

**PENNSYLVANIA FOOD
MERCHANTS ASSOCIATION**

AREA 6 REBUTTAL EXHIBITS

COST REPLACEMENT HEARING

FEBRUARY 05, 2014

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INTRODUCTION

The Pennsylvania Food Merchants Association (hereafter "PFMA") conducted an analysis of in-store handling costs related to fluid milk in 2008. The study was conducted utilizing stores located in the Pennsylvania Milk Marketing Board (hereafter "PMMB") Area 6 being studied. Raw data was obtained by PMMB and PFMA. PFMA has analyzed the raw data. The Cost Replacement Hearing exhibits data has been supervised by Thomas J. Price, CPA.

DEFINITIONS

In-store handling costs - In-store handling costs are defined as costs incurred from the time store personnel receive milk deliveries until the milk product is purchased and checked out at the check-out counter.

The total in-store handling cost is comprised of four separate components, which are personnel costs, building costs, equipment costs, and other operating costs.

Personnel costs - Costs relative to personnel, including salaries, wages, payroll taxes, fringe benefits and group insurance.

Building costs - Costs are comprised of rent, depreciation, and repairs.

Equipment costs - Costs are comprised of rent, depreciation, and repairs.

Other operating costs - Costs are comprised of utilities, telephone, insurance, advertising, bags, supplies, vehicle expense, business taxes, license fees, professional services, bad checks, cash loss, inventory and cash adjustments, G&A allocated from central headquarters, and miscellaneous expenses.

CROSS-SECTION

Stores included in the study are the same stores utilized by the PMMB in its cross-section. These stores are deemed to be representative of stores in PMMB Area 6 (see Table 1).

SCOPE OF WORK

The Kirkland formula was used to calculate the in-store handling cost. Table 2 presents the Kirkland method of calculating the in-store handling cost for a fictitious, example store.

April 2008 financial information was accumulated for each store in the cross-section and prepared in accordance with Generally Accepted Accounting Principles. The month of April is considered to be a representative month for the industry. Table 3 presents the results of the study for the entire cross-section of surveyed stores.

METHOD OF CALCULATION

Financial information was collected and analyzed on a store-by-store basis. The in-store handling cost has two components; a milk handling expense component and a checkout expense component. Each component is calculated by applying allocations based on store area used to store, display and sell milk as well as an allocation of checkout costs based on milk sales as a percentage of total sales.

Milk sales in the cross-section stores selling above the state minimum retail price have been restated to the minimum retail price based on the actual volume and packages sold by the stores. The restatement to the minimum retail price is considered necessary to avoid capturing costs due to any of the stores selling milk at levels higher than the state allowed minimum retail prices.

CURRENT COST BASED ON CONSUMER PRICE INDEX

The cost of handling milk in retail outlets is constantly changing as the personnel, building, equipment and other costs are all subject to change over time. The changes in costs are both a normal and ongoing part of doing business as a retail outlet. We have used the Consumer Price Index for All Urban Consumers (CPI-U) to calculate the change in costs over time and recommend that the CPI-U be used to adjust the in-store handling cost on a monthly basis. We have presented this calculation for the period from October 2012 to November 2013 (see Table 4). The CPI is the most widely used measure of price change. It is both a timely and reliable source of price change data.

The CPI is released monthly about two weeks after the end of the month. Therefore, it should be updated monthly to provide a current and accurate calculation of the cost of handling milk. In Area 6, the PMMB has adopted a policy to adjust the cost using a two-month delay. This means that the index for November would be used to calculate the January cost. The delay is acceptable to allow for timely, accurate calculations each month by the staff of the PMMB.

DEPARTMENTAL GROSS MARGIN COMPARISONS TO MILK

The graph (see Table 5) presents the gross margin by department of a variety of retail stores ranging from single store companies to multi-store companies for the 2012 reporting period representing a geographical area covering 39 states. Data was taken from the 2013 "Independent Grocers Financial Survey" report compiled by the National Grocers Association. Information from the study is presented with the gross margins realized by Area 6 retailers purchasing and selling at the minimum wholesale and retail prices.

TABLE 1

STORES INCLUDED IN THE AREA 6 SURVEY FOR IN-STORE HANDLING COSTS

Giant -- Eagle #54
Somerset

Red Apple Kwik Fill,
Johnstown

Stem's Clover Leaf Quick Shop,
Johnstown

Uni-mart,
Pleasant Gap

Kondak's,
Clarendon

Grocery Stretcher,
Bradford

Martin's General Store,
Alexandria

Fezzel's Market,
Punxsyawn

Weis Market,
State College

Nittany Oil Mini Market,
Port Matilda

Quality #626,
Kane

TABLE 2

PENNSYLVANIA FOOD MERCHANTS ASSOCIATION
PENNSYLVANIA MILK MARKETING BOARD AREA 6

COST FOR HANDLING MILK IN RETAIL OUTLETS
KIRKLAND METHOD - EXAMPLE STORE

IN-STORE HANDLING COST - INPUT INFORMATION

TOTAL SQ. FT. OF BUILDINGS	78,000	A
TOTAL SQ. FT. OF MILK DISPLAYS	60	B
TOTAL SQ. FT. DRY STORAGE FOR MILK	40	C
TOTAL SQ. FT. CHECK-OUT SPACE	2,200	D
TOTAL SQ. FT. MILK COLD STORAGE	130	E
TOTAL STORE LABOR HOURS (MONTHLY)	30,000	F
TOTAL MILK HANDLING HOURS (MONTHLY)	600	G
TOTAL CHECK-OUT HOURS (MONTHLY)	3,500	H
QUARTS DELIVERED (MONTHLY)	130,000	J
UNITS DELIVERED (MONTHLY)	43,000	K
UNITS SCANNED (MONTHLY)	2,300,000	L
TOTAL DOLLAR SALES (MONTHLY)	\$ 6,000,000	M
TOTAL MILK SALES IN \$'S (MONTHLY)	\$ 125,000	N
MILK LABOR COSTS - INCLUDING FRINGES	\$ 9,000	O
CHECKOUT LABOR COSTS	\$ 28,000	P
EQUIPMENT COSTS (MONTHLY)	\$ 42,000	Q
BUILDING COSTS (MONTHLY)	\$ 20,000	R
OTHER COSTS (MONTHLY)	\$ 1,400,000	S
TOTAL OPERATING EXPENSES	\$ 1,499,000	T

IN-STORE HANDLING COST - COMPUTATION FORMULA

	Expense		Sq. Ft. Allocation		Sales Allocation		Milk Handling Expense		Checkout Expense
PERSONNEL EXPENSE:									
CHECKOUT EXPENSE	\$ 28,000	P X	1.000000		X 0.018696	K/L =			\$ 523.48
MILK HANDLING EXPENSE	\$ 9,000	O X	1.000000		X 1.000000	=	\$ 9,000.00		
BUILDING EXPENSE:									
CHECKOUT EXPENSE	\$ 20,000	R X	0.028205	D/A	X 0.018696	K/L =			\$ 10.55
MILK HANDLING EXPENSE	\$ 20,000	R X	0.002949	(B+C+E)/A	X 1.000000	=	\$ 58.97		
EQUIPMENT EXPENSE:									
CHECKOUT EXPENSE	\$ 42,000	Q X	0.028205	D/A	X 0.018696	K/L =			\$ 22.15
MILK HANDLING EXPENSE	\$ 42,000	Q X	0.002949	(B+C+E)/A	X 1.000000	=	\$ 123.85		
OTHER EXPENSE:									
CHECKOUT EXPENSE	\$ 1,400,000	S X	0.028205	D/A	X 0.018696	K/L =			\$ 738.24
MILK HANDLING EXPENSE	\$ 1,400,000	S X	0.002949	(B+C+E)/A	X 1.000000	=	\$ 4,128.21		
TOTAL EXPENSES:									
									CHECKOUT EXPENSE
									\$ 1,294.42
									MILK HANDLING EXPENSE
							\$ 13,311.03		
DIVIDED BY:									
									UNITS DELIVERED
									K 43,000
									QUARTS DELIVERED
						J	130,000		
CHECKOUT COST PER CONTAINER:									\$ 0.0301
MILK HANDLING COST PER QUART:							\$ 0.1024		
TOTAL COST PER QUART CONTAINER:							<u>Per Container</u>		<u>Per Quart</u>
						J+K	\$ 0.1325		\$ 0.1325
TOTAL COST PER HALF GALLON CONTAINER:							\$ 0.2349		\$ 0.1174
TOTAL COST PER GALLON CONTAINER:							\$ 0.4397		\$ 0.1099
AVERAGE COST PER QUART - ALL CONTAINERS									<u>\$ 0.1200</u>

TABLE 3

PENNSYLVANIA FOOD MERCHANTS ASSOCIATION
PENNSYLVANIA MILK MARKETING BOARD AREA 6

COST FOR HANDLING MILK IN RETAIL OUTLETS
FOR THE MONTH OF APRIL, 2008
KIRKLAND METHOD - ALL CROSS-SECTION STORES

IN-STORE HANDLING COST - INPUT INFORMATION

TOTAL SQ. FT. OF BUILDINGS	187,820
TOTAL SQ. FT. OF MILK DISPLAYS	385
TOTAL SQ. FT. DRY STORAGE FOR MILK	127
TOTAL SQ. FT. CHECK-OUT SPACE	4,094
TOTAL SQ. FT. MILK COLD STORAGE	502
TOTAL STORE LABOR HOURS (MONTHLY)	54,196
TOTAL MILK HANDLING HOURS (MONTHLY)	458
TOTAL CHECK-OUT HOURS (MONTHLY)	14,641
QUARTS DELIVERED (MONTHLY)	158,688
TOTAL DOLLAR SALES (MONTHLY)	\$ 8,278,464
TOTAL MILK SALES IN \$'S (MONTHLY)	\$ 145,317
MILK LABOR COSTS - INCLUDING FRINGES	\$ 4,984
CHECKOUT LABOR COSTS	\$ 143,961
EQUIPMENT COSTS (MONTHLY)	\$ 57,932
BUILDING COSTS (MONTHLY)	\$ 111,308
OTHER COSTS (MONTHLY)	\$ 1,314,314
TOTAL OPERATING EXPENSES	\$ 1,632,499

IN-STORE HANDLING COST - COMPUTATION FORMULA

	Expense		Sq. Ft. Allocation		Sales Allocation	=	Milk Handling Expense		Checkout Expense
PERSONNEL EXPENSE:									
CHECKOUT EXPENSE	\$ 143,961	X	1.000000	X	0.020337	=			\$ 2,927.77
MILK HANDLING EXPENSE	\$ 4,984	X	1.000000	X	1.000000	=	\$ 4,983.79		
BUILDING EXPENSE:									
CHECKOUT EXPENSE	\$ 111,308	X	0.023845	X	0.020337	=			\$ 53.98
MILK HANDLING EXPENSE	\$ 111,308	X	0.006556	X	1.000000	=	\$ 729.69		
EQUIPMENT EXPENSE:									
CHECKOUT EXPENSE	\$ 57,932	X	0.021316	X	0.020337	=			\$ 25.11
MILK HANDLING EXPENSE	\$ 57,932	X	0.004743	X	1.000000	=	\$ 274.75		
OTHER EXPENSE:									
CHECKOUT EXPENSE	\$ 1,314,314	X	0.024122	X	0.020337	=			\$ 644.77
MILK HANDLING EXPENSE	\$ 1,314,314	X	0.005896	X	1.000000	=	\$ 7,748.63		
TOTAL EXPENSES:									
			CHECKOUT EXPENSE						\$ 3,651.63
			MILK HANDLING EXPENSE				\$ 13,736.86		
DIVIDED BY:			UNITS DELIVERED						55,630
			QUARTS DELIVERED				158,688		
CHECKOUT COST PER CONTAINER:									\$ 0.0656
MILK HANDLING COST PER QUART:							\$ 0.0866		
TOTAL COST PER QUART CONTAINER:							Per Container		Per Quart
							\$ 0.1522		\$ 0.1522
TOTAL COST PER HALF GALLON CONTAINER:							\$ 0.2388		\$ 0.1194
TOTAL COST PER GALLON CONTAINER:							\$ 0.4119		\$ 0.1030
AVERAGE COST PER QUART - ALL CONTAINERS									\$ 0.1249

TABLE 4

**PENNSYLVANIA FOOD MERCHANTS ASSOCIATION
PENNSYLVANIA MILK MARKETING BOARD AREA 6**

**COST FOR HANDLING MILK IN RETAIL OUTLETS
FOR THE THIRTEEN MONTHS ENDED NOVEMBER 2013**

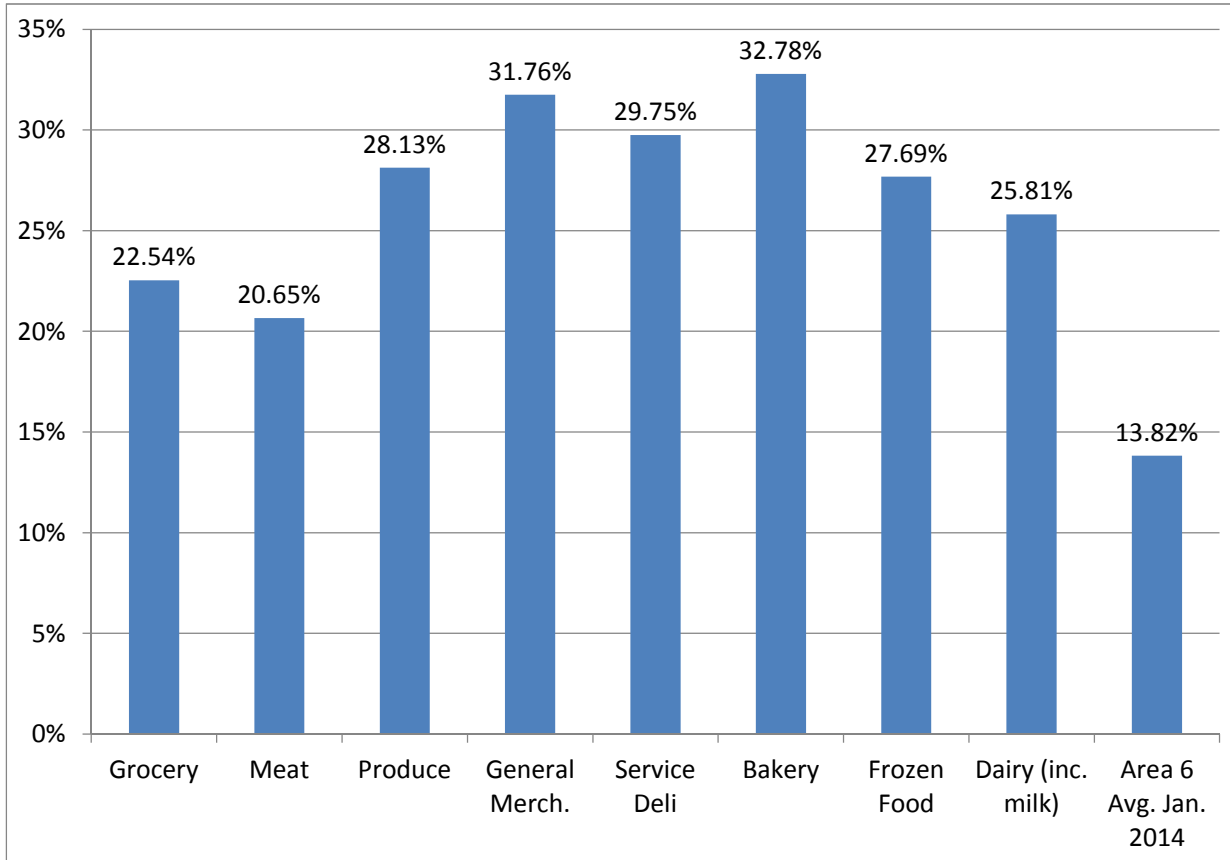
				In-Store Handling Cost Per PMMB Order A- 954	
				\$	
Milk expense per quart	October 2012			\$	0.1345
Divided by CPI-U Index	October 2012	231.317			
Multiplied by CPI-U index	November 2012	230.221	=	\$	0.1339
	December 2012	229.601	=	\$	0.1335
	January 2013	230.280	=	\$	0.1339
	February 2013	232.166	=	\$	0.1350
	March 2013	232.773	=	\$	0.1353
	April 2013	232.531	=	\$	0.1352
	May 2013	232.945	=	\$	0.1354
	June 2013	233.504	=	\$	0.1358
	July 2013	233.596	=	\$	0.1358
	August 2013	233.877	=	\$	0.1360
	September 2013	234.149	=	\$	0.1361
	October 2013	233.546	=	\$	0.1358
	November 2013	233.069	=	\$	0.1355

TABLE 5

**PENNSYLVANIA MILK MARKETING BOARD
MILK MARKETING AREA 6**

**DEPARTMENTAL GROSS MARGIN COMPARISONS TO MILK
JANUARY 2014**

DEPARTMENTS OF INDEPENDENT RETAILERS



Calculation for "Area 6 Avg. Jan. 2014"

Current Wholesale Price (per quart)	1.1819		
Deepest Discount (12.5%)	<u>(0.1477)</u>		
Current Cost Less Discount	1.0342	Current Retail Price	1.20
			<u>(1.0342)</u>
		Gross Profit	0.1658
		Gross Profit %	13.82%

TABLE 6

Thomas J. Price, CPA *Curriculum Vitae*

EDUCATION

Bloomsburg University – B.S. Degree in Accounting (1981)

EMPLOYMENT

Herbein + Company, Inc.

October 1994 to Present:

Partner

July 1989 to December 1991:

Manager of Accounting and Auditing Department

July 1986 to July 1989:

Supervisor of Accounting and Auditing Department

July 1984 to June 1986:

Senior of Accounting and Auditing Department

December 1982 to July 1984:

In-Charge of Accounting and Auditing Department

June 1981 to December 1982:

Staff Accountant

PROFESSIONAL AND CIVIC ASSOCIATIONS AND DESIGNATIONS

CPA – Commonwealth of Pennsylvania (February 1984)

Member – American Institute of Certified Public Accountants

Member – Pennsylvania Institute of Certified Public Accountants

Member – Reading Chapter of Certified Public Accountants

Finance Chairman – Frieden's Lutheran Church

Board Member – Frieden's Lutheran Church

Board Member – Thrivent Financial for Lutherans

SPECIFIC RELATED EMPLOYMENT EXPERIENCE

Assisted In the original development of the methodology of analyzing in-store handling costs.

Supervised in-store handling costs studies for Pennsylvania Food Merchants for the period 1987 to 1998.

I have spent over 32 years providing various accounting and tax services for retail manufacturing and service businesses including food industry manufacturers and distributors.