decline of nearly twenty percent in thirty three months.

Post-Hearing Brief

- Concerns regarding using WPC34 to value whey:
    - No factual basis.
    - No audited manufacturing costs for WPC34.
    - WPC34 does not represent whey's most basic unprocessed form.
    - Would depart from CDFA's long-standing practice of using California prices, costs and yields in the 4b formula.
    - Institute's proposal caps out at a much lower value than is fair.
    - Would make risk management tools less accessible.

- Volume of WPC34 is not the reason to use WPC34 in the 4b formula.

XAVIER AVILA
Testimony

- Supports the producer proposal.
- Does not understand the discount on 4b.
- A lot of competition with trees.
- Wants a Federal order with quota.

DON FRANCISCO, Ivan Rizo
Testimony

- Oppose the producer proposal.
- Supports no change, but would support Institute if changes are made.
- The financial harm the price increase of the producer proposal could result in an additional cost for milk of $240,000-$320,000 per month.
- The additional cost would annualize to $2.7-$3.8 million, reducing profits by 50-70 percent.
- Increasing the 4b price would not allow us the profits necessary to fund existing and future capital investments.
- Recovers approximately 1 percent of total revenue from whey.
- If producer's proposal is adopted, would expect to reduce production from five days a week to three or four, further eroding profitability.
- Increased cost to consumers would be $0.07 to $0.11 per pound. Could not pass this on immediately only incrementally over time, thus absorbing the costs due to highly competitive markets.
- Support Institute proposal, but would prefer status quo.
- Attachment A: Milk Cost Increase per Month
- Attachment B: Milk Cost Increase Net Income Impact
- Attachment C: Price Increase Needed to Recover Cost Increase per Pound

CORNELL KASBERGEN
Testimony

- I have dairies in both California and Wisconsin and I get $2.00-$3.00 more per cwt. in Wisconsin.
- What milk that is bought under class price in FO is insignificant.
- It is a misconception that plants in FO don't have to pay the Class III price, they do.
- There is a shift in dairying in California, we are losing ground.
- Supports the producer proposal.

ALLOUETTE CHEESE USA, John Rutherford
Testimony

- Whey not captured in our cheese making process is a negative value, hauled away at an expense.
- Our whey, due to its composition cannot be comingled with whey from other cheese plants.
- It is not economically feasible to invest in the equipment to process whey ourselves.
- We are not able to set the price of our product, we are too small, we are price takers.
- Reduced margins cuts into investment in the plant and undermines the long term competitiveness of our plant.

- The producer proposal would increase the cost of milk without any recoverable benefit.
- Both proposals are equivalent to a tax on our facility for producing California milk.
- Supports no change, but would support Institute if changes are made.

REIN DOORNENBAL
Testimony

- Supports the milk pricing proposal submitted by the producer trade organizations.
- It is not the job of the Department to balance the milk supply, it is the coops job through base systems and contracts.
- Is not going to continue to produce milk at prices that are not relative to what prices dairymen in other areas of the U.S. are.
- The mindset of the dairy community has changed, no longer expanding the dairy business, instead will be working on more permanent crops and farming other crops.
- Doesn't believe that the reason California dairymen could produce milk for less than the rest of the country had anything to do with cheaper cost of goods.
- Exhibit 61: Picture of walnut trees, picture of almond trees and a picture of corn.
- Dairymen have to diversify in order to stay in business.
- Does not believe that other states pay less than Class III due to depooling, evidence from his sons that dairy out of state.
- Does not believe that the correlation between 4b and Class III is accurate, the spread is too wide.

MILK PRODUCERS COUNCIL, Rob Vandenheuvel
Testimony

- Supports the milk pricing proposal submitted by the producer trade organizations.
- The seven year average (2008-2014) of the difference between the cost of production and milk prices received shows a negative $0.77/cwt.
- A dairy with 1,000 cows, producing an average of 70 pounds of milk per day, over the same seven years, shows a net loss of $1,375,472.
- The average overbase price for the fourth quarter of 2014 was $19.00/cwt.
- The average overbase price for January-April 2015 was $13.91/cwt., thus showing milk prices have dropped.
- Comparing mailbox prices with California and the rest of the nation shows California is receiving less than the rest of the nation.
- Milk production in California compared to the U.S. average (from May 2008-April 2015) shows the U.S. increasing by 9.26 percent while California only increased 2.9 percent.
- More recent months (February 2015-April 2015) year over year change, show California decreasing while the U.S. averaged an increase.
- Class III is an appropriate benchmark on which to measure our Class 4b price against.
- Class 4b averaged $0.41/cwt. below federal order Class III from 2000-2009, but increased to $1.82/cwt. from 2010-present, questioning how this is a reasonable relationship and believes there is no justification for the gap.
- In contrast, Class 4a averaged $0.40/cwt. below from 2000-present (with only one exception in 2007).
- Had the producer proposal been in place for the past five years, the average 4b price would have still been below the Class III price by $0.38/cwt., and the overbase price would have been $0.67/cwt. higher.
- While MPC would prefer permanent price adjustment equal to Class III, the producer proposal closes the gap.

- Institute's proposal falls short of closing the gap between 4b and Class III.
- With only two weeks prior to the hearing to analyze Institute's proposed change of utilizing WPC34 instead of dry whey, there was not enough time to provide a complete analysis.
- Institute's claim of plants selling liquid whey are more closely tied to the WPC34 market is not enough rational to make the change.
- A temporary change of the dry whey price series to WPC34 could create additional instability between 4b and Class III.
- Attachment 1: Analysis of Statewide Cost of Production versus Milk Price Received, 2008-2014.
- Attachment 2: Mailbox Milk Prices, 2008-2015.
- Attachment 3: 2014 Receipts of Producer Milk by Regulated Handlers- Monthly and Year to Date.

RUMIANO CHEESE COMPANY, John Rumiano
Testimony

- While we have invested in whey disposal, it started out profitable, but it is now losing money.
- We are struggling to make a profit and have moved to co-manufacturing specialty cheese and buying and selling cheese from other manufactures to supplement the cheese manufacturing side of our business.
- Current outside purchase account for 75 percent of our business (with the majority of it from out of state), with 25 percent our own cheese manufacturing.
- Even a $0.25/cwt. increase in the cheese price, would cause us to purchase even more cheese from out of state.
- The cheese market is extremely competitive and doing business in California is very difficult.
- Supports the Institute proposal.

LEPRINO FOODS COMPANY, Sue Taylor
Testimony

- Supports the Institute proposal.
- Opposes the milk pricing proposal submitted by the producer trade organizations.
- Regulated milk prices must be set at levels that contribute to orderly marketing of milk and that can clear the market.
- The valuation of whey in a regulated milk price is challenging due to the lack of market value of dilute whey and the scale-related barrier due to high capital costs for small operators.
- When whey was included in the Federal orders in 2000, it was expected that the small cheese plants that did not process whey would recover the cost through increased premiums on specialty cheeses. During the first year of implementation, the whey factor contributed $0.29/cwt. to the Class III formula.
- When California included whey in the 4b formula in 2003, the contribution was just shy of $0.24/cwt., with the same thoughts on small cheese plants and recovery of costs through premiums.
- The years that followed inclusion of whey in the formulas showed an increasing challenge for plants that did not process whey as the price increased by over $3.00/cwt. at times in 2007 and cheese plants struggled and went out of business.
- In Federal orders, some were able to recoup the cost by selling whey to consolidators but as time goes on, that has become problematic. In addition, even plants that manufacture

whey are struggling due to whey values in the milk price formulas outstripping returns. Plants turned to negotiating outside the regulated price.

- In California, all plants must pay the regulated price and cannot elect out of minimum prices.
- In 2006-2007 three cheese plants suffered financial stress and were placed in the ineligible list for coverage under the Milk Producers Security Trust Fund, one proprietary plant sold, a coop producing cheese sold its cheese plant and one coop closed its cheese plant.
- CDFA overvalued whey in the formula and it was replaced with a fixed factor of $0.25/cwt. in 2007.
- Since then a sliding scale has replaced the fixed factor but many plants still cannot capture the value of whey from the market place.
- Per CDFA exhibit for this hearing, 45 of the 57 cheese plants in California do not process whey, thus 14.2 percent of the milk processed in Class 4b recover no value from whey.
- The producer proposal attributes more value to whey than the Class 4b formula did in 2007, and $0.12/cwt. more than Federal order formulas, where a safety value is provided through voluntary participation.
- Federal order valuation of is problematic, as cited in recent editorials by John Umhofer, of the Wisconsin Cheese Makers Association.
- Increase in prices to producers signals producers to increase production, while signaling cheese makers to reduce manufacturing capacity.
- Consideration of costs associated with the make allowance and FOB adjusters as these factors used in the pricing formula are under stated making upward adjustments in the whey factor an even greater threat to the viability of cheesemakers.
- The value of milk for cheese making in California is not the same as it is in Wisconsin.
- Location to the market (costing California $0.10-$0.15/pound to transport), discretionary minimum pricing in Federal orders, higher labor, utilities, environmental and taxes in California, depict the differences.
- Producer arguments on premiums paid in Wisconsin are overstated using higher fat and protein numbers.
- Hedging can be effective for producers if they use an effective hedging strategy incorporating a combination of cheese and whey contracts.
- Adjustments to the milk pricing structure should facilitate not inhibit export opportunities.
- Need to review the pricing system to collaborate about production concentration that threatens transparent data.
- Attachment A: Estimated Class 4b Milk Volume Without Whey Capacity
- Attachment B: Dairy Farmers of America Announces Changes to American Cheese Division
- Attachment C: Cheese Market News, What Way to Price Whey?

Post Hearing Brief

- Attachment A: Post Hearing Brief for Leprino, May 31-June, 2012 Hearing.
- Correction to an overstatement of premiums, the levels cited in testimony regarding WUD's fat and protein levels were incorrect, but conclusion remains that the premium levels inferred were overstated.
- Adoption of a price level higher than generated by Institute's proposal imperils the viability of roughly 14 percent of the cheese milk capacity that does not recover any value from whey.

Special 3-Minute Testimony Session

Pete Van Warmerdam
Testimony

- California has the lowest price/cwt.
- California has lost hundreds of dairy farms due to the pricing system.
- Production costs have gone up significantly.
- February mailbox price for California is $14.49/cwt., $3.00 less than Wisconsin at $17.58/cwt.
- Increase the price to reflect what we deserve.
- Drought has not affected us much yet.
- Supports the producer proposal.

Lucas Deniz
Testimony

- The pooling system is not perfect but fair, ensures stability and that producers get a fair market price.
- Currently the whey price is not fair, not getting an accurate market price for the value of whey.
- Producers cannot pass on increased costs, small processors are doing value added products and can pass some of their costs along.
- Cheddar cheese is the value used in the 4b formula and the majority of the cheese produced in the state is not Cheddar, it is cheeses that produce a much higher yield, so processors are capturing that value as well.
- Supports the milk pricing proposal submitted by the producer trade organizations.

Jerry Corda
Testimony

- Supports the milk pricing proposal submitted by the producer trade organizations.

Antoinette Duarte
Testimony

- The drought is expected to increase feed supplies especially locally grown feeds. It is expected that producers will increase from importing 50 percent of feed to 60-70 percent due to the drought.
- Low prices this year do not help shield farmers from the effects of the drought, like high prices did in 2014.
- Some silage fields are being converted to nut trees, some are fallowing fields or diverting water to other commodity crops, or selling it to nearby farms.
- Changes to rations will most likely reduce protein content in dairy diets and lower milk output.
- In an effort to sharpen their margins, producers will shrink their herds, cull less productive cows and move cows out of state, some are contemplating selling out.
- Wisconsin dairies are making more money than we are and their costs are much lower.
- Supports the milk pricing proposal submitted by the producer trade organizations.

Tom Barcellos
Testimony

- Supports the milk pricing proposal submitted by the producer trade organizations.

- Trees are replacing dairy farms as they sell out and are owned by out of country companies.
- Several dairies are awaiting the outcome of this hearing and the Federal order hearing to determine if they will convert to trees.
- I am deciding whether to invest in upgrading my leased facility or plant trees myself.

Frank Mendonsa
Testimony

- Supports the milk pricing proposal submitted by the producer trade organizations.
- The mindset of dairymen have changed since 2009, used to be everyone just milked cows and expanded for their kids, now they consider planting trees and encouraging their kids to do something else.

LOS ALTOS FOOD PRODUCTS INC., Adolfo Sanchez
Testimony

- In 2011 California produced 41.4 billion pounds of milk, in 2013 a rough year for dairymen, they produced 41.2 billion pounds of milk, the milk supply is not decreasing.
- Supports no change, but would support Institute if changes are made.
- Estimates that the proposed whey cost increase from the producer group will cost between $1.50 and $2.00/cwt., or $1.7-$2.2 million annually.
- It will cost jobs, decrease margins and threaten economic viability.
- Entered into the record: Letter dated September 12, 2013 from Corin Andrade, Chief Financial Officer, Los Altos Food Products Inc.

AGRICULTURE COUNCIL OF CALIFORNIA, Emily Rooney
Testimony

- Supports the milk pricing proposal submitted by the producer trade organizations.
- Increased production costs in 2014 are due to higher environmental, regulatory and labor costs.
- Impacts of the drought are an increasing economic burden to dairy farmers. UC Davis projects the drought will:
    - Decrease revenues and potentially increase feed costs.
    - Projects losses at $2.7 billion for California agriculture for 2015.
    - Losses will be due to fallowed acres, and increased pumping costs.
    - Losses will be uneven, greater in the San Joaquin Valley (Tulare, Kings and Kern Counties).
    - Cause further job losses.
- Labor statistics for unemployment rates for 2015 for Tulare, Kings and Kern are 13.2, 11.9 and 11.1 percent, respectively, while statewide unemployment was 6.5 percent.
- On farm costs have increased $8.00-9.00/cwt. but milk prices have not.
- The proposal will provide immediate relief by increase milk prices in the short term until a determination is made on the federal order.

Post-Hearing Brief

- Since 2007, California has lost 480 dairies.
- Milk production for the first part of 2015 has decreased compared to 2014.
- Submitted Preliminary Analysis: 2015 Drought Economic Impact Study conducted by UC Davis.

Written Testimony Received and Entered Into the Hearing Record

TONY P. CARDOZA
Testimony

- Supports the milk pricing proposal submitted by the producer trade organizations.
- Owned and operated a dairy in Visalia for 27 years, exited the business in 2012.
- Past Vice President and Manager of the Tulare Branch of Crocker National Bank and financed dairy and farming operations.
- Has a brokerage business selling dairy assets, cows, quota and real estate.
- Most of the livestock sold have moved out of state
- Watched dairy operations in the area demolished and planted almonds or pistachios in their place.
- Dairymen themselves have planted trees.
- Feels the demise of the dairy industry in California is directly related to the economics of operating in the state and the whey value that is less in California than in federal orders.

MARQUEZ BROTHERS INTERNATIONAL, INC.
Testimony

- The last five hearings have resulted in price increases that presented challenges to their company.
- Supports the Institute proposal.
- The Hispanic cheese market is highly price sensitive and very competitive.
- Invested in whey processing in 2004 to deal with rising environmental concerns with whey disposal and the cost of whey disposal, not the projected financial return.
- A plant must producer at least 1.2 million pounds of whey per day in order to reach the economies of scale necessary for a return on investment or to break even.
- An increase in the 4b price will result in small/medium size cheese plants to not recoup their investment and force small/medium plants out of business.
- Table 1: Input of total solids
- Table 2: Output of solids that stay with cheese and go with whey.
- Graph 1: Milk Solids cheese and whey
- Graph 2: Cheese and whey composition
- Input: a cheese plant will have milk input of approximately 12.3 percent total solids.
- Output: from the 12.3 percent of total solids, approximately 48 percent of the solids stay with the cheese and 52 percent go with the whey.
- For every 100 pounds of milk, you get 10 pounds of cheese and 90 pounds of whey.
- Of the whey solids, approximately 9.45 percent of the whey solids go into manufacturing WPC 8, 5.11 percent to whey cream and over 85 percent to permeate.
- In California, 57 plants make cheese, only 13 plants have some sort of whey concentration facilities
- Table 3: Whey Output
- Graph 3: Cheese and Whey Solids
- To capture maximum value from the whey stream you must have the ability to dry the whey. This is very expensive and subject to economies of scale.
- Small and medium plants don't have the ability to fund this type of whey operation, thus cannot keep up with the rising milk costs and cannot recoup the full whey value.
- Forty three plants representing approximately 75 percent of the 57 plants process less than 664 thousand pounds of liquid whey.

- Six plants representing 10.5 percent of the 57 plants process less than 1.4 million pounds of liquid whey per day.
- Thus, 50 plants would be severely financially impacted by the increase in the mil price, 43 plants would never recover their investment and 6 other plants will struggle to break even.
- Marquez incurs $1.5 million a year to dispose of whey and no milk allowance in the 4b price to cover disposal costs.
- Marquez invested $20 million in a whey protein plant, and have not seen a return on that investment, are years away from a return due to not enough volume.
- In federal orders, the entire value of whey minus a make allowance is captured in the Class III formula, paying producers for the value of whey that could be potentially generated not the value the cheesemaker extracted from whey.
- The lack of correlation between the 4b price and Class III price is not valid.
- Exhibit A: Pounds of Milk Processed into Cheese
- Exhibit B: Article by John Umhoefer, WCMA Perspectives, The Whey Problem and California's Solution

SIERRA NEVADA CHEESE COMPANY

Testimony

- Does not recover any value from whey.
- Has limited options on whey disposal.
- Due to the small scale of operation, has high cheese processing costs.
- Supports no change.

SEIFERT DAIRY, L.P.

Testimony

- Believes the current milk pricing system is no longer relevant to present conditions.
- Class 1 is no longer the driving force behind the market, cheese is now the primary use for California's milk supply.
- Receive higher premiums for this market change, due to investments they have made on the dairy.
- Huge investments have been made by cheese processors to discover more uses for milk and more market values
- It would be devastating if the increases to the whey factor would go into effect.
- Supports the status quo.