

REBUTTAL TESTIMONY OF

ALEXANDRA DEIMLER, CPA

Appearing on Behalf of the Area 2 Milk Dealers

Rebuttal Testimony before Pennsylvania Milk Board

Cost Replacement Hearing Based on 2023 Annual Reports

March 5, 2025

Rebuttal Testimony of Alex Deimler, CPA

Area 2 – Cost Replacement Hearing

I am Alexandra Deimler, Consultant at Herbein + Company, Inc. and my address is 2763 Century Blvd., Reading, PA 19610. I am offering testimony on behalf of the Area 2 Milk Dealers. I attach my Curriculum Vitae, as Rebuttal Exhibit D1, which outlines my education, and experience in the dairy industry.

On behalf of the Area 2 Milk Dealers, I have reviewed the audit files and proposed adjustments prepared by the Pennsylvania Milk Board audit staff, have reviewed the financial information of each of the dealers in the cross-section and have prepared exhibits which present my findings.

Cross-Section

The Area 2 cross-section of dealers utilized in our exhibits is the same as last year's cross-section. Our cross-section includes Clover Farms Dairy Co., DFA Dairy Brands Fluid, LLC – Schuylkill Haven, Milk Industry Management Corp. T/A Balford Farms, Monroe County Milk Producers Coop Assoc. dba Pocono Mountain Dairies, Turkey Hill LP dba Turkey Hill Dairy, and Valley Farms Dairy LLC. These companies process, package, and deliver the majority of controlled milk products in Area 2, serving supermarkets, convenience stores, schools, institutions, and small retail outlets. The cross-section remains representative of dealers and sales in Area 2 and represents 63.39 percent of sales in the Area. Consistency between cross-sections in 2023 and now will reflect cost increases, or in this case, decreases due to changes in cross-section dealer sales and costs. Maintaining the same cross-section year-over-year, absent plant closings, new entrants with sustained and material participation, among other considerations, has been done previously for many years. In my opinion, it is necessary to use a consistent cross-section for this hearing because this year the cost build up is set to generate a significant unanticipated fluctuation in the wholesale minimum price having little to do with the costs experienced

by the dealers in the cross-section. Essentially, there is a significant change facing Area 2 due to a calculation error made last year when data was pulled from MARs. As a result, I recommend that the wholesale price build up is based on last year's cross-section so that any cross-section changes do not contribute to further unanticipated volatility.

Rebuttal Exhibits

Rebuttal Exhibit D2 reflects the processing, packaging, and delivery cost per point for calendar year 2023. Please note that the points presented in the exhibit are for sales in the PMMB Area 2 made by the cross-section dealers. These costs should replace the existing costs from 2022, which are currently being utilized by the Board in establishing prices. Our calculation of the processing, packaging, and delivery costs is \$0.3280 per point.

Exhibit D2 shows the number of points (quart equivalents) that are associated with each cost center. For example, the bottling department points for 2023 are 68,594,729 for the cross-section. This is a decrease of 7,814,763 bottling points from 2022, which is 10.23%.

Rebuttal Exhibit D2-A is prepared to compare the 2022 processing, packaging, and delivery costs in the current order with the 2023 processing, packaging, and delivery costs. Overall, for 2023, there was a decrease of \$0.0171 per point. Additionally, this exhibit reflects the 2024 cost increase adjustment from Exhibit D7 and removes the 2023 cost increase adjustment. Including the cost update adjustments, the increase in the cross-section costs from the prior cost replacement hearing is \$0.0100 per quart equivalent (point), or about 4 cents per gallon. This increase is driven by an increase in expenses coupled with significant decline in volume.

Rebuttal Exhibit D3 and D3-A have been updated to container costs utilized in the October 2024 minimum resale price calculation. The container shrinkage factor reflected on these exhibits is a statewide average and will be utilized for all areas. There are no controlled milk products sold in Area 2

in paper half gallons, 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 2024 as the new starting point.

Rebuttal Exhibit D4 is prepared to present the ingredient costs per pound of finished product as of April 2024 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 2024 minimum prices.

Rebuttal Exhibit D5 updates the cost of milk shrinkage and the costs and revenues from bulk cream and bulk milk transactions. The current order establishes a net revenue of \$0.0013 per pound and the new net cost, based on 2023 transactions is \$0.0036 per pound. There is a net change of \$0.0023 per pound. That means overall these three transactions resulted in a cost increase of about 2 cents per gallon.

Rebuttal Exhibit D6 reflects a comparison of the current order butterfat tests by product type and compares those tests with the 2023 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 2023 tests reflected on this exhibit.

Rebuttal Exhibit D7 is prepared to calculate the cost increases and decreases incurred during the six (6) month period ending June 30, 2024 compared with the six (6) month period ending June 30, 2023 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 2024 are 40,268,394, which is 2.1% less than the weighted points for the first six (6) months of 2023. In 2024, the three cost categories used in this calculation increased \$169,497 or 2.5% compared to 2023. These factors created an adjustment of (\$0.0112) per point.

Rebuttal Exhibit D8 has been updated to reflect the August 2024 diesel fuel costs, which were used in calculating the minimum prices for October 2024. Additionally, this exhibit reflects the calculation of the average diesel fuel cost for calendar year 2023, which becomes the new starting point for the monthly adjustments. I recommend that this adjustment be continued monthly. The average diesel fuel cost for 2023 for the cross-section dealers is \$0.0132 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 June 2024 natural gas costs. This exhibit reflects the calculation of the average heating fuel cost for calendar year 2023, which becomes the new starting point for the monthly adjustments. I recommend that this adjustment be continued monthly.

Container Efficiency Adjustment

Our calculation of updated container efficiency adjustments is shown at Exhibit D10. The actual quantity sold 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 \$555,028 of costs out of the gallon package and add \$383,262 of costs to the paper half pint. The net effect of the plusses and minuses is an expense to the dealers of \$(178). This amount is not zero because of rounding. 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 2024 using the updates proposed here. These exhibits also cross-reference the exhibits that support the individual line items.

Class II Controlled Products

The current process for updating Class II pricing monthly should be continued.

Rate of Return

I recommend that the Board maintain the rate of return for the Area 2 dealers at 3.5%. The rate of return serves as an important factor in the ability of Pennsylvania's fluid milk processors to maintain and invest in their operations. Maintaining the current rate of return is also important for consistency and stability when the fresh fluid milk industry continues to face a difficult business environment.

Summary and Recommendation

The Area 2 Milk Dealers recommend that the Milk Board make the cost replacement adjustments that I have just outlined. Thank you for your consideration of my analysis and opinions.