Approved: February 18, 2011
Date

MINUTES OF THE HOUSE AGRICULTURE & NATURAL RESOURCES COMMITTEE

The meeting was called to order by Chairman Larry Powell at 9:00 a.m. on February 10, 2011, in Room 783 in the Docking State Office Building.

All members were present except:
Representative Rocky Fund - Excused
Representative Bob Grant - Excused
Representative Michael Peterson - Excused

Committee staff present:
Sean Ostrow, Office of the Revisor of Statutes
Raney Gilliland, Kansas Legislative Research Department
Michael Wales, Kansas Legislative Research Department
Kay Scarlett, Committee Assistant

Conferees appearing before the Committee:
David Barfield, Chief Engineer, Division of Water Resources,Kansas Department of Agriculture
Dennis Reynolds, Chairman, Kansas Grape and Wine Industry Advisory Council
Steve Ohlde, Member, Kansas Dairy Marketing Advisory Board

Others attending:
See attached list.

Tracy Streeter, Director, Kansas Water Office, provided *A Quick Reference on Water Rights and Water Terms* as requested by the committee. (Attachment 1)

David Barfield, Chief Engineer, Division of Water Resources, Kansas Department of Agriculture, provided an overview of water appropriation control and regulation in Kansas. He discussed obtaining, maintaining, protecting, and changing a water right, as well as compliance and enforcement. There are seven Intensive Groundwater Use Control Areas (IGUCA) in the state where the Chief Engineer may implement corrective control provisions where it has been determined that groundwater levels are declining excessively to warrant additional regulation to protect public interests.

Mr. Barfield explained that flex accounts were established by the 2001 legislature as a voluntary program to allow water right holders to establish flexible accounts for groundwater use. The criteria allows eligible, participating water right holders to use, within a five-year period, an amount of groundwater that is no more than 90 percent of the actual base average use, times five, as long as it does not impair other existing water rights. Currently, there are no active flex accounts as all previously filed accounts have expired and not been renewed. The law requires that any groundwater water right holder who wants to establish a flex account to file an application no later than October 10 of the preceding year. The Division of Water Resources has proposed legislation to remove the deadline date and to allow a water right holder to file an application at any time. They continue to promote flex accounts as a viable option for groundwater users who have variable demands from year to year, particularly in areas in need of water management strategies. (Attachment 2)

Dennis Reynolds, Chairman, Kansas Grape and Wine Industry Advisory Council, reported that the grape and wine industry continues to grow in Kansas. In 2010, 24 wineries were licensed across the state. This year the Kansas Agricultural Statistics and the National Agricultural Statistics Service will conduct a survey of the impact of the Kansas grape and wine industry on the Kansas economy. The survey, funded by a USDA Specialty Crop Grant, will gather valuable data about the different grape varieties grown in the state, the different fruits used to make wine, the type and amount of wine produced, the level of tourism ties to grape and wine production, and other economic data. (Attachment 3)

Steve Ohlde, Member, Kansas Dairy Marketing Advisory Board, said the Kansas dairy industry continues to change. The state continues to have fewer dairy farms, but with higher milk production per cow and per farm. The dairy manufacturing industry has been relatively stable. Dairy processing

Unless specifically noted, the individual remarks recorded herein have not been transcribed verbatim. Individual remarks as reported herein have not been submitted to the individuals appearing before the committee for editing or corrections.

plants in Kansas have not grown as much as milk production from Kansas dairy farms. Kansas is a net exporting state for raw milk. Historically, dairy markets were local with farm produced milk being processed and marketed in the nearest city of any size. However, with the advent of better refrigeration and transportation, the dairy industry has become regionalized. Global markets now affect even the smaller producers. He said Kansas is adapting with many positive changes. Increases in total milk production improves the state's chances of attracting a new processing plant with jobs and economic benefits. Also, several smaller producers are developing ideas to produce cheese or bottled milk for niche markets. (Attachment 4)

The meeting adjourned at 10:05 a.m. The next meeting of the House Agriculture & Natural Resources Committee is scheduled for February 14, 2011.

Unless specifically noted, the individual remarks recorded herein have not been transcribed verbatim. Individual remarks as reported herein have not been submitted to the individuals appearing before the committee for editing or corrections.

HOUSE AG & NATURAL RESOURCES COMMITTEE
GUEST LIST

DATE: FEBRUARY 10, 2011

NAME	REPRESENTING
Steve Ohlde	Dairy Marketing Board
Sarah Green	KDA
Dennis Reynolds	Grape & Wine Council
Susan Stone	KWO
Lane Letourneau	KDA
Kent Astren	KFB
Tom Bruno	KS Dairy Assn.
CHRIS LAW	GMD3
Hal Scheuerman	GMD3
Steve Stone	GMD3
Mike O'Brate	GMD3
Clay Scott	Gmd 3
Jason Vorgetts	GMD3
TUCK DUNCAN	Member grape & wine Adv. Bd.

Kansas Water Office
901 S. Kansas Avenue
Topeka, KS 66612

Tracy Streeter, Director

Kansas

phone: 785-296-3185
fax: 785-296-0878
www.kwo.ks.gov

Kansas Water Office

Sam Brownback, Governor

As requested by the House Committee on Agriculture & Natural Resources
February 7, 2011

A Quick Reference on Water Rights and Water Terms

Groundwater: Water that exists below the water table and fills the pore space in the rock or sediment. Groundwater moves slowly in the same direction that the water table slopes.

Surface water: Water that is on the earth's surface, such as in a stream, river, lake or reservoir.

Aquifer: A subsurface rock, soil or sediment unit that is porous and permeable that stores and transmits useful quantities of water. Buried river sands ("alluvium"), sandstones and the Ogallala Formation are some of the best water-producing layers in Kansas.

Water Right: A Kansas water right provides the owner the right to use water, if available. It is limited to: 1) a maximum annual quantity of water; 2) a maximum rate of diversion; 3) a beneficial use authorized by the Chief Engineer; 4) the authorized place of use; and 5) diverted only from the authorized point(s) of diversion.

Vested Water Rights: Water rights developed for beneficial use prior to the Water Appropriation Act adoption (1945). A vested water right does not have an individual priority date as do the water rights issued after the adoption of the Water Appropriation Act. In times of shortages, vested water rights are protected before appropriated water rights.

Kansas Water Appropriation Act: (K.S.A. 82a-701 *et seq*) passed in 1945. The Act provides a basic framework of water law in Kansas which allows water users the right to use water in accordance with the principal of the prior appropriation doctrine. The Division of Water Resources (DWR) of the Kansas Dept. of Agriculture is charged with the administration and enforcement of the Act. When there isn't enough to meet all water rights, use is based on "first in time, first in right". A water right does not guarantee the water, just the right to use it when it is available. The date of priority of a water right, and not the type of use (domestic, municipal, irrigation, industrial, recreational and water power) determines the right to use water when there is not enough to satisfy all water rights. All water in the state of Kansas, both groundwater and surface water, are administered under a single priority system.

Appropriation Water Right: To use water for any purpose within the State of Kansas, except for domestic use, one must first apply to the Chief Engineer, DWR, Kansas Department of Agriculture for a permit. Once a permit is granted, the holder has a limited period of time to build the diversion works (well or pump site). The permit holder must then "perfect" (use) the right by applying water under the terms of the permit. The quantity of the water right used in the time and terms provided becomes the measure of the real property right.

Senior Water Right: A water right that was issued under the Water Appropriation Act. Its priority date is relative to all the other water right priority dates. It is senior to water rights that were applied for later, and junior to water rights that have earlier priority dates.

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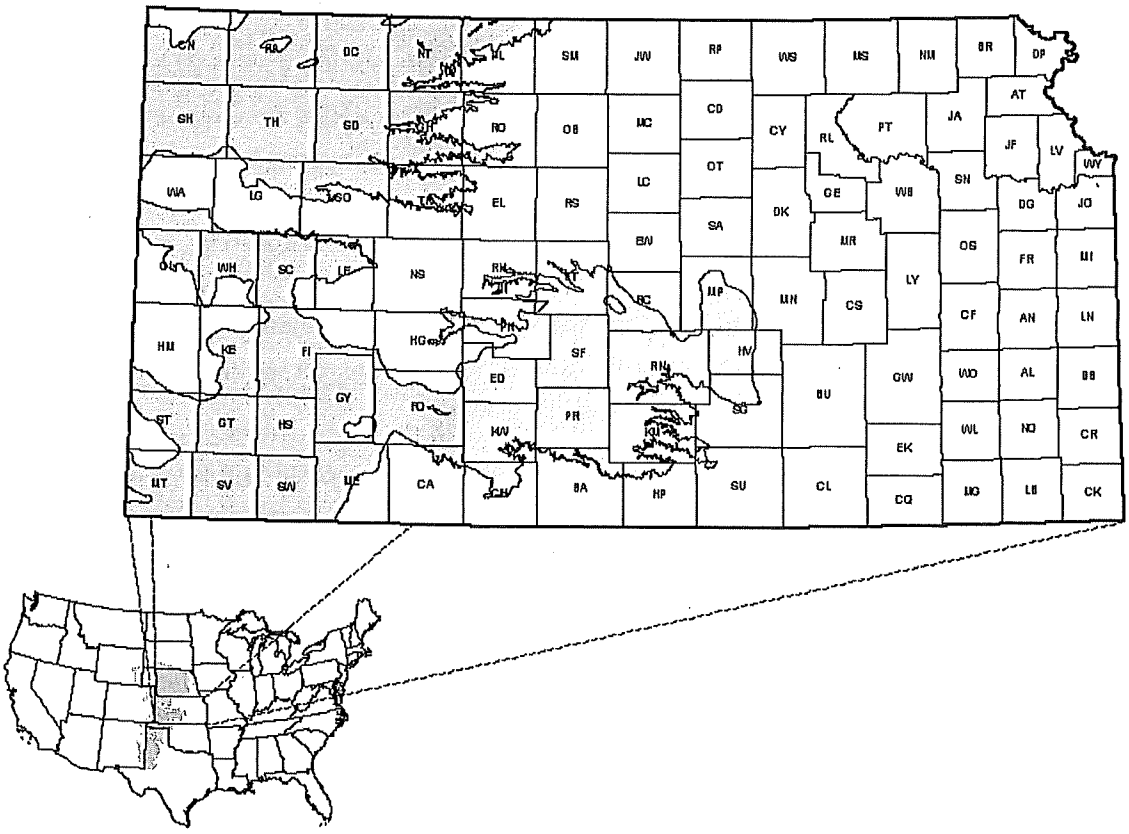
Attachment 1

Junior Water Right: A water .hat was issued under the Water Appr ion Act and has a priority date issued after other "senior" water rights. It is a relative term.

IGUCA: The Intensive Groundwater Use Control Area (IGUCA) statutes (K.S.A. 82a-1036 *et seq*) define when the Chief Engineer may initiate proceedings to designate an area an IGUCA. An IGUCA allows more flexibility in possible solutions to address on-going groundwater declines or water quality deterioration than is permitted under strict prior administration of the Water Appropriation Act alone. The priority dates of water rights may be taken into consideration in setting IGUCA corrective measures. Once an IGUCA order is finalized it has the force and function of law.

Walnut Creek IGUCA: An IGUCA that was that was ordered in the Walnut Creek subbasin in 1992 and amended in 1996, 1998, and 2001. To restore long term sustainability to the groundwater system, the Chief Engineer, DWR, Kansas Department of Agriculture, identified when the region appears to have become fully developed. He then grouped the water rights into three divisions: vested water rights (those developed prior to Kansas Water Appropriation Act), senior water rights (acquired on or prior to October 1, 1965 – the date when the subbasin became fully developed) and junior water rights (those acquired after October 1, 1965). Vested water rights retained their full authorization. Reductions made to appropriated water rights were based on seniority (senior or junior grouping), maximum acres irrigated 1985 to 1990, and county of use (Barton, Rush or Ness). Water quantity reductions are set in five-year allocations. The area was also closed to any future new water right development.

High Plains aquifer: In Kansas, three hydraulically connected, but distinct aquifers form the High Plains aquifer: the Ogallala, the Big Bend Prairie, and the Equus Beds aquifers. The Ogallala aquifer is the largest portion, underlying roughly the western 1/3 of Kansas (shown in blue below). The Big Bend Prairie and Equus Bed aquifers are geologically younger, are not as deep as the Ogallala aquifer, and receive more recharge. The High Plains aquifer is the most important water source in western Kansas, an area that lacks significant surface water sources. Groundwater flow in the High Plains aquifer in Kansas is slow moving; typically it is measured in inches per day.



Office of the Secretary
109 SW 9th Street, 4th Floor
Topeka, Kansas 66612-1280

Kansas

phone: (785) 296-3556
fax: (785) 296-8389
www.ksda.gov
ksag@kda.ks.gov

Dale A. Rodman, Acting Secretary

Kansas Department of Agriculture

Sam Brownback, Governor

Report on Implementing Multi-year Flex Accounts (K.S.A. 82a-736)
to
House Standing Committee on Agriculture and Natural Resources
and
Senate Standing Committee on Natural Resources

By David W. Barfield
Chief Engineer
Kansas Department of Agriculture
Division of Water Resources

February 1, 2011

K.S.A. 82a-736 became law May 9, 2001, and it requires the chief engineer of the Kansas Department of Agriculture's Division of Water Resources to implement a voluntary program to allow water right holders to establish flex accounts for groundwater use. The law also requires the chief engineer to submit a written report on the law's implementation to your standing committees by February 1 each year.

K.S.A. 82a-736 was amended by the Legislature in 2005 to change the base average use period from 1996 through 2000 to 1992 through 2002. The amendments also provided for the amount deposited into the flex account not to exceed 90 percent of the base average use multiplied by five, as opposed to being exactly 90 percent of the base average use multiplied by five.

Attached are the current rules and regulations related to K.S.A. 82a-736 originally promulgated in 2002, and revised January 6, 2006, to implement the program. The criteria allow eligible, participating water right holders to use, within a five-year period, an amount of groundwater that is no more than 90 percent of their actual base average use times five and as long as it does not impair other existing water rights.

The law requires that any groundwater water right holder who wants to establish a flex account and exercise its use do so through a application for a term permit filed no later than October 10 of the year preceding the first year for which application is made.

In 2010, water right holders were reminded of the flex account provision and filing deadline through an article in the August 10, 2010 edition of *DWR Currents*, our e-newsletter and an August 10, 2010 news release. As of October 10, 2010, no applications for term permits had been filed with the chief engineer for 2010, nor have we received any applications to date for participation in the program beginning in 2011.

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Attachment 2

In our day-to-day interaction with water right holders, we make sure that those individuals who we believe could benefit the most from this option know that it exists. We also make our flex account literature available to the public when we have a table or booth at water-related events. Information about flex accounts also is available on our website at http://www.ksda.gov/appropriation/?cid/297.

Currently there are no active flex accounts as the limited number of previously filed accounts have expired and not been renewed. Due to the limited interest shown in this program, no additional staff was hired to process applications with applications handled by existing staff in the water appropriation program.

We believe flex accounts can play a role in water management of over-appropriated area, particularly in areas where voluntary measures are adopted. Flex accounts provide for water savings of at least 10 percent while giving the water right holder flexibility to use the water for beneficial purposes over a five-year period without the annual limits on the quantity. This would allow an irrigator, during a year with below-average precipitation, to meet the higher water demand of his/her crop. Likewise, in years with above-average precipitation, the irrigator would use less water. Over a typical five-year period, there will be wetter and drier years, and flex accounts can help water users balance these highs and lows while avoiding civil penalties for overpumping the authorized quantity in a single year.

We continue to promote flex accounts as a viable option for groundwater users who have variable demands from year to year, particularly in areas in need of water management strategies.

As I wrote last year, due to the limited interest in this program so far, I raised the issue in a meeting with managers of the state's groundwater management districts. We agreed to work together to identify how the program can be made more attractive to water right holders in hopes of increasing the utility of this management tool while achieving its water conservation function. No progress was made on the task this past year. I hope to present findings from that work next legislative session.

We continue to hear that water users are put off by the required 10% conservation element, calculated from historic use.

I am currently working with Northwest Kansas Groundwater Management District No. 4, which is seeking means to implement a similar program of multi-use allocations to conserve water in one of its high priority areas. Experience gained in developing GMD 4's program may provide insight into improvements to make this program more attractive.

Additionally, KDA has requested legislation this year to further amend the statutes and perhaps make the program more attractive to groundwater users.

Attachment: Implementing regulations, K.A.R. 5-16-1 to 5-16-7

Division of Water Resources
Flex Account Rules and Regulations
K.A.R. 5-16-1 through 5-16-7

K.A.R. 5-16-1. Definitions. As used in this article of regulations, in the Kansas water appropriation act, and by the chief engineer in the administration of the Kansas water appropriation act, unless the context clearly requires otherwise, the following words and phrases shall have the meanings ascribed to them in this regulation. (a) "Base amount" and "BA" mean the quantity of water deposited into a flex account.

(b) "Base average usage factor" and "BAUF" mean the percentage of the "base average usage," as this term is defined in K.S.A. 82a-736 and amendments thereto, that is multiplied by five as a part of the calculations set out by K.A.R. 5-16-5 to determine the quantity of water that may be deposited into a flex account. The BAUF shall not exceed the maximum of 90% established by K.S.A. 82a-736 and amendments thereto.

(c) "Base water right" means a vested or certified water right or rights for which the owner applies to the chief engineer to establish a flex account pursuant to K.S.A. 82a-736, and amendments thereto.

(d) "BAU" means the "base average usage" as defined in K.S.A. 82a-736, and amendments thereto.

(e) "Good standing," only as that term is used in K.S.A. 82a-736, and amendments thereto, in reference to base water rights, means a base water right that meets the following conditions:

(1) Has been lawfully exercised within the 11-year time period specified in K.A.R. 5-16-5;

(2) has had all required water use reports filed and any civil fines assessed for failure to timely file a complete and accurate water use report paid; and

(3) has had no period of nonuse with a duration of five or more consecutive years since January 1, 1990, except for enrollment in the water right conservation program according to K.A.R. 5-7-4, enrollment in the federal conservation reserve program, or enrollment in another multiyear federal or state conservation program.

(f) "Significant water conservation measures" means actual physical changes in a water distribution system or management practices that improve water use efficiency, including the following:

(1) Conversion from flood irrigation to center pivot irrigation with a nozzle package designed to improve water use efficiency;

(2) irrigation scheduling;

(3) conversion to subsurface drip irrigation; and

(4) removal of an end gun, resulting in a significant reduction in the number of irrigated acres. (Authorized by K.S.A. 82a-706a; implementing K.S.A. 82a-706a and K.S.A. 2004 Supp. 82a-736, as amended by L. 2005, Ch. 142, § 3; effective Oct. 11, 2002; amended Jan. 6, 2006.)

K.A.R. 5-16-2. Fee to establish flex account and apply for term permit. The filing fee for establishing a flex account and applying for a five-year term permit to exercise the flex account shall be $400. (Authorized by K.S.A. 82a-706a; implementing K.S.A. 2001 Supp. 82a-708a(d), as amended by L. 2002, Ch. 181, § 21; effective Oct. 11, 2002.)

K.A.R. 5-16-3. Establishing a flex account. (a) A flex account shall be established by filing an application for a flex account and a term permit on a form prescribed by the chief engineer. The five-year period shall begin on January 1 of the next calendar year for which the application has been timely filed, unless expressly authorized by the chief engineer to begin the following January 1. The application shall also show the location of all wells located within one-half mile of the proposed point of diversion, and the names, addresses, and telephone numbers of the owners of those wells. Except as set forth in subsection (e), a separate application shall be filed for each water right and each point of diversion for which the owner desires to establish a flex account. Each application shall be accompanied by the filing fee specified in K.A.R. 5-16-2.

(b) Before any application to establish a flex account and a term permit will be accepted for filing, the application shall be signed by at least one owner of the water right, or a duly authorized agent of an owner of the water right.

(c) Before the flex account can be established or the term permit approved, all of the water rights owners, or a duly authorized agent of the owners, shall verify upon oath or affirmation that the statements contained in the application are true and complete.

(d) If one or more owners refuse to sign the application or if a written request is filed by one or more of the owners to withdraw their signatures from the application before the application is approved, the application shall be dismissed.

(e) A single application to establish a flex account and apply for a term permit may be filed in the following situations:

(1) Multiple water rights authorize the diversion of water from a single point of diversion that diverts water to an identical place of use for a single type of use.

(2) Multiple points of diversion are authorized by the chief engineer to divert water through a single water flowmeter before going to an identical place of use.

(f) The flex account shall not be established, and the term permit to exercise the flex account shall not be valid until both have been approved by the chief engineer. (Authorized by K.S.A. 82a-706a; implementing K.S.A. 82a-706a and K.S.A. 2001 Supp. 82a-736; effective Oct. 11, 2002.)

K.A.R. 5-16-4. Conditions on the term permit. (a) The place of use authorized by a term permit shall be identical to the place or places of use authorized by the base water right or rights.

(b) The type of use authorized by a term permit shall be limited to one of the types of use authorized by the base water right or rights.

(c) The rate of diversion authorized by a term permit shall not exceed the maximum instantaneous rate of diversion authorized by the base water right or rights. (Authorized by K.S.A. 82a-706a; implementing K.S.A. 82a-706a and K.S.A. 2001 Supp. 82a-736; effective Oct. 11, 2002.)

K.A.R. 5-16-5. Maximum annual quantity of water authorized by term permit. (a) Except as set forth in subsections (b) through (e), the maximum quantity of water deposited in a flex account and authorized to be diverted in five consecutive calendar years under the authority of a term permit shall be determined in accordance with K.S.A. 82a-736, and amendments thereto, by means of these calculations:

(1) Adding the total actual, legal annual water use of the base water right or rights for the period of calendar years 1992 through 2002;

(2) dividing that total quantity of water by 11;

(3) multiplying that quantity by the BAUF; and

(4) multiplying that quantity by five.

(b) If significant water conservation measures were implemented under the base water rights at any time during the period of calendar years 1992 through 2002, the average annual quantity of water actually used may be calculated using the five consecutive calendar years immediately preceding the implementation of significant water conservation measures, but these five calendar years shall not begin before calendar year 1987. The five-year allocation under the term permit shall be determined by means of these calculations:

(1) Adding the total actual, legal annual water use of the base water right or rights for the five consecutive calendar years;

(2) dividing that total quantity of water by five;

(3) multiplying that quantity by the BAUF; and

(4) multiplying that quantity by five.

(c) If water use records for a base water right are inadequate to accurately determine actual water use during any calendar year during the period used to determine the base average usage, then that year shall be counted as having no water use.

(d) No flex account shall be allowed if the flex account is inconsistent with the provisions of any intensive groundwater use control area created pursuant to K.S.A. 82a-1036 through K.S.A. 82a-1040, and amendments thereto.

(e) If water was authorized to be diverted for less than the entire period used to determine the base average usage, the five-year allocation shall be determined by means of these calculations:

(1) Adding the total actual, legal annual water use of the base water right or rights for the entire period used to determine the base average usage;

(2) dividing the total quantity by the number of years, or parts thereof, that water was authorized to be diverted by the chief engineer;

(3) multiplying that quantity by the BAUF; and

(4) multiplying that quantity by five.

Water rights that authorized use of water for less than two calendar years during period used to determine the base average usage shall not be eligible for a flex account. (Authorized by K.S.A. 82a-706a; implementing K.S.A. 82a-706a and K.S.A. 2004 Supp. 82a-736, as amended by L. 2005, Ch. 142, § 3. 82a-736; effective Oct. 11, 2002; amended Jan. 6, 2006.)

K.A.R. 5-16-6. Flex accounts and term permits. (a) The duration of the flex account and term permit shall be five consecutive calendar years.

(b) There shall be no extension of a flex account or a term permit beyond the period of five consecutive calendar years originally authorized.

(c) There shall be no carryover of unused quantities of water from one flex account or term permit to another flex account or term permit.

(d) Only one flex account shall be in force for a point of diversion or a water right at any time.

(e) A water flowmeter meeting the requirements of the chief engineer shall be installed on each point of diversion authorized by the term permit. If an existing water flowmeter had been required on or after September 22, 2000 or if there is no existing water flowmeter, the water flowmeter shall meet the requirements of the chief engineer in effect at the time the term permit is approved. If a water flowmeter was installed before September 22, 2000, the water flowmeter shall meet the requirements of K.A.R. 5-1-6(b).

(f) Only an entire water right, or a portion of a water right that has been formally divided, may be deposited in a flex account.

(g) All water diverted pursuant to a term permit and the base water rights associated with the term permit shall be counted against the quantity of water deposited in the flex account. (Authorized by K.S.A. 82a-706a; implementing K.S.A. 82a-706a and K.S.A. 2001 Supp. 82a-736; effective Oct. 11, 2002.)

K.A.R. 5-16-7. Conditions under which a base water right may be exercised. Each term permit approved by the chief engineer according to this article shall include the condition that if the term permit can no longer be exercised because of an order issued by the chief engineer, including an intensive groundwater use control area order, a minimum desirable streamflow order, or an order to administer water rights to prevent impairment, then any base water right may be exercised to the extent that all of the following conditions are met:

(a) The base water right is in priority.

(b) The annual quantity of water authorized by the base water right has not been diverted during that calendar year.

(c) The five-year allocation authorized by the term permit has not been used.

(d) The use of water under the base water right does not impair water rights senior to the base water right. (Authorized by K.S.A. 82a-706a; implementing K.S.A. 82a-706a and K.S.A. 2001 Supp. 82a-736; effective Oct. 11, 2002.)

Office of the Secretary
109 SW 9th Street, 4th Floor
Topeka, Kansas 66612-1280

Kansas

phone: (785) 296-3556
fax: (785) 296-8389
www. ksda.gov
ksag@kda.ks.gov

Dale A. Rodman, Acting Secretary

Kansas Department of Agriculture

Sam Brownback, Governor

Report of the Kansas Grape and Wine Industry Advisory Council
to
The Standing Agriculture Committees of the Kansas Legislature

February 2011

The Kansas Legislature created the Kansas Grape and Wine Industry Advisory Council in 1988 with the enactment of K.S.A. 74-551- 74-553. This board reports annually to the Senate and House Agriculture Committees.

The council is a nine-member body that is appointed by the Kansas secretary of agriculture. Council members are appointed to two-year terms and can be reappointed. Membership on the council includes representatives from Kansas State University, the commercial grape growing industry, licensed farm winery industry, wine distributors industry, retail liquor store industry, tourism industry and one member representing the public having experience in marketing.

The current board members are Chairman Dennis Reynolds, of Somerset Ridge Vineyard and Winery in Paola; Vice-Chairman Norm Jennings, of Smoky Hill Vineyard and Winery in Salina; James Pat Murphy, of Kansas State University; Steven Berger, owner of The Wine Cellar in Lawrence; R.E. "Tuck" Duncan, who represents Kansas Wine and Spirits Wholesalers; Susie Pryor, Ph.D., of Washburn University; Dr. John Brewer, of Wyldewood Cellars in Mulvane; Jo Ann Kuhlmann, of Eagle Creek Vineyards in Olpe; and Michelle Meyer, of Holy-Field Vineyard and Winery in Basehor.

The Kansas grape and wine industry

The grape and wine industry continues to grow in Kansas. In 2010, 24 wineries were licensed across the state. Many of these wineries were featured in the Bluestem building at the Kansas State Fair in September. The Kansas Department of Commerce hosted "Meet the Winemaker" events where Fair patrons could meet the producers and purchase their wine.

In 2011, Kansas Agricultural Statistics and the National Agricultural Statistics Service will conduct a survey of the impact of the Kansas grape and wine industry on the Kansas economy. The survey, funded by a USDA Specialty Crop Block Grant awarded to the Kansas Department of Agriculture in 2009, will gather valuable data about the different grape varieties grown in the state, the different fruits used to make wine, the type and amount of wine produced, the level of tourism tied to grape and wine production, and other economic data.

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Attachment 3

Legislative initiatives

The council has in the past recommended legislative changes for the industry. In recent years, including 2011, council members have not recommended changes to Kansas laws on behalf of the grape and wine industry.

Staff changes

The Kansas Department of Agriculture provides administrative assistance in coordinating meetings and the council's other affairs. However, because of budget reductions and open staff positions, the council has not submitted an annual report since at least 2009. Agency restructuring in mid-2010 opened a portion of a position to resume coordination of the council.

Office of the Secretary
109 SW 9th Street, 4th Floor
Topeka, Kansas 66612-1280

Kansas

phone: (785) 296-3556
fax: (785) 296-8389
www. ksda.gov
ksag@kda.ks.gov

Dale A. Rodman, Acting Secretary

Kansas Department of Agriculture

Sam Brownback, Governor

Report of the Kansas Dairy Marketing Advisory Board
to
the Standing Agriculture Committees of the Kansas Legislature

February 2011

The Kansas Legislature created the Dairy Marketing Advisory Board in 1994 with the enactment of K.S.A. 74-555. This board reports annually to the Senate and House Agriculture Committees.

The Kansas Dairy Association may make nominations to the governor for consideration as appointments on the board. The members of the board shall be appointed by the governor and is made up of two dairy producers, one dairy processor, one consumer and the secretary of agriculture or his or her designee. The current board members are: Steve Ohlde, producer; Lynda Foster, producer; Rabecca Harris, dairy processor; Kerri Ebert, consumer; and Acting Secretary of Agriculture Dale Rodman.

The dairy marketing advisory board is tasked with three duties: 1) to study and evaluate the need for establishing a statewide milk marketing order; 2) to make recommendations as to the implementation of milk marketing orders; and 3) to prepare and submit to the standing agriculture committees of the legislature a report of its findings and recommendations.

The Kansas Dairy Industry

The Kansas dairy industry continues to change. As we have reported the last few years, the state continues to have fewer dairy farms but with higher milk production per cow and per farm. The increase in production since about 1999 has been dramatic, with Kansas showing a 12.3 percent increase in total production in the reporting period of 2004 to 2009. This is attributed to not only the growing industry in western Kansas but the overall increase in dairy farm size throughout the state.

For benchmarking purposes, we can compare the early 1980s dairy picture with present numbers. There were 1,327 Grade A dairies and 738 manufacturing grade operations in 1981. Those dairies had 123,000 cows that produced nearly 1.4 billion pounds of milk. By the end of 2010, Kansas was down to 345 Grade A dairies and 42 manufacturing grade dairies. Those dairies had approximately 121,000 cows that produced more than 2.4 billion pounds of milk. Kansas ranks 9th in production per cow and is in the top 20 milk producing states, coming in at 16.

The Kansas dairy manufacturing industry has been relatively stable. Dairy processing plants in Kansas have not grown as much as milk production from Kansas dairy farms. Kansas

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Attachment 4

is a net exporting state for raw milk. Total dairy farm production in Kansas is approximately 135 tankers of milk each day. Kansas dairy processing plant capacity is approximately 26 tankers each day. There is some interest in building a large cheese plant in western Kansas to process some of this excess production, however regional processing plant capacity must be considered. When one considers the dairy manufacturing plant capacity within 300 – 400 miles of southwest Kansas, we see that there is a demand of more than 1000 tanker loads per day to fill currently existing dairy processing plants. The economics of investing millions of dollars in a new processing plant must be weighed against milk transportation costs before a new Kansas cheese plant becomes a reality.

Changing National Picture

Nationwide, United States milk production has increased 10.8 percent from 2004 to 2009. Nationally, the dairy growth areas continue to be in the west and southwest, including New Mexico, west Texas, west Oklahoma and southwest Kansas due to favorable environmental conditions. Southwest Kansas is benefitted by the drier climate with the added advantage of nearby dairy feed sources. The nationwide trend to larger regional processing plants continues.

Dairy product consumption has changed substantially over the past several decades. These changes have important implications for all involved in production, processing and marketing of milk and dairy products. A strong positive trend in per capita consumption of all dairy products has been shown since the mid 1970s, increasing by some 72 pounds per person (+13.4 percent). When one examines this increase in per capita consumption we see that cheese consumption has increased 130.3 percent while fluid milk and cream consumption has decreased 21.5 percent. The popularity of Hispanic foods and pizza, both utilizing large amounts of cheese, has fueled this overall increase in dairy consumption.

Milk Prices

Federal milk marketing orders have been an integral part of the U.S. dairy industry for many years. Milk orders were first implemented in the 1930s and have been a fixture ever since. They have been continually amended and updated, however, to accommodate industry modernization and changing marketing conditions. Fluid milk markets are inherently unstable due to the uncoordinated nature of fresh milk supply versus demand, which is compounded by milk's perishability and seasonal production variability. Federal milk orders were conceived and implemented with the goal of counteracting the inherent instability in fluid milk markets. The primary objective is to provide a framework to make buying and selling milk a more orderly process for producers and processors.

Milk prices received by dairy farmers hit a 30-year low in March 2009. The year 2009 was a difficult one for dairy producers. Plummeting prices in the dairy industry coupled with rising feed, energy and other input costs left many producers financially weaker. Producers who survived 2009 looked forward to a predicted milk price recovery in 2010. However 2010 milk prices did not recover to the extent expected.

For historical purposes we can compare late-year statistical uniform prices (SUP) in Central Federal Order No. 32. We see $20.36 for December 2007; $18.63 for December 2008; $14.96 for December 2009 and $15.29 for December 2010. In recent years the Cooperatives Working Together (CWT) program has tried to stabilize prices in a voluntary effort by producers to take cows out of production to help boost milk prices. The recent reduction in the number of Kansas dairies can mostly be attributed to CWT buy-out programs. Late in 2010 it was announced that the CWT programs would discontinue dairy buy-outs and focus more attention on increasing demand and sales of dairy products both domestically and exported.

The outlook for 2011 farm prices is somewhat better. Even though the future looks brighter, it is going to take time for dairy farmers to gain back the equity that they lost in past years.

Dairy Consumer Issues

Consumers of milk and dairy products have never had as many choices as today. Prices for whole milk in retail stores are currently averaging just over three dollars per gallon. Milk labeled "natural" or "rbST free" command higher prices and organic milk is priced even higher in the stores. Consumers are confused by the many labels they are confronted with in stores. Furthermore, processors sometimes label milks as "antibiotic free", "pesticide free" or "milk from cows not treated with rbST". All milk is tested repeatedly to assure it to be completely free of antibiotics and pesticides. The U.S. Food and Drug Administration approved the use of rBST in 1993. However, many dairy farmers and producer groups believe these label statements are misleading to consumers. Some producers fear that approved technologies such as rBST that allow them to efficiently produce milk may not be available to them in the future. The dairy industry has learned that it must listen closely to consumers and provide innovative ideas, products, ingredients and packaging to meet their needs.

Several Kansas dairy producers are pasteurizing, bottling and packaging dairy products on-farm in an effort to take advantage of consumer demand for "natural" dairy products. The success or failure of these operations will depend on the producer's ability to successfully compete with regional dairy processors in the market place. Small on-farm dairy processors trying to establish niche markets must somehow reach confused consumers trying to do the right thing while managing food budgets in a down economy. In the end high quality dairy products, produced locally can still command premium prices.

Regional Dairy Compacts

The Kansas Legislature acted in 1999 to allow the Kansas secretary of agriculture to enter into a southern interstate dairy compact if it was determined it would benefit Kansas producers. The Kansas Dairy Association supported this action. The goal of compacts was to stabilize prices paid to farmers for fluid milk, thus reducing business uncertainties and stabilizing the regional milk supply. There has been no action to form such a compact in the past year, and none is expected in the near future.

Conclusion

The dairy industry continues to change at a fast pace. Historically, dairy markets were local with farm produced milk being processed and marketed in the nearest city of any size. However with the advent of better refrigeration and transportation, the dairy industry has become regionalized. Global markets now affect even the smaller producers as evidenced by the pressure on United States milk regulators to lower somatic cell count levels. Kansas is adapting with many positive changes. Increases in total milk production improves the state's chances of attracting a new processing plant with jobs and economic benefits. Also, several smaller producers are developing ideas to produce cheese or bottled milk for niche markets.

At this time the Kansas Dairy Marketing Advisory Board does not see a current need to establish a statewide milk marketing order and respectfully recommends to the Kansas Legislature that it continues to monitor these issues and their impact on the production practices and the milk prices paid to the Kansas Dairy Industry. We thank the Kansas Legislature for its interest. The Board stands ready to appear before the Senate and House Agricultural Committees, if appropriate, to discuss these ongoing issues and any recent developments.