

UNITED STATES DEPARTMENT OF AGRICULTURE

BEFORE THE SECRETARY OF AGRICULTURE

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

VOLUME XXXIII

TRANSCRIPT OF PROCEEDINGS

November 9, 2015

Myra A. Pish, CSR No. 11613

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BEFORE U.S. ADMINISTRATIVE LAW JUDGE
JILL S. CLIFTON

Monday, November 9, 2015

9:03 a.m.

Piccadilly Inn Airport
5115 East McKinley Avenue
Clovis, California 93727

TRANSCRIPT OF PROCEEDINGS
VOLUME XXXIII

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Myra A. Pish CSR
Certificate No. 11613

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24 SELECT MILK PRODUCERS: MILTNER LAW FIRM, INC.
25 BY: KRISTINE REED, ESQ.

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I N D E X - V O L U M E 33

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1 MONDAY, NOVEMBER 9, 2015 - - MORNING SESSION

2 JUDGE CLIFTON: We're back on record on November 9, 2015.
3 It's a Monday. It's approximately 9:03 in the morning. We're
4 in Fresno, California. We're at the Piccadilly Inn Airport.
5 We have changed from our location of many weeks and we have
6 returned to this location. This is Day 33 of the milk hearing.

7 My name is Jill Clifton. I'm the United States
8 Administrative Law Judge whose been assigned in take in the
9 evidence at this rule making hearing. I work for the
10 United States Department of Agriculture and I would like now to
11 invite others who are employed by the United States Department
12 of Agriculture to come and enter their appearances. Be very
13 careful, anywhere there's a microphone, there is a tripod
14 supporting it that will trip you.

15 MS. MAY: Good morning, I'm Laurel May with USDA. I'm with
16 the AMS Dairy Program and glad to see all of you here this
17 morning.

18 MS. FRISIUS: Good morning, this Meredith Frisius,
19 F-R-I-S-I-U-S, with AMS.

20 MR. SCHAEFER: Henry Schaefer, H-E-N-R-Y, S-C-H-A-E-F-E-R,
21 Agricultural Economist for the Upper Midwest Milk Marketing
22 Order Federal Order 30 on detail to AMS Dairy Programs.

23 MR. HILL: Welcome to the eighth week. I'm Brian Hill, an
24 Attorney with the Office of the General Counsel.

25 MR. BESHORE: Good morning, Marvin Beshore. M-A-R-V-I-N,

1 B-E-S-H-O-R-E, attorney for the Proponents of Proposal
2 Number 1, California Dairies, Dairy Farmers of America, and
3 Land O'Lakes.

4 MR. VLAHOS: Good morning, John Vlahos, J-O-H-N,
5 V-L-A-H-O-S, law firm of Hanson Bridgett, H-A-N-S-O-N,
6 B-R-I-D-G-E-T-T, co-counsel for the Co-op Proponents of
7 Proposal Number 1.

8 MR. SCHAD: Good morning, Dennis Schad, S-C-H-A-D, I work
9 for Land O'Lakes.

10 MR. JABLONSKI: Gary Jablonski, G-A-R-Y, J-A-B-L-O-N-S-K-I
11 working with the Cooperatives of Proposal Number 1.

12 MR. ENGLISH: Good morning, Chip English, E-N-G-L-I-S-H,
13 I'm with the law firm of Davis, Wright, Tremaine, with an
14 office, I still think I do, in Washington DC, and I'm here on
15 behalf of the Dairy Institute of California, Proponents of
16 Proposal 1 -- 2, did it again.

17 JUDGE CLIFTON: I just have to comment for the record that
18 both Mr. Beshore and Mr. Vlahos signaled "touchdown".

19 MR. ENGLISH: Well, let's just say I didn't get any time
20 off for the weekend.

21 MS. VULIN: Good morning, Ashley Vulin, A-S-H-L-E-Y, V --
22 as in Victor -- U-L-I-N, also an Attorney with Davis, Wright,
23 Tremaine, with the Dairy Institute of California, supporting
24 Proposal 2.

25 DR. SCHIEK: Good morning, William Schiek, S-C-H-I-E-K,

1 Economist with the Dairy Institute of California.

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

4 MR. DeJONG: James DeJong, D-e, J-O-N-G, Dairy Policy
5 Economic Analyst for Hilmar Cheese, dairy farmer-owned
6 manufacturer of cheese, whey, and milk powder.

7 MR. ZOLIN: Alan Zolin, A-L-A-N, Z-O-L-I-N, Consultant with
8 Hilmar Cheese Company.

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

11 MR. RAMIREZ: Good morning, Miguel Ramirez, Leprino Foods
12 in Denver, Colorado.

13 MS. TAYLOR: And Sue Taylor with Leprino Foods,
14 L-E-P-R-I-N-O.

15 MS. HANCOCK: Nicole Hancock with Stoel Rives, representing
16 the California Producer Handlers Association and Ponderosa
17 Dairy. And I will note that Laurel reminded me first thing
18 this morning that it's no longer Love Your Lawyer Day so we're
19 back to normal.

20 MR. GONSALVES: My name is Anthony Gonsalves, I am
21 President of Joey Gonsalves and Son. I am here representing
22 the California Producer Handler Association, my last name is
23 spelled G-O-N-S-A-L-V -- as in Victor --E-S. My father was the
24 author of the Milk Pooling Act. Thank you.

25 MR. LAI: Good morning, my name is Victor Lai, V-I-C-T-O-R,

1 L-A-I, with Producers Dairy Foods. Thank you.

2 MR. VANDENHEUVEL: Good morning, Rob Vandenheuvel,
3 V-A-N-D-E-N-H-E-U-V-E-L, with Milk Producers Council.

4 MS. REED: Good morning, Kristine Reed, Attorney for
5 Select Milk Producers. I'm going crazy and not spelling my
6 name today because it is Week 8, so --

7 JUDGE CLIFTON: You know, we're extremely fortunate to have
8 consistency with the court reporter. The same court reporter
9 who is in the room with us is preparing the transcript. That
10 is not always the case. Sometimes someone who has never heard
11 any of it types the transcript. We are very blessed with the
12 arrangement that's made here.

13 Is there anyone who has not yet come to the podium who
14 would like to be identified at this time?

15 MR. BARCELLOS: Good morning, Tom Barcellos, T-O-M, B- as
16 in Boy -- A-R-C-E-L-L-O-S, dairy producer from Porterville,
17 California, which is in Tulare County. I will be looking to
18 testify at some point. I am very flexible so I understand
19 there's people that need to get done and get out, so I would be
20 more than happy to get them out of the room. So, thank you.

21 JUDGE CLIFTON: Thank you so much. I appreciate that.
22 We're very glad to have you here. All right.

23 Is there anyone else who would like to be identified at
24 this time? Seeing no hands or people coming to the podium,
25 we'll go on to the announcements and other preliminary matters.

1 MS. MAY: Good morning, Laurel May with USDA. Welcome to
2 the Piccadilly Inn at the Airport. Glad to see all of you here
3 this morning.

4 Since we have changed locations, maybe we'll go through
5 our whole list of announcements. As you know, everybody is
6 welcome to testify, if they would like to. And to do so, you
7 just need to let one of us know that you would like to get into
8 the schedule. Anybody in the audience may question any of the
9 witnesses. And to do that, you merely need to approach the
10 microphone up here at the podium and the Judge will recognize
11 you.

12 We are broadcasting this session of the hearing via
13 live audio feed which is accessible at www.ams.usda.gov/live.

14 The court reporter is recording official transcripts of
15 this hearing which will be available approximately two weeks
16 following the end of each hearing week. The transcripts and
17 exhibits can be accessed at our AMS Dairy Program website.
18 Some of the exhibits have left overs and so we have put those
19 in those file boxes in the back corner over there behind the
20 sound guy, and you can go through the files and see if there
21 are any exhibits that you would like to pick up.

22 There are light refreshments here in the back of the
23 room that you are welcome to enjoy. Mr. Lai told us that he
24 brought some G-rated Egnog to share, so please enjoy that.

25 Okay. The end of the day last Friday we had

1 Mr. Geoffrey Vanden Heuvel on the stand, and today I believe we
2 are going to begin by having Mr. Zolin return to the stand to
3 be crossed on some previous testimony that he gave, but we
4 didn't finish his cross-examination. Beyond that, I will let
5 Mr. English and Mr. Beshore and Ms. Hancock explain what's
6 going to happen.

7 JUDGE CLIFTON: Thank you, Ms. May. Mr. English?

8 MR. ENGLISH: Thank you, your Honor, Chip English.

9 So let me first describe what our plan was walking in
10 today, and then I'll talk about what I understand may be some
11 moving pieces and how we might try to address it.

12 There was a time 10 or 11 days ago when I predicted we
13 would be for the Dairy Institute of California with our
14 case-in-chief by tomorrow, Tuesday. At some point last week,
15 what I can only call irrational exuberance kicked in and I said
16 Friday of last week, so I'm not going to forecast anymore.
17 Although I do think, subject to what we're about to hear about
18 other issues, we would finish tomorrow morning.

19 So here's what I had for today before walking in the
20 door today. We have got Mr. Zolin on Section 9(d). He has
21 already given his testimony exhibits, which are Exhibit 131 and
22 Exhibit 132, in case people want to have those ready for his
23 return. What he did was his direct exam and Mr. Beshore had,
24 at least temporarily, concluded a cross, but of course
25 Mr. Zolin is back so there may be more questions there. We

1 have 9(d) to complete.

2 I then had Mr. Zolin staying on the stand and doing
3 Section 7(c), what I call the fix. This is in response to the
4 questions asked by Mr. Beshore weeks ago. And in addition,
5 Mr. Beshore had reserved his cross-examination of Mr. Zolin on
6 Section 13. And we call that all Al Zolin, Part 7, which is
7 also the last chapter for Mr. Zolin in this proceeding.

8 And then we had Dr. Schiek coming to the stand on
9 quota, and that's his Part 4. We also had a left over issue
10 from Mr. Blaufuss that never got on last Friday as we
11 anticipated, and so that would come after Dr. Schiek,
12 Rob Blaufuss, Part 4, on fortification, remembering that he's
13 already done Part 5.

14 After that, we had Sue Taylor, her Part 3, which is
15 called price impacts. And candidly, I would think that would
16 be somewhat ambitious, and I wasn't sure she would get on the
17 stand today, but I was also very confident that if she did her
18 direct she wouldn't finish her cross today.

19 We then would have, tomorrow morning, finishing
20 Ms. Taylor. And at that point we would have Mr. Blaufuss,
21 Part 6, transportation credit, ready to go so we could just
22 wrap up without any loose ends.

23 I presently have no other Dairy Institute of California
24 witnesses expected, of course, we reserve the right after
25 Proposal 3 and 4 to be heard, to come back. But right now,

1 that is our entire list.

2 So when I came in this morning Ms. Hancock approached
3 me and she indicated that Mr. Gonsalves has, is going to
4 testify and needs to leave by 1:00 p.m. tomorrow. Here's the
5 issues that we have. And I understand there's some dairy
6 farmers here and more dairy farmers coming. Mr. Zolin was
7 supposed to leave last week and put off his flight a couple
8 times and is now scheduled to leave tomorrow at 1:00, and he's
9 already paid extra money to change those air tickets, so we
10 have got to get Mr. Zolin on and off today no matter what,
11 that's why I'm putting him ahead of Dr. Schiek.

12 Mr. Blaufuss and Ms. Taylor need to be done by
13 Wednesday afternoon. So the easiest thing for me to do to
14 accommodate Ms. Hancock would be to put Dr. Schiek later, but
15 that creates the problem that we have been assuring Mr. Vlahos
16 that we would get Dr. Schiek on when it was convenient for him.
17 And he has a long-standing commitment for tomorrow, so that
18 makes it difficult, and Dr. Schiek's ready to go by the way.
19 So we are ready to go, and I want to live up to my commitment
20 to my friend and colleague, Mr. Vlahos.

21 What I need -- if we are going to accommodate, and
22 again, I didn't know about this until this morning, I'm not
23 just -- if we're going to accommodate Mr. Gonsalves, and I have
24 no idea what he's going to say and I have no idea how long his
25 cross is going to be, I have got to know that the witnesses who

1 are ready to go today, Mr. Blaufuss and Ms. Taylor, in agreeing
2 to go, I think effectively after Mr. Gonsalves tomorrow, are
3 going to get out of here on their schedule. And if I can get
4 that commitment from everybody in the room, then I am prepared
5 to make the accommodation to Ms. Hancock and Mr. Gonsalves. If
6 I can't get that commitment, then I need to move forward with
7 my witnesses who have been here a long time and, you know, they
8 need to get out of here. But I think it's probably doable, but
9 on the other hand, I was the one who predicted we would be done
10 last Friday, and I obviously cannot predict the length of
11 testimony, and I'm giving up. Maine weather forecasters do
12 better than I do. So that's the conundrum we have, your Honor.

13 We are prepared to be flexible, but I need to make sure
14 that Mr. Zolin gets done today, and I need to make sure that
15 Ms. Taylor and Mr. Blaufuss are done Wednesday afternoon. So
16 with that in mind, that's what I have got and I'll let others
17 speak to that.

18 JUDGE CLIFTON: Okay. I'll hear from the rest of you. I
19 would expect intensive cross-examination now that we're getting
20 into quota, so I think the witnesses will take some time. I
21 think it's very smart to have Dr. Schiek go forward on that
22 issue before the others go, so that's just off the top of my
23 head.

24 MR. ENGLISH: And I understand, your Honor. I just -- I
25 just need to make sure that people who have major meetings and

1 commitments that are both professional and personal, to get
2 done here, and have been here throughout the entire proceeding,
3 and literally have other things that they have scheduled, can
4 live up to those commitments, and that my accommodation doesn't
5 end up dis-accommodating them and their businesses. So that's,
6 that's my concern. And it is my obligation, both personally
7 and professionally, to Mr. Blaufuss and Ms. Taylor.

8 JUDGE CLIFTON: Mr. Beshore?

9 MR. BESHORE: Just real quick. From our perspective, we're
10 ready to accommodate in every way possible. We would like to
11 see Dr. Schiek go first with quota because Mr. Vlahos is only
12 available to our team today and that's an important part of his
13 contribution.

14 I would say, you know, Mr. Barcellos has introduced
15 himself and he's willing to accommodate, we really appreciate
16 that. I have, and just as an additional factor as we look
17 forward towards the week, I have a communication from
18 Ms. McBride that there are four dairy farmers that she was
19 expecting to come in on Wednesday. I have asked her if they
20 could be late Wednesday or even Thursday, to, you know,
21 accommodate the schedule, and I haven't heard back. But --
22 but, you know, that's our piece. We're ready to accommodate
23 Mr. English and Ms. Hancock in whatever way possible within
24 those minimal constraints.

25 JUDGE CLIFTON: Ms. Hancock?

1 MS. HANCOCK: What I would propose is that we just go ahead
2 and move forward with Mr. Zolin and then Dr. Schiek as planned,
3 and we see how far we get, and then we'll be in a position to
4 make another decision. It's definitely our scheduling issue,
5 and I don't want to do anything to try and upset the
6 opportunities for the people who have been here for eight weeks
7 to leave. So I don't think that would be fair to them. So my
8 proposal is, let's just move forward and see how far we get and
9 then we'll figure it out.

10 JUDGE CLIFTON: Great. Excellent. Thank you. Who else
11 would like to be heard on any preliminary issue? No one.
12 Good. Let's get on with the evidence. So Mr. Zolin, would you
13 return to the stand?

14 MR. ENGLISH: Your Honor, Chip English, and what Mr. Zolin
15 is testifying about is Exhibits 131 and 132, this is the
16 Section 9(d) provision, also known as the Proprietary Bulk Tank
17 Handler Provision. And as I indicated earlier, direct was
18 complete, Mr. Beshore had done preliminary cross, he may have
19 more, you know, with the intervening time to think about
20 things, and so Mr. Zolin is available for that further
21 examination.

22 JUDGE CLIFTON: Thank you, Mr. English. Mr. Beshore? And
23 Mr. Zolin, you remain sworn. I would like you to again state
24 and spell your name.

25 MR. Zolin: My name is Alan Zolin, A-L-A-N, Z-O-L-I-N.

1 JUDGE CLIFTON: All right. Make yourself comfortable with
2 the respect to your microphone. I know we have to see the
3 exhibit as well as speak into it. Is it good, do you think?

4 MR. ZOLIN: I'm okay.

5 JUDGE CLIFTON: All right. If you need to stop at any time
6 and we'll move the base of it, just let us know.

7 Mr. Beshore, you may proceed.

8 MR. BESHORE: Thank you, your Honor.

9 CROSS-EXAMINATION

10 BY MR. BESHORE:

11 Q. Marvin Beshore.

12 Just two questions further on the Proprietary Bulk Tank
13 Handler, Mr. Zolin. Does the request, the proposal to include
14 this 9(d) provision, have anything to do with quota?

15 A. It did at the beginning of our discussion, but as we
16 have progressed in our decision making, it does not.

17 Q. Okay. Second question, is it the contemplation of this
18 proposal that a handler or a plant operator could file both a
19 pool plant report and a Proprietary Bulk Tank Handler Report
20 and, you know, divide up milk supplies among them or between
21 them?

22 A. We did not contemplate multiple reports. And I guess
23 when I say "we" I would have to say I did a lot of the
24 contemplating on how this provision would work. I did testify
25 about the intake situation, how busy it is at our Hilmar plant,

1 and I looked at the Proprietary Bulk Tank Handler Report as
2 being the Hilmar Report if a Federal Order was put in
3 California, so I did not contemplate having multiple type
4 reports for my client.

5 Q. Okay. So it's not the intention of the proposal, then,
6 to facilitate multiple reports for the same handler, the same
7 plant?

8 A. That is not the intent of the proposal.

9 Q. Okay. Thank you.

10 JUDGE CLIFTON: Who next has questions for Mr. Zolin?
11 Now, let me ask, Mr. English, would you come back to the
12 podium? Shall we do this with the three categories one by one
13 or is he available for cross on all three that you mentioned?

14 MR. ENGLISH: I think that's going to make more sense, this
15 issue is discreet enough and separate enough from the 7(c) and
16 Section 13 issue that it would make more sense, and it may very
17 well be that the questions I expect now are going to be
18 technical from USDA at this point, so I would actually think it
19 would make sense, and this is a different enough issue in
20 Section 9, it's not about, it's about who needs to report and
21 how that reporting occurs, not who qualifies, not about
22 qualification issues, which are what the 7(c) and the 13 are
23 about, performance standards and qualification issues. So I
24 think it is discreet enough that it makes sense to keep it
25 divided.

1 Now, I know all the other issues combine, but I would
2 prefer we get this one done and then move on to the next one.

3 JUDGE CLIFTON: I like it. Thank you. Who else has
4 questions about Section 9(d)? Mr. Schaefer?

5 CROSS-EXAMINATION

6 BY MR. SCHAEFER:

7 Q. Good morning, Mr. Zolin.

8 A. Good morning.

9 Q. First thing I wanted to mention -- Henry Schaefer,
10 USDA -- first thing I wanted to mention is, I believe the
11 exhibits that we're looking at are 137 and 138, and I believe
12 Mr. English mentioned 131 and 132.

13 A. I thank you because I was looking at mine saying, I
14 wonder if I marked them incorrectly.

15 MR. ENGLISH: I apologize.

16 MR. SCHAEFER: Too bad they aren't all that easy.

17 JUDGE CLIFTON: Hold on just a minute, Mr. Schaefer, so we
18 can all get 137 and 138. Mr. Schaefer, you may proceed.

19 BY MR. SCHAEFER:

20 Q. Thank you, your Honor. A couple things here, I guess,
21 is, I want to kind of get a handle on to make sure we
22 understand where you are headed with this proposal. And my
23 first question, I guess, is, when the handler fills out the
24 report, as you mentioned your Hilmar client and they would fill
25 out a single report, will they be the handler then, for payment

1 to producers?

2 A. Our modification that we added to the proposal says
3 that the pool plant that receives the milk would be the handler
4 for that report. This is going back to some of the concerns
5 brought up in the Idaho-Oregon marketplace that had this
6 provision in there in the past. So the expectation would be
7 that the receiving pool plant or pool distributing plant would
8 be the handler for that milk.

9 Q. And so they would be the handler for the entire report?
10 So if you had 300 million pounds on the Hilmar report, for
11 instance, on this 9(d) report, then the pool plant, 7(a) or
12 7(b) plant, would therefore be responsible for minimum payment
13 on that 300 million pounds of milk?

14 A. That would be correct.

15 Q. You realize, of course, that if something does happen,
16 that handler is responsible for payment to those producers?

17 A. I do understand that. And from a standpoint of
18 relationships with that pool distributing plant, I'm sure a
19 contractual resolution will be handled between Hilmar and that
20 distributing plant.

21 Q. Do you know if any other, in your experience in your
22 consulting business and with Kraft, that any other
23 Federal Order has honored a contract between two proprietary
24 handlers, like in this scenario, if there was a default?

25 A. I do understand that, Henry, that is not the case. But

1 I wasn't thinking of a contract, I was almost thinking of like
2 a letter of credit or some form of instrument that would
3 guarantee payment.

4 Q. Along the same lines then, that the distributing plant
5 will be the handler responsible for that or the 9 or the 7(a),
6 7(b) plant, that milk would also, that handler would then also
7 be responsible to the Order for any classification on that
8 milk, so they would settle with the pool, the PSF, on that
9 entire quantity of milk?

10 A. Correct.

11 Q. Do you know if that would have any impact on any of the
12 qualification, any qualification of that 7(a) or (b) plant?

13 A. Henry, if I can ask a little more clarification
14 meaning. Would it cause the plant not to be a distributing
15 plant?

16 Q. Well, there's a number of questions there, obviously,
17 when you start to get into this. But one, of course, is would
18 it cause the distributing plant to not be able to qualify as a
19 distributing plant? And would it also affect the in-area sales
20 percentage?

21 A. I do not believe that would be the case because, again,
22 from a standpoint of mainly thinking of the diversion of milk
23 back to a nonpool plant, I do not believe that gets involved in
24 those calculations.

25 Q. Would the, since the 7(a) or 7(b) plant would be the

1 responsible handler on this milk, how do you intend that
2 payment between or settlement be here, will they be a single
3 payment to the 9(d) handler on Class or on producer blend
4 price?

5 A. Let me try to answer the question the way I think I
6 understood it. I'm -- my mind went to advance and finals, and
7 I'm not sure if that's where you wanted to go. But certainly a
8 settlement between the two parties could be an invoice that
9 involves, you know, the entire equation. So I believe there
10 could be a single settlement between the two parties.

11 Q. Okay. On your order language that, in Exhibit 138, in
12 number 2 and number 3, at the end of number 2 it sounds to me
13 like the applicant who is the 9(d) handler will be the
14 responsible handler for the milk, and in number 3 you are
15 saying that the pool plant will be responsible for the milk.
16 Which is it?

17 A. I would say it would be number 3.

18 Q. And so that last part of number 2 would need to be
19 deleted or reworded or something?

20 A. I would like for the Department to make any technical
21 corrections in the, in the Order language.

22 Q. Would there be any issues with the 9(d) handler being
23 the responsible party for all the milk on the report and
24 settling with the pool, with the PSF, on that milk?

25 A. I have no problems with that. And the reason we went

1 with this addition was the discussion that was held at the
2 Idaho, I'll just call it the Idaho hearing, to address issues
3 that were a concern of the Proprietary Bulk Tank Handler. So
4 from a standpoint of allowing the nonpool plant to be the
5 responsible handler, I'm fine with that. But I do recognize
6 that there were some concerns brought up back in, I think the
7 hearing was 2000, 2001, in that timeframe, to be sure that we
8 correct any imperfections in the proposal.

9 Q. Okay. And I think my last question, and this touches a
10 little bit on qualification, you realize that without having a,
11 the Hilmar plant, since you have brought them up as the party
12 that you are looking at in this scenario, would not have a pool
13 plant to it, that they would still have to qualify milk at some
14 pool plant, the either the one-day touch base or the 48,000,
15 they could not do it at that facility?

16 A. We understand that, yes.

17 Q. Okay. Thank you, Al.

18 JUDGE CLIFTON: Who next has questions for Mr. Zolin on
19 this issue? Is there any redirect on this issue?

20 REDIRECT EXAMINATION

21 BY MR. ENGLISH:

22 Q. Chip English. And thank you, Mr. Schaefer, for
23 correcting me on the exhibit numbers, I hope I don't hit the
24 Trifecta by having a third set of numbers wrong, if and when I
25 get to Mr. Blaufuss.

1 So I just want to follow up a little bit, Mr. Zolin,
2 and looking at the exhibit attachment which is Exhibit 138, I
3 believe, it is numbered on my screen. And so we added
4 paragraph 3 at the bottom of the first page, which was, do you
5 recall how many options there were that were offered back in
6 the Western Order? I know that's a week ago now.

7 A. If you give me a second, Chip, I can look. There were,
8 back to the attached to my testimony, Proposal 11, Proposal 12,
9 and Proposal 13, I believe were all options given.

10 Q. And the paragraph 3 was essentially the Proposal
11 Number 11 on page 5 of the exhibit?

12 A. That is correct.

13 Q. If you look briefly at Proposals 12 and 13, the purpose
14 of those proposals was to do what as opposed to Proposal 11?

15 A. The purpose of those other proposals, and I must -- I
16 must say, I'm looking, I have read through these a couple of
17 times, is to allow the Proprietary Bulk Tank Handler to be the
18 handler on that milk.

19 Q. But effectively to make a payment to that, it's a
20 payment from the entity that is bottling the milk, to the
21 Proprietary Bulk Tank Handler, correct?

22 A. Correct.

23 Q. Similar to an association?

24 A. Correct.

25 Q. Which would create an obligation under the pool for

1 minimum price, correct?

2 A. That is correct.

3 Q. Okay. And that, we're not saying you have to take
4 what's in paragraph 3 of Exhibit 138. You have indicated that
5 you are also thinking that it could look at what's our
6 proposals 12 and 13 on 138?

7 A. Yes.

8 Q. Okay. That's all I have on this particular issue, your
9 Honor.

10 JUDGE CLIFTON: Does that prompt further questions on this
11 issue? I see none. Mr. English, you may proceed to the next
12 issue.

13 MR. ENGLISH: Your Honor, this was produced last Thursday,
14 it is actually two documents, they are connected and they
15 should have been one document, but that's not what happened.

16 Your Honor, I don't dare try to predict what exhibit
17 number this is and get it wrong.

18 JUDGE CLIFTON: All right. I think our last exhibit number
19 already assigned was Exhibit 143. Ms. Frisius, will the
20 testimony of Alan Zolin be Exhibit 143?

21 MS. FRISIUS: It will be.

22 JUDGE CLIFTON: Okay. Exhibit 143 will be testimony of
23 Alan Zolin, Part 7, and the accompanying document I'll mark as
24 Exhibit 144, and I'll have Mr. English tell us what each of
25 these things is.

1 (Thereafter, Exhibit 143 and Exhibit 144
2 were marked for identification.)

3 MR. ENGLISH: Well, Exhibit 143 is a brief statement by
4 Mr. Zolin that I will then expand upon with him through
5 examinations, and it has to do with some proposed modifications
6 to Proposal 2 as printed in the Federal Register. On page, I'm
7 sorry, for the pause, your Honor, I was trying to get the page,
8 Exhibit 1, Proposal 2, this is going to modify language that's
9 found on 47220 -- I apologize, it starts on 47219, the bottom
10 of 47219, the last paragraph 3, carrying over to 47220 through
11 paragraph 4, and we'll renumber paragraph 5 as paragraph 4. So
12 that's what this testimony is going to be about.

13 Why don't we let him read it and then we can go through
14 the documentation. But the bottom line is, this is a proposal
15 to amend Proposal 2 starting on page 47219 of Exhibit 1, the
16 third column, the paragraph that starts 3. A supply plant
17 under this paragraph, the very bottom of the third column of
18 page 47219.

19 JUDGE CLIFTON: Good. That's very helpful.

20 MR. ENGLISH: Okay. And then carrying over to 47220, it's
21 going to, basically it is going to delete what's in the Federal
22 Register in 47219, that bottom paragraph, starting paragraph 3,
23 starting over to 47220, delete the paragraph 4, it's going to
24 insert a new paragraph 3 to replace 3 and 4, and renumber the 5
25 as 4.

1 JUDGE CLIFTON: Thank you. That's a good roadmap for us to
2 begin.

3 MR. ENGLISH: Okay.

4 JUDGE CLIFTON: All right. So I have marked as
5 Exhibit 144, a document that's entitled Dairy Institute of
6 California, Modified Proposed Section 1051.7(c). And
7 Mr. English, you may begin.

8 DIRECT EXAMINATION

9 BY MR. ENGLISH:

10 Q. All right. And Mr. Zolin, why don't you read your
11 statement that is the second, the back page of Exhibit 143, and
12 then we'll have some additional discussion.

13 A. Okay.

14 Introduction

15 My name is Alan Zolin. I have been retained by Hilmar
16 Cheese Company to work with Dairy Institute of California (DIC)
17 to develop an alternative proposal to Cooperative Proposal 1.
18 I have worked with a task force made up of a number of
19 representatives from DIC member companies in order to develop
20 and submit Proposal 2.

21 Description of Proposal 2 Modification of Shipping Requirements

22 DIC wants to modify Proposal 2, specifically in
23 Section 7(c). DCI would like to eliminate Paragraph 7(c)(3) in
24 its entirety. DIC requests a renumbering of paragraph 4 to be
25 Paragraph 3, and paragraph 5 would be the new paragraph 4. DIC

1 would also modify the new paragraph 7(c)3 to operate as a call
2 provision. DIC has decided to adopt a call provision from
3 Order 68 into Proposal Number 2. The call provisions that were
4 in Order 68 had the following provisions:

5 1. The Market Administrator (MA) will designate a
6 "call area" which will include pool supply plants and
7 distributing plants.

8 2. The MA will make an announcement about what the
9 minimum level of shipments is needed to meet Class 1 needs with
10 in the call area.

11 3. The MA may investigate supply and demand conditions
12 on his own initiative or by a request of an interested party.

13 4. Qualifying shipments to a pool distributing plant
14 in the call area must be in addition to any shipments the
15 handler is already making to distributing plants.

16 5. Credit is given to a supplier for performance to
17 distributing plants outside of the call area if the supply
18 plant notifies the MA prior to any call announcement.

19 6. Penalty provisions for any supply plant that
20 doesn't comply with a call shipping requirement is the loss of
21 pool status for one year.

22 DIC believes the call provisions proposed, in
23 conjunction with the shipping requirements discussed earlier,
24 will ensure an adequate supply of milk to be provided to the
25 fluid market.

1 This concludes my testimony on this issue.

2 Q. So that's what we're doing, and we'll describe it a
3 little more when we go look at Exhibit 144, but what was the
4 genesis, what caused this change to come about?

5 A. Within the Dairy Institute task force, we talked quite
6 a bit about having a call provision and we tried to tie the
7 call provision in to quota milk in California. As we started
8 to work through that process -- as we started to work through
9 that process, it became more difficult to actually get the
10 right percentages and identify percentages on what handlers
11 would have to perform to meet the standards in a particular
12 month. By revising the proposal the way we have, we now have
13 straight shipping percentages, as described in, bear with me,
14 in paragraph 2, as well as in paragraph 1. And the call, which
15 is again, an additional requirement if it's determined that
16 supply and demand conditions warrant additional milk to come to
17 the fluid market.

18 Q. Now, you obviously recall that you had some questions
19 for Mr. Beshore about how the math would work and how much milk
20 would be required to be shipped under the Dairy Institute of
21 California's proposal as drafted and published on page 4721 and
22 4722 of Exhibit 1, correct?

23 A. I do remember that.

24 Q. And do you remember similar questions to Mr. Blaufuss?

25 A. I do.

1 Q. Okay. So what, if anything, does this proposal found
2 in Exhibit 144 do with respect to that so-called math issue?

3 A. Okay. What it does is, number 1 -- and I'm going back
4 to my testimony, I believe it was Exhibit 114 where I had the
5 brackets listed towards the end of that proposal. The brackets
6 are now the shipping requirements that will be required of pool
7 supply plants in the Order.

8 Q. And unlike the way Proposal 2 read, especially in
9 deleted (c)(3), there's no sort of pyramiding of shipping
10 requirements that adds quota milk, correct?

11 A. That is correct. Quota milk has been removed from the
12 discussion.

13 Q. Okay. Before we look at Exhibit 144, and you have
14 mentioned your earlier exhibit, having looked at that, is there
15 anything you want to say about -- and that was Part 3
16 testimony, right?

17 A. That would have been Part 3 testimony, yes.

18 Q. In preparing for today, is there anything you would
19 like to say about that exhibit in Part 3?

20 A. I would. Re-reading the proposal, or, I'm sorry,
21 re-reading my testimony of Exhibit 114 I found an error on
22 Page 6. And what I state on page 6 is that I was describing
23 that we looked at the Texas --

24 JUDGE CLIFTON: Let me stop you until we all find our 114.
25 I'm turning in Exhibit 114 to page 6. All right. It is at the

1 very end of Exhibit 114. Mr. Zolin, you may proceed.

2 MR. ZOLIN: Okay. On the second line, the sentence that
3 starts, "in Texas there is no split plant provision," I believe
4 that's incorrect. I did look at the Order and I believe I saw
5 a split plant provision there, so I would like to strike that
6 and have the sentence read, "in Texas --"

7 MR. ENGLISH: Wait, I'm not sure we can strike it since
8 it's already been admitted.

9 JUDGE CLIFTON: That's correct. We won't change the
10 original exhibit, but anyone who is searching the record merely
11 needs to search for 114 to find this testimony, but, yes, I do
12 not propose that we, that we extract 114 from its place on the
13 website. It will stay there, but this testimony is just as
14 effective by the way you are giving it to us, Mr. Zolin. So
15 start again, please.

16 MR. ZOLIN: Okay. I would like the sentence to, that
17 sentence should have read, "in Texas there is no repooling
18 rule, such as Order 30's 125 percent rule."

19 BY MR. ENGLISH:

20 Q. And what you are correcting is the concept that there
21 is not a splint plant provision under the Order 126, correct?

22 A. That's correct.

23 Q. Okay.

24 JUDGE CLIFTON: All right. So what you would be striking
25 is just about, I don't know, seven words. The words being

1 stricken, if you are looking at it, Mr. Zolin, is, we could
2 strike "no split plant provision and there is".

3 MR. ZOLIN: If I may, your Honor. I would strike right
4 after the word "Texas" "there is no split plant provision and".

5 JUDGE CLIFTON: Okay. So, yes, I agree, that little phrase
6 goes together. So we strike "there is no split plant provision
7 and" -- and then the sentence reads as you have said, read it
8 one more time as it should have been stated.

9 MR. ZOLIN: In Texas there is no repooling rule such as the
10 Order 30's 125 percent rule.

11 JUDGE CLIFTON: Okay.

12 MR. ENGLISH: Okay. Thank you.

13 BY MR. ENGLISH:

14 Q. Before we turn to Exhibit 144, was there anything else
15 you wanted to say?

16 A. No, that is all.

17 Q. So now, looking at Exhibit 144, which is a three-page
18 document, we have reproduced in track changes, what I call
19 track changes from Word, Section 1051.7(c) from Proposal 2, but
20 as modified pursuant to Exhibit 143, your testimony, correct?

21 A. That is correct.

22 Q. Okay. So we have made no change to (c)(1) on page 1,
23 correct?

24 A. That is correct.

25 Q. And we have made no change to (c)(2) on page 1 over

1 through the first half of page 2, correct?

2 A. That is correct.

3 Q. And so first, before we look at the addition on page 2,
4 on page 3 you have deleted what was paragraph 3 and 4, correct?

5 A. That is correct.

6 Q. And you have renumbered 5 as 4, correct?

7 A. Paragraph 5 now becomes paragraph 4.

8 Q. So what, again, is paragraph 3?

9 A. Okay. Paragraph 3 is a restatement of the call
10 provision from the Order 68, I believe it was called the Upper
11 Midwest Order at the time. The only modification I'm aware of
12 from that original language is that we again reference the 9(d)
13 status at the very bottom of page 2, which would have been in
14 paragraph 3 (ii)(a).

15 Q. And obviously we have hopefully modified to conform to
16 what's proposed Order 1051, correct?

17 A. Correct.

18 Q. And then addition, looking at page 3 for a moment. In
19 paragraph (b) --

20 A. Yes.

21 Q. -- we have referenced section, in paragraph (b) the
22 last line we have referenced 1051.42(b)(2) and then it says as
23 other than Class I. Order, old Order 68 doesn't exist anymore,
24 correct?

25 A. That's correct. The Order was merged with Order 30.

1 Q. And is Section 42 the transfers and diversions section?

2 A. It is.

3 Q. Okay. So would you agree that we have made a
4 conforming change to account for changes in Federal Order
5 Reform that altered the language that Order 68 referred to?

6 A. I agree with that.

7 Q. Okay. So we have made that change as well; is that
8 correct?

9 A. Yes.

10 Q. Okay. So now, can you talk a little bit about your
11 experience in dealing with old Order 68 and the call provision,
12 so that this record has your professional experience and
13 historical experience with respect to how the call provision
14 actually operated?

15 A. Okay. In my time with Kraft foods, we had two
16 manufacturing plants located in Minnesota that pooled milk on
17 Order 68. And although I do not remember the call provision
18 ever being put into effect, although I could be wrong on that,
19 I do have a very strong memory of being called to the Market
20 Administrator's office to have a discussion about the
21 possibility of a call being invoked. And after that
22 discussion, it was suggested that those of us that were in the
23 "potential call area" make some more milk available for Class I
24 use in order to avoid a possible call, so I do have that
25 experience. And but, again, like I said, it was never an

1 actual call that I'm aware of, it was more of individual
2 parties getting together and making sure milk found its way to
3 the Class I needs.

4 Q. Is that byway of saying, in addition to the Market
5 Administrator having that heart-to-heart conversation with the
6 entities, that somehow that meant the milk flowed?

7 A. It flowed the next day.

8 Q. So with that, anything else you want to add about that?

9 A. No, that's all.

10 Q. So with that, your Honor, I'm sorry, there's one modest
11 correction on Exhibit 143. If you turn to the testimony,
12 Mr. Zolin, under description of Proposal 2, Modification of
13 Shipping Requirements, you read it as it is written, but I'm
14 wondering whether you want to correct the second sentence as
15 opposed to all the other references to Dairy Institute of
16 California reads "DCI", would you like to correct that?

17 A. I see that, yes, it should be Dairy Institute of
18 California or "DIC", yes.

19 JUDGE CLIFTON: All right. So Ms. Frisius, just under the
20 heading on the Exhibit 143, the heading that says, Description
21 of Proposal 2 Modification of Shipping Requirements, in the
22 first line, the second reference to the Dairy Institute of
23 California will be made to read "DIC" rather than "DCI", so we
24 strike "DCI" insert "DIC". All right?

25 MR. ENGLISH: Actually, I do have one more set of

1 questions, Mr. Zolin.

2 BY MR. ENGLISH:

3 Q. Was there another alternative that we considered with
4 respect to paragraph 3, using Order 68? Is there something we
5 also thought about?

6 A. The Order 68 also had a reserve supply plant program,
7 we did discuss that.

8 Q. Okay. How about the CDFA call provision issue, did we
9 talk about that?

10 A. Oh, certainly. Again, most of the discussion in our
11 task force was looking at the CDFA call provision, you know,
12 versus a call area. We found it interesting how CDFA runs the
13 program with identification of specific plants and the rotation
14 of plants. Again, we looked to the Department to determine
15 what is the most effective way to service the Class I market.
16 Obviously, Order 68 and these provisions that we're referencing
17 were written back, I'm imagining in the '70's or '80's. If
18 there's a better mousetrap, maybe we should address those as
19 well.

20 Q. Thank you, Mr. Zolin. Your Honor, at this point I move
21 admission of Exhibit 143 and 144, and then the witness will be
22 available for further examination on this issue, and by
23 Mr. Beshore on his reserved issue regarding Section 13.

24 JUDGE CLIFTON: Thank you, Mr. English. Mr. Zolin, when
25 you say you looked to the Department, you were referring to the

1 United States Department of Agriculture, correct?

2 MR. ZOLIN: That is correct.

3 JUDGE CLIFTON: And why is that even after you had looked
4 at what California did?

5 MR. ZOLIN: Well, from a standpoint, and it is after
6 attempting to write Order language, we have realized how
7 difficult that is. And so by being able to use Order 68 as the
8 guide, we feel we would minimize the mistakes we may make. The
9 Department is well-versed in writing Order language. And
10 again, by the suggestion of following the CDFA call provisions
11 with their technical expertise in writing the language, we
12 would other yield to that expertise.

13 JUDGE CLIFTON: Now, you just said CDFA, you would yield to
14 that expertise, and that confused me.

15 MR. ZOLIN: Because I was referring to the current CDFA
16 call provision, that's when I was trying to reference CDFA. It
17 is USDA that has the technical expertise in writing
18 Federal Order language.

19 JUDGE CLIFTON: Okay. So after looking at the CDFA, you
20 chose to rely on the expertise of the USDA?

21 MR. ZOLIN: Correct.

22 JUDGE CLIFTON: Okay.

23 MR. ENGLISH: But if I may, nonetheless, for now, based
24 upon past history and practice, and the fact that the language
25 worked, we're using Order 68 language, correct?

1 MR. ZOLIN: That is correct.

2 JUDGE CLIFTON: Who would like to begin with
3 cross-examination on this issue?

4 MR. ENGLISH: Actually, your Honor, I moved the admission
5 of Exhibit 143 and 144.

6 JUDGE CLIFTON: All right. Very good. Does anyone wish to
7 question Mr. Zolin with regard to Exhibit 143 or 144 before
8 determining whether you have any objection? And we're going to
9 move my microphone, it keeps drifting downward. Anyone who
10 wishes to question Mr. Zolin with regard to Exhibit 143 or 144
11 before determining whether you object? No one. Is there any
12 objection to the admission into evidence of Exhibit 143? There
13 are none. Exhibit 143 is admitted into evidence.

14 (Thereafter, Exhibit 143, was
15 received into evidence.)

16 JUDGE CLIFTON: Is there any objection of the admission
17 into evidence of Exhibit 144? There are none. Exhibit 144 is
18 admitted into evidence.

19 (Thereafter, Exhibit 144, was
20 received into evidence.)

21 JUDGE CLIFTON: Who would like to be the first to question
22 Mr. Zolin on these provisions? Mr. Beshore?

23 CROSS-EXAMINATION

24 BY MR. BESHORE:

25 Q. Thank you, your Honor. Marvin Beshore.

1 Good morning, Al.

2 A. Good morning.

3 Q. I just want to explore, I appreciate your, you know,
4 the modifications here, and the, actually, it probably moves us
5 incrementally closer, if that's conceivable.

6 I want to explore how this would work in particular
7 with respect to Hilmar using, since you are testifying for
8 Hilmar, and I want to use them as an example. Okay? So
9 Mr. DeJong has testified that Hilmar, if I remember correctly,
10 represents about 12 percent of the milk in California. Does
11 that sound right?

12 A. That sounds right.

13 Q. Okay. Which, by my math, is something over 400 million
14 pounds of milk a month.

15 A. I don't, I think in terms of milk a day, so the 400
16 is --

17 Q. At current production levels in California, my math
18 says around 14 million a day.

19 A. I testified on an earlier subject, 250 loads, over 250
20 loads of milk a day.

21 Q. 50,000 pound loads?

22 A. Rough number, yeah.

23 Q. So it would be 12 and a half million at 250 loads,
24 something, okay.

25 A. Right.

1 Q. So we're -- we're in the same area. So if you use
2 400 million pounds a month for math here, simple path. If
3 Hilmar were to qualify, if there was a Federal Order under
4 Proposal 2 and Hilmar were to seek to qualify its milk, it
5 would need deliveries of 40 million pounds to distributing
6 plants, correct?

7 A. That is correct.

8 Q. Okay. How many sales does Hilmar have now on a regular
9 basis to distributing plants?

10 A. On a regular basis, none.

11 Q. Okay. So if an order, if Proposal 2 went in, and
12 Hilmar wanted to qualify its producers for the blend, it would
13 need to find 40 million pounds of sales which it doesn't
14 presently have at distributing plants in California, correct?

15 A. That is exactly what would -- that's how it works,
16 Marv, yes.

17 Q. So that means that's someone else is supplying those
18 sales now, you would have to displace 40 million pounds of
19 sales of some other market participant in order to pool Hilmar,
20 correct?

21 A. It would have to displace, I'm assuming the markets are
22 being met, the fluid needs are being met today, so yes.

23 Q. Well, you don't have any information that they are not
24 being met, correct?

25 A. There was a couple of stutters during this hearing

1 process where Class I market wasn't being met. But in general,
2 I believe that's the case. And in order for Hilmar to pool all
3 of its milk, it would need 40 million pounds of Class I sales.
4 But I would also say, I'm not sure if all of that milk would be
5 pooled, Day 1. That's something that might take a very long
6 time to accomplish.

7 Q. In any event, it would, it would represent a huge
8 change in supply arrangements to California distributing
9 plants, that's fair, is it not?

10 A. It would -- we would become a new supplier. That would
11 definitely be the case.

12 Q. Would you agree with me that it's, it's presently, in
13 recent years it's been very beneficial for Hilmar to be part of
14 the California market-wide pool?

15 A. I'm not sure I understand what you mean by beneficial.

16 Q. It's been financially beneficial. It's drawn
17 consistently, month after month, it's drawn money from the
18 California pool to pay its producers the overbase, to assure
19 its producers the overbase price?

20 A. I would have to say yes.

21 Q. Do you have any idea how many how many millions of
22 dollars per month Hilmar has been drawing on average from the
23 California pool to pay its producers?

24 A. I do not know.

25 Q. Okay. But we can figure that out pretty readily by

1 looking at the 4b price and the overbase price and Hilmar's
2 volume and just doing that arithmetic, right?

3 A. It is a mathematical calculation.

4 Q. Okay. With respect to the producer, the producer milk
5 provisions in Proposal 2, 13, and the new, you know, the
6 modified provisions in Part 7, yeah, Part 7, do they, have you
7 reviewed them and do they fit together do you think? Or how do
8 they, you know, how does that work? Do you need to change up
9 anything in 13?

10 A. I do not believe we need to change anything in 13
11 because the shipping percentages that we modified will then
12 just be the reciprocal to get to the diversion limits earmarked
13 in 13. So if it is a ten percent shipping requirement, the
14 diversion limits would be 90. And if it's a 50 percent
15 shipping requirement, the diversion limitations would be 50
16 percent.

17 Q. If you did -- if you did not have the Bulk Tank Handler
18 Provision, Proprietary Bulk Tank Handler Provision, would you,
19 would the producer milk provisions remain the same?

20 A. Could you be a little clearer on the question?

21 Q. If under Proposal 2, if you didn't have, you know,
22 what, 9(d), if 9(d) wasn't a part of the proposal, would you be
23 making any changes to what you now have on the table in terms
24 of Part 13 and 7(c)?

25 A. I guess I'll say I have to think about that. I don't

1 have an answer coming right off the top of my head. If you
2 would like to point me on something I should be aware of that
3 I'm not aware of, I would appreciate that. But I can't see a
4 change I would have made. If there was no 9(d) would we be
5 changing anything in 7 and 13? I would have to say no.

6 Q. In terms of moving from the CDFA call framework to the
7 order, old Order 68 call provisions, in terms of, what do you,
8 how do you contemplate that working in terms of geography of
9 both plants requesting a call and handlers required to serve a
10 call?

11 A. Preventing uneconomical movements would be my first
12 thought as we start talking about geography. It's my
13 recollection in Order 68 the times, that the one time the
14 Market Administrator was considering the call area to be both
15 the same for the distributing plants and the suppliers, but I'm
16 not sure that is a requirement. The Department, the MA could
17 pick, let's just say Los Angeles as the call area for the
18 distributing plant and then pick a supply region, Bakersfield,
19 as a potential supply area, I believe that flexibility is
20 there.

21 Q. Okay. So from a supplier, your perspective, how would
22 you, how would you anticipate that being defined? Let's assume
23 you have three cooperatives that proponent, the cooperatives
24 supporting Proposal 1 represent roughly 75 percent of the milk,
25 let's assume they, you know, that they report as under 9(c),

1 and you have, you know, I don't know, how would you define the
2 geography? Who would you include in the geography? You are
3 not going to have a reserve supply plant system, so I'm just
4 wondering how you see that working?

5 A. You know, from a standpoint again, the Cooperative and
6 the Proprietary Bulk Tank Handler has to have a plant somewhere
7 in the marketing area. If the MA has to pick a geography, he
8 would pick that plant that would be either the 9(c) plant that
9 the cooperative is using and/or the Proprietary Bulk Tank
10 Handler plant, so is the way I see it. And I guess I'm not a
11 hundred percent sure if under the current CDFA, and I was
12 looking for it, if they, I know they have two regions for CDFA,
13 and when they mention the two regions, I don't know if they
14 specifically mention a, let's just say CDI plant location or
15 just mention CDI, Land O'Lakes, and I can't find that exhibit,
16 so I was trying to see who was in Region Number 1 and how they
17 are actually worded.

18 Q. Would you anticipate, how do you anticipate the call
19 being quantified? It -- would it be, just be a, you know, say
20 you have got ten percent, would it just be the, you know,
21 addition, that the handlers identified would have to go to 12
22 or 15, or how do you anticipate the call being -- what's your
23 intention with respect to how the call would be quantified?

24 A. It would be that addition, just like you described it,
25 Marv, it would be if the call, if the current shipping

1 requirements is ten percent and the Market Administrator has
2 issued a call and would raise the shipping requirements to 12,
3 let's just say, that would be the new performance requirements
4 for the suppliers in that call region. I did mention there
5 were a number of, well, a credit given if you are already
6 supplying. Let's just say you are a supplier that happens to
7 be shipping 14 percent, and the call goes to, forces go from 10
8 to 12, if you notify the Market Administrator prior to the call
9 announcement going out, that 14 percent would actually service
10 or meet the call provision.

11 Q. So if it was going to be set at 14, anybody that was
12 already there or above would not be subject to the call?

13 A. Correct.

14 Q. Okay. Do you, in your call framework, do you
15 anticipate the call being applicable for a month or for some
16 other time period?

17 A. I would say it would be applicable for a month.

18 Q. And do you intend that it would, the timing for
19 requesting and for the Market Administrator to invite data and
20 comment, would be, I'm looking if I see the 15-day language.

21 A. You won't, it's not in there.

22 Q. Okay. So what time period do you anticipate would be
23 involved in that process?

24 A. I would think it would be very short. My history with
25 the Order 68, it took a phone call, it took a flight up, and it

1 was solved the next day.

2 Q. Well, I understand the informal resolution of the
3 issue, but in terms of the formal resolution of it, if a call
4 is actually to be issued, did you intend there to be no time
5 framework specified around the process of, you know, requesting
6 a call inviting data views and arguments, and then making an
7 order?

8 A. If a call is going to be requested by a handler, it
9 usually means it is a very real time situation, so giving
10 15-days notice or 30-day notice was not in our intent. If the
11 Market Administrator, under his own investigation, and/or a
12 request from a handler would need to make a quick decision.

13 Q. Now, have you considered in re-evaluating Part 7(c)
14 here, have you -- have you evaluated the appropriateness of the
15 10 percent in view of the existence of dedicated blocks of milk
16 that are committed to and pooled at distributing plants?

17 A. When you say considered, obviously, Class I markets
18 being served, but the performance standards with a Federal
19 Order as they operate throughout the whole country, performance
20 is necessary to associate with the pool. So is it a situation
21 that I'm concerned of those pre-existing contracts with
22 bottlers and their suppliers? Sure. But we would become, and
23 I'm speaking now as Hilmar, we would become a new supplier on
24 the block.

25 Q. Okay. But what I was -- what I was getting at was

1 something a little, just slightly different.

2 Okay. There are, you are aware, and I think, you know,
3 this is all within the, within in-house in the Dairy Institute
4 here, that there are blocks of independent producer milk at
5 some distributing plants, we have had some testimony about
6 some.

7 A. I am aware of that, yes.

8 Q. Okay. And there may be, you know, relationships with
9 smaller entities in the marketplace at some of the distributing
10 plants, that is, neither Hilmar, nor Land O'Lakes, CDI, or DFA,
11 there may be some other supplies that are already committed to
12 those distributing plants. My question is, if you are, you
13 know, if you are requiring 10 percent, you know, performance
14 from the rest of the marketplace, have you evaluated whether
15 that will, will or will not generate uneconomic shipments of
16 milk?

17 A. I don't know if it would generate uneconomic shipments
18 of milk because I don't know where all of the suppliers milk
19 supplies are in relationship to their manufacturing plants, but
20 certainly it would, it would require someone who is not a
21 supplier to the Class I market today to look for and search for
22 a Class I market in order to meet these pooling provisions,
23 assuming the manufacturer is going to want to be in the pool.

24 Q. Okay. Thank you, Al. I don't have any other questions
25 at this time for you.

1 JUDGE CLIFTON: Who next has questions for Mr. Zolin on
2 this topic, or these topics? I'm waiting for just a moment
3 just to see if there's anything further. Anything further for
4 Mr. Zolin?

5 Mr. Beshore, you may, let's -- why don't we take a
6 break. This is a good time for one, anyway. So, please be
7 back and ready to go at 10:40,

8 (Whereupon, a break was taken.)

9 JUDGE CLIFTON: We're back on record at 10:41. If you are
10 not seated, just become quiet please. Who has additional
11 questions for Mr. Zolin? Does USDA have any questions for
12 Mr. Zolin on this topic? Mr. Zolin, you wowed 'em. All right.

13 This is the last opportunity to ask questions of
14 Mr. Zolin for this entire hearing. Can anyone think of
15 something? Mr. English, redirect?

16 REDIRECT EXAMINATION

17 BY MR. ENGLISH:

18 Q. Mr. Zolin, you were asked some questions by Mr. Beshore
19 about Hilmar's going to need to qualify to ship 40 million
20 pounds to qualify its milk. Do you have any additional
21 comments on that?

22 A. Well, you know, again, I would go back to the comment I
23 made about assuming all the milk would be pooled, is the first
24 comment. Because again, Proposal Number 2 does not have
25 mandatory pooling associated with it. I made the comment

1 inefficient movements is something that Hilmar is concerned
2 about having to ship milk long distances, but I also understand
3 that milk currently moves fairly long distances to service
4 Class I needs. There's out-of-state milk going into
5 California, maybe Hilmar is located closer to those bottlers
6 that might require that milk, and we might have somewhat of an
7 advantage in supplying those markets. And as always,
8 flexibility is another key area that a Federal Order has to
9 have flexibility. And I think we have discussed the
10 Market Administrator does have flexibility to adjust shipping
11 requirements, if a 10 percent level is deemed too high,
12 creating inefficient movement. So those were the break
13 thoughts that I had.

14 Q. And that's all I have. And that's my last question,
15 assuming nobody else has any follow up for Mr. Zolin. And
16 thank you very much for your testimony.

17 A. Thank you.

18 JUDGE CLIFTON: Yes, very few of us in this room could
19 craft the technical language required for this kind of an
20 operation, and so we really appreciate the work that you and
21 your task force did, Mr. Zolin. Thank you so much.

22 MR. ZOLIN: Thank you.

23 JUDGE CLIFTON: Our next witness will be Dr. Schiek, so if
24 there are any exhibits to distribute, we'll do that now.

25 MR. ENGLISH: Your Honor, Chip English. Yes, there will be

1 two documents, testimony of Dr. William Schiek, Part 4, and a
2 series of Exhibits A through H, that are 45 pages in length.

3 JUDGE CLIFTON: It appears that everyone has received a
4 copy, and some extras are being placed on the back table, which
5 is great. All right.

6 It's 10:47. Ms. Frisius, will the testimony of
7 Dr. Schiek, Part 4, be Exhibit 145?

8 MS. FRISIUS: Yes.

9 JUDGE CLIFTON: All right. I'm marking mine as Exhibit
10 145.

11 (Thereafter, Exhibit 145 was marked
12 for identification.)

13 JUDGE CLIFTON: And I'm marking the exhibits as
14 Exhibit 146.

15 (Thereafter, Exhibit 146 was marked
16 for identification.)

17 JUDGE CLIFTON: The title of Exhibit A, the top document,
18 starts out Draft Guidelines. Mr. English, you may proceed.

19 DIRECT EXAMINATION

20 BY MR. ENGLISH:

21 Q. Thank you, your Honor.

22 Dr. Schiek, why don't you begin reading your statement
23 and I will periodically interrupt, especially to discuss the
24 documents that are in Exhibit 146, which I meant to call
25 attachments and ended up calling exhibits. So go ahead and

1 start with Exhibit 145, please, sir.

2 A. Okay.

3 Introduction

4 California's quota system has its origins in the
5 Gonsalves Milk Pooling Act, as testimony from earlier in this
6 hearing indicates. Under the current state milk pooling plan,
7 producers receive an extra 19 and a half cents per pound of
8 solids nonfat on their milk production that is covered by quota
9 as compared to the price they receive for milk not covered by
10 quota, or non-quota milk. As I mentioned earlier in my
11 testimony -- as I mentioned in earlier testimony (Exhibit 79),
12 pool quota came about as a means of compensating producers who,
13 historically, had a higher percentage of their milk shipments
14 to Class 1 uses under the contract system that was in effect
15 prior to pooling. According to earlier testimony from Dr. Eric
16 Erba, (Exhibit 42): "One of the declared purposes of the
17 Gonsalves Milk Pooling Act is to equalize gradually the
18 distribution of Class 1 and Class 2 utilization." The notion
19 of quota equalization, where all producers would eventually
20 have quota allocations that covered 95 percent of their
21 production base, was anticipated as the state's population and
22 Class 1 use grew. The goal of equalization, where prices paid
23 to producers would become more uniform or equal, has
24 similarities to the notion of paying uniform prices to
25 producers under FMMO's.

1 Regarding our proposal on quota, I want to clarify what
2 might be a major misperception. The Dairy Institute and its
3 members did not set out, nor is it our goal, to destroy quota.
4 As you have heard, some of our member companies purchase milk
5 from farmers who own quota. We understand how important quota
6 is to California's dairy farmers. At this hearing, we have
7 heard the testimony of dairy farmers who own little or no
8 quota, but who nonetheless support the quota program and the
9 continued payment of quota value in California out of the pool
10 first.

11 The question of how to deal with quota going forward is
12 not new or unique to this FMMO promulgation proceeding. The
13 California dairy industry has been discussing the future of
14 quota for some time -- for quite some time. In 1978, the
15 California legislature passed a statutory amendment that
16 brought about the equalization of all original production base
17 and pool quota that existed at the inception of the pooling
18 program, noting that equalization had not occurred as rapidly
19 as expected. Later, as Dr. Erba noted in his testimony
20 (Exhibit 42, page 8) CDFA appointed a committee of producers in
21 1991 to conduct listening sessions --

22 JUDGE CLIFTON: 19 what?

23 DR. SCHIEK: '91.

24 JUDGE CLIFTON: Okay.

25 DR. SCHIEK: -- to conduct listening sessions throughout

1 the state to receive comments and input on the milk pricing
2 regulatory system. In 1993, a quota bill passed in the
3 California legislature that resulted in a change in the
4 distribution of quota revenues. Prior to enactment of the
5 legislation, higher milk class revenues were allocated directly
6 to quota milk first, before any of those revenues were made
7 available for non-quota milk. After 1993, the current "fixed
8 differential" of 19 and a half cents per pound of solids
9 nonfat, or SNF, also (\$1.70 per hundredweight at standard milk
10 test) was put in place.

11 The change to the fixed quota premium (quota
12 differential) did not put an end to discussions about possible
13 modifications and/or termination of quota. In the early
14 2000's, producer representatives from different organizations
15 met to consider changes to the milk pricing and pooling plan.
16 The group was assisted by a trio of analysts with long
17 experience in the California dairy industry; Jay Goold, former
18 Manager of Western United Dairymen; Glenn Gleason, former
19 Chief, CDFA Milk Pooling Branch; and Dr. James Gruebele, former
20 CEO of Dairyman's Cooperative Creamery Association. Quota and
21 the possibility of terminating the program was something that
22 was discussed during the group's meetings. In 2005, the
23 California Milk Advisory Board (CMAB) commissioned a study of
24 California's dairy industry that focused on how the industry
25 could be successful in the face of mounting environmental

1 challenges and global competition. CMAB hired McKinsey &
2 Company to study the California dairy industry and make
3 recommendations about strategies the industry could pursue to
4 meet the dairy farmers' challenges with increasingly onerous
5 environmental regulation and associated costs. One of the
6 options put forward was the idea of creating a debt obligation
7 or bond that would be paid back from the pool but which would
8 provide revenue for quota holders to pay for costs associated
9 with meeting new environmental regulations

10 Summary of California State Level Review of the Quota Program

11 In 2007, then CDFA Secretary Kawamura established an
12 advisory committee to analyze the current situation of
13 California Milk Pool quota and consider possible changes to
14 quota. The committee was asked to "explore if quota should
15 continue, be modified, or retired." These three options had
16 subset questions, including identifying various modification or
17 retirement plans, the advantages or disadvantages of each
18 option, legal or legislative requirements for modification or
19 retirement, and the financial consequences of modification or
20 retirement. The committee was also requested to "seek producer
21 input prior to making recommendations to the Secretary for
22 action."

23 The committee members and the process they undertook
24 are summarized in the California Dairy Review from August 2007,
25 published by CDFA. The committee held six public meetings on

1 the issue and undertook an "in-depth review of the California
2 milk pooling program -- past and present." This publication
3 also summarized some of the areas that generated the most
4 discussion of the committee, including an analysis of the price
5 formula, the financial and legal investment needed to buy out
6 quota, how such a buy out would be funded, and regional quota
7 adjusters (RQA's) (Exhibit A).

8 Q. So your reference to Exhibit A there is Exhibit 146?

9 A. Correct.

10 Q. And Exhibit A is the first 13 pages of Exhibit 146?

11 A. That's correct.

12 Q. First, let me just note, I think because we didn't
13 print it in color some of the headings say on page 7, look
14 arguably a little out of focus. Is that because the color
15 version would actually sort of highlight it a little bit?

16 A. Correct. I think that's, I don't know, maybe that's
17 called embossing and the multiple colors makes it stand out.
18 In black and white it just looks fuzzy.

19 Q. Is there anything in particular right now that you want
20 to point out before you continue your testimony about
21 Exhibit 146?

22 A. I don't believe so.

23 Q. Okay. So why don't you continue then on page 4 of
24 Exhibit 145?

25 A. On August 9, 2007, the committee issued its QRC (Quota

1 Review Committee) Executive Summary. After review, the
2 committee of 11 voted as follows: Quota unchanged (6 votes),
3 modify quota, (0 votes), retire quota, (5 votes). Since the
4 required super majority for retirement was not met, that's 8
5 out of 11, the recommendation was that quota be left unchanged.

6 Similar to the Dairy Institute of California
7 discussions regarding our FMMO proposal, the committee tried to
8 work through a number of different options to address revision
9 to the quota program -- to address a revision to the quota
10 program. However, it was unable to agree on an acceptable
11 manner in which quota could be modified or retired. As part of
12 the third option, retiring quota, the committee considered a
13 self-funding annuity method, a sunset provision on the quota,
14 and a single pay out via revenue bond funding. However, for a
15 variety of reasons (which can be found in greater detail in
16 reviewing the meeting notes of the committee) these options
17 were considered unworkable.

18 The committee did make some conclusions regarding the
19 option of leaving quota unchanged. These included that quota
20 could just "go away" or be retired with no value to quota
21 holders (but that that outcome would be an unlikely one.) It
22 even concluded that the complication of quota helped them
23 preserve the status quo system: Quote from the committee:
24 "Quota helps protect the pool. If we, dairy producers, move to
25 a referendum to change one aspect of quota/pooling, everything

1 may be up for evaluation." They also found that quota added
2 complexity to the California pricing structure, "increasing the
3 difficulty to understand the system."

4 The committee was unable to agree on a way that the
5 quota system could be altered, when its only task was to look
6 at the system in isolation of other provisions. It is also
7 interesting that the group recognized that no more quota would
8 be issued without growth in the Class 1 and 2 utilization
9 growth. Given the difficulty the committee had grappling with
10 changes to quota, it is not surprising that the Cooperatives'
11 proposal does not attempt to alter the quota system in any way
12 that might lead to easier integration into and greater
13 compatibility with the way existing FMMO's work.

14 Placing Quota Within a California FMMO

15 As I discuss below, we have struggled with the quota
16 issue for this proceeding, but it is important, I believe, to
17 recognize that our struggle is not new, is not unique to our
18 organizations discussions, and is not unique to this
19 proceeding. Our belief is that our difficulty grappling with
20 how to place quota into a California Federal Order is actually
21 natural since the concept of quota does not fit comfortably
22 within the FMMO framework.

23 While there have been various plans in FMMO's (such as
24 base excess plans in old Orders 4, 5, 7, 11, and 46) in the
25 past, we understand that authorization for those provisions

1 have have expired (see Exhibits B through E). One of the
2 central features of FMMO's is to require that minimum regulated
3 uniform class prices are paid by handlers, and in turn, that
4 minimum uniform prices be paid to dairy farmers subject to
5 specific authorized adjustments.

6 Q. So let me stop you there. In the middle that paragraph
7 you reference Exhibits B through E. Is that also from
8 Exhibit 146?

9 A. It is.

10 Q. So let me have you describe what those are. Starting
11 on page 14 through page 16 is Exhibit B, and is that a copy of
12 the Agricultural Marketing Agreement Act as it existed in 1940?

13 A. It is. So this is an old, older copy of the
14 Agricultural Marketing Agreements Act.

15 Q. Okay. And then we turn to Exhibit C, which fortunately
16 we had a larger-type version. Thank you to the International
17 Dairy Foods Association, MIF legislative history, so we have
18 got pages 17, 18, and 19, which are the Agricultural Marketing
19 Agreement Act of 1937 as amended effective January 1, 1971. Is
20 that?

21 A. That's correct.

22 Q. Okay.

23 A. And this section contains a lot of the language that
24 describes how, what, the authorizations for base excess plans
25 and seasonal plans under the Orders.

1 Q. Okay. So let's look at that for a moment, and looking
2 at, starting on page 17 you have Section 5, and you have got
3 (A) and (B), moving over to page 18, under under (B)(ii) you
4 have got adjustments, these are the specified authorized
5 judgments you were referring to a moment ago on page 5 of your
6 testimony?

7 A. Correct.

8 Q. And (A), (B), and (C) we're familiar with, and they
9 exist today correct? As written?

10 A. Yes, that's my understanding.

11 Q. If you look at (D), there's language in (D) that says,
12 "to encourage seasonal adjustments in the production of milk."
13 Is it your understanding that doesn't exist today?

14 A. That's my understanding. When I look at the current
15 copy, those provisions are no longer there.

16 Q. Okay. So then starting at the semi-colon, before, so
17 before (E), on the page 18 you have got a paragraph (E),
18 correct?

19 A. Correct.

20 Q. And then you have got a clause (F), that's two lines
21 down, three lines down from (E), correct?

22 A. Yes.

23 Q. All on page 18, correct?

24 A. Correct.

25 Q. And then over on page 19, all the way down to the last

1 two lines where it is (C) you have additional language for
2 clause (F), correct?

3 A. Correct.

4 Q. Okay. All of that language expired with the '96
5 Farm Bill?

6 A. Again, that's my understanding, yes, that language went
7 away in 1996.

8 Q. Okay. So let's now turn to Exhibit D which is page 20
9 through pages 23, and you have referenced old Orders 4, 5, 7,
10 11 and 46. What was Order 4?

11 A. Order 4 was the Middle Atlantic Milk Marketing Order.

12 Q. And Order 5 was?

13 A. Order 5 was, I believe, Carolina.

14 Q. And then maybe later Appalachian?

15 A. Later the Appalachian, but it was Carolina in the
16 1980's and '90's before Federal Order Reform.

17 Q. And then Order 7?

18 A. Would have been the Southeast.

19 Q. Order 11?

20 A. Order 11, I believe was Tennessee.

21 Q. And Order 46?

22 A. I believe was the Louisville Order.

23 Q. Okay. To be clear, 11 might have been Tennessee Valley
24 is that?

25 A. Tennessee Valley, yes.

1 Q. Okay. So you have included in Exhibit D of 146,
2 Pages 20 through 23, is one example of the base excess language
3 from Order 4?

4 A. That's correct.

5 Q. Okay. So now let's turn to Exhibit E, which is pages
6 24 through 27 of Exhibit 146. And what is Exhibit E?

7 A. Exhibit E contains the amendments to the Orders where a
8 lot of the language pertaining to the base excess plan was
9 removed.

10 Q. So for instance, on page 25 in the middle column, could
11 you read just above the language that says "list of subjects in
12 7 CFR" that paragraph that starts after "consideration"? I'm
13 on page 25, which is 69017 of the Federal Register, and in the
14 middle column, just above "list of subjects" down at the
15 bottom.

16 A. Okay. After consideration of all relevant material and
17 other available information, it is hereby found and determined
18 that effective January 1, 1997, the provisions of each of the
19 orders specified below do not tend to effectuate the declared
20 policy of the Act.

21 Q. And then if you go up in that same column, in that same
22 page, to the first full paragraph after the two line carry
23 over, could you read from "regardless"?

24 A. Regardless of the possible economic effects which may
25 result from termination of seasonal base plans upon small

1 entities, there is no alternative to this termination action
2 since under, since the underlying statutory authority expires
3 on December 31, 1996.

4 Q. Okay.

5 A. In considering the impact --

6 Q. You can stop. That's, I'm sorry, just the one
7 paragraph.

8 A. All right.

9 Q. All right. Could you then return to your statement 145
10 on page 5?

11 A. So the starting point in our thinking about quota was
12 to look at the Cooperative proposal and see whether it would
13 work given our understanding of the purposes and goals of
14 FMMO's. We have already noted our concerns about the mandatory
15 pooling aspects of the Cooperatives' proposal. These concerns
16 include its lack of traditional pooling standards that would
17 direct milk to Class 1 uses and the way that it captures all
18 manufacturing plants in the state as pool plants, not allowing
19 those plants to operate as nonpool plants. The consequences of
20 what we view as the implications of mandatory pooling were
21 discussed in earlier testimony.

22 When we examined the Cooperative proposal, we first
23 concluded that the non-quota blend price concept, setting aside
24 the quota payment first from overall Producer Settlement Fund
25 proceeds --

1 JUDGE CLIFTON: Let me interrupt you, Dr. Schiek. Please
2 start again from the beginning of page 6.

3 DR. SCHIEK: When we examined the Cooperative proposal, we
4 first concluded that the non-quota blend price concept, that
5 is, setting aside the quota premium payment first from overall
6 Producer Settlement Fund proceeds, does not properly address
7 the issue of out-of-state dairy farmer milk that will end up
8 being part of any FMMO pool. Historically, all out-of-state
9 dairy farmers' milk was credited at the plant blend under the
10 California State Order (CSO). Those farmers could not, and did
11 not, own any quota, and the plant blend they received
12 compensated them for the fact that they did not have the
13 opportunity to receive a quota price. It is, of course, the
14 case that FMMO's have the right to pool out-of-state milk,
15 unlike the CSO. However, we believe that the out-of-state milk
16 must receive the traditional FMMO blend price without
17 subtraction of the quota premium.

18 The 1996 Farm Bill language, which to my knowledge, did
19 not specifically amend the AMAA is as follows: "The order
20 covering California shall have the right to reblend and
21 distribute order receipts to recognize quota value." I will
22 discuss this provision a bit more below, but our view is that
23 provision does not alter uniform payment provisions of the Act.
24 (7 USC Section 608c(5)(B)), or the "trade barrier" language,
25 (7 USC Section 608c(5)(G)). While a California FMMO can (and

1 should) include out-of-state milk in its market-wide pool, it
2 is our view that paying the quota premium before calculating
3 the FMMO non-quota blend price clearly expands the California
4 quota program to cover out-of-state milk, something it does not
5 do today.

6 Based on the foregoing, our starting point is that USDA
7 must, instead, establish, first, a traditional FMMO Producer
8 Settlement Fund in order to pay uniform prices to dairy farmers
9 who could never own quota and, as proposed, will not be
10 permitted to own quota going forward. Even if out-of-state
11 producers were allowed to purchase quota today, the fact
12 remains that original issued quota, which was never available
13 to out-of-state dairy farmers, was free. As we heard in
14 testimony from Desert Hills Dairy, some of those out-of-state
15 farmers have been shipping to California Class 1 plants for
16 generations.

17 Given our view that out-of-state producers must be paid
18 a traditional blend, our first thought was that we would have
19 two pools or pool calculations. One would pay the full order
20 blend price to out-of-state producers first, the remaining
21 funds would be apportioned to all California producers in the
22 pool, on the basis of quota and non-quota prices that would be
23 calculated after the payments to out-of-state producers have
24 been made. Under our original concept, there would have been
25 no option for California producers to opt out of the

1 quota/non-quota payout system, and no option for them to
2 receive a traditional order blend. Based on our earlier
3 concerns about mandatory pooling, our concept as we were
4 thinking about it, would also have allowed for handlers to
5 elect not to pool their milk subject to repooling restrictions.

6 We next examine the consequences of this quota concept.
7 There has been discussion of an Arizona pool distributing plant
8 that is presently fully regulated on the Arizona FMMO, yet with
9 significant route disposition into California. We believe from
10 our knowledge of that plant, that it will likely easily meet
11 the Section 1051.7(a) "pool distributing plant" definition
12 under either Proposal 1 or 2. We see at least two additional
13 problems with the cooperatives' treatment of quota as applied
14 to that operation (or any similarly situated operation that is
15 located out-of-state and ends up being fully regulated under a
16 new California FMMO.)

17 First, it is our understanding that this plant receives
18 producer milk from both Arizona and California dairy farmers.
19 Again, we assert that the Arizona dairy farmer must receive the
20 traditional FMMO blend price and not the non-quota blend price.

21 JUDGE CLIFTON: Let me ask you there, you left out the word
22 "milk" in the sentence, and if you want it in there, I would
23 like to you read the sentence again.

24 DR. SCHIEK: Okay. First, it is our understanding that
25 this plant receives producer milk from both Arizona and

1 California dairy farmers. Again, we assert that the Arizona
2 dairy farmer milk must receive the traditional FMMO blend price
3 and not the non-quota blend price. But the California dairy
4 farmer shipping to that plant almost certainly owns no quota
5 based upon CDFA's quota holding requirements. So then we have
6 two dairy farmers, both shipping to an Arizona milk plant, who
7 today receive the traditional FMMO blend price under the
8 Arizona FMMO. If Proposal 1 were adopted, but with a
9 requirement that out-of-state milk be paid a traditional blend,
10 the two producers would find themselves treated differently --
11 the Arizona producer getting the traditional blend price, and
12 the California producer receiving the lower non-quota blend
13 price. That result makes us extremely uncomfortable, both
14 1) because the California dairy farmer is currently receiving
15 the Arizona FMMO blend price today and would, just because a
16 new California FMMO is created, receive a lower price that is
17 not a traditional FMMO blend price; and 2) because that
18 California dairy farmer shipping across state lines into that
19 Arizona plant would receive a lower FMMO minimum price than the
20 Arizona farmer simply because of his farm's location.

21 The second problem we identified is that the Arizona
22 plant will be contributing to the quota premium through the
23 pool on any California milk purchases, unlike what happens
24 today. To the extent that the plant -- to the extent that that
25 plant attracts a milk supply today using at least the full FMMO

1 traditional blend, the logical economic impact is that the
2 California milk supply will look to recoup some or all of its
3 lost revenue to over order premiums. This will increase the
4 Arizona plant's procurement cost and disadvantage that plant in
5 distributing products into the state, and as a result, will, in
6 a manner, limit the marketing of milk products into California.
7 That is our thinking. So when examining these transactions
8 between California dairy farmers and out-of-state pool
9 distributing plants, we conclude that such plants and the dairy
10 farmers who supply them, must be subject to the traditional
11 FMMO blend price program, just like out-of-state dairy farmers
12 whose milk is pooled under the order.

13 A California dairy farmer shipping to the Arizona plant
14 as we just described, will most certainly have neighboring
15 dairy farmers in California who will be subject to the
16 California quota program. Today, that California farmer
17 shipping to an Arizona pool distributing plant receives a
18 traditional FMMO blend price, while the CSO producer on his
19 overbase milk, receives the state's announced overbase price.
20 This situation is a consequence of the California State Order,
21 CSO and FMMO pricing systems existing side by side. Under a
22 California FMMO as proposed by the cooperatives, and with the
23 modifications that we believe will need to be made, it would
24 now have two dairy farmers located near each other, receiving
25 non-uniform regulated prices under the FMMO. The only thing

1 creating that new problem is the geographical distribution of
2 their milk to plant locations in different states under a
3 California FMMO with quota/non-quota pricing.

4 The cooperatives will maintain that the situations we
5 subscribe described are why the Order needs to take quota off
6 first and establish a non-quota blend for all milk, including
7 out-of-state milk. But our view is that paying producers
8 differently on the basis of quota holdings would seem to
9 violate the notion that all producers should receive a uniform
10 price, with the exception of allowable adjustments. This is
11 particularly true because the Farm Bill language merely says,
12 "the Order covering California shall have the right to reblend
13 an distribute order receipts to recognize quota value." The
14 cooperatives and their supporters have used many terms or
15 phrases that do not appear in the legislation, that we believe
16 alters the meaning of the words used by Congress.

17 (See Exhibit F).

18 BY MR. ENGLISH:

19 Q. So please stop, and please turn to page 28, and again,
20 Exhibit F of Exhibit 146, correct?

21 A. Correct.

22 Q. So if you turn to page 28, and first, this is just a
23 sample, correct?

24 A. Yes, I believe this is a sample.

25 Q. It is not intended to be exhaustive?

1 A. It is not exhaustive, correct.

2 Q. So without reading in all the language, we have got
3 eight examples, could you just put in the record the, in the
4 highlighted and underlined words that reflect your thinking
5 about Exhibit F as it applies to the statement you just made on
6 page 9 of Exhibit 145?

7 A. Well, I think what we're pointing out here is we have
8 just read the language and the words that are in that language,
9 these were additional words that Cooperative witnesses have
10 used to color or interpret that language. One word identified
11 first is "retaining", another would be "maintaining", another
12 would be "authorization", another would be "not in any way be
13 diminished or effective, affected", another would be "allow for
14 the continuation of the quota program", "the quota program
15 should have the right to exist", again, "not in any way
16 diminished or affected", that the "quota would be not in way
17 diminished or affected", that "the legislation allows for the
18 continuation of the quota program", and that "the full economic
19 value must be determined and maintained", and that "the
20 language authorized the Federal Order that incorporates quota".
21 And our point is that none of those words appear in the
22 statute.

23 Q. So if you could return to your testimony on page 9,
24 Exhibit 145.

25 A. Of particular note is the fact that the California Food

1 and Agricultural Code Section 62712(e) says, and I quote, "All
2 pool quotas initially determined or pursuant to Section 62707
3 shall be recognized and shall not in any way be diminished."
4 Congress could have used that precise phrase, but did not.
5 Nor did Congress amend the provisions requiring uniform payment
6 to producers or those preventing "barriers" to out-of-state
7 milk, this would be Section 608c(5)(B) and 608c(5)(G). Even if
8 the cooperatives' altered interpretation is correct, Congress
9 did not say, that the value of quota could only be recognized
10 in the fashion presented in Proposal 1. Indeed, the
11 cooperatives take it even further by enhancing the value of
12 quota at the expense of out-of-state milk, rather than simply
13 recognizing quota. The difficulties associated with fitting
14 quota into the FMMO structure is a conundrum that was not
15 created by the Dairy Institute.

16 So our belief is that USDA cannot treat those two
17 California Dairy Farmers differently, relying on the "recognize
18 quota value" language. The combined weight of these concerns
19 what brought us to our proposal as submitted to USDA. And is
20 part of Proposal 2 as contained in exhibit -- that should say
21 1. First, all out-of-state producers will receive the
22 traditional FMMO blend for their milk pooled in California.
23 For California, the basic concept is that there are two options
24 for producers. Producers may continue to receive
25 quota/non-quota prices, or they may opt to be paid the

1 traditional FMMO blend for the California order. The
2 traditional blend value applicable to those producers who elect
3 to be paid on a quota/non-quota basis, will be transferred to
4 the California Department of Food and agriculture (CDFA) for
5 reblending and distribution to producers. By giving producers
6 the choice to opt out of quota/non-quota pricing, our view is
7 that uniform payment provisions of the Act are satisfied
8 because it is the producers -- should say who, are electing to
9 be paid differently, as opposed to the order requiring that
10 they be paid differently. We also note that by paying the
11 traditional blend rather than the non-quota price to
12 out-of-state producers, we are not creating a trade barrier
13 with respect to such milk.

14 An overview of the quota provisions and the operation
15 of the Producer Settlement Fund is as follows: Quota terms and
16 reporting requirements are defined in Section 1051.11. The opt
17 out provision, Section 1051.68, for producers who wish to be
18 paid on the basis of a traditional FMMO blend is also included.
19 Provisions regarding payments to the Producer Settlement Fund
20 are contained in Section 1051.71, while payments from the
21 Producer Settlement Fund are specified in Section 1051.72. The
22 proposed order language also contains provisions for partial
23 payments to producers and Cooperative associations (Section
24 1051.73.) We also note that our proposal contains plant
25 location adjustments for producer milk and nonpool milk

1 (Section 1051.75) as is common in all other FMMO's.

2 I believe that most here are aware that we modeled
3 these provisions on the Oregon program. The language we used,
4 excuse me, the language used in the pool payments provisions
5 are based on those in the Oregon-Washington Order as published
6 in the Federal Register (34 Fed. Reg. 17684, 17711-17712
7 (October 31, 1969.)) The mechanism for irrevocable election by
8 a California dairy farmer is found in Section 1051.68. Under
9 this provision, the Market Administrator gives initial notice
10 of his intent to make payment of producer's returns to
11 producers who participate in the quota program, which would be
12 any California producer whose farm, whose milk is received at a
13 California plant. So producers are "in" unless they choose
14 irrevocably to "opt out" in writing before the first day of the
15 month that they want to be paid the uniform or order blend
16 price.

17 The partial payment would essentially work as with
18 other FMMO's (Section 1051.73.) A partial payment will be made
19 by handlers to producers who are not being paid through
20 cooperatives for milk received during the first 15 days of the
21 month. Such payments to individual producers will be made on
22 or before the 26th of the month. Partial payments for milk
23 received from Cooperative association members must be made on
24 or before one day in advantage of the date that such payment is
25 required to be made to individual producers. I'm using the

1 term individual producers here to apply to producers who aren't
2 being paid by cooperatives. Payments for milk received from
3 Cooperative association pool plants, or from Section 1051.9(c),
4 or Section 1051.9(d), handlers, must also be made on or before
5 one day in advance of the date that such payment is required to
6 be made to individual producers. Partial payments are to be
7 made at not less than the lowest class price for the preceding
8 month. Provisions are made for payments by handlers to
9 producers and Cooperative associations in unusual circumstances
10 such as death or inability to locate the payee in order to make
11 payment. The information that must accompany payments to
12 producers is also specified.

13 Under Section 1051.71, handlers make payment to the
14 Producer Settlement Fund. These payments must be made no later
15 than the 15th day after the end of the month. Payment shall be
16 the amount, if any, that the total value of milk to the handler
17 is in excess of the aggregate amount paid to producers or
18 Cooperative associations.

19 In order to calculate and facilitate payment of the
20 traditional FMMO blend and then the quota value, one hundred
21 percent of the final payment would be made to the Market
22 Administrator -- to the Market Administrator. The Market
23 Administrator, pursuant to Section 1051.72, would calculate an
24 amount due each producer based upon the volume of producer milk
25 times the producer price differential (at location value under

1 Section 1051.75), plus butterfat pounds times the butterfat
2 price, plus the protein pounds times the protein price, plus
3 the pounds of other solids times the other solids price, make
4 adjustment, if any, for somatic cell adjuster, reduced by the
5 partial payment made under 1051.73 and less an amounts due for
6 market services under Section 1051.86, and less authorized
7 deductions from the producer. Final payment is usually a
8 handler function, but given that money will need to move to
9 CDFA, for distribution, we could not find a way to recognize
10 quota, meet the requirements to pay uniform prices to
11 producers, and leave this final distribution in the hands of
12 the handlers.

13 California dairy farmers who do not elect to leave the
14 California quota program would have all monies due, have all
15 monies due, paid by the Market Administrator to CDFA for
16 redistribution of order proceeds under California's quota
17 program. It's under Section 1051.72(c)2. Out-of-state dairy
18 farmers and those California farmers who elect under
19 Section 1051.68, to irrevocably receive the traditional FMMO
20 blend, would be paid directly or as a handler payment to their
21 cooperatives for their milk based upon this method, unadjusted
22 for quota (Section 1051.72(b) and (c)(1)). Individual
23 producers must be paid on or before the 18th day after the end
24 of the month, while funds would be paid to Cooperative
25 associations and CDFA on or before the 16th day after the end

1 of the month.

2 In putting together this proposal, we knew that there
3 was some risk that the quota program would erode over time,
4 even as the Oregon program did over 18 plus years, but we also
5 acknowledged that USDA's preliminary economic analysis
6 conclusions were significantly faster in light of the Oregon
7 history than we anticipated. Despite the preliminary economic
8 analysis conclusions on a pure economic basis, we continue to
9 recognize that quota has had more staying power than would be
10 suggested by looking at just the revenue stream of various
11 alternatives. As noted above, regarding California non-quota
12 holders support for the quota, there is something more going on
13 that is undergirding the California quota system.

14 CDFA, I should say this is Exhibit 61 by CDFA, Table
15 AB, shows that more than 50 percent of the farmers in
16 California own 30 percent or less production quota. Farmers
17 with more than 50 percent of the solids, hold less than 35
18 percent of the total production quota -- that should be quota.
19 Doing some calculations with the data in this table suggests
20 that at least 62 percent of the producers representing 63
21 percent of the pool milk, would receive a higher price under a
22 traditional blend than under quota/overbase pricing. Strictly
23 speaking, and looking at pure economics, one would think that
24 political support for quota would be low, but that is hardly
25 the case. As such, it may be that the economic decisions

1 suggested by the Preliminary Economic Analysis and
2 Mr. Hatamiya's testimony, may not happen in the timeframe
3 expected. Regardless, the Dairy Institute does propose to
4 recognize quota value, but not in the manner done by the
5 cooperatives under Proposal 1, and it is what we see as the
6 limitations of the federal statute that pushed us to these
7 conclusions.

8 So what we proposed was based on our thinking about how
9 to wrestle with quota within a California FMMO. It attempts to
10 reflect both of the Farm Bill language about recognizing quota,
11 and the AMAA provisions that speak to uniform prices to
12 producers and trade barriers. But the foregoing is not the end
13 of our story or our discussions. We have certainly looked at
14 options throughout this hearing. While we do not have
15 consensus, we have discussed an alternative concept the
16 Secretary might consider when reviewing his options for a
17 California FMMO.

18 Recognizing the Value of Quota

19 A number of witnesses in this hearing, and a number of
20 reports on the history of FMMO and CDFA milk regulation, have
21 described the market chaos and inequity that preceded
22 government milk price and pooling regulation. Some producers
23 have a significant price advantage because they marketed their
24 milk to the more lucrative Class 1 market. Other producers
25 engaged in destructive competition to gain part of that, of the

1 higher valued market. Cooperatives had little bargaining
2 leverage to help even the playing field, and handlers played
3 one group of producers against the other.

4 At the request of dairy farmer cooperatives, USDA
5 created milk orders that required handlers to pay classified
6 minimum milk prices based on the handlers use of milk, and
7 distributed a revenue blend or uniform price to producers
8 irrespective of handlers use of their milk. In the FMMO model,
9 producers who enjoyed a Class I advantage before regulation,
10 immediately lost their favored status and received the same
11 uniform price as other producers when market-wide pooling
12 became effective.

13 California's route was somewhat different. From the
14 1930's to the late 1960's, CDFA regulated minimum milk prices
15 but did not prefer, did not provide for market-wide pooling of
16 milk revenues. Producers who sold to Class 1 plants,
17 therefore, received a much higher price than producers who did
18 not have a Class 1 market.

19 The Gonsalves Milk Pooling Act and a subsequent pooling
20 plan sought to introduce market-wide pooling to the California
21 system, but attempted to do so gradually. Producers with a
22 high share of the Class 1 market before pooling were permitted
23 to retain the benefit of historic use of their milk in Class 1
24 through the quota allocations they received, entitling them to
25 a higher quota pool price on those allocations. This, it was

1 thought, would induce the high Class 1 producers to approve of
2 a pooling system. The expectation was that more quota would be
3 issued to the less favored producers as Class 1 sales
4 increased, and pool revenue distribution would eventually
5 equalize among producers. As we know, this did not happen. In
6 nearly 50 years since revenue pooling was first authorized in
7 California, the state dairy industry, CDFA, and the state
8 legislature have grappled unsuccessfully with the problem of
9 quota and methods by which uniform pricing following the
10 federal model might be achieved.

11 The 2014 Farm Bill authorized Federal Milk Order
12 regulation for California with a caveat that USDA recognize
13 quota value. The cooperative proposal, Proposal 1, assumes
14 that Congress allowed USDA to incorporate the current state
15 quota system into a Federal Milk Order. Perhaps so, but if
16 this is the only on Congress intended, it would have been easy
17 to express it clearly. The problem with incorporation of quota
18 into a Federal Milk Marketing Order is the tension that it
19 creates with a purpose of the AMAA. The Federal Court of
20 Appeals Decision in Blair v. Freeman, 370 F.2d 229
21 (D.C. Cir. 1966) -- I'm going to start that sentence again.
22 The Federal Court of Appeals decision in Blair vs. Freeman has
23 interesting parallels with the quota issue. In that case, USDA
24 provided a nearby price differential to producers located close
25 to population centers and close to fluid milk plants that

1 supplied the market. The nearby differential was designed by
2 the Secretary to compensate nearby producers for the reduction
3 in their share of the fluid milk market resulting from their
4 inclusion in the blended uniform price system -- and that was a
5 quote, I'm sorry, it began with quote, "the nearby differential
6 was designed by the Secretary to compensate nearby producers
7 for the reduction in their share of the fluid milk market
8 resulting from a conclusion that the blended uniform price
9 system," end quote, Blair at 236.

10 Noting that "the core of the Congressional program was
11 a uniform minimum price for producers that did not turn or vary
12 with" handler use of milk. The court held "irrespective of
13 motive, the act forbids consideration of the use to which the
14 milk of a particular producer or class of producers is put,
15 historically, or potentially, in adjusting the uniform minimum
16 price to be paid to such producers." Blair at 237.

17 So is adjustment of producer prices by quota a payment
18 based on historic use of the quota holders -- it should say
19 Class 1 SNF volume -- permitted? In our view, no, unless the
20 2014 Farm Bill is read very differently, and we don't think it
21 can or should be. But even if it is, it would still be
22 intention with the core AMAA objective of market-wide revenue
23 pooling provisions that were not modified by Congress.

24 Our view is that the Secretary has the potential
25 opportunity to equalize milk revenue distribution of among

1 California producers as is done in all current Federal Milk
2 Order markets. As long as the "value of quota" is recognized,
3 this might be done gradually or quickly. But the U.S.
4 Secretary of Agriculture should be reluctant to perpetuate with
5 no end in sight, a payment system that strikes at the heart of
6 the federal program.

7 If incorporation of the existing quota plan into
8 federal regulation is authorized, USDA should expressly reserve
9 the option to gradually correct any non-uniformity in the
10 distribution of milk revenues to California producers.

11 A means to commence that process in the near future, or
12 when the Secretary may deem it appropriate, can be incorporated
13 by a simple addition under miscellaneous provisions at the end
14 of a Federal Milk Marketing Order for California as follows:

15 MR. BESHORE: Your Honor? Your Honor? I have an objection
16 to this proposed modification.

17 JUDGE CLIFTON: State who you are and begin again.

18 MR. BESHORE: Marvin Beshore. Before Dr. Schiek reads this
19 proposed modification, I have an objection. Of course,
20 modifications to proposals are properly brought, such as
21 Mr. Zolin's many modifications, such as Mr. Zolin's earlier
22 today. However, this is a proposed modification which would
23 not have been included in the Hearing Notice because it is
24 plainly explicitly not authorized by the Act in its regulations
25 and, therefore, it should not be heard in this hearing.

1 Now, what I'm -- what I'm talking about is the Revision
2 Request Notice and Comment Proceedings to change the payment
3 regulations of an order. The Act as embodied in
4 Section 7 CFR Section 900.32 regarding informal rule making,
5 specifically only authorizes informal rule making for non-price
6 issues. I'll quote it, "USDA may elect to use informal rule
7 making procedures under 553 of Title 5, United States Code, to
8 amend Federal Milk Marketing agreements and orders, other than
9 provisions that directly affect milk prices. In making this
10 determination, consideration shall be given to the nature and
11 complexity of the proposal, the potential regulatory and
12 economic impacts on affected entities, and any other relevant
13 matters."

14 This requested notice and comment provision, which is
15 553, as in Reg. 900.32, this notice and comment provision would
16 clearly affects blend prices, milk prices to producers, and
17 it's a provision, which, if it had been pre-submitted to the
18 Department in a proposed order, would not have been noticed,
19 because it's plainly, explicitly, not authorized. So I object
20 to it and we should not hear it in the proceeding.

21 MR. ENGLISH: Your Honor, there's a whole lot in this
22 proceeding that is extraordinary.

23 JUDGE CLIFTON: Go ahead.

24 MR. ENGLISH: Chip English. There's a whole lot in this
25 proceeding that's extraordinary, including what one might have

1 said should have been included in the hearing notice of an
2 improper and illegal attempt to maintain quota at the expense
3 of out-of-state dairy farmers, to maintain quota that's not
4 consistent with the Federal Order statute with respect to
5 recognize quota value. There's no harm in this witness at this
6 point, testifying about what could be done, and we can have
7 legal argument about what that could be. If we're going to
8 say, we're going to argue about what may or may not be
9 permitted, then we might as well go back to Day 1 and start
10 arguing about whether the Hearing Notice should have been
11 issued. Because the fact of the matter is, Proposal 1, in our
12 view, plainly relies on a language that does not amend the
13 AMAA, unlike what was done by Congress back in 1965 and 1970,
14 that led to provisions on Exhibit C of Exhibit 146 that covered
15 two full pages of text that don't exist today. And that's
16 because Congress knew how to modify uniform prices and they
17 didn't do that now. So if we're going to make the argument
18 that you can't testify on page 17 about this possibility of
19 something being done, or maybe a modification to it that could
20 cover it under formal rule making in some way, then -- then we
21 might as well be arguing all day long about whether any
22 provision should be heard at all, and we have not done that.

23 And what's sauce for the goose is sauce for the gander.
24 The fact of the matter is that, yes, we have a Hearing Notice.
25 We don't believe that the statute remotely says anything like

1 the co-ops want it to say, and if we want to say then,
2 therefore, that it should never have been heard, we could have
3 said that. The same argument applies.

4 JUDGE CLIFTON: Mr. Beshore?

5 MR. BESHORE: Marvin Beshore. Just a very brief reply.
6 The Secretary had before him the arguments which Mr. English
7 has stated now and rejected them and published the Hearing
8 Notice. This proposed modification was not before the
9 Secretary. That's the difference.

10 JUDGE CLIFTON: All right. Your very strong objection,
11 Mr. Beshore, is noted. Very interesting for Mr. English to use
12 the language "improper and illegal". You know, there's going
13 to be a lot of work done in Agricultural Marketing Service of
14 the U.S. Department of Agriculture determining just what is
15 allowed and is not allowed under the statute and everything
16 that has gone before us before today in interpreting it. I
17 have no idea what the ultimate decision will be.

18 First of all, one of the key issues, as Mr. English
19 points out, is there is a great deal of difference between
20 opinions about whether there's disorderly marketing in
21 California. That's a threshold issue.

22 This quota issue is so complicated that I will gladly
23 entertain anybody's ideas about how to do it. Mr. Beshore,
24 your objection is noted, and it is a strong caution to the
25 Department that this suggestion may not be legal, but I'll

1 still hear the evidence on it.

2 Mr. English, did you have anything further on that
3 issue?

4 MR. ENGLISH: No, your Honor, I think he can continue on
5 page 17.

6 JUDGE CLIFTON: Okay.

7 DR. SCHIEK: Okay. This is a citation of language,
8 Section 1051.91. The Administrator may, by notice and comment
9 rule making, prescribe a procedure or method to equalize blend
10 prices among producers by removing from this order provisions
11 relating to payment of quota, of a quota premium for some milk
12 and a non-quota price for other milk. These terms are defined
13 in Section 1051.17.

14 JUDGE CLIFTON: So Dr. Schiek, when you said this is a
15 citation, what this truly is is, as you said on the previous
16 page, proposed language?

17 DR. SCHIEK: Proposed language, that's correct.

18 JUDGE CLIFTON: And it's proposed language that wasn't in
19 Exhibit 1.

20 DR. SCHIEK: Correct.

21 JUDGE CLIFTON: And it was developed while we were here at
22 this hearing?

23 DR. SCHIEK: It was.

24 JUDGE CLIFTON: Okay. All right. You may continue to read
25 on page 17.

1 DR. SCHIEK: Although the efforts of the dairy industry and
2 regulators in California have not resulted in a solution to the
3 quota problem, these efforts have been constrained by state law
4 that does not constrain USDA's innovation in finding
5 alternative ways to "recognize quota value".

6 We have not found a consensus solution that addresses
7 all the concerns we have outlined in the relatively short time
8 since USDA received the Cooperative proposal. Clearly,
9 California producers are on a regulatory train that perpetuates
10 a form of the current quota system. But given time, USDA may
11 come up with solutions. We have, however, considered another
12 solution.

13 For example, quota certificates could be converted to
14 freely negotiable instruments unrelated to milk or SNF
15 production, having the same total economic value of quota
16 espoused by cooperatives' witness, Mr. Lon Hatamiya. Before
17 proceeding, which we should note, however, that the current
18 quota price of \$525 may overstate value of total quota. In a
19 recent publication, Dan Sumner and Jisang Yu called The
20 Agricultural Act of 2014 and Prospects for the California Pool
21 Quota Market, from the Journal of Agribusiness, Fall 2014,
22 pages 193 through 2006, Exhibit G --

23 BY MR. ENGLISH:

24 Q. 206, not 2006.

25 A. Sorry, 293 through 206, Exhibit G, observe that the

1 rise in quota prices during the spring and summer of 2014 may
2 be attributed to a producer perception of lower risk in quota
3 ownership due to the Farm Bill (page 204). The authors also
4 suggest that if an FMMO produces higher milk prices, the value
5 of quota will diminish and the opportunity of plants or
6 producers to depool in an FMMO would also diminish quota value.

7 To my understanding, the view of Sumner and Yu seem to
8 suggest that Mr. Hatamiya's calculation of total economic value
9 of quota is probably nearly as high as it can get. The fact
10 that interest rates are currently low would also drive up quota
11 prices, since it takes a greater investment to produce a target
12 income stream when interest rates are low than when interest
13 rates high. However, the purpose, for the purpose of
14 constructing an example, we use Mr. Hatamiya's estimate. Thus,
15 the total economic value of nearly 1.2 billion which creates --

16 JUDGE CLIFTON: 1.2 billion what?

17 DR. SCHIEK: Dollars. Plus the total economic value of
18 nearly \$1.2 billion, which creates for all quota owners an
19 annual income stream of \$139,329,759.23 (Exhibit 54, page 16).
20 That is the annual payout at variable quota rates with some
21 payments adjusted for farm location or RQA's. Converted to
22 equal monthly installments, the quota payout total
23 \$11,610,813.27 per month.

24 Several witnesses, including Mr. Hatamiya, likened the
25 quota investment and payout to an annuity. An annuity is a

1 similar asset providing an income stream over time from an
2 annuity price investment. An annuity investor may determine
3 what income stream a fixed investment will produce over
4 variable durations of annuity payouts, or determine what amount
5 of annuity investment is required to produce a targeted income
6 stream over a targeted period of time. For quota in the
7 aggregate, we know the quota investment value, approximately
8 \$1.2 billion, and the periodic income stream payment,
9 approximately \$11.6 million per month, so the full economic
10 value of the quota can be recognized by an annuity calculation
11 to determine the number of months of payout of \$11.6 million
12 needs to be made to conform to the full \$1.2 billion current
13 economic value.

14 Fortunately, the calculation required is made fairly
15 simple by banking website annuity calculators, such as the
16 calculator on the bankrate.com website. For the calculation, a
17 growth rate is also required. We used an investment growth
18 rate of 0.01 percent because of low, of current low interest
19 rates and the need to impute a conservative low risk investment
20 for this purpose. Any imputed growth rate would project an
21 increase in quota prices and thereby total economic value as
22 defined in this example. Quota provides an income stream and
23 not necessarily investment growth, so we use a nominal growth
24 rate in the annuity calculator. Thus, on the annuity
25 calculator, the starting principal is \$1,163,388,061.50. The

1 withdrawal amount is \$11,610,813, and the growth rate is 0.01
2 percent. The solution to the inquiry, length of payouts is
3 8.36 years (Exhibit H). In other words, recognition of the
4 value of quota can be fully accomplished by a payout over
5 8 years and 4 months of exactly the same monthly amount now
6 being paid to quota owners.

7 The sum of such value could be designated an obligation
8 or debt of the California Milk Pool, except USDA should still
9 deal with out-of-state milk in an appropriate way and paid out
10 as a form of annuity over a period of about 8.4 years. An
11 illustration of this is shown on the annuity calculation from
12 the bankrate.com website, which is attached, and that's
13 Exhibit H. The amount paid each month to retire the debt in
14 this illustration is exactly the amount that is paid out each
15 month in the form of quota premium milk prices, as calculated
16 by Mr. Hatamiya.

17 As we noted throughout this testimony, quota remains
18 difficult to incorporate into an FMMO. The solution contained
19 in Proposal 2 sought to reconcile the issue of -- and this is,
20 should be changed from "reconciling" to "recognizing" quota,
21 with the need to pay producers uniformly and avoid putting up a
22 trade barrier by forcing out-of-state producers to receive the
23 overbase price. In our view, Proposal 1 has the shortcomings
24 of its mandatory pooling aspects, its perpetuation of
25 non-uniform payment to producers, and its denying the

1 traditional order blend price to out-of-state producers. We
2 have looked at options other than what was contained in our
3 proposal as a way to recognize quota value. The annuity
4 proposal discussed above is one such example. Dairy Institute
5 does not endorse this particular solution at this time, but it
6 illustrates that there are solutions that recognize quota value
7 without unending perpetuation of non-uniform blend prices to
8 producers.

9 BY MR. ENGLISH:

10 Q. Now, at the very end of your statement on page 20 you
11 have six end notes, and has become the custom now, we're not
12 asking the court reporter to transcribe those into the
13 transcript, it will just carry over with Exhibit 145, correct?

14 A. Correct.

15 Q. Okay.

16 JUDGE CLIFTON: Just to summarize the end notes,
17 Dr. Schiek, it appears that all but one of them are references
18 to the California Department of Food and Agriculture website;
19 is that true?

20 DR. SCHIEK: I actually believe that all of them are
21 references to the -- well, they are all references to that task
22 force on quota from 2007. There's one, the California Dairy
23 Review Publication, that was a separate write up of the summary
24 of what took place and what's in those other exhibits.

25 MR. ENGLISH: But all of that is actually part of Exhibit A

1 to 146, correct?

2 DR. SCHIEK: Correct.

3 MR. ENGLISH: So the end notes are there, but frankly, your
4 Honor, it is all part of the exhibit. As we were developing
5 things, we ended up adding that.

6 JUDGE CLIFTON: Excellent. All right. So Mr. English,
7 what I would like to do next is go back through and have
8 Ms. Frisius and I coordinate on the little changes that were
9 made in Exhibit 145.

10 Do you want to begin that process or shall I begin with
11 what I noted?

12 MR. ENGLISH: Well, maybe we could do it together for
13 efficiency purposes, and I'll start on a page and say that's
14 what I have, and then you can chime in, does that make sense?

15 JUDGE CLIFTON: Excellent. So Ms. Frisius, you are ready
16 to copy regarding Exhibit 145?

17 MR. ENGLISH: And I have got one on page 1, the fifth line
18 down, he read, "as I mentioned in earlier testimony, Exhibit
19 79, pool quota came about as a means of compensating
20 producers." So unless Dr. Schiek disagrees with me, I would
21 propose we insert the word "a" between "as" and "means".

22 DR. SCHIEK: I would agree.

23 JUDGE CLIFTON: Done.

24 MR. ENGLISH: And that's what I have on page 1, your Honor.

25 JUDGE CLIFTON: All right. That's all. I didn't even have

1 that one. Well, you are going to get to chime in here, because
2 I don't have any for until --

3 JUDGE CLIFTON: I have page 2.

4 MR. ENGLISH: I don't have anything until page 7, your
5 Honor.

6 JUDGE CLIFTON: All right. So page 2, the third line up
7 from the bottom, Dr. Schiek, you read that line on "how the
8 industry could be successful in the face of mounting
9 environmental challenges" and so there's an insertion of the
10 word "of" after the word "face". Do you want that?

11 DR. SCHIEK: Yes, I do.

12 JUDGE CLIFTON: Okay. Done. Then, I also have nothing --
13 I have something on, yeah, page 7 is the next I have.
14 Mr. English, what do you have?

15 MR. ENGLISH: I believe he omitted the word "other" in the
16 next to the last paragraph, in the last sentence of the
17 paragraph that starts "we next examine" the last sentence in
18 the parenthetical he said "or any similarly situated operation"
19 so I think it should be "other" should be inserted and it
20 should be "situated" not "situation".

21 JUDGE CLIFTON: Okay. So I see "other".

22 MR. ENGLISH: I know, but I don't think he read the word.

23 JUDGE CLIFTON: Oh, I see. So there's nothing wrong with
24 the exhibit.

25 MR. ENGLISH: There's nothing wrong with the exhibit, but I

1 don't think he, I mean, he didn't read the word, and then I
2 think "situation" should be "situated".

3 JUDGE CLIFTON: All right. So, I agree. Dr. Schiek, on
4 page 7, seven lines up, would you like the word "situation" to
5 be made into "situated"?

6 DR. SCHIEK: Yes, I would.

7 JUDGE CLIFTON: All right. And would you read that
8 sentence one more time?

9 DR. SCHIEK: We see at least two additional problems with
10 the cooperatives' treatment of quota as applied to that
11 operation or any other similarly situated operation that is
12 located out-of-state and ends up being fully regulated under a
13 new California FMMO.

14 JUDGE CLIFTON: And Mr. English, where do you have your
15 next one?

16 MR. ENGLISH: Next one I have on page 8, your Honor, I
17 think he omitted the word "California" he read the word
18 "California" and it is not in the text, so I want to see if
19 that's what he wanted to say. This is the only full paragraph
20 on the page, Dr. Schiek, so up from the bottom about six lines
21 when you read you said "so in examining those transactions
22 between" you inserted the word "California dairy farmers" which
23 I think is correct, but I just wanted to make sure you intended
24 to insert the word "California" there.

25 DR. SCHIEK: I did.

1 JUDGE CLIFTON: Ms. Frisius, do you see where that is? All
2 right. We're six lines up from the bottom on page 6, and we're
3 going to insert the word "California" prior to the word "dairy
4 farmers". And so, Dr. Schiek, just read that sentence again,
5 please.

6 DR. SCHIEK: So in examining these transactions between
7 California dairy farmers and out-of-state pool distributing
8 plants, we conclude that such plants and the dairy farmers who
9 supply them, must be subject to the traditional FMMO blend
10 price program, just like out-of-state dairy farmers whose milk
11 is pooled under the order.

12 MR. CARMAN: Your Honor, you were on page 8 not page 6?

13 JUDGE CLIFTON: We were on page 8. Did I say 6? I'm so
14 sorry, thank you, that helps a lot. No wonder she couldn't
15 find it. Sorry, Ms. Frisius.

16 MR. ENGLISH: I have nothing else on page 8, and my next
17 are on both on page 10.

18 JUDGE CLIFTON: I agree.

19 MR. ENGLISH: And he actually said at the time that it
20 should read this way, so on page 10, in the full, the only full
21 paragraph on the page, the fourth line he said "Exhibit 1" he
22 inserted the word "1" and said the word "1" should be or the
23 number 1 should be inserted.

24 JUDGE CLIFTON: Do you agree, Dr. Schiek?

25 DR. SCHIEK: I do.

1 JUDGE CLIFTON: All right. So, Ms. Frisius, fourth line
2 down, where the word capital E "Exhibit" begins the line, we'll
3 add a number, Arabic "1" to refer to Exhibit 1.

4 MR. ENGLISH: And then the same paragraph, your Honor, four
5 lines up from the bottom, I think he even said "I want to
6 insert the word who", so "payment provisions of the Act are
7 satisfied because the producers who are electing to be paid
8 differently."

9 JUDGE CLIFTON: Ms. Frisius sees it. Yes. We'll make that
10 correction. And then just read that line, if you would,
11 Dr. Schiek, starting with "payment provisions of the Act".

12 DR. SCHIEK: Payment provisions of the Act are satisfied
13 because it is the producers who are electing to be paid
14 differently.

15 JUDGE CLIFTON: Good.

16 MR. ENGLISH: So then on page 11, the second paragraph or
17 the first full paragraph after the carry over paragraph, I
18 think you corrected something and then you also read something
19 correctly differently from what's in the text, and it is, they
20 are both in the last three lines. So the third line up from
21 that you said "which would be any California producer whose
22 milk as opposed to a farm being received at a California plant"
23 I don't want to picture the whole farm being received, that, so
24 the word "milk" should replace the word "farm", your Honor.

25 JUDGE CLIFTON: Yes, and Ms. Frisius has it. Done.

1 MR. ENGLISH: The next line down I think he read more
2 grammatically correctly, "producers are in unless they choose
3 irrevocably to opt out" so he moved the word "to" from before
4 "irrevocably" to after the word "irrevocably".

5 JUDGE CLIFTON: All right. So we just strike the word "to"
6 where it is and write it again just before the quotes and
7 that's so as not to split an infinitive. This is getting
8 really good. Dr. Schiek, would you begin to read from the
9 worded words "which would" and just read from there to the end
10 of this paragraph

11 DR. SCHIEK: Okay. Which would be any California producer
12 whose milk is received at a California plant. So producers are
13 in unless they choose irrevocably to opt out in writing before
14 the first day of the month.

15 JUDGE CLIFTON: Good.

16 MR. ENGLISH: All right. We can decide where the
17 infinitive got split another day. I have nothing else on
18 Page 11, your Honor, and I have nothing on page 12, but I have
19 some things on page 13.

20 JUDGE CLIFTON: All right. You may proceed.

21 MR. ENGLISH: So on page 13, in the first full paragraph
22 again, after the carry over paragraph in the fourth line down
23 in the parenthetical, it reads, "right now, in light of Oregon
24 history" and I believe he inserted the word "the" "in light of
25 the Oregon history."

1 JUDGE CLIFTON: Is that how you want it, Dr. Schiek?

2 DR. SCHIEK: That -- yeah, I think adding a "the" in there
3 is helpful.

4 JUDGE CLIFTON: All right. Do you see where he is,
5 Ms. Frisius? Good. That's done. (In light of the Oregon
6 history.)

7 MR. ENGLISH: The next paragraph down he noted these
8 corrections at the time, instead of saying "CDFA Exhibit 61" he
9 said CDFA, "Exhibit 61 by CDFA, Table AB."

10 JUDGE CLIFTON: Yes, Ms. Frisius has it. So just read that
11 first part of that sentence for us, Dr. Schiek.

12 DR. SCHIEK: Exhibit 61, by CDFA, Table AB, shows.

13 JUDGE CLIFTON: Good.

14 MR. ENGLISH: And then similarly two lines down from that,
15 the clause the carries over that says "then 35 percent of the
16 total production" he inserted the word "quota" after
17 "production" so "35 percent of the total production quota".

18 JUDGE CLIFTON: And Dr. Schiek, is that how you want it?

19 DR. SCHIEK: Yes.

20 JUDGE CLIFTON: So we insert after production "quota" and
21 then put the period. And Ms. Frisius has it. Would you just
22 read that sentence that begins on the line above with the word
23 farmers?

24 DR. SCHIEK: Farmers with more than 50 percent of the
25 solids production hold less than 35 percent of the total

1 production quota.

2 JUDGE CLIFTON: All right.

3 MR. ENGLISH: Your Honor, I have nothing else on page 13,
4 and the next one I have is on page 16. So I have nothing on 14
5 and 15.

6 JUDGE CLIFTON: I have a tiny one on 15. Dr. Schiek, the
7 first full paragraph, in the fourth line down, you have a Roman
8 numeral I for Class and I think you meant that to be Arabic.

9 DR. SCHIEK: That should be Arabic, that's correct.

10 JUDGE CLIFTON: All right. So we'll just strike the Roman
11 numeral I and make an Arabic 1 so that any reference to Class 1
12 in this paragraph has the Arabic 1. Ms. Frisius has it.

13 MR. ENGLISH: So the next one I have, your Honor, is on
14 page 16, and it's the, again, what I keep calling the first
15 full paragraph, but the paragraph after the carry over, and it
16 is the sentence that starts "so is it just producer prices by
17 quota" and in the next clause he said it should correctly read
18 "quota holders Class 1 SNF volumes" so inserting Class 1,
19 Arabic 1, in between "holders" and "SNF". Is that correct,
20 Dr. Schiek?

21 DR. SCHIEK: As I look at that, I really think that should
22 be Roman numeral, because we are really talking about
23 Federal Order now.

24 MR. ENGLISH: But, all right. So I got the wrong 1 between
25 the Arabic and the Roman, but I'm right you want to insert the

1 words "Class I".

2 DR. SCHIEK: Class I, yeah, after "quota holders" and
3 before "SNF volume".

4 MR. ENGLISH: Okay. But it is Class I then because you are
5 looking at Federal Order, okay. Sorry to confuse you.

6 JUDGE CLIFTON: So all we're adding then, Dr. Schiek, is,
7 two things, Class and I?

8 DR. SCHIEK: Correct.

9 JUDGE CLIFTON: And it goes just after "quota holders".
10 All right. Ms. Frisius has it.

11 MR. ENGLISH: And then I have nothing else on 16, nothing
12 on 17, 18, I have only one on 19.

13 JUDGE CLIFTON: But I have something else on 16. On the
14 last paragraph, which is not a full paragraph, I don't see
15 anything at all in that paragraph. I think I must have used it
16 to mark my place when Mr. Beshore objected. Okay.

17 MR. ENGLISH: So I have nothing on 17 or 18, your Honor.
18 And the next thing I have is on 19, when he changed reconciling
19 to recognizing.

20 JUDGE CLIFTON: A couple of things on 18. I got lost in
21 the grammar in the first paragraph. I, particularly the
22 sentence that begins with "thus".

23 DR. SCHIEK: Is this on 18 or 19?

24 JUDGE CLIFTON: Page 18.

25 DR. SCHIEK: Okay.

1 JUDGE CLIFTON: First full paragraph. If you could just,
2 to yourself, read it, Dr. Schiek, and tell me if you can do
3 anything to improve the grammar so that it flows better.

4 DR. SCHIEK: I think the word "of", "thus the total
5 economic value" should be "is" "nearly 1.2 billion, which
6 creates for all quota owners an annual income stream of" what
7 it is, 139,329,000.

8 JUDGE CLIFTON: Great. We just needed a verb. All right.
9 Ms. Frisius, do you see where that is? All right. We're
10 striking the word "of" and we're putting in "is", and that is
11 in the sixth line down from the top, on page 18. So just read
12 me that sentence, Dr. Schiek, beginning with thus.

13 DR. SCHIEK: Thus, the total economic value is nearly 1.2
14 billion, which creates --

15 JUDGE CLIFTON: Billion what?

16 DR. SCHIEK: Excuse me, \$1.2 billion which creates for all
17 owners --

18 JUDGE CLIFTON: Start again.

19 DR. SCHIEK: Okay. Thus, the total economic value is
20 nearly \$1.2 billion which creates for all quota owners an
21 annual income stream of \$139,329,759.23, Exhibit 54 page 16.

22 JUDGE CLIFTON: Good. Thank you. And then the only other
23 thing that I heard you add as you read it is in the next
24 paragraph, the fourth line up from the bottom, you read the
25 word "quota" before "investment value". And do you want us to

1 put it in the exhibit?

2 DR. SCHIEK: Okay. Where -- which paragraph am I?

3 JUDGE CLIFTON: So you are in the second paragraph on
4 Page 18, fourth line up from the bottom, you read the word
5 "quota" before the phrase "investment value". Now, maybe you
6 don't need it because the first part of your sentence says "for
7 quota in the aggregate" so we don't really need it, do we?

8 DR. SCHIEK: I agree, we don't need it.

9 JUDGE CLIFTON: We don't need it. Okay, good. So nothing
10 else on that page. Mr. English?

11 MR. ENGLISH: So I have one last one, which is on page 19
12 and he effectively already made the correction, it is in the
13 bottom paragraph, second line, next to the last word before
14 quota, the exhibit says "reconciling" and he said it should be
15 "recognizing".

16 JUDGE CLIFTON: Ms. Frisius, do you see that?

17 MS. FRISIUS: Uh-huh.

18 JUDGE CLIFTON: Good. Done.

19 MR. ENGLISH: And unless you have anything else, your
20 Honor, that's all the changes or corrections I had.
21 Dr. Schiek's raising his hand.

22 JUDGE CLIFTON: Dr. Schiek?

23 MR. ENGLISH: It is a new one, you have the witness wanting
24 to say something.

25 DR. SCHIEK: Yeah, in the proposed language on 17, very

1 last line of that it says Section 1051.17, I believe should be
2 .11, 1051.11.

3 JUDGE CLIFTON: Do you want to check that out, Mr. English?

4 DR. SCHIEK: I think when I was writing it I may have been
5 looking at someone else's proposal.

6 MR. ENGLISH: Well, 17 is reserved, so therefore, I don't
7 think we want to refer to it. 11 is the definition of
8 California quota program and producer quota, so I think 11 is
9 correct, your Honor.

10 JUDGE CLIFTON: All right. So Ms. Frisius, we're on
11 Page 17 at the end of the proposed language and we're striking
12 the .17 and making it be .11. Done.

13 JUDGE CLIFTON: Good catch. The only other thing I would
14 like to do, just for the benefit of those using the exhibit, on
15 page 19, in the middle of the page there's a paragraph that
16 includes an illustration of this is shown on an annuity
17 calculation. And you told us where to find it, Dr. Schiek, and
18 I would like for us to write it in on this exhibit on page 19.
19 You told us it was Exhibit H, so I want to make sure that's it.

20 MR. ENGLISH: It is, your Honor.

21 JUDGE CLIFTON: All right. Then I would like us to insert
22 there after the word "attached", we'll just insert "Exhibit H
23 of Exhibit 146". Done. All right. Thank you, Mr. English.

24 MR. ENGLISH: All right. Your Honor, I do have some
25 additional direct. I note we have been going, we took an early

1 first break, so I think we have been going for an hour and 45
2 minutes now, so depending on people's likes and dislikes, I
3 wonder whether, and especially the witness, but everybody else,
4 whether it makes sense to take our lunch now then I can finish
5 the direct after lunch. And that also gives people a chance to
6 look at the testimony and come up with cross-examine and maybe
7 there will be a minute or two shorter, or maybe a minute or two
8 longer. But I do know we have been going an hour and 45
9 minutes, at a it's been pretty intense I think for the court
10 reporter. So at a minimum, I would say we take a 15-minute
11 break, then the only question is do we take the lunch break
12 instead?

13 JUDGE CLIFTON: Okay. I agree that we need a break. I
14 want to know from first Mr. Beshore and then Ms. Hancock,
15 whether you would prefer, I'm going to ask for show of your two
16 hands, whether you would prefer lunch now or just 15 minutes.
17 If we take just 15 minutes then there will be more direct
18 before you go to lunch. So Mr. Beshore and Ms. Hancock, the
19 first vote is you want 15 minutes, the second vote is you want
20 lunch. Do you want 15 minutes? Do you want lunch? Okay. Do
21 you want lunch? Yes, they would prefer lunch.

22 Thank you, Mr. English, for letting the people who are
23 impacted the most choose. So let's see, please be back and
24 ready to go at 1:40. 1:40.

25 (Whereupon, the lunch recess was taken.)

1 MONDAY, NOVEMBER 9, 2015 - - AFTERNOON SESSION

2 JUDGE CLIFTON: We're back on record at 1:44. Let's see,
3 Dr. Schiek, he was here and he just disappeared. Very good.
4 Thank you, Dr. Schiek, for returning to the witness stand.

5 Before you begin, Mr. English, and I know we're about
6 to have cross-examination after you finish your direct, I had a
7 thought during lunch that I would just like to share with you.
8 When I was ruling on Mr. Beshore's objection, I mentioned the
9 term disorderly marketing. I think a threshold question, even
10 before the Department considers that issue when it determines
11 what's authorized under the Act, is whether it needs even to
12 find the condition of disorderly marketing or whether it needs
13 merely to find that something will promote orderly marketing in
14 California and/or elsewhere. I don't know. I don't know what
15 the answer is. There are so many very important questions
16 about what the Act authorizes that are going to have to be
17 dealt with and that's just the beginning of it all.

18 All right. Mr. English?

19 MR. ENGLISH: Thank you, your Honor.

20 BY MR. ENGLISH:

21 Q. So as we begin your additional direct, Dr. Schiek, I
22 think we have already discussed in Exhibit 146, A through F,
23 but we haven't spent anytime yet on Exhibits G and H. So could
24 you again tell us what Exhibit G is?

25 A. So Exhibit G is a copy of a journal article that

1 appeared in the Journal of Agribusiness, Fall 2014 issue,
2 entitled "The Agricultural Act of 2014, and Prospects for the
3 California Milk Pool Quota Market. And that was written by
4 Daniel Sumner and Jisang Yu.

5 Q. Had you read that before this proceeding?

6 A. I had. I actually was asked to review it before it was
7 put in for publication.

8 Q. What does that mean exactly?

9 A. I was contacted by the editor of that, of this
10 particular issue of the Journal of Agribusiness and he asked me
11 to submit a review of the article.

12 Q. And did you do so?

13 A. I did.

14 Q. And then turning to Exhibit H, which is the annuity
15 calculator. Could you walk us through, I mean, I know you
16 talked about it in the testimony, but could you walk us through
17 how this works, if it is somebody could duplicate it or make
18 changes if they wanted to and run it. So this starts on
19 Page 43 of the exhibit, so could you walk us through it?

20 A. Sure. Just off, this is Exhibit H, and in Exhibit 146,
21 just to say at the outset there are a lot of different
22 financial web sites out there, I think CNN has one, Yahoo has
23 one, bankrate.com is the one that this one refers to. And in
24 all those, there's certain financial calculators, you can have
25 a calculator that determines your, what your 401k might grow to

1 good given enough time and enough money, and there's others
2 that calculate savings rates to achieve some sort of savings
3 goal, and they are usually categorized in different ways. Like
4 there is a car finance payment applicator, there's a home
5 mortgage calculator, there's any number of things. Under the
6 category at the bankrate.com, you would click on, if you look
7 on Exhibit H, and you look at near the top there's three or
8 four words there, home, rates, calculators, and mobile. If you
9 click on the calculators button, it gives you a whole bunch of
10 different financial calculators, and they are grouped by area.
11 So this one is in the investments area or investment area. And
12 what you do, if you are interested in the length of the payback
13 period, which is kind of what we were looking at in this
14 example, we had this sort of starting principal value which was
15 based on the selling price of quota and the amount of quota out
16 there. And then we -- we looked at the withdrawal amount as
17 being the monthly quota payment that's, you know, historically
18 been made or something very close, or an average payment, it
19 varies a little bit from month to month, but we looked at a
20 fixed number. So we put that monthly quota payment in as the
21 withdrawal amount, where again, that's a monthly payment,
22 monthly amount that pays out on quota. So the interval between
23 withdrawals is monthly. The starting principal was that,
24 nearly \$1.2 billion worth of quota, that was actually 1.163 and
25 change, billion dollars.

1 And then we used a nominal growth rate. Because I
2 think as I pointed out in the text, the testimony using a
3 larger growth rate actually increases the value of the quota,
4 and so the point here was to look at quota's currently worth
5 and how long it would take to pay it back at this particular
6 rate. So you input those four items, the withdrawal amount,
7 the interval between withdrawals, the starting principal, and
8 the growth rate, and then you calculate and the answer came
9 back, it's 101 months, which I think is 8 years and five
10 months, or 8.4 years on a decimal basis. So that's -- that's
11 all that showed was just an example on how to sort of calculate
12 an annuity payout based on the value of quota.

13 Q. And were you here for the testimony of Annie AcMoody
14 with regard to quota?

15 A. I believe I was.

16 Q. Yeah. And so is this consistent with what she
17 testified about, about what annuity would be worth if you
18 bought the quota and what it would do, how long it would take
19 to pay it off, if you bought a pound of quota?

20 A. To my recollection it was, yeah.

21 Q. So you have discussed the Dairy Institute of
22 California's evolution on what it submitted and what its been
23 doing at the hearing. Can you describe how these documents,
24 especially Exhibit 145, got created?

25 A. Yes. So Exhibit 145 I would describe as really an

1 attempt, at least the first part of the document was more of an
2 attempt to describe how we thought about things as we were
3 preparing it proposal for this proceeding. And so it draws on
4 the meetings, the group meetings that we had with members of
5 our working group to think about how a Federal Order might work
6 for California. But, you know, as terms of putting this
7 document together when we, especially when we, after we heard
8 the USDA economic, preliminary economic analysis, we began to
9 think, you know, our goal was not to see quota disappear
10 quickly with -- with little value to producers. So we began to
11 think of alternatives, and met as a group the folks who have
12 been here pretty much at every hearing, we met as a group and
13 discussed how we might come up with an alternative way of
14 recognizing quota value from what we originally proposed. And
15 so in kind of working through our thought process, the group,
16 members of the group gave me a lot of input, a lot of
17 suggestions, but the document was my final work product. I had
18 to decide what I was going to put in and what I was not going
19 to put in.

20 Q. So I want to turn for a few minutes and talk about
21 Oregon. And I'm going to start with, obviously I want to know
22 where you came from on it in terms of our development of
23 Proposal 2. So based upon your reading of what the Department
24 did back in 1969, so how USDA get to the conclusions it
25 ultimately reached with respect to that Order?

1 A. Yeah.

2 JUDGE CLIFTON: Yes, let me hear the objection, Mr. Vlahos.
3 You are wondering how Dr. Schiek is going to know how USDA made
4 its determinations, but I'll hear it from you.

5 MR. VLAHOS: You correctly guessed. John Vlahos, by the
6 way. I'm going to object on the grounds speculation because it
7 calls for the witness to speculate what was the in mind of USDA
8 when they made this decision.

9 JUDGE CLIFTON: I note your objection. There may be some
10 objective observations that Dr. Schiek can make from history,
11 but I think, Mr. English, you at least need to reword your
12 question.

13 MR. ENGLISH: Sure.

14 BY MR. ENGLISH:

15 Q. Did you, in preparation for Proposal 2, and ultimately
16 for this testimony, did you study the decision on proposed
17 marketing agreement and order that you have cited in your
18 testimony for Oregon?

19 A. I did.

20 Q. Okay. And further, in light of what was proposed
21 Proposal 2, in light of that reading of actually what the
22 Secretary said, what did you take from it?

23 A. Sure.

24 MR. VLAHOS: Your Honor, John Vlahos again, I'm going to
25 object to the question. It's just a rewording and it suffers

1 from the same infirmity. He's asking, he's reading it, what he
2 drew from it, and that's speculating. If he's going to say
3 what the USDA thought about it, I still think it is
4 objectionable.

5 JUDGE CLIFTON: Your objection is noted but overruled. The
6 difference here is now he's focusing on what he reads in the
7 decision which is published, and we can all try to say what we
8 take from that. I know we have had objections in the past that
9 only the Secretary should tell us what the Secretary said. But
10 here, I'll hear what the witness believes.

11 Well -- welcome. Let me interrupt. We have a new
12 arrival. Would you identify yourself for the record?

13 MR. RICHMOND: Thank you, your Honor, very much.
14 William Richmond, R-I-C-H-M-O-N-D, with USDA AMS Dairy
15 Programs. Please forgive my tardiness. Good to be here.

16 JUDGE CLIFTON: Oh, you are not tardy, we're just so glad
17 to see you. Ms. Becker, I don't think I took your appearance
18 this morning either, so I should do that now.

19 MS. BECKER: Lauren Becker, Attorney for USDA.

20 JUDGE CLIFTON: Thank you. All right. And I just, because
21 I'm doing this, I just want to note that shortly after each
22 participant identified himself, Elvin Hollon arrived and has
23 been participating throughout.

24 MR. ENGLISH: Without dark glasses.

25 JUDGE CLIFTON: All right. So I interrupted. So I

1 overruled the objection, and you may answer, Dr. Schiek, as
2 based on what the Secretary said, what was your take on it?
3 You may answer.

4 DR. SCHIEK: Okay. Thank you. So as I looked at the
5 decision and how the Secretary responded, it seemed there were
6 some areas of note that the Secretary made. One was that the
7 importance of uniform prices to all producers was something
8 that was referenced by the Secretary, and the importance of
9 that, and equitably attributing uniform prices to producers in
10 the market.

11 He also talked about the issue of treating producers
12 differently depending on where they shipped milk to, whether
13 they were Oregon plants, whether they were located, whether the
14 producers were inside Oregon or outside Oregon. And but they
15 also noted that, you know, a quota program the way Oregon had
16 run it, was was not -- not something that they felt was
17 authorized by the Act. So instead, they noted that the Act
18 permitted or would permit producers to voluntarily, if they
19 desired to do so, assign their share of the uniform price to
20 the State of Oregon for redistribution on the basis of the base
21 plan that was in effect in Oregon. So --

22 BY MR. ENGLISH:

23 Q. SO tying that together then with page 10, would that be
24 ultimately, how does that connect rather than, how does that
25 connect ultimately to your statement in the middle of page 10,

1 which is that the traditional blend value applicable to those
2 producers who elect to be paid on a quota/nonquota basis will
3 be transferred to California Department of Food and Agriculture
4 for reblending and distribution to producers?

5 A. Yes. So I think the argument here is that in light of
6 what USDA's decision was from that rule making procedure, this
7 seemed to be a way of dealing with quota that was modeled after
8 that same procedure, and that was, in the words of the
9 Secretary, the Act did not prohibit the Secretary from doing
10 this, from just having producers elect to assign their uniform
11 price receipts to the state for redistribution on the basis of
12 quota value.

13 Q. Did the group consider whether we could forego that
14 particular route and allow or make it such that the
15 Market Administrator could stand in the shoes of CDFA there,
16 and therefore, we simplify the process by having the Market
17 Administrator make that distribution?

18 A. Yeah, I think, Mr. English, as a practical matter, in
19 some ways it would be easier if the Market Administrator could
20 handle all the money. And again, I think we were erring on the
21 side of looking at how in this decision in 1969, how the
22 Secretary handled the issue of the Oregon base plan and that
23 they felt they had the, the Act permitted them to handle it
24 that way, so we put our proposal together on those same lines.
25 But, you know, it might be that handling it within the, having

1 the Market Administrator handle it within, totally within his
2 authority, would be -- would be certainly an easier way to do
3 it.

4 Q. And it could be a mechanism by which Congress meant
5 when it said reblend and redistribute proceeds to recognize
6 quota value?

7 A. Yeah, it could mean that. Yes.

8 Q. All right. At this time, your Honor, I move admission
9 of Exhibits 145 and 146?

10 JUDGE CLIFTON: Didn't I do that already?

11 MR. ENGLISH: No, we went through all the corrections, but
12 we have not yet gone to the point of moving for admission.

13 JUDGE CLIFTON: Mr. Beshore?

14 MR. BESHORE: I have a conditional objection to the
15 admission of Exhibit 145 and the testimony accompanying it. It
16 is, and that is this. Early in this proceeding, it seems like
17 ages ago, our witnesses were interrupted repeatedly with the
18 objection on behalf, from Mr. English and the Dairy Institute
19 of California, that witnesses could not testify to what the
20 legislation means, and what the Secretary means when he's
21 saying this, that, or the other. We didn't think that was an
22 appropriate objection, your Honor allowed the testimony.

23 My conditional objection is this. If, in the decision
24 making process, the Administrator, or ultimately the Secretary,
25 were to grant that objection any weight, that I would move that

1 Dr. Schiek's exhibit not be admitted and that his testimony,
2 which is replete, in fact, the only basic function of it is to
3 argue what the legislation means, that it be stricken.

4 JUDGE CLIFTON: Thank you. Your objection is noted. I
5 reassert -- oh, Mr. English, did you wish to be heard?

6 MR. ENGLISH: I do. Obviously, I can understand where
7 Mr. Beshore's coming from. I would note what I think is a
8 distinction. And the distinction is, we didn't talk about, we
9 talked about how the group evolved to a position. And the
10 testimony is about how we got somewhere. We're obviously going
11 to have to argue the law. Whether or not Mr. Schiek's
12 statements about what the group thought were the law, the point
13 of the testimony is to describe for the Secretary how we got
14 from point A to point B. And in addition, how we developed or
15 why we developed a couple of alternatives. That is different
16 in scale than saying this is what the statute means. Because
17 it's all about how we got to where it. That's the testimony
18 and that's why it should be admissible, regardless of the legal
19 statements. It is different.

20 But I accept, you know, if I understand the point. If
21 there's legal statements in there and the Secretary should do
22 it, and frankly, the Secretary is going to have to make his own
23 decision about what the law means.

24 JUDGE CLIFTON: Mr. Vlahos?

25 MR. VLAHOS: John Vlahos. I don't think the distinction

1 made by Mr. English is correct. Although in some instances Dr.
2 Schiek has testified how they got from A to B, thereafter, in
3 discussing why Proposal 2 is proper and why Proposal 1 is not,
4 there's the same kind of legislative interpretation that's
5 used, and it is not used solely for the purpose of how they got
6 the thought process of how they got from A to B. If you
7 carefully examine the entirety of this document, it is replete
8 with testimony that is based on interpretation of statute.

9 JUDGE CLIFTON: I agree with you, Mr. Vlahos, there would
10 be no help from Exhibit 145 if it were completely
11 dis-associated with binding regulations or interpretations of
12 what's applicable under the statute. I repeat my appreciation
13 of the objections, I think they are wonderful caution signs.
14 And I repeat my determination that this is not a court
15 proceeding, and I welcome ideas, even those ideas that seek to
16 determine what the law requires. Ultimately, it is the
17 Secretary that must make that ultimate determination, but I do
18 not think lay witnesses or expert witnesses, or attorneys,
19 should be barred from giving it a try. And that's what we have
20 got going on here. Mr. English?

21 MR. ENGLISH: I have, I'm just waiting to see whether
22 there's questions before objection, and whether there's other
23 objections other than Mr. Beshore's conditional objection.

24 JUDGE CLIFTON: Does anyone wish to ask additional
25 questions of Dr. Schiek regarding Exhibit 145 or 146 before

1 determining whether you have any objections to their being
2 admitted? No one. Is there any objection of the admission
3 into evidence, other than those already stated, of Exhibit 145?
4 There are no additional objections. Exhibit 145 is admitted
5 into evidence over objections.

6 (Thereafter, Exhibit 145 was
7 received into evidence.)

8 JUDGE CLIFTON: Is there any objection to the admission
9 into evidence, other than that already stated, of Exhibit 146?
10 There are none. Exhibit 146, even though it wasn't
11 specifically targeted, it is, in fact, incorporated into
12 Exhibit 145, so I also consider it being admitted over
13 objections. Exhibit 146 is admitted over objections.

14 (Thereafter, Exhibit 146, was
15 received into evidence.)

16 MR. ENGLISH: Thank you, your Honor. The witness is
17 available for further examination.

18 JUDGE CLIFTON: Thank you. Who would like to go first?
19 Mr. Vlahos.

20 CROSS-EXAMINATION

21 BY MR. VLAHOS:

22 Q. First, your Honor, I would like to, on the record,
23 thank Mr. English for his courtesy in keeping me notified as to
24 when Dr. Schiek would be testifying as to quota because I'm
25 obviously quite interested in the subject. And I thank

1 Mr. English for that professional courtesy.

2 The second, I would like to make a little preliminary
3 thing, your Honor, in that this proceeding, in fact, this
4 examination is in the sense a grand de ja vu, because I got
5 involved with the dairy, legal side the dairy industry on
6 account of pooling and quota in defending it.

7 In the Spring of 1969, I walked into the office one day
8 as a young partner, and a senior partner said to me, "How would
9 you like to defend a suit that attacks the Constitutionality of
10 the Gonsalves Milk Pooling Act?" I said, "Sure, what is it?"
11 His response was not reassuring. He said, "Damned if I know."

12 And now I find myself, 46 years later, in exactly the
13 same position and who would have think it.

14 Anyway, good afternoon, Dr. Schiek.

15 A. Good afternoon, Mr. Vlahos.

16 Q. Dr. Schiek, when you are testifying here today, you are
17 testifying on behalf of the Dairy Institute, are you not?

18 A. I am.

19 Q. And the opinions that you are giving are not just your
20 own, but those of the Dairy Institute?

21 A. They are.

22 Q. Okay. Just some preliminary thing, a couple of
23 preliminary things. In the past, has it not been the position
24 of the Dairy Institute that quota is essentially a producer
25 issue and it's something it's about redistribution of producer

1 funds that are not of concern to the Dairy Institute? Would
2 that be a fair statement?

3 A. Yeah, I think within the context of the state program,
4 we have viewed the quota as a producer program. I think the
5 only time we have, times we have had objections has been when
6 it's impacted additional revenue generation by increasing
7 regulated minimum prices.

8 Q. But in terms of the quota program itself, can you cite
9 any times the Dairy Institute actually took a position against
10 the quota system?

11 A. I'm not aware of any.

12 Q. Okay. And you have been with the Dairy Institute how
13 long?

14 A. Since 1997.

15 Q. Okay. And when you got to the job in 1997, no doubt
16 you ascertained other prior positions had taken opposition to
17 the California dairy quota program?

18 A. Yeah, when I first got to the Dairy Institute, I think
19 we had come from a point where there had been a quota reform
20 bill, I think 1993, it became effective in 1994, that
21 established the \$1.70 or 19 and a half cent per pound solids
22 not fat, fixed differential. And I remember there was concern
23 at that time because some of the Class 1 prices were increased,
24 and that was an issue that Dairy Institute was very concerned
25 about. And I think the issue, the discussions at our meetings

1 on a policy basis was concern about the attempt to increase
2 regulated minimum prices to basically keep the quota program
3 going.

4 Q. And was there any formal position taken by the Dairy
5 Institute at that time?

6 A. I think we had a formal position.

7 Q. You think or do you know?

8 A. We had a formal position that basically said that we
9 would oppose price increases to accommodate quota.

10 Q. Okay. You indicated that, in your testimony at page 1,
11 that the Dairy Institute and its members did not set out nor
12 was it your goal, this is a Dairy Institute and it's members
13 goal, to destroy quota; is that correct?

14 A. That's correct.

15 Q. Did you, when you made that statement, recognize that
16 there were those who felt that by virtually the way Proposal 2
17 worked, that it would, in fact, destroy quota eventually?

18 A. Yeah. I believe that we understood, as I said in my
19 testimony, that given what happened with the Oregon program,
20 that quota would probably go away over time. What we didn't
21 understand was the analysis that basically indicated it would
22 occur more quickly. That was something we weren't aware of.

23 Q. Well, we'll go into that more later when we talk about
24 it in later portions of your testimony. The first part of your
25 testimony seems to be focused on various discussions and so

1 forth of how the producers and others wanted to deal with
2 quota. For example, you talk about the early 2000's, producer
3 representative, this is on page 2, by the way -- and I'll try,
4 if I forget to mention what page I'm talking about, would you
5 remind me because I don't mean to not to let you know what it
6 is?

7 A. Sure, I will do that.

8 Q. You state, it is in the first full paragraph, "that in
9 the early 2000's, producer representatives from different
10 organizations met to consider changes, including the
11 possibility of terminating the program."

12 Nothing came of that, did it?

13 A. No, nothing did come of it.

14 Q. In 2005, you mentioned that the Milk Advisory Board
15 commissioned a study of California's dairy industry, focusing
16 on how the industry could be successful and so forth, and hired
17 a firm, McKinsey & Company, to study the industry; is that
18 correct?

19 A. Correct.

20 Q. And in terms of dealing with quota, nothing came of
21 that, right?

22 A. That's correct.

23 Q. You mentioned that one of the options put forward was
24 the idea of creating a debt obligation, and by the way, that's
25 on the top of page 3?

1 A. Uh-huh.

2 Q. One of the options put forth was the idea of creating a
3 debt obligation or bond that would be paid back from the pool.
4 Nothing ever came of that?

5 A. That's correct.

6 Q. You mention that there was a, also on page 3, that "in
7 2007, the Secretary of Food and Agriculture of California,
8 Secretary Kawamura, established an advisory committee to study
9 the situation of pooling and set forth various options to
10 explore if quota should continue, be modified, or retire." And
11 nothing came of that, right?

12 A. That's correct.

13 Q. You mentioned that "the quota review committee," this
14 is on the top of page 4, "the quota review committee had an
15 executive summary and sort of voted on the issue." What's
16 that, terminating quota?

17 A. Yeah, they had three options to vote for, one was
18 leaving quota unchanged, another was to modify it in some way,
19 another was to retire it or terminate it, I guess you could
20 say.

21 Q. And they didn't reach the super majority, but the
22 majority of that committee voted for quota to be unchanged; is
23 that correct?

24 A. Correct. There were six votes for unchanged and five
25 for retiring.

1 Q. Okay.

2 JUDGE CLIFTON: Where are we?

3 MR. VLAHOS: Excuse me, your Honor, top of page 4.

4 JUDGE CLIFTON: All right.

5 MR. VLAHOS: I'm sorry if I didn't mention that before.

6 JUDGE CLIFTON: No, you did, 6 to 5, all right. Thank you.

7 MR. VLAHOS: Sorry.

8 BY MR. VLAHOS:

9 Q. The -- it said, the committee, you, on the second
10 paragraph, excuse me, of page on page 4, you indicate that
11 "this committee tried to work out a number of options, but they
12 all considered them unworkable." Is that correct?

13 A. Correct.

14 Q. Turn your attention to the top of page 6. First off,
15 the first paragraph, the second sentence says, "historically,
16 out-of-state farmers' milk was credited at the plant blend and
17 under the California State Order (CSO)."

18 What evidence do you have that out-of-state farmers'
19 milk was actually credited at the plant blend?

20 A. Well, I think we had the testimony of Mr. Lightenberg
21 here at the hearing in terms of how he was paid. If I remember
22 his testimony, he talked about receiving the plant blend.

23 Q. Other than his testimony, anything else?

24 A. In discussions with CDFA, my understanding from those
25 discussions was that there was a credit, it was essentially a

1 pass-through, a credit at the plant blend, and then a debit
2 back so that there was, there was no money owed to the pool.
3 But in terms of the actual pay prices, other than my
4 understanding from talking to members, plant blend is my
5 understanding what was being paid.

6 Q. It is your understanding. But other than what you have
7 testified to, you have no actual basis, evidentiary basis?

8 A. Correct. I have no payment receipts or anything.

9 Q. Thank you. Going through the process from which your
10 group, I'll just use that term, your group, if you don't mind,
11 reached its conclusions on how they were going to treat the
12 issues in Proposal Number 2, you talked about your group's, I
13 think it is the group's first thought that's on the top of
14 Page 7. Do you recall that; is that correct?

15 JUDGE CLIFTON: I've forgotten the first part of your
16 question, could you ask it again?

17 MR. VLAHOS: Excuse me, your Honor, I interrupted you and I
18 didn't mean to, excuse me. Do you want me to proceed?

19 JUDGE CLIFTON: Yes. Would you ask your question again?

20 MR. VLAHOS: Certainly.

21 BY MR. VLAHOS:

22 Q. I just want to refer you to the top of page 7 where it
23 says, "given our view that out-of-state producers must be paid
24 the traditional blend, our first thought was that we would have
25 two pools or pool calculation, one would pay the full order

1 price to out-of-state producers first, the remaining funds
2 would be apportioned to all California producers in the pool on
3 the basis of quota and non-quota prices that would be
4 calculated after payments to out-of-state producers had been
5 made."

6 JUDGE CLIFTON: You read it a little different from what
7 Dr. Schiek wrote. The beginning of that, "one would pay the
8 full order blend price" and you left out the word "blend" I
9 think.

10 MR. VLAHOS: Excuse me, consider it inserted, I meant to
11 insert it.

12 JUDGE CLIFTON: Okay. You may proceed, Mr. Vlahos.

13 BY MR. VLAHOS:

14 Q. Yes. You indicated that under that proposal, the next
15 phrase that "no option for them to receive a traditional order
16 blend," was that first thought rejected?

17 A. Yes, as we began thinking about the implications of
18 that.

19 Q. And were the implications based on two different
20 things, one was the out-of-state milk coming into California,
21 and the other dealt with the Arizona, issue of the plant in
22 Arizona?

23 A. I think the out-of-state milk coming in, Mr. Vlahos,
24 was part of what got us to the first thought.

25 Q. Okay.

1 A. And then the second thought was when we began thinking
2 about these interactions with out-of-state plant, Arizona
3 plant.

4 Q. Okay. Your first thought would have taken care of the
5 out-of-state milk coming in; is that correct?

6 A. Our first thought would have, would have dealt with the
7 issue of paying out-of-state milk producers a traditional
8 Federal Order blend price.

9 Q. And if there had not been that issue about the Arizona
10 plants, would that have been a sufficient way to deal with
11 out-of-state milk?

12 A. If you are just looking at out-of-state milk, the
13 out-of-state milk question, yes. I think that would be
14 appropriate. I think we -- we had concerns about uniform,
15 payment of uniform prices to producers as an overarching
16 concern as well.

17 Q. That overarching concern is based upon your
18 interpretation of what the Federal Farm Bill language means; is
19 that correct?

20 A. More based on our thinking of what the Agricultural
21 Marketing Agreement Act requires.

22 Q. But that's based, the reason that you are focusing on
23 the agricultural, on the Act, is that you interpret the Farm
24 Bill provision as quote, "not amending the Act" and therefore,
25 all these provisions of the Act concerning uniform prices are

1 still applicable?

2 A. It's true, yes, that our thinking was that the Act was
3 not amended in the process of the --

4 Q. And would your legal interpretation --

5 JUDGE CLIFTON: I'm sorry, were you finished? That the Act
6 was not amended in the process of what?

7 DR. SCHIEK: Of the Farm Bill.

8 JUDGE CLIFTON: Okay.

9 BY MR. VLAHOS:

10 Q. Then I asked you, if your interpretation of what the
11 Farm Bill allows or permits is wrong, your concern about your
12 first thought would also be wrong.

13 A. I'm not sure about that question. I think -- I think
14 the concerns about out-of-state producers being able to
15 participate in the quota program would still stand or their
16 lack of being able to participate. So I'm not sure I can agree
17 with you on that second piece.

18 Q. Perhaps I didn't make myself clear. I'm just saying,
19 suppose, suppose you were wrong about what the Act required.
20 Let me back up. Maybe I can make this clear. I think what you
21 said that your original proposal is if essentially you had sort
22 of like a two pool system?

23 A. Uh-huh.

24 Q. Where the out-of-state producers would be paid before
25 you deducted out the quota premiums and then the California

1 producers be paid a blend after deduction of those premiums, is
2 that sort of the idea of the first proposal?

3 A. If, I believe if I understand you, Mr. Vlahos, I think
4 you are correct in that the out-of-state, the blend price would
5 be calculated before any quota premiums were withdrawn.

6 Q. Okay. And you said even if, even if that were
7 permitted, there would still be a problem because there would
8 be the issue of non-uniform prices, correct?

9 A. I believe I said that non-uniform prices was our
10 overarching concerns -- one of our overarching concerns.

11 Q. And what I was trying to get at is your feeling that
12 your overarching concern that there had to be uniform prices is
13 based on your interpretation of the Congressional language in
14 the Farm Bill; is that correct?

15 A. I think, yes, it is based on the interpretation that
16 the uniform payment, the uniform prices provisions of the Act
17 are still valid.

18 Q. Okay. And if you were wrong about that, that that is
19 not the proper interpretation of the Farm Bill, then your
20 concern about the fact that, that the two pool way of handling
21 quota would still violate uniform price provisions of the Act
22 would also be wrong?

23 JUDGE CLIFTON: Don't answer that. When Dr. Schiek
24 clarified that he was concerned about provisions of the Act,
25 and then you asked him if his interpretation is wrong about the

1 language of the Farm Bill, which is not going back to the
2 Agricultural Marketing Agreement Act, I got confused.

3 MR. VLAHOS: Okay. If you got confused, that's enough for
4 me, I'll reword it.

5 JUDGE CLIFTON: Okay. So his concern is not just in
6 looking at that little phrase in the Farm Bill, his concern is
7 he states in his testimony is about particularly two provisions
8 of the Agricultural Marketing Agreement Act.

9 MR. VLAHOS: Yes, your Honor.

10 JUDGE CLIFTON: Yeah, so if you can take all that into
11 account and ask your question, I'm okay.

12 MR. VLAHOS: Perhaps I'm not clear, because as I understand
13 the witness' position, and the Dairy Institute's position, is
14 that the Farm Bill did not amend the Act. And because it did
15 not amend the Act, those provisions of the Act concerning
16 uniform prices paid are still applicable. And my point is, and
17 that's based on the idea that the Farm Bill did not amend the
18 Agricultural Act, which I'll call for shortness the Act.

19 My point is, if the farm, if the proper interpretation
20 of the Congressional Act is that whether it expressly amended
21 it or not, it permitted --

22 JUDGE CLIFTON: Now, Congressional Act. Of course they are
23 both Congressional acts.

24 MR. VLAHOS: The Farm Bill. The Farm Bill.

25 JUDGE CLIFTON: Okay. All right. Start again?

1 MR. VLAHOS: If the Farm Bill did, in fact, permit there to
2 be essentially two prices, a pool price that was, that was paid
3 after deduction of the quota premium, then the provisions of
4 the Act, meaning the Agricultural Marketing, Milk Marketing
5 Act, would no longer be a bar to a two pool provision.

6 JUDGE CLIFTON: Mr. English, I'll hear your comment.

7 MR. ENGLISH: I think there's a number of levels of
8 problems with the question. First, he didn't actually respond
9 to your issue, because you properly pointed out that there are
10 two sections of the Act, uniform payments and trade barriers.
11 And second, it's not a question of whether, it's not just a
12 question of whether, it's not just a question of whether
13 amended the Act, it's also a question what the language is
14 that's used. And I think the question is therefore, too
15 narrowly focused.

16 JUDGE CLIFTON: I agree. So I know, I know what you want,
17 it's just too complicated to boil it down to that simple a
18 question and answer.

19 MR. VLAHOS: You know what, your Honor, I think we're going
20 to boil it down in terms of our legal argument, and maybe that
21 will do it. But I want to identify, what I'm trying to
22 identify here is what are the objections to the idea of this
23 two pool thing. Not that we propose that, but I want to know
24 what the objections are. The one I understood was the trade
25 barrier issue, and there are two subparts of that. One was

1 milk coming out-of-state from out-of-state producers, the
2 others dealt with the Arizona plant out-of-state, I'm using
3 those as just shorthand. So that was, that was one set of
4 things.

5 So anyway I'm going to proceed on. I would like to
6 examine just for a moment, so that I can understand what the
7 concern about the Arizona plant. I know you have discussed it
8 but could you explain for me so that I can further understand
9 what the problems are that you see?

10 DR. SCHIEK: So, Mr. Vlahos, I think if I can kind of boil
11 that discussion down, I think there were a couple of
12 objections, but they were based on the fact that the first
13 objection, which is the out-of-state milk objection, has to be
14 dealt with. So it's sort of built on that.

15 BY MR. VLAHOS:

16 Q. Okay.

17 A. First premise. And then it's how two producers,
18 producer located in California versus a producer located in
19 Arizona, how they would get treated under that, if you, if you
20 kind of kept the idea of quota overbase for California
21 producers, and now you have got this traditional blend for
22 Arizona producers, for example, in that. They have a different
23 price among producers serving a pool plant under the Order,
24 that was the first concern. The idea was that, there ought to
25 be a uniform price -- our thinking, our thinking, what was

1 guiding our thinking was this notion of uniform prices to those
2 producers. Then that raised another issue in our mind. And
3 that is, now you have got, if you treat those producers the
4 same, you have got the two California producers, one shipping
5 to an Arizona plant and one shipping to a California plant, and
6 I'm not, there can be differences there because of the location
7 of the plant. I accept that. But the kind of differences that
8 go with one being paid a blend and one being paid an overbase
9 price, for example, that raised another slightly different
10 uniform price issue for us. And so the conclusion of that was
11 that this idea that all the California producers would be in
12 this quota overbase system we didn't think would work.

13 Q. Okay. And do you think it violated any provision of
14 the AMMA?

15 JUDGE CLIFTON: AMAA?

16 MR. VLAHOS: Didn't I say that?

17 JUDGE CLIFTON: Let's go with that, AMAA.

18 MR. VLAHOS: Yes.

19 JUDGE CLIFTON: Okay.

20 BY MR. VLAHOS:

21 Q. All right.

22 A. Yes, again, I think we're seeing the uniform prices
23 provision as sort of the core, and that was, that was what was
24 guiding our thinking.

25 Q. Okay. Commencing on page 11.

1 JUDGE CLIFTON: I would like to just ask a question, if I
2 could, Mr. Vlahos. Dr. Schiek, these are real life situations
3 currently existing; is that correct?

4 DR. SCHIEK: Yes.

5 JUDGE CLIFTON: All right.

6 BY MR. VLAHOS:

7 Q. There was discussion in both your written testimony and
8 answer to questions by Mr. English concerning the Oregon
9 program. Now, can you explain what the Oregon program was?

10 A. Yes, my understanding of the Oregon program was that it
11 was a producer-based program where dairy farmers were,
12 essentially had a base that was tied to their use, the usage of
13 their milk and they received a certain price on that base
14 program, that base plan, and then on the excess above that
15 base, received a different price, a lower price.

16 Q. Okay. And was there, in that program, was there any
17 Congressional authorization for that program?

18 A. I don't believe so, no.

19 Q. Okay. Not getting into what it exactly provides, but
20 there was nothing like the Farm Bill provision that we have
21 been discussing that applied to the Oregon situation.

22 A. No, I don't believe so.

23 Q. Okay.

24 JUDGE CLIFTON: Mr. Vlahos, if I could interrupt again, do
25 you, you used the word base, Dr. Schiek, as meaning a limit on

1 how much of their milk would get the best price?

2 DR. SCHIEK: Yes. It would, again, be a limit that was
3 based on their historical shipments.

4 JUDGE CLIFTON: All right. So there must have been a
5 surplus of milk?

6 DR. SCHIEK: Yes, I think the idea was that there were
7 producers who produced more than their base.

8 BY MR. VLAHOS:

9 Q. And if I understood your testimony, Dr. Schiek,
10 Proposal 2 was modeled after this Oregon program?

11 A. Yes, some of the provisions in Proposal 2 were, we
12 looked at the Oregon program in crafting some of those
13 provisions. The Oregon, not the Oregon program, but the
14 Oregon-Washington Order when Oregon became a part of the
15 Oregon-Washington Federal Milk Marketing Order.

16 Q. Okay. You mentioned in your discussion about Oregon,
17 and I'm going to quote it, it is in the first full paragraph on
18 page 11, and it's the last sentence of that paragraph that
19 says, "so producers are "in" unless they choose irrevocably to
20 "opt out" in writing before the first day of the month if they
21 want to be paid the uniform (order blend) price."

22 Was there a similar irrevocable opt out provision in
23 the Oregon plan?

24 A. Yes, I believe though, it was flipped. I think you
25 were out unless you opted in, so it --

1 Q. You could opt in, but otherwise you were out?

2 A. That's my understanding, yes.

3 Q. Why, in the Proposal 2, did you make the irrevocable
4 opt out provision?

5 A. As opposed to an opt in is that the question?

6 Q. Well, no, you have a provision now that once a, once a
7 producer decides to opt out, essentially makes the irrevocable
8 election, that's it forever; is that correct?

9 A. Correct.

10 Q. What's the purpose of that?

11 A. Again, I think it was this idea that the Order should
12 strive to have uniform prices, and I think the other issue is
13 the notion of producers going back and forth, and whether that
14 would be workable or not. In other words, being in, going out,
15 coming back into the program.

16 Q. Sort of like pooling and depooling of plants, milk?

17 A. Maybe you could say that. Although I see it more of
18 looking at the way the California system works, is where if you
19 don't deliver to the pool for a certain amount of time, you
20 are, you lose your quota.

21 Q. The effect of an irrevocable situation, once they make
22 the, producers once make the election, does that lead
23 eventually to a destruction of the quota program?

24 A. I think over time it would result in producers being
25 paid on the blend basis as opposed to quota overbase.

1 Q. Specifically, that would get rid of the quota?

2 A. Over time, yes.

3 Q. Over time. You, I'm going to refer you now,
4 Dr. Schiek, to page 13, the first full paragraph, and I'm going
5 to read it to you. I think this relates to your comment about
6 over time. "In putting together this proposal, we knew that
7 there would be some risk that the quota program would erode
8 over time, even as the Oregon program did over 18 plus years.
9 But we also acknowledge that USDA's preliminary economic
10 analysis conclusions were significantly faster (in light of the
11 Oregon history) than we anticipated. Despite the preliminary
12 economic analysis conclusions on a pure economic basis, we
13 continue to recognize that quota has had more "staying power"
14 than would be suggested by looking at it, at just the revenue
15 stream of various alternatives, as noted above regarding
16 California non-quota holders support for the quota, excuse me,
17 non-quota holders support for the quota, there is something
18 more going on that is undergirding the California quota
19 system."

20 Now, keeping that comment in mind, you are aware that
21 the preliminary economic analysis, impact analysis, predicted
22 that after three decision points, quota essentially would be
23 gone.

24 A. Yes, I'm aware of that.

25 Q. And you were present during Mr. Hatamiya's testimony,

1 correct?

2 A. I was.

3 Q. And in his analysis it would take four decision points,
4 by that time quota would essentially be gone.

5 A. Yes, I remember that.

6 Q. And you acknowledge that after some period of time, it
7 is really true that quota would essentially be gone.

8 A. Yes, I believe after a some period of time. It is a
9 question of how long.

10 Q. So your only question is how long it would take?

11 A. That's accurate.

12 Q. How, in your knowledge, how long would it take?

13 A. I don't really know. The experience of Oregon said
14 18 plus years, that was not as rapid as what was predicted by
15 the USDA analysis or by Mr. Hatamiya.

16 Q. Other than what happened in Oregon, do you have any
17 other basis for saying how long it would take?

18 A. Not how long, specifically. I do note that, you know,
19 in examining kind of the incentives, I guess, to, I think in
20 the following paragraph we talk about the fact that 62 percent
21 of the producers representing 63 percent of the milk, would
22 actually have a higher price than they do under the current
23 quota overbase system if they were to adopt a blend price
24 system, yet we haven't seen the sort of level of discontent or
25 drive toward a blend price system that might be, might be

1 suggested by the economic incentives.

2 Q. Well, we don't have, excuse me, were you through? I
3 didn't mean to interrupt.

4 A. Go ahead.

5 Q. We don't have a Federal Milk Marketing Order currently
6 that has provisions like Proposal Number 2.

7 A. Correct.

8 Q. And you think that producers would be, if there were
9 such a proposal, that they would not have the economic
10 incentives to opt out, so-to-speak?

11 A. If there were such a proposal as Proposal 2, is your
12 question would they have economic incentives to opt out?

13 Q. Yes.

14 A. Yes, they would.

15 Q. Okay. At the bottom of page 13, and I think it is the
16 second to the last sentence, it's the one that begins "as
17 such", and I'll quote it. "As such, it may be that the
18 economic decisions suggested by the preliminary economic
19 analysis and Mr. Hatamiya's testimony, may not happen in the
20 timeframe expected." What if they did happen in the timeframe
21 expected? Excuse me, the timeframe expected, yes.

22 A. Then it would be a rapid reduction or rapid decline in
23 quota.

24 Q. And do you think that would be a way that the Order
25 would recognize the value of quota?

1 A. I believe we recognize the value of quota simply
2 because of the way the quota premium can be paid out through
3 the, through the mechanism that we have proposed.

4 Q. But if quota is essentially phased out, destroyed after
5 three or four decision points soon after, do you consider that,
6 that quota, the value of quota has been recognized?

7 A. I think you could, yes, you could look at it that way,
8 that it has been recognized.

9 Q. How is it recognized?

10 A. By the fact that the quota premium can be paid through
11 that system. Producers are making a choice to decide to leave
12 the system, but the value can be paid.

13 Q. But if they make that choice, suppose a producer makes
14 that choice, and gosh, it was erroneous. He can't go back, can
15 he? It is irrevocable.

16 A. It is an irrevocable choice the way we proposed it.

17 Q. And that's why I'm wondering why you made it
18 irrevocable.

19 A. Again, I think my understanding in the Oregon program
20 was that there was also a choice there.

21 Q. Well, just because the Oregon program made it
22 irrevocable why include that in the California program when it
23 would just exacerbate the destruction of quota?

24 A. I think the idea that we had when we did that, was
25 that, that constructing it that way would be, would meet the,

1 what we saw as the requirements of the provisions of the Act
2 regarding uniform payment to producers, but allow for a
3 treatment of quota where the, where the \$1.70, for example
4 could be paid,

5 Q. What in the AMAA would require making that opt out
6 provision irrevocable?

7 A. I don't know that there is specifically anything in the
8 AMAA that would make it need to be irrevocable.

9 Q. Okay. I think you would agree with me that there is no
10 doubt that quota in California has significant value.

11 A. I would agree with you.

12 Q. Okay. You -- I think in your testimony you said that
13 maybe Mr. Hatamiya's testimony at 520, 525?

14 A. 525, yes.

15 Q. Maybe the high point, but that's certainly one point of
16 determining the value; is that correct?

17 A. Yes.

18 Q. Okay. And if you were to have a provision that
19 recognized, if you were compelled by a Farm Bill to recognize
20 the value, would that be a value that you would have to
21 recognize?

22 A. I think the term "recognize quota value" is, in my
23 view, again, this is just my thinking, not necessarily specific
24 enough to, I mean, you could recognize quota value by paying
25 out the \$1.70, not necessarily recognizing the asset value at

1 any particular point in time which has fluctuated over the
2 years.

3 Q. You have talked about, in your testimony, some
4 alternatives to recognizing the value. And one of them was
5 some sort of an annuity?

6 A. Correct.

7 Q. Do you know of any other FMMO that has created by the
8 regulation for the annuity?

9 A. I do not.

10 Q. Now, let's examine what the value of quota is to a
11 producer. First, I guess, it is an asset that can be bought
12 and sold, correct?

13 A. It is an asset that can be bought and sold, correct.

14 Q. And recently, in fact, almost uniformly for the last 14
15 months, something in the nature of \$525 per pound, correct?

16 A. I believe it's been in that range, yes.

17 Q. Okay. It is also a -- as an asset, it can be used, and
18 has been used, as some of the testimony producers have
19 indicated, as collateral for loans, correct?

20 A. Producers have testified to that, yes.

21 Q. Okay. And it's also, even if not used as collateral,
22 it is used to bolster up financial statements, balance sheets,
23 in order to secure financing with financial institutions; isn't
24 that correct?

25 A. I understand there's been testimony to that. I don't

1 have firsthand knowledge.

2 Q. It's also a valuable asset, is it not, in that it
3 produces a stream of income, correct?

4 A. Correct.

5 Q. And that stream of income is in the nature of 1.70 per
6 hundredweight of solids not fat quota, correct?

7 A. Well, yes. It is 19 and a half cents per pound of
8 solids not fat quota, and that equilibrates at a standard test
9 milk to \$1.70, yes. That's correct.

10 Q. So if quota is diminished or destroyed within two to
11 three, or excuse me, between three decision points, or four,
12 all those values are lost, aren't they?

13 A. Certainly if quota is gone after three or four decision
14 points, if those, whatever length those are, then, yes, that's
15 the asset value is not there anymore, that's correct.

16 Q. And have you considered what might happen to producers
17 who have used that quota to secure financing for their
18 operations?

19 A. I suspect that would make things difficult.

20 Q. Quite difficult.

21 A. Probably so.

22 Q. Okay. This annuity, let me see if I understand it.
23 First place, it is an annuity that would pay out the same
24 amount that quota holders are now receiving for the quota every
25 month.

1 A. Over the life of the annuity, yeah.

2 Q. But only over the life of the annuity?

3 A. Correct.

4 Q. And the life of the annuity that you have predicted is
5 8.4 years?

6 A. Correct.

7 Q. If there were no annuity, how long would they be
8 receiving that same amount?

9 A. Are you -- I guess I want to make sure I understand
10 your question. Are you saying if it was just the continuation
11 of the current program?

12 Q. Yes.

13 A. As long as the program would continue.

14 Q. And it has continued in the same form, namely 19 and a
15 half cents per pound of solids not fat, for, well, since 1994?

16 A. Since '94, yes.

17 Q. 21 years. And it actually can't be changed, can it?
18 Unless 1) the legislature changes it, the California
19 legislature, or 2) producers vote it out; is that correct?

20 A. That's my understanding.

21 Q. Okay. So that guaranteed stream of income that a quota
22 holder has under the quota program is not limited by 8.4 years?

23 A. Under the current program, no, it's not.

24 Q. Okay. If I understood your testimony correctly, the,
25 I'll use the term buy out, that would be accomplished by this

1 by an annuity, would be paid for out of the pool, correct?

2 A. Yes.

3 Q. That means that people who own quota would be paid to
4 buy out their own quota.

5 A. To the extent that they are not receiving the blend
6 price, yes. They would -- they would receive a somewhat lower
7 price because of the quota premium being taken off the top.

8 Q. Well, if it is coming out of the pool, and they are in
9 the pool, and they are using the pool funds to buy it out to,
10 this, to buy this annuity, they are paying for the annuity to
11 buy out their own quota, are they not?

12 A. Yes, I think you could look at it that way. I do
13 think, you know, what we're trying to do is think of an
14 alternative or present another way that USDA might be able to
15 recognize quota value that doesn't, as we said in our
16 testimony, doesn't lead to the perpetuation of paying producers
17 a non-uniform basis with no end in sight.

18 Q. Now, if I understood the letter that accompanied the
19 submission of Proposal 2, the primary, the very first point of
20 that was, there should be no Federal Milk Market Order in
21 California, correct?

22 A. I believe we made that statement, yeah.

23 Q. There are several ways to assure that, isn't there?
24 One is to, that the USDA agrees with the Dairy Institute's
25 position that there hasn't been a showing sufficient to justify

1 such an order for California. That's one way, correct?

2 A. Correct.

3 Q. Another way would be to propose a Federal Milk Market
4 Order for California that came, that contains such provisions
5 regarding quota as to make it very likely that dairy farmers
6 voting on the proposal would vote no.

7 A. I'm sure there's a lot ways one could construct an
8 Order. I am not convinced that necessarily, again, in light of
9 the fact that I believe 62 percent of the producers
10 representing 63 percent of the milk would be better off. I
11 don't know that it's a guarantee that it would be voted down.

12 Q. Okay. I'm not suggesting you guarantee, it would
13 enhance the possibility that it would be voted down, would it
14 not?

15 A. I think that's possible. Sure.

16 Q. Okay. Well, may I confer?

17 JUDGE CLIFTON: Certainly, Mr. Vlahos.

18 BY MR. VLAHOS:

19 Q. Dr. Schiek, I'm going to turn now to some questions
20 about the actual wording of Proposal Number 2 as regards to
21 quota, and I'm going to start that with the confession that the
22 labyrinthine nature of Federal Milk Market Order language, both
23 in the existing orders and those proposed, to me make the
24 Internal Revenue Code by comparison, as easy to read and
25 understand as the Ten Commandments. So it is a little

1 difficult, so please indulge me, and I may not have understood
2 fully some of your provisions, and that's why I'm seeking some
3 clarification. Do you have a copy of the Federal Register in
4 front of you?

5 A. I do.

6 Q. And I'm talking about the Notice of Hearing.

7 A. Exhibit 1?

8 Q. Yes.

9 A. Yep, I have that.

10 Q. First off, and correct me if I'm wrong, I find three
11 sections that actually talk about the California quota program.
12 One is 1051.11, which is definitions.

13 A. Uh-huh.

14 Q. One is 1051.68, which deals with producer payment,
15 notices of producers about payments. And one is 1051.72, which
16 deals with the computation of amounts due to producers and
17 co-ops, and payment to the same. Those are the three that I
18 notice. Have I missed any?

19 And let me parenthetically say, to be fair, that there
20 are some internal references to other sections, but one of them
21 that directly bears upon this is there's a reference in 1051.68
22 to 1051.62(h), although that doesn't actually use the word
23 quota in it, I think it is a section that specifically does
24 deal with quota, in part. Can you find any others?

25 A. I believe those are the primary ones, yes.

1 Q. Okay. And let's turn actually to 1051.68, and under
2 that section, let me get my page here, that's the one that
3 talks about the irrevocable notice, correct?

4 A. Correct.

5 Q. If a --

6 JUDGE CLIFTON: Let's make sure we're on the same page.
7 What I'm looking at, Mr. Vlahos, is Exhibit 1, and it's a
8 Federal Register excerpt, and I'm looking at page 47232. Is
9 that where you are?

10 MR. VLAHOS: That is where I am, your Honor, and
11 particularly in the third column of that page that deals with
12 1051.68.

13 BY MR. VLAHOS:

14 Q. If a quota holder makes that irrevocable notice, excuse
15 me, by the way, it says an irrevocable notice. What is
16 irrevocable, the notice or the election?

17 A. I believe it's the election is the intent there.

18 Q. The way it reads, it reads like it is the notice. The
19 intent was to make the election irrevocable, correct?

20 A. I believe so, yes.

21 Q. Okay. Now, if that irrevocable election is made, it's
22 an election to receive the prices that are set forth in
23 1051.62(b), correct? Excuse me, (h) not (b)?

24 A. Yes.

25 Q. Now, (h), 1051, and by the way, would you mind if

1 hereinafter I just say Section 62, knowing each time I mean
2 1051. is that all right with you?

3 A. It's okay with me.

4 Q. Okay. Section 62(h) says, calls for, defines the
5 statistical uniform price for milk containing 3.5 percent
6 butterfat, computed by combining the Class III price and the
7 producer price differential, correct?

8 A. Yes, that's Section (h).

9 Q. If you will just, for a moment I'm trying to see if
10 that means the same thing as in 1051.72. Subsection .72
11 subsection (a) talks about payments that are in an amount not
12 equal to, and then there's a list of things about what are
13 added and what are deducted and so forth and so on.

14 A. Could I shortcut you on that?

15 Q. Yeah, you can shortcut anything.

16 A. That's not -- the intent isn't to pay the statistical
17 uniform prices, it's to pay the pool prices. So it probably
18 should just say 1051.62.

19 Q. (h)? So in point of fact --

20 A. Just 62.

21 Q. The way this is drafted, subsection (a) which calls for
22 payment to certain producers, in 1062(h) which calls for
23 payment to other milk producers aren't the same?

24 A. Right. And that's -- that's not the intent.

25 Q. I see that, but I wanted to point out that -- that it

1 is, that it is wrong.

2 A. Yes. It is -- it is an error. It is a drafting error.

3 Q. All right. Now, let's turn to 1062, excuse me, to
4 Section 72, subsection (b). Subsection (b) deals with payments
5 to producers who haven't authorized a co-op associate to
6 receive them, what payments are to be to them; is that correct?

7 A. Yes.

8 Q. And these are not, are these producers who, excuse me,
9 do they include those producers who have opted out of the quota
10 system?

11 A. Yes. This would be producers who are not subject to
12 the California quota program. So by the provisions of 68, that
13 would have to be the producers either who were out-of-state
14 producers or who have opted out.

15 Q. And would also include, I guess, producers who had no
16 quota at all?

17 A. Not necessarily. I believe the way 68 is written, any
18 producer whose farm is located in California and whose milk is
19 received at a plant located in California, unless they notify.
20 So that would include California producers who have no quota
21 would be in, in the quota overbase calculation unless they
22 opted out.

23 Q. If I understand what you just said, you are saying that
24 68 includes producers that have no quota?

25 A. The way it is written, yes.

1 Q. Well, let me -- let's go through it, if we can,
2 together. And I'm not trying to be difficult, I'm truly trying
3 to understand.

4 A. Uh-huh.

5 Q. Section 68 begins with, "notification shall be given by
6 the market to producers of intent to make payment -- "

7 JUDGE CLIFTON: Well, now --

8 MR. VLAHOS: Slow down?

9 JUDGE CLIFTON: Yeah, because you left out a word.

10 MR. VLAHOS: I will try to slow down and be more thorough
11 in my reading.

12 JUDGE CLIFTON: And why don't you read the title, too,
13 since we are getting the whole section.

14 BY MR. VLAHOS:

15 Q. I shall. Payments to producers under the California
16 quota program. Notification, well, just starting off right
17 there, this is a notice to producers that have quota, isn't it?

18 A. It's a notification to producers.

19 Q. Well, okay. Let's go through it, and I'm going to
20 read, and correct me if I miss something.

21 Notification shall be given by the Market Administrator
22 to producers of intent to make payment of producer returns
23 attributable to producers who participate in the California
24 quota program in accordance with Section 1051.72.

25 So aren't we talking to producers who participate in

1 the program and not to participants -- am I missing something,
2 Mr. English?

3 MR. ENGLISH: Yes.

4 MR. VLAHOS: Okay. Thank you.

5 MR. ENGLISH: You know, order language it is very hard to
6 draft, this is all really one sentence. And so if you look at
7 the next part of this where the colon is, those who are
8 participating in the quota program, as he just said, shall be
9 identified as follows: "Any producer whose farm is located in
10 California and whose milk is received at a plant located in
11 California unless they have made this irrevocable election
12 out." So it's all producers in California start in --

13 MR. VLAHOS: With all due respect, Mr. English, I think
14 this section needs rewriting if it were to be adopted, because
15 what it says, "those who participate in the California quota
16 program", people who don't have quota don't participate in the
17 California quota, and the thing after the colon doesn't help
18 it. But anyway, that's argument. Let's not mess with that.
19 But I think there is a drafting error.

20 BY MR. VLAHOS:

21 Q. Now, also in that section, getting back to
22 Section 72 (b), there's a disjunctive there that I don't
23 understand. Again, to read, "on or before the 18th day after
24 the end of each month, the Market Administrator shall pay
25 direct to each producer who is not authorized the Cooperative

1 association to receive payment for such producer or for milk
2 not subject to the California quota program." I don't
3 understand the disjunction and perhaps you can help me out what
4 the intent here is.

5 A. I think the intent here is, we're using language to do
6 two things; one is to talk about payment to producers who are
7 not essentially being paid through their Cooperative
8 association. And the second is that this provision applies to
9 producers who are not subject to the quota program because that
10 payout is going to be done differently.

11 JUDGE CLIFTON: I want you to keep talking about it, but
12 just focus for a minute on the very last part of this
13 subsection (b) that Mr. Vlahos wants us to examine. So we're
14 on page 47233 of the Federal Register, this is in Exhibit 1,
15 and we're in the first column. And the very last phrase in
16 this subsection (b) does not, it does refer to Section 1051.86.
17 So would you turn, Dr. Schiek, to 1051.86, and tell us what
18 that is?

19 DR. SCHIEK: That is (c), Section 1000.86 which is the
20 deduction for marketing services.

21 JUDGE CLIFTON: Okay.

22 MR. VLAHOS: And actually, to be fair, Dr. Schiek, that
23 really has no relevance to what you and I have been talking
24 about. It's just another deduction. Correct?

25 DR. SCHIEK: Correct.

1 BY MR. VLAHOS:

2 Q. Okay. Okay. Let's turn to subsection 72(c)1, and that
3 deals to payments who co-ops whose members have authorized to
4 receive payments on their behalf; is that correct?

5 A. Yes.

6 Q. Now, this section in its language says that the
7 payments are going to be made to a Cooperative association, and
8 then later it says, which is not subject to the California
9 quota program pursuant to Section 1051.68. Just one reference
10 there, 1051.68 makes no reference to cooperatives; am I
11 correct?

12 A. No, it does not. So you are correct.

13 Q. Okay. Although again, is that maybe also one of those,
14 and I'm not criticizing, I'm just saying, may be one of those
15 drafting errors?

16 A. I think, again, the intent is the same to basically say
17 this payment provision applies to Cooperatives with respect to
18 producers who are not part of the quota system, or who have
19 elected to not be part of the quota system. That's the intent
20 anyway.

21 Q. Okay. Whatever the language says, that's the intent?

22 A. That's the intent.

23 Q. Okay. Do you think the language says that?

24 A. Well, it made sense to me when I read it, but it
25 doesn't necessarily mean it makes sense to everyone.

1 Q. Okay. Good enough. I'm also confused a little bit
2 though, even assuming that 1068 mentions Cooperatives, it says
3 that payments are going to be made to each Cooperative
4 association which is not subject to a California quota program
5 pursuant to 1051.68. But 1061.68 applies to producers and
6 let's say, and co-ops who are a part of the California quota
7 system. So I don't understand that sentence.

8 A. So, again, I think the intent here is to provide
9 requirements on payments to producers who receive their
10 payments from their co-ops, but it's to apply to producers who
11 are not going to be paid on the basis of quota and overbase.
12 So I don't know if that clarifies it any more, but that's what
13 the intent is there.

14 Q. I thank you for the intent, it does not clarify the
15 language for me. It does tell me what your intent is.

16 Now, I'm going to get into how the quota premium gets
17 paid. How does it get paid and where?

18 A. It gets paid by CDFA.

19 Q. And pursuant to what section?

20 A. So the Order language does not provide direction for
21 CDFA to pay for quota or to pay on the basis of quota or
22 overbase, or quota and non-quota. What it does is it, this
23 section (c)(2) directs the Market Administrator to make
24 payments to the Milk Pooling Branch of CDFA for the producers
25 and Cooperative association members, I guess this would be, for

1 milk subject to the quota program. So the producers who are in
2 the quota program and are going to be paid on the basis of
3 their quota and overbase, or quota and non-quota holdings, this
4 basically directs the Market Administrator to move those funds,
5 pay those funds to CDFA, and then CDFA will distribute them to
6 producers.

7 Q. Thank you. But what's unclear to me is what is paid
8 over to the California Department of Food and Agriculture Milk
9 Pooling Branch. I can't see anywhere where it says the quota
10 premium is paid there.

11 A. So, yeah, it references the aggregate of the payments
12 otherwise due such individual producers and Cooperative
13 associations pursuant to Paragraph B, and subparagraph c(1) of
14 this section.

15 Q. But those two paragraphs aren't, don't refer to payment
16 of quota premium?

17 A. What they refer to is essentially the payment of the
18 blend value. So what this is suggesting is, or the producer
19 payment prices under Section 62, so what this paragraph is
20 saying is that that value that those producers are owed at the
21 blend, that aggregate value would be paid to CDFA, and that
22 that would, CDFA would redistribute based on quota and
23 overbase.

24 Q. Well, I am sure that was your intent, but what I'm
25 finding difficulty is finding any language that says that. And

1 it is your contention that (c)(2) actually says that?

2 A. Yeah. Yes.

3 Q. Well, I guess we're going to have to have some
4 disagreement on that. And with that, I think I concluded my
5 cross-examination.

6 JUDGE CLIFTON: Thank you, Mr. Vlahos. Dr. Schiek, would
7 you look please with me at Provision A8, so that's the last
8 provision just before B that we discussed at length, and you
9 will see that that has a reference to the same kind of
10 marketing services being deducted.

11 Do you think that section should be conformed to be
12 like the last part of subsection (b)? Do you see the
13 difference between them?

14 DR. SCHIEK: So on the last part of subsection (b) you are
15 talking -- okay.

16 JUDGE CLIFTON: Would you help, Mr. English?

17 MR. ENGLISH: Yes. So while I might disagree about any
18 other drafting errors, I would say it does look like in 8 we
19 have 1000.86 versus B we have 1051.86, and so probably, would
20 you agree, Dr. Schiek, that in 8 it should be 1051.86, and you
21 just managed to miss one of those?

22 DR. SCHIEK: Yes, it should be.

23 MR. ENGLISH: Thank you, your Honor.

24 JUDGE CLIFTON: Thank you. See, I do the little stuff.
25 This complicated stuff is beyond me. Mr. Beshore?

1 CROSS-EXAMINATION

2 BY MR. BESHORE:

3 Q. Thank you, your Honor, Marvin Beshore.

4 Good afternoon, Dr. Schiek.

5 A. Good afternoon.

6 Q. I would like to explore with you just a bit the
7 legislative language that you are construing, and if you go to
8 page 6 of 145, in the middle paragraph, right about the middle
9 of the page, the sentence that starts with the 1996 Farm Bill
10 language, continues, "which to my knowledge did not
11 specifically amend the AMAA is as follows:" So I want to just
12 look at this language with you, see if I can understand what
13 your interpretation is. So the first part of it says, "the
14 Order covering California shall have the right to reblend."

15 Do you see that?

16 A. Yes.

17 Q. Okay. Now, prior to this legislation, would an Order
18 covering the State of California have had the right to reblend
19 under the AMAA?

20 A. I don't believe so.

21 Q. Okay. So prior to this legislation, a California order
22 would not have had the right to reblend, therefore, it must
23 follow that this legislation provided some right for that order
24 that it did not have under the legislation pre-existing,
25 correct?

1 A. As I read the language, yes.

2 Q. So what, if the order has new rights after the
3 legislation under the law than it did before, in what sense can
4 you say that it was not amended?

5 A. Mr. Beshore, in terms of our thinking, and certainly
6 others may have other thinking on this, there's no reference in
7 the language specifically to the AMAA, that would be one thing.
8 So our view in looking at it was we have this language that
9 says, "The order covering California shall have the right to
10 reblend and distribute order receipts to recognize quota
11 value."

12 Q. I'll get to the last half of it?

13 MR. ENGLISH: Would you let him answer the question,
14 please?

15 JUDGE CLIFTON: I agree. You will be able to examine
16 further on the last half, but it is proper for Dr. Schiek, in
17 formulating his thought, to get hold of the whole piece.

18 DR. SCHIEK: And at the same time, we have these provisions
19 of the AMAA that talk about uniform payment to producers, and
20 also the Section in 5(g) that talks about trade barriers. So,
21 you know, what we're thinking or what our thinking was, was
22 trying to reconcile those concepts, the Farm Bill language with
23 the AMAA language.

24 BY MR. BESHORE:

25 Q. So if these are separate, non-integrated pieces of

1 legislation, is that your -- is that your position? That since
2 it's not amending the Act, these are, these are separate and
3 you don't put them together, they are separate non-integrated?

4 A. I don't know if I would characterize it that way, but I
5 do see them as both still operative, I guess. And again,
6 that's the thinking that we had. Others may see it
7 differently, but that's how we thought about it.

8 Q. So when this law, when Congress said "the order" what
9 was it referring to there?

10 A. The order covering California.

11 Q. And what order would it have been talking about?

12 A. Well, it's going to be a Federal Order.

13 Q. Under what statute?

14 A. It's a Farm Bill language reference to a Federal Order.

15 Q. Under what statute would there be a Federal Order?

16 A. The statutory authority would be from the AMAA.

17 Q. Okay. So Congress was talking about an order under the
18 AMAA covering California, correct? You agree with that?

19 A. They are talking about a Federal Order.

20 Q. Okay. And it did not have the right to reblend,
21 Federal Orders did not have the right to reblend before this
22 legislation. You have acknowledged that, correct?

23 A. That would be my understanding, yes.

24 Q. Okay. And now it has the right to reblend. What does
25 reblend mean as far as you are concerned, in this Congressional

1 legislation?

2 A. Reblend would be to have the, would be to essentially
3 distribute order receipts on another basis.

4 Q. In a way --

5 JUDGE CLIFTON: Your voice dropped off. Say it again?

6 DR. SCHIEK: To redistribute order receipts on another
7 basis.

8 JUDGE CLIFTON: On another basis.

9 MR. BESHORE: In other words, on a basis that it could not
10 distribute them before this legislation, correct?

11 DR. SCHIEK: Yes. As I read the language, that's what it
12 means.

13 BY MR. BESHORE:

14 Q. Now, "distribute order receipts". What do you
15 understand that language in the '96 Farm Bill to be referring
16 to?

17 A. I think that would mean pool receipts.

18 Q. Okay. The, in other words, that speaks to how the
19 funds in the Producer Settlement Fund are distributed to dairy
20 farmers, correct?

21 A. Yes.

22 Q. And prior to this legislation, would a California
23 Federal Order have had the right to distribute pool funds to
24 recognize quota value?

25 A. I don't believe so.

1 Q. But now it does?

2 A. "Has the right" is what the language says. It has the
3 right.

4 Q. Now, so now a California Federal Order can do something
5 that it was not authorized to do under the Agricultural
6 Marketing Agreement Act before the 1996 Farm Bill was passed;
7 isn't that correct, Dr. Schiek?

8 A. It has the right to do something it could not do before
9 the Act was passed.

10 Q. Right. It has the right to distribute order receipts
11 to recognize quota value, which it could not do before the Act
12 was passed; isn't that correct?

13 A. Yes.

14 Q. Are you familiar with the parts of the Agricultural
15 Marketing Agreement Act which describe how the pool may be
16 distributed before this legislation was passed?

17 A. I'm familiar with Section 608c(5)(B).

18 Q. Okay. And that described how the order was authorized
19 to distribute pool proceeds before the 1996 Farm Bill was
20 passed; isn't that correct?

21 A. Yes.

22 Q. Okay. And now, as you have testified, after the 1996
23 Farm Bill was passed, the order can distribute, the California
24 Order has the right to distribute order proceeds to recognize
25 quota value, which it did not have before the Farm Bill was

1 passed; isn't that correct?

2 A. Yes, I think there was permission there there that was
3 not there before.

4 Q. So, therefore, as far as you are concerned, the law was
5 not amended?

6 A. My view is that the payment of uniform prices is pretty
7 much the heart of the order program. And as I look at this, it
8 is, again, you are asking me, so as I look at this language, I
9 see it as a permissive, shall, the order shall have the right.
10 But again, I think our thinking was we were trying to reconcile
11 both of those issues, that uniform payment to producers and
12 this language from the '96 Farm Bill.

13 Q. So when you say it is a permissive, when you are
14 looking at it as permissive, in your view, this was permitted
15 but not compelled?

16 A. I would say that would be right.

17 Q. Thank you.

18 JUDGE CLIFTON: Who next -- Ms. Hancock, do you have
19 something? Mr. Hill, would you pull the mic toward you?

20 MR. HILL: This is Brian Hill. Before we go into another
21 round of questioning, I think we need to have a slight break.
22 It's been nearly an hour and 50 minutes at this point.

23 JUDGE CLIFTON: That time really did fly, I'm telling you.
24 Okay. Let's be back and ready to go at 3:45.

25 (Whereupon, a break was taken.)

1 JUDGE CLIFTON: We're back on record at 3:46.

2 Ms. Hancock, I would like you to come to the podium. I have a
3 procedural matter I would like to address first. I wanted to
4 ask, Ms. Hancock, would you be the one presenting direct
5 testimony of Mr. Gonsalves?

6 MS. HANCOCK: Mr. Bao Vu from my office will present his
7 testimony.

8 JUDGE CLIFTON: All right. Do you have any interest in
9 presenting his testimony now in the hope that he could leave
10 today, or would you prefer, and it's entirely up to you, to
11 proceed with your cross-examination of Dr. Schiek?

12 MS. HANCOCK: So if it helps at all, I think my
13 cross-examination is going to be very short of Dr. Schiek, and
14 so I think it makes sense to just finish it. And Mr. Gonsalves
15 is here until 1:00 tomorrow, but there is a chance that he
16 could potentially be able to come back on Friday. And I think
17 it has to be, and I have told Chip this, or Mr. English this, I
18 think it's a priority that he is able to get his witnesses who
19 have been here for all these weeks out the door. And give him
20 a little bit of reprieve, too, because he can't really let down
21 until he is done with his case. So I'll leave it to him if he
22 wants to start, if he wants to start Mr. Gonsalves. And I told
23 him I would give him an advance copy of the testimony so he
24 could make the determination. It's -- it is just historical
25 legislative history, it is not getting into any opinion

1 testimony, so that might make it fast testimony.

2 JUDGE CLIFTON: Okay. So far that has not been fast
3 testimony.

4 MS. HANCOCK: Fair enough.

5 JUDGE CLIFTON: All right. Good. So you may resume, you
6 may begin your cross-examination of Dr. Schiek.

7 CROSS-EXAMINATION

8 BY MS. HANCOCK:

9 Q. Good afternoon, Dr. Schiek.

10 A. Good afternoon.

11 Q. Nicole Hancock for the Producer Handlers Association
12 and Ponderosa. Let me see, I just have a few questions. Am I
13 understanding correctly, you have, in your testimony, in
14 talking about quota, quota was put into place in order to
15 compensate producers; is that right?

16 A. It was put in place, I think, to get producers to
17 support pooling.

18 JUDGE CLIFTON: Your voice dropped.

19 DR. SCHIEK: It was put in place, I believe, to get
20 producers to support pooling, that was part of the overall
21 concept of bringing pooling in, and quota was necessary for
22 that.

23 BY MS. HANCOCK:

24 Q. And it was a form of compensation to the producers for
25 creating that Class I relationships with their processors?

1 A. Yeah, I think that's what I said in my testimony.

2 Q. Okay. And I said it before, I just want to make sure
3 that I'm understanding it correctly. So even if you have said
4 it, I just want to make sure that I have got it and I'm
5 understanding it the same way you meant it. So what about
6 exempt quota?

7 A. So are you asking about our proposal on exempt quota
8 or --

9 Q. No, I'm still talking about compensating producers.
10 Exempt quota was issued as a form of compensation at the same
11 time; is that right?

12 A. Exempt quota was -- yes. It was issued at the same
13 time pooling came into place to, to again, get support for
14 pooling from folks who were affected by that producer-handlers.

15 Q. Okay. But it was also a form of compensation, like the
16 quota, regular quota was issued to producers; is that right?

17 A. Yeah, it can be looked at that way, sure.

18 Q. And it's actually, for regular quota, it's the producer
19 that owns that quota; is that right?

20 A. Producer owns quota, yes.

21 Q. And it's issued in the form of a certificate of
22 ownership, were you aware of that?

23 A. Actually, no. So I'll take your word for that.

24 Q. Okay. So under Proposal Number 2 from Dairy Institute,
25 what happens to exempt quota?

1 A. So the way we treat exempt quota is it really, it
2 becomes regular quota under our proposal.

3 Q. And is there any compensation given to the exempt quota
4 holders to recognize the additional value that exempt quota
5 holds?

6 A. We haven't included any, no.

7 Q. Okay. You agree that there is a value above and beyond
8 regular quota that exempt quota represents to those who hold
9 it?

10 A. I believe there's -- there's certainly a market value
11 over that market value. There's a value to the holder of
12 quota, holder of exempt quota, and I think that's been
13 testified to. What that, you know, in terms of equating that
14 to a market value, I don't know exactly what -- what that would
15 be.

16 Q. Okay. But you agree that above and beyond regular
17 quota, the exempt quota holds an additional value?

18 A. Yeah, it holds an additional value for the
19 producer-handler.

20 Q. Under the Dairy Institute's proposal, would regular
21 quota remain transferrable as it is today under the California
22 state system?

23 A. Yes. We haven't -- we haven't provided any provisions
24 to keep that from happening, that's handled within the CDFA.

25 Q. And the depooling or the election not to pool, that's a

1 choice that's made by the producer?

2 A. That's a choice that's made by the handler, the
3 election to pool.

4 Q. I thought you said that the farmers get an option to
5 either stay in the pool and take their quota benefit, or accept
6 the traditional Federal Order price?

7 A. Okay. So what you are talking about there is the
8 election to either continue to be paid by, on the basis of
9 quota and overbase, and/or the decision to get a blend price,
10 and that is a producer decision.

11 Q. Okay. And I think you covered this. Once they make
12 the decision, it is a permanent decision if they have elected
13 to take the traditional Federal Order blend price?

14 A. Correct. That's how we proposed it.

15 Q. And then if they owned quota at the time that they make
16 that election, they would have to sell it to somebody who has
17 opted to stay in the pool?

18 A. Presumably that's what would happen, yeah.

19 Q. Okay. So do you just --

20 JUDGE CLIFTON: I'm confused by the who has decided to stay
21 in the pool. By that, Ms. Hancock, you mean who has decided to
22 stay with the option of having the value of the quota
23 recognized?

24 MS. HANCOCK: Yes.

25 JUDGE CLIFTON: Okay.

1 MS. HANCOCK: I get stuck in using the wrong terms so you
2 will have to forgive me for that. What I meant was, for those
3 producers who have elected to stay, who have elected to
4 continue to receive the quota benefit for the payments under
5 the, whatever it's called, the -- where they are receiving the
6 quota payment.

7 DR. SCHIEK: The quota plan.

8 BY MS. HANCOCK:

9 Q. The quota plan. So they would have to, if somebody
10 elected to take the traditional Federal Order payment, they
11 would have to then sell their quota to farmers who were still
12 electing to take the quota benefits; is that right?

13 A. Yes, that would be how it would work.

14 Q. Could they sell to a farmer who did not, was not
15 participating in the quota blend payment option, and allow
16 somebody new to enter into that payment plan?

17 A. I would think if it was a new producer, that would be
18 an option for them. I'm not sure if it's a producer that has
19 already opted out, whether that would, the way it's written
20 would work.

21 Q. So the number of potential buyers for the quota would
22 go down, it would have to be a new producer; is that right?

23 A. Yeah, depending on how many people decide to opt out.
24 The number of potential buyers could go down.

25 Q. So would you agree, then, that the market value for

1 that quota would be diminished because the number of potential
2 buyers would be reduced?

3 A. Yeah, I think that could be a consequence. Sure.

4 Q. So under Proposal Number 2 or, and/or Proposal
5 Number 1, if a producer-handler produced more than the three
6 million pound mark, they would not qualify as a
7 producer-handler within the definition; is that right?

8 A. That's correct.

9 Q. So then they would just really be a producer, a farmer?

10 A. Uh-huh. Correct.

11 Q. And a handler, a plant, right? It would just be
12 operating two separate entities without any regulatory, or they
13 would be operating under the regulations as an independent
14 producer and independent handler?

15 A. Right. If I understand your question, instead of
16 having a producer-handler status, they would be a handler with
17 respect to their processing plant, and a producer with respect
18 to their farms.

19 Q. Is that how you understand it basically?

20 A. Yes.

21 Q. Okay. So well, I think that's good. That's all I
22 have. Thank you.

23 JUDGE CLIFTON: Who else has questions for Dr. Schiek?
24 Mr. Schaefer?

25 /////

1 CROSS-EXAMINATION

2 BY MR. SCHAEFER:

3 Q. Henry Schaefer.

4 I don't know whether I got demoted or promoted but they
5 sent me over here.

6 Dr. Schiek, thank you for coming. A few questions in
7 Mr. Vlahos was kind of headed down this path, and he came just
8 about this close, and I was thinking, "oh, good, I don't have
9 to ask any questions." But didn't quite get there.

10 With regard to payment to producers, as I read the,
11 understand your order language, the partial payment portion of
12 that, the handlers would just pay the producers as currently in
13 most orders; is that correct?

14 A. Correct.

15 Q. Then when we get into 72, which is final payment to
16 producers, we have got (B), c(1), and c(2). And in (B), as I
17 understand from what you said and your order language,
18 basically the 72(B) provision, has the Market Administrator
19 paying producers who are not members of cooperatives, or have
20 not authorized the Cooperative to collect their payment and
21 have no quota; is that correct?

22 A. Or are, have elected not to be part of the quota. They
23 have elected to take the federal blend option, right.

24 Q. Okay. And so then in 72(C)(1), the Market
25 Administrator is paying the co-op for the producers that have

1 authorized the co-op to collect that for them, and they also
2 have no quota in that group; is that correct?

3 A. Again, I think that it's for those producers that are,
4 have opted to be part of the blend pay out as supposed to the
5 quota pay out.

6 Q. Okay. But that would also include ones that don't have
7 quota at all?

8 A. Okay. So I think the answer, the answer is no as I
9 understand what we attempted to do here, which is unless the
10 producer specifically opts out, they are going to get paid on
11 the basis of the quota and non-quota holding. So if they are a
12 hundred percent non-quota, they are going to get a hundred
13 percent of the non-quota price, if they stay in the
14 quota/non-quota pool, so-to-speak. If they opt out, then they
15 get the blend price. So if they have not opted out, if they
16 have opted out, they would they would be paid according to the
17 provisions of (C)(1).

18 Q. Okay. So the ones that don't have any quota at all
19 would just get paid by the Cooperative as in a normal payment
20 procedure?

21 A. That's not what we intended. I think the idea is, if
22 you have no quota at all and you are a California producer,
23 just like today, if you have no quota in California today, you
24 get paid the overbase price on all your milk. So the idea here
25 is that a producer has to elect to opt out if they want to

1 receive the blend price. So if they have not opted out, they
2 would, if they have not opted out, they would still be part of
3 the quota overbase or quota non-quota pool, and they would be
4 paid the non-quota price, a hundred percent non-quota price.
5 If they opt out, then they would get paid the blend.

6 Q. Okay. And then the co-op would pay that directly and
7 they would not, and the co-op would pay that directly just as
8 they would otherwise?

9 A. Right.

10 Q. Okay.

11 A. Right.

12 Q. And then in (c)(2), or yeah, 72 (C)(2), the Market
13 Administrator is going to pay for the producers that have quota
14 and are not part of a basically are not part of a Cooperatives;
15 is that correct?

16 A. They would pay for, I believe for both.

17 Q. Okay.

18 A. And that money would go over to CDFA for distribution.

19 Q. Okay. And so that brings up the question, where does
20 CDFA get the money to pay out the quota?

21 A. So what would be transferred from the Market
22 Administrator would be the blend value of all those producers'
23 quota, and then they would, CDFA would reblend it to pay it out
24 on a basis of quota and non-quota.

25 Q. And --

1 A. And they would pay it out.

2 Q. And as I read the order language in the calculation of
3 the blend price, there is nothing in that calculation that
4 shows any deduction for quota monies, so where would the Market
5 Administrator get the money to pay out the quotas at CDFA?

6 A. So the way it's set up is that they wouldn't be paying
7 quota, they would be transferring the blend value of all the
8 producers who want to be paid on the basis of quota and
9 non-quota to CDFA. CDFA would then figure out, okay, what's
10 the -- what's the quota price, what's the non-quota price,
11 based on that pool of revenue that they have. So it would be a
12 redistribution of that blended value revenue on the basis of
13 quota and overbase or quota and non-quota, I'm sorry.

14 Q. And would that be the last, since this is kind of a
15 three steps here, is that what remains after the first, after
16 72(b) and 72(c)(1) are paid out?

17 A. That's the intent, yeah.

18 Q. Okay. Okay. Since the Market Administrator is
19 involved quite a bit in the payment to producers and payment to
20 cooperatives here out of the, for the final payment, was there
21 any analysis or looking at what the cost would be to the Market
22 Administrator to do that?

23 A. No, there wasn't specifically an analysis of the cost,
24 so, no.

25 Q. Okay. And then, again, going back to a little bit to

1 the payment procedure. Who is going to be responsible for
2 minimum payment? Since the Market Administrator is paying some
3 of these producers, is it the Market Administrator, then, would
4 be responsible for minimum payment to the producer, or the
5 handler that they are, were -- that pooled them, which is how,
6 normally the handler who pooled them is responsible for minimum
7 payment and the Market Administrator assures that that is done.
8 In this case, would that still be true?

9 A. So I think this is different. The handlers are still
10 responsible on that partial payment at the terms that are kind
11 of listed here. But, yes, the final payment would be made to
12 the Market Administrator. They would have to make that
13 calculation to determine that the payment was made, or to make
14 the correct payment. Correct.

15 JUDGE CLIFTON: Would you just express that thought again,
16 Dr. Schiek? So you have gotten to the final payment, who makes
17 it to the producer?

18 DR. SCHIEK: The Market Administrator, which is different
19 than, yes, how it's done in most orders.

20 BY MR. SCHAEFER:

21 Q. So the Market Administrator has to get the information
22 from the handler.

23 A. Right.

24 Q. And the pool would have to be structured so that the
25 money is in the pool --

1 A. Correct.

2 Q. -- to make that final payment?

3 A. Correct.

4 Q. Okay. Thank you very much, Dr. Schiek.

5 JUDGE CLIFTON: Ms. May.

6 CROSS-EXAMINATION

7 BY MS. MAY:

8 Q. Good afternoon, Laurel May with USDA.

9 A. Good afternoon.

10 Q. I have a few questions for you. Your discussion about
11 this alternative proposal, is that something that you are
12 actually proposing or is that just an example of something that
13 you looked at that might work?

14 A. I would say the latter. It is something we looked at.
15 We still, I think, had issues in terms of, we weren't certain
16 about whether it satisfies our concerns about out-of-state milk
17 the way it's structured, but we wanted to put it out as an
18 example of what we thought was another way to recognize quota
19 value. That's essentially what it was.

20 Q. Okay. My impression from your discussion is that you
21 are perhaps inviting USDA to come up with a solution here or an
22 alternative?

23 A. I think what we were saying is that USDA is ultimately
24 going to make a decision about how -- how things are going to
25 work with regard to quota in a California Federal Milk

1 Marketing Order, and we were, I guess, providing an example on
2 just another item to consider or another idea to consider.

3 Q. Well, and we certainly welcome ideas. On that one
4 proposal, one of the questions I had was about setting the
5 value of quota at any given point from which you would start,
6 you know, calculating the annuity. And so how, where would you
7 see that happening?

8 A. You know, I think using the example that we have used,
9 we were looking at a point in time, and you know, one option
10 would be to kind of look at a point in time like when the order
11 becomes effective, what is it, what is the trading value of
12 quota, or you could look, I suppose, at an average over a
13 recent period of time, recognizing that there's fluctuations.
14 So those would be the ways I would look at it.

15 Q. Okay. So it wasn't necessarily that number that you
16 had in the --

17 A. No, that -- no, no.

18 Q. -- proposal. Okay. Hang on one second. One of our
19 colleagues suggested that we ask you about your example of the
20 Arizona plant on page 8. The second problem that you
21 identified is that "the Arizona plant will be contributing to
22 the quota premium through the pool on any California milk it
23 purchases, unlike what happens today. To the extent that the
24 plant attracts a milk supply today using at least the full FMMO
25 traditional blend, the logical economic impact is that the

1 California milk supply will look to recoup some or all of that
2 lost revenue through over order premiums."

3 I, for sure, was having a hard time getting my head
4 around that whole diagram.

5 A. Okay. That's fair. I think the idea there is that the
6 producer is receiving one price today. As we see that
7 situation, under a Federal Order, they would be receiving a
8 lower price. Obviously, it depends on the competitive
9 conditions, whether that producer is able to basically say I
10 want to get the higher price that I was being paid before, but
11 if that is the case, they might, the issue is that plant would
12 pay over order premiums to make that happen, whereas other
13 plants may be similarly situated who are located in California
14 maybe aren't paying those over order premiums, or don't need to
15 pay those over order premiums, because there was no
16 pre-existing, different payment level to begin with.

17 Q. Okay. So it's the change from one --

18 A. It is the change.

19 Q. Okay. That makes more sense.

20 A. Okay.

21 Q. All right. Thank you.

22 CROSS-EXAMINATION

23 BY MR. RICHMOND:

24 Q. Bill Richmond, USDA. Thank you, Dr. Schiek.

25 Just one additional minor clarifying question to just

1 revisit a question that Ms. May had.

2 You say on page 1, I believe, that the Dairy Institute
3 and its members did not set out basically to destroy the quota
4 program. Yet, you agree throughout your, the line of cross
5 examination that you agreed with the Department's analysis that
6 if the Dairy Institute's proposal were, in fact, adopted, that
7 there essentially wouldn't be enough money to pay out quota in
8 a relatively short amount of time. Correct?

9 A. Or, yeah, or another way to look at it is quota holders
10 would exit the system, and pretty much at the end, the
11 producers in there would be receiving just a blend value.

12 Q. Okay. And so based on the shortcomings of Proposal 1
13 as you have described, so you know, mandatory pooling,
14 non-uniform payments to producers, denying the traditional
15 order blend price to out-of-state producers, is it your intent
16 to basically give the Department some kind of flexibility in
17 recognizing the California quota program?

18 A. Yeah, I think that's accurate. That's an accurate
19 statement. I mean, we were trying to describe how we ended up
20 where we ended up with the proposal that we put forward. We
21 also tried to say, Hey, there might be another way, another way
22 to, potential way to recognize quota, but, yes, the flexibility
23 I think is what we're giving or what we're arguing for.

24 Q. Okay. Just a flexibility with what we're able to do
25 under the statute. Okay. We appreciate it very much. That's

1 all. Thank you.

2 JUDGE CLIFTON: Dr. Schiek, did your group discuss what
3 would happen if California changed the rules about quota? Such
4 as changing from the way they now pay for the solids not fat
5 part or any other change that might make a big difference in
6 what percentage of revenues were required to satisfy quota?

7 DR. SCHIEK: We didn't specifically look at that. We, you
8 know, we did kind of look at maybe different, you know, on this
9 annuity idea, different payback lengths, but didn't reach any
10 particular conclusions on that.

11 JUDGE CLIFTON: Because that's a fixed dollar amount and
12 not a percentage, you would think it would need updating from
13 time to time, but it hasn't been updated for, what was it, 21
14 years or something of the like? Am I right on that?

15 DR. SCHIEK: That's correct. The pooling statute
16 amendments from 1994 set that rate at 19 and a half cents per
17 pound of quota, solids not fat, and it hasn't been changed
18 since.

19 JUDGE CLIFTON: And as you see it, USDA would have nothing
20 to do with any changes, it would all be done under California's
21 system?

22 DR. SCHIEK: Yeah, I think, you know, what we proposed was
23 having, having the State or the Federal Order collect the
24 revenue and then transfer it to the state for distribution.

25 JUDGE CLIFTON: And the way the Market Administrator would

1 decide what amount of money to turn over to the California
2 Department of Food and Agriculture is based on what
3 calculation?

4 DR. SCHIEK: It's based on the producers, the blend value
5 or the uniform price that would be paid to those producers in
6 aggregate who elect to stay as part of the quota/non-quota
7 system. That's the total amount of money that would be
8 available and transferred.

9 JUDGE CLIFTON: And you call it a quota/non-quota group,
10 but is there anybody in that group that's non-quota?

11 DR. SCHIEK: Well, any individual producer is going to have
12 some share of quota and non-quota.

13 JUDGE CLIFTON: I get it. Thank you. So we know that the
14 California producers all are crying out for the Federal Order
15 prices, we have heard heard it over and over and over again. It
16 seems somehow Draconian to me to say to people holding quota,
17 "Everybody can have those Federal Order prices but you." That
18 that seems really unfair to me.

19 DR. SCHIEK: So under the proposal, they would have the
20 option to say, we want to be paid the Federal Order blend
21 price. So they could, they could have access to that by making
22 that election.

23 JUDGE CLIFTON: But only if they give up their valuable
24 asset?

25 DR. SCHIEK: That's true, the way it is structured, which

1 is one of the reasons why we looked at another alternative as
2 more of an annuity pay out to essentially pay off the quota.

3 JUDGE CLIFTON: And yet, the only way that can be funded is
4 out of the revenue stream for each month's receipts from the
5 sale of the milk?

6 DR. SCHIEK: That's correct.

7 JUDGE CLIFTON: That's the rub.

8 DR. SCHIEK: Yep.

9 JUDGE CLIFTON: There's no fund. Yeah, I think USDA is
10 going to have to have a lot of flexibility. It's just a very,
11 very difficult problem. Who else has questions for Dr. Schiek?
12 Any redirect?

13 REDIRECT EXAMINATION

14 BY MR. ENGLISH:

15 Q. At the danger -- Chip English -- at the danger of
16 making things more confusing. Going back to the questions from
17 Judge Clifton, one of the, is it one of the conundrums for USDA
18 that if they adopt, as in Proposal 1, the quota system, that
19 California can change by statute how the quota system works,
20 effectively changing the pricing under the Federal Orders?

21 A. I believe that would be a possibility, yes.

22 Q. So let me just see if I can clarify Section 68, and we
23 acknowledge it came from Oregon, so maybe if you turn it
24 around. If the concept is that on Day 1, first of all, we take
25 the out-of-state milk out, correct, Dr. Schiek?

1 A. Correct.

2 Q. On Day 1 every dairy farmer in California, whether they
3 have quota or not, or if they have a hundred percent quota or
4 one percent quota, is part, is a California, is a participant
5 in the California quota program, correct?

6 A. Correct.

7 Q. Okay. So when one reads the Section 72, assume for a
8 moment that no one opts out the first month, just to read
9 Section 72, then the only monies paid under (b) or (c) would be
10 for out-of-state milk, correct?

11 A. Correct.

12 Q. Okay. And so to the extent that, and I can understand
13 why, to the extent questioners have said that overbase milk is
14 automatically included in (b) or (c), that's not right, it is
15 only milk that has opted out of being a participant in the
16 California quota program, correct?

17 A. It's only -- right. It's only the out-of-state milk or
18 milk that's opted out.

19 Q. Okay. That's all I have, your Honor.

20 JUDGE CLIFTON: Additional questions from USDA?

21 RE-CROSS-EXAMINATION

22 BY MR. CARMAN:

23 Q. Clifford Carman, USDA. Could you clarify the opt out
24 timing that you are talking about? For example, if the Order
25 were to start January 1, 2017, would the opt out provision be

1 acceptable issued in December of 2016?

2 A. Okay. So there's no Order yet, and yet they wouldn't
3 be able to -- you are saying they wouldn't be able to opt out a
4 month ahead of time because there is no Order, so that would
5 mean the first month everybody would be in. That's the way it
6 is drafted. Maybe that's something we need to look at in terms
7 of providing for that flexibility so they could opt out that
8 first.

9 Q. Well, it would make a provision in the Order effective
10 before the Order was effective, so I think there's a timing
11 issue.

12 A. Okay. Well -- well said, and thank you for noting
13 that.

14 JUDGE CLIFTON: Are there any other questions before I
15 invite further redirect? I see none. Further redirect? There
16 is none. Dr. Schiek, thank you for helping us with an
17 extremely difficult subject.

18 MR. ENGLISH: So, your Honor, what I propose doing is
19 getting Mr. Blaufuss started, and getting him on the stand,
20 getting his testimony distributed, and going those 30 minutes
21 or whatever we have. And then I commit, to look at, if
22 Ms. Hancock can share with me the testimony. And if I think
23 that as a result of that, cross-examination will be limited,
24 I'll try to work with her or otherwise come back Friday. I do
25 understand from Mr. Beshore that there are four dairy farmers

1 coming Wednesday and they couldn't move. So that may make it a
2 little harder. I'm trying to work with you, Ms. Hancock, but
3 I'm not sure if -- let me stop talking and get Mr. Blaufuss on
4 the stand.

5 JUDGE CLIFTON: We appreciate that. And I'm very glad to
6 know about the dairy farmers have to be Wednesday, which makes
7 it harder for us to finish Ms. Taylor and Mr. Blaufuss on time.

8 MR. ENGLISH: We are distributing a relatively short
9 statement, a little over six pages -- well, six pages plus an
10 end note, testimony of Rob Blaufuss, Part 4, and a modest
11 little 62 page exhibit also labeled Part 4. And for those who
12 weren't here or have conveniently forgotten for good and
13 sufficient reason, Part 4 is coming after Part 4 -- I think
14 that's perfectly appropriate for this proceeding -- but this is
15 the fortification allowance section.

16 JUDGE CLIFTON: Does everyone get colored copies of the
17 exhibits?

18 MR. ENGLISH: Yes, at great expense it turns out.

19 JUDGE CLIFTON: Yeah, it is extremely expensive, and I
20 appreciate it because it's very helpful.

21 Ms. Frisius, I'm going to mark the testimony of
22 Mr. Blaufuss, Part 4, as 147; that is right? Then I'm going to
23 mark the exhibits of Mr. Rob Blaufuss, Part 4, as Exhibit 148.

24 (Thereafter, Exhibit 147 and Exhibit 148,
25 were marked for identification.)

1 JUDGE CLIFTON: Mr. Blaufuss, you remain sworn. Would you
2 again state and spell your name?

3 MR. BLAUFUSS: Rob Blaufuss, B-L-A-U-F-U-S-S.

4 JUDGE CLIFTON: Please raise your hand if you do not have a
5 copy of both these exhibits? Does anyone else need the
6 exhibits? All right. Mr. English, you may proceed.

7 DIRECT EXAMINATION

8 BY MR. ENGLISH:

9 Q. And I note, again, that Exhibit 147, on page 7, has an
10 end note that we don't ask to be put into the transcript as
11 being in the exhibit, and I ask Mr. Blaufuss -- although I do
12 think those of us who attend this should get some kind of
13 honorary Ph.D. in Economics -- but I ask Mr. Blaufuss to read
14 his statement, and I will ask that especially when you read
15 numbers, and there's going to be a lot of them, if you could
16 read slowly as you get to those. All right.

17 A. All right.

18 Class I Formula Revisions

19 Prior to providing my testimony regarding the
20 fortification of fluid milk products, I would first like to
21 make revisions to the Dairy Institute of California hearing
22 proposal. The revisions would make adjustments to the Class I
23 price calculations as found in Section 1051.50(a)(d).

24 JUDGE CLIFTON: All right. And just so everyone can hear
25 what you are saying, you are saying A like apple, D like dog?

1 MR. BLAUFUSS: That is correct.

2 JUDGE CLIFTON: Okay.

3 MR. BLAUFUSS:

4 (d)Class I Fluid Carrier Price=(Class I Skim Price*.24)/87.5

5 (a)Class I Price=(Butterfat Price per Pound*3.5) + (Class I SNF
6 Price per Pound*9) + (Class I Fluid Carrier Price per Pound
7 *87.5)

8 Fortification Credit Revision

9 Proponents of Proposal 2 will also revise the
10 fortification credit calculation currently found in
11 Section 1051.60(6) for both nonfat dry milk and condensed skim.
12 The revised fortification language will mirror current
13 California statutory language. The stabilization plan
14 language, as it is, as it relates to condensed skim, states the
15 following:

16 Each handler, using condensed market skim milk for
17 fortifying Class I products, may deduct for each
18 pound of milk solids nonfat in such condensed
19 market skim milk, a maximum charge of 9 and 87
20 hundredth cents (\$0.0987) cents per pound. This
21 deduction shall be allowed in calculating the
22 gross pool obligation of such handler pursuant to
23 the provisions of the Pooling Plan.

24 JUDGE CLIFTON: Now, a tiny thing, but you seem to have
25 here a quotation, and if you read "solids nonfat" rather than

1 "solids not fat", does it mean the same thing?

2 MR. BLAUFUSS: I would leave it as it's written because
3 that was pulled from the statutory language.

4 JUDGE CLIFTON: All right. And so would you just read the
5 first two lines of the quote again?

6 MR. BLAUFUSS: Each handler, using condensed market skim
7 milk for fortifying Class I products, may deduct for each pound
8 of milk solids not fat in such condensed market skim milk a
9 maximum charge.

10 JUDGE CLIFTON: Good. Thanks. You may proceed.

11 MR. BLAUFUSS:

12 Fortification of Fluid Milk in California

13 As a result of California's higher fluid milk standards
14 (as compared to Federal Standard of Identities), differences
15 exist in raw milk costing compared to the Federal Order system.
16 In the Federal Order system, per FDA, fluid milk standards have
17 have a minimum milk solids nonfat level of 8.7 percent
18 regardless of fat content. In California, the base fluid milk
19 standards are set at 8.7 percent milk solids nonfat -- I'm
20 sorry, correct that -- in California, the base fluid milk
21 standards are set at 8.7 percent MSNF for whole, 10 percent
22 MSNF for reduced fat milk, 11 percent MSNF for lowfat milk, and
23 9 percent MSNF for skim milk. The elevated level of skim
24 required for reduced fat and lowfat milks in California fluid
25 milks, necessitates that Class 1 processors in the state

1 fortify their milk, either with condensed skim or nonfat dry
2 milk.

3 Currently, in all Federal Orders, the Class I mover
4 price in any given month is set by just two factors, skim and
5 butterfat. In California, however, there are three factors
6 which are used to set Class 1 prices. These three factors are
7 butterfat, solids nonfat, and fluid carrier. The California
8 Class 1 price splits the skim value into two different value
9 streams, solids nonfat and fluid carrier. In order to ensure
10 equal raw product costing under CA fluid milk standards, a
11 three factor Class 1 price is necessary. The goals in setting
12 up a system of a three factor Class 1 pricing system is to make
13 plants indifferent as to who they receive their milk from and
14 to ensure the orderly movements of milk in the state. Those
15 plants which receive higher solids milk will pay a higher price
16 for milk coming into the plant compared to those plants with
17 lower solids milk. The low test milk comes at a lower cost to
18 those plants, allowing them to pay for a higher level of
19 fortification and not be uncompetitive with the plant receiving
20 high test milk.

21 At the onset of the initial discussion around the
22 possibility of California Federal Order hearing, I believe I
23 began analyzing what the impact would be to Class 1 milk
24 costing under a Federal Order system compared to current
25 pricing mechanisms.

1 JUDGE CLIFTON: Current what kind?

2 MR. BLAUFUSS: Current California pricing mechanisms. Of
3 particular interest was the impacts of fortification costing
4 differences between the Federal Order and California. The
5 process of calculating the cost to fortify milk in California
6 is fairly straightforward. The additional solids used to
7 fortify the fluid milk products are brought into the plant on a
8 Class 2 basis. In the handler report, however, there is an
9 adjustment made, be it an increase or decrease, to convert the
10 Class 2 skim cost of fortification into a -- into a Class 1
11 price. At the end of the day, all solids used to manufacture a
12 Class 1 fluid product in California --

13 JUDGE CLIFTON: Read that line again, just from the top of
14 page 3.

15 MR. BLAUFUSS: -- manufacture a Class 1 fluid milk product
16 in California are priced at the Class 1 price. For those
17 plants which use condensed skim, an .0987 cent per pound credit
18 is applied for each pound of solids used to fortify the fluid
19 milk product.

20 JUDGE CLIFTON: And let me just make sure I understand what
21 the dollar amount is. Looking at that dollar amount, it's what
22 again?

23 MR. BLAUFUSS: It would be 9.87 cents per pound.

24 JUDGE CLIFTON: Thank you.

25 MR. BLAUFUSS: The Federal Orders fortification costing is

1 handled noticeably different than current California costing.
2 Federal Orders bring in milk solids nonfat used in
3 fortification as a receipt into the plant and then allocates
4 the vast majority of the skim as Class IV utilization. USDA
5 then converts the receipts to a skim equivalent using set
6 factors. The difference between a receipt factor volume and
7 the utilization factor volume represents the volume increase in
8 Class I volume due to fortification. This increased Class I
9 volume is what is better known as displacement. The full list
10 of fortification factors can be found in Table 1 in
11 Exhibit 148.

12 JUDGE CLIFTON: And, Ms. Frisius, will you please insert
13 there 148 on page 3 in the blank?

14 MS. FRISIUS: Yes.

15 JUDGE CLIFTON: Thank you.

16 MR. BLAUFUSS: In consultation with Pacific Northwest
17 Federal Order staff, I developed out a time series model to
18 calculate the full per hundredweight Class I costs, factoring
19 in the costs associated with the USDA fortification
20 regulations. I will show the differences in per gallon cost
21 for two percent and one percent milks, as well as whole and
22 skim milks, for manufacturers with high (9.2 percent SNF), low
23 (8.8 percent SNF), and standard tests (actual California SNF
24 test levels) milk using both Dairy Institute's three
25 factor Class I price formula and the current Federal Order two

1 factor Class I price formula. Both analysis will use, both
2 analyses will use the Dairy Institute's proposed pricing
3 formulas and adjusted make allowances. I will illustrate just
4 how much of an impact not having a three factor Class I formula
5 has on a plant's ability to remain competitive in the market.

6 From a Dean Foods perspective, condensed skim is the
7 preferred method to fortify fluid milk products in California
8 to meet the fluid standards. In my analysis I will focus
9 solely on fortification costing using condensed skim. My
10 analysis used what is called Pearson's Square to arrive at a,
11 at the combination of market test skim milk and condensed skim
12 milk to reach the required MSNF level per the California fluid
13 milk standards for both 2 percent and one percent. Pearson's
14 square is a mathematical formula which calculates what pounds
15 of two different testing products (milk and condensed) are
16 needed to arrive at a specified number of pounds at a specific
17 skim test.

18 To calculate the skim equivalent of the fortifying
19 agent for a two factor pricing system, I multiplied the pounds
20 of condensed skim needed to fortify a hundredweight of milk
21 standardized to either two percent or one percent milk fat, by
22 their respective USDA fortification factors. My analysis
23 assumes a condensed skim solids nonfat percentage of 33.5
24 percent. This level of solids nonfat in the fortifying agent,
25 per USDA guidelines, equals a volume factor of .904 and a

1 Class IV fortification factor of 2.709. Multiplying the pounds
2 of condensed needed to fortify two percent and one percent milk
3 by their respective factors provides the skim equivalent pounds
4 which will then be used to calculate the cost of fortification.
5 Once the skim equivalent pounds of the fortifying agent are
6 known, I was then able to calculate the value of fortification.
7 There are two separate calculations made in the fortification
8 cost build up. The first step is to multiply the skim
9 equivalent pounds assigned to the volume factor by the per
10 pound Class I price, at a \$2.10 per hundredweight base
11 differential level. Next, the skim equivalent pounds allocated
12 to fortification is multiplied by the per pound Class IV skim
13 price.

14 The fortification and milk cost build up for milk at
15 test can be found in Table 3.

16 JUDGE CLIFTON: All right. So this is Table 3 of
17 Exhibit 148?

18 MR. BLAUFUSS: Correct.

19 JUDGE CLIFTON: All right. And I would like, Ms. Frisius,
20 for us to show that Table 3 of Exhibit 148 here in the last
21 paragraph of page 4.

22 MS. FRISIUS: Okay.

23 JUDGE CLIFTON: You may proceed.

24 MR. BLAUFUSS: Thank you. The same model discussed just
25 now was then used to calculate milk at fortification costs for

1 producer milk at 9.2 percent and 8.8 percent SNF levels to test
2 how differences in the MSNF content of producer milk impacts
3 raw product costing. Using the model just laid out for a two
4 factor Class I pricing system, I then calculated the milk cost
5 in California with a three factor Class I pricing system. The
6 only functional differences between the two factor and three
7 factor model is that the skim cost portion is broken into two
8 separate cost categories, solids nonfat and fluid carrier. The
9 three factor pricing calculation, for California milk at test,
10 can be found in table 4, of Exhibit 148.

11 JUDGE CLIFTON: All right. Ms. Frisius, would you enter
12 that on the record copies, on top of page 5?

13 MS. FRISIUS: Yes.

14 JUDGE CLIFTON: Table 4, Exhibit 148. Thank you. You may
15 proceed.

16 MR. BLAUFUSS: Using the Class 1 pricing formula as laid
17 out in the Dairy Institute hearing proposal and actual
18 commodity prices from 2010 through 2014, I calculated per
19 gallon cost for whole, reduced fat, low fat, and skim milks.
20 Also factored into the per cost build up, per gallon cost build
21 up, was the fortification and displacement cost to fortify
22 reduced fat and lowfat milks to meet the California fluid milk
23 standards. A shrink factor of one percent was assumed for all
24 fat categories. The final piece of the total per gallon cost
25 build up is the fortification credits. The total level of

1 fortification credits are estimated using the Dairy Institute's
2 proposal and are adjusted to reflect the solids nonfat content
3 of the milk coming into the plant. Dairy Institute language
4 would have provided the maximum allowed fortification credit
5 throughout 2010 through 2014 of 9.87 cents per pound of skim
6 solids. The level of fortification credit was corrected to
7 reflect a percentage of MSNF in producer milk, be it 8.8
8 percent, 8.9 percent, or 9.2 percent.

9 The per gallon cost differences of fluid milk products
10 show notable differences under a three factor Class I pricing
11 system compared to the two pricing, two factor pricing formula.

12 JUDGE CLIFTON: So let us make though changes, Ms. Frisius.
13 So we're on page 5, we're in the last full paragraph, second
14 line, and the first thing we do is strike the "a" just after
15 the word "the". Is that right, Mr. Blaufuss?

16 MR. BLAUFUSS: Actually, strike out the "the" leave the
17 "a".

18 JUDGE CLIFTON: Oh, all right. Strike the "the".

19 MR. BLAUFUSS: Yeah, I had to re-read the sentence to see
20 what fit better.

21 JUDGE CLIFTON: Okay. And then we call it "two factors",
22 so we insert "factor" between "to" and "pricing".

23 MR. BLAUFUSS: That is correct.

24 JUDGE CLIFTON: Would you read that sentence again, please.

25 MR. BLAUFUSS: The per gallon cost differences of fluid

1 milk products show notable differences under a three factor
2 Class I pricing system, compared to a two factor pricing
3 formula.

4 The key difference is that while prices for reduced fat
5 and low fat milks are higher under a three factor formula than
6 they would be under a two factor formula, the price gap between
7 high test milk and low test milk is much flatter. As Table 2
8 of Exhibit 148 shows, a three factor Class I pricing formula
9 levels the competitive playing field by significantly reducing
10 the per gallon price gap between a plant taking in high solids
11 milk and a plant which takes in low solids milk.

12 JUDGE CLIFTON: And Ms. Frisius, will you fill in the blank
13 in that last full paragraph on page 5 to show Table 2 of
14 Exhibit 148? Thank you. You may proceed, Mr. Blaufuss.

15 MR. BLAUFUSS: Thank you.

16 Under a two factor price formula, the 2010 through 2014
17 per gallon cost of reduced fat milk at a high test skim
18 averaged \$1.6171 cents per gallon, while the low test skim
19 averaged 1.65, \$1.6565, a difference of .0394 per gallon. That
20 price difference --

21 JUDGE CLIFTON: All right. So let's -- let's just make
22 sure it is clear what dollar amounts we're talking about. So
23 the first number, okay. So the way I would like you to read
24 it, if you would, is, for example, 161. or, no, you can't read
25 it that way. What is the best way to read this so that it is

1 right in the transcript? I'll ask you to read it this way,
2 Mr. Blaufuss, just read, \$1.6171, if you will, just so it's
3 clear. And read the sentence from the beginning.

4 MR. BLAUFUSS: Okay.

5 Under a two factor price formula, the 2010 through 2014
6 per gallon cost of reduced fat milk at a high test skim
7 averaged \$1.6171, while the low test skim averaged \$1.6565, a
8 difference of 3.94 cents per gallon. That price difference
9 averaged 3.82 cents per gallon for lowfat milk, over that same
10 period. In comparison, the 2010 through 2014 reduced fat per
11 gallon cost with high test skim milk under a three factor
12 formula, averaged \$1.6815, while the low test skim milk per
13 gallon price averaged \$1.6810, a difference of only \$0.0005 per
14 gallon. Lowfat per gallon cost for high and low test skim
15 solids milk under a three factor pricing formula averaged
16 \$1.6234 and \$1.6228, respectively, a difference of only \$0.0006
17 per gallon.

18 Given the nature of the California fluid milk market,
19 the 3.94 and 3.82 cents per gallon price advantage enjoyed by
20 plants taking in milk with high nonfat solids, would represent
21 a significant competitive price advantage over those plants
22 which are taking in low nonfat solids milk. This per gallon
23 price gap would give an incentive to fluid milk processors to
24 procure milk from those farms which have a higher level of milk
25 solids, while at the same time jettisoning those farms that are

1 producing milk with lower solids levels

2 JUDGE CLIFTON: All right. We'll just insert the word
3 "time" as you read it, we're on page 6, about the middle of the
4 page, the first full paragraph, fifth line down. We're
5 inserting the word "time" after the word "same" and before the
6 word "jettisoning".

7 MR. BLAUFUSS: Shifting from using milk from Holstein herds
8 Jersey herds could potentially lead to disorderly marketing for
9 no other reason than to take advantage of the two factor
10 Class I pricing regulations. As my calculation shows, the
11 competitive advantage enjoyed by a plant taking in high nonfat
12 solids milk is significantly reduced in a Class I pricing
13 system, which splits the skim pricing into two separate
14 components, nonfat solids and fluid carrier. It is also
15 important to note that a three factor Class I pricing formula
16 would represent the status quo for Class 1 in California.
17 Those involved in the fluid milk industry in the state have a
18 strong understanding and comfort level in a pricing formula
19 which splits the value of skim into two separate components,
20 solids nonfat and fluid carrier. The three factor Class I
21 pricing formula, per my analysis, would actually lead to higher
22 per gallon cost for whole, reduced fat, low fat, and skim
23 milks. Despite this, Dean feels that a three factor pricing
24 formula is necessary in order to ensure orderly conditions in
25 the California Class 1 market.

1 BY MR. ENGLISH:

2 Q. Chip English. I have about four or five minutes to
3 start and I was trying to figure out what might make the most
4 sense, and I might jump ahead and then come back, well,
5 tomorrow or Wednesday, or whenever we do this. So if I can
6 just try to tie things together today. If you could look first
7 at the bottom of page 5 of your testimony, Mr. Blaufuss, and
8 also have your exhibit handy.

9 When you say "under a two factor price formula for 2010
10 to 2014 for gallon cost reduced fat milk at a high test skim,"
11 you say averaged 1.6171; is that correct?

12 A. Correct.

13 Q. If you look at Exhibit 148, Table 2, page 2, which IS
14 headed Per Gallon Cost Sheet for High SNF, Actual SNF, and Low
15 SNF Milk, where would we find the 1.6171 for the two factor
16 2010, 2014 average for high test skim?

17 A. It would be in the upper left for high test. So 9.2
18 percent is high test, the actual is just actual test, and the
19 8.8 is considered to be low solids.

20 Q. So let's just look at Table 2. You have got six little
21 tables there, correct, in Table 2?

22 A. That's correct.

23 Q. So upper left corner, would that be the two factor
24 analysis for high test?

25 A. That's correct.

1 Q. And the right hand side in the upper is the three
2 factor analysis for high test; is that correct?

3 A. That's correct.

4 Q. And then the actual is the middle and the two factors
5 on the left; is that correct?

6 A. That is correct.

7 Q. And on the right you have got the three factor for the
8 actual SNF, correct?

9 A. That's correct.

10 Q. And so finally on that page, you have got the, on the
11 left hand column, the lower side, the two factor for 8.8 SNF,
12 so low SNF, correct?

13 A. Correct.

14 Q. And then the final is the three factor on the right; is
15 that correct?

16 A. That's correct.

17 Q. So going through, I'm not sure, maybe that's the only
18 one. So that's how Table 2 works. And a lot of the other data
19 is the build up to Table 2; is that correct?

20 A. Correct. So I thought about being a jerk and putting
21 the cliff notes at the back to make sure everybody had to look
22 through the analysis, but like the friendly professor that I am
23 today, I made sure to put them up front for those who did not
24 want to do all that reading.

25 Q. Okay. So continuing back to page 5, you have

1 referenced the low test milk averaged 1.6565, and where do we
2 find that on Table 2, page 2?

3 A. It would be the third column on the bottom.

4 Q. And the lower --

5 A. Third column from the left.

6 Q. And it is the left hand side for two factor, correct?

7 A. Correct.

8 Q. Because on this chart, everything on the left is two
9 factor, everything on the right is three factor, correct?

10 A. That is correct.

11 Q. All right. So trying to use my time very wisely,
12 turning to page 6, when you reference the three factor for high
13 test milk for 2010, 2014 is \$1.6815, where do we find that?

14 A. That would be in the upper right table, the third
15 column from the left.

16 Q. Okay. And in the next line you said for low test is
17 \$1.6810, and we drop down to the bottom table, right hand side,
18 third column, correct?

19 A. Correct.

20 Q. Okay. And just to complete the picture on page 6 for
21 the day, you could do the same thing you have for the high test
22 three factor pricing for lowfat milk, you would find the
23 \$1.6234 in the column immediately right of \$1.6815, correct?

24 A. Correct.

25 Q. And so similarly, you would find the \$1.6228 down at

1 the bottom right, correct?

2 A. Correct.

3 Q. Okay. I think I went as fast as I can to try to move,
4 now, tomorrow, or whatever day we put you back up, we're going
5 to undo the cliff notes and go figure out how you got there,
6 correct?

7 A. I believe we will be doing that.

8 JUDGE CLIFTON: I'm going to start calling him
9 Dr. Blaufuss.

10 MR. ENGLISH: So, your Honor, I would then propose we stop
11 there for now. I think we have wisely used 30, 35 minutes of
12 time to move forward.

13 JUDGE CLIFTON: Yes, I appreciate very much that you have
14 given us all that data so that everyone can analyze it.

15 MR. ENGLISH: And I want everybody to do their homework
16 tonight, because I'm working tonight.

17 Let me just preview. I will try to spend five minutes
18 or so talking to Ms. Hancock. I remain a little concerned
19 about four dairy farmers coming on Wednesday, but I don't know
20 how extensive the cross-examination of Mr. Blaufuss might be,
21 and I think the analysis is what it is, but I don't know. I'm
22 a little -- I'm getting a not sure. So I just don't know what
23 to do. So I'll try to have a conversation with Ms. Hancock and
24 we'll try to reach some resolution tonight or tomorrow morning.
25 I'm -- I think Ms. Taylor's testimony that's left, the

1 statement will be shorter and the tables will be complex.

2 JUDGE CLIFTON: What is she talking about?

3 MR. ENGLISH: This is her part, this is the impact on
4 pricing of the California, the Dairy Institute of California
5 proposal. It is very unimportant, very short. I think
6 Mr. Beshore will stipulate that he will have like five minutes
7 of questions -- so I will do what I can, but I just have to get
8 these witnesses done Wednesday afternoon no matter what.

9 JUDGE CLIFTON: Understood. We'll get 'er done. You know,
10 we don't want to go without lunch, but we could.

11 MR. ENGLISH: As long as that's just before
12 cross-examination.

13 JUDGE CLIFTON: Somebody's suggesting we order in pizza.
14 All right. So there's a lot of interest in what Ms. Hancock is
15 going to show Mr. English as in who else the exhibit? So the
16 question is who else gets to preview it?

17 MS. HANCOCK: Ms. Hancock. So we have agreed to share
18 Mr. Gonsalves' testimony just so they have an idea, with the
19 hopes that we can get him on in the morning and off. And I
20 think what Chip had thought was that if we can, if it was short
21 enough, that he thought we could get him on and off, we
22 wouldn't have a lot of the stuff, then we would maybe do that.
23 Otherwise, we're going to have to punt him later.

24 But I just found some errors that we need to correct,
25 and so I think -- and he doesn't know this, but what I'm going

1 to propose is that we just e-mail it to him as soon as we are
2 done. We said we would give it to Marvin as well, if you guys
3 want it, you can have it, too. And then we'll hand out the
4 exhibits tomorrow, because those are not scanned in the way
5 that we could share it.

6 JUDGE CLIFTON: Is it easy for you, Ms. Hancock, to send
7 your e-mail to Mr. English, Mr. Beshore, Mr. Vlahos, and
8 Laurel May?

9 MS. HANCOCK: Yes.

10 JUDGE CLIFTON: Okay. Let's do that. Laurel May can
11 decide whether to distribute it to USDA personnel or not.

12 MS. HANCOCK: I don't know if I have John Vlahos and
13 Kristine, I already asked Kristine and she told me she didn't
14 care.

15 JUDGE CLIFTON: But thank you, yes. Kristine Reed, if she
16 wants it. And Mr. Vandenheuvel, do you want it as well? Yes.
17 So would you get Mr. Vandenheuvel's e-mail, Ms. Hancock? Right
18 behind you.

19 MS. HANCOCK: I got him.

20 JUDGE CLIFTON: Good. Thank you so much. That will help a
21 lot.

22 MS. HANCOCK: And I don't know how this fits in. After
23 Mr. -- Mr. Gonsalves, and then after Chip is done, our next
24 witnesses are going to be Mr. Shehadey, Mr. Otis, Ted DeGroot,
25 and a Federal Order specialist. I will note that, you know,

1 our, three of those are producers as well, and I don't know if
2 they get the same privilege to try and get them on and off the
3 stand, but they have some scheduling issues, too, that we're
4 trying to get through. So I think if we can get them through
5 by the end of the week, we'll be all right. And then Ponderosa
6 goes after that. Right now we have two witnesses for
7 Ponderosa.

8 I think Ponderosa, we might have to do one of them on
9 Friday because he's not available on Thursday, so as long as we
10 can get them, I mean, we might have to move that around, but I
11 think definitely by Friday. Only one of the producer-handlers
12 is going to have any meat, any bulk to their testimony. The
13 others are going to be fairly succinct. So, I mean, I think
14 once we get through the first one, it's going to go pretty
15 fast.

16 JUDGE CLIFTON: Ms. Hancock, what was the person you named
17 after Mr. Otis?

18 MS. HANCOCK: Ted D-E, G-R-O-O-T, from Rockview.

19 JUDGE CLIFTON: From Rockview?

20 MS. HANCOCK: Yes.

21 JUDGE CLIFTON: Thank you. All right. Does anyone else
22 have questions for Ms. Hancock about what her line up is? No.

23 Ms. Hancock, thank you so much for the courtesy of the
24 e-mailing of the exhibit, that's very helpful. Mr. English?

25 MR. ENGLISH: As I say, we'll do the best we can. My life

1 is not particularly well ordered, which is why I'm working
2 constantly all weekend. I have a client who is literally
3 flying in tonight to have dinner with me on an unrelated
4 subject, insisting that I actually spend a little time on
5 something else. So that means I'm not going to be reading this
6 until tomorrow morning.

7 JUDGE CLIFTON: Ms. May?

8 MS. MAY: I just wanted to mention that there are two other
9 producer witnesses coming in this week, one will be here and
10 only available Thursday afternoon, and the other will be here
11 Thursday but will also be available Friday. And those are both
12 witnesses that Mr. Dan Smith is bringing out here. So we have
13 agreed to allow to get them on the schedule, too. But
14 Mr. Smith says they will probably both only take about half
15 hour each.

16 JUDGE CLIFTON: Very good. Thank you. Ms. May, do we, can
17 we leave anything in this room?

18 MS. MAY: I believe we can.

19 JUDGE CLIFTON: So sound system can stay in place. If we
20 want to leave our exhibits, we can leave them. Thank you so
21 much. All right. A good day, truly a good day. We're off
22 record now at 5:01.

23 (Whereupon, the evening recess was taken.)

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