

UNITED STATES DEPARTMENT OF AGRICULTURE  
BEFORE THE SECRETARY OF AGRICULTURE

In re: ) [AO]  
 ) Docket No. 15-0071  
 )  
Milk in California )  
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\_\_\_\_\_ )

VOLUME XXIV

TRANSCRIPT OF PROCEEDINGS

October 27, 2015

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Milk in California )  
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BEFORE U.S. ADMINISTRATIVE LAW JUDGE  
JILL S. CLIFTON

Tuesday, October 27, 2015

9:00 a.m.

Clovis Veterans Memorial District  
808 4th Street  
Clovis, California 93613

TRANSCRIPT OF PROCEEDINGS

VOLUME 24

Reported by:

Myra A. Pish CSR  
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 6 PAMELA ELLIOTT, Marketing Specialist

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 OF AMERICA, INC., Hanson Bridgett, San Francisco  
 9 LAND O'LAKES, INC.: BY: JOHN VLAHOS, ESQ.

10 DAIRY INSTITUTE OF Davis Wright Tremaine  
 11 CALIFORNIA: BY: CHIP ENGLISH, ESQ.  
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12 LEPRINO FOODS: SUE TAYLOR, Vice-President  
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 MIGUEL RAMIREZ

14 DEAN FOODS COMPANY: ROB BLAUFUSS

15 HILMAR CHEESE JOHN VETNE  
 16 COMPANY: JAMES DeJONG

17 CALIFORNIA PRODUCER Stoel Rives  
 18 HANDLERS ASSOCIATION: BY: NICOLE HANCOCK, ESQ

19 SELECT MILK PRODUCERS: MILTNER LAW FIRM, INC.  
 20 BY: RYAN MILTNER, ESQ.

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1 TUESDAY, OCTOBER 27, 2015 - - MORNING SESSION

2 JUDGE CLIFTON: We are back on record, it is  
3 October 27, 2015. It's a Tuesday. It's 9:00 in the morning.  
4 We're in Clovis, California, and today is Day 24 of the milk  
5 hearing. My name is Jill Clifton. I'm the United States  
6 Administrative Law Judge who is assigned to take in the  
7 evidence at this hearing. I am a USDA employee. My  
8 involvement with the decision making process ends when I  
9 certify the record. That is, I say what the exhibits are, I  
10 say what the transcript volumes and pages are, and I have made  
11 any corrections to the transcript using as guidance, proposals  
12 made by anyone who wishes to propose a change.

13 All right. Let me now take the appearances of others  
14 participating. I would like to begin with USDA employees, and  
15 after that go onto other participants in the hearing.

16 MR. FRANCIS: Good morning. William Francis,  
17 F-R-A-N-C-I-S, Dairy Marketing Specialist United States  
18 Department of Agriculture Marketing Services, Dairy Programs.

19 MS. MAY: Good morning, Laurel May, USDA AMS Dairy Program  
20 Marketing Specialist.

21 MS. ELLIOTT: Hello, my name is Pamela Elliott,  
22 E-L-L-I-O-T-T, I am a Marketing Specialist with the USDA AMS  
23 Dairy Program.

24 MR. CARMAN: Good morning, Clifford Carman, C-A-R-M-A-N,  
25 Assistant to the Deputy Administrator Dairy Programs

1 Agricultural Marketing Service U.S. Department of Agriculture.

2 MR. MYKRANTZ: John Mykrantz, J-O-H-N, M-Y-K-R-A-N-T-Z  
3 Agricultural Economist with the Pacific Northwest and Arizona  
4 Orders on detail with Dairy Programs.

5 MR. SCHAEFER: Henry Schaefer, H-E-N-R-Y, S-C-H-A-E-F-E-R.  
6 Agricultural Economist for the Upper Midwest Milk Marketing  
7 Area Federal Order 30, on detail with USDA Dairy Programs.

8 MR. HILL: Good morning, I'm Brian Hill, B-R-I-A-N,  
9 H-I-L-L, with the Office of the General Counsel's Regulatory  
10 and Food Safety Programs Division.

11 MS. CHILUKURI: Good morning, I'm Rupa Chilukuri, R-U-P-A,  
12 C-H-I-L-U-K-U-R-I, and I'm an Attorney with the Office of the  
13 General Counsel.

14 MR. BESHORE: Good morning, Marvin Beshore, M-A-R-V-I-N,  
15 B-E-S-H-O-R-E, Attorney for the three cooperatives which are  
16 Proponents of Proposal Number 1, California Dairies, Dairy  
17 Farmers of America, and Land O'Lakes.

18 MR. VLAHOS: Good morning, John Vlahos, J-O-H-N,  
19 V-L-A-H-O-S, with the firm of Hanson Bridgett, H-A-N-S-O-N,  
20 B-R-I-D-G-E-T-T, co-counsel for the co-op Proponents of the  
21 Proposal Number 1.

22 JUDGE CLIFTON: Mr. Vlahos, if you would come back to the  
23 podium. I didn't take your appearance in the morning but I  
24 know that you were here shortly after noon yesterday, and I  
25 just wanted to note that.

1 MR. VLAHOS: Thank you very much.

2 JUDGE CLIFTON: You're welcome.

3 MR. SCHAD: Good morning, my name is Dennis Schad,  
4 S-C-H-A-D, I work for Land O'Lakes.

5 MR. ENGLISH: Good morning, your Honor, my name is  
6 Chip English, C-H-I-P, E-N-G-L-I-S-H, I'm an Attorney with the  
7 law firm of Davis, Wright, Tremaine, with my principle office  
8 in Washington DC. I'm here on behalf Proponents of Proposal 2,  
9 Dairy Institute of California.

10 MS. VULIN: Good morning, Ashley Vulin, A-S-H-L-E-Y, V - as  
11 in Victor -- U-L-I-N, I'm also an Attorney representing the  
12 Dairy Institute of California.

13 MS. KALDOR: Good morning, Rachel Kaldor, R-A-C-H-E-L,  
14 K-A-L-D-O-R, Executive Director of Dairy Institute of  
15 California.

16 MR. HOFFERBER: Good morning, your Honor, I'm  
17 Scott Hofferber, S-C-O-T-T, H-O-F-F-E-R-B-E-R, and I'm with  
18 Farmdale Creamery.

19 MR. RAMIREZ: Good morning, my name is Miguel Ramirez,  
20 R-A-M-I-R-E-Z, I'm with Leprino Foods in Denver, Colorado.

21 MR. ZOLIN: My name is Alan Zolin, A-L-A-N, Z-O-L-I-N, I'm  
22 a consultant representing Hilmar Cheese.

23 MR. DeJONG: James DeJong, D-E, J-O-N-G, Dairy Policy  
24 Economic Analyst with Hilmar Cheese, dairy farmer-owned  
25 manufacturer of cheese, whey, and milk powders.



1 MR. De CARDENAS: Good morning, Gil de Cardenas with  
2 Cacique, G-I-L, d e, C-A-R-D-E-N-A-S, thank you.

3 MR. MOORE: Good morning, your Honor, Mac Moore with  
4 Cacique, M-O-O-R-E.

5 JUDGE CLIFTON: And how is Mac spelled?

6 MR. MOORE: M-A-C.

7 MR. VETNE: John Vetne, also a representative for Hilmar  
8 Cheese Company.

9 MR. BLAUFUSS: Rob Blaufuss, B-L-A-U-F-U-S-S, with  
10 Dean Foods Company.

11 MS. HANCOCK: Nicole Hancock, I'm an Attorney with Stole  
12 Rives, S-T-O-E-L, R-I-V-E-S, I represent the California  
13 Producer Handlers Association and Ponderosa Dairy.

14 MR. VANDENHEUVEL: Rob Vandenheuvel,  
15 V-A-N-D-E-N-H-E-U-V-E-L, here on behalf of Milk Producers  
16 Council, a California dairy farmer trade association.

17 MR. MILTNER: Good morning, Ryan Miltner, M-I-L-T-N-E-R,  
18 Attorney for Select Milk Producers.

19 JUDGE CLIFTON: Thank you. Is there anyone who has not yet  
20 come to the podium today who expects to testify today? All  
21 right. I see no one at this time.

22 I would like now to take announcements and other  
23 preliminary issues.

24 MS. MAY: Good morning, Laurel May, again. As you know, we  
25 are in this room today, and then tomorrow we will be in the

1 Independence Room for the rest of the week. I will find out  
2 some time today whether or not we can leave our things here in  
3 the building or if we need to completely take them away, and I  
4 will let you know that later.

5 As always, anybody that would like to, is invited to  
6 testify at this hearing, and anybody who would like to ask  
7 questions of any of the witnesses may do so.

8 We are broadcasting via live audio feed, and that link,  
9 if you want to send it to people, is [www.ams.usda.gov/live](http://www.ams.usda.gov/live).

10 We are recording transcripts of this hearing, which are  
11 available approximately two weeks after the end of each hearing  
12 week, and those are available for you to see at our AMS dairy  
13 site. And some copies of exhibits that we have already been  
14 presented with, are in the file boxes on the table in the back  
15 of the room if you would like to help yourself to any of those.

16 At the end of the day yesterday, Mr. Zolin was on the  
17 stand giving us his testimony, and I believe today we are going  
18 to switch gears a little bit and hear from some of the  
19 gentlemen that introduced themselves earlier. So I will let  
20 Mr. English describe his plan.

21 MR. ENGLISH: Good morning, again, your Honor,  
22 Chip English.

23 So partly because of how things went yesterday with  
24 witnesses, I think as a general matter going forward, if we  
25 have witnesses who are here for the long-term, they have to go

1 later in the day, so that if we have witnesses who need to get  
2 out today, or in future days, we'll put them on. So for  
3 instance, I think if I had known how things were going to go  
4 yesterday, and my dis-accommodation of Mr. Ahlem, I probably  
5 would have suggested to Mr. DeJong that he wait so that we  
6 could get all these things done. But that's, in retrospect,  
7 that's sort of helping people look at how to go in the future,  
8 at least as I plan to do it. That's how I would like to do it.

9 So I literally put Mr. Zolin on the stand yesterday  
10 because we had about ten minutes, and as it turned out, he had  
11 a statement that worked out in ten minutes. But I don't think  
12 doing his cross now is necessary, and so what I would like to  
13 do is have the following order today:

14 For Farmdale, the first witness will be  
15 Scott Hofferber, whose already introduced himself for the day;  
16 and followed by Cacique. And that will be, I have already let  
17 USDA know, the two gentlemen would like to testify as a panel  
18 for more efficiency, especially for cross-examination.

19 Obviously, if and when Mr. Ahlem shows up, my  
20 understanding is that he will know by 1:00 p.m. today about the  
21 jury duty issue, and so he could be here sometime in the  
22 mid-afternoon. We will absolutely accommodate him.

23 The next witness on the list, tomorrows, after  
24 tomorrows, after tomorrows, is Rob Blaufuss for Dean Foods.  
25 And my anticipation, based upon how yesterday went, is that

1 will fill the list. If it doesn't, I will deal with it then.

2 JUDGE CLIFTON: Thank you. That's very helpful. Are there  
3 any other preliminary issues? I will read into the hearing,  
4 the transcript, excuse me, the docket number by which this case  
5 is known by the Hearing Clerk in the U.S. Department of  
6 Agriculture. In brackets, [AO] number 15-0071. The AO stands  
7 for agreements and orders.

8 I just wanted to ask, for those of you who have  
9 exhibits that you have prepared ahead of time, how many of you,  
10 and I'll just ask counsel to raise their hands, how many of you  
11 are making the initial copies of those at a commercial place,  
12 like a Fed Ex office, or, you know, Kinko's or something like  
13 that? Okay. Nearly everybody. I would like you to keep  
14 trying to do that, if you can. We have this copy machine here,  
15 but as you probably have noticed, sometimes we need it  
16 immediately for a speaker whose just arrived, and it's very  
17 helpful if it's available then. So, that we'd still like to  
18 use it whenever we need it, but not for major production, if we  
19 can.

20 MR. ENGLISH: And this is Chip English. Your Honor, we're  
21 trying very hard. Every once in awhile something goes wrong.  
22 We appreciate the fact that it is here. But, for instance,  
23 Mr. Hofferber actually brought his own copies today, as did  
24 Cacique, so they have been made elsewhere, and we're very hard  
25 to make those offsite. But obviously, every once in awhile

1 like a one-page exhibit or something, and we really appreciate  
2 USDA's having the machine here.

3 JUDGE CLIFTON: Excellent. All right. You may call your  
4 first witness, Mr. English.

5 MR. ENGLISH: So I call to the stand Scott Hofferber of  
6 Farmdale Creamery.

7 JUDGE CLIFTON: Please make yourself comfortable.  
8 Ms. Elliott, we're marking an exhibit, will it be 107?

9 MS. ELLIOTT: That's correct.

10 JUDGE CLIFTON: All right. 107,

11 (Thereafter, Exhibit 107 was marked  
12 for identification.)

13 JUDGE CLIFTON: The exhibits are being distributed now.

14 MR. ENGLISH: Your Honor, between passing out the exhibits  
15 and the fly swatters, I lost track of what the exhibit number  
16 was.

17 JUDGE CLIFTON: 107.

18 MR. ENGLISH: Thank you.

19 JUDGE CLIFTON: Please raise your hand if you do not yet  
20 have a copy of Exhibit 107. USDA is going to share for now.  
21 All right.

22 I would like to swear you in in a seated position.  
23 Would you raise your right hand, please? And I'm going to have  
24 you speak into the microphone rather than to me, and we'll test  
25 how close you need to be.

1 MR. HOFFERBER: Certainly.

2 JUDGE CLIFTON: All right. Do you solemnly swear or affirm  
3 under penalty of perjury that the evidence you will present  
4 will be the truth?

5 MR. HOFFERBER: I do.

6 JUDGE CLIFTON: Please state and spell you name.

7 MR. HOFFERBER: My name is Scott Hofferber, spelled  
8 S-C-O-T-T, H-O-F-F-E-R-B-E-R.

9 MR. ENGLISH: So a couple preliminary things.

10 JUDGE CLIFTON: And you are?

11 MR. ENGLISH: Chip English.

12 So Mr. Hofferber's statement really consists of 11  
13 pages. And then on the back of 11 pages, are listed items 1.1,  
14 1.2, and 1.3, which is a portion of a transcript from CDFA. We  
15 don't expect or intend the court reporter to write into the  
16 record that portion of the transcript. Some of it will be  
17 quoted from anyway, but that's just a part of the exhibit that  
18 will be otherwise, hopefully admitted. But we're not asking  
19 for that to be typed into the transcript, and he won't be  
20 reading it, except to the extent he reads in his testimony.

21 And 2. Mr. Hofferber, if you can, when you have a  
22 heading, read the heading in along with your testimony.

23 MR. HOFFERBER: Very well.

24 DIRECT EXAMINATION

25 BY MR. ENGLISH:

1 Q. So why don't you get through the first paragraph of  
2 page 2 of your statement and I'll have a few questions.

3 A. In this testimony, the following definitions shall  
4 apply:

5 1. "We" or "we" or "Our" or "our" or "Farmdale", refer  
6 to Farmdale Creamery, Inc.

7 2. "COS" refers to "California Order System" as  
8 previously defined in this hearing's record.

9 3. "FMMO" refers to "Federal Milk Marketing Order"

10 4. "CDFA" refers to "The California Department of Food  
11 and Agriculture"

12 5. "Stab Plan" refers to the "Stabilization and  
13 Marketing Plans for Market Milk for the Northern California and  
14 Southern California Marketing Areas" as administered by CDFA,  
15 as well as any other related laws and regulations administered  
16 by CDFA.

17 6. "RDW" refers to "Roller-dried (popcorn) whey for  
18 animal feed"

19 7. "WPC-80 refers to "whey protein concentrate-80  
20 percent protein, human grade, powder".

21 I am Scott Hofferber, the Chief Financial Officer at  
22 Farmdale Creamery, Inc., and I am here at the direction, and on  
23 the authority, of its Board of Directors. I have been employed  
24 directly by Farmdale since May 1997, and was our outside  
25 Certified Public Accountant (CPA) in various capacities for

1 most of the prior 15 years while practicing in public  
2 accountancy. I received my Bachelor of Science degrees from  
3 the University of Redlands in 1978, and my Master's of Business  
4 Administration from the University of Phoenix online campus in  
5 2004. I achieved my CPA credential in 1988. I have actively  
6 served the California dairy industry during my tenure at  
7 Farmdale by testifying at hearings held by CDFA, serving on  
8 CDFA Secretary Kawamura's "Whey Review Committee", CDFA  
9 Secretary Ross' "Dairy Future Task Force" and as Vice-Chair of  
10 the Milk Producers Security Trust Fund.

11 Q. Thank you. Now, this is a Federal Milk Order  
12 proceeding under USDA as opposed to CDFA. Have you ever  
13 participated in a Federal Milk Order hearing?

14 A. No.

15 Q. Please continue.

16 A. Farmdale is a third-generation family-owned and  
17 operated dairy processing facility in Southern California in  
18 the City of San Bernardino. Farmdale was established in 1979  
19 by the Sibilio and Shotts families, spelled S-I-B-I-L-I-O and  
20 S-H-O-T-T-S, who had been operating in the dairy industry  
21 around the Los Angeles area since the 1950's. With fewer than  
22 500 employees, Farmdale processes an average 28 million pounds  
23 of milk and cream per month, or about 120 loads per week, into  
24 cheese, sour cream, WPC-80, and buttermilk. Farmdale is  
25 considered a "proprietary plant" because we have no ownership



1 interest in cows and must rely on supply relationships with the  
2 dairy producer community.

3 We are here to:

4 1. Express our opposition to the Cooperatives'  
5 Proposal 1, and our concern over the use of the phrase  
6 "disorderly marketing" to describe the current milk marketing  
7 situation in California.

8 2. If a Federal Order is offered for California,  
9 Farmdale would advocate for proposal proffered by the Dairy  
10 Institute of California, Proposal 2, which brings market-driven  
11 and market-clearing minimum values for milk, especially in  
12 valuing the whey stream, as a starting point for  
13 end-product-based value determinations.

14 3. Express our concern about the competitive  
15 disadvantage we face with the continuation of the preferential  
16 treatment enjoyed by producer-handlers in the milk pricing  
17 scheme.

18 Disorderly Marketing

19 The "Manufacturing" classes of milk in California are  
20 Classes 2, 3, 4a and 4b. Farmdale's operations have included  
21 California Classes 2, 4a and 4b. As such, we are periodically  
22 reminded of the "call provisions" within the Stab Plan where we  
23 would be put on notice that, if milk for the bottle should come  
24 into short supply, processors like us would be required to  
25 forego expected milk receipts in order to meet the needs of the

1 fluid markets. This is a clear indication that the Stab Plan  
2 was designed to assure an orderly supply to California Class 1  
3 utilization. We understand that, unless a shortage occurs, all  
4 is well and orderly with the Stab Plan and the marketing of  
5 milk. To use the term "Disorderly Marketing" to apply to any  
6 other issues such as the profitability of individuals or  
7 segments of the supply chain, is inappropriate in our view.

8 We also take exception to the phrase "The California  
9 Discount" as described by some producers. While there is  
10 clearly a difference between California Class 4b and the  
11 Federal Class III milk prices, the differences are explainable  
12 and are a significant part of this hearing process. We defer  
13 the detailed technical discussion of this issue to the  
14 testimony of others, but will discuss the impact of  
15 inappropriate end-product price setting where the whey stream  
16 is concerned in a moment.

17 The phrase "The California Discount" could just of well  
18 have been "The Federal Premium". Had that phrase been adopted  
19 instead, the tone of this debate might have turned away from  
20 raising minimum prices through the regulatory process, to  
21 raising premiums charged to processors through face-to-face  
22 arm's-length business negotiation, either through the  
23 producer's co-op leadership or directly with individual  
24 processors. The practice of adding a premium to the minimum  
25 regulated price has always been a tool available to the

1 California dairy industry under the Stab Plan. The use of  
2 premiums could have been employed to appropriately recognize  
3 the widely varying methods for dealing with the whey stream  
4 which results from cheese making.

5 The reality is best described by Land O'Lakes Vice  
6 President, Pete Garbani, in his responses to CDFA hearing panel  
7 member Don Shippelhoute's questions from the June 3rd, 2015,  
8 CDFA hearing. That hearing was called by CDFA Secretary Ross  
9 to consider temporary changes to the whey factor in the  
10 California Class 4b formula for pricing milk used to make  
11 cheese. The relevant portion of that hearing's transcript is  
12 attached hereto in Items 1.1 through 1.3. The text is  
13 recounted here as:

14 "MR. SHIPPELHOUTE: You are marketing some of your  
15 member milk to proprietary cheese plants, are you not?

16 MR. GARBANI: Yes.

17 MR. SHIPPELHOUTE: And you are able to extract premiums  
18 above and beyond the class price?"

19 JUDGE CLIFTON: Start that one again, please, the question.

20 MR. HOFFERBER:

21 "MR. SHIPPELHOUTE: And are you able to extract  
22 premiums above and beyond the class price?

23 MR. GARBANI: It's funny because when that negotiation  
24 happens the conversation usually heads toward, well, go to the  
25 Department and get it.

1 MR. SHIPPELHOUTE: So I'll take that as a no, you are  
2 not getting a premium?

3 MR. GARBANI: No, there -- there are premiums but it is  
4 not nearly what we think the milk is worth.

5 MR. SHIPPELHOUTE: And so what keeps you from getting  
6 what you think the milk is worth?

7 MR. GARBANI: Supply and demand."

8 We applaud Mr. Garbani's courage to tell it like it is:  
9 "Supply and demand". To cause a regulatory body to force  
10 prices above what can be recovered from the end-products is as  
11 disorderly as any other concept under discussion in this  
12 proceeding. To tie the value of the whey stream to dry whey or  
13 any other product of value, certainly places at fiscal risk all  
14 cheese makers who do not process whey into a product of value.

15 For example, as a result of CDFA's hearing process, a  
16 variable whey factor tied to a product called dry whey, was put  
17 into effect in 2003. At that time, we, Farmdale, considered  
18 the cost of disposal of the whey stream in the form of RDW as  
19 an additional cost of making cheese and did not segregate the  
20 cost component for whey from the cost of fat SNF and premium in  
21 the California Class 4b milk price. Also, the following  
22 figures are calculated using the full absorption cost  
23 accounting method, meaning that general administrative and  
24 overhead costs are allocated to the product lines, including  
25 RDW, in recognizing the profit or loss of any particular

1 product line. For 2005, we lost \$439,000 making cheese,  
2 including a \$260,000 loss from our waste whey stream sold as  
3 RDW. For 2006, we lost \$413,000 making cheese, this includes a  
4 \$142,000 loss from our waste whey stream sold as RDW. In 2007,  
5 through August, we lost \$347,000 making cheese, this includes a  
6 \$1,383,000 gain from our waste whey stream sold as RDW.

7 We concluded that the cost of milk for cheese had  
8 become greater than our ability to recover that cost in the  
9 marketplace. Continuing to pay for the whey in the cheese milk  
10 at a price which was based on a product we weren't making, and  
11 at a level that was severely negatively impacting the cheese  
12 product line, was untenable. Upon the realization of this  
13 collapse and the viability of cheese making, we shut our plant  
14 down on August 12, 2007. We, along with a number of other  
15 smaller cheese makers, immediately petitioned CDFA for a  
16 hearing on an expedited basis to correct this failure in the  
17 California Class 4b milk pricing formula. Thankfully, CDFA  
18 responded on an expedited basis with a call of a hearing that  
19 was held on October 10th and 11, 2007, and a hearing decision  
20 that was implemented on December 1st, 2007. As an aside, we  
21 expect that this responsiveness by the COS will be lost with an  
22 FMMO, a concern of ours contributing to our reluctance to  
23 support the move to an FMMO for California. With cooperation  
24 from our supplier co-op and our customer base, we returned our  
25 plant to operation on August 19th, 2007 and were able to stay

1 afloat for the three month hearing process.

2           Following the 2007 hearing decision, repeated efforts  
3 to re-introduce a variable whey factor into the pricing formula  
4 finally succeeded on September 1st, 2011, with subsequent  
5 repeated petitions for further increases. Recognizing that the  
6 COS had now been set up to repeat the terrifying situation we  
7 had experienced in 2005 through 2007, we had to take a hard  
8 look at our options, including going out of the cheese business  
9 all together, and decided to bite the bullet and make the very  
10 significant investment in a higher value whey processing  
11 facility. Our WPC-80 processing plant went into full operation  
12 in August of 2013. This so-called upgrade to our ability to  
13 efficiently eliminate the waste whey stream comes with great  
14 risk. The required capital investment, market development,  
15 global demand, and other factors, make this course of action  
16 worthy of our retaining any marginal improvements gained by  
17 affecting this change. It remains to be see whether or not we  
18 made the right choice.

19           With the advent of the WPC-80 product line, and in  
20 consideration of the enormous capital investment required, we  
21 changed our cost accounting practice to including the whey  
22 component cost portion of the California Class 4b milk price in  
23 the WPC-80 department, rather than leaving it in the cheese  
24 milk cost. For the following analysis, we included the whey  
25 component cost portion of the California Class 4b price in the

1 cost to process RDW in order to compare apples with apples.

2 The 18 months ending June 2013 of our RDW operation  
3 resulted in a loss of 1.21 cents per pound of cheese produced,  
4 a cost which was absorbed by the cheese operation. In the  
5 final six months ending June 2013 of the RDW operation, the  
6 result was a loss of 2 and a half cents a pound of cheese  
7 produced. This increase in loss was directly attributable to  
8 the -- strike the second to the -- higher California Class 4b  
9 milk price resulting from the increased whey scale implemented  
10 on September 1, 2011, in combination with the higher market  
11 prices for dry whey.

12 I want to re-read that sentence, if it's all right.

13 JUDGE CLIFTON: Please.

14 MR. HOFFERBER: It is kind of an important one.

15 This increase in loss was directly attributable to the  
16 higher California Class 4b milk price resulting from the  
17 increased whey scale implemented on September 1, 2011, in  
18 combination with higher market prices for dry whey. It was  
19 this continued erosion in our ability to recover the costs of  
20 RDW that reaffirmed our decision to move to WPC-80.

21 The 25 months ending August 2015 of our WPC-80  
22 operation resulted in a profit of .51 cents per pound of cheese  
23 produced, an improvement of 1.72 cents per pound of cheese  
24 produced (.0051- -.0121) gets you to 1.72 -- over the  
25 aforementioned 18-month period in the RDW process. The most

1 recent eight months ending August 2015 of the WPC-80 operation,  
2 however, resulted in a loss of 7.57 cents per pound of cheese  
3 produced, an additional loss of 5.07 cents of per pound of  
4 cheese produced (-0757- -.0250) over the similar RDW process  
5 timeframe.

6 The improvement to 0.51 cents per pound of cheese  
7 produced falls woefully short of the return on investment, or  
8 ROI, necessary to service the debt incurred on making the  
9 necessary investment. Further, the continuing price slump in  
10 the WPC-80 market strains our ability to service the debt and  
11 to remain in the cheese business.

12 The dramatic downturn in the market prices of WPC-80 in  
13 the last eight months leading to the aforementioned loss of 7.5  
14 cents per pound of cheese produced with our new operation,  
15 amplifies our earlier points regarding the risk we have  
16 undertaken to stay afloat in the cheese business. The  
17 inability of the pricing system to appropriately track the  
18 value of WPC-80 markets, or any particular whey disposal  
19 method, and translate that into an appropriate milk pricing is  
20 obvious and not accounted for in the Stab Plan or the FMMO  
21 Proposal 1.

22 In 2007, a variable whey factor nearly ruined the  
23 smaller cheese makers when dry whey prices went unexpectedly  
24 high. A hearing at that time returned the whey valuation to a  
25 reasonable flat rate of 0.25 cents per hundredweight.



1 JUDGE CLIFTON: That's 0.25 dollars.

2 MR. HOFFERBER: I'm sorry, you are correct. Yes. Right.  
3 25 cents a hundredweight. However, as the economic model for  
4 dairy farming in California has continued to underperform  
5 mostly due to an oversupply of milk in the existing and  
6 un-incented-to-expand processing complex, the outcry from the  
7 producer community has been reduced to the unwarranted,  
8 unjustified, and unproductive focus on the whey valuation in  
9 the 4b formula as a means to an end; that end being pure price  
10 enhancement.

#### 11 Mandatory Pooling

12 We believe that the COS has responded to the needs of  
13 the whole dairy industry in a timely and orderly manner. Some  
14 of the hearing decisions have fostered growth and prosperity  
15 and some have provided significant challenges to our operation.

16 That said, if the USDA determines that disorderly  
17 marketing does, in fact, exist in the COS, then we must  
18 advocate in the strongest manner possible for the proposal  
19 offered by the Dairy Institute of California. The Co-Op -- it  
20 says petition, I meant proposal -- the Co-Op proposal is vastly  
21 overreaching in its assertion that mandatory pooling is  
22 necessary for the new FMMO. Mr. Garbani's words echo here:  
23 "Supply and demand." To build a guaranteed price level at too  
24 high a cost to us, removing any ability to mitigate the costs  
25 of clearing the market in times of excess supply, would

1 certainly put our operation at greater risk than we already  
2 face with our move into WPC-80.

3 To our knowledge, no other FMMO has mandatory pooling.  
4 Rather, there is greater flexibility to find a market clearing  
5 price level in the current FMMO's than would result from the  
6 structure requested in the Co-Op's Proposal 1 for an FMMO for  
7 California.

#### 8 Proposal 3 - Producer-Handlers

9 Farmdale is opposed to Proposal 3; the maintenance of a  
10 producer-handler or producer-distributor exemption. This is an  
11 extremely delicate topic for us, as we have long-standing  
12 business relationships with some of the producer-handlers in  
13 the COS. It is, however, yet another peculiarity in the COS, a  
14 topic of disharmony within the producer community, and a real  
15 item of business concern to Farmdale. We appreciate that the  
16 Federal Orders have appropriately regulated producer-handlers  
17 whose markets attain a specified volume and support such  
18 regulation if a Federal Order is offered for California.

19 Farmdale is a "proprietary plant" meaning we have no  
20 source of milk or cream supply other than that which can be  
21 purchased from producers. In other words, we don't own or  
22 control any cows.

23 Sales-below-cost prohibitions exist in the Stab Plan in  
24 an attempt to prevent predatory pricing practices in the  
25 marketplace. Ostensibly, this prohibition leads to orderly

1 marketing and a level playing field among the purveyors of the  
2 end-products.

3 A producer-handler is, by definition, a cow-owning  
4 group who also manufactures end-products for sale into the  
5 marketplace. There is a limited volume of raw product that  
6 escapes certain costs relating to the pool and quota for these  
7 entities. This limited volume, however, is significant enough  
8 to create a competitive advantage at the customer-by-customer  
9 level over a proprietary plant which is fully regulated and  
10 supporting the pool and quota pricing system.

11 The raw product, being milk and cream, constitutes 64.7  
12 percent of the total cost to make our California Class 2, or  
13 Federal Class 1 and 2, end-products. A producer-handler could  
14 allocate that portion of raw product which benefits from  
15 preferential exempt quota treatment, segregating that product  
16 from its regulated price based products, and target another's  
17 customer with that temporarily cheaper product creating a  
18 predatory pricing opportunity that escapes sales-below-cost  
19 prohibitions. This competitive advantage in favor of a  
20 producer-handler is a continuing threat to our California 2 or  
21 Federal Class I and II operations.

22 JUDGE CLIFTON: Read that sentence again, please.

23 MR. HOFFERBER: Sure.

24 This competitive advantage in favor -- we're going to  
25 have to insert the word "of" there -- in favor of a

1 producer-handler is a continuing threat to our California  
2 Class 2 or Federal Class I and II operations.

3 Thank you, your Honor.

4 Hypothetically, a producer-handler offers a competitive  
5 product to an existing customer of ours at a price below our  
6 cost to make it. We then, would lose that customer to the  
7 producer-handler because their end-product is significantly  
8 cheaper. It then becomes quite a lot of effort to retrieve the  
9 customer. We frequently do get the customer back once pricing  
10 get normalized, as it inevitably would. In the meantime, the  
11 producer-handler could shift its "small volume" production  
12 focus to another customer. We agree that this would be an  
13 appropriate strategy if we had the same exemption that is  
14 afforded to the producer-handler. We don't have that  
15 exemption, and have to find other measures to retain customers  
16 when we compete head-to-head with a producer-handler enjoying  
17 the exemption.

18 Where we have no direct evidence that this hypothetical  
19 practice occurs, as we do not, nor should not have access to  
20 the books and records or internal communications of any  
21 producer-handler organizations, we have experienced  
22 circumstances in our market and our customer base which  
23 strongly suggest it has occurred, and is occurring. It is time  
24 for this inappropriate opportunity to be removed from the  
25 conversation.

1           And our testimony is respectfully submitted by me,  
2       Scott Hofferber.

3           JUDGE CLIFTON: Yes, go ahead and read exactly what you  
4       have got at the bottom of page 11.

5           MR. HOFFERBER: Very good.

6           Respectfully submitted, Farmdale Creamery, Inc.,  
7       Scott Hofferber, CFO.

8           JUDGE CLIFTON: Thank you. I would like to go back with  
9       Ms. Elliott and make the very small corrections. I would like  
10      us to turn to page 7, and in the middle of the page we're going  
11      to strike one of the phrases "to the".

12          MS. ELLIOTT: Okay.

13          JUDGE CLIFTON: "TO THE." All right. The next one is at  
14      the bottom of page 8, the last line, we're going to strike the  
15      word "petition" and insert the word "proposal".

16          MS. ELLIOTT: Okay.

17          JUDGE CLIFTON: And then the last one is on page 10, in the  
18      middle of the page we're merely going to insert the word "of"  
19      in the sentence that begins "this competitive advantage in  
20      favor."

21          MS. ELLIOTT: Okay.

22          JUDGE CLIFTON: And there we insert the word "of". Thank  
23      you, Ms. Elliott.

24      BY MR. ELLIOTT:

25      Q. And thank you, your Honor. Chip English.

1           Thank you for your testimony, Mr. Hofferber. Can you  
2 tell us a little bit about Farmdale Creamery, Inc.'s size?  
3 There's a -- there's a Small Business Administration rule that  
4 USDA applies, and it has to do with the number of employees  
5 throughout the entire company, so not just in the plant. But  
6 can you tell me how many employees your company has?

7           A. Yes, we have 100 employees.

8           Q. I know you weren't here yesterday, but at the end of  
9 the day Judge Clifton remarked on whether or not there's an  
10 ability to get what would otherwise be confidential information  
11 in the record with the respect to some of the costs and yields  
12 and perhaps even moisture levels. Have you participated in  
13 CDFA's cost studies?

14          A. Yes.

15          Q. For about how long?

16          A. 19 years.

17          Q. And as you say, you are a Certified Public Accountant?

18          A. I am.

19          Q. And what can you tell us about CDFA's cost studies with  
20 respect to the issues in this hearing, especially as to whey?

21          A. The Stab Plan includes, the pricing formulas under the  
22 Stab Plan include a make allowance, and in assessing where that  
23 make allowance should be set, the Department, the CDFA conducts  
24 a cost survey audit, if you will, of the cheddar makers in the  
25 state with respect to cheese, the butter powder makers. They

1 will test the manufacturing classes for cost figures. Those  
2 studies include inquiries about yields and inquiries about  
3 volumes of cheese processing, primarily cheddar. There are  
4 statistics calculated on a Monterey jack as well, but the goal  
5 is to get a cheddar-based make allowance number.

6 Those data I know have been presented in what are  
7 called pre-hearing workshops in the past at some of the prior  
8 hearings, that leads me to believe that those data are  
9 published by CDFA in a manufacturing cost study, which I have a  
10 pretty strong recollection that that is out there as public  
11 record. If not, it can certainly be ascertained from a number  
12 of the hearing records where those data have been included in  
13 the pre-hearing workshop materials.

14 Q. Thank you. You have used some phrase, we have had a  
15 lot of Economists on the stand, we have a couple of accountants  
16 but they have done a specific things. But you have used some  
17 terms of accountancy in your statement, and so I want to maybe  
18 explore a little bit more what you mean by full absorption cost  
19 accounting.

20 A. Certainly. In the academics of accounting you take  
21 classes that are sometimes called managerial accounting or cost  
22 accounting, and you learn how to construct a presentation of  
23 your financial information that is useful analysis to determine  
24 your profitability in any particular manufacturing or in any  
25 sort of production environment. Cost accounting is a method by

1 which you stratify your costs in a manner that causes them to  
2 be directly attributable to the product. So to describe this,  
3 there are a group of costs called direct costs. So for cheese  
4 making, if I put that cheese in a box, that box is a direct  
5 cost, the bag it is in is a direct cost, the milk that gets  
6 used in that production of that cheese is a direct cost, it  
7 just doesn't belong to any other department or any other  
8 product, it's a direct, what we call a direct cost. So we will  
9 classify a number of our expenditures as direct cost.

10 Now, the work of art in accounting is, how do you take  
11 something like your telephone bill and convert that to a direct  
12 cost? Well, unless you keep unreasonably expensive records in  
13 order to do that, you generally end up with that as a general  
14 and administrative expense. So you end up with a pool of costs  
15 over here of things that aren't directly attributable to the  
16 product, and you have to ultimately get them back into the cost  
17 of the product somehow. So some of the work of professional  
18 art here is to come up with the schemes by which you fairly  
19 allocate your G and A pool, general and administrative, pools,  
20 to the product lines such that you fully absorb all of the  
21 costs of your enterprise into getting it into the product. So  
22 when the sales guys come to me and say, what price do I need to  
23 get out of this product to cover all of our costs? You can  
24 provide them that number to some level of precision.

25 When I say that we're using full absorption cost, what



1 I am getting at is exactly that process. We have direct costs,  
2 we have operating costs, what's our, somewhat the work of art  
3 in terms of being directly or indirectly allocable, and then  
4 there's things you just have to give up on. The electricity  
5 bill that goes into the boilers, that goes into all the  
6 products, you have to meter the stuff and come up with a  
7 methodology.

8 Now, my allocation schemes at Farmdale, I probably have  
9 about 20 different allocation schemes with different bases for  
10 which we move things around on our cost accounting sheet. For  
11 our G and A pool itself, we have six pools. You have a G and A  
12 pool, we have a transportation pool, we have a maintenance  
13 department pool. And so we can say these costs are directly  
14 allocable to the maintenance department, but then that  
15 maintenance department serves the products somehow. And so  
16 there are different allocation schemes for each of these groups  
17 of costs.

18 For the G and A pool, we use a blended number of total  
19 revenue and total pounds of product moved through the plant.  
20 That was the fairest way we could think of at the time to move  
21 our G and A pool. All of that to say, once we have done all of  
22 that exercise in the accounting department, we come down with a  
23 profit or loss for that particular product line, and then take  
24 those numbers against whatever it is we're trying to measure  
25 and account for.

1           In my testimony, I talk about full absorption cost  
2 applying to profitability or loss relative to the whey stream.  
3 And so when I make that shift from including the price of whey  
4 in the milk in our RDW process, to moving it directly to the  
5 whey, we changed basically our cost allocation method once we  
6 went to the WPC-80 plant, to include the cost of whey against  
7 that. We believed that that line was going to become an  
8 end-product line in itself, profitable in its own accord and  
9 wanted to put the cost of the whey in the milk price against  
10 that profit center or cost center as it turns out. That's --  
11 something more?

12           Q. No, well, I think that's -- unless does Judge Clifton,  
13 do you want to ask?

14           JUDGE CLIFTON: So in what year did you move it? It is in  
15 your testimony, but I've forgotten.

16           MR. HOFFERBER: Yes, and actually, it can exist in both  
17 places, depending on the presentation. Yes, the question, well  
18 you heard the question.

19           How I present the information is fluid. I can change  
20 that at any time. For the sake of this testimony, when I first  
21 presented the RDW fiscal results, the cost of whey in the milk  
22 was not included in those numbers because at that time it was  
23 actually allocated back, it was its own cost department and got  
24 allocated fully back to the cheese to determine the  
25 profitability of the cheese.

1           Once we took on the WPC-80 line, with the huge  
2 investment that was involved, we determined that we wanted to  
3 make that then a profit center of its own. And so in doing  
4 that, we changed our methodology from leaving the cost of whey  
5 in the cheese milk number, to moving it to the whey number so  
6 that we had that number to compare to going forward. For this  
7 presentation, in order to compare apples to apples, I went back  
8 to the RDW world and took the whey component out and added it  
9 to the RDW line so that we have got the cost of whey in both of  
10 those sets of numbers for this analysis.

11           In terms of my presentation to the external world, like  
12 the banks and everybody, it started with the WPC-80 plant.

13 BY MR. ENGLISH:

14 Q. Which opened when?

15 A. We went full operation August 2013.

16 Q. Okay. Now, you just said for presentation to banks,  
17 etcetera. So this full absorption cost accounting is not just  
18 something you do internally, correct?

19 A. Absolutely not.

20 Q. It is something that you need to show for the purposes  
21 of getting and maintaining loans, correct?

22 A. That's correct.

23 Q. Okay.

24 JUDGE CLIFTON: So when you, in your testimony, show me a  
25 period of time in which cheese production lost money and

1 processing the whey stream lost money, is the loss of  
2 processing the whey stream included also in the cost of making  
3 cheese?

4 MR. HOFFERBER: In this presentation, the number where I  
5 say we lost X amount of money in cheese, did include the whey  
6 portion, and I broke that out as my second number in those  
7 three statements, lost or made. Because actually in 2007, the  
8 whey stream was actually very valuable because the price went  
9 up so high and our cost didn't change that much. It actually,  
10 the price in the market went up so high that it actually got  
11 stripped the cost of the whey in the whey stream.

12 JUDGE CLIFTON: As well it should, you would think.

13 MR. HOFFERBER: Well, yeah. The problem was, the cheese  
14 was kinda, sorta didn't really do the same thing, because for  
15 our operation, the cost of the whey in the milk was still in  
16 the cheese number. So even though the whey side went way  
17 north, we're absorbing all the cost of the milk in the cheese  
18 side, and the cheese side was where I said I was, \$1.383  
19 million to the good on the whey side, but I lost \$387,000 on  
20 the cheese side.

21 MR. ENGLISH: \$347,000.

22 MR. HOFFERBER: Sorry, 347 on the cheese side. So the  
23 cheese went down 1.8 million'ish, and the whey side, actually,  
24 in isolation, without the cost of the whey in that number, went  
25 up, because all the revenue was against the RDW and none of the

1 cost of the milk in that particular presentation.

2 BY MR. ENGLISH:

3 Q. So to be clear, back in those days when you are doing  
4 the calculation, you had the revenues over in the whey side,  
5 but you had the costs over in the cheese side.

6 A. The other way around.

7 Q. Okay.

8 A. For the RDW.

9 Q. For the RDW.

10 A. Because all the costs were against the RDW none of  
11 the -- well, all of the costs except for the milk --

12 Q. Right. Okay.

13 A. -- piece were in the RDW.

14 Q. So milk piece wasn't in the RDW, the milk piece was in  
15 the cheese?

16 A. Correct.

17 Q. So to the extent you had a \$1.8 million loss in cheese,  
18 some element of that is attributable to the actual cost of the  
19 whey being attributable to the cheese?

20 A. Correct.

21 JUDGE CLIFTON: Thank you, Mr. English, for letting me  
22 interrupt.

23 MR. ENGLISH: You're welcome, your Honor, please do. And  
24 I -- this is one of those cases where, because of my accounting  
25 background, I might start asking questions where I understand,

1 Mr. Hofferber understands, and maybe nobody else understands  
2 what we're talking about.

3 MR. HOFFERBER: I'm getting some affirmative nods.

4 JUDGE CLIFTON: Well, this witness, as you know, is  
5 extremely valuable because of his accounting background, plus  
6 his hands-on operation at a plant, so I am very grateful that  
7 he's here.

8 MR. ENGLISH: Thank you, your Honor, I am, too.

9 BY MR. ENGLISH:

10 Q. All right. Anything else on the full absorption issue  
11 or accounting issues for the moment? You may get some cross  
12 that goes there as well.

13 A. Sure.

14 Q. Now, you just mentioned, and I was going to go to page  
15 6 anyway, about the required capital investment, and I'm  
16 certainly not looking for a specific number, I'm very  
17 respectful of confidential information, but what was the  
18 relative size of that investment for the WPC-80 operation?

19 A. It was an amount, the amount of that investment -- I  
20 have phrased it this way in hearing testimony before -- the  
21 amount of that investment equalled the entire rest of our  
22 plant, Class 2, Class 4a, all the rest of our plant, at  
23 depreciated cost at that point in time. This investment was  
24 equal to everything else we had going on.

25 Q. Now, why did you choose to make, you know, to create a

1 WPC-80 operation, rather than a drying operation for dry whey?

2 A. All of the history of the price of that product allowed  
3 us to pencil out and come to an adequately profitable model for  
4 disposing of the whey stream by making this investment, and for  
5 a ten-year horizon I think is what we had picked as a payback  
6 on the thing.

7 Q. Are you going to make a ten-year horizon?

8 A. No, we're not, not if this keeps up.

9 Q. It's going to be longer?

10 A. It will be longer now.

11 Q. Does that mean that you couldn't pencil out a dry whey  
12 operation?

13 A. Dry whey had become a product in California that  
14 basically nobody was making. I think there's one operation  
15 maybe, one and a small one, that make the product. That's been  
16 an issue in hearings testimony over time, that how are we  
17 pegging dry whey, any value to dry whey when virtually there's  
18 really none of it going on in California. Now that we're  
19 talking about a national exposure, I think that conversation  
20 might change, because I think there's probably enough dry whey  
21 out there being made that it -- it can enter the conversation  
22 as a target. But our continuing position on this is that the  
23 amount of investment to do any sort of value added whey  
24 processing is so different between the different processes,  
25 that you really need to have a mechanism in the pricing scheme

1 to recognize all these individual methodologies in making whey.  
2 It turns out, WPC-80 has been so attractive for so long, we're  
3 so late to the game in this thing. The guys that were doing 80  
4 ten years ago are now doing isolates and other even higher  
5 value stuff. And it is just a quickly moving target in a world  
6 of making an investment that really needs a long payback  
7 period, and really can't suffer the kinds of changes in the  
8 underlying fundamentals to justify the investment. And that is  
9 a real problem with any of the regulatory ideas, in my opinion.

10 Q. So one final line of questions for direct. On page 6  
11 you referenced sort of what I would view as an extraordinary  
12 event, which was the shutting down of your plant in August of  
13 2007.

14 A. Yes.

15 Q. So I would like to discuss a little bit about what  
16 happened in sort of the milk movement marketplace as a result  
17 of that, you know, one-week shutdown.

18 A. Okay.

19 Q. So you have said that you have a cooperative  
20 Cooperative supplier. And but obviously for that week, I  
21 assume you didn't take any milk?

22 A. We took no milk that week, in our cheese operation.

23 Q. In your cheese operation.

24 A. We continued the Class 2 operation.

25 Q. But you didn't absorb into the Class 2 operation the



1 volume that was in the cheese?

2 A. No.

3 Q. Do you know where the milk went for that week that it  
4 normally would have come into your plant?

5 A. We made that inquiry at the time, and we were told that  
6 the milk that we would have taken, ended up in DFA's Corona  
7 plant, at Golden Cheese, which very shortly after that, they  
8 shut down, but that's another deal.

9 Q. Then --

10 A. We then inquired, well, how did that displace any of  
11 the Golden's milk? And we were told by our co-op rep that the  
12 DFA ended up then diverting milk into Idaho. And what we  
13 discovered a few months down the streamline is, we had cheese  
14 coming back into the LA market at prices lower than we could  
15 make it at under the state plan.

16 Q. And was that coming from Idaho?

17 A. Yes.

18 Q. Okay. So just to summarize that, for a one-week  
19 shutdown with milk being displaced, you ended up with  
20 competition coming from unregulated part Idaho, coming back  
21 into California as cheese?

22 A. Yes, that was our observation.

23 Q. And that was being priced lower than you were able to  
24 sell it at at a regulated price?

25 A. Correct.

1 Q. Okay. Now, you also referenced on page 6, the  
2 cooperation of your supplier co-op. And I don't want to go  
3 into a lot of details into that, but was there some kind of  
4 accommodation when you reopened in order to make everything  
5 work?

6 A. Yes. As I have spoken earlier in my testimony about  
7 premiums being charged over the minimum regulated price, in our  
8 agreement with our suppliers, we were paying a premium, a  
9 service charge, to get the milk to us. And part of the  
10 cooperation during this unusual event for us, the co-op  
11 suppliers suspended charging us those service charges for a  
12 period of time.

13 I also mentioned that we got cooperation from our  
14 customer base as well, and that was, we implemented a price  
15 increase at the same time, straining some of those  
16 relationships, but explaining to them the situation and  
17 educating them on what all was going on in the business. And  
18 they worked with us on that for a timeframe that got us through  
19 to the December 1 hearing decision.

20 Q. Now, given the circumstances of supply and what was  
21 going on in the marketplace, as opposed to having to have that  
22 discussion with your cooperative cooperative supplier, it would  
23 have been much simpler if you could have purchased milk below  
24 class, correct?

25 A. Yes.

1 Q. Your Honor, I have no further questions on direct, and  
2 I move the admission of Exhibit 107.

3 JUDGE CLIFTON: Is there anyone that wishes to ask  
4 questions of Mr. Hofferber about Exhibit 107 before determining  
5 whether you object? No one. Is there any objection to the  
6 admission into evidence of Exhibit 107? There are none.  
7 Exhibit 107 is admitted into evidence.

8 (Thereafter, Exhibit 107 was  
9 received into evidence.)

10 JUDGE CLIFTON: Who would like to ask questions of  
11 Mr. Hofferber to begin? Mr. Beshore.

12 CROSS-EXAMINATION

13 BY MR. BESHORE:

14 Q. Good morning, Mr. Hofferber. Marvin Beshore.

15 A. Good morning, sir.

16 Q. So, as you know, I represent your cooperative  
17 Cooperative.

18 A. Yes.

19 Q. I'm not sure -- one of them is. So we appreciate your  
20 patronage, certainly your -- and I appreciate, you know, some  
21 of the information you have provided here, which, you know, is  
22 beyond what's been provided by some other witnesses, which, you  
23 know, I think we all understand that.

24 Do you report, does Farmdale report to the National  
25 Dairy Products Weekly Mandatory Reporting?

1 A. Yes.

2 Q. Okay. So --

3 A. Weekly reporting meaning the price survey?

4 Q. Yes.

5 A. Yes.

6 Q. That's the one. Okay. You have indicated on page 2 of  
7 your statement, you process an average of 28 million pounds of  
8 milk and cream per month. So some of that, I take it, as you  
9 have stated, is cream, not milk. Do you purchase cream on the  
10 open market?

11 A. As opposed to?

12 Q. Well, cream is not regulated, the price of cream is not  
13 regulated by CDFA, correct?

14 A. Yes.

15 Q. Okay. So that's what I'm talking about, is the open  
16 market for cream.

17 A. The answer is yes.

18 Q. Okay. How do those values compare to, if you compare  
19 them to the minimum regulated values?

20 A. We pay, generally we pay class price plus a service  
21 charge for the skimming of the milk to get it into a form of  
22 cream. Once in awhile we have paid for a load at a multiplier  
23 of the Double A commodity butter price, which is, has been more  
24 expensive than the California regulated price or developed  
25 under the previous described scheme.

1 Q. Okay. So when you are paying class price for cream,  
2 what class is that?

3 A. Class 2, currently.

4 Q. Of the 28 million pounds of milk, do you care to say  
5 how much is milk versus cream?

6 A. 90 percent is Class 4b.

7 Q. 90 percent Class 4b?

8 A. 10 percent would be to Class 2.

9 Q. Okay.

10 A. Currently. We suspended our, abandoned our 4a  
11 operation five years ago or something. We stopped making  
12 butter about five years ago.

13 Q. Okay. But the sour cream, sour dressing, buttermilk,  
14 etcetera, that I'm just reading off your web page products --

15 A. I understand.

16 Q. -- they are about 10 percent of your volume?

17 A. 10 percent of the volume of milk going through the  
18 plant, yes.

19 Q. Are the -- was the cost pricing profitability,  
20 etcetera, of those products, rolled into your cheese cost  
21 accounting?

22 A. No.

23 Q. So when you offered P and L, profit and loss numbers  
24 here on cheese and whey in total operation, you have actually  
25 got another bucket, which is the Class 2 products?

1 A. Right. There's a buttermilk bucket and there's a sour  
2 cream bucket.

3 Q. Okay. And are those profitable lines?

4 A. Year over year, yes. There are periods of time during  
5 the year where they will become only marginally profitable.  
6 Actually, buttermilk is about break even actually for us, at  
7 full absorption.

8 Q. Okay. So but at full absorption, the other Class 2 --

9 A. Sour cream --

10 JUDGE CLIFTON: I have got to caution you. For this to  
11 look good when it's typed, his voice has to stop before yours  
12 starts.

13 MR. HOFFERBER: You are right. I have adopt my deposition  
14 mentality. Right?

15 JUDGE CLIFTON: You do.

16 MR. HOFFERBER: Everybody finishing.

17 JUDGE CLIFTON: You do. You were, you got an A plus, plus,  
18 on your testimony. Extremely excellently and paced beautifully  
19 presentation. But this part you are getting right now a C.

20 MR. HOFFERBER: Well, as a career overachiever, I will  
21 endeavor to do better.

22 JUDGE CLIFTON: Very good. And Mr. Beshore is formulating  
23 his question as he goes, so he's not finished until he stops.  
24 Okay. Mr. Beshore, do that again, wherever you were.

25 MR. BESHORE: And your Honor is absolutely correct, I am

1 formulating as I go and sometimes it's rather deliberately, or  
2 in a deliberate pace, put it that way.

3 And I don't know where I stopped, where I was, or  
4 where -- where you were.

5 JUDGE CLIFTON: Well, okay. So you were talking about, you  
6 know, were each of the lines profitable, and then he said  
7 buttermilk about break even. Does that help? Do you want it  
8 read back?

9 MR. BESHORE: Do you remember what you were responding to?

10 MR. HOFFERBER: I was -- you had asked about other buckets,  
11 and I had identified two of them, the buttermilk bucket being  
12 more or less break even over time, and the sour cream bucket  
13 being a profitable for us.

14 BY MR. BESHORE:

15 Q. Thank you. Okay.

16 At some point in response, perhaps in response to  
17 Mr. English, you were identifying six pools of costs and you  
18 talked about three. You, on my notes at least, you identified  
19 three, which were G and A, transportation, maintenance. What  
20 are the other three?

21 A. Warehousing, what I called indirect production costs  
22 which would include things like boiler systems, the cooling  
23 systems that apply to all of the buckets. Continue the phrase.

24 Q. Right, that's five.

25 A. Yeah, well, okay. We have ten, we had ten total when

1 we were doing butter, so we have nine now, and four of those  
2 are the profit centers; cheese, whey, sour cream, buttermilk.  
3 Now I need to identify five. And they are; transportation,  
4 warehousing, indirect production costs, maintenance, and  
5 G and A.

6 Q. Okay. Five rather than six?

7 A. Well, we had this butter department that was floating  
8 out there as a number when it was ten, but that's, like I say,  
9 been gone for about five years.

10 Q. That's gone. Very good.

11 JUDGE CLIFTON: That last one, G and A, what does that  
12 stand for?

13 MR. HOFFERBER: General and Administrative costs; the phone  
14 bill.

15 JUDGE CLIFTON: Thank you.

16 MR. BESHORE: Executive salaries.

17 MR. HOFFERBER: Yes.

18 BY MR. BESHORE:

19 Q. Right. Okay. Let me, a couple of questions about the  
20 cheese operation. Do you -- do you -- how do you market your  
21 cheese? Strictly at 40 pound blocks or do you process it into  
22 consumer packages or can you tell us about that?

23 A. We make a 40 pound block product solely. We do market  
24 a very small amount of shreds of our own product, where we will  
25 make the product in a 40 pound block, send it out to a



1 shredder, take it back, and re-sell it. But it is an  
2 experiment for us right now, it doesn't hit the radar in terms  
3 of any kind of real numbers.

4 Q. To what locations do you -- do you sell the 40 pound  
5 blocks?

6 A. Okay. Our product is sold as far East as Colorado; as  
7 far South as into Mexico; and as far North as, we have product  
8 going into Washington and Idaho at one time, and that would be  
9 not 5 percent of our overall output. The by far majority of  
10 our overall output stays in Southern California. San Diego, to  
11 Calabasas, to Las Vegas. Las Vegas not being Southern  
12 California, per se.

13 Q. Okay. How much of it stays in-state, if you know?

14 A. What's that?

15 Q. What percentage stays in the state California?

16 A. 95 percent.

17 Q. Of the total cheese production?

18 A. Yes.

19 Q. Okay. So that mostly goes then to what have been  
20 referred to in some of the testimony here earlier, to  
21 converters who cut and wrap it and into consumer packages?

22 A. Right, shreds is a big portion of our customer base.

23 Q. Okay.

24 A. Institutional food service. We'll sell it into  
25 restaurants that will shred it themselves or do whatever they

1 want with it, but it's going off of our side as a 40 pound  
2 block.

3 Q. Do the customers to whom you sell for shredding,  
4 converting for shredding and cutting and wrapping, do they also  
5 purchase from other sources?

6 A. Yes.

7 Q. From what -- from where?

8 A. I --

9 Q. Who are your competitors, I guess?

10 A. This is only to my knowledge, I'm not on the sales  
11 team, so I have a very limited awareness of all of this. But I  
12 know we do compete head-to-head with Hilmar quite often, and  
13 then Pacific Cheese for the shred stuff, we'll compete with  
14 them.

15 Q. Okay. How about out-of-state competitors?

16 A. Yes, but I don't know names of where that we do run  
17 with.

18 Q. Do you know, without the names of the companies, do you  
19 know the location of the out-of-state --

20 A. No --

21 Q. -- competitors?

22 A. -- I do not.

23 Q. Okay. Other than in the 2007?

24 A. 2007, we were given that specific knowledge on inquiry,  
25 yes.

1 Q. So in 2007, when you shutdown for a month, were you at,  
2 a week, I'm sorry, were you at the same volumes back then,  
3 roughly?

4 A. No.

5 Q. You were at a lesser or greater?

6 A. We were lesser. We were probably running, I would  
7 have, I can look at my testimony from that time, but I would --  
8 I would say 25 to 26 million pounds.

9 Q. Okay. So when you shut down for a week, you turned  
10 away, what, five million pounds of milk or so?

11 A. No, we turned away 90 percent of say 25 million, 23  
12 million pounds.

13 Q. Okay. I understood --

14 A. Oh, a month, sorry, you are right, five million pounds.  
15 Right. That's a fair number.

16 Q. Okay.

17 A. Probably 6, we were doing about a million pounds a day  
18 in the cheese side, so between 5 and 6.

19 Q. Okay. In your current whey processing operation of  
20 WPC-80, what do you do with the permeate?

21 A. Lactose permeate is sold back to a dairy farmer group  
22 as feed.

23 Q. So is there any -- as animal feed?

24 A. Yes.

25 Q. Okay. So is there any reason why that's not what

1 process for lactose, edible lactose or other --

2 A. There's no -- we were out of a capital budget, we  
3 couldn't afford to put that extra processing in.

4 Q. Okay. So when you made the, if I understood you  
5 correctly, when you made the investment in the WPC-80  
6 equipment, you projected, you did that over a ten-year horizon?

7 A. That's right, yes.

8 Q. Okay. So you were, you were projecting a ten percent  
9 return on the capital per year over that period of time?

10 A. Yes.

11 Q. And that was after a full cost absorption accounting?

12 A. Yes.

13 Q. Okay. And you based that off of the history of WPC-80  
14 market that, as you understood it?

15 A. Yes.

16 Q. Do you purchase, do you process whey for other  
17 entities? I mean, do you buy whey from other entities?

18 A. No.

19 Q. Is that a choice or, that you don't choose to purchase  
20 it, or is it not available from other entities, or can you tell  
21 us about that?

22 A. It's difficult to process whey from other facilities  
23 that aren't making the same product we make. If you are  
24 dealing with a cheese maker who is making a saltier product, or  
25 a more colored product, or, you need to conform their input to

1 your throughput. Does that make sense to you?

2 Q. I think -- I think so.

3 A. You have to -- I mean, if it comes in too salty, you  
4 are going to have to find a way to strip the salt out of it, so  
5 it is consistent with the rest of what you are putting through  
6 the process. So although we built our plant with some capacity  
7 to take external whey streams, we haven't found one yet that's  
8 compatible with our process. And that excess capacity isn't  
9 remarkable. We were expecting we might be able to help  
10 somebody else much smaller than us out, but there's another  
11 problem with whey in that it doesn't travel well. You will  
12 have to pasteurize it on creation, and you will have to  
13 re-pasteurize it when it shows up, because sitting in the truck  
14 for any length of time at all is a petri dish for the bugs.

15 Q. Okay. So there are some other cheese plants in your  
16 part of the state that do not have whey processing capability;  
17 is that not true?

18 A. Not the same as ours, correct.

19 Q. Okay. They make different cheese products than you do?

20 A. And they have their own whey settlement going on,  
21 whatever they can figure out how to do for themselves, yes.

22 Q. Okay. So their whey is either not available or not  
23 useful to you?

24 A. Or not economically viable to put through our system.

25 Q. Okay. Page 8 of your testimony you make the comment at

1 the middle of the page, that, I'm taking a phrase out of the  
2 sentence, "the economic model for California -- for dairy  
3 farming in California has continued to underperform."

4 What do you mean by that?

5 A. Dairy farmers aren't getting enough money.

6 Q. And that's due to their economic model?

7 A. That's due to the California Stab Plan not returning to  
8 them the money that they think it's worth. We need that. We  
9 need the dairy farmer in the community to run our plant, but we  
10 need to be working off the same page so that we're both  
11 profitable.

12 Q. So if they are not getting enough money and you are  
13 paying too much already --

14 A. No. Well, yeah. I mean, I'm paying too much already.  
15 I don't think I said that.

16 Q. Are you paying just the right amount?

17 A. I pay what the Stab Plan tells me to pay at this point.

18 Q. Okay. Well, if you are -- okay. Is that about the  
19 right amount as far as you are concerned?

20 A. I don't know that I'm allowed to have an opinion about  
21 it. It is what it is. I mean, we'll testify at hearings that  
22 we think that the variable factor in the whey stream when the  
23 underlying product is out of whack with what's reality of what  
24 we're making, yeah, we're paying too much in that situation.

25 Q. Okay. Like I said, how are the farmers going to get

1 more while you pay less?

2 A. That's the \$64,000 question.

3 Q. Okay.

4 A. Again, I'm an Accountant, not an Economist.

5 Q. You make some comments on pages 8 and 9 about, you  
6 know, under the heading "Mandatory Pooling". And I guess my  
7 only question about that is, where, you haven't testified in  
8 any Federal Order hearings, I think you made that clear,  
9 correct?

10 A. Correct.

11 Q. You have no, you have you have no business experience  
12 in a Federal Order regulatory system, correct?

13 A. Correct.

14 Q. Okay. So where do you get the information that leads  
15 you to make the comments you make on pages 8 and 9?

16 A. Industry publications, industry trade associations,  
17 Milk Producers Council Weekly Report, Cheese Reporter, Dairy  
18 Institute publications. I mean, I read.

19 Q. Okay. I think that's all the questions I have at this  
20 time. Thank you very much, Mr. Hofferber.

21 A. Thank you.

22 JUDGE CLIFTON: Mr. Hofferber, when you were describing  
23 where your cheese goes --

24 MR. HOFFERBER: Yes.

25 JUDGE CLIFTON: And I recognize the name San Diego, and you

1 named another name in Southern California that I did not  
2 recognize.

3 MR. HOFFERBER: Yeah, I said Calabasas, and actually that's  
4 kind of our sour cream world goes there, but our cheese will  
5 make it out to Ventura. Calabasas is C-A-L-A-B-A-S-A-S, by the  
6 the way. But then there's Ventura, Oxnard, we know we have  
7 some product making at that far Northwest of us.

8 JUDGE CLIFTON: All right. And when you say 95 percent of  
9 your cheese stays in-state in California, do you mean it's  
10 packaged in California or do you mean it's consumed in  
11 California?

12 MR. HOFFERBER: My comment with that has to do with my  
13 knowledge of the location of our customers. If they take the  
14 product and further broadcast it, I don't know that. So I, we  
15 do a study every year. We have to, we have to report to the  
16 City of Los Angeles for a tax that they impose on products  
17 being sold in Los Angeles, whether they are delivered into  
18 Los Angeles, or whether they are picked up and taken into  
19 Los Angeles we have to differentiate. So we do a study every  
20 year on our entire customer base, where is the stuff going. So  
21 based on that study as to where our products are landing, both  
22 by our own delivery, which is about 40 percent of our product,  
23 we deliver it, and it's about 60 percent is picked up will  
24 call. And once we pull the tailgate down and put the seals on  
25 it, I don't know where it goes necessarily. All I know is my



1 buyer, the buying entities account for about that number, 95  
2 percent staying home.

3 JUDGE CLIFTON: Thank you. Who next will ask questions?

4 CROSS-EXAMINATION

5 BY MR. VETNE:

6 Q. John Vetne, representative for Hilmar Cheese. Thank  
7 you, Mr. Hofferber, for interesting and detailed information  
8 about your system and costs, and not just abstract, but hard.

9 Along some of the lines that you just discussed about  
10 your product, somehow I lost the connection of the dots there,  
11 so pardon me if I go over ground that's previously been plowed.

12 At your plant you make 40 pound block cheese, correct?

13 A. Yes.

14 Q. And you do a little tiny bit of shredding at your own  
15 plant?

16 A. No, all the shredding is done offsite.

17 Q. Okay. So it is just 40 pound block. And is it just  
18 cheddar or are there other varieties you produce in block form?

19 A. We make cheddar, we make Monterey Jack, we make reduced  
20 fat versions of both, and we do some culture product of those  
21 same flavors.

22 Q. Okay. So it leaves your plant in 40 pound block and  
23 goes to a converter, cut-and-wrap operation. Are there  
24 multiple locations that you send your product to for that  
25 purpose?

1       A. Again, once we pull the tailgate down and put the seal  
2 on it, I don't know exactly where everything is going. But  
3 generally speaking, yes, there are more than one customer that  
4 will take the product and cut and wrap it; there's more than  
5 one customer that will take the product and shred it, or take  
6 the product and put it into their restaurant systems, and then  
7 the restaurants will do whatever they are going to do with it,  
8 shred it, or slice it, or whatever.

9       Q. Okay. Once you put the tailgate down, is that your way  
10 of describing the way you market FOB your plant?

11       A. That's correct. A hundred percent, FOB my plant.

12       Q. Okay. And you have buyers that receive it in bulk?  
13 You transfer title at that point?

14       A. Yes.

15       Q. Okay. Do you have multiple buyers or a principle  
16 buyer?

17       A. We have 130 customers.

18       Q. 130 converters that --

19       A. No, just all purpose, everybody that buys.

20       Q. Okay.

21       A. Plus or minus.

22       Q. For your block cheddar. Are there multiple --

23       A. The cheese, that's our total customer count. A lot of  
24 them buy both Class 2 and 4a product, so there's a lot of cross  
25 over between the two universes. I would say there's probably

1 90 cheese customers.

2 Q. Okay. Are any of the cheese products made from the  
3 block that you sell tailgate down at your plant, are any of  
4 those packaged under a label that is your own or is it all  
5 somebody else's label?

6 A. No, the only label that's our own is on the 40 pound  
7 block itself. We do not have it reconfigured with our label on  
8 it for cheese.

9 Q. Okay. So you identify your product by putting a label  
10 on the packaging of the block?

11 A. Correct.

12 Q. And then your customers convert it to something else  
13 and if they want to put their own, well, they put their own  
14 label on it and show the plant?

15 A. We're done with it.

16 Q. Okay. Okay. In '07, you indicated that you made  
17 inquiries about product coming in from Idaho. Was it your  
18 understanding that product was coming in from Idaho in bulk  
19 block form to some of your customers that were receiving your  
20 block?

21 A. It would be an assumption on my part, but because  
22 that's the only layer that we play on, I would have, I would  
23 believe that would be the case. But, specifically, I couldn't  
24 tell you.

25 Q. Okay. And the source of your information concerning

1 the source of Idaho milk was that business people in California  
2 with which you deal?

3 A. Yes.

4 Q. Okay. Your milk supplier?

5 A. My hesitance indicates yes.

6 Q. Okay. Now, let me talk about the buckets.

7 A. Sure.

8 Q. I want to get to your bucket list. When you calculate  
9 an account for cost, as I understand it, you originally took  
10 all the milk that came in for cheese and you disposed of the  
11 whey, and whatever costs those were, were allocated back to the  
12 cheese. So if you made a profit, you took value of cheese,  
13 minus the cost to dispose of whey and other costs, and  
14 determined a net profit, correct?

15 A. Correct.

16 Q. And now you split the milk going into cheese into two  
17 cost buckets to see how each performed separately, correct?

18 A. Correct.

19 Q. Okay. And there were times, as I understand it, when  
20 the cheese bucket made money but the whey bucket didn't.

21 A. You are talking about subsequent to the split?

22 Q. Yes.

23 A. Yes.

24 Q. Okay. And vice versa?

25 A. Yes.

1 Q. And in times when both buckets had a hole in them,  
2 neither bucket performed with a profit.

3 A. I would have to kind of look at the detail of those 25  
4 months just to be able to say absolutely yes to that. There  
5 are times when the whey bucket would do well enough and the  
6 cheese bucket would be breaking even.

7 Q. Okay.

8 A. And vice versa. I mean, I think the matrix is  
9 complete. I think all combinations of those opportunities have  
10 presented themselves in those 25 months.

11 Q. And you understand what's being proposed here in  
12 Proposal Number 1 would affect your cost input in both cheese  
13 and whey buckets?

14 A. Yes.

15 Q. Okay. The cheese bucket would come in your cost  
16 accounting with a regulated price from the Federal Order system  
17 that substantially exceeds the regulated price you have been  
18 paying in California, correct?

19 A. That's our understanding.

20 Q. And the whey bucket would come in with a regulated  
21 price in excess of what you have been paying in California?

22 A. That's what I understand.

23 Q. So if that, if that produces a loss in both of those  
24 accounting buckets, you might be able to continue to operate  
25 your entire company by making sour cream and cheese, correct?

1       A. Well, if whey is inextricably attached to cheese. So  
2 if the whey suffers enough such that it wipes out the cheese,  
3 we would have to seriously consider stopping both. But now,  
4 because we are doing what we are doing, it's a decision on both  
5 buckets.

6       Q. Okay. And if it's just a little bit of a loss, let's  
7 say you continue to operate --

8       A. As I described in my testimony, the 2005 to 2007 window  
9 in there, we were running the combined operations at a loss for  
10 an extended period of time.

11      Q. Okay.

12      A. And I was asked at that time "Why do you stay in the  
13 business?" And it was, we believe the system will correct  
14 itself and we have got a huge investment in place, we have got  
15 families here in California, we really would rather not go.  
16 But these days it's, everybody's older, and the kids are out of  
17 school, so we don't have that tie anymore.

18      Q. Well, in that circumstance where there's a little bit  
19 of a loss, little bit of a struggle to continue to make cheese  
20 and cheese byproducts, when there's a bit of a loss in the  
21 cheese, combined cheese operations, what does that do to your  
22 competitiveness in the sour cream and buttermilk end of your  
23 business? Does that affect your ability to compete with sour  
24 cream manufacturers or buttermilk manufacturers that don't have  
25 a component of cheese and whey loss?

1 A. No.

2 Q. It doesn't affect that?

3 A. It affects us if generally, but it does not affect the  
4 competitiveness in those two markets. They stand on their own.  
5 They are their own customers. There's not a lot of  
6 cross-reliance on the two products with our customer base.

7 Q. Okay. I'm talking about cross-reliance within your  
8 company of one profit center to another. For your whole  
9 company business, if --

10 A. I'm going to have to ask you to star that over.

11 Q. I'm not talking about competitiveness or your customer  
12 base outside, I'm talking about how you allocate costs and  
13 losses within your company. If you have, within your entire  
14 company structure, all the buckets put together, if you are  
15 losing money, a little money on making cheese and whey, you are  
16 making a little money on sour cream and buttermilk, aren't you  
17 losing some of your competitiveness? You would have to try to  
18 recover that in the sour cream, buttermilk market, or you would  
19 hope to?

20 A. Well, you would, of course, hope to. But, I mean,  
21 there's -- there's competition. We have a number of other  
22 processors out there that are making the same products and  
23 competing for the same customers, so you have to hold the line  
24 on the prices for the products.

25 Q. So as a matter of supply and demand and competition

1 reality, you can't pass that cheese cost on to your sour cream  
2 customers?

3 A. Only in our own internal mind, we'll subsidize the  
4 other side as long as we can go, but it's not going to  
5 translate to the marketplace.

6 Q. Thank you. You indicate that you dispose of your  
7 lactose stream to a dairy farmer group?

8 A. Yes.

9 Q. Describe physically the process for that in the  
10 transaction process?

11 A. You just want the financial transaction or do you want  
12 how the lactose is made?

13 Q. The -- well both.

14 A. Okay.

15 Q. Do you RO the lactose and condense it a little bit?

16 A. Yes. Cheese making is, you take 100 pounds of milk and  
17 turn it into 10 pounds of cheese, or 11 pounds of cheese, you  
18 end up with ostensibly 90, 89 or 90 pounds of whey. That's  
19 what happens.

20 You got to do something with the whey stream. 50 years  
21 ago we put it down the drain; 40 years ago we spread it over  
22 fields and sent it back as feed; 30 years ago people started  
23 cooking it and turning it into something else; 20 years ago we  
24 started making WPC-80 out of it and actually getting some money  
25 back for the, for the, you know, out of the milk. You know, 5



1 years ago or 3 years ago we joined that part of the fray.

2 This 90 pounds of whey, then, goes through what you and  
3 I would call centrifuges, but they are called separators and  
4 clarifiers, and a number of pieces of equipment to strip the  
5 rest the fat out, because traditionally fat is where the money  
6 is, and that ends up going back into the cheese, or utilized in  
7 some way in a higher value product than the whey stream. You  
8 don't want the fat going through your membranes anyway, because  
9 it will clog them up. But anyway, this now, I guess for a lack  
10 of a better word, clarified fluid stream now has protein in it,  
11 lactose in it, and other minerals, caseinates, and stuff that's  
12 left over from the cheese making process that doesn't get put  
13 into the cheese.

14 Q. And lots of water?

15 A. And a ton of water. A lot of it. So in our process,  
16 we take that now, and we run it through an ultra filtration  
17 membrane system. So we're pushing this fluid through very tiny  
18 membrane systems, and what comes out one side is lactose-laden  
19 water with the minerals in it, and what goes out the other side  
20 is a concentrated protein liquid. So we capture that protein,  
21 we blow it through a dryer system, and we make the powder out  
22 of it, the WPC-80 powder out of it. The permeate side of that  
23 now goes through an RO system, another membrane system --

24 Q. RO meaning reverse osmosis.

25 A. Reverse osmosis, right. We push this liquid through

1 that now, and we end up with two piles of liquid at this point.  
2 One is lactose-laden, or sugar, which we then collect and sell  
3 off as animal feed, and the remainder then gets through a third  
4 membrane system called a polisher, which takes all this little  
5 bitty amount of minerals and caseinates and stuff that's left  
6 in that, and we end up with water that's basically could be  
7 bottled as distilled water. It is very clean. So we recapture  
8 that water and put it back into our process for cleaning  
9 equipment and other usefulness where we don't have to buy water  
10 off the city instead.

11 Q. Okay. So now you have the RO'd --

12 A. But I'm just an Accountant.

13 Q. Okay. I'm enjoying this. Thank you so much.

14 So now you have the RO'd concentrated lactose, and  
15 describe physically where it goes from, after the RO process to  
16 your week, to your door, to some container, to a farm, or group  
17 of farmers.

18 A. As it's transferred off the RO system it goes into a  
19 50,000 gallon silo, and our customer for this product sends  
20 their trucks in and pumps that product off to the tune of about  
21 three or four truck loads a day of that lactose product, and  
22 then they drive it offsite in their truck and deliver it to  
23 their cows, however they, however they do.

24 Q. Okay. So that also is marketed FOB your plant to a  
25 buyer who picks it up.

1 A. Correct.

2 Q. And you don't really follow -- do you know what happens  
3 to it after the buyer picks it up? Do they combine it with  
4 other feed materials?

5 A. I have no -- I am sorry, I stepped on him.

6 Q. Just asking if you know what happens after they pick it  
7 up.

8 A. I do not.

9 Q. Okay. And then you mentioned part of the whey  
10 byproduct, a small part, is whey cream. You try to separate  
11 that. What do you do with that?

12 A. That returns to the cheese process.

13 Q. Okay. So you try to recover all of the butterfat in  
14 whey, in part of your cheese process?

15 A. Correct.

16 Q. Okay. Going back just momentarily to 2007 when you  
17 shut down your plant. As I understand it, you made a  
18 determination at that time that you could not receive raw milk  
19 of California origin for purposes of making cheese because the  
20 regulated price exceeded your ability to convert that milk into  
21 cheese and make any return on investment; is that correct?

22 A. That's correct.

23 Q. Okay. So there's been discussion here, I'm not sure if  
24 you have been following, about capacity. And the discussion  
25 has been two categories of capacity, one is absolute capacity,

1 is there a place where all the milk can go; and the other  
2 category has been willing capacity.

3 Do you understand what I mean by willing capacity?

4 A. I think I do.

5 Q. Okay. Would it be fair to characterize your cheese  
6 plant in 2007, and the experience you went through there, as  
7 one of those places where there was not willing capacity  
8 because the regulated price was just out of kilter?

9 A. Yes.

10 Q. Thank you. My notes are complete. Thank you so much.

11 A. Thank you.

12 JUDGE CLIFTON: Mr. Vetne, walking him through the actual  
13 manufacturing is very helpful. I'm glad you asked. Who next  
14 has questions for Mr. Hofferber?

15 MS. VULIN: Your Honor, I think the court reporter  
16 indicated she needs a break.

17 JUDGE CLIFTON: Oh, he's just getting good. All right.  
18 Let's take a break now. It's 10:44. Please be back and ready  
19 to go at 11:00.

20 (Whereupon, a break was taken.)

21 JUDGE CLIFTON: We're back on record at 11:00. Who next  
22 will question Mr. Hofferber?

23 CROSS-EXAMINATION

24 BY MS. HANCOCK:

25 Q. Nicole Hancock. Good morning.

1 A. Good morning.

2 Q. So let's start with, does Farmdale Creamery have any  
3 Class 1 sales?

4 A. No. Federal Class I, yes. California Class 1, no.

5 Q. Where would your Federal Class I sales occur?

6 A. It is in our buttermilk line. Buttermilk would be a  
7 Class I federal sale.

8 Q. Oh, you are saying it would be classified under Class I  
9 if you were under a Federal Order?

10 A. Correct. Right.

11 Q. Okay. So under the California State Order system you  
12 have no Class 1 sales?

13 A. That's correct.

14 Q. And is it, you have a section in here on disorderly  
15 marketing. Is it fair to kind of sum up by saying that it's  
16 your position that there is no disorderly marketing in  
17 California?

18 A. Yes.

19 Q. And on page 3 of Exhibit 107, your prepared statement,  
20 under "Disorderly Marketing", the last sentence in the first  
21 paragraph says, "to use the term disorderly marketing to apply  
22 to any other issues, such as profitability of individuals or  
23 segments of the supply chain, is inappropriate in our view."

24 Do you remember talking about that?

25 A. Yes.

1 Q. Did you write that sentence?

2 A. Yes.

3 Q. Okay. So when you say "profitability of individuals",  
4 are you meaning entities?

5 A. Yes.

6 Q. Okay. And --

7 A. And individual people. I mean, and processors, and  
8 producers. It's, profitability is not germane to the  
9 disorderly marketing term in our view. It has only to do with  
10 whether Class 1 is being supplied or not.

11 Q. So you were just intending it to be all-encompassing.  
12 So individuals meaning everyone within the California State  
13 Order system?

14 A. Yes.

15 Q. Okay. And then you used "individuals" to refer to all  
16 of the people and entities, whether it be processors or  
17 producers, and then you "use" segments to mean all different  
18 classes of milk; is that right?

19 A. That's a fair interpretation.

20 Q. Okay. And you say "segments of the supply chain" but  
21 do you mean to include production and processing as well?

22 A. Yes.

23 Q. Okay. And when you say "inappropriate in our view",  
24 you mean it would be an inappropriate characterization to say  
25 that there would be disorderly market conditions in any of

1 those aspects?

2 A. Other than, the only disorderly marketing is when  
3 Class 1 is not being supplied. I believe that's the technical  
4 definition, and that's what I'm talking about there.

5 Q. Okay. All right. So I want to talk a little bit about  
6 the California State Order system and how much familiarity you  
7 have with it. You have been working for a long time in the  
8 industry, right?

9 A. 19 years.

10 Q. I had to wait, because you have to -- they won't  
11 capture the nod of the head. You have to say it out loud.

12 A. I understand.

13 Q. So 19 years. And has it all been with Farmdale or as  
14 an Accountant servicing the industry?

15 A. The 19 years has been with Farmdale.

16 Q. And before that, you also worked as an Accountant  
17 servicing Farmdale; is that right?

18 A. Yes.

19 Q. And did you service other --

20 A. No.

21 Q. -- other dairies within the industry or other  
22 processors within the industry?

23 A. No.

24 Q. But you had other customers as well during the 10 years  
25 you worked as a CPA?

1 A. Yes.

2 Q. Did you work in private practice or on your own?

3 A. I was in public accounting the 15 years prior to  
4 joining Farmdale.

5 Q. And so since you have been with Farmdale you have had  
6 the opportunity to work within the California State Order  
7 system?

8 A. Yes.

9 Q. And have you participated in any of the hearings with  
10 CDFA?

11 A. Yes. In my opening descriptive paragraph I discuss  
12 that I attended a number of hearings, as well as served on a  
13 number of commissions, or groups set up by the Secretaries to  
14 deal with Stab Plan issues.

15 Q. And to deal with -- say that again?

16 A. Stab Plan issues. Stabilization Marketing Plan issues.  
17 That's defined in my testimony, Stab Plan.

18 Q. And were you, on behalf of Farmdale, ever a sponsor or  
19 a requesting party to CDFA to ask for any kind of changes to  
20 the system?

21 A. Yes.

22 Q. And have any of those changes ever been implemented?

23 A. Yes.

24 Q. And what about any type of legislative changes, have  
25 you participated in proposing or putting information into the



1 record for any legislative amendments?

2 A. Yes.

3 Q. And were any of those changes made?

4 A. No.

5 Q. Okay. But you have participated then, in both the, on  
6 the regulatory side and the legislative side under the State  
7 Order system?

8 A. Yes.

9 Q. And are you familiar with the California quota system?

10 A. Yes.

11 Q. And what do you understand that to include?

12 A. My understanding of the California quota system is that  
13 it was implemented in the '60's, I think, at the time when the  
14 pooling system was set up, in order to incent Class 1 producers  
15 to join the pool. And so those folks who were benefitting from  
16 the higher valued milk would retain some relative higher value  
17 to the rest of the producers in order to cause the pool to be  
18 created in the first place.

19 Q. And that -- that translated into, quota was assigned  
20 based on the historical production of Class 1 milk?

21 A. Historical production and utilization on a  
22 farmer-by-farmer basis, I would say.

23 Q. Okay. And then at the same time, the exempt quota was  
24 assigned based on the historical production and sales of  
25 Class 1 milk to the producer-handlers?

1 A. Yes.

2 Q. Okay. And those are what you understand to be what has  
3 now, kind of through the years, evolved into be the quota  
4 system in the State Order system today?

5 A. Yes. And if I do understand it, that evolution is that  
6 we, the producer community has grown beyond the original volume  
7 of the assigned quota, so you have quota holders and non-quota  
8 holders now, and the exempt quota set up has stayed relatively  
9 the same, although maybe some of those original exempt quota  
10 members are gone. There's fewer of them than there were at the  
11 outset. I don't know if that's true or not, but I, that's my  
12 sense of it anyway at this point.

13 Q. And quota has moved around and --

14 A. And it's a saleable right.

15 Q. And do you ever, as part of the work that you do for  
16 Farmdale, ever do any kind of tracking of where that quota is  
17 sold to or who buys it and who sells it?

18 A. No.

19 Q. Okay. Do you ever do any kind of economic analysis  
20 about the effects of any kind of pricing impacts on your  
21 business?

22 A. No.

23 Q. What about with respect to exempt quota, do you do any  
24 kind of financial analysis with respect to the buying or  
25 selling of milk on your business?

1 A. No.

2 Q. And did you do any kind of economic analysis or  
3 financial evaluation for purposes of this hearing?

4 A. With respect to exempt quota?

5 Q. With respect to any quota?

6 A. No.

7 Q. And that includes exempt quota?

8 A. Correct.

9 Q. Okay. You mentioned in your testimony that, or not  
10 just mention, but you had a pretty sizeable discussion about  
11 the capital investments that were made so that you could evolve  
12 the business, so that Farmdale could evolve the business, to  
13 capture some of the whey value; is that right?

14 A. Yes.

15 Q. And in that, I think you then mentioned on page 7 of 11  
16 on your testimony, and you discussed it further, that part of  
17 the analysis that you conduct is what type of return on  
18 investment your going to get from making that capital  
19 investment; is that right?

20 A. Yes.

21 Q. And as your profits are trimmed down, it then cuts into  
22 the ability for you to make a return on the capital investments  
23 that you made into your plants and facilities?

24 A. Yes.

25 Q. So when you make an investment into plants and

1 facilities, is that because it is, is it a kind of vote of  
2 confidence into what you project your future revenues are going  
3 to be for your business in that market?

4 A. It would be an element of the analysis, yes.

5 Q. And if you had profits or you know, your profits were,  
6 your margins were so thin you weren't really sure if you could  
7 cover your cost of production, you would likely not be able to  
8 make those types of capital investments in your business; is  
9 that fair?

10 A. You would likely make another decision, yes.

11 Q. Such as selling off that arm of your business,  
12 potentially?

13 A. Yes, that's an option.

14 Q. Or changing business models into another, going in  
15 another direction?

16 A. Yes.

17 Q. Okay. Because if you make that investment into your  
18 business, you expect that you are going to be able to reap the  
19 benefits of that investment, right?

20 A. Of course.

21 Q. You talked about the time period where you had to shut  
22 down one of your plants for a week, and that was a big hit to  
23 your business as far as its operations, right?

24 A. Yes.

25 Q. And during that time, you mentioned that you had some

1 assistance from your customers and from a cooperative. Is  
2 that --

3 A. Yes.

4 Q. In the form of, your customers allowed you to increase  
5 prices and your cooperative allowed you to avoid some costs  
6 that you would have otherwise had to pay?

7 A. Yes.

8 Q. Why did they do that, do you know?

9 A. Processing capacity in the State of California is not  
10 growing, and wasn't growing at that time. We were losing  
11 processing capacity at the time, and I can see why the supply  
12 side of that calculation would want to assure that we survived.  
13 Back in those days, our co-op supplier would use the phrase "a  
14 balancing plant" and that was part of our conversation with  
15 them, that we would act as our, with our willing capacity, to  
16 run extra, or utilize excess normal capacity toward full  
17 capacity in situations of excess milk supply. I imagine,  
18 though I'm not part of their internal discussions, that was an  
19 element of why they would make that concession to keep us  
20 going. A million pounds a day is nothing to sneeze at, and  
21 they didn't need us to hand them five million pounds of milk  
22 back that week, so it was prudent for both of us, as we want to  
23 keep our plant running, keep our employees employed and stay in  
24 business, and they do too, that we came up with a methodology  
25 of helping to mitigate the problem at that time with the cost

1 of whey and the milk, and they helped us out with that.

2 Q. So the cooperative had some incentives to eliminate  
3 those additional costs as a way to try and help you stay  
4 afloat; is that fair?

5 A. It was a cost to them, a cost of their doing business  
6 for them to give up those service charges for that period of  
7 time, sure.

8 Q. And then what about your customer side? What is it  
9 that you understand would be the reason that they would allow  
10 you into crease costs?

11 A. They like our product, they want us to stay around.  
12 They like our service. They, you know, we have spent a long  
13 time building longstanding, good relationships with our  
14 customer base.

15 Q. So in both those instances you have some leverage over  
16 your cooperative and over your customers in order to help  
17 negotiate a better deal that would allow you and your business  
18 to continue a viable operation?

19 A. Leverage is kind of a, kind of a tough word. It would  
20 be, when it is all or nothing, you don't kinda, sorta. You are  
21 not sorta pregnant. You are either on or you are off when you  
22 are in this sort of situation, if that makes any sense.

23 Q. Yeah, but if a farm were to to go out of business, you  
24 have other farms that you can go to, right? It's a commodity.  
25 You don't really have to go to any one producer, right?

1       A. That statement is correct. My customers have other  
2 suppliers as well. So I mean, if we go out of business, I  
3 don't think it's the end of the world. I think it makes Hilmar  
4 happy on some level.

5       Q. And that's because Hilmar is a competitor of yours; is  
6 that right?

7       A. A direct competitor. We both make block cheddar cheese  
8 in the marketplace.

9       Q. And if you can get a better deal from one of your  
10 customers and displace customers of Hilmar, that's a benefit to  
11 you as well; is that right?

12       A. Our customer bases are fairly discreet. Hilmar is an  
13 operation 15 to 20 times bigger than me. They play on a full  
14 truck load kind of playing field. We more play on a  
15 pallet-to-pallet level. So we're not, we have access to a  
16 different market one layer away from Hilmar. Hilmar would have  
17 to sell their truck loads to a distributor who would break them  
18 down into the smaller pallet sort of deal. We're already there  
19 as an OEM, and that's part of how we can differentiate  
20 ourselves from their business model and compete with them.

21               We also have a transportation advantage into  
22 Southern California because we're there and they are up here.

23       Q. Tell me about -- what does that mean you have a  
24 transportation advantage?

25       A. Well, as long as there's enough milk in

1 Southern California to feed my plant, I can create cheese and  
2 ship it around Southern California at a milk reduced mileage  
3 component, in terms of transportation cost of that product.

4 Hilmar is making their product up here in  
5 Central Valley and would need to truck it all the way into  
6 Southern California.

7 We have, in the finance world, a thing called SWOT  
8 analysis, if anybody's familiar with that. It's, you look at  
9 your business and you analyze your strengths, your weaknesses,  
10 your opportunities, and your threats. And when we did our SWOT  
11 analysis on going to the WPC-80 plant, the two biggest threats  
12 we have are the regulatory milk pricing system and disconnected  
13 whey prices and all of that stuff when we're going into that  
14 whey plant. And the second biggest threat is the waning of  
15 milk supply in Southern California. There's going to come a  
16 day when we will be trucking 10 loads of milk to make one load  
17 of cheese out from the Central Valley, and Hilmar only has to  
18 truck that milk down the street. So they are going to drive  
19 one load of cheese into the Southern California, we're going to  
20 drive 10 loads of milk into Southern California out of the  
21 Central Valley. That's a threat. That day is coming. We hope  
22 it is 20 years out when we're all retired, but that clock is  
23 ticking. And that's -- that's an element of why we felt we  
24 needed to get into the 80 market, we wanted in a ten-year  
25 timeline on that project. There, so now you guys have all seen



1 behind the curtain.

2 Q. So I want to go back to the beginning of that. That  
3 was all really helpful. I want to make sure I understand the  
4 beginning part of that where you said that transportation is an  
5 advantage in Southern California. Is it too simple to say the  
6 advantage is just that you don't pay transportation cost that  
7 Hilmar has to pay in order to get product into the same  
8 location?

9 A. To ship cheese at a distance as X-cents a pound to the  
10 product, and I don't off top of my head recall what that number  
11 is, I get confused between loads and individual blocks and  
12 pounds and everything. But there is an increment of cost per  
13 mile to move that product. And so if I'm 50 miles from  
14 Los Angeles and they are 300 miles from Los Angeles, I have an  
15 advantage because I'm not moving that product that far, the  
16 finished product.

17 Does that answer your question?

18 Q. I think it does. So the answer is yes, then, right?  
19 You have a transportation advantage because it costs you less  
20 to sell into the Southern California market than it would  
21 Hilmar in order to truck the product down to the same area?

22 A. You understand.

23 Q. Okay. And does that give you a competitive advantage  
24 over Hilmar?

25 A. Well, it's a competitive advantage on that element.

1    However, there are a number of other disadvantages to where we  
2    are particularly located.  We, you know, you would have to, we  
3    would have to sit down with Hilmar and line up our cost  
4    accounting models next to each other, but we're not going to do  
5    that, of course, but I mean, if we compared item for item,  
6    there are a number of things for us that would be more  
7    expensive just because we're 1/15th their economies of scale.  
8    That alone is an enormous difference in our comparable cost  
9    structures.

10       Q.  Just your G and A bucket alone would -- would be  
11    different, than?

12       A.  Are you saying I'm being paid too much?

13       Q.  Because you fall into your G and A bucket, right?

14       A.  I absolutely do, both feet.

15       Q.  I think the lawyers do, too, so I feel your pain.  So,  
16    but -- but so there's different things that allow different  
17    businesses to have advantages over their customers one way or  
18    the other; is that right?

19       A.  Yes.

20       Q.  And any one of those competitive advantages is not  
21    going to create a disorderly market condition.  Would you  
22    agree?

23       A.  I would say in the aggregate, they individually would  
24    not create disorderly marketing.

25       Q.  I would --

1 A. Unless they ended up somehow shorting the Class 1 milk  
2 supply.

3 Q. I want to talk a little bit about, I guess what  
4 everybody's waiting for me to get to --

5 A. Yes.

6 Q. -- is page 9. Okay. So let me make sure my record's  
7 concise on this part. Let's look at Exhibit 107, I'm on page  
8 9. And I want to talk about "Proposal Number 3,  
9 Producer-Handlers" heading, the items that are underneath that  
10 section.

11 You have in here under the first paragraph in the  
12 section, it says, "It is, however, yet another peculiarity in  
13 the COS" and that's California State Order or order --

14 A. California Order System is how it's been defined in the  
15 hearing.

16 Q. "California Order System, a topic of disharmony within  
17 the producer community and a real item of business concern to  
18 Farmdale."

19 Do you see that?

20 A. Yes.

21 Q. What do you mean by "topic of disharmony"?

22 A. In my experience at the hearings that CDFA have held,  
23 the topic comes up from time to time, and we observe different  
24 producers groups talking about the producer-handlers and their  
25 differentiated status within the system, and that's the

1 disharmony I'm talking about. It's really discussions we  
2 observe inside the producer community about that, their  
3 existence, and their -- I like my other, their differentiated  
4 status.

5 Q. Okay. So there's a differentiated status is what you  
6 mean by disharmony?

7 A. Well, the disharmony is the fact that it gets talked  
8 about. If it just existed and nobody talked about it in the  
9 context of the hearings, then I would not see it as  
10 disharmonious.

11 Q. And then those discussions and the difference is what  
12 you say, it's a real item of business concern to Farmdale?

13 A. The real item of business concern to Farmdale is what I  
14 discuss later on in that testimony.

15 Q. Which would be what?

16 A. Which would be the hypothetical situation that could  
17 occur, where we get a, what I've called it a predatory pricing  
18 scheme that could hurt us on a customer-by-customer basis.

19 Q. And the hypothetical can't ever really come to fruition  
20 for you, because you don't have any Class 1 sales, right?

21 A. Well, I'm saying that, I'm saying there that if that --  
22 okay. I acknowledge that the exempt quota is aimed at Class 1  
23 utilization. However, if you are also a Class 2 plant, there's  
24 nothing keeping you from, in your internal buckets, taking that  
25 extra value that you are extracting on the Class 1 side, and in

1 your pricing, applying it to your Class 2 product, or your  
2 Class 3 product, or whatever, and saying, "Okay. That little  
3 benefit that we got over here in the Class 1 side, we're going  
4 to pull that out and call all of our Class 1 the same as  
5 everybody else's Class 1. We're going to take that benefit  
6 we're going to stick it against this Class 2 deal internally  
7 and we going to go get this customer." That opportunity  
8 exists. I'm not saying it's happening, we feel like it's  
9 happening.

10 Does that sufficiently separate the two things? And so  
11 you go back to the disharmony. What we're advocating here is  
12 just do away with it and nobody has this discussion or argument  
13 anymore.

14 Q. Right. So if you just do away with it, then there's  
15 nobody that will talk about it anymore, right?

16 A. There's nobody that will talk about it, our little  
17 paranoia goes away. That's really all we're saying here.

18 Q. I just want to dig in a little bit deeper.

19 A. Sure.

20 Q. So if you -- wouldn't the same be true for any  
21 efficiencies that you find in the business? I mean, like,  
22 let's take your transportation credits, or your transportation  
23 advantage that you just talked about between you and Hilmar.  
24 All right. Let's put a number on it, hypothetically, right?  
25 We're in hypothetical world. So hypothetically we'll put on

1 what, 5 cents a hundredweight, okay? I know it's a big number,  
2 but I'm just using a number that I can calculate easily. And  
3 you are a transportation allowance that is a benefit to you of  
4 5 cents a hundredweight that Hilmar would not have, if we were  
5 calculating hundredweight --

6 A. Don't worry about it, I got it. We're going to take  
7 exception to the word allowance when she gets done. That's  
8 fine.

9 Q. Let me say it over again, because I have bumbled my  
10 words up before up here, so I want to make sure that I say it  
11 correctly for you.

12 Your trans -- what you have described as your  
13 transportation advantage, right? Is that fair?

14 A. Sure.

15 Q. Okay. So let's say you have a transportation  
16 advantage. You can move that into the line items that allow  
17 you to negotiate your sales price to your customers as well,  
18 can't you?

19 A. Sure.

20 Q. And that gives you an advantage over, a competitive  
21 advantage over Hilmar?

22 A. I'm not physically co-located with Hilmar. The  
23 producer-handlers that we are paranoid about or that we have  
24 concern about, are in our market directly.

25 Q. But Hilmar sells product into your market; is that

1 right?

2 A. At a distance, yes.

3 Q. And it's that distance that gives you the competitive  
4 advantage, right?

5 A. Okay.

6 Q. Is that yes?

7 A. Yes.

8 Q. Because it's the distance that they have to travel that  
9 adds additional costs onto their products?

10 A. Yes.

11 Q. So when they are selling into your market in  
12 Southern California, you have a competitive advantage over them  
13 based on your transportation advantage; is that right?

14 A. Yes.

15 Q. Okay. So do you think it would be a meritoriously, a  
16 meritorious argument to say then, that Hilmar should not be, or  
17 that Hilmar could argue that you shouldn't be allowed to have  
18 that cost advantage in the market because it creates some  
19 disruption or some discussions?

20 A. No.

21 Q. It is not the same, right?

22 A. No, it's completely different. This is a regulatory  
23 piece that is being potentially used out of context, where this  
24 is supposed to be a Class 1 benefit. Because these  
25 producer-handlers are now into Class 2's and other products,

1 that compete with me, they have the ability to use that benefit  
2 out of context. And the transportation thing is just part of  
3 the noise in doing business. It's a completely different  
4 concept, completely different construct, in my view.

5 Q. And are transportation allowances regulatory?

6 A. We're not talking about transportation allowances,  
7 we're talking about the reality of the 5 Freeway.  
8 Transportation allowances are also a regulatory thing, which we  
9 don't necessarily have an opinion about because that's money  
10 changing hands between the producer community. They can fight  
11 that out among themselves all they want. That's them trying to  
12 figure out how to share the revenue pile among themselves.

13 Q. So I want to back up for a second. The transportation  
14 allowances are regulatory?

15 A. If you are going to use the technical term  
16 transportation allowances in the context of this hearing, yes.

17 Q. Okay. And that's a regulatory benefit that's given to  
18 producers in order to encourage milk to move into, say,  
19 Southern California?

20 A. That's my understanding, yes.

21 Q. Okay. So if a producer were in Northern California and  
22 making, producing milk and they were shipping it to a plant in  
23 Southern California, that producer would be allowed to take out  
24 of the pool some transportation allowances to help offset that  
25 additional cost. Is that your understanding?



1       A. At a high level, I think that's true. I believe  
2 there's some restrictions in the transportation allowance  
3 calculations, although I'm not that familiar with them, that  
4 just say you just can't ship this there because you feel like  
5 it, you know, there has to be some, there's some amount of  
6 control or whatever in there about utilizing that  
7 transportation allowance. There's rules about, you know, where  
8 you start and where you end, and where the processing plants  
9 are and all that stuff, but I'm not that familiar with it.

10       Q. And the reason you are making sure that I didn't  
11 confuse the two, is because you, as a handler, your business as  
12 a handler, you pay the same for the milk regardless, you don't  
13 pay the transportation allowances; is that right?

14       A. They are factored into the milk price, so I mean,  
15 dollars are being extracted from me in paying the minimum  
16 regulated price to cover the dollars that are used to be shared  
17 among the producers for those transportation allowances. But  
18 it doesn't matter to me which of the producers get the  
19 particular transportation allowance, I'm still paying the  
20 minimum regular price.

21       Q. So is that a yes?

22       A. Rephrase your question.

23       Q. You're paying the same price regardless of which  
24 producer has produced the milk; is that right? You are paying  
25 based on the class into the pool?

1 A. Yes.

2 Q. And the producer gets the transportation allowances  
3 paid out of the pool, and so -- well; is that right?

4 A. As far as I know, yes.

5 Q. Okay. And are you, is it your understanding that  
6 exempt quota producer holders, producers holding exempt quota,  
7 are not entitled to obtain any kind of transportation  
8 allowances?

9 A. I don't know that.

10 Q. You haven't conducted any kind of financial analysis to  
11 the pool to determine what kind of, what kind of impact would  
12 be had if the exempt quota was eliminated and then those  
13 producers would be entitled to transportation allowances?

14 A. I have not.

15 Q. Are you aware of how much exempt quota is held by any  
16 other producer-handlers?

17 A. Not as I'm sitting here today. I probably did at one  
18 time, but I don't know now. It's not very many entities, I  
19 know that. It's a small universe.

20 Q. Are you, so I'll tell you there's four entities, but  
21 are you aware of the volume of milk that is subject to exempt  
22 quota treatment?

23 A. No, it's small also. Relatively small.

24 Q. Small in comparison with the pool in the Class 1  
25 market?

1 A. Yes.

2 Q. I'm on page 10 of your prepared statement on  
3 Exhibit 107. And the paragraph where we were just talking  
4 about this, the hypothetical that you had proposed here, did  
5 you write this hypothetical?

6 A. I did.

7 Q. Did you write it on your own?

8 A. No.

9 Q. Did somebody give you the hypothetical to include in  
10 your statement?

11 A. No, I took information from the President of our  
12 company and his concern about this issue, and I drafted the  
13 language to go with it, to go with his narrative.

14 Q. So this is, this is all your own work then, or all  
15 yours and others within the Farmdale Creamery operation?

16 A. It is Farmdale's only.

17 Q. So if a producer, if a producer-handler was set up in a  
18 way that the producer was one entity and the handler side was  
19 one entity, and assuming they still met the ownership  
20 obligations, and it, and the producer, or the handler paid a  
21 Class 1 price for the milk, would your hypothetical still hold  
22 true?

23 A. Is the handler strictly a Class 1 handler or is it a  
24 Class 1 and Class 2 handler?

25 Q. Let's say it's a Class 1 and Class 2?

1       A. Then I think the situation would remain if they are  
2 completely co-owned. I don't know that splitting the entities  
3 would make any difference. I would have to analyze that  
4 because I'm sure there's all kinds of other state plan stuff  
5 that would come into play there in terms of the transfer of  
6 cost. But changing those two entities I don't think would  
7 matter much if it was all the same common ownership.

8       Q. And that's because even if there were some additional  
9 profits made by a separate entity, those profits could then be  
10 used by the handler side to generate a competitive advantage in  
11 marketing that product to a customer? Is that why you mean  
12 that they would both -- it wouldn't matter?

13       A. Yes.

14       Q. Okay. So we had a handler here yesterday that had an  
15 entity -- were you here yesterday?

16       A. No, I was not.

17       Q. We had a handler here yesterday that, they had a  
18 business and some related additional businesses in the  
19 entertainment industry, completely outside of the dairy  
20 industry.

21       MR. ENGLISH: I object to that characterization. The  
22 witness clarified that he thought that was advertising.

23       BY MS. HANCOCK:

24       Q. Okay. Let's go with that, then. So we had a handler  
25 here that had a separate business that was an advertising

1 business --

2 MR. ENGLISH: I think that's still a mischaracterization of  
3 what he said. That is absolutely not what he said. I think  
4 what he said was, that's our advertising. It's not a separate  
5 business. That's not what he said.

6 BY MS. HANCOCK:

7 Q. Okay. Well, let's go into hypothetical world then, so  
8 that we can avoid this. Let's say a handler had an  
9 entertainment business on the side that generated profits.  
10 Same ownership, same board -- same ownership, same board but  
11 separate legal entities. Okay?

12 A. Okay.

13 JUDGE CLIFTON: Same -- separate legal entities what, one  
14 is an entertainment and the other is a milk processor?

15 MS. HANCOCK: Yes.

16 JUDGE CLIFTON: Okay.

17 MS. HANCOCK:

18 Q. One is an entertainment business, one is a milk  
19 processor, but the ownership structure is the same between the  
20 separate legal entities.

21 A. They have common ownership.

22 Q. Common ownership.

23 A. Okay.

24 Q. And let's say that this entertainment business was  
25 wildly successful and that allowed them to reinvest those

1 profits into their processing business. Would that give the  
2 processing business a competitive advantage over others within  
3 the processing industry?

4 A. If they were able to use that advertising business to  
5 generate capital for their processing side that was more  
6 efficient than capital than mine, investment in the company,  
7 they would have a competitive advantage over me because they  
8 had access to cheaper capital, of course. That doesn't have  
9 anything to do with the flow of the minimum price of Class 1  
10 milk and being -- being dealt with in a Class 2 processor.  
11 We're getting away from the point of my testimony, actually.

12 Q. I think, I guess I'm just trying to figure out at what  
13 point does it become a situation that should be disallowed  
14 because it gives a competitive advantage. Can you answer that?

15 A. It becomes an issue inside a regulatory system that's  
16 trying to manage five different classes of milk, where you are  
17 trying to grant an advantage inside one class where it can  
18 bleed over into another class without any kind of, transparency  
19 I guess, for lack of a better word, I would say that would  
20 create disharmony.

21 Q. Okay. And if those potential differences or disharmony  
22 was just based on some subjecture that hasn't actually, that  
23 hasn't actually occurred, do you still think a change should be  
24 made?

25 A. It goes -- yes. It goes to a broader discussion about

1 a lot of little different things within the current COS that  
2 cause the spirit of pooling to be damaged, in my opinion.

3 Now, we're not inside the pool, so we really don't have  
4 a right to have an opinion about it. Really? Because I mean,  
5 the producer community gets to do what they want to do with  
6 that. But as an outside observer whose been watching this  
7 thing for a long time, it's fascinating to me how the, I have  
8 heard it phrased, "have and have not's" argument goes. There's  
9 lots of little silos, and lots of little special stuff going on  
10 inside the pool that makes one group of producers not happy  
11 with another group of producers. And, you know, if we're going  
12 to level the playing field, let's level the playing field.  
13 That's what we're talking about right here.

14 Q. Do you -- do you believe that quota should be preserved  
15 then, if a Federal Order is implemented?

16 A. I do not.

17 Q. And is there any -- let's say quota and exempt quota,  
18 are there any differentiating factors in preserving one over  
19 the other?

20 A. No.

21 Q. And just so we're clear, you don't have any instances  
22 to describe where you have had any customers that were  
23 displaced?

24 A. It is testified to.

25 Q. Thank you.

1 JUDGE CLIFTON: Ordinarily I would wait a minute to ask my  
2 additional questions, but I want to ask them now because I'll  
3 need follow up from people who understand this industry better  
4 than I do.

5 I would like to go to the bottom of page 9 of your  
6 testimony, Mr. Hofferber, and I'm looking at the very last  
7 paragraph. That phrase, "Sales below cost prohibitions exist  
8 in the Stab Plan," and I want to know how it works that people  
9 know what a below cost sale would be? How are these costs  
10 known?

11 MR. HOFFERBER: Right. How does this become apparent?

12 JUDGE CLIFTON: Yes.

13 MR. HOFFERBER: Yes, your Honor. In my direct experience  
14 with Farmdale, we will have a customer get on the phone and  
15 call us and say, "X, Y, Z Company is offering us a cheese  
16 3 cents a pound cheaper than you got it, how can that be?"  
17 Well, if it doesn't get below the minimum reg price of the milk  
18 translated into the cheese, there's not a lot I can do about  
19 that. For some reason, they have found an efficiency somewhere  
20 that allowed them to do that.

21 It hasn't happened that I can recall on the cheese side  
22 where a sales-below-cost issue has come up, but we have seen it  
23 on the sour cream side. Where, we look at our costs and our  
24 efficiencies, and we're not talking about, just about raw  
25 product costs being paid for by the minimum regulated price,



1 this is the whole surveyed cost engine that CDFA works with.  
2 But if we run onto a sour cream customer that's selling sour  
3 cream at, let's say \$3.00 a 32-pound tub cheaper than us, there  
4 is absolutely no way on the planet, if we're paying an equal  
5 minimum regulated price, Class 2 price in California, that that  
6 could even happen based on electricity costs being what they  
7 are, labor costs, I mean, we all pretty much are going to  
8 operate the same. So we have a pretty good idea of the  
9 relevant range of what cost would be for a 32-pound tub of sour  
10 cream. So when that happens, we, of course, hair goes up on  
11 the back of our neck, and we go, "how in the world can this be  
12 happening?"

13 So then to answer your question, your Honor, the  
14 mechanics of that are is that we would report that incident to  
15 the CDFA, and they would assign that case to an investigative  
16 group inside CDFA, and they would then dig into that. Go to  
17 the retail site, or wholesale site, whatever, they would start  
18 doing an investigation. Theoretically, that's how it is  
19 supposed to work. The fact of the matter is, the resources at  
20 the CDFA are such that that doesn't get done very often. So if  
21 they get a couple of complaints a year about something like  
22 that, they are even hard-pressed to really dig down into that.  
23 So the game is, is we try to convince our customer that that's  
24 just some sort of short-term stealing strategy or something  
25 like that, and we attempt to hang onto them as good as we can

1 in that situation. Is that relatively clear?

2 JUDGE CLIFTON: Very. Thank you. And then my other  
3 question is about the value of components of milk as the milk  
4 arrives at your processing facility. So from your point of  
5 view, I would like to take two points of view. I would like  
6 you to give me your point of view as a cheese manufacturer, and  
7 then I would like you to give me your point of view as a cheese  
8 manufacturer that operates a whey stream operation, such as you  
9 do. So -- so looking at the value of the solids in the milk as  
10 they arrive at your plant as a cheese manufacturer, what of  
11 those solid components have value for you, and how should their  
12 value be determined if there is to be a regulation governing  
13 the minimum regulated price?

14 MR. HOFFERBER: Milk for cheese rolls in at a nominal 3 and  
15 a half percent fat, 8.6, 8.7 percent solids not fat. Solids  
16 not fat includes the protein, and the lactose, and the  
17 caseinates, and all the other jazz that's in milk, it's  
18 everything that's solid that's in the water, that's not fat.

19 So when we make cheese, we end up extracting all the  
20 fat out of it that we can, even in the post-processing for the  
21 whey stream, and returning the fat to the cheese. So fat is  
22 the most valuable thing. Although you would still extract, I  
23 think it's about half the protein that is in the milk that  
24 stays in the cheese, I don't know, it's a rough number. You  
25 are still going to end up with a little bit of lactose, but for

1 all of those lactose intolerant people we recommend you try  
2 cheese, because there's not a lot of lactose that ends up  
3 staying in the cheese, it stays in the whey stream, so you can  
4 take one of your pills instead of four.

5           So when you look at it from a cheese-only perspective,  
6 it is fat and protein is what is of value in there. When you  
7 look at it including the whey stream, of course the entire  
8 protein stream becomes important, because what you have done  
9 now, is that 50 percent or so of the protein that's in the milk  
10 that previously escaped capture prior to the ability of  
11 membrane systems and what not to extract it, and preserve it,  
12 and convert it into something useful, you're dealing with that  
13 part of it as not as valuable, because you were just trying to  
14 get rid of it.

15           Lactose, you know, because of membrane systems, we have  
16 been able to figure out a way to efficiently take the water out  
17 of it and transport it in a concentrated form and exact a  
18 little bit of value out of that part of it. And then as I said  
19 earlier, the polished water that comes out the back end of it,  
20 we are able to supplant our purchases from street water to wash  
21 the plant and do some other nice things with it.

22           Is that satisfactory?

23           JUDGE CLIFTON: It is. And the product that you make, this  
24 protein product from the whey, it's not dry, the kind you make.

25           MR. HOFFERBER: Yes, it is.

1 JUDGE CLIFTON: It is. That portion is dry?

2 MR. HOFFERBER: If you like, I'll complete that first  
3 model.

4 JUDGE CLIFTON: Please.

5 MR. HOFFERBER: Okay. So we have taken the liquid protein  
6 in that first stage of the membrane systems in that whey  
7 processing plant, and we have parked it in a silo in a liquid  
8 form. We then take that and we put it in what's called a box  
9 dryer. Our particular system is a box dryer. Our particular  
10 system is a box dryer. There are two or three different  
11 methodologies by which you dry this stuff. But in our WPC-80  
12 process, you will heat that dryer up to something like 375  
13 degrees or 400 degrees, it's pretty hot in there -- and then  
14 you will aerosol this protein-concentrated liquid into that air  
15 space, and it flashes the water out of it. The powder falls to  
16 the bottom of the box dryer, it's swept out one end and  
17 conveyed and then bagged into a powder. So now it's in a dry  
18 form. The water went up the chimney that was flashed out of  
19 it.

20 Now, we have taken most of the water out of the whey by  
21 the time it gets to that point anyway, because we end up with  
22 better than 50,000 gallons of water out of that process  
23 everyday, of polished water.

24 JUDGE CLIFTON: All right. And do you have any other  
25 wisdom to impart as to how a regulator might value these milk

1 solids?

2 MR. HOFFERBER: Well, honestly, between the COS and the  
3 FMMO, I don't think we're particularly nervous about either  
4 construct, whether you have a protein component, or fat, or  
5 SNF, I mean, the construct of it isn't what's our big issue  
6 here. Our big issue here is that you set that minimum price  
7 and force me to pay it when it's not, to use Mr. Shippelhoute's  
8 word, worth it. You know, the market has to find that value,  
9 not the regulators, the regulated system. That's the bottom  
10 line to nearly everything that we testify to at these hearings,  
11 "we" being Farmdale.

12 JUDGE CLIFTON: Are you saying there should not be any  
13 minimum regulated price for milk?

14 MR. HOFFERBER: It should be, in our opinion, set at a  
15 minimum value that would allow the market to differentiate  
16 between the end product in the whey stream, at least. I mean,  
17 it might even be better to have it differentiate between the  
18 end-product between cheddar and Mozzarella, since Mozzarella is  
19 now dominating the overall -- I'm stepping on some of my  
20 cheese-making brothers' toes here -- but the point being --  
21 okay. Let me step way back. Now I'm on my soap box and Chip's  
22 going to hate this.

23 We have to go vertical in this business. We have to  
24 find the dairy farmers that want to make the product that we  
25 are making and we team up vertically. And we stop worrying

1 about what every other dairy farmer is doing in the state  
2 inside the pool, and we just go do business. And the co-ops  
3 are kind of doing that by building powder plants. I mean, this  
4 verticality idea has been around for a long time, but it's not  
5 working because the expertises don't line up.

6           You have had, DFA's Golden plant couldn't hang. You  
7 know, there are example after example through the California  
8 system, I don't know about Federal so, but in the California  
9 side, you know, co-ops seem to be doing okay by making this  
10 powder. By CDI making powder plants now, we're no longer a  
11 balancing plant for them. Their balancing plant is this  
12 lower-value powder thing. These dynamics here are missing the  
13 point, in our opinion.

14           Our -- my advocacy to my owners over the last five  
15 years or something, I says, "we have got to find 25,000 cows  
16 and we have got to make friends with them." And we need to be  
17 able to do that apart from a regulated system that keeps us  
18 from doing that deal.

19           So if you set, "you", set the minimum regulated price  
20 low enough, that's going to give us space to do that. And if  
21 my WPC-80 powder is worth a ton, my guys are going to benefit.  
22 And if goes in the tank, we're all going to suffer together.

23           And, okay. So in the '30's when we started all this  
24 mess, there were 17,000 dairy farms in California and 625  
25 processors. We're down to 1450 farms and 125 processors. Why

1 can't we just sit down around a table and do this vertical  
2 idea? Okay. End of soapbox. I'm sorry. I have been sitting  
3 on that all day.

4 JUDGE CLIFTON: We need to hear it. I mean, if you don't  
5 have a vision, how do you write the rules?

6 MR. HOFFERBER: Well, I mean, that's been my vision for  
7 quite awhile. Coming from the outside and watching it unfold  
8 before me, and migrate the way it is migrating, I came to one  
9 of two conclusions. There was one hearing when I went up to  
10 Kevin Mazahara, who was the Deputy Director, or the Deputy  
11 Secretary, or I don't know, the head of milk pooling he was the  
12 third in charge of Milk Pooling in CDFA. I said, "Kevin, the  
13 only way out for this is for you guys to buy all the cows and  
14 the State runs the whole thing, top to bottom." That's the  
15 only way we are going to eliminate having a hearing every two  
16 years. Because we are going to keep, me and Rob are going to  
17 keep butting heads at these things -- Rob Vandenheuvel,  
18 V-A-N-D-E-N-H-E-U-V-E-L. Okay.

19 No, I mean, we, this carousel just keeps going around  
20 and around. Guys we got to break out of this. This has got to  
21 become something very different. And we're trying to shove it  
22 into another, you know, intelligent box. I mean, it's, but  
23 it's -- it's just become like Tax Code. It's so freaking  
24 complicated now. How do we -- how do we get past this? And,  
25 you know, maybe it's a complete collapse of the whole system

1 and we all, you know, rise from the ashes, or we step in now  
2 when we have an opportunity here and do something innovative,  
3 for the lack of a better word. Okay. I'm done with that. You  
4 sense I could go on for hours, but I won't.

5 JUDGE CLIFTON: Well, I appreciate very much everything you  
6 have had to offer here. And Mr. Vandenheuvel, would you like  
7 to be the next to ask questions of this witness?

8 MR. VANDENHEUVEL: I'm okay.

9 JUDGE CLIFTON: Ms. Hancock?

10 CROSS-EXAMINATION

11 BY MS. HANCOCK:

12 Q. Nicole Hancock.

13 You had been talking with the Judge, you had mentioned  
14 on the sales-below-cost prohibitions, that there's a mechanism  
15 for you to make reports to CDFA if you, if you think that  
16 something like that has occurred.

17 A. Yes.

18 Q. Have you ever made any reports to CDFA?

19 A. I believe that one of our owners did do that about, I'm  
20 thinking eight years ago, something like that. It's outside my  
21 recollection at this point in terms of any specifics.

22 Q. Do you know what, who it was that they were reporting?

23 A. I don't recall.

24 Q. Do you know if it was related to the California  
25 Producer Handlers Association?



1 A. I do not recall.

2 Q. Have you, yourself, ever made any kind of report?

3 A. No.

4 Q. Do you -- well, that's good. Thank you.

5 JUDGE CLIFTON: Mr. Miltner?

6 CROSS-EXAMINATION

7 BY MR. MILTNER:

8 Q. Mr. Hofferber, my name is Ryan Miltner, I represent  
9 Select Milk Producers.

10 A. Hello.

11 Q. I know you have heard this a couple of times already, I  
12 want to thank you for your frank and thorough testimony. It's  
13 been a joy to listen to.

14 A. Thank you.

15 Q. My question --

16 A. But?

17 Q. No, there's no but.

18 A. But I have a question.

19 Q. I do have some questions.

20 A. Sure.

21 Q. And I think they are all related to this concept of  
22 disorderly marketing, that, quite frankly, everybody in this  
23 room is trying to put some details to. And you have put a lot  
24 of time into the industry as a whole and working with CDFA.  
25 And is it correct for me to summarize your testimony as saying

1 that, as long as there's sufficient Class 1 milk, there is no  
2 disorderly marketing?

3 A. That's my understanding of the technical definition of  
4 disorderly marketing within the Stab Plan.

5 Q. Okay. So that's specifically your understanding for a  
6 California definition of disorderly marketing?

7 A. Correct. I only have the COS experience.

8 Q. Okay. And I suppose you are also advocating that USDA  
9 apply that same definition to the situation today?

10 A. Yes.

11 Q. And my background is in the Federal system, obviously,  
12 I only know enough about California perhaps to be dangerous.  
13 So when California, when CDFA has a hearing to modify a formula  
14 or any other aspect of the Stab Plan, are they required to  
15 determine that there are disorderly marketing conditions in  
16 terms of --

17 A. In terms of whether or not to hold a hearing?

18 Q. Whether or not to change the terms, to change the  
19 formula?

20 A. I don't think so. I think the way the Stab Plan is set  
21 up is that we can have hearings to discuss all sorts of  
22 elements of that plan, whether or not it's, it creates  
23 disorderly marketing in the technical sense.

24 Q. So your understanding is that California, that CDFA can  
25 modify the terms of their Marketing Order without there being

1 disorderly marketing conditions?

2 A. We do regularly with make allowance changes and formula  
3 changes to the milk prices based on economic conditions  
4 surrounding in the state, sure.

5 Q. Let me throw out a concept and see if you agree with  
6 this. Is it, would it be accurate to say that there is, that  
7 order in terms of milk marketing is a continuum? That there's  
8 perfect order, and there's disorder, and there's a bunch of  
9 states in between?

10 A. The dance we're doing here is around a technical  
11 definition of the word "disorderly marketing". I will say, as  
12 I did I in my testimony, there are some decisions in these  
13 hearings that cause prosperity and there's some decisions in  
14 these hearings that cause real distress to my company.  
15 Business happens. And so that's why it's my understanding that  
16 this definition of disorderly marketing is somewhat critical to  
17 this hearing process, as to whether the USDA even gets involved  
18 in it. So where something would distress my company, I could  
19 say "gosh, this is really disorderly," you know. But we don't  
20 use that technical term. We say, "Well, this is a bad thing  
21 for my business. What am I going to do now to go mitigate  
22 that, you know, within my business model?" Or, "This is going  
23 to be really good for us for a little while, how can we pay our  
24 debt off faster?" Or however that particular hearing goes.

25 Q. I guess to kind of to relate back to your testimony a

1 few minutes ago, the issue becomes how do we make things, how  
2 do we come together as an industry to make, to improve upon  
3 everything, even if we haven't reached that point of market  
4 disorder? Is that accurate?

5 A. Sure. That's fine.

6 Q. And so when California, I guess going back to my  
7 initial jumping off point, when California decides to modify  
8 their Order, I guess they are looking at some sort of  
9 incremental improvement upon the terms of regulation after they  
10 have weighed all the positives and negatives to both producers  
11 and processors?

12 A. One man's ceiling is another man's floor. Improvement  
13 might be good for one person, it might not be an improvement  
14 for the person on the other side of the equation.

15 Q. I think that's all I have. Thank you, your Honor.

16 JUDGE CLIFTON: I think I'll start with Mr. Vetne.

17 CROSS-EXAMINATION

18 BY MR. VETNE:

19 Q. John Vetne for Hilmar Cheese. This is going to be  
20 quick.

21 A. Sure.

22 Q. As I understand your testimony, your characterization  
23 of the CDFA process, or your expectation for that process, is  
24 that CDFA will address an issue that appears to be creating  
25 distress, or looks like it might produce distress in the near

1 future, so let's deal with it before distress turns to  
2 disorder. Correct?

3 A. Yes.

4 Q. Okay. If --

5 A. I was great with that question until you stuck the word  
6 disorder on the end of it.

7 Q. Let's deal with it before it becomes great distress.

8 A. Okay.

9 Q. And if we can -- you used the term at the beginning of  
10 Nicole Hancock's questions, you used OEM. I have no idea what  
11 that means.

12 A. OEM is an acronym for Original Equipment Manufacturer.  
13 Now, I use that fairly loosely because I don't think we would  
14 characterize cheese or sour cream as equipment. But as a  
15 manufacturer we would be considered an OEM when you are  
16 discussing things of manufactured ilk.

17 Q. Okay. And then you used the word which I regret hasn't  
18 been brought up before, and I should have anticipated it. You  
19 used the word caseinates in milk. A component of milk. Is it  
20 correct to say that caseinates are a subset of the proteins  
21 contained in milk?

22 A. I am not a biochemist or whatever that person would  
23 need to be to know how that breaks down. It is just a phrase I  
24 know is a component in milk. If it is part of proteins, so be  
25 it, I don't know.

1 Q. All right. Then, I, since you don't know, we'll deal  
2 with that later. Thank you.

3 A. I am aware that it becomes part of the cheese. I mean,  
4 it is part of the binding of the cheese and some, I mean, my  
5 depth in that whole, at the molecular level is limited.

6 Q. Well, my questions were going to lead to casein is a  
7 subcomponent of the proteins, which creates the matrix, the  
8 structure, and binds to the fat to create the functional value  
9 of cheese. And non-casein proteins are generally what is  
10 extracted.

11 A. In the whey stream.

12 Q. In the whey stream.

13 A. We're all here to learn.

14 Q. Okay. Thank you.

15 A. Thank you.

16 JUDGE CLIFTON: Mr. Beshore?

17 CROSS-EXAMINATION

18 BY MR. BESHORE:

19 Q. Thank you. Marvin Beshore.

20 I want to get down on the ground a little bit more, not  
21 in the concept level. WPC-80, are you aware of any publicly  
22 available sources of price information for that market?

23 A. No.

24 Q. So when you were, when you were determining whether to  
25 invest millions of dollars I assume, some millions of

1 dollars --

2 A. Yes.

3 Q. How did you -- how did you price -- how did you, you  
4 know, how did you come to assumptions about your revenue  
5 stream?

6 A. We had hired a consultant to help us develop and design  
7 the project, who is also a marketer of the project and he  
8 brought us his historical information over some relevant range  
9 of history.

10 Q. A marketer of the product?

11 A. That's correct. And we did some projections off of  
12 that, and said, you know, it's only going to get as bad as this  
13 and we're going to be okay, and of course it's gotten a lot  
14 worse than that.

15 Q. Are you aware of any publicly available information  
16 about what it cost to turn whey into WPC-80?

17 A. I am not.

18 Q. Can you tell us what yield in cheese you experience at  
19 Farmdale, pounds per hundredweight?

20 A. Yeah, this starts falling into proprietary stuff, and I  
21 don't want to dance the question. So what I do is refer you  
22 back to, I think I had an earlier question about where to go to  
23 find that information, and I believe the CDFA cost studies with  
24 respect to the make allowances carry some of those data for you  
25 as to what's going on in California about that.

1 Q. Okay. So the yields in the study information would be  
2 representative, in your view?

3 A. Right. In their audit they specifically ask me those  
4 questions, what are your production yields, and they include  
5 them in their conclusions when they publish the generalized  
6 study that doesn't identify all of us individually.

7 Q. Okay. So one final area. When you determine a price  
8 for the product at your dock for your cheddar, how do you go  
9 about, without telling me what the price is, how do you go  
10 about determining what price to put on that product?

11 A. Sure. Well, of course, the general sales rule is, you  
12 get what the market can bear, right? So the way cheddar is  
13 priced, certainly in Southern California, and I think  
14 everywhere, is that we use the CME market price for 40 pound  
15 block cheddar cheese. There is a market for it, treaded on the  
16 exchange at the CME. CME is Chicago Mercantile Exchange, by  
17 the way. And we price that with our customers at a plus or  
18 minus penny per pound from the dollars and cents per pound  
19 number coming off the CME. And that CME number is updated once  
20 a week in terms of a weekly, we use the weekly average number.  
21 And so come noon on Friday we know what the number is going to  
22 be for the following week. And we, and this is almost probably  
23 somewhat proprietary to us, because I don't think everybody  
24 also does this. Some people will price their cheese on the day  
25 of make, we price it on the day of delivery. So we waited for



1 the CME study to come out -- traditionally, that's how  
2 everybody did it, but as the markets change and people want to  
3 get a jump on pricing and whatever. Whatever internal reason  
4 they have. But internally for us, it's a plus or minus the  
5 CME.

6 Q. And does the bulk of your cheese is sold in less than  
7 truck load quantities, I take it from what you said, what you  
8 have testified?

9 A. The bulk, you know, I really don't know where to place  
10 it. I guess let's call it 50/50 we'll do a full truck load and  
11 partial truck loads. And I don't mean 50/50 on deliveries, I  
12 mean 50/50 on the total volume of cheese. So we'll have X  
13 number of full truck load deliveries, and 3X number of partial  
14 truck load deliveries to get the same total value of cheese.  
15 That's my guess. It is kind of a like a thumbnail thing.

16 Q. Do you -- do you read Dairy Market News? Do you follow  
17 it?

18 A. Occasionally, mostly when articles are in there about  
19 the whey factor.

20 Q. In Dairy Market News?

21 A. Well, I'm thinking about Cheese Reporter. In Dairy  
22 Market News, actually we go to their website and look up survey  
23 information.

24 Q. And they publish, do you compare your, reference your  
25 pricing to prices that are, that are reported in Dairy Market

1 News? Product prices?

2 A. Are you talking about for cheese?

3 Q. Yes.

4 A. Yeah, but I think we can go to the CME directly and get  
5 the numbers we're looking for.

6 Q. Well, there are other numbers besides CME numbers that  
7 are in Dairy Market News.

8 A. We're strictly tied to CME with our customer base.

9 Q. Okay. So you wouldn't, for instance, there's a 40  
10 pound block, California, you know, Western 40 pound block  
11 survey reported there. Do you -- how to your prices compare to  
12 that, if you know?

13 A. I don't know. My company President does those sorts of  
14 analyses and works with the sales team on their own internal  
15 strategies. If a customer comes at us and asks us, what's the  
16 what compared to this particular survey? You know, we will --  
17 we will educate them on the delays in the numbers, and how all  
18 of that comes together and creates these disparities, and we  
19 just try to stay consistent within our own business model.

20 Q. Have you ever looked at your prices in terms of  
21 out-of-state competitors plus transportation in?

22 A. We look at it when a customer says I can get it cheaper  
23 from that out-of-state supplier.

24 Q. But in terms of what the market will bear?

25 A. I do not believe we have done any kind of prospective

1 study of that. It is all reactive for us.

2 Q. Okay. But that would be one way of looking at what the  
3 market might bear?

4 A. Oh, definitely. Yeah.

5 Q. For instance, out-of-state competitors that have  
6 Federal Order prices plus transportation to get into  
7 Southern California.

8 A. If we were to run into one of those in our customer  
9 base, then we would have to look at our overage, or over or  
10 under the CME number and see if we could afford to do it. If  
11 that happens then you will go find another customer that will,  
12 you know, we may have to split that load down into two smaller  
13 loads in order to get the right price out of the cheese. There  
14 is volume considerations in our pricing. If you take a full  
15 truck load, you are going to get a little different  
16 differential than you would if you took one pallet at a time.

17 Q. But I guess my, wouldn't the out-of-state plus,  
18 out-of-state manufactured at Federal Order price, plus  
19 transportation in tend to be at a higher price than you would  
20 be?

21 A. I -- I wouldn't have any knowledge of that.

22 Q. Okay. One final question. Do you know or has your  
23 company ever evaluated whether California is a cheddar surplus  
24 or deficit market? For cheddar cheese, do you know?

25 A. To my knowledge, we do not, we have not studied that

1 internally. I think CDFA and probably even Dairy Institute  
2 would have this data.

3 Q. Okay. What do you think it is?

4 A. I think we're probably a net exporter from cheddar.

5 Q. Of cheddar?

6 A. I think so.

7 Q. Okay. Thank you.

8 JUDGE CLIFTON: Mr. Hofferber, when Mr. Beshore was asking  
9 you about the Dairy Market News survey information, you started  
10 to mention some other source of information that started with  
11 the word cheese?

12 MR. HOFFERBER: Yes, there's a publication called The  
13 Cheese Reporter, and I believe that comes out of Wisconsin.  
14 But that's a regular circular around our office between me and  
15 the President and a couple of the other owners, keep an eye on  
16 that.

17 JUDGE CLIFTON: Thank you. Who next has questions for  
18 Mr. Hofferber? Mr. Vlahos?

19 CROSS-EXAMINATION

20 BY MR. VLAHOS:

21 Q. John Vlahos, good afternoon.

22 A. Good afternoon almost, is it?

23 Q. It is, yeah. I just, I was going to say good morning  
24 but then it lasted longer, so good afternoon.

25 A. Thank you.

1 Q. I would have just a few questions for clarification of  
2 some of your testimony. And if it over the course of asking  
3 those questions, I have either misunderstood, mischaracterized,  
4 mistranslated what I thought the testimony was, please correct  
5 me because I want to get it right.

6 I believe you testified that it was your belief that  
7 the technical definition of disorderly marketing is only when  
8 Class 1 is not being adequately supplied; is that correct?

9 A. Yes.

10 Q. Have you ever seen that technical definition in any  
11 statute, Federal or State?

12 A. No.

13 Q. Have you ever seen it in any regulation, either Federal  
14 or State?

15 A. No.

16 Q. What is your source for that your belief about the  
17 technical definition?

18 A. Multiple communications surrounding the preparation for  
19 this hearing, actual discussions in previous testimony in this  
20 hearing that I have heard listening in on the website, it's  
21 been discussed in that context a couple of times, as I recall.

22 Q. You said part of it is based on discussions with people  
23 during this hearing?

24 A. In preparation for the hearing. Leading up to.

25 Q. With whom would that be?

1 MR. ENGLISH: Excuse me, do not respond to the extent that  
2 any discussions were with counsel.

3 MR. VLAHOS: Are you representing Mr. Hofferber?

4 MR. ENGLISH: I represent the Dairy Institute of California  
5 and he is testifying on their behalf.

6 MR. VLAHOS: That doesn't make him your client.

7 MR. ENGLISH: My instruction remains and it is improper to  
8 overrule it.

9 MR. VLAHOS: Well, I think that, I think the Judge is the  
10 one who determines that.

11 JUDGE CLIFTON: You know, I realize that this witness is  
12 here on behalf of Farmdale, but I do not believe we are here to  
13 intrude upon the discussions with counsel, regardless of  
14 whether they are a direct client in the traditional sense.

15 MR. VLAHOS: Okay. I'll accept that, your Honor.

16 JUDGE CLIFTON: Thank you, Mr. Vlahos.

17 BY MR. VLAHOS:

18 Q. Any other source for your belief about the technical  
19 definition?

20 A. No.

21 Q. Now, you have also --

22 JUDGE CLIFTON: Now, wait, I don't quite understand your  
23 question. Your question, Mr. Vlahos, is, other than counsel,  
24 have you had any discussions with anyone else? Is that what  
25 you are saying?

1 MR. VLAHOS: No, no, no, no, I want to know if there's any  
2 other source, other than what he's testified to, for his belief  
3 as to what the technical definition of disorderly marketing is.  
4 I'm just trying to find out all the sources, your Honor.

5 MR. HOFFERBER: I understand. The primary source has been  
6 this hearing record itself actually, and prior discussions in  
7 testimony.

8 MR. VLAHOS: Thank you very much, that clarifies it for me.

9 MR. HOFFERBER: Thank you.

10 BY MR. VLAHOS:

11 Q. You also indicated that, in your testimony, that you  
12 support the Proposal Number 2 made by the Dairy Institute; is  
13 that correct?

14 A. That's correct.

15 Q. And you have also testified that you do not believe, if  
16 I got this correctly, that you do not believe that in any  
17 potential Federal Milk Marketing Order in California, that  
18 quota ought to be preserved?

19 A. That's correct.

20 Q. And is that one of the reasons you support the Dairy  
21 Institute's proposal?

22 A. I'm -- I do not believe the Dairy Institute proposal  
23 specifically talks about excluding quota. The exclusion of  
24 quota goes back to what I said during my Q and A, I think, in  
25 my original testimony. And that is, I see quota as an

1 incentive to set up the pool in the first place. In business,  
2 when we try to incent something, we typically put a sunset on  
3 it. I'm going to incent you to do this, and after X amount of  
4 time, this incentive would expire. And what is unfortunate, in  
5 my view, about quota is, that it's turned into a forever  
6 intangible asset. And I think it would have been much more  
7 productive to have it had sunset after 10 or 20 years or  
8 something. We can get into the whole big economic discussion  
9 about that, but again, it's an opinion and a view of mine that  
10 if you are going to incent somebody to do something, if you  
11 make it a forever incentive, it becomes an entitlement or it  
12 becomes this whole asset thing that it's turned into, and now  
13 another point of disharmony among this extended now, producer  
14 community, the have's and have not discussion.

15 Q. Have you done any analysis of the Dairy Institute  
16 proposal as to its potential effect upon the preservation of  
17 quota?

18 A. No.

19 Q. Okay. Thank you. That's all I have.

20 JUDGE CLIFTON: Who next has questions for Mr. Hofferber?  
21 Mr. Francis, would you prefer to go before or after redirect?

22 MR. FRANCIS: Will Francis, USDA. No preference. We can  
23 do either way.

24 JUDGE CLIFTON: All right. Then, why don't you ask your  
25 questions now.



1 CROSS-EXAMINATION

2 BY MR. FRANCIS:

3 Q. Just a couple things to clarify. I am still confused  
4 about your operation relative to whey. You mentioned you made  
5 a significant investment, you produce WPC-80, and later on in  
6 response to some questions you referred to dry whey. What --  
7 what products are you currently producing? Are you producing  
8 WPC-80 in a liquid form or does it get further dried?

9 A. No, we are producing WPC-80 dried powder for human  
10 consumption, and that's been our sole whey product since  
11 August of 2013.

12 Q. So no liquid form of whey comes out of your facility?

13 A. Yes. No whey comes out of our facility.

14 Q. Okay. Thank you.

15 A. Liquid whey comes out of our facility.

16 Q. And then just a quick follow up on sales below cost.  
17 We're not that familiar with the California program, but at  
18 what level of marketing does that prohibition apply to? So  
19 it's you as a manufacturer of a finished product, selling to a  
20 customer?

21 A. It gets measured at, well, it gets discovered at the  
22 customer level. It gets reported by me, if I discover it.  
23 Right? Now, the out is, the out for the person who is selling  
24 it at that low price, is if you can find other retail outlets  
25 to show that that really is the street market value of the

1 product, you escape any enforcement. Even though my  
2 inefficiencies may drive my cost higher than you, that's just  
3 too bad for me. Does --

4 Q. I'm still confused. So somebody for, let's talk about  
5 a pound of cheese, a pound of cheese. So a retailer who is  
6 selling a pound of cheese for 99 cents --

7 A. We would go ask him -- we would, actually what we do is  
8 go look at the plant number on that cheese and say, okay, now  
9 how is that plant putting anything out of their plant that  
10 could arrive at the retail level at this price, and that would  
11 trigger the question.

12 Q. Okay.

13 A. Because there ain't no way, in our opinion, with the  
14 regulated price at the level that it was at at the timeframe  
15 that that cheese would have been made, they could have done it.

16 Q. And when that's reported to CDFA, you indicated CDFA  
17 would do an investigation and they would go to the source plant  
18 who offered that cheese for sale to the retail customer?

19 A. And investigate.

20 Q. Okay. And do you know if they go back to look at the  
21 raw milk cost going into those facilities?

22 A. Once it is in their hands, I do not know what their  
23 process is. And it is, like I said before, it's actually been  
24 attempted so few times, I'm not really even sure if there's  
25 much of a body of knowledge. It's more of a concept that's out

1 there, that's an attempt to keep us all at a level playing  
2 field, and I'm more concerned about things that will disturb  
3 that level playing field.

4 Q. Okay. And separate but sort of related to selling  
5 below cost, would you describe the current California system  
6 where they establish minimum prices for Grade A milk, you, as a  
7 purchaser of that milk, cannot buy that milk for less than that  
8 minimum regulated price?

9 A. That's correct.

10 Q. So would that be sort of like a sales-below-cost  
11 prohibition, that the seller cannot offer it to you for a lower  
12 than that minimum price?

13 A. Well, you would think that that would be the low and  
14 limiting number to the whole thing, if we're all paying the  
15 same minimum regulated price. And that actually is the trigger  
16 point. That's how you would have to boil that analysis out to  
17 determine if they were going, you know, they are basically  
18 taking their own capital and subsidizing that product into the  
19 market at a price that just is intended to take me out of the  
20 competition.

21 Q. Okay. And in your operation, would you have the  
22 ability to purchase Grade B milk?

23 A. Yes.

24 Q. Okay. And that would not be subject to the price,  
25 minimum price regulation under the current California program?

1 A. That's correct.

2 Q. And I had another question about the source of, you  
3 mentioned in your testimony that the Stabilization Plan is  
4 where the sales-below-cost regulation --

5 A. Well, in my definition of the Stab Plan at the  
6 beginning of my testimony, it was expansive. It just wasn't  
7 inside the actual stabilization market, but it includes all  
8 surrounding --

9 Q. Other regulations?

10 A. -- I just call the whole pile of the Stab plan.

11 Q. Okay.

12 A. I would like to amplify, if you don't mind, your  
13 question about Grade B milk. That isn't done as a rule because  
14 a couple of bad things happen, one, to the producer, in that it  
15 goofs them up with the pooling system if they go Grade B; and  
16 the second thing is, I have got to explain to my customer now,  
17 why I'm using Grade B milk in their product. So that  
18 disruption also is a fairly good deterrent from going down that  
19 path. I know testimony in this hearing will bring that up. We  
20 have always had the ability to escape the minimum regulation,  
21 go do Grade B. Well, yeah, you can technically, but it's --  
22 it's very disruptive to both parties.

23 Q. Thank you for the clarification.

24 A. You're welcome.

25 Q. In response to some questions you talked about your

1 location, your physical location, being close to consumers and  
2 that the transportation. Are there other handlers nearby that  
3 you compete with to bring milk into your plant?

4 A. Yes.

5 Q. And are there other cheese plants or other sour cream,  
6 buttermilk?

7 A. All classes.

8 Q. And who are your primary competitors? Are they fluid  
9 plants or manufacturing plants?

10 A. If by fluid plant you mean Class 1, we do not compete  
11 in Class 1 at all, so it is all manufacturing level products.

12 Q. But to compete for the raw milk that comes into your  
13 facility, if there are nearby Class 1 plants, they are also  
14 competing to bring milk into their facility?

15 A. And they will get first strike at the milk.

16 Q. And why, in your words, why would they get first strike  
17 at the milk?

18 A. In theory, and in mostly in practice, they receive the  
19 highest value for the milk going into a Class 1 product back to  
20 the producer community.

21 Q. Okay.

22 A. That's the nature of the beast.

23 Q. Okay. Thank you. One last question. On page 6, in  
24 the, toward the end of that first paragraph, you say, "as an  
25 aside, we expect that this responsiveness by the California

1 Order system will be lost with an FMMO." Can you elaborate on  
2 what you mean by that statement?

3 A. Sure. Here's a hearing in 2001; here's a hearing in  
4 2003; here's a hearing in 2005; here's a hearing in 2006,  
5 here's a hearing -- I mean, FMMO -- FMMO, by design, is not  
6 going to respond like that. We're going to -- it is clearly a  
7 protracted process compared to what we are able to do in  
8 California.

9 Now, in some times, if I'm going to my banker when I'm  
10 trying to lay out a ten-year plan on a whey plant and say,  
11 "These numbers are really good today, but we're having a  
12 hearing in six months that could goof this up pretty  
13 seriously," that's a dance I get to do. And when we have  
14 argued a number of times for some of these hearings, "please  
15 don't have this hearing, we just had this hearing a year ago."  
16 So there's give and take in all of that.

17 I think ultimately, with the sensitivities that we  
18 have, and what we call beta, B-E-T-A, in economics the  
19 volatility in pricing, and even electricity costs and  
20 everything else -- this thing just wants the feedback, it's  
21 just a notch too loud. It's the way it is. I also work with  
22 PA systems on a regular basis.

23 JUDGE CLIFTON: Is that your theatrical segment of the  
24 business?

25 MR. HOFFERBER: Yes, I'm the CFO and resident bass player

1 for the, for Farmdale.

2 MR. FRANCIS: That's all the questions we have. Thank you  
3 very much for your testimony.

4 JUDGE CLIFTON: I want to go back to Mr. Beshore's  
5 question. We have got lots more questions, but his question  
6 where he asked if there were publicly available cost and price  
7 data on this product, this 80 product.

8 MR. HOFFERBER: Uh-huh.

9 JUDGE CLIFTON: Since there aren't on that, what are there  
10 available --

11 MR. HOFFERBER: Yes.

12 JUDGE CLIFTON: -- published prices that relate to whey in  
13 some form?

14 MR. HOFFERBER: Okay. So the direct answer to your  
15 question is, I'm aware of two studies; there's a dry whey study  
16 and there's a WPC-34 study, that puts a price for some form of  
17 whey out into the public. But what you, what you observe and  
18 understand if you watch these markets, is they don't move  
19 together. They are really different markets for these  
20 different potential indexed products or products with which we  
21 would tie the whey to. So then I would go back to my previous  
22 discussion about, we really got to get to a place where the  
23 minimum price is minimum, and for the individual kinds of whey  
24 that are being made, we figure out how to revenue share that  
25 part of it. Because they are just so dramatically different.

1 I mean, the dry way number can be doing this, and the 80 number  
2 is in the tank right now because Russia stopped buying, and  
3 China did this, and because they are living in the 80 world,  
4 not really living in the dry whey world. So it is very  
5 difficult to pick a competent index considering how varied the  
6 whey processing complex is.

7 JUDGE CLIFTON: Now, when you just used the term dry whey,  
8 I presume that's not a concentrated protein product.

9 MR. HOFFERBER: It is, but it's -- it's not as -- it's not  
10 80 percent. I don't know what the percent of protein in dry  
11 whey is. Capital dry, capital whey, is a surveyed product of  
12 its own. I'm not even sure how it's made. We used to do, like  
13 I said, with our RDW, we were roller drying the whey, we would  
14 concentrate the whey stream in an RO up to about 20 percent  
15 solids, 19 percent solids from 6. When it comes off the cheese  
16 line, there's 6 percent solids in that the 90 pound blob of  
17 whey. Okay? So we would run that through an RO, drive it up  
18 to about 19 percent or so, and then we would just drip it on a  
19 steam-heated roller and cook it into popcorn-looking stuff. We  
20 would bag that up and ship it to the Midwest as an ingredient  
21 for animal feed.

22 Well, it's certainly not human grade, and if you saw  
23 the process, you would be happy you weren't consuming any of  
24 it. But now we have gone all indoors, and all stainless  
25 everything and, you know, it's all nice and pretty and



1 expensive, and all of those good things, and we now make a  
2 powder that is just a very fine talcum powder almost  
3 consistency stuff. It is very, very fine powder that we make  
4 now.

5 JUDGE CLIFTON: So what was it called when it was dripped  
6 onto the roller?

7 MR. HOFFERBER: RDW, roller dried whey. And I give that  
8 lengthy definition at the front of my testimony. I use the  
9 popcorn phrase in there, too.

10 JUDGE CLIFTON: Would that be the least expensive to make  
11 form of whey?

12 MR. HOFFERBER: Probably not. I mean, I think, who knows?  
13 I mean, before we did roller dried whey, we were concentrating  
14 it and putting it back in a tanker and shipping it out as  
15 animal feed in the liquid form. We did that for awhile. You  
16 know, way back when we started, I think we were putting it back  
17 in a tanker and sending it back just as raw whey back as animal  
18 feed, back to pig farmers and cow farmers and what not, as a  
19 protein lactose source, without concentrating it. And then we  
20 started concentrating that, because that makes the shipping  
21 more efficient, right? Because you are shipping, instead of 6  
22 percent stuff in a blob of water, you are shipping 20 percent  
23 stuff in a blob of water.

24 JUDGE CLIFTON: What did you call it when it was still 6  
25 percent stuff?

1 MR. HOFFERBER: That's pretty much raw whey, the raw whey  
2 stream. And you may hear people talk about that. There's  
3 certain advocates that say the only baseline value in the whey  
4 stream is really at that raw, at that raw level. Everything  
5 else is value-added, added by cheese makers. Simple.

6 JUDGE CLIFTON: Not so simple. Not so simple. So when  
7 these markets don't stay aligned with one another, in other  
8 words, sometimes one of the whey products is more valuable than  
9 another, do you have any incite for us on that?

10 MR. HOFFERBER: Again, my only incite would be, you would  
11 either have to come up with as many different adders for the  
12 whey stream as there are whey streams, or retreat back to a  
13 minimum price that leaves a ton of space for us to work it out  
14 with our supplier as to tying it to a market that we actually  
15 make, because the disparity is huge. This whole example I gave  
16 of 2007, where -- where the dry, the true dry whey price just  
17 took off and we were paying for that dry whey price when we  
18 were making the RDW and getting, as our price we were getting  
19 80 percent of the western mostly and we were paying for the  
20 freight on the product. So when dry whey is up here, we're  
21 getting a better price for it, that's why I made a million 380  
22 or whatever, in that final year. I made a bunch of money  
23 selling that. But if I had moved the cost of it in the milk  
24 over against that number, and then blended it back in my  
25 cheese, I ended up losing \$347,000 in those eight months

1 leading up to that shutdown.

2 JUDGE CLIFTON: That's another question I had. When you  
3 gave us the figures that showed either loss or profit, you used  
4 different time periods. One of them was 8 months, one of them  
5 was 18 months.

6 MR. HOFFERBER: Right.

7 JUDGE CLIFTON: But why did you pick the time period you  
8 picked?

9 MR. HOFFERBER: Okay. The 18-month RDW period was picked  
10 as part of my testimony last June, and I left those numbers  
11 alone so I didn't re-analyze them. The fact that I reduced  
12 those numbers to a loss per pound of cheese kind of makes the  
13 time period a little less impactful on the numbers. I didn't  
14 leave anything out because it -- it distorted the number and  
15 made it any more or less representative of my point.

16 My point was more that, in the 18-month window in the  
17 RDW we lost a penny and a quarter, I'm trying to remember the  
18 numbers without looking at them, and in the last six months we  
19 lost two and a half cents. So, you know, as that variable whey  
20 factor that got re-introduced started taking off again, it was  
21 blowing up on us. And then my numbers for the WPC-80 plant,  
22 where I picked 25 months, I picked that because it is the  
23 entire operational window of the WPC-80 plant through the most  
24 completed numbers I had, which were August 31, 2015. And then  
25 I just picked the last 8 months because that pretty much

1 represents the timeframe when the whey market has, the WPC-80  
2 market has just bottomed out.

3 So the only manipulation of the timeframe was for  
4 expediency and developing the numbers, and to show the  
5 degradation of the profitability of both of those methodologies  
6 in those relative timeframes.

7 JUDGE CLIFTON: Now, I'm going to ask for other questions  
8 before the redirect. Who has other questions before the  
9 redirect? Mr. Vetne?

10 CROSS-EXAMINATION

11 BY MR. VETNE:

12 Q. Thank you. You just referred to a hearing last June.  
13 Was that the hearing called by CDFA, by the State Secretary of  
14 Agriculture on her own motion that was held last June?

15 A. Yes.

16 Q. Okay. So you used some of these same analyses in the  
17 course of that hearing?

18 A. Yes.

19 Q. Okay. You referred to market bottoming out. I think  
20 you refer to Russia and China; is that correct?

21 A. Yes.

22 Q. Did I hear correctly? And that's an international  
23 market for the WPC-80 product?

24 A. Yes.

25 Q. Okay. Does your product get into the export markets,

1 your WPC-80?

2 A. We do not sell it directly to an export market, but  
3 some of the people that we are selling it to inform us that it  
4 is getting there. Does that make sense?

5 Q. Yes, it does. So your buyers of WPC-80 in bulk, in  
6 turn, remarket that, in part, into the export market?

7 A. That's correct.

8 Q. And then finally, you had some, an exchange with  
9 Will Francis about your opportunity to use Grade B milk. I  
10 wanted to take that a little step further.

11 A. Sure.

12 Q. You can use either Grade B or Grade A milk to make  
13 cheddar cheese, correct?

14 A. Yes.

15 Q. Okay. And that could be marketed throughout the  
16 United States?

17 A. Yes, with the disclosure that you are using Grade B  
18 milk.

19 Q. Okay. But you also make some products other than  
20 cheddar cheese. Your buttermilk, for example, you must use  
21 Grade A milk to make buttermilk, correct?

22 A. Yes.

23 Q. What about sour cream?

24 A. Grade A only.

25 Q. Grade A only. So in order to make cheddar cheese out

1 of Grade B milk, you would have to have either separate silos  
2 or separate processing days for receipt of Grade B milk to make  
3 cheese, and another day to make sour cream and buttermilk. You  
4 couldn't use co-mingled milk to make your Class 2,  
5 State Class 2 products, or Federal Class I and II products,  
6 correct?

7 A. Correct.

8 Q. Okay. And that would create great inefficiency in both  
9 operations, correct?

10 A. It could, yes.

11 Q. And your WPC-80, to market that internationally, do you  
12 not also need to represent that that came from a Grade A milk?

13 A. Yes.

14 Q. So you could even use it in cheese, based on the way  
15 you used the whey byproduct of cheese?

16 A. Unless you could find a Grade B market for whey powder,  
17 you would be in the same boat you would be with the cheese.

18 Q. Thank you.

19 JUDGE CLIFTON: Are there any other cross-examination  
20 questions? Mr. English, for direct?

21 MR. ENGLISH: I'm hoping very few.

22 REDIRECT EXAMINATION

23 BY MR. ENGLISH:

24 Q. Chip English.

25 So you had some discussion with Mr. Beshore about the

1 purchase of cream --

2 A. Yes.

3 Q. -- a long time ago now.

4 A. Yes. I remember.

5 Q. To the extent that is California cream, someone has to  
6 account to the pool for that at minimum price, correct?

7 A. Correct.

8 Q. It shows up on the Form 800?

9 A. Our Class 2 plant is a pooling plant. All raw product  
10 taken into the plant is processed through the form 800, the  
11 Milk Pooling Reporting System.

12 Q. Okay. And you also had a, some commentary response to  
13 some questions, and I've forgotten who it was from, with  
14 respect to the whey stream, at some point that you pull some  
15 fat out of the whey stream and it goes back into the cheese,  
16 remember that?

17 A. Yes.

18 Q. First, is that a really small amount of fat?

19 A. Very small amount.

20 Q. And second, is that being priced as producer milk fat  
21 when you first get it? Again, on the form 800?

22 A. Yes, it is priced at the point it enters the vat for  
23 the first time in the cheese vat. It gets allocated to  
24 Class 4b.

25 Q. So finally, and I don't want to make too much time, but

1 we talked about full absorption, and then we talked about 2007,  
2 and I think we might have missed one concept. What is  
3 contribution margin, and how did it factor into the decision to  
4 shut the plant for one week in 2007?

5 A. Okay. So let's go back to my discussion about the  
6 direct and indirect costs. To the extent that you can identify  
7 costs as direct against a particular product, and when you take  
8 the sales price of the product, after it's, I think for being  
9 in inventories and all that stuff, and you get down to a number  
10 that represents the direct cost in the product you sold. So  
11 you take sales price at 5, minus direct cost at 3, you have  
12 what's called gross margin. And against that, you'd take your  
13 G and A, and other operating costs, and what not to get down to  
14 the bottom line profit.

15 The contribution margin is this number that comes up  
16 when you take sale price minus direct costs. As long as that  
17 number is positive, you're making some money to do something  
18 with some of these overhead costs. You are not covering all of  
19 them in that department, but if you shut that department off,  
20 you lose that contribution margin, and the rest of your  
21 department's now are going to absorb what that was covering on  
22 top of absorbing everything it was covering in that negative  
23 situation that you were in.

24 If you get to a point where you are not even covering,  
25 you have a negative contribution margin and you are not even



1 covering your direct costs, you are in the old situation where  
2 we say, we're losing it on every unit, but we're going to it  
3 make up in volume. And the more you do, the worse you get.  
4 And that's the situation we found ourselves in.

5 By the time we woke up to it, we already actually had  
6 been in it for awhile, but it took us awhile to wake up to in  
7 in 2007, that the cost of milk and the cost of the labor to  
8 convert the milk and the boxes and all of that stuff, that was  
9 more than the price we could get out of the market for the  
10 cheese. And so it had negative contribution margin, we said,  
11 phooey, we're done. So when I say our co-op cooperated, and  
12 our customers cooperated and all that, we were able to push our  
13 sales number up a little bit, we were able to push our cost of  
14 milk number down a little bit, to the point where we were at a  
15 break even at the contribution margin level. And we let the  
16 rest of our departments eat up all the overhead, and we muddled  
17 through until that December hearing decision came in and fixed,  
18 my word, "fixed", the whey factor for us, and then we could  
19 return to the normal business opt at that point.

20 Q. Thank you. That's all I have.

21 JUDGE CLIFTON: Mr. Francis, anything more for  
22 Mr. Hofferber? All right.

23 You have been an amazing help and I appreciate it. I  
24 appreciate very much your willingness to disclose some internal  
25 information about costs and losses. It's very helpful. Thank

1 you.

2 MR. HOFFERBER: Thank you.

3 MR. ENGLISH: Chip English. Having consulted with the next  
4 witnesses, they would prefer to have lunch first, and we can be  
5 back hopefully at 1:55 and get started, unless you say 2:00.

6 JUDGE CLIFTON: I think 2:00 is what I would say.

7 MR. ENGLISH: All right.

8 JUDGE CLIFTON: All right. Let's break for lunch at 12:42,  
9 we'll be back and ready to go at 2:00 p.m.

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1 TUESDAY, OCTOBER 27, 2015 - - AFTERNOON SESSION

2 JUDGE CLIFTON: We're back on record at 2:03. We have an  
3 exhibit that's being distributed now. Ms. Elliott, I believe  
4 the number we'll have for this one is 108. Is that correct?

5 MS. ELLIOTT: That's correct.

6 JUDGE CLIFTON: All right. I'm marking mine as  
7 Exhibit 108.

8 (Thereafter, Exhibit 108 was marked  
9 for identification.)

10 JUDGE CLIFTON: Ms. Vulin, do you want to begin us before I  
11 swear these gentlemen in, or should I swear them in first?

12 MS. VULIN: You may swear them in first. Thank you.

13 JUDGE CLIFTON: I'm going to swear you in at the same time,  
14 but when you are ready to say you will, or I do, or I so swear,  
15 or whatever you are going to say, I would like you to do it one  
16 at a time and say who you are.

17 Does each of you solemnly swear or affirm under penalty  
18 of perjury that the evidence you will present will be the  
19 truth?

20 MR. MOORE: I do swear. Mac Moore.

21 MR. de CARDENAS: I do swear. Gil de Cardenas.

22 JUDGE CLIFTON: Thank you. And beginning with Mr. Moore, I  
23 would like you to state and spell your name.

24 MR. MOORE: Mac Moore, it's M-A-C, and the last name is  
25 Moore, M-O-O-R-E.

1 JUDGE CLIFTON: And Mr. De Cardenas, likewise.

2 MR. de CARDENAS: Gil de Cardenas, G-I-L, d e,  
3 C-A-R-D-E-N-A-S.

4 JUDGE CLIFTON: Thank you. So I actually said your name  
5 wrong, because I forgot the "de" as part of your name.

6 MR. de CARDENAS: You are not the first, you won't be the  
7 last.

8 JUDGE CLIFTON: All right. I'm not the first and I won't  
9 be the last.

10 All right. Now, you will have to experiment a little  
11 bit with how close you will need to be with the mic, so we'll  
12 do that as we go along. Generally, you have to be fairly  
13 close, but since the mics are so close to each other, and you  
14 also have a speaker right there. We'll try to avoid feedback,  
15 but we may have to experiment just a bit.

16 Ms. Vulin, you may proceed.

17 DIRECT EXAMINATION

18 BY MS. VULIN:

19 Q. Thank you, your Honor.

20 Mr. Moore, if we can start with you. Just before we  
21 begin, can you give us a little bit of background on how you  
22 got involved in the dairy industry and what your role is now?

23 MR. MOORE: Sure. I was in the grocery business from '73  
24 until about '85. I worked for Ralph's Grocery Company. Then  
25 in '85, I was asked to assist in opening a new cheese plant out

1 in Corona, California, called Golden Cheese Company of  
2 California, and I began working as, in sales. At that time I  
3 was Vice President of Sales, and about three, four years later,  
4 DFA came in and purchased Golden Cheese. I moved to Kansas  
5 City with all the other officers, I was there as Vice President  
6 of Sales for a short period. Then I got drafted to go to work  
7 for Darigold. And I had a short stint at Darigold, and DFA  
8 called me back and gave me a better deal and asked me to come  
9 back, but I would let me continue living in Southern  
10 California. So I came back and worked in Southern California  
11 for several years as Vice President of Sales. At that time we  
12 had, I don't know how many cheese plants, but throughout the  
13 United States I would travel and work with them.

14 And then I got a phone call from one of the dairymen  
15 telling me that Cacique Cheese was looking for some help with a  
16 project. So I went in, I met for the first time, Gil's father.  
17 And as it turns out, when it was time for Gil was getting ready  
18 to go off and get his Master's degree, and we refer to Gilbert  
19 as the senior, and Gil as the younger one. So Gilbert, at the  
20 time, he wanted me to come onboard and help him with that  
21 transition while his son was off to college and doing other  
22 things.

23 So I came onboard. And in a few years I had another  
24 opportunity to go into process cheese business. I went to work  
25 for a company in LA, it was called Chateau Cheese. And so, to

1 give you an idea, we sold cheese to people like Jack-in-the-Box  
2 for their hamburgers. And after a few years there, Gil had  
3 restructured Cacique, and he had a new team together, and he  
4 asked if I could come back and be a part of a different branch.  
5 He wanted to, he wanted to expand the food service industry at  
6 Cacique and a few other ideas and some industrial accounts, and  
7 he thought I had the expertise to help him get that direction.  
8 And it sounded exciting to me because we were getting ready to  
9 sell Chateau Cheese anyway, so I would be without a job if I  
10 didn't have one going. So I took the opportunity, and that's  
11 where I have been since.

12 And so my job today is Director of Business  
13 Development. And I chase after the food service, industrial,  
14 and because of my background, I get involved with a little bit  
15 of risk management to help out on the Risk Management Team.

16 MS. VULIN: And I didn't hear any educational background.  
17 Is that something --

18 MR. MOORE: I have an MBA from University of Phoenix.

19 MS. VULIN: Thank you. And Mr. De Cardenas, I know we're  
20 going to hear a bit about your background in the written  
21 testimony, but if you wouldn't mind just telling us a little  
22 bit about your story and your current role at Cacique.

23 MR. de CARDENAS: Sure. I'm currently the CO of the  
24 company, been in this role for the last seven years.

25 Should we just wait for the rest of the testimony or --

1 MS. VULIN: Sure.

2 MR. de CARDENAS: Okay. Thank you.

3 MS. VULIN: Okay. So I'll have you begin, then, reading  
4 the testimony.

5 MR. de CARDENAS: Thank you. Good morning and thank you  
6 for taking the time to visit with us this morning. Clearly  
7 it's not morning anymore, but this afternoon, and we really  
8 appreciate it.

9 I'm Gil de Cardenas and I run our family business,  
10 Cacique, Inc. Cacique was founded by my parents, Gilbert and  
11 Jennie, in 1973. The company was funded with an \$800 loan from  
12 my grandmother, and \$800 from my aunt, that started with just  
13 two employees, Gilbert and Jennie. The first few years were  
14 very tough, with my dad leaving before the sun came up to start  
15 the cheese making process, while my mother woke us up, made  
16 breakfast, and took us to school. She then went to the plant  
17 (which was a tiny bottling plant at the back of a drive-up  
18 dairy) and took over the cheese making process from my dad and  
19 stayed until he returned from selling cheese from Styrofoam  
20 coolers in the trunk of his teal green, 1966 Pontiac. I won't  
21 forget that car, it made an impression. He would park his car  
22 on Vermont Street near downtown Los Angeles, and sell product  
23 door-to-door. My dad returned from his route, finishing the  
24 cheese making process, and cleaned the plant while mom came  
25 home to cook dinner and care for us. There were days when we

1 barely saw her and didn't see him at all.

2           At the start, times were so tough. My parents could  
3 only afford to rent the plant during daylight hours, and the  
4 owner of the plant used it to bottle his product at night. At  
5 the beginning, our capacity was about 80 pounds of milk -- I'm  
6 sorry, 80 pounds of cheese per day. That was all one person  
7 could make. This went on for a couple of years. A major leap  
8 forward was when my dad removed the back seat to make room for  
9 more coolers in his Pontiac. In effect, the this doubled the  
10 distribution capacity, and we were able to hire our first  
11 employee. True story. Absolutely true story. The company was  
12 literally built one pound of cheese at a time.

13           MS. VULIN: What kind of cheese were you making at this  
14 time?

15           MR. de CARDENAS: Queso Fresco at the time.

16           MS. VULIN: Queso Fresco?

17           MR. de CARDENAS: A note about the original plant. The  
18 facility was used for bottling drinks for a drive up dairy and  
19 originally was not set up for dairy processing. My dad rented  
20 the space and worked tirelessly for weeks to get it up to code.  
21 On inspection day, the inspector walked the plant and gave my  
22 dad a rather long punch list before he would approve the  
23 facility. To say my dad was disappointed is really an  
24 understatement. However, he doubled down and passed inspection  
25 several weeks later. There was no money to use for



1 professional help so my parents did all the improvements by  
2 themselves.

3 I grew up in the business and did everything from  
4 sweeping floors, to cleaning vats, to driving trucks. I rose  
5 through the ranks, earned an MBA at University of Chicago, and  
6 have been running the company for the past several years.

7 Over the last several years, we have been invited by  
8 numerous out-of-state municipalities and farmers to move our  
9 facility outside of California. I must admit, several of those  
10 offers were very enticing, but we have resisted. I share our  
11 history with you to illustrate our commitment to our business  
12 and to our farmers.

#### 13 Current Operations

14 Taking a leap to the here and now, Cacique continued to  
15 grow by providing quality products to the Hispanic consumers  
16 that live in the U.S. We specialize in products like Queso  
17 Fresco, panela, cotija, and cremas. We are now in our fifth  
18 plant since our tiny location in Lakewood, California. The  
19 original plant's milk consumption of 860 pounds per day is  
20 dwarfed by the current plant's consumption of about a million  
21 pounds of milk a day, and that's in the City of Industry. Over  
22 the course of the last 30 years, we have invested \$91 million  
23 into the current plant to stay competitive, and we are  
24 investing a significant amount of capital to expand current  
25 capacity.

1 Cacique currently has about 320 California-based  
2 employees, and 55 non-California employees. More than 70  
3 percent of Cacique employees are minorities. It is important  
4 to understand that Cacique is not a minimum wage employer. We  
5 demand higher skill levels and pay a premium. It's our  
6 educated estimate that between employees and vendor/suppliers,  
7 we help support more than a thousand families.

8 MS. VULIN: In terms of your employees for your company  
9 itself, you have 320 in California and 55 outside of  
10 California?

11 MR. de CARDENAS: That's correct.

12 MS. VULIN: So in total, you have less than 500 employees?

13 MR. de CARDENAS: That's correct.

14 MS. VULIN: Thank you.

15 MR. de CARDENAS: By basing such a large portion of its  
16 sales force in other states, we have made a very deliberate and  
17 expensive commitment to grow our business out-of-state.  
18 Cacique spends a considerable amount of marketing funds in  
19 activities like demos, advertising, and retailer ads to grow  
20 its out-of-state volume.

21 Every pound the cheese we ship out-of-state is equal to  
22 ten pounds of California milk being shipped into competing  
23 markets.

24 MS. VULIN: This is because it took you ten pounds of milk  
25 to create the product?

1 MR. de CARDENAS: On average, that's correct.

2 MS. VULIN: Okay. Thank you.

3 MR. de CARDENAS: Most of our consumers are on the lower  
4 end of the income range, and as a result, retail price points  
5 are crucial. As I mentioned previously, on average, Cacique  
6 consumes about one million pounds of milk on any given day,  
7 seven days a week. About 47 percent of that milk is shipped  
8 out of California as cheese, cream, and yogurt. It is  
9 estimated that about 60 percent of the United States population  
10 lives east of the Mississippi River.

11 Do you want me to read the reference point?

12 JUDGE CLIFTON: Sure. I like to see Wikipedia cited, so I  
13 would have you do it.

14 MR. de CARDENAS: ([En.wikipedia.org/wiki/Eastern United](http://En.wikipedia.org/wiki/Eastern_United)  
15 States.)

16 As our products travel east, transportation and other  
17 expenses drive our costs higher. Depending on load size,  
18 refrigerated freight cost into other, into the Midwest and East  
19 Coast, drives about 7 -- I'm sorry, between 30 and 70 cents per  
20 pound of product for LTL -- LTL is less than truck load --  
21 which is the most common method. As you can see, Cacique's  
22 Midwest and East Coast based competitors enjoy a significant  
23 competitive product transportation advantage, and in order to  
24 stay on the same level price point with these brands, Cacique  
25 is unable to pass the full cost onto the consumer, and is often

1 having to subsidize the freight expense just to keep the  
2 playing field level.

3 MS. VULIN: Can you tell me again about the LTL, less than  
4 truck load? How does that work in terms of practice when  
5 computing this number?

6 MR. de CARDENAS: So a truck load is about 40,000 pounds.  
7 There's a certain cost associated with 40,000 pounds, that's  
8 the most efficient way of shipping. However, because we are in  
9 a specialty cheese business, we rarely ship full truck loads.  
10 We'll ship anywhere from 1,200 pounds to 5,000, 10, 15, 20.  
11 And the further east you go, the higher the cost, so we end up  
12 shipping less, therefore making less efficient. And that's the  
13 range. Once you get to the Mississippi, east, it is from 30 to  
14 70, depending on the location it is going to, and how many  
15 pounds are going there.

16 MS. VULIN: And part of that variation is, you might not be  
17 shipping a full truck, you might have half of a truck or there  
18 might be a combination of products in a truck?

19 MR. de CARDENAS: I wish it was half a truck over there.  
20 It's usually a pallet to 5,000 pounds, somewhere in that range.  
21 Hence, why the costs are so high.

22 MS. VULIN: Thank you.

23 MR. de CARDENAS: Cacique's Out-of-State Competitors Lower  
24 Operating Costs

25 One of our competitors testified that our products are

1 aggressively competing with their Texas-based plant as a result  
2 of lower California milk prices. However, I would like to  
3 point out that the economics of the situation place Cacique at  
4 a disadvantage, not an advantage:

5 \* It takes about 12 cents just in freight costs to get  
6 to Texas from our plant. Using industry standards,  
7 this represents about \$1.20 per hundredweight in cost.

8 \* Since 2011, the gap between the published Class III  
9 and 4b is \$1.78. In effect, \$1.20 of the gap is  
10 consumed by freight alone.

11 \* That leaves only about 58 cents per hundredweight to  
12 pay the higher operating costs in California or roughly  
13 about 6 cents per pound of cheese.

14 It is no secret that doing business in California is  
15 difficult. In fact, I'm sure every farmer here today and in  
16 the state, are well aware of the serious challenges of running  
17 a California operation. The state is continuously listed near  
18 the bottom of any recent list of business-friendly  
19 environments.

20 We compete directly with regional manufacturers that  
21 aggressively defend their markets. Most of the competitors are  
22 east of the Rockies. While milk prices are higher, the  
23 operating costs are considerably lower. Expenses in states  
24 outside of California are considerably lower and these states  
25 are much more business-friendly than California. Below are a

1 few examples of the high cost of business operation in  
2 California compared to national averages:

3 \* Electrical costs for industrial companies. The  
4 United States March 2015 average retail price of  
5 electricity in the industrial sector, was 6.79.

6 JUDGE CLIFTON: That's \$6.79?

7 MR. de CARDENAS: Yes, that's correct. Excuse me.

8 JUDGE CLIFTON: Okay.

9 MR. de CARDENAS: California's rate in the industrial  
10 sector is \$10.63 or 56.55 percent above the national  
11 mean and rising. See Exhibit B, U.S. Energy  
12 Information Administration.

13 \* Workers' Compensation in California. Workers'  
14 Compensation costs in California is 188 percent higher  
15 than the national mean. California businesses spend  
16 \$3.48 for every \$100 of payroll, compared to the  
17 national mean of \$1.85. Cacique employs about 320  
18 California-based employees. See Exhibit A, Oregon  
19 Department of Consumer and Business Services, 2014  
20 Oregon Workers' Compensation Premium Rate Ranking  
21 Summary.

22 \* California Taxes. California ranks 48th out of 50  
23 states for least business-friendly states. See  
24 Exhibit C, Tax Foundation, October 2013 publication.

25 \* Cost of Energy in California is ranked 49th out of

1           50 states. See Exhibit D, California Foundation for  
2           Commerce & Education, the Cost of Doing Business in  
3           California, August 2014.

4           \* Cost of Labor in California is ranked 41st out of 50  
5           states. See Exhibit D, California Foundation for  
6           Commerce & Education, The Cost of Doing Business in  
7           California, August 2014.

8           MS. VULIN: These exhibits you didn't prepare yourself,  
9           correct?

10          MR. de CARDENAS: I did not.

11          MS. VULIN: But you are using them as an illustration of  
12          some of the challenges that you face operating in California?

13          MR. de CARDENAS: Correct.

14          MS. VULIN: And these are things that in your practice,  
15          excuse me, I practice, you do, in your business that you have  
16          experienced challenges in these areas here in California?

17          MR. de CARDENAS: We have.

18          MS. VULIN: Great. You may continue.

19          MR. de CARDENAS: Cacique, as a result of manufacturing in  
20          California, must bear these and other costs which far exceed  
21          national averages. Using these factors and others from our  
22          research, we estimate that raw material not included, it's  
23          costlier to make cheese in California by 18 cents per pound of  
24          cheese. This represents an equivalent of about \$1.80 per  
25          hundredweight higher than milk to run in California.

1 MS. VULIN: Can I have you -- that's an incredibly  
2 important sentence, so I'm going to ask if you might read that  
3 again for us.

4 MR. de CARDENAS: Using these factors and others from our  
5 research, we estimate that raw material not included, it's  
6 costlier to make cheese in California by 18 cents per pound of  
7 cheese. This represents an equivalent of about \$1.80 per  
8 hundredweight higher cost to run a California operation.

9 MS. VULIN: And that's a dollar -- excuse me, I'll let you  
10 finish.

11 MR. de CARDENAS: Cacique's out-of-state competition has  
12 key strategic cost advantages because they are located in more  
13 business-friendly state.

14 MS. VULIN: So this is really interesting, this idea of  
15 \$1.80 per hundredweight, and a number that is very tangible for  
16 us to work with that we haven't seen yet. So without asking  
17 anything specific that might get into confidential information,  
18 could you tell us a little bit about how you came to this \$1.80  
19 amount of cost added to milk produced, added to products  
20 produced in California?

21 MR. de CARDENAS: As I mentioned earlier, companies, I'm  
22 sorry, municipalities have come to us and offered to help us  
23 move into their locations to be part of their tax base, and  
24 also part of their buying from their milk, their co-op. These  
25 proposals have included all the differences in California to



1 these areas in the Upper Midwest. Everything from electrical  
2 power, waste water, garbage, disposal, labor, of course,  
3 sewage, workmans' comp, tax, overtime for labor, a whole host  
4 of things, and that's how we came to the number. They have  
5 given us their costs if we were to operate the same size  
6 facility in their area, and that is the delta. It's 18 cents a  
7 pound to operate in California more so, same size facility,  
8 same products, than it is in their area.

9 MS. VULIN: Thank you.

10 MR. de CARDENAS: The sum of the freight in California  
11 operating costs, less the historical Class III and 4b gap,  
12 results in product produced in California is costlier by 12  
13 cents, .1220, is that 12.2 cents, per pound, when shipped to  
14 Texas from So Cal. This represents --

15 JUDGE CLIFTON: Now, So Cal is a little shorthand there.  
16 What are you referring to?

17 MR. De CARDENAS: Southern California.

18 JUDGE CLIFTON: Thank you.

19 MR. de CARDENAS: This represents about \$1.222 per  
20 hundredweight of cheese. The formula would be: Freight, which  
21 is 12 cents, plus California operating cost, which is 18 cents,  
22 less the milk price gap which is 17.8 cents, and that's how we  
23 get to the 12.2 cent cost difference:

24 Freight(\$0.12) + CA operating cost (\$0.18)-milk price  
25 gap(\$0.178) = \$0.1220 lb./cheese

1 MS. VULIN: So you are taking the cost of shipping your milk  
2 to Texas, you are adding the 18 cents that has been calculated  
3 by all of these different municipalities trying to woo you, as  
4 they say, into their areas, you are subtracting the milk gap,  
5 which you noted was the between Roman numeral IV and the 4b  
6 price, and then you get a number that shows how expensive it  
7 is, essentially, to produce this cheese in California.

8 MR. MOORE: Roman numeral III.

9 MS. VULIN: Oh, yeah. Sorry.

10 MR. de CARDENAS: And it is 12 cents a pound to ship  
11 cheese, not milk.

12 MS. VULIN: Yes, thank you.

13 MR. de CARDENAS: So it is correct.

14 JUDGE CLIFTON: Now, when you read the formula the first  
15 time, I didn't quite catch the numbers the way I think I'm  
16 looking at them at the bottom of page 4. So would you please,  
17 again, read the formula at the bottom of page 4?

18 MR. de CARDENAS: Freight (\$0.12) + CA operating cost  
19 (\$0.18) - Milk price gap (\$0.178) = \$0.1220 lb./cheese more  
20 expensive in California.

21 JUDGE CLIFTON: Per pound of cheese.

22 MR. de CARDENAS: Per pound of cheese, correct.

23 JUDGE CLIFTON: And when, higher in the explanation on  
24 Page 4, when you talk about running a California operation,  
25 were you talking about a particular type of operation when you

1 said it is about \$1.80 per hundredweight higher to run a  
2 California operation?

3 MR. de CARDENAS: We're talking about a company like  
4 Cacique.

5 JUDGE CLIFTON: Thank you.

6 MS. VULIN: Because that number is based on actual analysis  
7 of a company like Cacique?

8 MR. de CARDENAS: Correct. It is the same size company  
9 elsewhere, Upper Midwest, and the difference is operating  
10 expenses. Your Honor, does that answer your question?

11 JUDGE CLIFTON: Yes, thank you.

12 MR. de CARDENAS: However, California recently changed its  
13 4b formula by raising the whey value. Using current market  
14 data, we estimate the gap between Class III and 4b narrows to  
15 54 cents per hundredweight in 2016. The new formula affects  
16 are:  
17 Freight (\$0.12) + California operating costs (\$0.18) - milk  
18 price gap (\$0.054) = \$0.246 per pound of cheese more expensive  
19 in California.

20 The new California price, in effect, raises the cost of  
21 making cheese in California from 12 cents, 12.2 cents, to 24.6  
22 cents per pound of cheese when delivered to Texas.

23 MS. VULIN: So really, when you are competing with products  
24 in the Texas market, it costs you more money to either produce  
25 and/or transport those products to Texas?

1 MR. de CARDENAS: The combination of both put us at a  
2 deficit of 24.6 cents. The results are staggering.

3 JUDGE CLIFTON: Now, that is a future cost projected there?

4 MR. de CARDENAS: That's correct, with a new milk formula  
5 for next year.

6 JUDGE CLIFTON: Right. Okay. And currently, based on your  
7 current costs, that's represented by the prior formula on the  
8 prior page?

9 MR. de CARDENAS: Correct.

10 JUDGE CLIFTON: Okay. I'm with you.

11 MR. de CARDENAS: The results are staggering, California  
12 made product is more expensive to make by about 12.6 per pound  
13 of cheese, or the equivalent of \$1.28 per hundredweight of milk  
14 before adding shipping costs. That formula is California  
15 operating cost, 18 cents, less future milk price gap of 5.4  
16 cents, equals 12.6 cents per pound higher in California.  
17 CA operating costs (\$0.18) - Milk price gap (\$0.054) = \$0.1260  
18 lb./cheese

19 As mentioned earlier, freight costs increased to 30 and  
20 up to 70 cents the further you go north and east, as we are  
21 unable to compete with local suppliers and ship smaller and  
22 less efficient loads or orders.

23 The only reason Cacique competes today, is not because  
24 of lower milk prices, but a continued commitment to investing  
25 in cutting edge technology. The notion that California made

1 cheese has a price advantage because of milk costs, may have  
2 been true in the past, but it is simply not true today, and it  
3 hasn't been for some time.

4 Current Market Conditions

5 As I mentioned earlier, most of our consumers are  
6 minorities and lower income brackets. Price point is  
7 understandably very important to these families. We are unable  
8 to absorb the increases a shift to FMMO brings, and will pass  
9 along the increase to the market. Our out-of-state competitors  
10 have not experienced the cost increase of a change in the milk  
11 formula and have no need to increase their prices. Therefore,  
12 they are in a position to gain distribution due to more  
13 favorable cost structure without lifting a finger. It is no  
14 wonder they are hoping California makes the change.

15 This will create an unorderly shift in economics,  
16 whereby the 47 percent of the milk we use for cheese making is  
17 substantially at risk to be lost to out-of-state competitors  
18 and milk suppliers. We are shifting milk demand out of  
19 California. How will dairies maintain efficiencies when volume  
20 leaves the state? Will they be able to operate efficiently?  
21 Will this cause a reduction in available Class I? This is  
22 especially true if California moves into the FMMO, but  
23 maintains provisions such as mandatory pooling.

24 Thank you for your time and consideration.

25 Sincerely, Gil de Cardenas, Cacique, Inc., family

1 member and Owner.

2 MS. VULIN: Mr. de Cardenas, you added a phrase there right  
3 at the end, provisions such as mandatory pooling.

4 MR. de CARDENAS: Correct.

5 MS. VULIN: Would you like us to insert that into the  
6 official copy of your testimony?

7 MR. de CARDENAS: Yes, please.

8 JUDGE CLIFTON: When you read the initials in that last  
9 sentence, I think you might have said, FFMO. That is the  
10 hardest phrase. Would you read that last sentence one more  
11 time, please? Starting with this is especially true if  
12 California?

13 MR. de CARDENAS: This is especially true if California  
14 moves into the FMMO, but maintains provisions such as mandatory  
15 pooling.

16 JUDGE CLIFTON: And, Ms. Elliott, I would like you to  
17 insert the word "mandatory" before "pooling" on page 6 of  
18 Exhibit 108. And I have two other little changes I would like  
19 you to make on the record copy. The first one, or tell me when  
20 you are ready to turn there. Are you already ready?

21 MS. ELLIOTT: Yes, I'm keeping track.

22 JUDGE CLIFTON: All right. So on page 1, the word "plant"  
23 instead of the word "plan" did you notice that already?

24 MS. ELLIOTT: Yes.

25 JUDGE CLIFTON: I would like to you add the "T", so that

1 the sentence reads, "at the start, times were so tough my  
2 parents could only afford to rent the plant during the daylight  
3 hours."

4 And then the only other one I noticed that I would like  
5 to you make, Ms. Elliott, is on page 3, in the first bullet  
6 point, second bullet point, "published Class III" I believe we  
7 just need to strike one of the Roman numeral 1's.

8 MS. ELLIOTT: Okay.

9 JUDGE CLIFTON: All right. Thank you. Ms. Vulin, back to  
10 you. But I do have a question. Mr. de Cardenas, in your  
11 signature block there's a capital D for DE, but on the opening,  
12 the cover, the cover of Exhibit 108, the de Cardenas has a  
13 small DE. Which do you prefer?

14 MR. de CARDENAS: The correct is small "de", we were  
15 rushing last night to get this printed and get it here this  
16 morning.

17 MR. MOORE: With a space.

18 JUDGE CLIFTON: With a space. So as it shows on the top  
19 page of Exhibit 108 is actually correct?

20 MR. de CARDENAS: Correct. Excuse me.

21 JUDGE CLIFTON: Thank you.

22 MS. VULIN: Thank you, your Honor, the Class III, 4 mixed  
23 me up as well.

24 So thank you very much for your testimony. I would  
25 like to just ask a couple of questions about the exhibits, if I

1 could. So Exhibit A, the 2014 Oregon Workers' Compensation  
2 Premium Rate Ranking Summary. Where did you get this document?

3 MR. de CARDENAS: This was given to me by our attorney, not  
4 you.

5 MS. VULIN: Is this a document from a government website?

6 MR. de CARDENAS: It is.

7 MS. VULIN: And you rely on it because it's a publication  
8 by, it looks like on the second page here, the Department of  
9 Consumer Business and Services?

10 MR. de CARDENAS: Correct.

11 MS. VULIN: Let's turn to Exhibit B, now, please. So it  
12 looks like this document is from the U.S. Energy Information  
13 Admission?

14 MR. de CARDENAS: That's correct.

15 MS. VULIN: Do you rely on it because it is a government  
16 published document?

17 MR. de CARDENAS: I believe it is, yes.

18 MS. VULIN: Do you believe this data to be correct?

19 MR. de CARDENAS: Yes.

20 MS. VULIN: We'll go now to Exhibit C. It looks like this  
21 document was published by the Tax Foundation?

22 MR. de CARDENAS: Correct.

23 MS. VULIN: And in their 2013 publication?

24 MR. de CARDENAS: I believe it was 2014 publication.

25 MS. VULIN: 2014 publication, thank you. And, well --



1 JUDGE CLIFTON: Well, how come it says --

2 MR. de CARDENAS: The publication is 2013 for the 2014.

3 MS. VULIN: And you believe the data in this document to be  
4 correct?

5 MR. de CARDENAS: Yes.

6 MS. VULIN: Is the Tax Foundation a government entity?

7 MR. de CARDENAS: I'm not sure of that.

8 MS. VULIN: And then we'll go to the last page, or the last  
9 exhibit, excuse me. California Foundation for Commerce and  
10 Education, the Cost of Doing Business in California. And you  
11 rely on this document as true because it's been put out by the  
12 California Foundation of Commerce and Education?

13 MR. de CARDENAS: Correct.

14 MS. VULIN: What, the data in the document you believe to  
15 be true?

16 MR. de CARDENAS: Yes.

17 MS. VULIN: Your Honor, I move for admission of  
18 Exhibit 108.

19 JUDGE CLIFTON: Is there anyone that would like to question  
20 the witness before determining whether you have an objection?  
21 No one. Are there any objections to the admission into  
22 evidence of Exhibit 108?

23 MR. BESHORE: Yes.

24 JUDGE CLIFTON: Mr. Beshore?

25 MR. BESHORE: I have a limited objection to Exhibit 108, C

1 and D, Exhibit C and D in particular. Which are publications  
2 of foundations, I mean, if they are in the record, you might as  
3 well just bring the library in, that's my objection. They are  
4 obviously hearsay. They are not anything that he, that he has  
5 prepared. We can all read anything and rely on it, but it  
6 doesn't, that's not enough to properly bring it into the record  
7 as if it is evidence to base a decision upon.

8 MS. VULIN: May I respond, your Honor?

9 JUDGE CLIFTON: You may.

10 MS. VULIN: So, first, hearsay evidence is admissible in a  
11 proceeding such as this, and we have seen plenty of it  
12 throughout. And as he stated in his testimony, these exhibits  
13 are more to demonstrate an experience that he's had in running  
14 his business. The data is a reflection of a true experience  
15 that he's had. He states very clearly that he didn't create  
16 the data and has incorporated it in a way in his testimony that  
17 reflects what sort of role it should play, which is to  
18 corroborate a personal experience that he's had, and the USDA  
19 is free to give it whatever weight it deems reasonable based on  
20 that testimony.

21 JUDGE CLIFTON: Does anyone else want to be heard on the  
22 issue of whether Exhibits C and D are objectionable for  
23 consideration in this hearing? When I look at, when I look at  
24 Exhibit D, let me start with that one. That's the more, the  
25 easier one for me to address.

1 I -- if Andrew Chang were here and he were presenting  
2 this, I know we would have all kinds of questions for him,  
3 which we're not able to ask if all we have is the document. So  
4 I don't accept it as an exhibit that is admitted into evidence  
5 with the same, what shall I say, with the same value as the  
6 other exhibits, but we won't take it out of the exhibit, we'll  
7 leave it in. Anyone's free to look at it. So I'm -- I am  
8 rejecting it as far as being as probative as the other  
9 exhibits. But it's food for thought. And anyone is welcome to  
10 use it as the beginning of their research on this topic. This  
11 is not the first witness whose testified about the higher costs  
12 of doing business in California, and so I think it has some  
13 use, even though I'm rejecting it as part of the evidence.

14 With regard to C, I feel a little different about that.  
15 Maybe I'm impressed by the name of the organization that put it  
16 together. I think it adds a significant data that's useful.  
17 Again, USDA can give it what weight it wishes.

18 So with regard to your objection, Mr. Beshore, it is  
19 sustained in part and overruled in part. I do admit into  
20 evidence, oh, is there anyone else who has any objection to the  
21 admission into evidence of Exhibit 108? No one.

22 I admit into evidence Exhibit 108 in its entirety,  
23 except for Exhibit D, which I reject, but it will remain part  
24 of the record. All documents that are rejected are kept as  
25 part of the record just as the accepted ones. The difference

1 is, it can't be relied on as evidence in the case. Ms. Vulin?

2 (Thereafter, Exhibit 108 was

3 received into evidence.)

4 MS. VULIN: Mr. de Cardenas, I would ask, absent Exhibit D,  
5 what has been your personal experience in terms of operating a  
6 business in California and the kind of more general sense of if  
7 it feels like a cost friendly environment or if you face  
8 significant hurdles in terms of costs specific to California?

9 MR. de CARDENAS: California'S definitely a very difficult  
10 to place to do business. It is getting more so, more  
11 challenging, to the point that many manufacturers in  
12 discussions I have had with them, feel unwelcome in California.

13 MS. VULIN: And this is from your personal experience of  
14 the costs you have related to electrical, or the costs you have  
15 related to Workers' Compensation, to the taxes, to the cost of  
16 energy. All of those factors have led you to conclude in your  
17 personal operation of a business in California, that it's a  
18 more difficult regulatory environment than other states?

19 MR. de CARDENAS: That is correct.

20 MS. VULIN: No further questions, your Honor.

21 JUDGE CLIFTON: Thank you, Ms. Vulin. This is a very  
22 valuable document and we appreciate your preparing it. And  
23 particularly, since it's based on personal experience of your,  
24 of your family, your parents first and then yourself, is there  
25 anything you would like to add before I ask for other people's

1 questions?

2 MR. de CARDENAS: No, not at this time.

3 JUDGE CLIFTON: All right. And how are the two of you, you  
4 and Mr. Moore, wanting to proceed with who will answer which  
5 questions?

6 MR. de CARDENAS: We'll see how the questions come up and  
7 we'll tag team.

8 JUDGE CLIFTON: Very good. Who would like to begin with  
9 questions of this panel? I'm going to reverse direction and  
10 have Mr. Miltner go first.

11 CROSS-EXAMINATION

12 BY MR. MILTNER:

13 Q. Thank you, your Honor. My name is Ryan Miltner I  
14 represent Select Milk producers.

15 Good afternoon.

16 MR. MOORE: Good afternoon.

17 MR. de CARDENAS: Good afternoon.

18 MR. MILTNER: Usually, as the Judge noted, I go last and  
19 that makes my list of questions shorter. We'll see if, how  
20 much longer it gets since I have to go first.

21 Thank you for your testimony. I appreciate the  
22 information you shared with us. Let me just start with  
23 clarifying a couple of questions that I had from your  
24 statement.

25 Mr. de Cardenas, I heard you mention that you are the

1 COO. Mr. Moore, I didn't get your title though. What is your  
2 title with the company?

3 MR. MOORE: Director of Business Development.

4 MR. MILTNER: Thank you. In your statement on page 2 you  
5 testified that you are now on your fifth plant. And I  
6 understand that to be that you still operate a single plant,  
7 this just happens to be the fifth one you have been in. Is  
8 that correct?

9 MR. de CARDENAS: We operate one dairy plant that we are  
10 currently in, it is the fifth one since that very first plant.  
11 From there we moved to location, location, location, bigger,  
12 bigger, bigger, to our current facility, but it's just one  
13 dairy plant.

14 MR. MILTNER: You have grown and evolved, and still operate  
15 out of one facility?

16 MR. de CARDENAS: Yes, sir.

17 JUDGE CLIFTON: Mr. de Cardenas, will you move your chair a  
18 little closer to the table? Thank you.

19 MR. MILTNER: Were you gentlemen in attendance yesterday  
20 for any of the hearing?

21 MR. MOORE: No.

22 MR. de CARDENAS: No.

23 MR. MILTNER: We had some testimony regarding the  
24 production of Hispanic cheeses and coming from the east  
25 especially, I'm not terribly knowledgeable about them, so I'm

1 hoping you can help me get a better idea of the products you  
2 guys produce.

3 My first question is, Queso Fresco versus Queso Blanco.  
4 Is there a, what's the distinction between those two cheeses  
5 from your perspective?

6 MR. de CARDENAS: Depends on who the manufacturer is.  
7 Some will make it very similar to Queso Fresco, so it is almost  
8 difficult to tell them apart. Others will take Queso Blanco,  
9 it's more like a Monterey Jack. The Spanish word or the  
10 translation is white cheese. So it is kind of open to  
11 interpretation.

12 MR. MILTNER: Okay. And you write in your testimony that  
13 you produce a Queso Fresco. So could you describe that cheese  
14 for us so we have a better idea what it's like?

15 MR. de CARDENAS: Queso Fresco is a fresh milk cheese, at  
16 least the way we make it. It is crumbly, it has a dairy note,  
17 very mild, almost like a milk-like taste.

18 MR. MILTNER: Is it a whole milk cheese?

19 MR. de CARDENAS: We make both.

20 MR. MILTNER: Okay.

21 MR. de CARDENAS: Part skim and whole milk.

22 MR. MILTNER: Would you consider it a soft cheese or a  
23 cheese of medium hardness a hard cheese?

24 MR. de CARDENAS: I would say it is a medium hardness.

25 MR. MILTNER: Okay. Is that a, would you consider it a

1 high moisture cheese?

2 MR. de CARDENAS: Define high moisture, please.

3 MR. MILTNER: More than 50 percent?

4 MR. de CARDENAS: Some of it.

5 MR. MILTNER: Okay. How about panela? What type of  
6 product is that and can you describe that for us a little bit?

7 MR. de CARDENAS: Panela is a different texture. It is a  
8 fresh cheese but it is a different texture. It is a tighter  
9 knit, it does not crumble, and it is made in a basket.

10 MR. MILTNER: Okay. Would that also be, would you consider  
11 that a high moisture cheese?

12 MR. de CARDENAS: That tends to fall right at the, right  
13 below the 50 percent.

14 MR. MILTNER: Okay. And cotija, did I pronounce that  
15 correctly?

16 MR. de CARDENAS: Correct.

17 MR. MILTNER: Okay. How about that type of cheese? Is  
18 that similar in nature to the other two? Is it different?

19 MR. de CARDENAS: No, that's at the other spectrum. That  
20 will be a dry, salty cheese. Very crumbly. Sort of like a  
21 Mexican style parmesan, at least the way it is used.

22 MR. MILTNER: I think that's how it was described  
23 yesterday, it is similar to a parmesan in its texture I guess.

24 MR. de CARDENAS: And usage.

25 MR. MILTNER: And usage. Thank you. And the cremas you



1 produce. Do you consider those cheeses? Do you consider those  
2 creams? How would you describe those for us?

3 MR. de CARDENAS: Those are creams.

4 MR. MILTNER: Okay. In terms of their classification, the  
5 cheeses we discussed, those are all California 4b products?

6 MR. de CARDENAS: Correct.

7 MR. MILTNER: Okay. And the cremas, what category would  
8 those fall into?

9 MR. de CARDENAS: 2.

10 MR. MILTNER: California Class 2?

11 MR. de CARDENAS: Correct.

12 MR. MILTNER: Thank you. Looking at your product mix, do  
13 you tend to produce more cheeses? More creams? About equal  
14 amounts of each?

15 MR. de CARDENAS: Far more cheese.

16 MR. MILTNER: Far more cheese. Your exported products, do  
17 your exports tend to match your overall production in terms of  
18 how they break down across products?

19 MR. de CARDENAS: Not sure I understand your question.

20 MR. MILTNER: Let me try again. Let's assume, okay, that  
21 you produce 80 percent cheese and 20 percent creams. Of the  
22 cheese that leaves California, and I guess when I say export, I  
23 mean export out-of-state. Do you tend to export in the same  
24 percentage so you export 80 percent cheese, 20 percent cream,  
25 or more cheese, more cream?

1 MR. de CARDENAS: The break down by category is about the  
2 same.

3 MR. MILTNER: Okay. Let me ask about your transportation.  
4 There's been some testimony in the hearing that the cost to  
5 ship a pound of cheese in a full load, a full 40,000 pound  
6 truck load to say Wisconsin, is somewhere 8 to 10 cents, if you  
7 were to shipping a full load, would that be consistent with  
8 your experience?

9 MR. de CARDENAS: No, it would not.

10 MR. MILTNER: Okay. Would you care to offer a thought of  
11 what it might be for you if you were going to ship a full load?

12 MR. de CARDENAS: We normally don't ship truck loads into  
13 that area, but we ship into Texas truck loads and it is about  
14 12. But Wisconsin, Illinois is far further, so I'm going to  
15 guess it is north of that.

16 MR. MILTNER: When you say Texas, Texas a big place. From,  
17 you know, LA to El Paso is a lot different from LA to Houston.  
18 So when you say ship to Texas, where would you be shipping that  
19 to for 12 cents?

20 MR. de CARDENAS: The San Antonio, Dallas, Houston area.

21 MR. MILTNER: It seems from your testimony that you base,  
22 you base your testimony on a perception that the market for  
23 manufacturing production is, tends to be regional in nature.  
24 Is that an accurate characterization?

25 MR. de CARDENAS: Could you repeat that again, please?

1 MR. MILTNER: Sure. Is the market for your products, do  
2 you consider that a regional market or a national market?

3 MR. de CARDENAS: From whose perspective?

4 MR. MILTNER: From your perspective as a manufacturer and  
5 seller?

6 MR. MOORE: Both.

7 MR. de CARDENAS: Yeah, we look at it in both. There are  
8 regional subtleties, actually, there's quite a lot, quite a big  
9 difference. You said from the east, right? You were coming  
10 from the east you said?

11 MR. MILTNER: I'm from Ohio, but when we have --

12 MR. de CARDENAS: That's east from here.

13 MR. MILTNER: Yeah. We tend to consider ourselves Midwest  
14 and not eastern, but my clients, Select Milk Producers, has  
15 producers in the Southwest and the Midwest.

16 MR. de CARDENAS: So -- so, for example, if you were to go  
17 to, would go to the East Coast, that tends to be a little  
18 Hispanic, a very different market, that's more Caribbean.  
19 Different products. So it's still a national market with very  
20 strong regional differences.

21 MR. MILTNER: In terms of the pricing regulations, whether  
22 they are California, where I guess, let's talk about the  
23 Federal regulations only. Do you believe that those, that the  
24 Federal pricing regulations should be regional in nature?

25 MR. de CARDENAS: I haven't given that any thought.

1 MR. MILTNER: Would your preference be that the prices  
2 applicable to you as a California manufacturer, be considered  
3 differently than the pricing regulations applicable to a cheese  
4 plant in, say, New Mexico or Texas?

5 MR. de CARDENAS: It's more expensive to operate here. If  
6 we did not treat it differently, it would be very challenging  
7 to operate at all.

8 JUDGE CLIFTON: Let's go off record just a moment. I don't  
9 want my witnesses to compete with the blowing machine outside.  
10 (Whereupon, a break was taken.)

11 JUDGE CLIFTON: It is better now. Mr. Miltner?

12 MR. MILTNER: Because you gentlemen were sitting right next  
13 to me during this morning's testimony, you heard some of the  
14 comments about the producer-handler regulations. Do you guys  
15 have any opinion on those at all?

16 MR. de CARDENAS: I don't.

17 MR. MOORE: No. We were interested in what he had to say,  
18 too.

19 MR. MILTNER: Okay. Let me look at -- let me offer you a  
20 hypothetical.

21 I want you to consider the situation of a cheese plant  
22 in a Federal Order subject to Federal minimum prices. If that  
23 plant pays its producers the Federal Class III price, your  
24 cheese is able to be transported into that market and compete,  
25 in part because your minimum regulated price is lower, correct?

1 MR. de CARDENAS: A small portion.

2 MR. MILTNER: A small portion?

3 MR. de CARDENAS: I would say so, yes.

4 MR. MILTNER: I understood your testimony to be that if you  
5 were subjected to the same price formulas, the Federal  
6 Class III prices, that your cheese would no longer be  
7 competitive with that plant in my hypothetical. Am I  
8 misunderstanding you?

9 MR. de CARDENAS: So maybe I misunderstood your question.

10 MR. MILTNER: So let's say you have got a plant, we'll put  
11 the plant in West Texas. They -- they pay their producers  
12 Class III.

13 JUDGE CLIFTON: So when you started your hypothetical, "so  
14 you have got a plant," you didn't mean Cacique has a plant?

15 MR. MILTNER: I did not. I mean, let's take the example of  
16 a plant in West Texas that pays the Federal Class III price to  
17 its producers supplying it. Okay?

18 MR. de CARDENAS: Correct.

19 MR. MILTNER: Your cheese produced in California, using  
20 the, you pay the California 4b price for the milk coming into  
21 your plant, you're able to ship that cheese into Texas and  
22 compete with that cheese produced in Texas, in part, because  
23 your regulated price is lower than the regulated price in  
24 Texas, correct?

25 MR. de CARDENAS: I don't agree with that.

1 MR. MILTNER: Okay. Why don't you agree with that?

2 MR. de CARDENAS: Because my operating costs here are  
3 higher than their operating costs in Texas.

4 MR. MILTNER: Today you make that shipment though, correct?

5 MR. de CARDENAS: I do.

6 MR. MILTNER: Okay. And what if we -- what if we told  
7 Cacique right now, you have to pay the Federal Class III price  
8 instead of the California 4b price? What does that do to your  
9 ability compete with that plant?

10 MR. de CARDENAS: I would -- my operating costs are still  
11 higher, I would pass that cost on to the customer.

12 MR. MILTNER: You would pass that cost on to the customer?

13 MR. de CARDENAS: Yes.

14 MR. MILTNER: Okay. Today you are competing with such  
15 plants, correct?

16 MR. de CARDENAS: Where?

17 MR. MILTNER: In, I guess in any market. Your cheese  
18 competes against cheese produced at plants subject to Federal  
19 prices, correct?

20 MR. de CARDENAS: Yes.

21 MR. MILTNER: Okay. Yet you have different regulated milk  
22 costs, correct?

23 MR. de CARDENAS: Yes.

24 MR. MILTNER: I don't have any other questions. Thank you.  
25 I apologize, I did have one more. Let me circle back to

1 something. In your testimony you said every pound of cheese  
2 that gets shipped out of California is ten pounds of milk that  
3 is sucked up, right? Because what you are saying is it takes  
4 ten pounds of milk to make one pound of cheese, right?

5 MR. de CARDENAS: On average, yes.

6 MR. MILTNER: Okay. And that's the Van Slyke formula, you  
7 know, 38 percent moisture, whatever. If you are producing a  
8 cheese that has 50 percent moisture, aren't you getting about  
9 13 pounds of cheese out of that instead of 10?

10 MR. de CARDENAS: Balance by cheeses, we get 8.

11 MR. MILTNER: I'm sorry?

12 MR. de CARDENAS: And that's balanced by cheeses we get 8.

13 MR. MILTNER: Sure. Because they have a lower moisture  
14 content, right?

15 MR. de CARDENAS: So our average is about ten.

16 MR. MILTNER: You are averaging about ten?

17 MR. de CARDENAS: Yes.

18 MR. MILTNER: But I guess, okay. I'll take that. That  
19 makes sense. Thank you.

20 MR. de CARDENAS: Thank you.

21 JUDGE CLIFTON: Mr. De Cardenas, did you say that the  
22 current plant location in is in the City of Industry?

23 MR. de CARDENAS: You are correct.

24 JUDGE CLIFTON: And is that in, you need to tell me where  
25 that is.

1 MR. de CARDENAS: About 20 miles dead east of downtown  
2 Los Angeles.

3 JUDGE CLIFTON: That would seem to me to be a perfect  
4 location.

5 MR. de CARDENAS: Getting to be less so, but the weather is  
6 nice.

7 JUDGE CLIFTON: Who next has questions for the panel?  
8 Thank you. Mr. Beshore.

9 CROSS-EXAMINATION

10 BY MR. BESHORE:

11 Q. Good afternoon, Mr. de Cardenas and Mr. Moore.

12 MR. MOORE: Good afternoon.

13 MR. de CARDENAS: Good afternoon.

14 MR. BESHORE: Marvin Beshore. I have a couple of questions  
15 about your, some of your calculations and projections. Let me  
16 start with THE top of page 5, you project, as I understand it,  
17 and I mean, you may correct me if I'm wrong here, the price for  
18 2016, under the newly, the recently changed California 4b  
19 formula; is that correct?

20 MR. de CARDENAS: Correct.

21 MR. BESHORE: Okay. So I'm wondering what assumptions you  
22 made, how did you make the calculation, come up with the  
23 calculation that the class, the new, under the new formula the  
24 gap between the Class III and 4b narrows to 54 cents?

25 MR. de CARDENAS: So every year about this time we budget



1 for the following year. And then we take all measurements, we  
2 also bring our consultants in, that specialize specifically in  
3 this area, and this is actually their number.

4 MR. BESHORE: Okay. Now, you have been under the new  
5 system for two months; is that right? As I understand it?

6 MR. MOORE: Yes, I think so.

7 MR. de CARDENAS: Close enough.

8 MR. BESHORE: Do you know what the difference has been for  
9 those two months?

10 MR. de CARDENAS: Not off the top of my head.

11 MR. BESHORE: Okay. So your consultants projected that for  
12 the year 2016, the difference would be just 54 cents between  
13 Class III and 4b?

14 MR. de CARDENAS: That is correct.

15 MR. BESHORE: Okay. Now, you have said, and I think this  
16 is, let's see, prior page, page 4, that, presently, at the  
17 bottom the formula at the very bottom, and maybe you got into  
18 this with Mr. Miltner a little bit, too. You are saying that  
19 presently you start out, when you are selling into Texas, ship  
20 to Texas from So Cal, are you starting at 12 cents behind? Is  
21 that how I understand it?

22 MR. de CARDENAS: The cost -- I'm not sure what you mean by  
23 behind.

24 MR. BESHORE: Well, I'm trying to -- you have indicated it  
25 costs 12 cents freight to get there, your operating costs are

1 18 cents, this is all per pound of cheese, higher, so that's 30  
2 cents. And then you're reducing that for the milk price gap of  
3 17.8 cents, so that when you start out, you're 12.2 cents, your  
4 costs, your cheese product, has cost 12.2 cents per pound more  
5 than your competitor in Texas, as I understand it. Is that --  
6 is that wrong?

7 MR. de CARDENAS: That's our estimate.

8 MR. BESHORE: So why would you compete down there?

9 MR. de CARDENAS: I'm not sure I understand the question.

10 MR. BESHORE: Well, how do you get sales there, if, you  
11 know, you are already -- does your product have a, command a  
12 premium so that you can be profitable in that marketplace even  
13 with those kind of costs deficits?

14 MR. de CARDENAS: I also mentioned that the reason we are  
15 able to compete is our commitment to technology. We have  
16 committed quite a bit into technology. So we have to be  
17 extremely efficient in manufacturing.

18 MR. BESHORE: So where does that -- where does the  
19 technology factor into these, the cost equation here?

20 MR. de CARDENAS: It wouldn't. This is the cost of two  
21 different plants, same plant, two different locations, what are  
22 the input costs that are different. Such as fuels, such as  
23 water, such as electricity, such as gas, labor, all those  
24 factors. And it turns out that in California, it's more  
25 expensive by 18 cents a pound.

1 MR. BESHORE: So where do you -- how do you experience  
2 savings through technology? What technology allows you to  
3 reduce your costs or be more efficient?

4 MR. de CARDENAS: There's a lot of technology we have  
5 developed in-house. We ARE probably the largest Queso Fresco  
6 manufacturer in the country. And as a result, there's scale.  
7 But there's also a lot of investment into home built  
8 technologies, let's call them.

9 MR. BESHORE: So your -- your make cost, if you will, for  
10 the cheese is less than your competitors because of the  
11 technology that you use?

12 MR. de CARDENAS: We are more efficient as a result of  
13 significant investments that make us more efficient.

14 MR. BESHORE: Okay. So how much of the 18 cent California  
15 operating cost deficit does the technology make up?

16 MR. de CARDENAS: I'm sorry, I'm not going to get into  
17 that, that's proprietary. Very proprietary.

18 JUDGE CLIFTON: But I think the main take away from this  
19 exchange between the two of you, Mr. de Cardenas, is that when  
20 we look at this formula at the bottom of page 4, it's not meant  
21 to include everything. It is not your entire cost. And it's  
22 not, it's just showing, you're wanting us to focus on a few  
23 things, a few components of the cost of the production of your  
24 cheese, not all of them; is that correct?

25 MR. de CARDENAS: To some degree. What I'm trying to show

1 here is the cost of having a plant in California and a plant in  
2 the Upper Midwest. All things being equal, where are the  
3 savings or which is more expensive to operate? And it tells us  
4 that California is more expensive to operate because of the  
5 negative business environment we have here, by that amount.

6 JUDGE CLIFTON: Okay. But you haven't tried to show us in  
7 this formula at the bottom of page 4 what it costs you to  
8 operate have you? Aren't you just trying to show us the  
9 additional costs of being in California?

10 MR. de CARDENAS: Correct.

11 JUDGE CLIFTON: And so this doesn't include either the cost  
12 of production or A make allowance, or the efficiencies you have  
13 achieved?

14 MR. de CARDENAS: That is correct. True statement.

15 JUDGE CLIFTON: Okay.

16 MR. BESHORE: Okay. So what makes up the operating cost  
17 deficiency of a difference of 18 cents?

18 MR. de CARDENAS: So there's tax involved, labor costs,  
19 electricity, packaging supplies, sewage, waste disposal,  
20 workmans' comp, water, those are the main components.

21 MR. BESHORE: And the components then, that would go into  
22 your, you know, your efficiencies, are none of those but they  
23 are something else in your processing operation?

24 MR. de CARDENAS: Correct.

25 MR. BESHORE: What states solicited you to relocate and

1 gave you all the raw material for comparing costs?

2 MR. de CARDENAS: Upper Midwest.

3 MR. BESHORE: Okay. As in Wisconsin?

4 MR. de CARDENAS: As in the Upper Midwest.

5 MR. BESHORE: And you declined their offer?

6 MR. de CARDENAS: We did not feel it was appropriate for  
7 us. We're a California company, been here all our lives, and  
8 we would like to stay in California.

9 MR. BESHORE: Okay. So a couple of percentages here. On  
10 page 3 you talk at the top about 47 percent of that milk is  
11 shipped out of California as cheese, cream, and yogurt. Is  
12 that, that's 47 percent of your production? Is that what that  
13 refers to?

14 MR. de CARDENAS: It is.

15 MR. BESHORE: Okay. And on the -- on page 5, at the  
16 bottom, we talk about 47 percent of the milk we use for cheese  
17 making, is that the same 47 percent or is that a different 47  
18 percent?

19 MR. de CARDENAS: It's the same. It should be cheese  
20 making, cream, and yogurt.

21 MR. BESHORE: Okay. Do any companies from other areas  
22 compete for sales of Hispanic cheeses in California, any  
23 out-of-state companies compete in California? Out-of-state  
24 cheese manufacturers?

25 MR. MOORE: Yes. There's -- there are quite a few.

1 California's kind of an attraction. When you consider the  
2 greatest percentage of our consumers live in the west, so it is  
3 a, it's a hot market for a lot of people. So we get  
4 competitors coming in from Chicago; we get competitors coming  
5 in from Georgia; and they are pretty dominant on the shelf, and  
6 a lot from Wisconsin.

7 MR. BESHORE: Okay. And those are manufacturers of  
8 Hispanic cheeses?

9 MR. MOORE: Absolutely. Queso Fresco.

10 MR. BESHORE: And other besides Queso Fresco, any other  
11 varieties?

12 MR. MOORE: Well, they usually bring in a whole line of  
13 products all the way from panela, to Oaxaca, to Queso Blanco,  
14 Fresco.

15 MR. BESHORE: Okay. So how could a manufacturer from  
16 Georgia, assuming we know, that they would have to pay at least  
17 the Class III price for their milk down there, they are  
18 producing -- producing cheese at a milk deficit area, supplies  
19 got to be challenging. How can they land product on a store  
20 shelf in California?

21 MR. MOORE: That's our question, too.

22 MR. BESHORE: Do you have an answer to it?

23 MR. MOORE: That's the study. That's how we get these  
24 numbers. That's why we study them so hard. How are they doing  
25 it? They are bringing it in, and they can't wait to get in.

1 And so it's -- we worry about this day and night. This keeps  
2 us up at night.

3 MR. BESHORE: And your sales, I take it, in California, are  
4 profitable ones?

5 MR. MOORE: Yes.

6 MR. BESHORE: Okay. Would you say your product is a  
7 premium product? Do you sell at premium prices, like I think  
8 you indicated you were able to in Texas, generally?

9 MR. de CARDENAS: I don't think I indicated premium. I  
10 didn't answer that question, I don't think, in Texas. Okay.

11 MR. BESHORE: So you don't, your products do not command  
12 premium prices?

13 MR. de CARDENAS: So we go to market with a multi-brand  
14 strategy. We have a premium, we have a -- we have a middle  
15 market, and we have a very aggressive price product. So we go  
16 to market all three.

17 MR. BESHORE: Okay. And are all these of them marketed  
18 nationally?

19 MR. de CARDENAS: Yes.

20 MR. BESHORE: Okay. So I went to your website the other  
21 day, and I, you have a store locator and I put my zip code in.

22 MR. de CARDENAS: Did it work?

23 MR. BESHORE: It worked. And I'm interested in learning  
24 about it.

25 MR. MOORE: We'll tell our team. They will like that.

1 MR. BESHORE: So I'm from Pennsylvania, okay? 17070.  
2 Bang. It flags all over the place. Okay? Lots of Cacique  
3 product in Pennsylvania. Most of them at least, appear to be  
4 in Wal-Mart stores. Can you tell us -- okay. So where --  
5 where do you deliver to Wal-Mart?

6 MR. de CARDENAS: FOB our dock.

7 MR. BESHORE: So Wal-Mart comes and picks up product at  
8 your dock, and then the product that I get in California, if I  
9 go to the one of the Wal-Marts that are around there, with your  
10 label, would have been, would have come from your dock in  
11 California? Wal-Mart would have transported it there?

12 JUDGE CLIFTON: You asked about when you get your product  
13 in California.

14 MR. BESHORE: Well, I misspoke. When I get my product at a  
15 Wal-Mart store in Pennsylvania, it would have been picked up by  
16 Wal-Mart at your dock in the City of Industry, California; is  
17 that correct?

18 MR. MOORE: That's correct. That's the amazing part about  
19 Wal-Mart, those guys can move product.

20 MR. de CARDENAS: Very efficiently.

21 MR. BESHORE: I think that's all the questions I have right  
22 now. Thank you very much, gentlemen.

23 MR. MOORE: Thank you.

24 MR. de CARDENAS: You're welcome. And by the way, you  
25 should try it. You should go to the store and buy it.



1 JUDGE CLIFTON: If we ever get him out of this place, he'll  
2 have a chance. In a moment, Mr. Vetne, I'll call on you.  
3 Mr. Moore, you -- you named something I didn't have before,  
4 Oaxaca. Is that a cheese?

5 MR. MOORE: Absolutely. It is a gorgeous cheese. You will  
6 like it. We didn't put it on there, but it is spelled  
7 O-A-X-A-C-A. There's an invisible W at the beginning.

8 It is from a state in Northern Mexico. And it's a  
9 long, long rope. We make it in a five pounders, about 35 feet  
10 long rope, and you just tie it up in a knot and it is a big ole  
11 ball.

12 JUDGE CLIFTON: So that's one of the products that Cacique  
13 produces?

14 MR. MOORE: Yes, ma'am.

15 JUDGE CLIFTON: Very interesting. Mr. Vetne. Mr. English.

16 CROSS-EXAMINATION

17 BY MR. ENGLISH:

18 Q. Chip English, thank you, your Honor.

19 So let me see if I can, in case there's still some  
20 confusion in the record, look at this comparison you are trying  
21 to do on page 4 and on page 5.

22 You were trying to do an apples to apple comparison, as  
23 I read it. You were taking, here's your plant with your  
24 technologies, and if you took that plant and instead were  
25 physically able to, Star Trek-wise, beam it, to say, the Upper

1 Midwest, that you were looking at what the cost difference  
2 would be for the identical plant with the identical kind of  
3 technology; is that correct?

4 MR. de CARDENAS: It is.

5 MR. ENGLISH: Okay. So what you were trying to say in  
6 response to the competition questions is, that while you don't  
7 know everything about your competitors, they may not have those  
8 technological advantages that you have, correct?

9 MR. de CARDENAS: Correct.

10 MR. ENGLISH: But nonetheless, if you are doing a  
11 comparison of what your plant would be, that's what this is  
12 trying to show on page 4. So you are not leaving any cost out,  
13 you were trying to show how those costs would be different if  
14 it was located, say, for example, in Wisconsin, or somewhere in  
15 the Upper Midwest, like Indiana or something? Is that what you  
16 are trying to do?

17 MR. de CARDENAS: Yes, it is.

18 MR. ENGLISH: Now, so you also were asked questions about,  
19 you know, well, how do products get here from, say, the Upper  
20 Midwest? And, you know, in 2015, the retail landscape is a  
21 pretty amazing place, isn't it?

22 MR. de CARDENAS: Yes, it is.

23 MR. ENGLISH: You know, I don't know whether you know, but  
24 you know, we have clicked on it, Mr. Beshore said he's clicked  
25 on it, so for instance, we've had testimony about how, you

1 know, some cheddar cheese, California ends up in the Northeast  
2 to compete with a company called Cabot's. Have you ever heard  
3 of Cabot's Cheese?

4 MR. MOORE: Yes.

5 MR. de CARDENAS: I have.

6 MR. ENGLISH: If you click right here, right here in  
7 Clovis, would you be aware that you could buy Cabot's cheese  
8 within a couple of blocks from this location?

9 MR. MOORE: I believe that.

10 MR. de CARDENAS: I buy Cabot's in Southern California, so  
11 I believe it.

12 MR. MOORE: They make a fine white cheese.

13 MR. de CARDENAS: Yes, they do.

14 MR. MOORE: One of the best cheddars you can buy. Very  
15 good.

16 MR. ENGLISH: Thank you. That's all I have got.

17 JUDGE CLIFTON: Now, Mr. Vetne, this is a perfect time for  
18 you to come. And I would like that, when you introduce  
19 yourself, you tell us where you are from.

20 CROSS-EXAMINATION

21 BY MR. VETNE:

22 Q. Gentlemen, I'm John Vetne. I'm a representative for  
23 Hilmar Cheese Company. And I was glad to yield to the other  
24 gentleman from the state of Maine, that's where we are both  
25 from, and we love that white cheddar from Cabot. Okay.

1 I have a couple of questions. You described the  
2 process by which your products are found in the stores of  
3 Wal-Mart, apparently throughout much of the country. For milk  
4 that's, for milk products that are not going to Wal-Mart that  
5 are picked up at your plant in the these trucks carrying up to  
6 40,000 pounds, is that similarly delivered to a truck FOB your  
7 dock? Is it your own trucks? How does that -- how does that  
8 get distributed?

9 MR. de CARDENAS: So depending on the customer, they are a  
10 pick up at our dock, like a Wal-Mart, or other customers who  
11 prefer us to ship to them, in which case we have got an FOB  
12 price plus a freight component, depending on the volume,  
13 volume, how much, how many tons or how much weight goes on the  
14 truck is the freight rate.

15 MR. VETNE: Okay. So all of your product is priced FOB  
16 your plant, and for some customers, you additionally arrange  
17 for transportation and add a transportation cost to deliver to  
18 their location; is that correct?

19 MR. MOORE: Correct.

20 MR. de CARDENAS: Correct.

21 MR. VETNE: I like it, two corrects. Double the pleasure,  
22 double the fun.

23 MR. MOORE: It's good when we agree.

24 MR. VETNE: And you indicated that sometimes these trucks  
25 don't have 40,000 pounds of cheese. Would it be correct for me

1 to infer that if it's 10,000 pounds of cheese, that there are  
2 30,000 pounds, as close as you can get, of things other than  
3 cheese on the trucks?

4 MR. de CARDENAS: That would be a fair assumption.

5 MR. VETNE: Okay. And would that be, the remainder be your  
6 products?

7 MR. de CARDENAS: No, not necessarily.

8 MR. VETNE: So some trucks may come to your plant partially  
9 filled, and you would add cheese to the load, or you would put  
10 cheese and partially fill a truck and they would go somewhere  
11 else and get the rest of the load?

12 MR. de CARDENAS: Correct.

13 MR. VETNE: Mr. Miltner asked you some questions about  
14 whether you think the same considerations should be given to  
15 pricing milk at your plant if there's a Federal Milk Marketing  
16 Order that had been given to other plants in the Federal system  
17 in establishing a price. Do you recall that conversation with  
18 Mr. Miltner?

19 MR. de CARDENAS: Yes.

20 MR. VETNE: Okay. So assume with me that considerations  
21 given for pricing milk used to produce cheese in the Federal  
22 Order system, and it is a system that currently doesn't include  
23 California, but in that system, that the considerations given,  
24 are, the price must be such that there will be willing buyers,  
25 that milk will clear the market, and that the manufacturers of

1 those cheese will make at least some profit.

2 Do you think those considerations should apply to your  
3 plant?

4 MR. de CARDENAS: And every day is Christmas.

5 MR. VETNE: Do you agree that those considerations should  
6 be applied in the same way to cheese making in California?

7 MR. de CARDENAS: I need a lot more detail to understand  
8 what you mean.

9 MR. VETNE: How about, let's go backwards. Make a profit.  
10 Should milk be priced so the cheese makers can make a profit?

11 MR. de CARDENAS: What profit is that?

12 MR. VETNE: Profit for the plant in making cheese?

13 MR. de CARDENAS: Again, what profit would that be?

14 MR. VETNE: I'm, you know, for regulatory purposes,  
15 sometimes it's small.

16 MR. de CARDENAS: So how do I then, bring new consumers  
17 into my category? How do I educate new consumers?

18 MR. VETNE: I did not understand the question because I'm  
19 asking one. I can't -- I can't multi-task.

20 JUDGE CLIFTON: Mr. Vetne, I frankly don't understand your  
21 question either. Are you asking should all cheese processors  
22 be guaranteed a profit? Is that your question?

23 MR. VETNE: No, that wasn't the question.

24 JUDGE CLIFTON: Okay.

25 MR. VETNE: Let me ask it this way. Can you continue to

1 make cheese if you cannot make profit in the future?

2 MR. de CARDENAS: No.

3 MR. VETNE: Okay. Are you willing to take milk into your  
4 plant if making cheese causes you to lose money for each pound  
5 of cheese you make?

6 MR. de CARDENAS: No.

7 MR. VETNE: In that circumstance, you would not be a  
8 willing buyer of milk for cheese; is that correct?

9 MR. de CARDENAS: That is correct.

10 MR. VETNE: Okay. And then the question that hasn't been  
11 asked. What do you do with your whey?

12 MR. de CARDENAS: We process our whey.

13 MR. VETNE: You process your whey?

14 MR. de CARDENAS: We do.

15 MR. VETNE: Well, how do you process it?

16 MR. de CARDENAS: We run it through a membrane system.

17 MR. VETNE: And do what, after it is through the membrane?  
18 What does it become?

19 MR. de CARDENAS: WPC-37 I think it is, and then we ship  
20 it, we sell that to a customer, and then we have our lactose  
21 hauled off.

22 MR. VETNE: Lactose, water-reduced lactose?

23 MR. de CARDENAS: Yes.

24 MR. VETNE: Run it through a reverse osmosis system or  
25 something before you have it hauled off?

1 MR. de CARDENAS: Correct.

2 MR. VETNE: Okay. And when it is hauled off, is somebody  
3 buying that lactose?

4 MR. de CARDENAS: Actually, it is a cost to us.

5 MR. VETNE: It is a cost? You pay somebody to remove it?

6 MR. de CARDENAS: Yes.

7 MR. VETNE: Okay. And what do you do with whey cream?

8 MR. de CARDENAS: We use it back into the process.

9 MR. VETNE: You try to make use of it back in your cheeses?

10 MR. de CARDENAS: Correct.

11 MR. VETNE: Okay. Good. You were asked some questions  
12 about, well, let's see. You are aware that there's some  
13 competitor in Georgia that makes Hispanic cheeses; is that  
14 true?

15 MR. de CARDENAS: Yes.

16 MR. VETNE: Okay.

17 MR. de CARDENAS: But it is not clear to us they make it in  
18 Georgia. The company's headquartered in Atlanta.

19 MR. MOORE: Right.

20 MR. VETNE: Oh, I see, so you don't know where they get  
21 their product from?

22 MR. de CARDENAS: We believe it is the Upper Midwest.

23 MR. VETNE: Okay. Are you aware that in the Upper Midwest  
24 there are still a few remaining Grade B producers?

25 MR. de CARDENAS: No, I'm not.



1 MR. VETNE: You are not aware of that. Okay. Are you  
2 aware that in the Upper Midwest, milk may be purchased by  
3 nonpool plants, that is not a fully regulated plant, at below  
4 Class III prices?

5 MR. de CARDENAS: Yes.

6 MR. VETNE: Okay. And then finally, you were asked, I  
7 think it was Judge Clifton asked you a question about your  
8 calculation at the very top of page 5, where you estimated a  
9 gap between Class III and 4b, and the new formula for what you  
10 calculate as your disadvantage. In response to the question, I  
11 think you said you projected this will be your loss in the  
12 future, correct?

13 MR. de CARDENAS: We project it as to the delta in the  
14 future, yes.

15 MR. VETNE: Okay. But, in fact, it also represents the  
16 present, because you have operated under that new formula since  
17 August 1, correct?

18 MR. de CARDENAS: Correct, but as we did the formula, it  
19 was an entire year where all the differences we have only got a  
20 couple of months in the formula. Yes, we are already affected.

21 MR. VETNE: You were already affected by that and have  
22 operated, you have lived with it for a couple months already?

23 MR. de CARDENAS: Yes.

24 MR. VETNE: Okay. Thank you.

25 JUDGE CLIFTON: Mr. de Cardenas, would you look at page 1

1 of Exhibit 108, and in the second line where you are saying who  
2 you are, and that you run the family business, that second  
3 sentence of that paragraph, has an "S" on the end of Cacique.  
4 Does that belong there, the "S" that's there?

5 MR. de CARDENAS: No, it does not.

6 JUDGE CLIFTON: Okay. I'm going to ask that that be  
7 changed on the record copy, and just strike the "S". So when  
8 you are parents ran the company it was named exactly what it is  
9 named now, but it's now a corporation?

10 MR. de CARDENAS: Correct.

11 JUDGE CLIFTON: And I presume that's a Spanish word?

12 MR. de CARDENAS: It is.

13 JUDGE CLIFTON: Does it have a particular meaning other  
14 than the name?

15 MR. de CARDENAS: It does.

16 JUDGE CLIFTON: What is that meaning?

17 MR. de CARDENAS: That the Cacique is the leader of a  
18 Native American tribe, Caribbean specifically, so it would be  
19 the chief.

20 JUDGE CLIFTON: Thank you.

21 MR. de CARDENAS: You're welcome.

22 JUDGE CLIFTON: Mr. Beshore?

23 CROSS-EXAMINATION

24 BY MR. BESHORE:

25 Q. Just one other question. I'm struggling trying to

1 understand the cost side of your business. In particular, you  
2 have the technology efficiencies that you have, that you have  
3 mentioned, and I'm struggling in part because we had testimony  
4 from a Hispanic cheese manufacturer yesterday, that the  
5 Hispanic cheese manufacturing business was particularly labor  
6 intensive. Is that true?

7 MR. de CARDENAS: I have no idea who this is or how they  
8 process.

9 MR. BESHORE: Well, but they were making the same kinds of  
10 cheeses that you make.

11 JUDGE CLIFTON: So you are asking if that's been his  
12 experience?

13 MR. BESHORE: Yes, is that his experience?

14 MR. de CARDENAS: At one point in time it was.

15 MR. BESHORE: But not today?

16 MR. de CARDENAS: That's correct.

17 MR. BESHORE: Okay. So you have displaced labor in the  
18 manufacturing process with technology?

19 MR. de CARDENAS: We have gotten far more efficient.

20 MR. BESHORE: And is that a yes that you have displaced  
21 labor in the manufacturing process with technology?

22 MR. de CARDENAS: No.

23 MR. BESHORE: That's not correct. Your labor is more  
24 productive?

25 MR. de CARDENAS: Yes.

1 MR. BESHORE: Are you familiar with the CDFA cheese cost  
2 studies, cheese making cost studies?

3 MR. de CARDENAS: I know of them.

4 MR. BESHORE: And have you ever compared your cost profile  
5 to what CDFA, through their plant cost auditing process has  
6 shown to be the cost profile for making cheddar cheese?

7 MR. de CARDENAS: No, I have not.

8 MR. BESHORE: Okay. So you don't have any idea whether  
9 packaging is the same, miscellaneous ingredients are about the  
10 same percentage, processing labor, non-processing labor, how  
11 they compare to cheddar manufacture?

12 MR. de CARDENAS: I don't.

13 MR. BESHORE: Have you ever made cheddar?

14 MR. de CARDENAS: I think we made long point cheddar in the  
15 early '80's.

16 MR. BESHORE: Okay. Not recently?

17 MR. de CARDENAS: No, sir.

18 MR. BESHORE: Thank you. That's all.

19 MR. de CARDENAS: You're welcome.

20 JUDGE CLIFTON: Mr. de Cardenas, this is not the subject of  
21 your testimony, but do you have an opinion as to how the  
22 components of milk should be priced to meet the needs of a  
23 cheese manufacturer such as yourself? And I'm aware you are  
24 not just a cheese manufacturer, you also produce yogurt and  
25 cream, I'm just asking in your experience operating the plant

1 you operate, do you have an opinion as to what a more realistic  
2 pricing scheme might be for your operation?

3 MR. de CARDENAS: Not necessarily, but it just seems that  
4 we're always arguing about this, and it's a zero-sum game. One  
5 side wins, the other side loses, and we forget about the market  
6 as a result. So we, as an industry in California, are leaving  
7 a lot of money on the table through this process. Instead of  
8 finding a way to work together and then going to the market and  
9 growing our business, instead, we're arguing. And we heard it  
10 this morning, I completely agree. Every couple years, here we  
11 are doing the same thing.

12 We need to find a solution that allow us as an industry  
13 to go forward long-term without all of these stops and goes.  
14 California has got to find a way to be efficient in its  
15 manufacturing practices, its dairy practices, to be able to  
16 cross the Rockies into the Midwest effectively or it will not  
17 survive long-term. It just won't.

18 Does that answer your question?

19 JUDGE CLIFTON: It certainly does.

20 MR. de CARDENAS: Thank you.

21 JUDGE CLIFTON: Who else has questions for Mr. de Cardenas?

22 CROSS-EXAMINATION

23 BY MR. VANDENHEUVEL:

24 Q. Good afternoon, Rob Vandenheuvel, Milk Producers  
25 Council. We represent dairy farmers here in the State of

1 California. I don't think we have met so I just wanted to give  
2 you an idea of who you are talking to.

3 MR. de CARDENAS: Thank you.

4 MR. VANDENHEUVEL: First off, I did really appreciate the  
5 story of your origins. I have heard those same types of  
6 stories from grandfather and dairy farmers that started earlier  
7 in the 20th century, and certainly can appreciate starting from  
8 humble beginnings, and appreciate hearing that.

9 Your testimony talked quite a bit about comparing the  
10 cost of operating a business here in California to other  
11 regions. And you, it wasn't in your testimony because you  
12 don't represent them, but you would agree that dairy farmers  
13 who operate in the State of California face some of these same  
14 challenges of operating a business in California, correct?

15 MR. de CARDENAS: I think anyone operating in California  
16 faces challenges no one else would believe outside of  
17 California.

18 MR. VANDENHEUVEL: So but the position taken in the  
19 testimony advocating for a continuation of the lower regulated  
20 minimum pricing in California, relative to other regions,  
21 wouldn't take into account the fact that California dairy  
22 farmers face some of those same higher costs, wouldn't you say?

23 MR. de CARDENAS: I'm not a dairy, I imagine they have  
24 similar or other issues. I have not run a dairy, so I can't  
25 speak to it.

1 MR. VANDENHEUVEL: But the cost of electricity, certainly  
2 when you get your milk at the plant, that milk is held below  
3 the appropriate temperatures, around 40 degrees, and that takes  
4 electricity to keep that milk at temperature to get it to your  
5 plant, correct?

6 MR. de CARDENAS: Sure, but electricity in a dairy would be  
7 the same rate, but the consumption I think would be far  
8 different. We are A very heavy consumer of electricity. The  
9 rates are probably about the same, but the consumption would be  
10 very, very different. I'm guessing. Again, I haven't run a  
11 dairy, so I can't speak to it.

12 MR. VANDENHEUVEL: I understand. And electricity is just  
13 one cost that businesses face. We would have other costs.  
14 Disposing of manure was referenced yesterday as a major cost  
15 consideration for California dairies, perhaps similar to the  
16 history of trying to dispose of a whey stream, and so it's  
17 different, but there's some similarities in higher cost of  
18 California, correct?

19 MR. de CARDENAS: Yes.

20 MR. VANDENHEUVEL: Okay. I actually had a chance to stop,  
21 and I probably destroyed your product here because it's not  
22 refrigerated, but this is a, actually a 10-ounce container of  
23 your Queso Fresco, and I wanted to just kind of get a couple of  
24 things, ask a couple of questions about this. Now, I bought  
25 this at a local Wal-Mart. As you explained, Wal-Mart would

1 pick up this product at your facility or arrange for  
2 transportation from your facility to their store, or to  
3 distribution, but they pick it up and price it at your  
4 location, correct? It is priced FOB your location, sorry.

5 MR. de CARDENAS: From that perspective, yes.

6 MR. VANDENHEUVEL: Okay. Now, this this particular  
7 container is a 10-ounce container that Wal-Mart extracted \$2.98  
8 out of my pocket, which is a lot of money to a cheap Dutchman  
9 like myself. That's about 29.8 cents an ounce, if I divide  
10 correctly. Which, if you multiply that to come up with a pound  
11 equivalent, I come up with about \$4.77 per pound. Would that  
12 make logical sense, my math of trying to figure that out based  
13 on how I conveyed it just now?

14 MR. MOORE: I'll take your word for it.

15 MR. de CARDENAS: I'll take your word for it.

16 MR. VANDENHEUVEL: \$2.98 on 10-ounce would equate to \$4.77  
17 per pound on a pound. Now, this particular container  
18 identifies what I assume is an expiration date of January 20,  
19 2016. About what is the shelf life of a Queso Fresco product?

20 MR. de CARDENAS: That particular product that we make,  
21 speaking only for our company, is about 102 days from pack.

22 MR. VANDENHEUVEL: About 102 days from pack. And so if I  
23 back out 102 days, or roughly three months and change, this was  
24 probably manufactured sometime in early October, if not late  
25 September is what I'm guessing. That would make sense --



1 MR. de CARDENAS: Yes.

2 MR. VANDENHEUVEL: -- based on that date? Now, in  
3 September, the Class 4b price which would have applied to your  
4 plant at least for the milk used to make this product, was  
5 \$14.94, and included in that calculation was an implied, or it  
6 was a cheddar value from the CME of \$1.66, \$1.66.99 cents per  
7 pound. Now, even though you didn't make cheddar and you had  
8 made another product, your regulated minimum price was still  
9 the same 4b price that every other cheese maker in the state  
10 was, that they were subjected to, correct?

11 MR. de CARDENAS: As far as I know.

12 MR. VANDENHEUVEL: So you don't pay a different Class 4b  
13 price, a different regulated minimum price based on the product  
14 that you make, you pay the state regulated price based on what  
15 CDFA announces every month?

16 MR. de CARDENAS: Correct.

17 MR. VANDENHEUVEL: Now, Wal-Mart doesn't sell your product  
18 for free, and I understand that. There is a margin in there,  
19 and I'm not asking you to divulge that. I understand it would  
20 be proprietary. But it does, is it correct for me to assume  
21 that the price that Wal-Mart paid was north of the \$1.67 CME  
22 cheddar price that was included in the formula for the  
23 September Class 4b price?

24 MR. de CARDENAS: Yes.

25 MR. VANDENHEUVEL: And you also testified in earlier

1 cross-examination, that Queso Fresco is a, what was defined in  
2 that line of questioning, a higher moisture product, and the  
3 definition at that point was a roughly 50 percent moisture  
4 product, and you confirmed in that question that this would  
5 meet that definition pretty close of a higher moisture product?

6 MR. de CARDENAS: Yes.

7 MR. VANDENHEUVEL: And included or embedded into the  
8 Class 4b formula here in California is an assumption that 100  
9 pounds of milk would yield approximately 10 or 10.1 I believe  
10 is the exact number, pounds of cheese. So based on a higher  
11 moisture content, though, would you agree that that process  
12 would yield more than 10.1 pounds of cheese for 100 pounds of  
13 milk?

14 MR. de CARDENAS: On that process, yes.

15 MR. VANDENHEUVEL: It's specific to this product and I know  
16 you --

17 MR. de CARDENAS: Specific to that product, yes.

18 MR. VANDENHEUVEL: Okay. So specific to this product,  
19 well, you know what? I think I have hit the items I wanted to  
20 clarify for the record. So I really appreciate that.

21 How long have you been selling your products outside of  
22 the State of California?

23 MR. de CARDENAS: Since the late '70's, on a very small  
24 scale.

25 MR. VANDENHEUVEL: You've mentioned, if I remember

1 correctly, that your current state approximately 47 percent of  
2 your products are being sold outside the California, correct?

3 MR. de CARDENAS: Yes.

4 MR. VANDENHEUVEL: When would you say, it is such a  
5 subjective term, but when would you say you reached kind of  
6 this higher level? If I said that more than 25 percent of your  
7 product being sold outside of the state was significant, when  
8 would you say you hit that significant level, that you were  
9 selling more than a quarter of your product outside the State  
10 of California?

11 MR. de CARDENAS: I would be guessing.

12 MR. VANDENHEUVEL: Are we talking in the last five years  
13 it's exploded, or it's been a longer term trajectory?

14 MR. de CARDENAS: It's been a longer term trajectory.

15 MR. VANDENHEUVEL: So as you know, California has  
16 maintained a closer relationship in our 4b price relative to  
17 the Federal Order Class III price in the past. It hasn't  
18 always been the \$1.78 per hundredweight that you referenced in  
19 the testimony. During those periods of time in pre-2010, when  
20 our relationship was much closer, roughly 50 cents per  
21 hundredweight average gap, you were able to sell product  
22 outside of the California into the national markets?

23 MR. de CARDENAS: Yes.

24 MR. VANDENHEUVEL: So that smaller gap, that closer  
25 relationship that we saw in the earlier 2000's did not stop you

1 from being able to branch out and sell products outside of the  
2 state?

3 MR. de CARDENAS: No, IT did not.

4 MR. VANDENHEUVEL: I really appreciate your time here. And  
5 I promise to buy one that I'll actually refrigerate and consume  
6 it and look forward to it.

7 JUDGE CLIFTON: Who --

8 MR. HILL: Your Honor, can we take a small break for the  
9 court reporter?

10 JUDGE CLIFTON: Well, not just for the court report, but  
11 yes, we can. So it's almost 4:00, but let's take a 17 minute  
12 break. Please be back and ready to go at 4:00.

13 (Whereupon, a break was taken.)

14 JUDGE CLIFTON: We're back on record at 4:03. Before  
15 resuming examination of the witnesses, I have asked Ms. May to  
16 make an administrative announcement.

17 MS. MAY: Okay. Laurel May. As I mentioned earlier we are  
18 going to move to the Independence Room for tomorrow, Thursday,  
19 and Friday. There is a group using that room tonight until  
20 late, and so the people that run this facility have said that  
21 we can leave our things here, but we need to come tomorrow at  
22 7:30 in the morning and move them over to the Independence  
23 Room. So I would say box it all up and make sure we're ready  
24 to vacate, because they have another group coming into this  
25 room tomorrow at 9:00.

1 JUDGE CLIFTON: That's of course, very good news so that we  
2 don't have to haul everything away. It's particularly good  
3 news for the sound man. All right. And I have homework for  
4 you all. I believe that the mydairyman website is operational.  
5 I believe that you can now find recorded testimony to play. So  
6 I would like you to try it out and see if that's true. So if  
7 you would, please, try tonight [www.my-dairyman.com](http://www.my-dairyman.com). That  
8 particular dairyman publication, the long name of it is  
9 Agribusiness Dairymen, as opposed to, for example, to Hoard  
10 H-O-A-R-D Dairymen. So if you just Google Dairymen, I don't  
11 think the Agribusiness site will be among the first that come  
12 up. So if you will remember, even if you just were to use a  
13 search engine for my-dairyman, I don't think the site you are  
14 looking for would necessarily come up. So you may want to use  
15 [www.my-dairyman.com](http://www.my-dairyman.com), all right.

16 Now, we have three hands up for further questioning.  
17 I'll stat with Mr. Beshore.

18 CROSS-EXAMINATION

19 BY MR. BESHORE:

20 Q. Mr. de Cardenas, this is just a follow up on the whey  
21 question that Mr. Vetne asked. Is the WPC-37 product dry or  
22 liquid?

23 MR. de CARDENAS: Liquid.

24 JUDGE CLIFTON: Your mic wasn't on.

25 MR. de CARDENAS: Liquid.

1 JUDGE CLIFTON: Thank you.

2 MR. BESHORE: Are there multiple options for selling that,  
3 like competing buyers that you can have some options, or how is  
4 that market?

5 MR. de CARDENAS: Right now it is very difficult, very  
6 challenging.

7 MR. BESHORE: To find a buyer?

8 MR. de CARDENAS: Yes.

9 MR. BESHORE: Have there been multiple outlets over the  
10 time you have been producing that product? Multiple buyers,  
11 potential buyers?

12 MR. de CARDENAS: No.

13 MR. BESHORE: You have only ever had one customer?

14 MR. de CARDENAS: We have had two.

15 MR. BESHORE: And how long have you been making that whey  
16 product?

17 MR. de CARDENAS: Just over a year, about 18 months, maybe.  
18 Just shy of 18 months.

19 MR. BESHORE: Okay. Thank you. I think Mr. Vlahos has a  
20 question.

21 JUDGE CLIFTON: Mr. Vlahos?

22 CROSS-EXAMINATION

23 BY MR. VLAHOS:

24 Q. Mr. De Cardenas, just to complete the record. Could  
25 you describe, when the product leaves your plant you cut and

1 wrap it or could you explain what process is used with the  
2 products leaving your plant?

3 MR. de CARDENAS: Leaving the plant?

4 MR. VLAHOS: Well, do you cut and wrap? The package we  
5 see, like Mr. Vandenheuvel brought up, is that how it leaves  
6 your plant?

7 MR. de CARDENAS: That is how it leaves our plant, yes.

8 MR. VLAHOS: Could you describe in general how products in  
9 general leave your plant?

10 MR. de CARDENAS: They leave in a blocks. I'm sorry, I  
11 don't understand your question.

12 MR. VLAHOS: You sold blocks rather than that consumer size  
13 package?

14 MR. de CARDENAS: No, I said a box.

15 MR. VLAHOS: Oh, a box. But they are all in the consumer  
16 size package like that?

17 MR. de CARDENAS: No.

18 MR. VLAHOS: Could you describe how they leave then, other  
19 than that?

20 MR. de CARDENAS: You mean what shape?

21 MR. VLAHOS: Well, in what type of packaging that you use.

22 MR. de CARDENAS: I'm not sure I -- so we have multiple  
23 sizes. They are all in that similar package as a film  
24 overwrap, but in different sizes.

25 MR. VLAHOS: Okay. That's what I wanted to know. And

1 what about shredded products? Do you shred in-house or is that  
2 sent out to shred?

3 MR. de CARDENAS: That's sent out to shred.

4 MR. VLAHOS: Thank you very much.

5 MR. de CARDENAS: You are welcome.

6 JUDGE CLIFTON: Mr. Vetne? No more you say? All right.  
7 Now, are there any other questions? Mr. Hill?

8 MR. HILL: Brian Hill. I don't want to be a math snob but  
9 I'm going to go through this anyway. Can you look at page 4,  
10 please, of your testimony? And this would be the second bullet  
11 point. And you talk about California businesses spending \$3.48  
12 for every \$100 of payroll compared to national mean of \$1.85?  
13 Do you see that?

14 MR. de CARDENAS: I do.

15 MR. HILL: I know there has been much consternation about  
16 doing math here, so I'm going to try to avoid that. But in the  
17 first sentence it says, "Workers' Compensation cost in  
18 California is 180 percent higher than the national mean." I  
19 would suggest there it is 88 percent higher than the national  
20 mean, and not 188 percent higher than the national mean.

21 MR. de CARDENAS: I haven't done the math, so I'll take  
22 your word for it.

23 MR. HILL: A hundred percent would be twice as high and  
24 this isn't quite twice as high, so I believe that it would  
25 probably be 88 percent higher without doing the math.



1 MR. MOORE: I see your point.

2 MR. de CARDENAS: I can see your point, but depends how it  
3 is measured, and I'm not saying it is right or wrong.

4 JUDGE CLIFTON: Okay. That's good. Thank you. That is a  
5 good observation. So it might be 188 percent of the national  
6 mean?

7 MR. de CARDENAS: Depends how it is measured.

8 JUDGE CLIFTON: So that might be how that should read. Why  
9 don't we get it right. Ms. Vulin, if you have got a  
10 calculator, or Mr. English has a calculator, let's get it right  
11 so that it's right.

12 MR. ENGLISH: Well, without looking at a calculator, I  
13 think it could be one of two things. It is either 88 percent  
14 higher or 188 percent of the national mean, and so it could be  
15 worded either way. It seems to me it is either 88 percent  
16 higher or it is 188 percent of the national mean. And those  
17 are the same thing, those work to be the exact same thing.

18 JUDGE CLIFTON: Yeah, but if you don't do the math, we're  
19 not sure.

20 MR. ENGLISH: Well, then, you know what, your Honor? I  
21 have an answer. And I'm serious. We'll take a break for five  
22 minutes with the witnesses to get it done. If we're going to  
23 do math, your Honor, I'm just not prepared to do math on the  
24 witness stand again after what happened last week.

25 JUDGE CLIFTON: That's why I suggested the lawyers do it.

1 MR. ENGLISH: Well, but I don't have my calculator with me  
2 either. You know, one the things we talked about recently  
3 about this issue was that when you are pushing an iPhone, you  
4 don't necessarily know what's going to come up. So, I mean,  
5 I'm happy to take a quick break and we'll come up and fix it.

6 So if you look at the chart in the exhibit, Mr. Yonkers  
7 just helped me out here, who actually hasn't made an appearance  
8 but --

9 JUDGE CLIFTON: Okay. I did the calculation, so, yes, it  
10 is higher, and it is 188 percent of the national mean. So I  
11 can see why you would want the word "higher" in there, so we  
12 can either say 88 percent higher or we can say it is 188  
13 percent of the national mean.

14 MR. ENGLISH: And I'll let the witnesses choose which they  
15 prefer.

16 MR. de CARDENAS: I would say of the national mean.

17 JUDGE CLIFTON: Ms. Elliott, are you on page 4?

18 MS. ELLIOTT: I am.

19 JUDGE CLIFTON: All right. On the second bullet point, the  
20 second line down, it right now starts with "higher than" you  
21 will strike those and just put "of the national mean."

22 MS. ELLIOTT: Okay.

23 JUDGE CLIFTON: Good catch, Mr. Hill. Mr. Vandenheuvel?

24 MR. VANDENHEUVEL: Excuse me, Judge. Rob Vandenheuvel. We  
25 put so much time into an accurate reading, the exhibit actually

1 says it is 188 percent of the study median, and median does  
2 mean something different than mean. I'll let the Economists in  
3 the room explain that difference, but I know that mean and  
4 median are different.

5 JUDGE CLIFTON: And you got the median from where?

6 MR. VANDENHEUVEL: From the actual exhibit from the Oregon  
7 Workers' Compensation, this is Exhibit A, and it is page 2, and  
8 it is the fourth column, fifth column, percent of study median,  
9 not mean. I believe mean is a simple average and median is the  
10 middle, same number of states above and below.

11 JUDGE CLIFTON: That's a very good catch, also. Thank you.  
12 So gentlemen, shall we replace, in Bullet 2, the word "mean"  
13 with the word "median" every place it appears? Which I think  
14 is two places.

15 MR. de CARDENAS: Are you asking us?

16 JUDGE CLIFTON: Yes.

17 MR. de CARDENAS: Yes.

18 JUDGE CLIFTON: All right. Ms. Elliott, would you do that,  
19 please? So you are still on page 4 and you are in the second  
20 bullet point and you are just replacing M-E-A-N, with  
21 M-E-D-I-A-N.

22 MS. ELLIOTT: Okay.

23 JUDGE CLIFTON: Good. Thank you. Yes. Actually, I really  
24 appreciate these changes. We do require precision. Okay.  
25 Good. Who else would like to ask questions or raise issues?

1 All right. Redirect?

2 REDIRECT EXAMINATION

3 BY MS. VULIN:

4 Q. Ashley Vulin.

5 So still here on page 4. Mr. Vandenheuvel had asked  
6 you that when the Class III and 4b prices were closer, you were  
7 still selling your products out-of-state. But in looking at  
8 this formula which takes into account freight, and operating  
9 costs, and price, milk price gap, is it not true that at that  
10 time both the freight and the operating costs would have also  
11 been different?

12 MR. de CARDENAS: Correct.

13 MS. VULIN: So the cost for gas might have likely been  
14 lower back then?

15 MR. de CARDENAS: Yes.

16 MS. VULIN: Also the cost of labor likely lower?

17 MR. de CARDENAS: Yes.

18 MS. VULIN: So we really can't conclude anything about the  
19 output number of that formula just by knowing the change in the  
20 single variable?

21 MR. de CARDENAS: Correct.

22 MS. VULIN: Mr. Vandenheuvel also asked you about the  
23 cheddar value from September in 2015, which he represented  
24 being \$1.69.99 cents. When making Hispanic cheese, as opposed  
25 to bulk cheddar, are you handling much smaller volumes?

1 MR. de CARDENAS: Yes, we are.

2 MS. VULIN: So you lack some of the economies of scale that  
3 bulk cheddar processing would have?

4 MR. de CARDENAS: Very much so.

5 MS. VULIN: And you have more handling, you have more  
6 packaging, more operational costs?

7 MR. de CARDENAS: All of the above. We're a specialty  
8 cheese maker, we'll make five or six different cheeses on one  
9 day with a same vats. So there are, there is a lot of lost  
10 efficiency as a result, compared to a cheddar plant or a pure  
11 Mozzarella plant or something like that.

12 MS. VULIN: So just looking at this \$1.69.99 cents, that  
13 can't tell us everything we need to know about your costs are?

14 MR. de CARDENAS: That's correct.

15 MS. VULIN: And, lastly, we have talked a lot about the  
16 sales of your products out-of-state, particularly to the East  
17 Coast, and we have been focusing a lot on transportation costs.  
18 But there are other increased costs you face when selling on  
19 the East Coast; is that not correct?

20 MR. de CARDENAS: We've got to introduce our brand, so  
21 there is a lot of marketing that goes into it. For example,  
22 the store locator was actually created as an advance into the  
23 East Coast to make it easier for consumers to find us in an  
24 area that we weren't normally known to be in. So there are a  
25 lot of marketing expenses to go into new markets.

1 MS. VULIN: No further questions. Thank you, your Honor.

2 JUDGE CLIFTON: Thank you, Ms. Vulin.

3 Mr. de Cardenas, do you have anything you would like to  
4 add before you step down?

5 MR. de CARDENAS: No, I don't.

6 JUDGE CLIFTON: Mr. Moore, do you have anything you would  
7 like to add before you step down?

8 MR. MOORE: No, just one comment on the \$1.69. That's  
9 that's a 40 pound block of cheese, and it is usually a cheddar  
10 plant and that's all they do. But like I said, we're, we make  
11 multiple products everyday in small batches, so it's a  
12 completely different world.

13 JUDGE CLIFTON: Thank you. You both may step down and I  
14 thank you both very much for this contribution to our evidence  
15 and to our awareness of all the diversity within the industry.  
16 Thank you.

17 MR. de CARDENAS: Thank you very much.

18 MR. MOORE: Thank you very much.

19 MR. ENGLISH: Good afternoon again, your Honor.

20 Chip English. Yesterday we had a short statement from  
21 Mr. Zolin that's Exhibit 106. And although it was a short  
22 statement, he had not had any cross-examination with respect to  
23 Exhibit 106. And so we would have him come to the stand at  
24 this time.

25 JUDGE CLIFTON: Mr. Zolin, you remain sworn. Would you

1 again state and spell your name?

2 MR. ZOLIN: Alan Zolin. A-L-A-N, Z-O-L-I-N.

3 JUDGE CLIFTON: Thank you. Mr. English, is there anything  
4 you want to ask him before cross-examination begins?

5 CONTINUED DIRECT EXAMINATION

6 BY MR. ENGLISH:

7 Q. Just a -- since it was yesterday, almost 24 hours ago,  
8 maybe just summarize a little bit that, Mr. Zolin, there are  
9 provisions that appear in Proposal 2 that do not point back to  
10 Part 1000 because we, as a group, either added a provision for  
11 9(d), correct --

12 A. Correct.

13 Q. -- which you are going to talk about in later  
14 testimony?

15 A. Correct.

16 Q. And/or, because sometimes it was in both, there was a  
17 reference to the old terminated Western Order that we, for sort  
18 of conforming changes purposes, deleted, correct?

19 A. Correct.

20 Q. Okay. And so for instance, last night, when, maybe it  
21 was this morning I have forgotten, when we were looking at this  
22 Section 76, the partially regulated plant provision is one of  
23 those, for instance, that is, we don't have pointing back to  
24 Part 1000, correct?

25 A. That is correct.

1 Q. And that is because in the calculations under both  
2 paragraph A and paragraph B we inserted a reference to 9(d),  
3 correct?

4 A. That is correct.

5 Q. Your Honor, that does complete my direct examination  
6 and the witness is available, and I believe we did admit  
7 Exhibit 106 yesterday.

8 JUDGE CLIFTON: All right. Thank you, Ms. Elliott?

9 MS. ELLIOTT: Yes.

10 JUDGE CLIFTON: Thank you. Yes, it is admitted. Who would  
11 like to ask the first questions of Mr. Zolin on this exhibit.  
12 I don't mean just on the exhibit, but on this topic.  
13 Mr. Beshore?

14 CROSS-EXAMINATION

15 BY MR. BESHORE:

16 Q. Thank you, your Honor. Marvin Beshore.

17 Just a couple of questions, Al. The 9(d), can you tell  
18 us where all that is now referenced? I don't want to go into  
19 it, but I would like to know where all it pops up, if you can  
20 tell me?

21 A. Okay. As far as every provision, every section in  
22 Proposal 2, I cannot, off the top of my head, I'll have to kind  
23 of scan through. But certainly I do know, in the pool plant  
24 definition 7, it's mentioned a number of times, specifically in  
25 paragraph C and further through it. Then, of course, in



1 paragraph 9, it's a whole new section, paragraph 9(d). I guess  
2 the easiest way for me to say it, is wherever the letters 9(c)  
3 show up, which is Cooperative pooling handler, you will see and  
4 9(d) following after it. So wherever a pool plant is referred  
5 to, you will see the insertion of 9(d), and that carries pretty  
6 much through quite a few of the provisions in the Order.

7 Q. Okay. Basically that's how it was, every place you saw  
8 the 9(c) you added 9(d), basically?

9 A. And I know that the people that are computer whizzes  
10 just did exactly that, tracked where 9(c) was, we looked to see  
11 if 9(d) was appropriate to put right after that, and if it was,  
12 we did.

13 Q. Okay. So one other question, I think. With respect to  
14 1051.51 and .52, I think .52, which is the 1000.52, Class 1  
15 differential surface, that is, you're adopting that? You are  
16 adopting that as it is in part 1000?

17 A. Let me find what it says in our -- we have a Section  
18 1051.51 in Proposal 2, so it is not referring back to Proposal  
19 1000.

20 JUDGE CLIFTON: He asked about 52 rather than 51, didn't  
21 you, Mr. Beshore?

22 MR. BESHORE: I was going backwards. I saw the 52 first.

23 MR. ZOLIN: 52 is part of the Section 1000 where we made no  
24 changes.

25 BY MR. BESHORE:

1 Q. Okay. But 51 is language which you have, which you  
2 have crafted for Proposal 2?

3 A. Correct.

4 Q. And 51 doesn't propose, just so I'm clear about this, I  
5 think it seems pretty straightforward, but I need to be sure.  
6 51 doesn't propose any changes to 52, to Uniform Section 52?

7 A. Mr. Beshore, I have not looked that specifically at 51.  
8 If you give me a second and let me read it. I believe this is  
9 putting Los Angeles as the center of the marketplace, looks  
10 like Chicago is in Order 30.

11 Q. Okay. And the Los Angeles price is as provided under  
12 Uniform 1000.52?

13 A. Correct.

14 Q. I think that's all I have. Thank you, Al.

15 JUDGE CLIFTON: Who next would like to ask questions of  
16 Mr. Zolin? Mr. Francis?

17 CROSS-EXAMINATION

18 BY MR. FRANCIS:

19 Q. Will Francis, USDA.

20 I just want to clarify. In your statement on page 1,  
21 down at the bottom under that "Purpose" section, you refer to  
22 "Proposal 2 incorporates with no changes Sections 2 through 6."  
23 And so typically in the individual orders, Section .2, if you  
24 go to like 1001.2, 1030.2, it is the description of the  
25 marketing area, so it lays out the geography. But if you go to

1 1000.2, I don't know if you have a Code book with you?

2 A. I do have one up here.

3 Q. So in Part 1000.2 there's a section for general  
4 definitions.

5 A. I see that.

6 Q. And so we're just wondering which part 2 you are  
7 referring to.

8 A. Well, from a standpoint, definitely the general  
9 definitions is what we are referring to. And I see in our  
10 proposal we do have the California marketing area, so that's,  
11 you know, identifying it for Federal Order 51. So I guess I  
12 said the .2, I was referring to that Section 100, general  
13 definitions.

14 Q. I think that clarifies it, but I'm just wondering if  
15 we're missing including something when we adopt, you know, part  
16 51. If we're missing .2 under 1000.2.

17 A. Yes, I would agree with that.

18 Q. Okay.

19 A. I think it was one of those, as you are looking through  
20 all the numbers, you tend to maybe overlook one.

21 Q. Okay. And then just one additional question, on page 2  
22 where you're referencing 1000.14 with what you call the cleanup  
23 language because of the termination of Order 135. Just want to  
24 clarify, it's not your intention to open up other sections of  
25 Part 1000?

1 A. No, it is not.

2 Q. It is just strictly clean up for the California Order?

3 A. Correct. Since we were writing a new order, we felt  
4 let's use that opportunity as we bring it into the order to not  
5 duplicate that language for a terminated order so, correct.

6 Q. So you are proposing a 1051.14 and not changing  
7 Part 1000?

8 A. Correct.

9 Q. Got it. That's all we have. Thank you.

10 JUDGE CLIFTON: Mr. English?

11 REDIRECT EXAMINATION

12 BY MR. ENGLISH:

13 Q. Thank you, your Honor, let me see if I can clarify and  
14 not unclarify.

15 So let me start where we just ended. Part 1000, there  
16 was a Part 1000 before Federal Order Reform, correct

17 A. Correct.

18 Q. Okay. But after Federal Order Reform, it was greatly  
19 expanded to include a number of other provisions, correct?

20 A. Correct.

21 Q. So we understood that we were not, and frankly, going  
22 back to the very first day of this hearing, Part 1000 is not  
23 open for this proceeding, correct?

24 A. Correct.

25 Q. Okay. So if there's going to be a difference between

1 what I call the point, that is to say if an Order like  
2 Order 30, for Section 8, which is a definition of a nonpool  
3 plant, with the Order points back to part 1000, what it does is  
4 it's really incorporated by reference the Part 1000 language,  
5 correct?

6 A. Correct.

7 Q. So where we weren't incorporating by reference because  
8 we're making a change, we didn't do so, and therefore we have  
9 special language, correct?

10 A. Correct.

11 Q. Okay. So I hope that clarifies that. So now let's go  
12 to the general provisions, and maybe it's my fault for not  
13 noticing Section 2, because I think maybe if we took 2 out we  
14 wouldn't have a problem. If you look at both Proposal 1 on  
15 page 47211 of Exhibit 1, and Proposal 2, 47219, they each have  
16 a Section 1. And Section 1, amazingly enough, we agree, is,  
17 actually incorporates the terms and definitions in Part 1000,  
18 which I would take, Mr. Zolin, would mean that the 1000.2 is  
19 being incorporated in both Proposals 1 and 2?

20 A. That is correct.

21 Q. Okay. And finally, and I would put this under the most  
22 picayune point of the day, in response to a question from  
23 Mr. Beshore, I think you said initially, that wherever you said  
24 9(c) it was, you said and 9(d). But I think you really had or  
25 9(d); is that correct?

1 A. Yes. That is, in some places we may have put and, but  
2 you are right. We looked for 9(c) and then followed it with a  
3 9(d) right after.

4 Q. Okay. And since Exhibit 1 is searchable, people could  
5 search for where 9(d) is, since it does appear a number of  
6 times, correct?

7 A. I learned that today.

8 Q. Okay. So that's all the questions I have. And I hope  
9 that helped, Mr. Francis, in answering especially those  
10 questions you had on that.

11 JUDGE CLIFTON: Does anyone else have questions for  
12 Mr. Zolin? There are none. Mr. Zolin, thank you. You may  
13 step down. Did you want to add something?

14 MR. ZOLIN: I'm getting a shake of no, so I will step down.

15 JUDGE CLIFTON: You thought you wanted to add something?

16 MR. ZOLIN: I was kind of thinking we might, we have,  
17 unless Mr. English has something else planned.

18 MR. ENGLISH: Not for you.

19 MR. ZOLIN: The follow up questions for Mr. DeJong or is  
20 that tomorrow?

21 MR. ENGLISH: No.

22 JUDGE CLIFTON: Thank you so much. Before we have the next  
23 witness I would like to take a dead fly count? The answer was  
24 two flies and one mosquito. We were entirely scoreless up here  
25 at the witness and Judge's table.

1 MR. ENGLISH: So your Honor, although -- Chip English --  
2 although it is far from ideal, and I would not that at least  
3 once during the co-ops presentation we didn't put a significant  
4 witness on at 4:30. I'm prepared to go ahead and get started.  
5 Obviously we have 21 minutes before we do administrative  
6 things.

7 So the next witness, would be then, Mr. Rob Blaufuss.  
8 I did manage to get him on tomorrow, today, whatever it is, for  
9 Dean Foods. And he has a statement and exhibits.

10 JUDGE CLIFTON: Good. All right. I'm very pleased. I  
11 really am amazed that all of you are able to cross-examine with  
12 so little time with the exhibits. And this is helpful that we  
13 have it overnight.

14 MR. ENGLISH: Let's be clear, what's being passed out is  
15 one document, they both look very similar, but one says  
16 Testimony of Rob Blaufuss, Part 1 and the other one says  
17 Exhibits of Rob Blaufuss, Part 1, but both have the caption of  
18 our proceeding.

19 JUDGE CLIFTON: Raise your hand if you still need copies.  
20 It appears everyone has. Which one would be the first to be  
21 numbered, Mr. English?

22 MR. ENGLISH: Your Honor, the testimony of Rob Blaufuss  
23 will be the first exhibit.

24 JUDGE CLIFTON: Ms. Elliott, will that be 109?

25 MS. ELLIOTT: That's correct.

1 JUDGE CLIFTON: Testimony will be Exhibit 109. 109. The  
2 exhibits will be 110. 110.

3 (Thereafter, Exhibit 109 and Exhibit 110,  
4 were marked for identification.)

5 JUDGE CLIFTON: Mr. Blaufuss, is this the first time you  
6 have testified in this proceeding?

7 MR. BLAUFUSS: It is, yes.

8 JUDGE CLIFTON: I'll swear you in in a seated position. If  
9 you would raise your right hand, please.

10 Do you solemnly swear or affirm under penalty of  
11 perjury that the evidence you will present will be the truth?

12 MR. BLAUFUSS: Yes.

13 JUDGE CLIFTON: Thank you. Please state and spell your  
14 name.

15 MR. BLAUFUSS: My name is Rob Blaufuss, B-L-A-U-F-U-S-S.

16 JUDGE CLIFTON: Thank you. Mr. English, you may proceed.

17 DIRECT EXAMINATION

18 BY MR. ENGLISH:

19 Q. Thank you, your Honor.

20 Mr. Blaufuss, why don't you read paragraph 109, and as  
21 with other witnesses, I'll interrupt you and discuss a few  
22 issues about your background?

23 A. Okay. First is the introduction. Like I said, my name  
24 is Rob Blaufuss and I am currently employed by Dean Foods as  
25 the Senior Manager of Dairy Risk Management and Economics. My



1 business address is located at 2711 North Haskell Avenue,  
2 Dallas, Texas, 75204. Dean Foods is the largest fluid milk  
3 processor in the U.S., with 67 plants in 32 states. While  
4 fluid milk represents the bulk of Dean Foods' business, we also  
5 manufacture ice cream, cultured products, juices, and teas. We  
6 own and operate three bottling plants located in the State of  
7 California; Berkeley Farms, which serves Northern California;  
8 and Alta Dena and Heartland Farms, both of which serve  
9 Southern California. Dean also has one ice cream plant located  
10 in Buena Park.

11 Q. So Mr. Blaufuss, what's your educational background?

12 A. I have my undergraduate degree in Agricultural  
13 Economics with a minor in Political Science from the  
14 North Dakota State University and Fargo, North Dakota. I went  
15 on and got my Master's degree also in Agricultural Economics  
16 from the University of Illinois, at Urbana-Champaign.

17 Q. And other than educational background, what  
18 agricultural background did you have before any professional  
19 employment, after getting your Master's?

20 A. After getting my Master's --

21 Q. No, before getting your Master's, I'm sorry.

22 A. Before? Well, I was born and raised on a small family  
23 farm in West Central Minnesota. If want to put a map down,  
24 about 45 minutes south of Fargo. Obviously, I have lived at  
25 home for quite awhile, my accent has been desensitized quite a

1 bit.

2 Q. So you say.

3 A. Or at least I think it has. But we had, we produced  
4 corn, soy beans, wheat. We also had about four to five hundred  
5 head farrow-to-finish hog facility as well. The hogs quickly  
6 left, as I, the youngest in the family, went off to school, as  
7 animal agriculture sometimes tends to do.

8 JUDGE CLIFTON: What type of hogs were they?

9 MR. BLAUFUSS: Farrow-to-finish, from birth to culling,  
10 I'll say.

11 JUDGE CLIFTON: Thank you.

12 BY MR. ENGLISH:

13 Q. So what is your employment background, other than on  
14 the farm?

15 A. So I guess I'll say the first employment I had is in  
16 between my Junior and Senior year at NDSU I actually had the  
17 opportunity to be an intern at the U.S. Senate, under former  
18 Senator Kent Conrad of North Dakota. And actually once I  
19 finished, that kind of spurred my interest in wanting to get  
20 back to DC, which is what led me to, after I graduated with my  
21 Master's of going to IDFA in 2008 after I graduated.

22 Q. And what is IDFA?

23 A. The international Dairy Foods Association. So the  
24 Dairy processor lobby group located in Washington DC.

25 Q. Trade association?

1 A. Correct.

2 Q. Okay. And what your duties at the International Dairy  
3 Foods Association?

4 A. So my primary responsibilities, perform economic  
5 research and analysis to assist in strategy and policy making.  
6 Also, monitoring domestic international trends to help, you  
7 know, members stay informed of what was going on in the  
8 marketplace.

9 Q. And how long were you at the International Dairy Foods  
10 Association?

11 A. About two and a half to three years. Two and a half,  
12 if you want to get specific.

13 Q. And after IDFA, where did you go?

14 A. So I went to Dean Foods, which would have been just  
15 after the first of the year, or I guess March is when I started  
16 in 2011, which is where I have been since.

17 Q. And what is your job title -- what have your job titles  
18 been and what is your job title today at Dean Foods?

19 A. So I joined Dean Foods as the Manager of Dairy Policy  
20 and Economics, and in 2013 took on the responsibility of  
21 managing price risk, dairy price risk for the company as well.

22 Q. And you are here testifying today on behalf of  
23 Dean Foods?

24 A. That's correct.

25 Q. All right. Why don't you continue with your statement?

1 A. All right. Title:

2 Disorderly Marketing, or Lack Thereof

3 The Proponents of Proposal 1 spent a great deal of time  
4 testifying to the regulated price differences between  
5 California State Order and the Federal Orders. However, there  
6 was minimal data put into the record as to how these price  
7 differences have led to inefficient movements of milk, both in  
8 and out of the state. While differences in regulated prices  
9 have the potential to cause disorderly marketing conditions,  
10 the mere fact that prices are different does not alone indicate  
11 disorderly marketing conditions.

12 The declared policy goals of the Agricultural Marketing  
13 Agreement Act of 1937, the Act which provides for the forming  
14 of FMMO's, are to, "establish and maintain such orderly  
15 marketing condition for any agricultural commodity enumerated  
16 in Section 8c(2) (the section which includes milk) as will  
17 provide in the interest of producers consumers, in orderly flow  
18 of the supply thereof to market throughout its normal marketing  
19 season to avoid unreasonable fluctuations in supplies and  
20 price." With these goals in mind, Federal Milk Marketing  
21 Orders have sought to ensure the stable supply of milk to the  
22 market. Historically speaking, this has routinely,  
23 consistently and only been interpreted to mean milk for fluid  
24 purposes.

25 While milk production in California has experienced

1 year-over-year declines throughout January through September  
2 2015, Dean Foods has not experienced problems of procuring an  
3 adequate supply of milk for our manufacturing facilities in the  
4 state. Historically we have felt comfortable with the amount  
5 of milk available to Class I bottlers, as well as with the  
6 level of reserve supply which stands ready to meet the needs of  
7 Class I handlers. Consumers have experience no interruptions  
8 in their ability to buy fresh, safe, and wholesome fluid milk  
9 products.

10           Currently, however, we are experiencing a significant  
11 milk supply issue. For the past two weeks we have struggled to  
12 source an adequate supply of milk for our Southern California  
13 facilities. We have reached out to all the major Cooperatives  
14 in the state, as well as others, and found a limited response  
15 to make milk available. The severity of our current issue was  
16 such that the idea of asking for enacting the call provision in  
17 the State's statute was raised as an option. Thus far we have  
18 focused on the commercial options available to us, allowing the  
19 market to work. We think others could be having challenges as  
20 well. For legal reasons, we have not worked to find out what  
21 is happening with our competitors. We have been in discussion  
22 with CDFA staff around how this provision would ultimately  
23 work. Our current expectation is that our milk supply issue  
24 will last at least another two weeks. Should our supply issue  
25 not improve in the coming weeks, we could still yet file a call

1 petition with the State.

2 I will admit that a significant portion of our current  
3 predicament comes as a result of the rain and subsequent  
4 mudslides which impacted the state two weeks ago. Issues will  
5 always arise when one is dealing with production agriculture.  
6 Things happen, from natural disasters, to farm production  
7 issues, to differing consumer trends. An individual Market  
8 Administrator has limited tools at their disposal to ensure an  
9 adequate supply of fluid milk to Class I handlers, with the  
10 main tool being the ability to adjust shipping percentage  
11 requirements. In the past, Market Administrators have used  
12 this provision, a provision that is uniform to all Federal  
13 Orders, to adjust the amount of milk supply plants must ship to  
14 Class I plants. Dean believes it is critical that the Federal  
15 Order language provide the Market Administrator the discretion  
16 to make changes to shipping percentages without requiring the  
17 administrative process of a Federal Order hearing. Changes  
18 happen quickly in the dairy industry, and responses are needed  
19 in like fashion. In failing to include any shipping  
20 requirements in their California Federal Order proposal, the  
21 Proponents of Proposal 1 have eliminated the Market  
22 Administrator's main tool in the toolbox.

23 Dean Foods procures, manufactures, and sells a  
24 significant amount of milk in the State of California. We are  
25 actively engaged in the California dairy market. Our milk

1 supply is sourced through both direct supply and through  
2 cooperative suppliers. All milk used in our fluid plants  
3 located in the state is sourced from California producers. We  
4 do not typically import bulk milk into our plants from  
5 out-of-state producers. A significant portion of our milk  
6 supply comes from producers located within a hundred miles of  
7 our bottling plants. At our Alta Dena facility, 54 percent of  
8 our raw milk supply is located within a hundred miles of the  
9 plant, with the remainder the milk located 250 miles or less  
10 from the facility. A map of our Alta Dena milk supplies can be  
11 found in Figure 1. At our Berkeley Farms facility, 99 percent  
12 of the milk is sourced from locations within a hundred miles  
13 from the plant, with the remaining one percent located within  
14 250 miles. The sourcing footprint for this facility is  
15 highlighted in Figure 2. As for Heartland Farms facility, 99  
16 percent of the monthly milk supply comes from sources 250 miles  
17 or less from the plant, with one percent of the plant's total  
18 milk supplies located within a hundred miles of the facility.  
19 The supply locations for Heartland is located in Figure 3.

20 JUDGE CLIFTON: Is what?

21 MR. BLAUFUSS: Is provided, thank you, in Figure 3. The  
22 milk supply geographies in Figures 1 through 3 was reflective  
23 our milk supplies as of June 2015.

24 BY MR. ENGLISH:

25 Q. As long as you are taking a break, let me take a break.

1 When you referenced the figures, you are referring to  
2 Exhibit 110?

3 A. That's correct.

4 Q. And this shows how production difficulties can go.  
5 When I look at Exhibit 110, I looked in vain for Figures 1, 2,  
6 and 3. So why don't we, while we're there, obviously, the  
7 cover sheet of Exhibit 110 is not what you are referring to.  
8 So the next page from the cover sheet, which in most copies is  
9 front and back, which says Alta Dena map in the upper left hand  
10 corner, and the color versions have red circles, that would be  
11 Figure 1?

12 A. Correct.

13 Q. And then the next page which says Berkeley Farms map,  
14 and has blue circles, that would be what should be labeled as  
15 Figure 2?

16 A. That is correct.

17 Q. And then finally, the page that's on the back, for  
18 those that have front and back, Figure 2 is the Heartland map,  
19 and I believe I'm not color blind, I believe those are orange  
20 circles, and that should be Figure 3; is that correct?

21 A. That is also correct.

22 Q. Your Honor, if we could have that marked for the record  
23 copies.

24 JUDGE CLIFTON: Yes, I would like Ms. Elliott to do that.  
25 I wonder, Mr. English, where you suggest she write.



1 MR. ENGLISH: Well, I would say either the bottom left hand  
2 corner, I think about the left hand corner may be best, because  
3 that's away from the staple, but I will let her decide what's  
4 best, but I wrote mine on the bottom left hand corner of each  
5 of those, because when you turn the maps horizontally, I sort  
6 of just looked at that way. So I would think the bottom left  
7 hand corner would be the logical place to put Figure 1,  
8 Figure 2, and Figure 3.

9 JUDGE CLIFTON: I agree. And I like that she would hold it  
10 horizontally the way you would be looking agent the map.

11 MS. ELLIOTT: Okay.

12 JUDGE CLIFTON: All right. So Figure 1 is the first one,  
13 Figure 2 is the second one, and Figure 3 is the third one.

14 MR. ENGLISH: And again, the first one is Alta Dena, red  
15 circles; the second one is Berkeley Farms, blue circles; third  
16 one is Heartland map, orange circles.

17 Ms. Elliott, does that all work for you?

18 MS. ELLIOTT: Yes.

19 JUDGE CLIFTON: Okay.

20 MR. ENGLISH: I'm sorry to interrupt, but I figured this  
21 was the best time to do that.

22 JUDGE CLIFTON: I agree.

23 BY MR. ENGLISH:

24 Q. All right. If you could continue with your testimony  
25 on page 5, Mr. Blaufuss.

1       A. All right. We have been given no indication from  
2 either our direct shippers or our cooperative suppliers,  
3 instances of chaotic and inefficient movements of milk  
4 occurring in California. Significant changes in premiums paid  
5 in excess to the regulated classified minimum prices, can often  
6 be indicative of disorder in a Marketing Order. Our California  
7 Class 1 over order premiums have remained steady for quite some  
8 time. As a manufacturer of Class 1, 2, and 3 products in the  
9 State of California, I can tell you that we do not view current  
10 milk marketing conditions in California to be disorderly. The  
11 conditions, as we see them, can only be described as orderly.

12             In is opening statement, Mr. Hollon discussed in detail  
13 the regulated price differences between Federal Order Class II  
14 and California Class 2 and 3 prices. However, the comparison  
15 between FMMO regulated minimum prices for Class II, and  
16 California Class 2 and 3 is not an apples to apples comparison.  
17 The cities mentioned as destination points for condensed skim,  
18 Denver, Kansas City, and Nashville, are all areas regulated by  
19 the Federal Order system. What the Proponents of Proposal 1  
20 fail to mention is that current Federal Order language allows  
21 all Class II, III, and IV plants to depool from their  
22 respective orders when there are economic incentives to do so.  
23 Nonpool plants, per FMMO provisions, are not required to pay  
24 the regulated minimum class prices. The Cooperatives simply  
25 call out September 2014 as a month with a wide disparity of

1 \$2.14 per hundredweight between Federal Order regulated minimum  
2 Class II prices and California Class 2 prices. The Class II  
3 plants located in Federal Order 32, the Order in which both  
4 Denver and Kansas City are located, would have had very little  
5 incentive to be in the pool in September 2014. The regulated  
6 minimum Class II price in September 2014 was \$26.11 per  
7 hundredweight. The FMMO blend price at base zone differential  
8 for the month was \$24.83 per hundredweight.

9 Q. Would you either re-read the sentence or I think you  
10 omitted the number 32. You said the FMMO blend price, so why  
11 don't you re-read the sentence, Mr. Blaufuss?

12 A. All right.

13 The FMMO 32 blend price at base zone differential for  
14 the month was \$24.83 per hundredweight. A Class II plant  
15 located in Kansas City, Missouri, which happens to be the base  
16 zone location for Federal Order 32, would have chosen to depool  
17 in an effort to avoid having to pay \$1.28 per hundredweight  
18 into the Federal Order 32 pool. A Class II plant in Denver  
19 would have depooled from Federal Order 32 to avoid paying into  
20 pool a location adjusted 73 cents per hundredweight. A  
21 Class II plant in Nashville would have been, would be regulated  
22 under Federal Order 7. A high Class I utilization in this  
23 Order ultimately means the Class II plants would nearly always  
24 choose to remain in the pool due to the higher blend prices  
25 enjoyed in that area of the country.

1 JUDGE CLIFTON: Now, let me stop you. I just want to do a  
2 couple of words. Right there where you just read, we're on  
3 page 6 of Exhibit 109. And I want you to look at that  
4 sentence, the sentence begins "the high Class I utilization" so  
5 read that slowly and tell me if words need to be added? It  
6 starts about five lines down at the end of the line.

7 MR. BLAUFUSS: The high Class 1 utilization in this Order,  
8 ultimately means that Class II plants would nearly always  
9 choose to remain -- to remain pooled due to the higher blend  
10 prices enjoyed in that area of the country.

11 JUDGE CLIFTON: So you think we just need to add an "ed" to  
12 the word pool?

13 MR. BLAUFUSS: No, actually take the "remained" out, choose  
14 to pool due to the higher.

15 MR. ENGLISH: Well, then you need a be to be pooled, it's  
16 either remain pooled, or to be pooled.

17 MR. BLAUFUSS: Nearly always choose to pool due to the  
18 higher blend price.

19 MR. ENGLISH: I'm wrong.

20 MR. BLAUFUSS: Doing this on the fly.

21 JUDGE CLIFTON: You have been talking about incentives to  
22 not be pooled, but with this sentence there's an incentive to  
23 pool.

24 MR. BLAUFUSS: That is correct.

25 JUDGE CLIFTON: Okay. So "would nearly always choose to

1 pool" so we just strike the word "remain".

2 MR. BLAUFUSS: That is correct.

3 JUDGE CLIFTON: Ms. Elliott, do you see?

4 MS. ELLIOTT: Yes.

5 JUDGE CLIFTON: All right. So we'll strike that word  
6 "remain", that's 2, 4, 6, 7 lines down on page 6, and then on  
7 the prior page, I hope I can find it.

8 MR. BLAUFUSS: The \$2.14 per hundredweight?

9 JUDGE CLIFTON: Yes.

10 MR. BLAUFUSS: Yeah, I caught that last night, and I  
11 figured since we made 40 copies, I would rather just change the  
12 word doing it this way rather than printing another 40 copies.

13 JUDGE CLIFTON: I agree. Are you ready, Ms. Elliott, for  
14 the other one? You are on page 5, and you go up 5 lines, and  
15 Mr. Blaufuss, what do you want her to do on that line?

16 MR. BLAUFUSS: So after the \$2.14 and before the  
17 hundredweight put "per".

18 JUDGE CLIFTON: So we're inserting "PER". Good.

19 MR. BLAUFUSS: And if you want to work ahead and be  
20 studious, there's also one other correction that I note.

21 MR. ENGLISH: Well, I was just going to say why don't we, I  
22 mean, it is now 4:56.

23 JUDGE CLIFTON: Remember that, Mr. Blaufuss, for tomorrow.

24 MR. BLAUFUSS: Made a mental note.

25 JUDGE CLIFTON: Very good. So, yes, if we're going to give

1 you anytime at all, Mr. English, to give us a preview, it  
2 should be now.

3 MR. ENGLISH: So your Honor, tomorrow for the 25th day of  
4 the hearing, we, well obviously Mr. Blaufuss is on the stand  
5 and will return, although, I do understand that Mr. Ahlem,  
6 thanks to all our good wishes and everything, was able to not  
7 get on a jury today, so I believe that he will be here and I  
8 just don't know what time. But we absolutely commit that he  
9 gets priority slot tomorrow. And so Mr. Ahlem would be on the  
10 list, along with Mr. Blaufuss. We may have a witness on a  
11 policy history, sort of ala Paul Christ. We have Dr. Schiek  
12 expected to return to the stand with respect to pooling.  
13 Mr. Zolin with respect to pooling/7(c), and then we'll see  
14 where we go from there. I know I keep mentioning Ms. Taylor, I  
15 don't think she's going to be on tomorrow.

16 JUDGE CLIFTON: All right. Now, the person who is like  
17 Mr. Christ, who is that person?

18 MR. ENGLISH: Your Honor, it hasn't been decided yet  
19 whether it is definitely going to happen, until I know what's  
20 definitely going to happen, even as with Mr. Christ, who we  
21 didn't know his name before he got on the stand, or Mr.  
22 Hatamiya, until I know for sure we are going to do it, I'm not  
23 yet prepared to say.

24 JUDGE CLIFTON: All right. And did you say he's a policy  
25 person or history?

1 MR. ENGLISH: Policy history, USDA policy history.

2 JUDGE CLIFTON: Perhaps.

3 MR. ENGLISH: Yeah.

4 JUDGE CLIFTON: Okay. All right. That sounds excellent.

5 I would like to ask you all, since we need to be here at 7:30  
6 to move everything out of here, if you prefer to take it with  
7 you, no, Ms. May, an update?

8 MS. MAY: Yes. Laurel May. I don't think everybody needs  
9 to be here at 7:30. Somebody from your, group, if you leave  
10 stuff behind, needs to be here to move it out, but we're, for  
11 instance, we're going to box all of our stuff up and get it  
12 ready to go

13 JUDGE CLIFTON: You are going to box up tonight.

14 MS. MAY: Because we have to take the wires and all of that  
15 stuff. So if you get here by 8:30 and are completely out of  
16 here by 9:00, I think we'll be good tomorrow.

17 JUDGE CLIFTON: So the people that are going to be in here  
18 beginning at 9:00, how much set up do they need?

19 MS. MAY: I was told that they are coming at 9:00, so we  
20 need to be gone before they get here.

21 JUDGE CLIFTON: Okay.

22 MS. MAY: So I will leave that up to you to figure out how  
23 long it is going to take you to de-camp. But AMS, we have got  
24 it down.

25 JUDGE CLIFTON: Great. Okay. But you would like to see

1 one member of each group, if they leave things here tonight, at  
2 7:30.

3 MS. MAY: Right. If not, we'll see you at Independence  
4 tomorrow morning.

5 JUDGE CLIFTON: All right. So if you want to take your  
6 things with you, those of you who have been issued fly  
7 swatters, you are in charge of keeping them and transporting  
8 them. All right.

9 So we look forward to going on the record at 9:00  
10 tomorrow, but you are welcome to come as early as 8:00, we  
11 expect some of you to be here at 7:30. Thank you.

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DATED:           December 4, 2015  
                      FRESNO, CALIFORNIA



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