

REBUTTAL TESTIMONY OF

RON MONG, CPA

Appearing on Behalf of the Area 4 Milk Dealers

Rebuttal Testimony before Pennsylvania Milk Marketing Board

Cost Replacement Hearing Based on 2018 Annual Reports

DECEMBER 4, 2019

Rebuttal Testimony of Ron Mong, CPA

Area 4 – Cost Replacement Hearing

I am Ronald W. Mong, Senior Manager at Herbein + Company, Inc. and my address is 2763 Century Blvd., Reading, PA 19610. I wish to present Rebuttal Testimony on behalf of the Area 4 Milk Dealers. I attach my Curriculum Vitae, as Rebuttal Exhibit D1, which outlines my education, and experience in the dairy industry.

Study Conducted

On behalf of the Area 4 Milk Dealers, I have reviewed the audit files and proposed adjustments prepared by the Pennsylvania Milk Marketing Board audit staff, have conducted fieldwork at each of the dealers in the cross-section and have prepared exhibits which present my findings.

Cost Replacement Process

This hearing will accomplish the annual cost replacement process in which the Pennsylvania Milk Marketing Board substitutes new cost information for the prior information, which is then utilized in developing its wholesale and resale prices. This hearing will include a container cost update utilizing April 2019 cost information as the new starting point for container updating. Once the cost replacement data is adopted, the April 2019 container costs will be updated monthly based upon cost information submitted by the cross-section dealers and reviewed by Board staff. This hearing will also include ingredient cost updating utilizing April 2019 cost information. Ingredient costs will then be updated on a quarterly basis for flavored milk, flavored reduced fat milk and flavored non-fat milk. These updates occur on January 1st, April 1st, July 1st, and October 1st of each year. All exhibits are prepared utilizing a weighted average based on each dealer's percentage of controlled sales in the area relative to its total sales of such products. All exhibits have been adjusted for inter-plant transfers. An inter-plant transfer is a transaction where a product is manufactured in one plant and transferred to an

affiliate plant that then sells the product to the ultimate consumer such that these exhibits have been prepared reflecting the sales to the ultimate consumer in the applicable area. This weighting and averaging method has been consistently applied from year to year.

Cross-Section

The Area 4 cross-section of dealers utilized includes Dean Dairy Holdings LLC dba Swiss Premium Dairy, Galliker Dairy (Johnstown), Harrisburg Dairies Inc., Rutter Brothers Dairy, Inc., Turkey Hill LP, and Tuscan/Lehigh Valley Dairies, Inc. (Schuylkill Haven). This is the same cross-section that was used in the prior hearing. The cross-section companies process, package and deliver most of the controlled milk products in Area 4 (65.0 percent). This group of companies includes organizations that deliver to supermarkets, convenience stores, schools, institutions, and small retail outlets. In my opinion this cross-section of dealers is representative of the dealers selling controlled milk products in Area 4.

Rebuttal Exhibits

Rebuttal Exhibit D2 reflects the processing, packaging, and delivery cost per point for calendar year 2018. Please note that the points presented are for sales in the PMMB Area 4 made by the cross-section dealers. These costs should replace the existing costs from 2017, which are currently being utilized by the Board in establishing prices. These costs are calculated in accordance with PMMB rules and regulations and have been consistently applied from the previous year. Our calculation of the processing, packaging, and delivery costs agrees with the amount expected to be presented by Board Staff on Staff Surrebuttal Exhibit 2.

Rebuttal Exhibit D2-A is prepared to reflect the effect of the cost replacement process by comparing the 2018 processing, packaging, and delivery costs in the current order with the 2017 processing, packaging, and delivery costs. Additionally, this exhibit reflects the 2019 cost increase

adjustment from Exhibit D7 and removes the 2018 cost increase adjustment. Including the cost update adjustments, the increase in the cross-section dealer costs from the prior cost replacement hearing is \$0.0048 per quart equivalent (point) or about two cents per gallon.

Exhibit D2 shows the number of points (quart equivalents) that are associated with each cost center. For example, the bottling department points for 2018 are 287,451,505 for the cross-section. This is a decrease of about 25,600,000 bottling points from 2017, which is about 8.2 percent.

Rebuttal Exhibit D3 and D3-A have been updated to container costs utilized in the October 2019 minimum resale price calculation. The container shrinkage factor reflected on this exhibit is a statewide average and will be utilized for all areas. This study was conducted for the period January to March 2009 and it is my opinion that it is reasonable to continue using this study's container shrinkage statistics for these Cost Replacement Hearings. There are no controlled milk products sold in Area 4 in paper half gallons, paper quarts, 12-ounce containers, or 10-ounce containers. The container sizes indicated with footnote (5) on Rebuttal Exhibit D3 and footnote (2) on Exhibit D3-A should continue to be updated monthly when minimum prices are announced using April 2019 as the new starting point.

Our container cost calculations agree with those calculated by Board Staff and expected to be presented in their Staff Surrebuttal Exhibit 3.

Rebuttal Exhibit D4 is prepared to present the ingredient costs per pound of finished product as of April 2019 for inclusion in the product formulas used in the monthly price announcements. Rebuttal Exhibit D4-A reflects the ingredient costs presented on Rebuttal D4 and shows the increase or decrease from the ingredient costs used in calculating the October 2019 minimum prices.

The ingredient costs are shown on D4 in cents per pound of finished product. The PMMB minimum price calculations multiply these ingredient costs per pound times the milk weight of each container size. For example, a quart of flavored milk weighs 2.0 pounds. The PMMB price formulas

would calculate the ingredient costs of a quart of flavored milk by multiplying the quart weight of 2.0 pounds times the ingredient cost of \$0.0439 per pound, which is \$0.0878 per quart.

Our ingredient cost calculations agree with those calculated by Board Staff and presented in their Staff Exhibit 4.

Rebuttal Exhibit D5 updates the cost of milk shrinkage and the costs and revenues from bulk cream and bulk milk transactions. Milk shrinkage in a dairy plant is the cost of milk that is purchased from dairy farmers or dairy cooperatives, but which is lost in the manufacturing process. The cross-section dairy plants have two types of bulk milk transactions. The first type of transaction is when raw milk not needed by the plant goes directly from the farm to another dairy plant. The plant buying the unneeded milk typically manufactures cheese or nonfat dry milk. The plant buying the milk can negotiate a price that is less than the price a fully regulated fluid milk plant must pay for that milk, so depending on market circumstances, this transaction (a diversion) can result in losses. The second type of transaction is when milk is received, standardized, and pasteurized, and then shipped to a food manufacturing plant. The purchasing plant could make candy, baked goods, puddings, soups, or many other varieties of food products. These transactions are called transfers. In Exhibit D5 both types of transactions are combined on the bulk milk row. Bulk cream sales occur at fluid milk plants because the butterfat test of the incoming raw milk is about 3.8% butterfat, and the average butterfat test of the packaged products sold is closer to 2.0% butterfat.

The PMMB monthly price calculations correctly account for the costs of milk shrinkage and the costs and revenues for the sales of bulk cream and bulk milk.

The current order establishes a net cost of \$0.0005 per pound and the new net cost, based on 2018 transactions is \$0.0003 per pound. There has been a new net change of (\$0.0002) per pound. That means overall these three transactions resulted in a slight cost decrease.

Our calculation of milk shrinkage costs and the costs and revenues of bulk milk and bulk cream transactions agree with those calculated by Board Staff and expected to be presented in their Staff Surrebuttal Exhibit 5.

Rebuttal Exhibit D6 reflects a comparison of the current order butterfat tests by product type and compares those tests with the 2018 actual butterfat tests. This exhibit also reflects the increase or decrease in butterfat content. Because the butterfat component of milk has a higher cost than the skim component, a decrease in butterfat content will result in a decrease in the cost of milk in the wholesale and resale prices. An increase in butterfat content will increase the cost of milk in finished products. I recommend that the Board replace the current butterfat by product with the 2018 tests reflected on this exhibit.

Our calculations of butterfat content by product type agree with those calculated by Board Staff and presented in their Staff Exhibit 6.

Rebuttal Exhibit D7 is prepared to calculate the cost increases and decreases incurred during the six (6) month period ending June 30, 2019 with the six (6) month period ending June 30, 2018 for three important cost categories in a dairy plant. These three costs are: labor and fringe benefits, utilities, and insurance. This adjustment allows for an updating of significant costs, which can change materially from year to year. The weighted points for the first six (6) months of 2019 are 129,452,912, which is (1.9%) less than the weighted points for the first six (6) months of 2018. In 2019 the three cost categories used in this calculation decreased \$441,663 or (2.3%) compared to 2018.

Our calculation of the cost increases for labor, insurance and utility agree with those calculated by Board Staff and presented in their Staff Exhibit 7.

Rebuttal Exhibit D8 has been updated to reflect the August 2019 diesel fuel costs, which were used in calculating the minimum prices for October 2019. Additionally, this exhibit reflects the

calculation of the average diesel fuel cost for calendar year 2018, which becomes the new starting point for the monthly adjustments. I recommend that this adjustment be continued monthly. The average diesel fuel cost for 2018 for the cross-section dealers is \$0.0110 per point. This amount varies in each area based on distances traveled, delivery sizes, and fleet fuel efficiency.

Rebuttal Exhibit D9 has been updated to reflect October 2018 natural gas costs and reflects OGO A-937 effective June 1, 2006 concerning heating fuel costs. Additionally, this exhibit reflects the calculation of the average heating fuel cost for calendar year 2018, which becomes the new starting point for the monthly adjustments. I recommend that this adjustment be continued monthly.

Our calculation of the cost increases for the diesel fuel adjustment and the heating fuels adjustment agree with those calculated by Board Staff and presented in their Staff Exhibits 8 & 9.

Container Efficiency Adjustment

An important part of the calculation of PMMB's minimum resale prices is the container efficiency adjustment. These adjustments are in place to allocate the fluid milk processors' costs appropriately to the various sizes of containers sold. The impact of the container efficiency adjustment is to deduct costs from the two larger packages, gallons and half gallons, and to add costs to the smaller containers. Our calculation of updated container efficiency adjustments is shown at Exhibit D10.

The container efficiency adjustment was implemented to be revenue neutral, meaning the container efficiency adjustment did not add costs and did not generate new revenue. The adjustments as originally calculated added a dollar of costs to the smaller containers for every dollar deducted from the larger containers. When correctly calculated the container efficiency adjustments will not be a revenue-generation tool, but instead will serve as a cost allocation tool. The plusses should equal the minuses so that the total of plusses and minuses foots to zero.

The container efficiency adjustment has two components:

- 1) Bottling costs allocation – based on filling speeds at each processing plant
- 2) Cold room and delivery costs allocation – based on number of units packed in a plastic

milk case.

Bottling Cost Center

The 2018 bottling cost center costs shown on Exhibit D2 are \$0.0423 per point. This is an average of all sizes packaged at all the cross-section plants. Our calculation starts with this average cost. The goal of the calculation, which we achieved, is to adjust the average bottling cost center costs for the individual container sizes so that in total the average cost per point remained \$0.0423.

Cold Room and Delivery Cost Centers

The 2018 cold room cost center costs shown on Exhibit D2 are \$0.0384 per point and 2018 delivery cost center costs per point are \$0.0999 per point. An allocation of the costs in these in two cost centers is needed because dairy container packages are not sold individually but in plastic milk cases. The dairy employees handle these cases and not the individual units. Each plastic case holds a different number of points for each container size.

We calculated the number of milk cases each plant used to handle the containers it sold in 2018. We allocated the total cold room and delivery costs to each size based on the number of milk cases used for that size. As we did in the bottling cost center allocation, we made certain we only allocated the actual costs at that plant. No additional costs were added or deducted. The cold room and delivery costs pluses and minuses were equal. The adjustments were revenue neutral.

Exhibit D10

Exhibit D10 shows the results of our container efficiency update calculations. The actual quantity of each size container is shown in the first column. These quantities are multiplied by our

calculated container efficiency adjustments to determine the impact on cross-section dealer revenue. For example, the updated adjustments would allocate \$1,380,279 of costs out of the gallon package and add \$1,110,254 of costs to the paper half pint. The net effect of the plusses and minuses is revenue to the dealers of \$1,538. This isn't zero because we are only calculating the container efficiency adjustments to four decimal places, but in the world of accounting this kind of small difference due to rounding is reasonable.

I recommend that the container efficiency adjustments be updated in this cost replacement hearing.

Summary

Rebuttal Exhibit D11-A and D11-B are prepared to reflect the wholesale minimum price for a gallon of reduced fat milk and a half pint of flavored non-fat milk for October 2019. These exhibits also cross-reference the exhibits that support the individual line items.

Class II Controlled Products

The annual cost replacement process could include an updating of Class II product costs. Class II controlled products include half & half, light cream, sour cream, and heavy cream. We are not presenting any recommendation to change the method used for Class II pricing. We ask that the Board continue with the existing methodology. The Area 4 milk dealers have considered and will continue to review other approaches but do not see a need for modifying the status quo.

Rate of Return

I recommend that the Board maintain the rate of return for the Area 4 dealers at 3.4%, or increase it to 3.5%. Milk dealers in Area 4 and across the Commonwealth are facing a serious battle for profitability as fluid milk demand continues to decline year-over-year.

I reviewed the Statements of Operations for the year ended 12/31/2018 for the five cross-section dealers. These are submitted by the dealers on Exhibit B of the PMMB-60 Milk Dealer's Financial Statement. The 2018 weighted average rate of return for the Area 4 cross-section dealers was a profit of 4.0%. However, most of the profit comes from the cross-section dealers that have more than 33% of their bottling points from non-controlled products. The operating profit of the cross-section dealers with less than 20% of their bottling points from non-controlled products is 1.5%, which is low by industry standards and below the statutory minimum. As I mentioned in the other hearings, one factor affecting profitability that adversely affects dealers predominantly focusing on milk rather than non-controlled products is that cost replacement lags the period when the operating costs were incurred. Given this profit and loss situation, it is essential that the Board continue the rate of return of 3.4%, or increase it to 3.5%.

Summary and Recommendation

The Area 4 Milk Dealers recommend that the Milk Marketing Board make the cost replacement adjustments, which are reflected in my testimony and exhibits. Thank you for your consideration of my analysis and opinions.

AREA 4

COST REPLACEMENT HEARING DEALER REBUTTAL EXHIBITS

DECEMBER 4, 2019

PMMB AREA 4

DECEMBER 4, 2019 COST REPLACEMENT HEARING

INDEX OF REBUTTAL EXHIBITS

**Dean Dairy Holdings LLC dba Swiss Premium Dairy, Galliker Dairy (Johnstown),
Harrisburg Dairies Inc., Rutter Brothers Dairy, Inc., Turkey Hill LP,
Tuscan/Lehigh Valley Dairies, Inc. (Schuylkill Haven)**

Rebuttal Exhibit D1	Ronald W. Mong, CPA Curriculum Vitae
Rebuttal Exhibit D2	Processing, Packaging and Delivery Costs/Point
Rebuttal Exhibit D2-A	Cost Replacement Adjustments for Processing, Packaging and Delivery Costs
Rebuttal Exhibit D3	Summary of Current Container Costs with Adjustments for Shrinkage and Loss and Update to Current Month
Rebuttal Exhibit D3-A	Adjusted Container Costs Compared to Current Month Container Costs
Rebuttal Exhibit D4	Summary of Current Ingredient Costs
Rebuttal Exhibit D4-A	Cost Replacement Adjustments for Ingredients
Rebuttal Exhibit D5	Weighted Cost of Shrinkage and Weighted Costs and Revenues from Bulk Cream and Bulk Milk
Rebuttal Exhibit D6	Butterfat Content of Price Controlled Products
Rebuttal Exhibit D7	Cost Increases (Decreases) for Labor, Insurance and Utility Costs
Rebuttal Exhibit D8	Changes in Diesel Fuel Costs
Rebuttal Exhibit D9	Changes in Heating Fuel Costs (Natural Gas)
Rebuttal Exhibit D10	Adjustments for Container Efficiencies Due to Container Size
Rebuttal Exhibit D11A	Calculation of Minimum Wholesale Price Gallon Reduced Fat Milk (2%)
Rebuttal Exhibit D11B	Calculation of Minimum Wholesale Price Half Pint Flavored Nonfat Milk (Skim)

Ronald W. Mong, CPA
Curriculum Vitae

EDUCATION

Pennsylvania State University – B.S. Degree in Accounting, High Distinction (1977)

EMPLOYMENT

Herbein + Company, Inc., Reading, PA

2003 to present

Senior Manager – Dairy Consulting

- Cost benchmarking
- Milk shrinkage reduction projects
- Dairy accounting seminars
- Regulatory issues – PA Milk Marketing Board, Federal Milk Marketing Orders, other state regulatory agencies
- Mergers and acquisitions
- Specialized financial reporting for dairy businesses
- Software installation assistance
- Dairy cost accounting for basic and complex products

Wilcox Farms, Inc., Roy, WA

2001 – 2003

Director of Finance & Administration (CFO)

- Developed and implemented a Balanced Financial Scorecard
- Supervised and trained accounting, office, and information technology staff at multiple locations
- Negotiated innovative bank financing package that significantly lowered interest costs
- Successfully managed the financial, banking, and accounting aspects of a significant acquisition

Herbein Consulting, Inc., Reading, PA

1999 – 2001

Manager – Dairy Financial Consulting

- Performed a variety of financial consulting services to dairy processing plants of varying sizes, product lines, and locations
- Served as interim CFO for dairy companies during personnel transitions
- Developed content for the IDFA Dairy Cost Accounting workshops

Ronald W. Mong, CPA

Schneider's Dairy, Inc., Pittsburgh, PA

1996 – 1999

General Manager, Mong Dairy Division

- Profitably managed and grew an ice cream manufacturing and dairy distribution business
- Successfully managed transition from non-union to union workforce
- Effectively directed sales, purchasing, personnel, distribution, maintenance, and accounting functions

Mong Dairy, Inc., Seneca, PA

1990 – 1996

President

- Expanded market share and distribution area
- Increased product lines and installed new packaging line
- Effectively positioned company for sale

1979 – 1990

Vice President and Controller

- Selected, planned, and installed first computerized accounting system
- Successfully reorganized work to reduce office staff by 50%
- Increased sales with key accounts
- Developed and implemented financial reporting

Arthur Andersen & Co., Pittsburgh, PA

1977 – 1979

Senior Accountant

- Supervised audit and tax work for a variety of public and private clients

PROFESSIONAL AND CIVIC ASSOCIATIONS AND DESIGNATIONS

CPA – Commonwealth of Pennsylvania

Firm Member – Allinial Global

Member – American Institute of Certified Public Accountants (AICPA)

Member – Pennsylvania Institute of Certified Public Accountants (PICPA)

Board of Directors – Pennsylvania Association of Milk Dealers

Board of Directors, Secretary-Treasurer – National Ice Cream Mix Association

Board of Governors & Insurance Committee – Manufacturer's Association of Northwest Pennsylvania

Board of Directors – Oil City Area Chamber of Commerce

Board of Directors (charter) – MilkPEP

Chairman of the Board – Oil City Housing Authority

Ronald W. Mong, CPA

PROFESSIONAL AND CIVIC ASSOCIATIONS AND DESIGNATIONS (Cont'd)

Board of Directors – Venango County United Way

Chairman of Administrative Board – Calvary United Methodist Church

Distinguished Service Award – Oil City Jaycees

COURSES INSTRUCTED

International Dairy Foods Association (IDFA) Dairy Cost Accounting Workshop – May 16, 2006

International Dairy Foods Association (IDFA) Dairy Cost Accounting Workshop – May 16, 2007

Dairylea Cooperative – Dairy Accounting 101 & 102 – May 2008

International Dairy Foods Association (IDFA) Dairy Cost Accounting Workshop – May 14, 2008

International Dairy Foods Association (IDFA) Dairy Cost Accounting Workshop – May 13, 2009

International Dairy Foods Association (IDFA) Dairy Cost Accounting Workshop – May 11-12, 2010

Dean Foods – Northeast Marketing Area Federal Order 1 – July 20-21, 2010

International Dairy Foods Association (IDFA) NEW Dairy Cost Accounting Workshop – May 11, 2011

International Dairy Foods Association (IDFA) Dairy Accounting & Finance Workshop – May 15-16, 2012

Farmland Dairy – Dairy Accounting Workshop – August 21-22, 2012

Wawa – Dairy Accounting Workshop – November 7, 2012

HP Hood – Dairy Accounting Workshop – February 12-13, 2013

International Dairy Foods Association (IDFA) Dairy Accounting & Finance Workshop – May 14-15, 2013

Saputo Dairy – Dairy Accounting Workshop – April 15, 2014

International Dairy Foods Association (IDFA) Dairy Accounting & Finance Workshop – May 20-21, 2014

Webinar – Intro to Dairy Product Costing – September 10, 2014

Webinar – Applying Dairy Product Costing to Finished Products – September 17, 2014

Webinar – Advanced Milk Accounting Topics – September 24, 2014

International Dairy Foods Association (IDFA) Dairy Accounting & Finance Workshop – May 12-13, 2015

Rutter's – Dairy Accounting Workshop – November 4, 2015

Dean Foods – Dairy Accounting Workshop – April 27, 2016

International Dairy Foods Association (IDFA) Dairy Accounting & Finance Workshop –
November 16-17, 2016

Kemps LLC – Dairy Accounting Workshop – December 15, 2016

Byrne Dairy – Dairy Accounting Workshop – April 11-12, 2017

International Dairy Foods Association (IDFA) Dairy Accounting & Finance Workshop –
December 12-13, 2017

Dean Foods – Dairy Accounting Workshop – January 10, 2018

Webinar Series – California Federal Milk Marketing Order – September 13, 20, & 27, 2018

Dairy Institute of California - Milk Pricing & Cost Accounting Workshop – October 17-18, 2018,
October 24-25, 2018

Submitted: November 15, 2019

Ronald W. Mong, CPA

COURSES INSTRUCTED (Cont'd)

Readington Farms - Milk Pricing & Cost Accounting Workshop – January 14-15, 2019

Maryland & Virginia Milk Producers Cooperative - Milk Pricing & Cost Accounting Workshop –
January 31- February 1, 2019

Johanna Foods- Milk Pricing & Cost Accounting Workshop – July 29-30, 2019

Dairy Farmers of America- Milk Pricing & Cost Accounting Workshop – September 19-20, 2019

SPECIFIC DAIRY RELATED EXPERIENCE

Considerable experience in implementing the prices and regulations of the Pennsylvania Milk Marketing Board; has presented sworn testimony in General Price Hearings.

Extensive experience in costing, pricing, and marketing of milk, cultured products, and ice cream.

Significant experience in production, distribution, and quality assurance of dairy products.

Management experience includes both union and non-union environments.

Great deal of experience in the installation and ongoing operation of the major computerized route accounting systems.

Served on the Charter of Board of Directors of the National Fluid Milk Promotion Board (MilkPEP), the group that developed the now-famous “milk mustache” ads.

EXPERT WITNESS TESTIMONY

Pennsylvania Milk Marketing Board – Expert Testimony – Over Price Premium Adjustment Hearing (hearing held February 2, 2005)

Pennsylvania Milk Marketing Board – Expert Testimony – Area 5 and Area 6 Cost Replacement Hearings (hearings held on March 11, 2019)

Pennsylvania Milk Marketing Board – Expert Testimony – Area 2 and Area 4 Cost Replacement Hearings (hearings held on April 3 and May 1, 2019)

Pennsylvania Milk Marketing Board – Expert Testimony – Area 1 and Area 3 Cost Replacement Hearings (hearings held on May 1, 2019)

Pennsylvania Milk Marketing Board – Expert Testimony – Area 3, Area 5, and Area 6 Cost Replacement Hearings (hearings held on November 6, 2019)

PMMB AREA 4

DECEMBER 4, 2019 COST REPLACEMENT HEARING

PROCESSING, PACKAGING AND DELIVERY COSTS/POINT
(WEIGHTED AVERAGE BASED ON SALES IN AREA 4)

Dean Dairy Holdings LLC dba Swiss Premium Dairy, Galliker Dairy (Johnstown),
Harrisburg Dairies Inc., Rutter Brothers Dairy, Inc., Turkey Hill LP,
Tuscan/Lehigh Valley Dairies, Inc. (Schuylkill Haven)

<u>Cost Center</u>	<u>Total 2018 Points in PMMB Area 4 (1)</u>	<u>Weighted Average 2018 Cost/Point (1)</u>
Receiving, lab and field work	155,159,418	\$ 0.0206
Standardization and pasteurization	319,975,057	0.0144
Bottling	287,451,505	0.0423
Cold room	305,973,688	0.0384
Delivery	155,007,145	0.0999
Selling	143,700,414	0.0285
		<u>\$ 0.2441</u>

(1) Reflects points (and related cost/point) for sales in PMMB Area 4 for the cross-section dealers.

PMMB AREA 4

DECEMBER 4, 2019 COST REPLACEMENT HEARING

COST REPLACEMENT ADJUSTMENTS FOR PROCESSING, PACKAGING AND DELIVERY COSTS

Dean Dairy Holdings LLC dba Swiss Premium Dairy, Galliker Dairy (Johnstown),
 Harrisburg Dairies Inc., Rutter Brothers Dairy, Inc., Turkey Hill LP,
 Tuscan/Lehigh Valley Dairies, Inc. (Schuylkill Haven)

	2018 Weighted Average Cost/Point	2017 Cost/Point Included in Existing Order (1)	Increase (Decrease)
Receiving, lab and field work	\$0.0206	\$0.0180	\$0.0026
Standardization and pasteurization	0.0144	0.0179	(0.0035)
Bottling	0.0423	0.0393	0.0030
Cold room	0.0384	0.0352	0.0032
Delivery	0.0999	0.1037	(0.0038)
Selling	<u>0.0285</u>	<u>0.0298</u>	<u>(0.0013)</u>
Sub total	\$0.2441	\$0.2439	\$0.0002
Add:			
2019 Cost increase (decrease) adjustment - Exhibit D7			(0.0005)
Less:			
2018 Cost (increase) decrease adjustment (1)			<u>0.0051</u>
Net change			<u><u>\$0.0048</u></u>

**PMMB AREA 4
DECEMBER 4, 2019 COST REPLACEMENT HEARING**

**SUMMARY OF CURRENT CONTAINER COSTS WITH ADJUSTMENT FOR SHRINKAGE AND LOSS AND
UPDATE TO CURRENT MONTH**

**Dean Dairy Holdings LLC dba Swiss Premium Dairy, Galliker Dairy (Johnstown),
Harrisburg Dairies Inc., Rutter Brothers Dairy, Inc., Turkey Hill LP,
Tuscan/Lehigh Valley Dairies, Inc. (Schuylkill Haven)**

Container Size	Adjust from		Subtotal	Calculated Shrinkage and Loss (4)	Shrinkage Cost	Total Container Cost
	April 2019 Container Cost (1)	April 2019 to September 2019 - Current (2)				
Gallon (5)	\$ 0.1941	\$ 0.0034	\$0.1975	1.18%	\$ 0.0023	\$ 0.1998
1/2 gallon - plastic	0.1425					
1/2 gallon - paper	(3)					
1/2 gallon - blended (5)	<u>0.1425</u>	0.0021	0.1446	1.25%	0.0018	0.1464
Quart - plastic	0.1402					
Quart - paper	(3)					
Quart - blended (5)	<u>0.1402</u>	(0.0020)	0.1382	1.57%	0.0022	0.1404
Pint - plastic	0.1280					
Pint - paper	0.0413					
Pint - blended (5)	<u>0.1264</u>	(0.0009)	0.1255	1.62%	0.0020	0.1275
Twelve ounce	(3)					
Ten ounce	(3)					
1/2 pint - plastic (5)	0.0693	(0.0012)	0.0681	0.92%	0.0006	0.0687
1/2 pint - paper (5)	0.0303	0.0007	0.0310	0.85%	0.0003	0.0313
Four ounce - paper	0.0310		0.0310	1.53%	0.0005	0.0315
Dispenser	0.0469		0.0469	1.30%	0.0006	0.0475

- (1) For containers not purchased in April 2019 the most recent invoice was used.
- (2) September 2019 container costs were used by the PMMB to establish minimum resale prices for October 2019.
- (3) Container not packaged in this Area.
- (4) Calculated based on actual container loss from a state-wide cross section of processing dealers for controlled containers used during the period January – March 2009. This state-wide cross section is composed of every processing dealer that participates in a cost replacement hearing.
- (5) Current container costs would replace these costs monthly when the PMMB minimum resale prices are announced.

PMMB AREA 4

DECEMBER 4, 2019 COST REPLACEMENT HEARING

ADJUSTED CONTAINER COSTS COMPARED TO CURRENT MONTH
CONTAINER COSTS – MARCH 2019

Dean Dairy Holdings LLC dba Swiss Premium Dairy, Galliker Dairy (Johnstown),
Harrisburg Dairies Inc., Rutter Brothers Dairy, Inc., Turkey Hill LP,
Tuscan/Lehigh Valley Dairies, Inc. (Schuylkill Haven)

<u>Container Size</u>	<u>Adjusted Container Costs from Exhibit D3</u>	<u>Container Costs in Current Prices (1)</u>	<u>Difference</u>
Gallon (2)	\$ 0.1998	\$ 0.1652	\$ 0.0346
Half Gallon (2)	0.1464	0.1230	0.0234
Quart (2)	0.1404	0.1413	(0.0009)
Pint (2)	0.1275	0.1253	0.0022
1/2 pint - plastic (2)	0.0687	0.0636	0.0051
1/2 pint - paper (2)	0.0313	0.0307	0.0006
Four ounce - paper	0.0315	0.0304	0.0011
Dispenser (per quart)	0.0475	0.0436	0.0039

(1) Per General Order No. A-963 (CRO 9) as updated.

(2) These container costs to be updated monthly.

PMMB AREA 4

DECEMBER 4, 2019 COST REPLACEMENT HEARING

SUMMARY OF INGREDIENT COSTS
(WEIGHTED AVERAGE BASED ON ACTUAL SALES IN AREA 4)

Dean Dairy Holdings LLC dba Swiss Premium Dairy, Galliker Dairy (Johnstown),
Harrisburg Dairies Inc., Rutter Brothers Dairy, Inc., Turkey Hill LP,
Tuscan/Lehigh Valley Dairies, Inc. (Schuylkill Haven)

	April 2019 Ingredient Cost Per Pound (1)
Standard	\$.0000
Reduced fat (2%) milk	.0001
Lowfat (1%) milk	.0002
Nonfat (skim) milk	.0024
Flavored milk	.0439
Flavored reduced fat milk	.0363
Flavored nonfat milk	.0269
Buttermilk	.0385
Eggnog	.1720

(1) For ingredients not purchased in April 2019 the most recent invoice was used.

PMMB AREA 4

DECEMBER 4, 2019 COST REPLACEMENT HEARING

COST REPLACEMENT ADJUSTMENTS FOR INGREDIENTS

Dean Dairy Holdings LLC dba Swiss Premium Dairy, Galliker Dairy (Johnstown),
Harrisburg Dairies Inc., Rutter Brothers Dairy, Inc., Turkey Hill LP,
Tuscan/Lehigh Valley Dairies, Inc. (Schuylkill Haven)

	<u>April 2019 Weighted Average Cost/Pound</u>	<u>Cost/Pound included in Existing Order (1)</u>	<u>Increase (Decrease)</u>
Standard milk	\$0.0000	\$0.0000	\$0.0000
Reduced fat milk (2%)	0.0001	0.0001	0.0000
Lowfat milk (1%)	0.0002	0.0015	(0.0013)
Nonfat milk (skim)	0.0024	0.0016	0.0008
Flavored milk (2)	0.0439	0.0428	0.0011
Flavored reduced fat milk (2)	0.0363	0.0350	0.0013
Flavored nonfat milk (2)	0.0269	0.0271	(0.0002)
Buttermilk	0.0385	0.0318	0.0067
Eggnog	0.1720	0.1732	(0.0012)

(1) Per General Order OGO A-963 (CRO 9) as updated for flavored milks on October 1, 2019.

(2) Ingredient costs to be updated on a quarterly basis for flavored milk, flavored reduced fat milk and flavored nonfat milk. Updates should be effective on January 1, April 1, July 1 and October 1.

PMMB AREA 4

DECEMBER 4, 2019 COST REPLACEMENT HEARING

WEIGHTED COST OF SHRINKAGE AND WEIGHTED COSTS AND REVENUES FROM BULK CREAM AND BULK MILK

Dean Dairy Holdings LLC dba Swiss Premium Dairy, Galliker Dairy (Johnstown),
 Harrisburg Dairies Inc., Rutter Brothers Dairy, Inc., Turkey Hill LP,
 Tuscan/Lehigh Valley Dairies, Inc. (Schuylkill Haven)

PMMB Area 4	Weighted Net		Weighted Pounds	Weighted Cost (Revenue) Per Pound
	Costs	Revenues		
Shrinkage	\$ 962,339	\$ 962,339		
Bulk milk revenue minus milk costs		(159,437)		
Bulk milk cost center costs & freight	5,690			
Net bulk milk cost (revenue)		165,127		
Bulk cream revenue minus milk costs		1,361,168		
Bulk cream cost center costs	310,854			
Net bulk cream cost (revenue)		(1,050,314)		
Total	<u>\$ 1,278,883</u>	<u>\$ 1,201,731</u>		
Net cost (net revenue) - calendar year 2018	\$ 77,152		287,093,951	\$ 0.0003
Net cost (net revenue) in current order - calendar year 2017	\$ 178,414		329,277,645	0.0005
Net change - cost increase (cost reduction)	<u>\$ (101,262)</u>			<u>\$ (0.0002)</u>

PMMB AREA 4

DECEMBER 4, 2019 COST REPLACEMENT HEARING

BUTTERFAT CONTENT OF PRICE CONTROLLED PRODUCTS

Dean Dairy Holdings LLC dba Swiss Premium Dairy, Galliker Dairy (Johnstown),
 Harrisburg Dairies Inc., Rutter Brothers Dairy, Inc., Turkey Hill LP,
 Tuscan/Lehigh Valley Dairies, Inc. (Schuylkill Haven)

	2018 Weighted Average Butterfat Test	Butterfat Test included in Existing Order (1)	Increase (Decrease)
Standard milk	3.3030%	3.2958%	0.0072%
Reduced fat milk (2%)	2.0013%	1.9788%	0.0225%
Lowfat milk (1%)	0.9868%	0.9683%	0.0185%
Nonfat milk (skim)	0.1014%	0.1040%	-0.0026%
Flavored milk	3.3647%	3.2310%	0.1337%
Flavored reduced fat milk	1.0387%	1.0271%	0.0116%
Flavored nonfat milk	0.0488%	0.0667%	-0.0179%
Buttermilk	0.9991%	0.9996%	-0.0005%
Eggnog	7.1482%	6.9765%	0.1717%

(1) Per General Order No. A-963 (CRO 9)

PMMB AREA 4

DECEMBER 4, 2019 COST REPLACEMENT HEARING

COST INCREASES (DECREASES) FOR LABOR, INSURANCE AND UTILITY COSTS

Dean Dairy Holdings LLC dba Swiss Premium Dairy, Galliker Dairy (Johnstown),
 Harrisburg Dairies Inc., Rutter Brothers Dairy, Inc., Turkey Hill LP,
 Tuscan/Lehigh Valley Dairies, Inc. (Schuylkill Haven)

Type of Expense	Weighted Expenses for the Six Months Ended June 30 (1)		Weighted Points for the Six Months Ended June 30 (1)		Cost Per Point		Increase (Decrease) Per Point
	2019	2018	2019	2018	2019	2018	
Labor and fringe benefits	\$ 17,921,448	\$ 18,604,608	129,452,812	131,917,052	\$ 0.1384	\$ 0.1410	(\$0.0026)
Utilities	708,613	716,489	129,452,812	131,917,052	0.0055	0.0054	0.0001
Insurance	505,199	255,826	129,452,812	131,917,052	0.0039	0.0019	0.0020
					<u>\$0.1478</u>	<u>\$0.1483</u>	<u>(\$0.0005)</u>

(1) Weighted based on sales in PMMB Area 4

PMMB AREA 4

DECEMBER 4, 2019 COST REPLACEMENT HEARING

CHANGES IN DIESEL FUEL COSTS

Dean Dairy Holdings LLC dba Swiss Premium Dairy, Galliker Dairy (Johnstown),
Harrisburg Dairies Inc., Rutter Brothers Dairy, Inc., Turkey Hill LP,
Tuscan/Lehigh Valley Dairies, Inc. (Schuylkill Haven)

Diesel fuel costs – calendar year 2018 (1)	\$1,711,008
Delivery points – calendar year 2018 (1)	<u>155,007,145</u>
Diesel fuel cost per point delivered	<u><u>\$0.0110</u></u>
Average diesel price – calendar year 2018 (2)	\$3.361
Average diesel price – August 2019 (2) (3)	<u>\$3.208</u>
Increase (decrease) from year 2018 to month August 2019	-4.55%
Increase (decrease) in diesel fuel cost per point delivered	<u><u>(\$0.0005)</u></u>

- (1) Costs of cross-section dealers weighted by sales in Area 4.
- (2) On-highway diesel prices per gallon for the Central Atlantic Region as published by the U.S. Energy Information Administration.
- (3) August 2019 diesel fuel costs were used by the PMMB in establishing minimum prices for October 2019.

PMMB AREA 4

DECEMBER 4, 2019 COST REPLACEMENT HEARING

CHANGES IN HEATING FUEL COSTS (NATURAL GAS)

Dean Dairy Holdings LLC dba Swiss Premium Dairy, Galliker Dairy (Johnstown),
Harrisburg Dairies Inc., Rutter Brothers Dairy, Inc., Turkey Hill LP,
Tuscan/Lehigh Valley Dairies, Inc. (Schuylkill Haven)

Heating fuel costs – calendar year 2018 (1)	\$131,159
Standardization & pasteurization points – calendar year 2018 (1)	319,975,057
	<hr/>
Heating fuel cost per point pasteurized	<u>\$0.0004</u>
Average heating fuel costs – calendar year 2018 (2)	\$8.68
Average heating fuel costs – June 2019 (2) (3)	<u>8.35</u>
Increase (decrease) from year 2018 to month June 2019	-3.80%
Increase (decrease) in heating fuel cost per point pasteurized	<u>\$0.0000</u>

- (1) Costs of cross-section dealers weighted by sales in Area 4.
- (2) Industrial natural gas prices for Pennsylvania in dollars per thousand cubic feet as published by the U.S. Energy Information Administration.
- (3) November 2018 natural gas costs were used by the PMMB in establishing minimum prices for March 2019.

PMMB AREA 4
 DECEMBER 4, 2019 COST REPLACEMENT HEARING

ADJUSTMENTS FOR CONTAINER EFFICIENCIES
 DUE TO CONTAINER SIZE

Dean Dairy Holdings LLC dba Swiss Premium Dairy, Galliker Dairy (Johnstown),
 Harrisburg Dairies Inc., Rutter Brothers Dairy, Inc., Turkey Hill LP,
 Tuscan/Lehigh Valley Dairies, Inc. (Schuylkill Haven)

<u>Container Size</u>	<u>Container Quantities Sold by Cross-Section Dealers in 2018 in Area 4</u>	<u>Proposed Container Efficiency Adjustments</u>	<u>Impact on Cross-Section Dealer Revenue</u>	<u>Container Efficiency Adjustments in Current Order (1)</u>	<u>Impact on Cross-Section Dealer Revenue</u>
Gallon	16,894,478	\$ (0.0817)	\$ (1,380,279)	\$ (0.0667)	\$ (1,126,862)
Half gallon	14,052,059	(0.0404)	(567,703)	(0.0354)	(497,443)
Quart	3,520,516	0.0208	73,227	0.0213	74,987
Pint	6,886,525	0.0914	629,428	0.0868	597,750
Half pint - plastic	3,383,951	0.0245	82,907	0.0250	84,599
Half pint - paper	45,316,473	0.0245	1,110,254	0.0250	1,132,912
4 oz.	931,845	0.0338	31,496	0.0393	36,622
Dispenser (per quart)	941,036	0.0236	22,208	0.0270	25,408
Net impact on cross-section dealer revenues			\$ 1,538		\$ 327,973

(1) Per OGO A-963 (CRO 9) as updated.

REBUTTAL EXHIBIT D11-A

PMMB AREA 4
 DECEMBER 4, 2019 COST REPLACEMENT HEARING
 CALCULATION OF WHOLESALE MINIMUM PRICE
 GALLON REDUCED FAT MILK (2%) FOR OCTOBER 2019
 Dean Dairy Holdings LLC dba Swiss Premium Dairy, Galliker Dairy (Johnstown),
 Harrisburg Dairies Inc., Rutter Brothers Dairy, Inc., Turkey Hill LP,
 Tuscan/Lehigh Valley Dairies, Inc. (Schuylkill Haven)

	<u>Reference</u>	<u>Proposed Order</u>	<u>Current Order (2)</u>	<u>Change</u>
Butterfat test	D6	2.0013%	1.9788%	0.0225%
Butterfat price as announced by PMMB	(1)	\$ 2.5799 per lb.	\$ 2.5799 per lb.	
Extended butterfat value		\$ 0.0516 per lb.	\$ 0.0511 per lb.	
Skim price as announced by PMMB	(1)	\$ 13.58 per cwt.	\$ 13.58 per cwt.	
Extended skim value		\$ 0.1331 per lb.	\$ 0.1331 per lb.	
Total milk value at announced prices		<u>\$ 0.1847 per lb.</u>	<u>\$ 0.1842 per lb.</u>	<u>\$ 0.0005</u>
Ingredient cost	D4	0.0001	0.0001	
Cost of shrinkage / bulk milk & cream	D5	0.0003	0.0005	
Total milk cost per pound		<u>\$ 0.1851 per lb.</u>	<u>\$ 0.1848 per lb.</u>	<u>\$ 0.0003</u>
Pounds per gallon (conversion)		8.62	8.62	
Total milk cost per gallon		<u>\$ 1.5956</u>	<u>\$ 1.5930</u>	<u>\$ 0.0026</u>
Container cost (adjusted for shrinkage)	D3	0.1998 each	0.1652 each	0.0346
Cost center costs	D2	0.9764	0.9756	0.0008
1st half 2019 to 1st half 2018 adjustment	D7	(0.0020)	0.0204	(0.0224)
Container efficiency adjustment	D10	(0.0817)	(0.0667)	(0.0150)
Percentage discount adjustment	(3)	0.0044	0.0044	-
Diesel fuel adjustment	D8	(0.0020)	0.0052	(0.0072)
Heating fuels adjustment	D9	-	-	-
		<u>\$ 2.6905 each</u>	<u>\$ 2.6971 each</u>	<u>\$(0.0066)</u>
Dealer profit at 3.4%	(2)	0.0947	0.0949	\$(0.0002)
Subtotal		<u>\$ 2.7852 each</u>	<u>\$ 2.7920 each</u>	<u>\$(0.0068)</u>
Less: average delivery cost	(2)	(0.4352)	(0.4352)	
Add: high cost delivery	(2)	0.9664	0.9664	
Wholesale minimum price		<u><u>\$ 3.3164 each</u></u>	<u><u>\$ 3.3232 each</u></u>	<u><u>\$(0.0068)</u></u>

(1) As announced for October 2019 by PMMB on September 19, 2019.

(2) Per OGO A-963 (CRO 9) as updated.

(3) Per OGO A-972 "Price Adjustments to Account for Interaction of Milk Prices and Wholesale Percentage Discounts."

PMMB AREA 4
DECEMBER 4, 2019 COST REPLACEMENT HEARING

**CALCULATION OF WHOLESALE MINIMUM PRICE
HALF PINT FLAVORED NONFAT MILK (SKIM) FOR OCTOBER 2019
Dean Dairy Holdings LLC dba Swiss Premium Dairy, Galliker Dairy (Johnstown),
Harrisburg Dairies Inc., Rutter Brothers Dairy, Inc., Turkey Hill LP,
Tuscan/Lehigh Valley Dairies, Inc. (Schuylkill Haven)**

	<u>Reference</u>	<u>Proposed Order</u>	<u>Current Order (2)</u>	<u>Change</u>
Butterfat test	D6	0.0488%	0.0667%	-0.0179%
Butterfat price as announced by PMMB	(1)	\$ 2.5799 per lb.	\$ 2.5799 per lb.	
Extended butterfat value		\$ 0.0013 per lb.	\$ 0.0017 per lb.	
Skim price as announced by PMMB	(1)	\$ 13.58 per cwt.	\$ 13.58 per cwt.	
Extended skim value		\$ 0.1357 per lb.	\$ 0.1357 per lb.	
Total milk value at announced prices		<u>\$ 0.1370 per lb.</u>	<u>\$ 0.1374 per lb.</u>	<u>\$(0.0004)</u>
Ingredient cost	D4	0.0269	0.0271	
Cost of shrinkage / bulk milk & cream	D5	0.0003	0.0005	
Total milk cost per pound		<u>\$ 0.1642 per lb.</u>	<u>\$ 0.1650 per lb.</u>	<u>\$(0.0008)</u>
Pounds per gallon (conversion)		0.50	0.50	
Total milk cost per half pint		<u>\$ 0.0821</u>	<u>\$ 0.0825</u>	<u>\$(0.0004)</u>
Container cost (adjusted for shrinkage)	D3	0.0313 each	0.0307 each	0.0006
Cost center costs	D2	0.0610	0.0610	-
1st half 2019 to 1st half 2018 adjustment	D7	(0.0001)	0.0013	(0.0014)
Container efficiency adjustment	D10	0.0245	0.0250	(0.0005)
Percentage discount adjustment	(3)	0.0003	0.0003	-
Diesel fuel adjustment	D8	(0.0001)	0.0003	(0.0004)
Heating fuels adjustment	D9	-	-	-
		<u>\$ 0.1990 each</u>	<u>\$ 0.2011 each</u>	<u>\$(0.0021)</u>
Dealer profit at 3.4%	(2)	0.0070	0.0071	\$(0.0001)
Subtotal		<u>\$ 0.2060 each</u>	<u>\$ 0.2082 each</u>	<u>\$(0.0022)</u>
Less: average delivery cost	(2)	(0.0272)	(0.0272)	
Add: high cost delivery	(2)	0.0604	0.0604	
Wholesale minimum price		<u><u>\$ 0.2392 each</u></u>	<u><u>\$ 0.2414 each</u></u>	<u><u>\$(0.0022)</u></u>

(1) As announced for October 2019 by PMMB on September 19, 2019.

(2) Per OGO A-963 (CRO 9) as updated.

(3) Per OGO A-972 "Price Adjustments to Account for Interaction of Milk Prices and Wholesale Percentage Discounts."