

Prepared Remarks for Federal Milk Marketing Order Hearing  
January 24, 2006  
Alexandria, Virginia

My name is Kelly Krug, I am the Director of Marketing Services for the California Department of Food and Agriculture. Thank you for the invitation to give a statement regarding the California Department of Food and Agriculture's use of manufacturing cost allowances. With me is Venetta Reed, Supervising Auditor from our agency who is prepared to give a more detailed summary and overview of the process of acquiring and posting manufacturing cost data for California manufacturing plants.

One of the functions within our Division is to collect cost data from California manufactured milk processing plants on a voluntary basis. The level of cooperation from plants is very high and the studies cover nearly all the production of the intended products in the analyses we perform. California's end-product dairy pricing formulas start with the wholesale prices for Grade AA butter, nonfat dry milk, and Cheddar cheese and subtract a manufacturing cost allowance to determine the value (price) for milk. It is customary for the Department to hold hearings generally, in response to industry petitions, to consider adjustments to pricing formulas including the values of the manufactured cost allowances.

A key factor for Department determinations that may adjust the manufacturing cost allowances for the Class 4a and 4b pricing formulas is the Department's work of conducting annual manufacturing cost studies to ascertain processing costs for butter, nonfat dry milk, and Cheddar cheese. The Department has a long standing history of relying on the processing cost study data combined with the relevant economic supply/demand factors to update the manufacturing cost allowances for butter, nonfat dry milk, and Cheddar cheese. Additionally, in 2003 the Department also added a make allowance factor for dry whey. At public hearings, interested parties are given an opportunity to provide testimony and evidence regarding the manufacturing cost data and any relevant economic factors that should be considered in evaluating the appropriate level of the manufacturing cost allowances.

Toward the goal of keeping the Department's cost studies as relevant and accurate as possible, in 2002 we employed a private accounting firm with experience the field of cost accounting to review the work of our Dairy Manufacturing Cost Unit. Following an extensive examination, the firm determined the methodology the Department has been using is sound and follows customary cost accounting techniques.

At this time, Venetta Reed will provide a more detailed summary of how we conduct the dairy manufactured cost studies.