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USDA - FEDERAL MILK ORDER HEARING

Sheraton Hotel Station Square
300 West Station Square Drive
Pittsburgh, PA 15219

Wednesday, June 22, 2005
8:00 a.m.

BEFORE: PETER M. DAVENPORT
U. S. ADMINISTRATIVE JUDGE

TRANSCRIPT OF PROCEEDINGS

VOLUME III

Reported by:

Cheri A. Redlinger
Professional Court
Reporter

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HP Hood and Chelsea Mass.:	Lois Jewell & Associates, P.C. by John H. Vetne, Esq.
National Yogurt Association:	Coolley Godward, LLP by Aaron F. Olsen, Esq.

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ROBERT ANDERSON
JEFF SHAPIRO

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P R O C E E D I N G S

JUDGE DAVENPORT: I'm going to call the meeting to order. This is day three of the National Federal Milk Order hearing on the definition of milk. We have a number of witnesses that are scheduled to testify today. At this time what I would like to do is just briefly recap who they there and then if there are some additions, you can let me know.

I have the witness from General Mills and his research people. I have Mr. Tipton. I have Mr. Bunting. I have Ms. Taylor. I have Mike Suever from Hood. I understand that Hormel is not going to be here so I will tentatively mark them off.

Mr. Beshore, I understand there is a possibility that you may want to put Mr. Hollon back on for clarification.

MR. BESHORE: Yes.

JUDGE DAVENPORT: Very well. Then Mr. Yonkers, I understand that you're going to have a presentation. Is there anyone else in the audience at this time that

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anticipates needing some time either today or at some later time? Excuse me. I left off Mr. Wilson, and Mr. Wilson did want to go last. Are there any other people that I did not touch upon? Very well. Ms. Grocholski, if you want to come forward at this time or you and your witnesses.

(At this juncture, the witnesses were collectively sworn in.)

JUDGE DAVENPORT: Would you identify yourselves for the record, please?

MR. WALDRON: Robert F. Waldron, General Mills.

MR. ANDERSON: Robert M. Anderson, General Mills.

MR. SHAPIRO: Jeff Shapiro, S-H-A-P-I-R-O, General Mills.

(Exhibit No. 26 was marked for identification.)

JUDGE DAVENPORT: Gentlemen, why don't you be seated. I have a statement which has been marked as Exhibit No. 26. Are you prepared to enter that into the record at this time?

1 R. Waldron - Direct Testimony

2 MR. WALDRON: Yes, Your Honor.

3 JUDGE DAVENPORT: Very well.

4 You may proceed to give your statement.

5 -----

6 ROBERT WALDRON

7 a witness herein, having been first duly sworn,
8 testified as follows:

9 DIRECT TESTIMONY

10 MR. WALDRON: On behalf of
11 General Mills and Yoplait, I would like to
12 thank the U.S. Department of Agriculture and
13 the Agricultural Marketing Service for this
14 opportunity. My name is Bob Waldron. I am
15 president of Yoplait which is a division of
16 General Mills and the leading brand yogurt in
17 the country.

18 I am joined today by Bob Anderson,
19 Yoplait's director of consumer insights, Jeff
20 Shapiro from our government affairs office and
21 Deb Grocholski, Yoplait's legal counsel.
22 Headquartered in Minneapolis, Minnesota,
23 General Mills is the world's sixth largest food
24 company with more than 12 billion dollars in
25 annual sales and more than 28,000 employees

1 R. Waldron - Direct Testimony

2 worldwide. We market consumer food products in
3 more than 100 countries, and we generally have
4 the number one or number two brand in every
5 category in which we compete.

6 We know how to develop and market
7 our products to meet the needs of our consumers
8 so when we talk about consumers view or use of
9 our products, you can trust that we know what
10 we are talking about. We are the Big G Company
11 and Pillsbury. We are Betty Crocker and Green
12 Giant. We are a leader in branded organic
13 products and, of course, we are also Yoplait
14 yogurt which brings us here today.

15 General Mills began selling Yoplait
16 in America in 1977. I would have you refer to
17 the chart to my left. Over the years, Yoplait
18 has expanded from its original line of flavors
19 to Light, Whips, Thick & Creamy and more
20 recently Healthy Heart.

21 We have also expanded the brand to
22 attract younger consumers in providing the
23 health benefits of yogurt to a new generation
24 with products such as GoGurt--yogurt in a tube
25 form, Trix yogurt and Yumsters.

1 R. Waldron - Direct Testimony

2 As Yoplait's product offerings have
3 expanded, so too have our purchases of dairy
4 ingredients. As a company, General Mills is
5 one of the largest purchasers of dairy products
6 in the U.S., and we are proud of that. We are
7 partners with dairy producers in the same value
8 chain, and we want and need to have a healthy
9 U.S. dairy industry.

10 My primary purpose here today is to
11 support a proposal that we believe will
12 continue the win-win relationship between dairy
13 producers and manufacturers of dairy-containing
14 products. Yoplait products are offered in
15 dozens of flavors and available in every U.S.
16 market. Yoplait consumers have come to rely on
17 us to provide great tasting yogurt products.

18 The main line of Yoplait products is
19 six-ounce cups that consumers often eat away
20 from home. We saw an opportunity to provide
21 the Yoplait consumer an even more convenient
22 yogurt product.

23 As a result, we introduced our
24 Nouriche yogurt smoothie. Sold in 11-ounce
25 bottles, Nouriche provides more than 20 percent

1 R. Waldron - Direct Testimony

2 of the daily recommended intake of
3 carbohydrates, protein and more than 15 other
4 vitamins and nutrients including folic acid and
5 vitamins A, C, D and E. Nouriche packs 260
6 calories and is marketed as a yogurt smoothie
7 with superior nutrition. To compare, Nouriche
8 has more than twice the calories of an
9 equivalent amount of nonfat milk and 25 percent
10 more calories than the equivalent amount of
11 whole milk.

12 Like all of our yogurt smoothie
13 products, Nouriche is shelved in the yogurt
14 section of the dairy case and is commonly
15 consumed in place of our other
16 yogurt-containing products.

17 The chart to my left shows the
18 yogurt section in a common U.S. retail store.
19 It shows that Nouriche is shelved with cup
20 yogurts. In short, consumers are under no
21 impression either in the grocery store or by
22 our marketing that Nouriche is anything other
23 than another form of yogurt.

24 Today we will provide evidence
25 demonstrating that our yogurt smoothies

1 R. Waldron - Direct Testimony

2 including Nouriche, GoGurt Smoothie and Yoplait
3 Smoothie are not a substitute for or in
4 competition with fluid milk.

5 Rather, these products are marketed
6 by Yoplait as yogurt products and are, in fact,
7 used by consumers as they would use a food
8 product. Accordingly, these food products
9 belong in Class II with other yogurt products
10 rather than in Class I fluid milk.

11 As has been reviewed in earlier
12 testimony, the Agricultural Marketing Agreement
13 Act requires that milk be classified according
14 to its form and use.

15 With respect to both form and use,
16 Yoplait's yogurt smoothies are fundamentally
17 different than fluid milk. They don't have the
18 same form as fluid milk and consumers use them
19 for very different purposes than fluid milk.

20 Over the past two years, Yoplait has
21 made several presentations to the Department
22 outlining the form and use of Nouriche. We are
23 pleased to present the same data here despite
24 the lack of any evidence that suggests yogurt
25 smoothies compete with fluid milk.

1 R. Waldron - Direct Testimony

2 The data we have already provided
3 demonstrates that yogurt smoothies while made
4 from dairy components do not compete with fluid
5 milk. Mere assertions to the contrary will not
6 change the facts.

7 An objective assessment of the
8 marketing and consumption of these products
9 makes clear that these are food products that
10 are marketed, sold and used by such consumers
11 and are in competition with other food
12 products, not fluid milk.

13 The fundamental reality is that
14 consumers' preferences are changing to more
15 convenient and portable food products that fit
16 in better with today's ever more active and
17 hectic lifestyles.

18 Just two weeks ago, the Wall Street
19 Journal ran an article that focused on this
20 trend profiling the proliferation of on-the-go
21 stain removers because so many Americans today
22 eat in the car. A Yoplait portable product was
23 specifically referenced not because it's messy
24 to eat, of course, but rather because of its
25 convenience and portability.

1 R. Waldron - Direct Testimony

2 Successful products in today's
3 marketplace are reflective of and often
4 responsive to changing consumer needs. What
5 yogurt makers have done is give the consumer a
6 more eat-in-the-car-friendly form of yogurt
7 and, in my view, petitioners should be
8 embracing the development and success of these
9 new products.

10 Continued and expanded use of dairy
11 ingredients provides increased revenue for
12 dairy farmers. As I will discuss later,
13 increasing the costs of these ingredients will
14 make it harder for food companies to innovate
15 and create new dairy-containing products.

16 It will also make it more likely
17 that companies will take advantage of recent
18 and upcoming technological innovations and use
19 non-dairy ingredients that provide comparable
20 functionality and nutrition. Either outcome is
21 far more likely than expecting a manufacturer
22 to simply assume the increased ingredient costs
23 and either outcome will most certainly decrease
24 farmer income.

25 Given that both dairy producers and

1 R. Waldron - Direct Testimony

2 General Mills are in the same value chain, we
3 all suffer if we turn consumers away from dairy
4 and dairy-containing products.

5 I want to briefly walk you through
6 now how a company like General Mills researches
7 a new product like our yogurt smoothies as well
8 as tests consumer interest.

9 In 2003, our team of researchers ran
10 a comprehensive study to capture consumer
11 attitudes about a wide variety of portable
12 products. We tested 30,000 adults ages 18 to
13 70 years old over a period of one workweek.
14 The goal of such testing discovered not only
15 what consumer interest is but also to identify
16 where there may be opportunities that have not
17 yet been captured.

18 We showed 67 products individually
19 to different groups of consumers. These
20 products included both products already
21 available and some that were at that time only
22 concepts under consideration. Consumers were
23 asked both their intent to purchase and how
24 often they would buy the product.

25 We also collected their perceptions

1 R. Waldron - Direct Testimony
2 of the product on a wide variety of attributes
3 covering taste, satiety, nutrition and
4 convenience among many other areas.

5 We learned from this study that a
6 portable yogurt product that is calorie dense,
7 high in vitamins and nutrients yet similar
8 enough to other products to which the consumer
9 is already loyal would be a viable product.

10 We also learned that consumers view
11 these yogurt smoothies as competitors to
12 nutritious snacks like Power Bars and tubed
13 yogurt and secondarily to cup yogurt products.
14 Fluid milk, in contrast, has very different
15 perceptions and expected use.

16 In providing this new product, we
17 recognize that we have essentially created
18 competition for some of our own products, but
19 this is what consumers are saying they want and
20 if we don't make it, we know others will.

21 We know that when we discover a
22 consumer trend, that people want filling,
23 nutritious portable food products. Consumers
24 loyal to Yoplait expect us to provide a product
25 to meet their demand. If we don't, we risk

1 R. Waldron - Direct Testimony

2 losing consumers to a competitor.

3 Nouriche satisfies the need for
4 on-the-go nutritious food. When we tested
5 consumers for awareness, attitude and usage of
6 the product and asked "Would you consider
7 Nouriche to be an acceptable meal replacement?"
8 63 percent said yes.

9 Not surprisingly, consumer surveys
10 also indicate Nouriche is competing against
11 other food products and is not competing
12 against fluid milk or other beverages.

13 In fact, verbatim analysis shows
14 that instead of Nouriche, consumers would
15 eat -- and this list is in order -- cereal, cup
16 yogurt, fruit, a sandwich, dessert, chips,
17 pretzels, Slim-Fast, a hamburger, a bagel,
18 candy, orange juice, soda, a granola bar, fast
19 food, ice cream, cookies and pizza all before
20 they would reach for a glass of milk. In fact,
21 less than one percent of those tested even
22 mentioned milk as a possible substitute.

23 In recent weeks, Yoplait has
24 introduced two new yogurt smoothie products:
25 GoGurt Smoothie, a five-ounce product for

1 R. Waldron - Direct Testimony

2 children sold in a four-pack and Yoplait
3 Smoothie, an eight-ounce snack size product for
4 adults.

5 While our experience with these
6 products is young, there is some data I would
7 like to share with you as further evidence that
8 our smoothies are viewed by the American
9 consumer as food products, not fluid milk.

10 When was the last time you saw a
11 consumer reach for a gallon of milk and the
12 first thing they did was look at the nutrition
13 panel? My guess would be nearly never, yet six
14 out of ten consumers selecting Yoplait
15 Smoothies turned to the nutrition panel first
16 akin to what consumers do before they purchase
17 a box of cereal, package of granola bars or
18 even a TV dinner.

19 Similar to our experience with
20 Nouriche, these products are not turning milk
21 drinkers into yogurt eaters; instead nearly 80
22 percent of Yoplait smoothie's consumers would
23 buy another yogurt product as an alternative.
24 In fact, 68 percent of consumers eat our yogurt
25 smoothies for breakfast and 32 percent of

1 R. Waldron - Direct Testimony

2 adults tested said they would have a Yoplait
3 smoothie in place of dessert.

4 If consumption of anything slows in
5 markets where new yogurt smoothie products are
6 introduced, it would be spoonable cup yogurt.
7 I would have you refer to the chart to my left,
8 your right.

9 As you can see from this chart, the
10 annual compound growth rate of cup yogurt has
11 slowed considerably since yogurt smoothies were
12 introduced. Clearly these yogurt smoothies
13 products are competing with other food products
14 such as yogurt and not competing with fluid
15 milk.

16 These findings are consistent with
17 consumer consumption data which demonstrate
18 that milk is viewed primarily as a component to
19 a meal while yogurt-containing products such as
20 one of our yogurt smoothies are seen as a snack
21 or a meal.

22 I want to show you two charts based
23 on NPD Group's National Eating Trends study, a
24 widely recognized and respected industry
25 standard, both of which show stark differences

1 R. Waldron - Direct Testimony

2 between how consumers use yogurt, yogurt
3 smoothies and fluid milk.

4 In this first chart, this first set
5 of data was derived from asking consumers how
6 they classify the foods they eat into four
7 choices with one being a base dish, something
8 eaten on its own; two, an additive; three, an
9 ingredient; four, a cooking aid.

10 As you see, yogurt smoothies are
11 eaten almost exclusively on their own.
12 Consumers use them as a base dish nearly 96
13 percent of the time. In contrast, consumers
14 use milk as an additive or ingredient over 54
15 percent of the time and milk is consumed on its
16 own less than half the time.

17 In this next chart, the second set
18 of data is derived from evaluating the eating
19 occasion in which consumers are using certain
20 foods or beverages. The most telling fact here
21 is how rarely fluid milk is seen as a snack
22 while yogurt smoothies are commonly enjoyed as
23 a snack.

24 Consumers are more likely to drink
25 milk with meals, particularly breakfast or

1 R. Waldron - Direct Testimony

2 dinner and are much more likely to consume
3 products like Nouriche as a snack.

4 Of course, I'm sure that some people
5 might try to argue that yogurt smoothies are
6 competing with fluid milk because they compete
7 with cereal and that's where consumers use a
8 lot of fluid milk.

9 The fact of the matter is our market
10 research demonstrates that the breakfast market
11 can be divided into eight subgroups of products
12 based on consumer perceptions and use. Within
13 these groups, yogurt smoothies are in the same
14 group as cup yogurt, and there are no cereal
15 options in that group.

16 Within this group, yogurt smoothies
17 compete most closely with granola and cereal
18 bars, other portable options. To state the
19 obvious, General Mills also markets cereal as
20 well as granola and cereal bars, and we know
21 what we are talking about when we talk about
22 these markets.

23 As I stated previously, our yogurt
24 smoothie products are shelved with other yogurt
25 products, not fluid milk. In at least 95

1 R. Waldron - Direct Testimony

2 percent of all stores that carry our yogurt
3 smoothie products, they are placed in the
4 yogurt case and 72 percent of the time, they
5 are placed directly with other Yoplait-branded
6 products. Fundamentally, smoothies are a food
7 product. They are not beverages that compete
8 with fluid milk.

9 Yoplait yogurt smoothie products are
10 manufactured in and shipped from three
11 manufacturing facilities in the United States
12 and distributed nationally. Part of the reason
13 that they can be shipped so far is due to a
14 shelf life that greatly exceeds the shelf life
15 of fluid milk.

16 In fact, factors determining
17 shelf-life for yogurt smoothies vary greatly
18 from those that affect the shelf-life of fluid
19 milk. If all of these differences are not
20 enough, I will refer you to an additional
21 chart. This is "Trends in Milk Consumption
22 Versus Yogurt Smoothies."

23 While it is clear that milk
24 consumption began its decline well-before
25 yogurt smoothies hit the market, it is hard to

1 R. Waldron - Direct Testimony

2 imagine how a relatively tiny volume of yogurt
3 smoothies sold each year could ever have a
4 meaningful impact on the fluid milk business.

5 As we have demonstrated, our yogurt
6 smoothies do not compete with fluid milk. In
7 both form and use, they are products and should
8 be classified as such.

9 If you don't believe us, believe our
10 consumers, one of whom sums it up quite nicely
11 in a recent consumer focus group -- and I
12 quote -- "Perfect for a quick meal on the run
13 or a good snack for a growing teenager."

14 I would like to now take a moment to
15 review the proposal offered by General Mills
16 with respect to this hearing. Food and dairy
17 product manufacturers have been utilizing
18 current standards as a guide for developing new
19 food products for decades.

20 While we believe there is clear,
21 irrefutable evidence that our yogurt smoothies
22 would be Class II, we also recognize that
23 modifying the current classification scheme
24 raises a host of issues and questions for the
25 entire industry. Thus, we would support

1 R. Waldron - Direct Testimony

2 maintaining the status quo and leaving the
3 existing classification system in place.

4 If USDA believes that it's necessary
5 to change the current system, it should act to
6 classify yogurt smoothie products as Class II.
7 In our proposal to USDA, we advocate that if
8 the department proceeds to convert to a protein
9 standard, the department should exclude from
10 the fluid milk product definition any product
11 with less than or equal to 2.2 percent skim
12 milk and at least 20 percent yogurt by weight.

13 By requiring that products meet both
14 a protein and percentage yogurt requirement,
15 our proposal represents a modest additional
16 restriction to the current regulation. This
17 percentage yogurt requirement should address
18 producers' concerns that Class II products are
19 in direct competition with fluid milk.

20 In the calculation of the 2.2
21 percent standard, I want to make clear that our
22 proposal does not include milk protein obtained
23 from added concentrated or dried whey including
24 whey protein concentrate or WPC and here is
25 why. When considering a protein source, it is

1 R. Waldron - Direct Testimony

2 relevant to consider the other nutrients also
3 supplied with the ingredient under
4 consideration. I refer you to the chart again
5 to my left.

6 For simplicity, the example in this
7 chart is based upon 100 grams of protein via
8 nonfat dry milk and a commonly used variety of
9 WPC. I won't read the entire chart, but note
10 the substantial difference in calcium, for
11 instance. Nonfat dry milk provides ten times
12 the calcium than is found in WPC.

13 Though the quality of the actual
14 protein from nonfat milk and whey protein
15 concentrate is similar on the basis of protein
16 efficiency ratios, it is clear that when one
17 sources protein from WPC rather than nonfat dry
18 milk, additional fortification would be needed
19 to match the complete nutrient profile. The
20 value of WPC just isn't the same and pricing it
21 like nonfat dry milk is not going to sell more
22 dairy.

23 Food manufacturers will look for
24 other sources of protein. Yoplait, for
25 example, principally uses added whey as a

1 R. Waldron - Direct Testimony

2 protein source. As such, whey is an efficient
3 but replaceable ingredient, and we are not
4 alone in this regard.

5 If USDA includes added whey in any
6 protein classification, the USDA should set the
7 milk protein standard consistent with the
8 current standards of identity for fluid milk in
9 order to create some rational, objective
10 relationship between the standards and the
11 nutrient profile of the products.

12 While the standard of identity for
13 milk does not contain any protein requirement,
14 the requirement that milk contain 8.25 percent
15 milk solids converts roughly to 2.84 percent
16 milk protein.

17 As such, if AMS is inclined to adopt
18 a milk protein standard that includes all dairy
19 protein in determining product classification
20 including added whey, we would advocate the
21 2.84 milk protein standard so that dairy
22 products containing less than 2.84 protein and
23 containing 20 percent yogurt would be a Class
24 II product.

25 Converting to a 2.2 percent protein

1 R. Waldron - Direct Testimony

2 standard or (2.25 percent protein standard as
3 National Milk Producers Federation has
4 proposed) and including whey in the calculation
5 of protein is not a simple conversion of the
6 current 6.5 percent nonfat milk solids, as the
7 current standard does not include whey.

8 If the Department is inclined to
9 include whey in such a calculation,
10 establishing it based upon the objective
11 standard of identity for fluid milk would
12 preserve the spirit of the current standard,
13 especially since doing so would not create an
14 inherent disincentive to use whey as a protein
15 source.

16 Furthermore, by using the standards
17 of identity for fluid milk as a benchmark from
18 which to establish a protein standard, USDA can
19 guarantee further that refinement of the
20 classification standards will be done in a
21 manner reflective of modern formulation and
22 technological advances all while ensuring that
23 fluid milk and fluid milk products remain in
24 Class I.

25 If the standards of identity of milk

1 R. Waldron - Direct Testimony

2 were to change as dairy producers have
3 advocated and as AMS has studied for quite some
4 time, the milk protein standard would move as
5 well.

6 Finally, we request USDA allow for
7 normal process variances that may occur during
8 the manufacturing process. While neither
9 appreciable to the consumer nor meaningful in
10 the product's application, it is our hope that
11 if AMS adopts any protein standard, it do so
12 with the understanding that insignificant
13 variation may occur and that such variance
14 should not be cause for reclassification.

15 Both USDA and FDA recognize this
16 fact in regulations pertaining to nutrition
17 labeling and both provide for a 20-percent
18 variance. We believe this approach should also
19 be utilized by AMS if it determines a protein
20 standard is the appropriate method of
21 classification.

22 As I noted, if USDA were to include
23 added whey in the calculation of a milk protein
24 standard, it will directly lead to increased
25 utilization of alternative proteins.

1 R. Waldron - Direct Testimony

2 Companies will look for ways to
3 reformulate in order to reduce or even
4 eliminate the use of milk and dairy proteins in
5 their products. Market innovation will
6 continue and new products will be developed
7 that do not use milk or milk proteins.

8 The end result could be that dairy
9 prices will drop and dairy producer income will
10 decline. Instead of benefitting from a
11 proliferation of new products that utilize
12 dairy ingredients, dairy producers could
13 undercut their own market by creating
14 incentives for food manufacturers to move away
15 from using dairy in their products all
16 together.

17 Already we have seen suppliers of
18 dairy proteins begin to offer their consumer
19 nondairy proteins that can replace or
20 substitute for dairy. Take, for instance,
21 Armor's announcement last month that a soy
22 protein isolate it manufactures could be used
23 to replace some or all of the dairy proteins
24 traditionally used in several products on the
25 marketplace today.

1 R. Waldron - Direct Testimony

2 Armor is not alone. Other major
3 suppliers have begun developing vital wheat
4 gluten, wheat protein isolates and egg-based
5 ingredients as comparable alternatives to
6 dairy-based ingredients. Consumer acceptance
7 of these proteins is already very high.

8 For instance, the FDA may allow a
9 qualified health claim linking soy protein
10 consumption with a reduced risk of certain
11 cancers and has already approved a claim
12 linking soy protein with lower cholesterol.

13 Such claims only increase demand for
14 soy proteins. In recent weeks, soy producer
15 Solae announced a partnership with Yoplait in
16 France which is a separate and distinct company
17 from Yoplait USA but does offer similar yogurt
18 products. Throughout France, Solae and Yoplait
19 will begin Bioplait, a spoonable yogurt product
20 containing soy protein.

21 Closer to home, White Wave has begun
22 selling its Silk Live product which is a
23 soy-based live-cultured smoothie. White Wave's
24 product contains six live and active cultures,
25 is sold in single serving ten-ounce bottles and

1 R. Waldron - Direct Testimony

2 contains 200 calories per serving. Similar to
3 our fortified yogurt smoothies such as
4 Nouriche, Silk Live is in competition with our
5 yogurt smoothie products, not fluid milk.

6 The use of the non-dairy proteins in
7 dairy products can be done here and now. It is
8 not some technological fantasy. Companies can
9 and will respond immediately if USDA acts to
10 change the terms or application of the current
11 classification standards to make these protein
12 sources more expensive.

13 While consumers certainly have an
14 appreciation for dairy-containing packaged
15 goods, our experience also shows consumers to
16 be very sensitive to even the slightest changes
17 in price. Facing increased commodity prices
18 when cheaper, comparable alternatives are
19 available, manufacturers will simply move to
20 lower cost options.

21 We believe that the fluid milk
22 definition should not change. The proposal
23 that we have brought forward, we believe,
24 preserves the current standard with the
25 restriction that they contain a significant

1 R. Waldron - Direct Testimony

2 amount of yogurt. That restriction is
3 consistent with the data we have provided.

4 General Mills could support Proposal
5 7 if added whey was not included in the protein
6 standard, just as it is not included today. We
7 do not support any of the other proposals in
8 general because they are either too subjective
9 or represent a significant departure from
10 today's definition of fluid milk.

11 To review, as early as January 2004,
12 General Mills requested that USDA conduct an
13 economic analysis to determine what yogurt
14 smoothies products, if any, were competing
15 against fluid milk. To date, such analysis by
16 the Department has not been conducted.

17 It is troubling that USDA is
18 advancing an agenda to change the terms of the
19 current classification standards in the absence
20 of any data that support the need for such a
21 move.

22 Conducting a thorough economic
23 analysis would demonstrate a number of
24 realities. One, yogurt smoothies are in no way
25 competing with fluid milk. Secondly, the

1 R. Waldron - Direct Testimony

2 presence of such products in the marketplace-as
3 Class II-actually add revenues for producers;
4 and finally; three, USDA understands the value
5 that manufacturers such as Yoplait provide
6 dairy producers by marketing and developing
7 dairy-containing products.

8 USDA's approach to this issue should
9 be broad enough to promote innovation to meet
10 demand, recognizing that innovation is likely
11 to increase dairy consumption and result in
12 higher producer revenues.

13 Are yogurt smoothies consistent with
14 the form and use of fluid milk? Clearly not.
15 Fluid milk contains neither the calories nor
16 the nutrients of Yoplait's yogurt smoothies
17 which are characterized by the yogurt contained
18 in the product. Consumers use these products
19 as food much the same way as they consume
20 yogurt.

21 With that, I appreciate the
22 opportunity to be here today, and I would be
23 happy to try to answer any questions that you
24 may have. Thank you.

25 JUDGE DAVENPORT: Examination

1 R. Waldron - Cross - by Mr. Yale
2 of this witness? Mr. Yale?

3 MR. YALE: Ben Yale on behalf
4 of Select Milk Producers and Continental Dairy
5 Products, Inc.

6 -----

7 CROSS-EXAMINATION

8 BY MR. YALE:

9 Q. Good morning, gentlemen.

10 A. Good morning.

11 Q. I want to kind of go back and start
12 with the end arguments you made, this comment
13 that this would provide added revenue to
14 producers.

15 Have you done any analysis in terms
16 of the economic impact by going from Class I to
17 Class II for the smoothies, one in terms of
18 what it would do overtly to the producer income
19 which we can do in terms of the difference
20 between I and II and not as obvious, but
21 clearly I think one that could occur and that
22 is that the reduced price could create
23 increased consumption and the whole demand and
24 supply deal. Have you done any analysis on
25 that?

1 R. Waldron - Cross - by Mr. Yale

2 A. I would like to restate your
3 question and make sure that I have it
4 correctly. The first part of your question is
5 that an analysis has been done between Class I
6 and Class II milk consumption, the
7 classification of these products and the second
8 is more sensitivity of our products. Would
9 that be correct?

10 Q. Well, that's kind of it. Tell me
11 what your study is, what you know. It's all
12 economics; right? We are not here to talk
13 about theory. My producers want money in their
14 pocket and however it comes, they are happy.
15 I'm just trying to figure out whether there is
16 a way that you can win and we can win and
17 that's the purpose of the question.

18 A. I apologize. We have many studies.
19 I'm trying to get you the best answer that you
20 want.

21 Q. It comes down to the obvious one we
22 can do mathematically is we take the volume of
23 milk that was in Dr. Rourke's testimony two
24 days ago of 3.0 percent of Class I and market
25 it, and we can kind of come up with a volume

1 R. Waldron - Cross - by Mr. Yale
2 and we can estimate what the differences are
3 between Class I and Class 2 and we can come up
4 with a dollar contribution to the producer
5 settlement fund that would be a reduction by
6 going from I to II. That one we know. But do
7 we have anything that would say that because
8 you are now paying Class II that that reduction
9 in price would increase the demand for milk to
10 produce the smoothies sufficient that that
11 would create an offset in the producer
12 settlement fund by just raising the overall
13 level of milk prices? Have you done anything
14 like that?

15 A. We do not have economic analysis of
16 the full value chain that I believe you're
17 talking about. What we have focused on is more
18 price sensitivity analysis that showed that
19 consumers are highly susceptible to even the
20 slightest change in price.

21 When we look at our ability to
22 market as efficiently as possible and the
23 ability then to have margins that allow us as a
24 marketing company to support new products, the
25 differential for us which is more classified in

1 R. Waldron - Cross - by Mr. Yale
2 the differential to promote end users who use
3 these categories so we know that price
4 sensitivity is very high among our consumers,
5 but I do not know exactly the economic analysis
6 back through the pricing of milk.

7 Q. Have you computed what the
8 difference in raw product cost per unit is
9 between Class I and Class II for your product?

10 A. We would have that information, but
11 I believe that is information that is of a
12 proprietary basis that I don't believe should
13 be discussed in the public forum. I would say
14 this. We would be happy to provide that
15 information to the USDA in a more confidential
16 setting.

17 Q. Some of it isn't all that
18 confidential, and I'm talking in terms of the
19 difference between Class I and Class II. Those
20 are public numbers; right? Those are public
21 routinely. We know what that number is; right?
22 We know what that difference is, and we know
23 the volume of milk that goes through your
24 products. Is that proprietary?

25 A. That is proprietary. We do not

1 R. Waldron - Cross - by Mr. Yale
2 share just for general forum for this group
3 here. We have proprietary sourcing,
4 proprietary recipes that we do not wish out in
5 public forum.

6 Q. That really wasn't my point. I
7 really don't want those, but in general are we
8 talking a nickel a unit or are we talking a
9 penny a unit? What range are we talking in
10 terms of the change in price to consumers based
11 upon this change?

12 A. I consider all of that within the
13 classification of proprietary information that
14 we will gladly discuss in a confidential manner
15 with the USDA but not in a public forum.

16 Q. You would agree, would you not,
17 that -- You understand that what is in the
18 record is the basis of what the department has
19 to base its decision on? Are you aware of this
20 process?

21 A. I am not fully aware of all of the
22 details of this process. I would not consider
23 myself an expert at dealing with the legalities
24 of this process.

25 Q. I'm going to give you kind of a

1 R. Waldron - Cross - by Mr. Yale
2 paraphrase and then I'm going to ask the
3 question. The point is that in principle, the
4 concept, and I think Dr. Stephenson did an
5 excellent job the day before yesterday, talks
6 about that if you move something from one class
7 to another, it has positive impact on the
8 producer income and this way has a negative
9 impact on that way.

10 The idea is that price, a lower
11 price creates higher demand, higher demand
12 creates higher overall pricing and income to
13 the producers. That's the concept.
14 Fundamentally for producers, that's the whole
15 issue that they are here today for. I'm just
16 trying to get information to arrive at that.

17 The question that comes to mind is:
18 Is a change from Class I to Class II going to
19 change the consumer price enough to generate
20 additional demand to offset the value of Class
21 I? Can you answer that question?

22 A. I would answer the question in this
23 form is that for at least a year, year and a
24 half now General Mills has promoted that an
25 economic study be done of these products and

1 R. Waldron - Cross - by Mr. Yale
2 inclusive with that study could be the full
3 economic analysis that you're talking about and
4 within this could have been the next logical
5 step versus the hearing today. So I support
6 your line of thinking and would recommend a
7 full economic analysis be done.

8 Q. Currently it is priced as Class I,
9 these smoothies; am I correct on that?

10 A. Once again, a lot of that
11 information is confidential in our mind because
12 of the proprietary sourcings and methodologies,
13 but I will say this. Some of our products are
14 priced in the Class II range and if they change
15 to the classification were it to be done, that
16 would probably change at least one of our
17 products from Class II to Class I.

18 Q. Do you have any products that are in
19 Class I?

20 A. Yes.

21 Q. And your proposed change would move
22 those from I to II?

23 A. Well, our proposed change is no
24 change. We are recommending the status quo at
25 this time. Much of my commentary were if the

1 R. Waldron - Cross - by Mr. Yale
2 USDA wants to go and make a change with the
3 proteins standard, but the General Mills
4 classification or proposal is for no change at
5 this time so those products in Class I would
6 stay in Class I. Those products in Class II
7 would stay in Class II.

8 Q. Including any products that Yoplait
9 currently makes that is classified as Class I
10 if such exist, that wouldn't change; is that
11 correct?

12 A. At this time, that's correct.

13 Q. As I see it, this hearing is really
14 coming down to proposals, one, how to treat
15 yogurt and the other one is how to define the
16 nonsolids fat portion of the fluid milk
17 beverage issue, but generally right now it says
18 solids not fat and the proposal is to just go
19 to the value part and that's the protein;
20 right? So that's the change that you're
21 objecting to where it goes to the 2.2 percent
22 or 2.25 percent for protein as the trigger?

23 A. We are not objecting to anything.
24 Quite honestly, we are saying the status quo
25 works. We would like to stay there. If a

1 R. Waldron - Cross - by Mr. Yale
2 protein standard were to change where you're
3 challenging the added weight protein
4 concentrate, that would be in that measure.

5 Q. Are you aware that the proposal to
6 go from the 6.5 percent solids not fat to the
7 protein was just to find what the protein
8 portion pro rata would be of 6.5 percent
9 solids, not fat and just speaking not in terms
10 of all solid not fat and just a protein? Do
11 you understand that that's the gist of the
12 proposal?

13 A. It is my understanding that is the
14 intent of the proposal.

15 Q. Let's talk a moment about where you
16 also understand the proposal is not to price
17 the whey that goes into the products, the whey
18 protein but to use it for classification
19 purposes only. Do you understand that?

20 A. I would not express myself to be an
21 expert in this matter, but I would think that
22 would be something I would expect.

23 Q. And that the rationale for the
24 whey -- I mean, I think your point about the
25 value of whey versus other proteins is very

1 R. Waldron - Cross - by Mr. Yale
2 well taken. I don't want to disagree with
3 that, but I want to get down to this question
4 and that is that the purpose of the whey is a
5 concern that if you set that 2.25,
6 manufacturers are very innovative, not only to
7 meet consumer needs but to work their ways
8 around economic, noneconomic regulations,
9 however one wants to view them to come out with
10 the best dollar value that they can. I think
11 we can all agree on that position.

12 The purpose of this whey addition is
13 to take away an opportunity for somebody to
14 create a loophole to come in with, say, 1.9 or
15 2.0 percent regular milk proteins and then add
16 some whey to get their protein level up to what
17 they want simply for purposes of avoiding the
18 regulation and that's its purpose. Do you
19 understand that that is why that was put in
20 there? I don't know whether you have been
21 through the testimony or understood the --

22 A. I do understand that and its general
23 application.

24 Q. At that point there is still an
25 opposition to making that as a basis for

1 R. Waldron - Cross - by Mr. Yale
2 classification?

3 A. We also believe that there is
4 further ramifications that should be considered
5 in this area.

6 Q. And those are?

7 A. Those are essentially we can have a
8 classification standard, but also there will be
9 a pricing standard that comes with that and the
10 necessary reality of it is we can classify
11 things many different ways; but if we price
12 yellow ties like you have at one price and blue
13 ties that I have, they are both ties but if
14 your tie is priced higher than mine, I think we
15 will see a lot of people start wearing blue
16 ties.

17 So there is economic reality that
18 follows through from the line of reasoning that
19 we have here that could impact a manufacturer's
20 decision to use added whey as a protein source
21 that would move us away from dairy ingredients,
22 something that we don't wish to do, but
23 economic reality would cause us to do that to
24 stay competitive in a marketplace that
25 ultimately services our end consumer which is

1 R. Waldron - Cross - by Mr. Yale
2 the daily user.

3 Q. Maybe to paraphrase it in a
4 different way, you're saying that it might even
5 create incentive to using more whey although it
6 might classify as one, the product is so much
7 less expensive than the others that it might
8 decrease the use of actual dairy proteins in
9 the product?

10 A. No. I wasn't referring to that at
11 all. Maybe I misstated such that you didn't
12 pick up my gist. It was more that we would
13 walk away from dairy-based ingredients more
14 than to exact or substitutes that are coming
15 onto the market very quickly.

16 I did state earlier that a company
17 that we are distinct and separate from, Yoplait
18 France, has already started moving toward soy
19 protein alternative. That was really the gist
20 of where I was going is that we would prefer to
21 use dairy ingredients.

22 We believe a healthy dairy industry
23 has really helped supply us with better
24 product, better ideas to new products that we
25 can use; but if we are basically forced in a

1 R. Waldron - Cross - by Mr. Yale
2 sense to look at other alternatives, those
3 other alternatives become more attractive and
4 those other alternatives are non-dairy based.

5 Q. Price obviously is one of the things
6 that can drive a manufacturer to go to a
7 soy-based protein or some vegetable protein as
8 opposed to dairy; right?

9 A. Could you repeat that?

10 Q. Price can be one of the factors that
11 can drive a user to a soy based or a
12 vegetable-based protein as opposed to dairy
13 ingredients. Would you agree with that?

14 A. Right.

15 Q. But isn't there also a drive, I
16 think you mentioned in your testimony, that the
17 soy promotes the fact that there is low
18 cholesterol and it has some other healthy
19 health benefits by using soy as opposed to
20 dairy; right?

21 A. Correct.

22 Q. And that that in itself is a driver
23 of consumers to go to that product, not so much
24 the price but the supposed benefit. I'm not
25 saying supposed, but the expressed benefit of

1 R. Waldron - Cross - by Mr. Yale
2 soy over milk; right?

3 A. Well, there are benefits to dairy
4 ingredients, and there are going to be benefits
5 to non-dairy used ingredients. While we have
6 dairy ingredients in our product formulations,
7 we are quite accustomed to handling dairy
8 ingredients in our manufacturing process so
9 it's better for us to continue use of dairy
10 ingredients. At this time we have also
11 actively explored the benefits or finding the
12 benefits of increased usage of dairy news, so
13 to speak.

14 What I mean by that is years ago we
15 worked with Dr. Zemel of the University of
16 Tennessee to really kind of unlock the code as
17 the dairy industry has been also working with
18 him on weight loss through calcium as delivered
19 through a dairy environment, so it's really
20 organic to the product itself.

21 We continue to explore ways in which
22 dairy will be able to promote news that we will
23 bring the goodness of dairy out to more and
24 more consumers. We have seen phenomenal growth
25 in our yogurt light products.

1 R. Waldron - Cross - by Mr. Yale

2 My original chart in our blue cups
3 which is highlighted, the Dr. Zimmel or our
4 weight loss news so we would hope to partner
5 with the dairy industry to continue to find
6 ways of promoting the benefits of dairy. I
7 think my guess would be in the future we will
8 continue to unlock the power of dairy due to
9 its nutritional density.

10 Q. Let's go to the products you
11 mentioned. Early in your testimony, you talked
12 about that it's more than just milk. There is
13 other higher calories and other food
14 ingredients that are added to the product, and
15 I wasn't sure whether you were saying that you
16 have more than 20 percent of the RDA vitamins
17 or you just have additional vitamins in your
18 products. What is the content of the vitamins?
19 Do you have any claim there that you're getting
20 20 percent of the RDA or all of the major
21 vitamins and minerals or just additional
22 vitamins and minerals?

23 A. We have claims as to its ability to
24 fit within a meal replacement position. I take
25 you back to the beginning of Nouriche. It is

1 R. Waldron - Cross - by Mr. Yale
2 consumers, and I should have brought the
3 advertising for this product, but a lot of
4 consumers are walking out the door in the
5 morning with simply a cup of coffee, and we saw
6 the opportunity to get them started right in a
7 day by at least having some sort of meal fuel
8 in their system so we fortified our product to
9 meet the positioning standards as required for
10 meal replacement.

11 Q. Looking at page 2, here is the
12 ambiguity I saw on the top of page 2, Nouriche
13 provides more than 20 percent of the daily
14 recommended intake of carbohydrates, protein
15 and more than 15 other vitamins and nutrients
16 including folic acid and vitamins A, C, D, E.

17 My question is: Are you saying that
18 you have more than 20 percent of the daily
19 recommended intake of those other 15 vitamins,
20 or do you have 20 percent of the carbohydrate
21 and protein and in addition to that you have
22 some of the supplemental vitamins?

23 A. You're correct in your latter
24 statement.

25 Q. So it's not saying that you have

1 R. Waldron - Cross - by Mr. Yale
2 more than 20 percent of the daily recommended
3 of those vitamins and minerals?

4 A. We may have on certain vitamins. I
5 don't have the nutrition panel right in front
6 me at this time, but at this point the clarity
7 is the 20 percent on the daily recommended
8 intake of carbohydrates, protein and that we do
9 have more vitamins and minerals.

10 Q. The reason I asked that is we have
11 talked about the infant formulas and the diet
12 drinks and meal replacements in the testimony
13 here, and I didn't see any effort to tie that
14 in. That's my question, whether you thought
15 that you really were a meal replacement or one
16 of those types of products?

17 A. We are a yogurt product, and we tend
18 to think from a yogurt classification when we
19 see from some of the testimony that I gave that
20 the vast majority of the usage of Nouriche
21 smoothie, for example, is coming from current
22 yogurt consumption so we tend to think from a
23 yogurt basis.

24 I will say that my 3-1/2 year old
25 daughter has been drinking Nouriche as an

1 R. Waldron - Cross - by Mr. Yale
2 afternoon snack for a long time because it's
3 healthy and it keeps her on the go.

4 Q. Let's follow-up on that. You
5 mentioned that if the product contained at
6 least 20 percent yogurt, it would not be a
7 Class I product. I think that was your
8 proposal. When you use the term "yogurt," are
9 you talking about the standard of identity for
10 yogurt or are you talking about any cultured
11 milk snack or milk product that's comparable to
12 yogurt? As you know, there has been a move
13 away from the pure yogurt products getting to
14 the consumer. Not being critical of that, but
15 what do you mean by yogurt?

16 A. Let me answer that question first by
17 restating that we propose the status quo on the
18 classifications, but if a change is made, we
19 would classify our yogurt under the standard
20 identity of yogurt.

21 Q. Finally, you talk about this margin
22 of error, I think the point being that you
23 don't want to have somebody pull one sample out
24 of the dairy case and do a test because of the
25 dairies and manufacturing and have a spike in

1 R. Waldron - Cross - by Mr. Yale
2 protein or something like that. Is that kind
3 of what you're saying?

4 A. That's what we are saying.

5 Q. What the appropriate thing to do is
6 to base it, first of all, upon what is on your
7 label in terms of the contents of your product
8 mix. Would that be the beginning point?

9 A. Correct.

10 Q. Then if there are variations from
11 there, I think even the FDA allows some
12 variation?

13 A. Yes. That's what I said. The USDA
14 and FDA have allowed for a 20-percent variance,
15 but we generally want to label what we are
16 providing to the consumer and we do our best.
17 We have a very consistent track record with our
18 manufacturing facilities.

19 MR. YALE: I do have just an
20 inquiry, Your Honor. The charts, are copies of
21 them made part of the record?

22 JUDGE DAVENPORT: They are
23 part of the record, and they are in reduced
24 form in the record. I don't think I want to
25 put the large ones into the record.

1 R. Waldron - Cross - by Mr. Vetne

2 MR. YALE: Thank you very
3 much.

4 MR. WALDRON: I do have one
5 addition and given the nutritional label for
6 Nouriche and the other vitamins and minerals
7 that were mentioned, A, C, D and E are all at
8 the 25 percent level of the daily intake, so
9 they are also over the 20 percent. That was
10 not the key determinant in our decision as much
11 as it was developing a product that would meet
12 the classification for meal replacement under
13 U.S. guidelines.

14 MR. YALE: So you consider it
15 a meal replacement under those guidelines?

16 MR. WALDRON: Correct.

17 JUDGE DAVENPORT: Other
18 examination? Mr. Vetne?

19 -----

20 CROSS-EXAMINATION

21 BY MR. VETNE:

22 Q. Good morning. I'm John Vetne. On
23 page 2 of your testimony, you refer to several
24 presentations to the department, that's to USDA
25 outlining the form and use of Nouriche. Do you

1 R. Waldron - Cross - by Mr. Vetne
2 refer to that?

3 A. Yes. Our pages don't line up with
4 yours and I'm trying to find it.

5 Q. Under the heading "Products Must Be
6 Classified in Accordance with Form and Use."

7 A. Oh, yes, I remember.

8 Q. Were those presentations in
9 connection with discussions with USDA
10 concerning the proper classification of your
11 products under the current fluid milk product
12 definitions?

13 A. I would like Jeff Shapiro to handle
14 that because he was more closely aligned with
15 that.

16 MR. SHAPIRO: Yes, that's
17 correct.

18 MR. VETNE: And you made an
19 effort to persuade USDA that some of your
20 beverage yogurts that were Class I were similar
21 in form and use and content and function to --

22 MR. SHAPIRO: I think not
23 persuaded. We just wanted to walk USDA through
24 our product. I wouldn't characterize it as
25 persuaded.

1 R. Waldron - Cross - by Mr. Vetne

2 MR. VETNE: But there were
3 issues concerning which classification certain
4 Yoplait beverage yogurts would be in?

5 MR. SHAPIRO: I wouldn't
6 characterize it like that. I would just say
7 that we viewed those discussions as proprietary
8 discussions, but it would be unfair to
9 characterize it like that.

10 MR. WALDRON: If I may add in
11 here, I think one of the keys that we are
12 trying to do is drive innovation in the
13 industry and sometimes innovation leads to
14 products that are not maybe quite classified
15 yet, and we want to make sure we interpret the
16 classification well so we have a great working
17 relationship with USDA and on major new
18 innovations we like to make sure that we both
19 understand how this product will be classified
20 going forward.

21 That, I would say, is true of the
22 nature of discussions just to make sure that we
23 truly understand together what this new really
24 form-breaking category is going to be about.

25

1 R. Waldron - Cross - by Mr. Vetne

2 BY MR. VETNE:

3 Q. Would it be correct for me to
4 conclude from that answer that it's important
5 for you to have some understanding at the
6 concept and development stage even before
7 commercialization to know how USDA will price
8 your dairy ingredients?

9 A. It can depend. I would like to give
10 you an answer to the question, but it really
11 can depend. In this, it was ongoing discussion
12 of a new emerging segment in our yogurt area,
13 but often we will follow the end user of the
14 dairy chain so we develop concepts.

15 As I talked about before on
16 Nouriche, we spoke to over 30,000 users. The
17 concept was then developed and moved forward to
18 market. We did not then talk to USDA because
19 we were still putting the product formulation
20 together.

21 In reality, we went to market and
22 then started negotiations with USDA as to what
23 is this product. Negotiations is probably the
24 wrong word, probably discussions to make sure
25 we knew what it was.

1 R. Waldron - Cross - by Mr. Vetne

2 Q. Under the General Mills proposal
3 which is your second preferred option to the
4 status quo, Yoplait yogurt-containing beverages
5 that are currently Class I would become Class
6 II; am I correct?

7 A. Well, that is once again, I will
8 say, proprietary information that we would
9 share with USDA in a manner that would be
10 confidential.

11 The status quo is what we promote at
12 this point. Under our movement to the General
13 Mills proposal, we would find that to be very
14 similar to the status quo.

15 Q. I believe you said that if unaltered
16 Proposal No. 7 is adopted, one or more of your
17 yogurt products would move from Class II to
18 Class I?

19 A. That's correct.

20 Q. Are you familiar with a cultured
21 beverage product called kefir?

22 A. I am familiar with products on the
23 market with the kefir makeup, yes.

24 Q. Kefir is a product similar to yogurt
25 but uses cultures other than those identified

1 R. Waldron - Cross - by Mr. Vetne
2 to produce yogurt; is that correct?

3 A. I would not go as far as to say
4 kefir is identical or similar to yogurt. It
5 has characteristics of live and active
6 cultures, but the forms that I have seen of
7 kefir today on the marketplace are still a
8 small category and do not seem to be the same
9 forms that yogurt primarily comes in.

10 Q. Kefir is primarily sold in a
11 drinkable form; correct?

12 A. That is what I have seen on the
13 marketplace to date.

14 Q. So let's just limit it to drinkable
15 yogurts and kefir. Are you aware that when
16 produced, kefir is in a fermented cured form
17 similar to yogurt and solid and then the cured
18 is broken to produce the liquid?

19 A. I'm not aware of the details of
20 kefir production. We are in the yogurt
21 business at this point, not in the kefir
22 business.

23 Q. Do any of the data that you have
24 produced or studied or are aware of give us any
25 information on the competition between beverage

1 R. Waldron - Cross - by Mr. Vetne
2 yogurt and beverage kefir?

3 A. No. We have no information. I'm
4 just confirming with my CI director here on
5 kefir or its relationship to yogurt. It's a
6 broad spectrum I would say. Many dairy
7 products are cultured. Cheese uses the rennin
8 culture, for example. As you're probably
9 well-aware of, we don't study every cultured
10 dairy product. We are primarily looking at
11 yogurt, so I would not have any information on
12 its relationship to kefir at this time.

13 Q. I was thinking primarily of your
14 testimony on consumer inclinations to pick one
15 product over another from milk to cookies. Did
16 any of those questions include to consumers a
17 selection of beverage Yoplait versus beverage
18 kefir?

19 A. No. I don't know how to more
20 plainly say this. We have absolutely no data
21 on kefir other than the market data. I can
22 tell you sales of maybe several products, but
23 we have no market research on kefir itself.
24 Specifically when we asked them what they would
25 substitute for Nouriche, there was no mention

1 R. Waldron - Cross - by Mr. Vetne
2 of kefir.

3 Q. That wasn't an option?

4 A. These were verbatim responses so all
5 options were available for consumers to
6 respond. So kefir was obviously an option that
7 they could have mentioned, but there were
8 absolutely no mentions of kefir in our
9 expansive Nouriche research.

10 Q. Was that research a nationwide group
11 of consumers?

12 A. Correct.

13 Q. How many consumers were questioned?

14 A. 30,000 consumers were impacted in
15 our study.

16 Q. Were all 30,000 asked the same
17 questions?

18 A. Correct.

19 Q. Does Yoplait currently use -- and
20 this would be revealed on the ingredient panel
21 of your products -- any whey protein, isolate,
22 or whey ingredients in any of the products?

23 A. As I said, Yoplait does use WPC,
24 whey protein concentrate as a primary protein
25 source in some of our products.

1 R. Waldron - Cross - by Mr. Vetne

2 Q. When you purchase whey protein
3 concentrate, you purchase certain protein
4 specifications?

5 A. No. I will not say I'm fully
6 knowledgeable of the exact technical detail of
7 our procurements, and I don't feel comfortable
8 answering that question.

9 Q. Does any of the panel know?

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

11 Q. Do you know whether General Mills
12 tests the whey protein concentrate received
13 currently for conformity with whatever
14 specifications there might be or whatever
15 expectations you might have?

16 A. I would think General Mills has an
17 excellent supply chain to make sure that we
18 have end user consistency, so it would be my
19 guess that there is a testing process, but I
20 wouldn't speculate on how that is done or if
21 it's done by ourselves in conjunction with
22 suppliers or not.

23 Q. So you may rely on suppliers in
24 which you have confidence?

25 A. It is potential, but that would be

1 R. Waldron - Cross - by Mr. Beshore
2 speculation on my part.

3 Q. If Proposal 7 is adopted, do you
4 anticipate that you may have to undergo new
5 testing protocols to ascertain the whey protein
6 versus other proteins in milk?

7 A. We do not believe so at this time.

8 Q. You haven't studied that?

9 A. There is a gentleman in the audience
10 that is my director of quality and regulatory
11 operations, and he is saying that we would
12 probably not have to test it. I trust his head
13 nod to the negative.

14 MR. VETNE: That's it. Thank
15 you.

16 JUDGE DAVENPORT: Other
17 examination? Mr. Beshore?

18 -----

19 CROSS-EXAMINATION

20 BY MR. BESHORE:

21 Q. Good morning. Gentlemen, Marvin
22 Beshore for Dairy Farmers of America. Can you
23 tell me the average retail price of the
24 11-ounce Nouriche smoothie?

25 A. The average retail price is roughly

1 R. Waldron - Cross - by Mr. Beshore
2 around 1.82. It's a little higher on the West
3 Coast, a little lower in the southern part of
4 the country or a little higher depending upon
5 retailers' pricing practices, not ours.

6 Q. Is Nouriche smoothie presently
7 classified as Class I?

8 A. That is information that I would
9 prefer not to discuss in a public forum, but
10 that is probably already on record with the
11 USDA and we would be happy to provide that
12 information again to the USDA in a confidential
13 setting.

14 Q. Just so there is no
15 misunderstanding, the decision in this
16 proceeding by law must be made only upon the
17 information presented in this public hearing
18 record. Okay? Those are the legal
19 requirements that we are proceeding under so
20 that any information that has been privately
21 presented to the market administrator or
22 anybody else at the USDA may not by law be
23 considered in making this decision.

24 A. Okay.

25 Q. With that understanding, can you

1 R. Waldron - Cross - by Mr. Beshore
2 tell us whether the Nouriche smoothie is Class
3 I or Class II?

4 A. I would like to reiterate my
5 position to your first question. I believe
6 some of that is confidential information. We
7 would also say that that information is most
8 likely already in the records of USDA, so it
9 would be part of the intelligence of that
10 organization already, and we would assume that
11 they would use that knowledge in forming
12 decisions along with the testimony they hear.

13 Q. Chart 3 shows, if I understand, on
14 the bottom line, the red line on the graph, the
15 sales during -- What is the fiscal year
16 represented?

17 A. They are fiscal years, so they are
18 from June and end in May.

19 Q. So FY 00 would be June 1999 to May
20 2000?

21 A. Yes.

22 Q. Tell me as much as you can about
23 what data is represented in that autumn or red
24 line, bottom red line on chart 3.

25 A. I'm going to turn that over to my

1 R. Waldron - Cross - by Mr. Beshore
2 director Bob Anderson.

3 MR. ANDERSON: The red line
4 captures all of the products that we consider
5 to be yogurt smoothie products. That would
6 include our own Nouriche, Dannon's Frusion,
7 Light & Fit and products like that.

8 MR. BESHORE: Can you tell us
9 whether that includes products that are
10 presently classified both as Class I and as
11 Class II or is it exclusively one or the other,
12 if you know?

13 MR. ANDERSON: I believe I
14 told you which products that includes. I'm not
15 knowledgeable about what classification they
16 may be.

17 MR. BESHORE: We have some
18 information from the Dannon witness yesterday,
19 and the Dannon products would be included
20 within this data?

21 MR. ANDERSON: Yes.

22 MR. WALDRON: I think from the
23 testimony yesterday and now today, you would be
24 able to surmise that both Class I and Class II
25 products are in that red line.

1 R. Waldron - Cross - by Mr. Beshore

2 MR. BESHORE: Has General
3 Mills done any studies which compared the
4 growth rates of these drinkable products Class
5 I versus Class II?

6 MR. ANDERSON: No.

7 BY MR. BESHORE:

8 Q. The 11-ounce Nouriche, do you have
9 the nutrition label for that product available?
10 That's a public document. I assume you
11 wouldn't have any problem with having that in
12 the hearing record.

13 A. We would have no problem with that.

14 Q. Is it available to be included?

15 A. It was up here just a second ago.
16 Yes, we have it right here. I don't know what
17 the protocol is.

18 MR. BESHORE: I would like to
19 ask that that be marked.

20 JUDGE DAVENPORT: It is added
21 as an additional exhibit to their testimony
22 here today. We will just add it as the next
23 chart. The last chart was chart 7, so it will
24 be chart 8.

25 Q. Looking at chart 8, Nouriche a

1 R. Waldron - Cross - by Mr. Beshore
2 serving size of one container, 325 milliliters,
3 is that the 11 ounce?

4 A. Yes, that is the 11 ounce.

5 Q. Zero fat in Nouriche?

6 A. Correct. It's a healthy product.

7 Q. It has ten grams of protein. Are
8 all those all dairy proteins?

9 A. I believe that's once again a
10 proprietary recipe item that I would not like
11 to discuss in a public forum, but I would
12 believe that would be on record with the USDA.
13 If not, if there is a confidential setting that
14 we would share that information, that would be
15 fine.

16 Q. Ingredients are on the label, of
17 course, and they are listed in order of what?
18 Magnitude? Is that how they must be listed?

19 A. If I recall, the ingredient panel as
20 dictated, it must be listed by ingredient
21 percentages, percent of what is the end
22 product.

23 Q. Is that percentage by weight?

24 A. Percentage by weight.

25 Q. Pasteurized nonfat milk is the

1 R. Waldron - Cross - by Mr. Beshore

2 number one ingredient?

3 A. It is also the number one ingredient
4 in cup yogurt.

5 Q. If I were to show this label to any
6 of the members of the panel, I wonder if you
7 could identify any non-dairy protein sources of
8 the ingredients? Would you be able to do that?

9 A. You're talking to three nontechnical
10 experts.

11 Q. So the panel would not have the
12 expertise?

13 A. I would not trust our answers. We
14 can take a look. I don't know if we would be
15 able to give you an accurate answer.

16 Q. General Mills' primary position is
17 to retain the status quo in terms of the
18 classification regulations; is that correct?

19 A. That's correct.

20 Q. I take it from that that you're
21 satisfied with the fact that some yogurts are
22 classified as Class I. Others may be
23 classified as Class II?

24 A. We are satisfied with the objective
25 criteria that seems to be working right now in

1 R. Waldron - Cross - by Mr. Beshore
2 the marketplace for a stable market. We
3 function within that stable market.

4 Q. Your objection to changing that
5 objective criteria from nonfat solids to
6 protein, as I understand it, is that some
7 products that have more than 2.25 percent
8 protein might be bumped to Class I?

9 MR. SHAPIRO: It's not so much
10 that we have objection. It's just that we
11 don't believe there is any evidence of
12 disorderly marketing and absent that evidence
13 with the current classification framework
14 obviously working, we are happy to operate
15 within that.

16 MR. BESHORE: So you don't
17 have any objection to going on the protein
18 standard if it were found to be appropriate
19 under the legal standards required under the
20 act?

21 MR. SHAPIRO: We believe that
22 there is no evidence currently before the
23 Department that would suggest that disorderly
24 marketing is occurring.

25 MR. BESHORE: Is it your

1 R. Waldron - Cross - by Mr. Beshore
2 understanding that in order to revise milk
3 classification criteria that the Secretary must
4 determine that there are disorderly marketing
5 conditions prevailing?

6 MR. SHAPIRO: I wouldn't
7 characterize it like that, but I would say that
8 in our opinion that should be an assessment.
9 There is no reason to change for the sake of
10 change if we believe that everything is working
11 fine.

12 MR. BESHORE: How about
13 keeping up with changing technologies? Isn't
14 that an appropriate thing for a regulatory
15 agency to do?

16 MR. SHAPIRO: We think it's
17 appropriate certainly to study which is I think
18 why, as Bob referenced, for quite some time we
19 have urged that an economic analysis be
20 conducted.

21 MR. BESHORE: The consumer
22 study information that you have provided here
23 on chart 4 and chart 5 and some comments in
24 your testimony, do you have any of the backup
25 data for that information that you are prepared

1 R. Waldron - Cross - by Mr. Beshore
2 to place in the record such as Dr. Cryan's data
3 regarding the NPD panel that he had here?

4 MR. ANDERSON: I'm prepared to
5 describe in general terms how NPD collects this
6 data, its sample size and so forth. The data
7 themselves that we are entering into the record
8 is represented by these charts. This is the
9 data. NPD, of course, collects this data
10 across many different food and beverage
11 categories, some of which we have access to and
12 some we don't.

13 MR. BESHORE: Do you recall
14 seeing that question and answer data assessed
15 that Dr. Cryan provided? Do you have that sort
16 of data available for your studies?

17 MR. WALDRON: Let me just add
18 one thing. Remember this is an independent
19 third-party study.

20 MR. BESHORE: I understand.

21 MR. ANDERSON: The way the
22 national survey works is that they give
23 consumers a diary to fill out during a 14-day
24 period. During this 14 days, they record all
25 of the food and drink products that they use

1 R. Waldron - Cross - by Mr. Beshore
2 whether they are used inside the home or
3 carried from the home.

4 I have a sample of the diary here.
5 It's quite extensive, and it provides for
6 specific ways in which these consumers are to
7 characterize and/or categorize what they are
8 using. That would represent the form of the
9 questions that consumers are answering in that
10 study.

11 MR. BESHORE: From that study
12 then, the study group presented you with a data
13 set of the results, I take it?

14 MR. ANDERSON: Yes. It's not
15 unlike AC Nielson data in the sense that it's a
16 large database, and we can extract from it data
17 such as these that you're interested in seeing.

18 MR. BESHORE: So these are
19 extracts from that data set?

20 MR. ANDERSON: Correct.

21 BY MR. BESHORE:

22 Q. Do you have the full data set? Are
23 you prepared to make that a part of this
24 record?

25 A. Only the NPD group has the full data

1 R. Waldron - Cross - by Mr. Beshore
2 set. They sell it on a subscription basis. We
3 have access to certain categories. We don't
4 own the data. We only have access to data on a
5 limited basis.

6 Q. Can you make available for the
7 record all of the data that you have access to?

8 A. No, I can't.

9 Q. Because you're not allowed to or
10 because you're not prepared to?

11 A. Because we are not allowed to. It's
12 not our data to give to anyone else to access.
13 The subscription is limited to our access only.

14 Q. But you're allowed to extract parts
15 of it and make it available as you choose; is
16 that right?

17 A. Yes. But I'm sure NPD would be
18 happy to get a subscription and payment from
19 yourself if you wanted to have access to the
20 full data set.

21 Q. I think the dairy farmers of DMI are
22 supporting NPD substantially.

23 A. My guess is your access to it is
24 even more expansive than our access to it.

25 Q. I certainly don't have access and

1 R. Anderson - Redirect - by Ms. Grocholski
2 neither does this record and neither will the
3 Secretary when making any decisions to the full
4 set of data that General Mills has. You have
5 presented some extracts of that, and I was just
6 inquiring whether you would make available all
7 that you have. I gather that you're not
8 inclined to do that?

9 MR. ANDERSON: As I have said,
10 we don't have the data. We have computer
11 access to limited parts of the data, and we
12 have provided the data that we have access to.

13 MR. BESHORE: That's all I
14 have.

15 JUDGE DAVENPORT: Other
16 examination? Ms. Grocholski? Is this in the
17 form of redirect?

18 MS. GROCHOLSKI: You might say
19 so. Really this is more in the form of trying
20 to clarify.

21 JUDGE DAVENPORT: Very well.

22 MS. GROCHOLSKI: Bob Anderson,
23 let's just make sure we are understanding this
24 NPD service. When NPD has consumers fill out
25 that diary, are they having them fill out that

1 R. Anderson - Redirect - by Ms. Grocholski
2 diary for General Mills?

3 MR. ANDERSON: No, they are
4 not. They are filling it out for the NPD
5 group.

6 MS. GROCHOLSKI: So NPD has
7 many consumers fill out this diary and they
8 have all of this information that they put in a
9 big database; is that correct?

10 MR. ANDERSON: That's correct.

11 MS. GROCHOLSKI: General Mills
12 and many, many other companies have
13 subscriptions to this service that's provided
14 by NPD group; is that correct?

15 MR. ANDERSON: That's correct,
16 and they do refer to it as a service.

17 MS. GROCHOLSKI: So we have a
18 subscription and we can ask a question like
19 what time of the day does someone eat yogurt;
20 is that correct?

21 MR. ANDERSON: That's correct.

22 MS. GROCHOLSKI: In the case
23 of these charts 4 and 5, you made a specific
24 inquiry pursuant to the subscription we have to
25 the service about the use, how and when people

1 R. Anderson - Redirect - by Ms. Grocholski
2 are using yogurt and yogurt smoothies; isn't
3 that correct?

4 MR. ANDERSON: That's correct,
5 as well as fluid milk.

6 MS. GROCHOLSKI: All of the
7 information that you got in response to that
8 inquiry has been provided in this record today?

9 MR. ANDERSON: That's correct.
10 If I were to give you a piece of paper with the
11 numbers on them, they would be the exact
12 numbers that are reflected in our exhibit.

13 MS. GROCHOLSKI: I just want
14 to turn now to clarifying a couple of other
15 points. In the General Mills proposal where it
16 says 20 percent yogurt, and any of you can
17 answer this, that proposal is indicating that
18 to the extent that a product has an ingredient
19 in it, yogurt and it's at the 20 percent or
20 more level, that's when the proposal is
21 triggered; is that correct?

22 MR. SHAPIRO: That's correct.

23 MS. GROCHOLSKI: That yogurt
24 component that we are talking about would meet
25 the standard of identity for yogurt under

1 R. Waldron - Cross - by Dr. Cryan
2 federal regulation; is that correct?

3 MR. SHAPIRO: That's correct.
4 We believe consumers need that as a
5 characterizing ingredient.

6 MS. GROCHOLSKI: Finally, and
7 I think this is clarification that hopefully
8 will be appreciated, while I recognize you're
9 not prepared to talk about the specific
10 classifications of specific products, do you
11 agree with me that Yoplait has no products in
12 Class I?

13 MR. SHAPIRO: That's correct.

14 MS. GROCHOLSKI: If proposal
15 No. 7 is adopted, would any Yoplait products go
16 from Class II to Class I?

17 MR. SHAPIRO: Yes.

18 MS. GROCHOLSKI: That's all I
19 have. Thank you.

20 JUDGE DAVENPORT: Other
21 examination?

22 -----

23 CROSS-EXAMINATION

24 BY MR. CRYAN:

25 Q. Roger Cryan with National Milk. I

1 R. Waldron - Cross - by Dr. Cryan
2 have this chart which I'll give back to you for
3 the record. Nouriche contains 25 percent of a
4 long list of nutrients. Most of those are
5 added; is that correct?

6 A. Well, it's a mix from that being in
7 the product itself and the dairy ingredients
8 and then some are added on top of that.

9 Q. In fact, the nutritional content of
10 Nouriche is not typical of the drinkable
11 yogurts like the yogurt drinks on the market
12 today; is that correct?

13 A. Nouriche is the number one branded
14 yogurt in the category of yogurt smoothie, so I
15 don't know if your question is right. It is
16 not a majority of the category, but it is the
17 number one brand as far as size. So I think
18 the jury is still out as to what the
19 nutritional profile will be of this small
20 segment category.

21 Q. But drinkable yogurt or a
22 yogurt-containing drink does not necessarily
23 have this nutritional profile. This is a
24 specific formulation for Nouriche that does not
25 necessarily represent the generic yogurt drink.

1 R. Waldron - Cross - by Dr. Cryan

2 It is representative to the extent that
3 Nouriche is a large share of the market?

4 A. No. Nouriche was formulated for
5 meal replacement position in the marketplace.
6 We have formulated two other yogurt smoothie
7 products for other positionings in the
8 marketplace, so they are customized to those
9 positionings.

10 MR. ANDERSON: I would add
11 though that we do have research evidence that
12 consumers perceive Nouriche to be similar to
13 other yogurt smoothies in the market.

14 DR. CRYAN: The perception is
15 similar regardless of the nutritional content?

16 MR. ANDERSON: The perception
17 is that they are more similar to yogurt
18 smoothies than they are, for example, to other
19 food products they might eat.

20 Q. Is Nouriche a beverage?

21 A. Nouriche is drinkable yogurt. It is
22 not a beverage.

23 JUDGE DAVENPORT: Other
24 examination? Mr. Tosi?

25 -----

1 R. Waldron - Cross - by Mr. Tosi

2 CROSS-EXAMINATION

3 BY MR. TOSI:

4 Q. My name is Gino Tosi. I'm with the
5 Department of Dairy Programs. I have a series
6 of questions that I would like to ask you. One
7 of the things that I take away from your
8 testimony is that if we improperly price things
9 like yogurt smoothies, products like Nouriche
10 and Class I that it may result in the
11 formulation of products or shift in consumer
12 preferences away from dairy products because
13 they would become so expensive that it would
14 make other products more attractive, for
15 example, soy-based products and in that regard
16 you mentioned a Yoplait product in Europe that
17 has been based in soy. Would that soy-based
18 product still be considered a dairy product?

19 A. I don't know the exact
20 classification standard, but it depends, I
21 guess, on how much soy is put in. In France,
22 it is a yogurt product with soy, so I believe
23 that they would still classify it as a yogurt
24 product.

25 Q. If you could refer to your chart 3,

1 R. Waldron - Cross - by Mr. Tosi
2 are you familiar with the recent history of
3 milk prices as recorded under federal milk
4 marketing orders, as established by milk
5 marketing orders?

6 A. I am not.

7 Q. If I told you that between 2003 to
8 2004 we had the highest record milk prices ever
9 in the country, if I told you that and if you
10 would just assume that that's true for a moment
11 and that Class II products have a differential
12 added to it although not as high as the Class
13 I, to the extent that dairy products have
14 become that much more expensive, record high,
15 how do you explain the increase in the
16 consumption of your products how it was able to
17 increase during a time when milk prices were
18 record highs?

19 A. Just for clarity, increase in both
20 spoonable and drinkable yogurt is your
21 question?

22 Q. Well, I'm assuming what you're
23 showing here is the growth or you were able to
24 sell quite a bit of cup yogurt and your adult
25 smoothies?

1 R. Waldron - Cross - by Mr. Tosi

2 A. I would go back to the 30-year
3 history or so of yogurt and the category.
4 Whereas in the sixties it was probably a hippie
5 product eaten by a few people out in
6 California, and it has become a mainstream
7 product category now and through our continued,
8 the industry's continued innovation, new
9 products keep coming on board to make yogurt
10 category more mainstream so the growth rate in
11 the last 30 years has been roughly ten percent.
12 This shows components of the category that we
13 have been able to keep innovation coming that
14 has allowed for a greater household penetration
15 and buying rate of yogurt products.

16 Q. So what we are talking about here is
17 the innovation of the company perhaps
18 advertising, the impressions that you leave in
19 consumers' minds about the product have more to
20 do with sales than what that cost difference
21 might be between classification of a product
22 whether it be Class I or II?

23 A. I would say it's not just the
24 company first. I'm talking about the industry
25 in general has been continuing growth, and

1 R. Waldron - Cross - by Mr. Tosi
2 there has been innovation from multiple
3 competitors.

4 I don't know. I think pricing of
5 milk is a component obviously of our margin
6 structure, but coming out with meaningful
7 position products that people are willing to
8 pay for and then telling them that it's now
9 available has been a primary factor of our
10 success.

11 Q. Were any of your products deemed to
12 be fluid milk products by the Department?

13 A. No.

14 MR. SHAPIRO: No. I don't
15 believe currently any of them are fluid milk
16 products.

17 Q. Were they at one time?

18 A. We don't believe so, but we don't
19 know that with certainty.

20 Q. For example, you're not sure if
21 Nouriche was ever determined to be a fluid milk
22 product and the milk should be priced at Class
23 I?

24 MR. SHAPIRO: I believe -- I'm
25 not certain, but I believe though with respect

1 R. Waldron - Cross - by Mr. Tosi

2 to that question, the answer would be yes.

3 Q. If the product was priced at one
4 time, talking about the milk, was priced at
5 Class I and today it's priced at Class II, was
6 there a change in price at retail?

7 A. There would have been no change in
8 the price at retail so far for the launch of
9 Nouriche. It has been in the market for
10 roughly three years, so there has been no price
11 change that we have taken necessarily, but I
12 would say that there has been a greater
13 proportion of our money being spent for
14 consumer awareness of the product so to promote
15 the expanded use of our product line with more
16 consumers.

17 Q. I want to refer to your written
18 statement. Just a few things struck me as
19 curious. On page 3 when you were talking about
20 the consumer surveys that indicate Nouriche is
21 competing against other food products and is
22 not competing against fluid milk or other
23 beverages, would you consider orange juice and
24 soda to be beverages?

25 A. Are you asking for my opinion or a

1 R. Waldron - Cross - by Mr. Tosi
2 technical assessment?

3 Q. Well, we have to go back and
4 interpret what this means. I would like a
5 clarification. In my opinion, orange juice and
6 soda are beverages. I drink them. I don't use
7 them, for example, as a meal replacement. I
8 drink them as a beverage. But your statement
9 in here says that Nouriche is not competing
10 against fluid milk or other beverages.

11 A. Primarily, yes, that is true.

12 Q. The other thing that struck me was
13 that consumer preferences would actually state
14 the name of a branded product, for example,
15 Slim-Fast. When they said that, are we talking
16 about Slim-Fast in the can that you drink or
17 are we talking about the Slim-Fast in the
18 powder that you mix up with milk?

19 A. This is simply verbatim response
20 Slim-Fast, so whatever the consumer is thinking
21 when you say it. We capture the absolute
22 verbatim response, so it could be canned or it
23 could be powder or it could be another product
24 in the Slim-Fast category.

25 It would be like if a consumer, in

1 R. Waldron - Cross - by Mr. Tosi

2 my opinion on this one, said Kleenex which is
3 now a generic for facial tissues so Slim-Fast
4 could be a generic for the line of diet
5 slimming items that are out there.

6 Q. I guess that kind of struck me as
7 odd in that they would say something like that
8 and they would be so specific as to say cup
9 yogurt. It would seem to me if I were asked
10 what are your food preferences, I might say
11 yogurt. I don't know that I would have said or
12 I highly doubt that I would have said to you
13 cup yogurt.

14 A. Consumers continue to surprise us
15 with their responses. That's why we do so much
16 investment in market research with the end user
17 of products that we either have now or are
18 going to have so these are the verbatim
19 responses.

20 Q. What is General Mills' opinion about
21 what does disorderly marketing mean to you?

22 MR. SHAPIRO: I guess I would
23 say the products that are known to compete with
24 other products. I guess I'll break it down to
25 with respect to our yogurt smoothies.

1 R. Waldron - Cross - by Mr. Tosi

2 We believe, and we have shown
3 conclusively that they compete against fluid
4 but does not compete against fluid milk and
5 should, therefore, not be classed as such in
6 doing so and in our opinion would be
7 classifying it inappropriately.

8 MR. TOSI: Please say that
9 again because I'm not sure if I followed
10 through with you on that.

11 MR. SHAPIRO: When producers
12 gain revenue from Class I products, it should
13 be revenue from all products that compete in
14 Class I with Class I fluid milk products. To
15 capture revenue as a Class I product for a
16 product that does not compete against Class I
17 would be disorderly. In our opinion then, the
18 products that compete in Class II particularly
19 yogurt products, cup yogurt products, et cetera
20 should then be classified as Class II.

21 MR. TOSI: If all drinkable
22 yogurt products were classified the same across
23 the country, that means all handlers that are
24 making that product are charging the same price
25 and producers are receiving the appropriate

1 R. Waldron - Cross - by Mr. Tosi
2 share of that revenue, where is the disorder?
3 Where would there be disorder in something like
4 that?

5 MR. SHAPIRO: I think for us
6 the question is Class I has fluid milk in the
7 sense Proposal 7 would change the
8 classification of at least one of our products
9 from Class II into Class I, a/k/a fluid milk.
10 It's not a fluid milk product. It shouldn't be
11 classed as fluid milk and producers shouldn't
12 receive the revenues from those products as
13 fluid milk products because they are not fluid
14 milk.

15 MR. WALDRON: If I may just
16 answer your question, there would be order in
17 the fact that everyone would be charged the
18 same, but the disorder comes in in the
19 necessary nature of the charging itself. If
20 the charge is wrong, then that will lead
21 manufacturers in a different direction that may
22 not be beneficial for all of us in the dairy
23 chain together.

24 As I said, while everybody is being
25 charged the same, if they are being charged

1 R. Waldron - Cross - by Mr. Tosi
2 incorrectly, the by-product behavior of that
3 will eventually lead maybe not to disorder but
4 an orderly march away from dairy.

5 MR. TOSI: With respect to the
6 goal of the Federal Milk Marketing Order
7 Program, what is your understanding of the goal
8 of the program with respect to the relationship
9 between dairy farmers and the folks that buy
10 milk from the handlers?

11 MR. SHAPIRO: Well, I think as
12 Bob said in his testimony, we all benefit from
13 the greater promotion of dairy and
14 dairy-containing products. As Bob said in his
15 testimony, we are all part of the same value
16 chain.

17 MR. TOSI: I was wanting to
18 hear your views and opinions on what you
19 understand the goal of the Federal Milk
20 Marketing Order Program is with respect to
21 dairy farmers and the folks that buy milk from
22 dairy farmers meaning handlers.

23 MR. SHAPIRO: I guess I'm not
24 familiar with the term "handlers."

25 MR. TOSI: Do you buy milk

1 R. Waldron - Cross - by Mr. Tosi
2 from dairy farmers?

3 MR. SHAPIRO: I'm sorry. I
4 just need clarity on that terminology I have
5 not heard before.

6 MR. TOSI: If I made a
7 statement and asked you to assume that it was
8 true, would you go along with that for right
9 now?

10 MR. SHAPIRO: Yes, I would.

11 MR. TOSI: If I told you that
12 the Agricultural Marketing Agreement Act that
13 you guys referred to earlier describes handlers
14 as those that buy milk from dairy farmers, the
15 first buyers of milk from dairy farmers, those
16 would be handlers and if General Mills does
17 that --

18 MR. SHAPIRO: We are a
19 handler. I just did not hear the terminology
20 before. That's what sort of threw me.

21 MR. TOSI: The milk program
22 I'm sure you have learned has its own unique
23 terminology. What is your understanding of
24 about what the goal of the milk order program
25 is with respect to what your relationship is

1 R. Waldron - Cross - by Mr. Tosi
2 with dairy farmers? What does it try to do?

3 MR. SHAPIRO: I think its goal
4 should be to classify products appropriate to
5 the form and use. When that is done, I think
6 our relationship to producers and handlers can
7 remain a very positive one.

8 MR. WALDRON: I'm not an
9 expert in this area, but it's my understanding
10 that the USDA and related divisions of it have
11 a long tradition of protecting, so to speak,
12 and stabilizing ultimately the farmer base so
13 that we have become the greatest
14 dairy-producing nation in the world bar none.
15 We have that.

16 That allows them, the rest of us,
17 the handlers, so to speak, to capitalize on
18 that stable supply chain so that we can help
19 expand consumption of dairy in the formats that
20 we choose. We happen to be a yogurt food
21 company and we capitalize on that dairy market.

22 If the dairy at the beginning of the
23 value chain, if the dairy industry is weakened,
24 we are weakened also so we ultimately see the
25 role of the USDA keeping the value chain

1 R. Waldron - Cross - by Mr. Tosi
2 healthy.

3 MR. TOSI: With regard to the
4 Agricultural Market Agreement Act 37, was it
5 your testimony that the act says that we should
6 classify milk in accordance with form and its
7 intended use; is that correct?

8 MR. SHAPIRO: Part of our
9 testimony, correct.

10 MR. TOSI: In that regard
11 then, you seem to be suggesting in your
12 testimony that determinants of classification
13 should be based on an economic study, and
14 you're bringing into the equation now an
15 economic study that would probably reveal
16 things that have to do with what producers
17 receive, what it is costing processors like
18 yourself or handlers like yourself. What would
19 that have to do with form and use?

20 MR. SHAPIRO: I have to
21 clarify. Classification should be done in
22 conformance with form and use. It was our
23 testimony and has been our communication to
24 USDA previously that an appropriate first step
25 in this proceeding would have been and would

1 R. Waldron - Cross - by Mr. Tosi
2 remain to be an economic analysis to determine
3 just the competitive landscape, what is going
4 on with these products, are they having an
5 effect on producer revenue, et cetera. So not
6 that a product could be classified in
7 accordance with the findings of such an
8 economic study, but that that would have been
9 the first step for these proceedings.

10 MR. TOSI: Do you know what is
11 going on with respect to fluid milk consumption
12 in general?

13 MR. ANDERSON: Yes. It is
14 generally declining.

15 MR. TOSI: If that were the
16 case, would you think it would be appropriate
17 then with respect to maintaining the health of
18 the industry that the reason consumers are
19 drinking less milk has to do with the milk
20 prices?

21 MR. ANDERSON: There is
22 probably many variables, consumers' lifestyles,
23 pricing could be a variable, but I would not go
24 out on record and say that pricing is the
25 variable.

1 R. Waldron - Cross - by Mr. Tosi

2 MR. TOSI: You seem to be in
3 your testimony making a really strong statement
4 about how it's going to be really bad for dairy
5 farmers if milk use and drinkable yogurts were
6 priced at Class I. There is going to be all of
7 these dire consequences of shifting to
8 soy-based products.

9 To the extent that your products
10 used to be Class I and are now Class II, you're
11 saying that there has been no change at the
12 price at retail, that sort of brings in the
13 question, the points that you're trying to make
14 here.

15 MR. SHAPIRO: I think the
16 distinction perhaps is consumer price on the
17 shelf versus our input costs on how that might
18 determine our behaviors.

19 BY MR. TOSI:

20 Q. When your input costs go down, do
21 you go back out to your retailers and say we
22 are really concerned about the health of the
23 dairy industry and milk prices really fell here
24 over the last few months, could you guys cut
25 your price at retail?

1 R. Waldron - Cross - by Mr. Tosi

2 A. We are not at liberty to discuss
3 prices with our retail partners. That is their
4 choice. We supply one price to the retail
5 trade and we have taken prices down.

6 Q. But if prices go the other way where
7 they go up, you will pass that cost onto the
8 retailer then?

9 A. Sometimes we do; sometimes we don't.
10 Under the current conditions, we have not
11 changed pricing on our cup yogurt although our
12 input cost of milk are, as you stated, at
13 record high levels, yet we do not believe that
14 it would be wise for us to change pricing at
15 this time.

16 Q. But your link out to the consumer
17 from your link to the dairy farmer and the
18 other thing that happens in-between, your link
19 from taking what dairy farmers receive that's a
20 result of classification and the impact that's
21 going to be out there to the consumers that's
22 going to end up driving what the overall demand
23 is for your products or dairy products in
24 general, it's kind of fuzzy. You can't say
25 that the increase in the cost of milk is going

1 R. Waldron - Cross - by Mr. Tosi
2 to change what the consumers are going to pay
3 for it in the end?

4 A. Well, we don't have an explicit
5 economic model that models the entire value
6 chain of dairy starting with the dairy farmers
7 to the handlers to the end consumer. We know
8 our perspective though and what we must do to
9 help keep expanding our product portfolio.

10 What we see is the expansion of the
11 industry portfolio and price sensitivity is
12 high on our list. Sometimes we have to absorb
13 that price and other times when we get
14 favorability in the dairy markets, then we
15 transfer that into consumer communication
16 vehicles like TV, out into the world. So they
17 are a weakened link pretty clearly, price
18 sensitivity studies to the volume and demand
19 for our products, but we do not have a full
20 value chain equation built out.

21 Q. But that concern is more between the
22 product that you're making at retail versus the
23 product that you're making and what the cost of
24 milk is that contains dairy products?

25 A. Correct, but the cost of milk we are

1 R. Waldron - Cross - by Mr. Wilson
2 paying back to the dairy farmers is obviously
3 an important part of that equation.

4 Q. Do you know what percent of what
5 you're selling your product like Nouriche, what
6 percent of that price is actually returned to
7 dairy farmers?

8 A. I don't know that exact number.

9 MR. TOSI: That's all I have.
10 I have a couple of colleagues that might like
11 to ask you some other questions. I would like
12 to say that I'm a regular buyer of Nouriche. I
13 think it's very expensive.

14 MR. ANDERSON: Remember, we
15 put it out at one price and then there is other
16 margins added to it.

17 JUDGE DAVENPORT: Let's take
18 our morning break at this time. Let's take ten
19 minutes and be back at 10:10.

20 (Short recess taken.)

21 JUDGE DAVENPORT: We are back
22 in session. Ms. Carter, is it going to be you
23 or Mr. Wilson?

24 MR. WILSON: It will be me.

25 -----

1 R. Waldron - Cross - by Mr. Wilson

2 CROSS-EXAMINATION

3 BY MR. WILSON:

4 Q. Todd Wilson, USDA. Good morning,
5 gentlemen. In reading some of the testimony
6 that you had in response to your proposal, I
7 would like to go over some of the terms and
8 some of the specifications that are in both
9 your testimony and in your proposal as issued.
10 Could you define for us the term "drinkable
11 food products"?

12 A. Define drinkable food products?

13 Q. Yes, sir.

14 A. A less friendly word that we used to
15 use at General Mills was liquid meal systems.
16 That was generally the concept. I don't know
17 if you have heard that, but liquid meal systems
18 is really the term that initiated our thinking
19 behind the whole meal replacement strategy for
20 Nouriche which was our first yogurt smoothie
21 and now is drinkable food products is a food
22 that literally is portable, and it is generally
23 in a format that tends to be in a manner that
24 passes over the tongue very quickly. That's
25 usually done in a bottle, so a lot of people

1 R. Waldron - Cross - by Mr. Wilson
2 will say well, this is yogurt, but it's
3 drinkable. So we kind of reclassified
4 ourselves from liquid meal systems to drinkable
5 food products.

6 Q. Does it have to have a lot of
7 different ingredients in it? The reason I'm
8 asking --

9 A. Let me try this. We have found in
10 the United States marketplace, most
11 beverages -- I will say fluid milk has a slight
12 differentiation, but most beverages are
13 refreshing, the sodas of the world, the orange
14 juices or juices in general, most of them are
15 refreshing. Milk is more of a complement to a
16 meal.

17 Then what we are trying to do is
18 provide people a meal that is handheld, that
19 you can hold the steering wheel in one hand and
20 basically eat in another hand and a drinkable
21 format comes to play as a very convenient way
22 that people recognize. Those particular
23 products generally have a food item as the
24 characterizing agent whether it be yogurt or
25 yogurt and fortification.

1 R. Waldron - Cross - by Mr. Wilson

2 Q. Is milk a drinkable food product?

3 A. We think milk is a complement to a
4 meal. Quite honestly, consumers tell us milk
5 is milk and milk is the category of milk.
6 That's probably the greatness of milk.

7 Q. The only reason I'm asking these
8 questions is the section of the order that we
9 are dealing with here is a definitional
10 section, but yet it seems like we are putting
11 in another term that we might have to further
12 identify or further define.

13 A. We would say for the record milk is
14 not a drinkable fluid product. I hate to say
15 this, but we simply respond to what consumers
16 tell us. Milk is milk, and it is a
17 classification in and of itself and that our
18 drinkable food products are more on the basis
19 of base uses themselves. They are used in and
20 of themselves more like a snack or a mini meal.

21 MR. SHAPIRO: I think perhaps
22 to sort of refine that, that's one of the
23 reasons we included a 20-percent standard so
24 dairy is a characterizing ingredient in the
25 product.

1 R. Waldron - Cross - by Mr. Wilson

2 MR. WILSON: Under your
3 definition, chocolate milk might be a drinkable
4 food product, but yet it would not have yogurt
5 or it might not --

6 MR. SHAPIRO: I don't think we
7 would characterize chocolate milk as a
8 drinkable food product.

9 MR. WALDRON: I think we would
10 categorize that as milk that is chocolate once
11 again in the milk category.

12 MR. WILSON: In your proposal,
13 you have 2.2 percent as a compositional number.
14 Can you elaborate maybe how you arrived at that
15 number?

16 MR. SHAPIRO: Sure. Similar
17 to the milk research proposal, it's a rough
18 conversion from the 6-1/2 nonfat milk solids.
19 Based on 2.25, we just rounded down to 2.2.

20 MR. WILSON: So the difference
21 in Proposal 7 and yours is merely a rounding
22 difference?

23 MR. SHAPIRO: I think to get
24 to a number. Now, when you begin discussing
25 what is included in that number --

1 R. Waldron - Cross - by Mr. Wilson

2 MR. WILSON: I'm just talking
3 about the number itself, the 2.25 versus the
4 2.2.

5 MR. SHAPIRO: Correct, just
6 the number, but the discussion about whey is a
7 significant difference.

8 MR. WILSON: In your proposal,
9 you have listed as 2.2 percent "skim milk
10 protein." Can you identify what that would be?

11 MR. SHAPIRO: I would admit
12 that I don't have the expertise to define that.

13 MR. WILSON: If I listed some
14 products, could you identify whether or not
15 they would be skim milk protein or not?

16 MR. SHAPIRO: I don't think
17 so.

18 MR. WILSON: Would fluid milk
19 be skim milk protein?

20 MR. SHAPIRO: I don't know.

21 MR. WILSON: You also have a
22 composition of 20 percent yogurt, and I'm
23 reading from the hearing notice, it seems like
24 in your testimony there was a little bit of a
25 difference so we might talk about that, too.

1 R. Waldron - Cross - by Mr. Wilson

2 In the hearing notice, it says 20
3 percent yogurt, (nonfat yogurt, low fat yogurt
4 or yogurt by weight). First of all, it says
5 2.2 percent of protein provided the product
6 contains, so in your scenario it would have to
7 meet both 2.2 and the 20-percent yogurt
8 composition standard.

9 MR. SHAPIRO: That's correct.

10 MR. WILSON: By weight, can we
11 go through that computation for clarification
12 of how you would compute that?

13 MR. SHAPIRO: We can certainly
14 try.

15 MR. WILSON: In your exhibits,
16 if you have a bottle of Nouriche and it has a
17 certain level of yogurt containing in it;
18 correct?

19 MR. SHAPIRO: It does. The
20 exact amount we wouldn't have.

21 MR. WILSON: I know. Let's
22 say it's a 100-gram bottle for simplicity sake.
23 You're saying it would have to have 20 grams of
24 yogurt weight in it or, conversely, yogurt
25 equivalent? In other words, is my

1 R. Waldron - Cross - by Mr. Wilson
2 understanding -- and maybe I need to ask this
3 question first -- in the process of yogurt,
4 from 100 pounds of milk to make yogurt, how
5 much yogurt do you get? Do you get 100 pounds
6 of yogurt or do you have some type of yield?

7 MR. WALDRON: You're talking
8 to nontechnical experts up here for the
9 manufacturer of a product. I'm looking to the
10 back of the room and not getting a head nod in
11 any direction, so I want to suggest to you that
12 we don't feel comfortable giving you a correct
13 answer here.

14 We use a lot of fluid milk, and we
15 culture that milk in our yogurt. That's what
16 happens in our marvelous plants. Your line of
17 questioning, the ingredient panel is listed by
18 the weight and percentage of the weight in the
19 product, so it is my understanding that that
20 would be at least 20 percent of the weight of
21 the product or would be the characterizing
22 agent of yogurt.

23 We believe 20 percent, and this is
24 from our knowledge of characterizing agents in
25 the cereal category and other categories also

1 R. Waldron - Cross - by Mr. Wilson
2 that 20 percent provides the minimum that
3 consumers then classify that product by that
4 ingredient type. That's why we chose that
5 standard.

6 I think then it would also prevent
7 somebody from culturing .05 percent yogurt, for
8 example, of a product and then someone trying
9 to classify it as a yogurt smoothie. That's
10 why we try to come up with a level that we
11 believe from a consumer end point is
12 characterizing.

13 BY MR. WILSON:

14 Q. On a different line of questioning
15 here, the raw milk that you use or you might
16 use in your yogurt products, and I'm really not
17 differentiating between yogurt smoothies and
18 cup yogurt, just in yogurt in general, do you
19 have a sense of added value sense to the
20 proteins you buy from producer's milk?

21 A. A sense of the value that is
22 inherent with the milk that we buy? Is that
23 your question?

24 Q. The value of the protein in the milk
25 as a component that increases your meal,

1 R. Waldron - Cross - by Mr. Wilson
2 increases the favor of the products, increases
3 the texture of the products. Is protein a
4 valuable ingredient as it comes from the milk?

5 A. Let me answer it this way, and I
6 hope to answer your question for you. I'll try
7 my best. We have experts at product
8 formulation that rely on their creativity and
9 wisdom and experience with dairy products to
10 make us the products that consumers are
11 expecting to taste once they have told us that
12 a concept of the mind that we have presented to
13 them is something they want to buy. They will
14 then use milk and whatever ratio of ingredients
15 to try to deliver upon that expected or
16 anticipated expectation of what the product
17 will taste like.

18 Sometimes the milk protein or the
19 protein inherent with the milk becomes a
20 characterizing agent either in a nutritional
21 profile delivery or in taste, texture.
22 Sometimes added whey in a relationship to the
23 natural milk can do that, so it really depends
24 upon what the end user wants. Then we back up
25 from there can we deliver it and how do we

1 R. Waldron - Cross - by Mr. Wilson
2 deliver it?

3 In some of those circumstances, the
4 protein of the milk will play a different role
5 in the delivery of that end product hopefully
6 making it successful, hopefully expanding the
7 market.

8 Q. One last question. You talked about
9 form and use a lot in your testimony and that
10 it's an inherent characteristic of the Act that
11 we operate under. I asked this question
12 before, and I will ask it again of you guys.
13 Sometimes those two terms can be at differing
14 results. Do you see one taking more of a
15 priority over the other or less of a priority?

16 MR. SHAPIRO: I think if there
17 were to be a priority, probably use would, for
18 lack of a better word, trump form. That is
19 just, I think, a way of how we start with
20 determining what products we are going to
21 offer. We start with how are you going to use
22 it? What are you going to use it for?

23 MR. WILSON: So the
24 composition standards that your proposal
25 includes are to aid?

1 R. Waldron - Cross - by Mr. Wilson

2 MR. SHAPIRO: I think we would
3 say form and use collectively. You were asking
4 if you had to pick one?

5 MR. WILSON: Sometimes the
6 form of the product might dictate that it
7 exceeds or doesn't exceed 2.2 percent, but yet
8 the use of it is in line with a product that is
9 opposite on that level.

10 As in your testimony earlier about
11 orderly marketing in a lot of products and
12 handlers' relationships, which of those two
13 scenarios do you view as being more or less
14 important or do you view either one as more or
15 less important?

16 MR. WALDRON: We are a small
17 yogurt company in the world of a lot of big
18 milk manufacturers here and what we would say
19 is orderly market for us would be that which if
20 we are making a drinkable form of yogurt is
21 priced in line with the base yogurt itself so
22 that incentives for us to keep expanding the
23 market for yogurt consumption is rational.

24 The form and use argument we would
25 hold for you guys to come back to us and say

1 R. Waldron - Recross - by Mr. Beshore
2 what is appropriate, but we tend to think of
3 use first and yogurt is tended to be used as
4 food, and we are just looking for kind of
5 uniformly across yogurt products.

6 MR. WILSON: That's all I
7 have.

8 JUDGE DAVENPORT: Mr. Beshore?

9

10 RECROSS-EXAMINATION

11 BY MR. BESHORE:

12 Q. Thank you. Marvin Beshore for Dairy
13 Farmers of America. One question with respect
14 to consumer price elasticity. You made some
15 mention of that. With respect to, for
16 instance, the Nouriche product, what does your
17 data show with respect to the change in price
18 that shows a measurable consumer response? For
19 instance, would a ten-percent change in that
20 product price lead to a consumer response in
21 terms of demand for the product?

22 A. We have extensive price sensitivity
23 studies that I would prefer not to put out in a
24 public forum. I would be glad to share that
25 with the USDA in a confidential setting. I

1 R. Waldron - Recross - by Mr. Beshore
2 would hope that it would be delayed after this
3 testimony to make sure that it stays
4 confidential .

5 We do know that the basic law of
6 supply and demand works with regard to pricing.
7 As we take our pricing up, it does have a
8 negative impact on the sales of our Nouriche
9 product.

10 What I would tell you though is
11 sometimes we are able to price and sometimes we
12 are not. As long as it is a situation that
13 input costs go up and we are unable to price,
14 we have to absorb that loss of either margin or
15 to us more importantly, what has made General
16 Mills great is a focus on consumer marketing
17 and we often have to pull back on those
18 consumer marketing levers which ultimately is
19 limiting our ability to expand that particular
20 market segment, and it provides question to our
21 ability to do more innovation in that segment
22 or area of the market.

23 Q. I just want to explore whether there
24 is any information with respect to price
25 sensitivity that you can provide without

1 R. Waldron - Recross - by Mr. Beshore
2 violating your proprietary concerns, and I just
3 threw out ten percent as possibly a
4 nonproprietary level that was sufficiently
5 generic that you could say something about it.
6 I guess you can't.

7 A. We have in-market studies
8 extraordinaire I would say. We know the exact
9 relationship, and I will not be sharing that in
10 a public forum.

11 Q. Let me try it on the other end of
12 the spectrum. Do your studies show whether
13 movement in the retail price of a product like
14 Nouriche at \$1.82 average price whether
15 movements of a penny one way or the other are
16 detectable at the consumer response level?

17 A. We have information that allows us
18 to actually go down to the account level. Now
19 per penny or not, we tend not to do exact
20 measures of that but more about what
21 realistically happens in the marketplace, and I
22 will tell you that higher prices lead to lower
23 volume.

24 Q. Can you tell us then realistically
25 what is the increment that you collect data on,

1 R. Waldron - Recross - by Mr. Beshore
2 the increment of price change? I take it
3 yogurts don't move penny by penny on the shelf?

4 A. Well, again it depends really. The
5 pricing is dictated by the retailer on the
6 shelf. We set a price, and that is
7 differentiated by every retailer and even
8 within retailers they have pricing zones that
9 change by marketplace, and we are simply not
10 able to control that nor do we want to.

11 I don't want to go to jail for any
12 Robinson-Patman violations. We can tell the
13 details and what I am trying to communicate is
14 I will not be going through that detail today.

15 Q. So there is no minimum increment
16 that your data is based on in terms of price
17 changes per unit, retail price changes per
18 unit?

19 A. We view the data and aggregate the
20 real live data that's out in the marketplace,
21 so whatever increments are happening in the
22 marketplace AC Nielsen helps us analyze and
23 pick up those increments.

24 Q. Just one other area. I'm not sure
25 that I understand your concerns with respect to

1 R. Waldron - Recross - by Mr. Beshore
2 whether whey should be counted or not versus
3 the status quo. You don't want to count whey
4 because it's not as valuable as other proteins.
5 I take it that was the purpose of one of your
6 charts which shows the different functional
7 characteristics of whey versus casein; is that
8 correct?

9 A. That was part of the explanation,
10 but also it gets back into some of the
11 explanation I was just talking about the
12 functional characteristics of using different
13 components in our proprietary recipes to
14 deliver upon what the consumer is expecting in
15 the product formula itself and ultimately the
16 product experience.

17 Q. In supporting the status quo which
18 values from the producer's perspective, which
19 values all nonfat solids, lactose and all
20 proteins at the same value, do you understand
21 that they have widely different marketplace
22 values, lactose versus protein? Do you
23 understand that?

24 A. Yes. I just hope you understand
25 that we support no change. That is our first

1 R. Waldron - Recross - by Mr. Beshore
2 proposal, but if a change, if USDA decides to
3 make a change, then that is the proposal we
4 have put forth with the exclusion of added whey
5 plus a minimum characterizing standard of 20
6 percent for yogurt. I hope that's clear.

7 Q. That is clear, but just so you
8 understand, in supporting no change as far as
9 dairy farmers are concerned, you are supporting
10 a definition which values a pound of lactose at
11 the same value as a pound of protein which the
12 market says is worth ten times as much. Do you
13 understand that's how dairy farmers' product is
14 priced under the present standard which you are
15 advocating?

16 A. Our first proposal is no change.

17 MR. BESHORE: That's all.

18 JUDGE DAVENPORT: Mr. Vetne?

19 -----

20 RECROSS-EXAMINATION

21 BY MR. VETNE:

22 Q. John Vetne, counsel for Hood. In
23 response to a question from Mr. Beshore on
24 demand elasticity, you indicated that higher
25 prices lead to lower volume. Let me make sure

1 R. Waldron - Recross - by Mr. Vetne
2 I'm clear and the record is clear what you mean
3 by that.

4 When consumers respond to a higher
5 price by buying less, it doesn't mean that the
6 volume necessarily of the product sold goes
7 down from one point in time to another. It
8 could also mean that the rate of growth has
9 slowed; am I correct?

10 A. That could be true in a generic
11 sense, sure. The price sensitivity that I was
12 speaking to was specific to Nouriche smoothie
13 which I felt I was the answering the question
14 to versus I sense your question is more
15 theoretical.

16 Q. It's more general, and it calls upon
17 you perhaps in your experience with more than
18 just smoothies but General Mills products or
19 Yoplait products.

20 A. It is a general question that I will
21 answer with my general background being from
22 multi-categories in General Mills is that
23 generally your statement would be true.

24 Q. Does General Mills produce or
25 co-pack yogurt in the west outside of the

1 R. Waldron - Recross - by Mr. Vetne
2 federal marketing order area?

3 A. We have a manufacturing facility in
4 California.

5 Q. All of the products that are
6 produced containing yogurt are Class II in
7 California?

8 A. I believe so.

9 Q. Does Yoplait produced elsewhere in
10 the country that is from federal order milk
11 compete with beverage yogurts produced in
12 California other than Yoplait's own brand?

13 A. Can you repeat the question?

14 Q. Does Yoplait products produced
15 elsewhere in the country other than California
16 compete with California-produced yogurt
17 beverages?

18 A. There are no beverages from the
19 Yoplait portfolio produced in California at
20 this time. One, because we don't have
21 beverages; we have smoothies.

22 Number two is that we don't
23 currently manufacture any of our smoothies in
24 California, but the question is yes, those
25 products produced under the federal milk order

1 R. Waldron - Recross - by Mr. Vetne
2 would compete with products produced from our
3 California location.

4 Q. My apologies for confusing the
5 record with my use of the term "beverages."
6 Let me refine that to mean yogurt products that
7 pour that you can hold in one hand and drive
8 with the other. Are any of those produced in
9 California?

10 A. No.

11 Q. Including Nouriche?

12 A. Correct.

13 Q. But the pourable Yoplait products
14 are distributed nationally including
15 California?

16 A. Correct.

17 Q. And they compete in California and
18 much of the west with pourable yogurts that are
19 produced in California?

20 A. Well, they are on the retail shelf
21 in California. I do not know of other yogurt
22 smoothies made in California. There may be the
23 potential of one private label in Northern
24 California that is produced in California, but
25 I do not know the exact location of the

1 R. Waldron - Recross - by Mr. Vetne
2 manufacturing center.

3 Q. Do you have competitors that
4 produce, for example, beverages containing
5 pourable forms of yogurt in Utah which is not
6 federally regulated?

7 A. Yes.

8 Q. Perhaps it's just that I'm confused,
9 and I fear that the record may also be
10 confused. When I previously asked questions,
11 my recollection is that I received an answer to
12 the effect that some, one or more of the
13 pourable yogurt-containing products produced by
14 your company is or are in Class I and others is
15 or are in Class II. Your responses to
16 questions from the government and, I think,
17 Mr. Yale or Mr. Beshore later suggested to me
18 that there are no products in pourable form
19 that are Class I at the current time. Which is
20 correct?

21 A. Legal counsel for General Mills came
22 up and corrected my previous statement. We did
23 have a drinkable yogurt in Class I that later
24 was changed to Class II. The actual story is
25 that it was initially sent to market as a Class

1 R. Waldron - Recross - by Mr. Vetne
2 II product, was changed to Class I and then
3 changed back to Class II.

4 That was my confusion, and that's
5 why the testimony later was corrected to put it
6 on the record that these are Class II products.

7 Q. So currently they are all Class II?

8 A. Correct.

9 Q. That is a product that is still
10 being produced and marketed?

11 A. Correct.

12 Q. And was there any change in the
13 formulation of that product which resulted in
14 the change in classification?

15 A. Not to my knowledge, no.

16 Q. Was that product when it was moved
17 at some point to Class I moved there because of
18 the 6.5 percent solids nonfat standard in the
19 rules?

20 A. I don't know the exact details of
21 why it was moved to Class I.

22 MR. SHAPIRO: I think
23 specifically the product you're talking about
24 that our formulation is proprietary. Our
25 discussions with USDA were confidential. I

1 R. Waldron - Recross - by Mr. Vetne
2 think our preference would be to keep it that
3 way.

4 MR. VETNE: My question was
5 simply whether the 6.5 percent solids nonfat
6 standard in Section B was at issue and
7 interpreted?

8 MR. SHAPIRO: Yes, and I would
9 refer you to my previous response.

10 BY MR. VETNE:

11 Q. Similarly, will you tell us for the
12 record whether the use of the product as a meal
13 replacement played any role in USDA's
14 reclassification and interpretation of its own
15 rules?

16 A. I was not in those specific meetings
17 so I cannot respond to that.

18 Q. Can others on the panel?

19 MR. SHAPIRO: I think you
20 might have to ask the USDA about their
21 interpretation, but use of the product, actual
22 market use of the product was a part of that
23 discussion.

24 MR. VETNE: When the product
25 was classified into Class I, did Yoplait

1 R. Waldron - Recross - by Mr. Vetne
2 receive a letter from USDA explaining why that
3 was being done?

4 MR. SHAPIRO: I don't know.
5 We may have. It's a big company.

6 MR. VETNE: When the product
7 was brought back into Class II, did Yoplait
8 receive a letter from USDA?

9 MR. SHAPIRO: Yes. I did
10 receive a confirmation letter.

11 MR. VETNE: Can you tell us
12 the approximate time that the classification
13 from I back to II happened?

14 MR. SHAPIRO: To the best of
15 my recollection, I received a letter last
16 February of 2004, I believe. I'm not certain
17 when I received the letter to be honest with
18 you. I believe it was last February.

19 MR. VETNE: The reference in
20 your testimony to various presentations to
21 USDA, did those presentations precede your
22 receipt of that letter?

23 MR. SHAPIRO: Yes.
24 Presentations took place, to the best of my
25 knowledge, before the receipt of that letter,

1 R. Waldron - Recross - by Mr. Vetne
2 and I'm not sure if further discussions took
3 place. We are in constant communication with
4 them, as you can imagine.

5 MR. VETNE: Were those
6 presentations to the USDA in the Washington
7 offices of USDA?

8 MR. SHAPIRO: They were all
9 throughout. They were in Washington as well as
10 outside of Washington.

11 MR. VETNE: As well as in the
12 market administrator's office?

13 MR. SHAPIRO: That's correct.

14 MR. VETNE: And that would be
15 the market administrator's office for what
16 market?

17 MR. SHAPIRO: I know the
18 market, but I would prefer not to say.

19 MR. VETNE: Thank you.

20 JUDGE DAVENPORT: Other cross?
21 Ms. Carter?

22 -----

23 CROSS-EXAMINATION

24 BY MS. CARTER:

25 Q. Antoinette Carter with the USDA.

1 R. Waldron - Cross - by Ms. Carter

2 Good morning. I believe my colleague had a
3 question with regards to the skim milk protein
4 and what is included in that. I'm going to
5 attempt to rephrase that question.

6 In your statement, you specifically
7 indicated that should a protein standard be
8 recommended for adoption that whey protein or
9 whey protein solids be excluded from the
10 categorization of the standard. Do you have a
11 position on other dairy solids such as milk
12 protein concentrate in terms of including or
13 excluding other dairy solids in the calculation
14 of the standard?

15 MR. SHAPIRO: I guess I would
16 answer that two ways. First, to start we
17 believe the defining characteristic of our
18 product to be yogurt and that with respect to
19 form and use that our products should be
20 classified as such. As far as what is
21 included, our concern with including
22 dairy-derived proteins, they are used as added
23 protein. They are added in to get up to the
24 protein content.

25 Our concern would be that the

1 R. Waldron - Cross - by Ms. Carter
2 inclusion of that might lead to manufacturers
3 seeking alternative non-dairy based proteins,
4 and it is our preference as a company to
5 continue to source dairy, all dairy all the
6 time.

7 MS. CARTER: Just to clarify,
8 are you stating that other dairy solids or
9 proteins besides whey or including whey should
10 be excluded from the calculation?

11 MR. SHAPIRO: Our position is
12 specific to whey. With respect to MPCs,
13 et cetera, I don't know if we have a position.

14 MS. CARTER: If I could
15 reference you to page 5 of your statement.
16 It's under the subheading General Mills Protein
17 Proposal.

18 The 20-percent yogurt standard by
19 weight, how was that derived? What is the
20 basis for that 20-percent standard?

21 MR. SHAPIRO: How did we end
22 up with that?

23 MS. CARTER: Yes.

24 MR. SHAPIRO: Again, as a
25 characterizing ingredient, Anderson can

1 R. Waldron - Cross - by Ms. Carter
2 probably talk more about what consumers use a
3 characterizing ingredient, but we do start with
4 yogurt, culturing yogurt and the yogurt that we
5 refer to standard identity yogurt with the
6 cultures, the consumers identify as this being
7 a yogurt product so we came up with the 20
8 percent as that defining characteristic.

9 MR. WALDRON: Some of that is
10 our knowledge of other categories also with
11 consumer resource, cereal, granola, other
12 categories that allows us to say that 20
13 percent usually with the end consumer is a
14 characterizing ingredient that we can call
15 something by a cereal or with oats, it is oat
16 based, it is yogurt based, so that's where we
17 came up with that specific number.

18 MR. ANDERSON: As Bob was
19 saying here, anything really below that, our
20 experience in many categories is that once you
21 fall below that minimum level, consumers begin
22 to reject the product and see it as
23 masquerading as being something that it really
24 isn't.

25

1 R. Waldron - Cross - by Ms. Carter

2 BY MS. CARTER:

3 Q. Again, under that subheading, you
4 have indicated the standard of identity for
5 milk in terms of it containing 8.25 percent
6 milk solids. Is that the standard identity
7 under FDA regulations?

8 A. That's my understanding, yes.

9 Q. I believe there were some questions
10 earlier with regards to the role of Federal
11 Milk Marketing Orders. In your opinion, what
12 the role of FDA?

13 A. We would prefer to leave the role of
14 classifying products up to USDA.

15 Q. Just to kind of rephrase that, in
16 your opinion, should FDA regulations be
17 considered in product classifications that are
18 done under the Federal Milk Marketing Order
19 Program?

20 MR. SHAPIRO: Generally
21 speaking, FDA is the agency that has defined
22 what certain products are called. When we make
23 yogurt, we are formulating yogurt to the
24 standard of identity as established by FDA. As
25 such, fluid milk, the standard of identity of

1 R. Waldron - Cross - by Ms. Carter
2 milk, I guess, would be determined by looking
3 at what FDA has defined as milk.

4 As far as classifying which products
5 in class with other products as far as how they
6 compete with one another in the marketplace,
7 that's for you all to determine and we are
8 quite happy with that.

9 Q. On page 6 of your statement which is
10 under the same subheading, you reference a
11 20-percent variance. You indicate that both
12 USDA and FDA recognize this variance level as
13 it pertains to nutritional labeling. What USDA
14 agency are you referring to there in that
15 statement?

16 A. I don't know the exact agency of the
17 USDA. I'm sure someone in the room would, but
18 I do not know the exact agency. To be clear,
19 the main goal of our manufacturing process is
20 to produce the same product, the same grade
21 product every time it comes off the line.

22 We put a great deal of resources
23 into consistency of production; but with any
24 manufacturing production, particularly with
25 ours which is a live and active environment

1 R. Waldron - Cross - by Ms. Carter
2 because of our cultures, there can be process
3 variation, but that is not the goal, just
4 making sure that a normal small percentage of
5 variation does not dominate the way products
6 are classified.

7 Q. In terms of how that variance is
8 administered under FDA regs and the other USDA
9 agency or program, that variance, how is that
10 administered? Can you comment on that?

11 A. I will speak briefly to it from my
12 indirect relationship with quality control, so
13 to speak, but our plants are regulated and
14 routinely monitored and production samples are
15 tested and measured to see if we are within
16 specs. We work very strongly with the
17 government regulators to make sure that our
18 plants are always in compliance.

19 If there are any issues, we are
20 given a short time period to fix those issues
21 which we do to make sure we are back to
22 producing a consistent product every time. So
23 it's a routine basis having people in our
24 plants from a government agency that is
25 monitoring our production.

1 R. Waldron - Cross - by Ms. Carter

2 MS. CARTER: That's all I
3 have. Thank you.

4 JUDGE DAVENPORT: Is there any
5 other cross of these witnesses? Very well.
6 Thank you for appearing here today. You may
7 step down. At this time I would like to call
8 on Mr. Logan representing the Ohio Farmers
9 Union.

10 MR. YALE: Your Honor, with
11 regard to the testimony that has just been
12 done, there have been a lot of comments that we
13 ask the Department look at, you know,
14 confidential records and things like that, and
15 I know some of this is out of a
16 misunderstanding of the process; but this has
17 to be on the record that we would request a
18 statement on the record from the Department
19 that they will not consider any of that
20 information and, alternatively, we would move
21 to strike any request that they consider that
22 information and that information not be
23 considered.

24 MR. BESHORE: I join in
25 Mr. Yale's request.

1 R. Waldron - Cross - by Ms. Carter

2 MR. STEVENS: Your Honor, I'm
3 Garrett Stevens from the General Counsel Office
4 U.S. Department of Agriculture. With respect
5 to the comments of counsel on the state of the
6 record, certainly this hearing, this
7 rule-making proceeding like every proceeding
8 conducted in formal rule making under the
9 Agricultural Act of 1937 is a decision based on
10 the record made in the hearing and is not based
11 on other data and material which is not part of
12 this record.

13 JUDGE DAVENPORT: Is that
14 satisfactory, Mr. Yale, or Mr. Beshore?

15 MR. YALE: That is
16 satisfactory.

17 MR. BESHORE: Yes.

18 JUDGE DAVENPORT: Thank you.

19 (Exhibit No. 27 was marked for
20 identification.)

21 JUDGE DAVENPORT: Mr. Logan,
22 you have given me a statement. That statement
23 is now being marked as Exhibit No. 27. Are you
24 prepared to enter this into the record?

25 MR. LOGAN: Certainly. Thank

1 J. Logan - Direct Testimony

2 you, sir.

3

4

JOSEPH LOGAN

5

a witness herein, having been first duly sworn,

6

testified as follows:

7

DIRECT TESTIMONY

8

MR. LOGAN: Once again, my

9

name is Joe Logan speaking on behalf of the

10

Ohio Farmers Union.

11

Fresh wholesome milk has helped to

12

sustain human species for many thousands of

13

years. No other food product enjoys such a

14

wholesome nurturing connotation than fresh

15

fluid milk.

16

That impression carries a tremendous

17

marketing value and dairy farmers and

18

processors have spent millions of dollars

19

annually to support and preserve that positive

20

image of milk as a healthy beverage option.

21

That said, it seems unimaginable

22

that any serious consideration would be given

23

to tampering with the definition of a product

24

with such an overwhelmingly positive

25

perception. In fact, I have personally heard

1 J. Logan - Direct Testimony

2 Dr. Lester Crawford now heading the FDA comment
3 that only God could change the definition of
4 milk and that his ancestors would turn over in
5 their graves if such a change were to be
6 contemplated. Yet, we stand here today in
7 legitimate consideration of precisely that
8 action.

9 Innumerable wise and practical
10 people have adopted an often heard mantra "If
11 it isn't broke, don't fix it." Despite all of
12 the reasons not to fix a definition which is
13 obviously not broken, our governmental agencies
14 seem dedicated to making changes to accommodate
15 the wishes of dairy processors and marketing
16 industry by changing the meaning of the term
17 "milk."

18 We understand that flexibility and
19 ingredient formulation is a serious matter
20 affecting productivity and efficiency in the
21 food and beverage processing industry. We have
22 no opposition to the industry having the
23 latitude to reconfigure and reformulate
24 products as they see fit, but we do have grave
25 concerns about the industry's current proposals

1 J. Logan - Direct Testimony

2 which would legitimize production and marketing
3 of products made from a wide variety of
4 ingredients sourced from locations across the
5 globe and all under the name plate of fluid
6 milk.

7 We encourage new product development
8 in the food and beverage processing industry,
9 but we urge that those creative efforts be
10 combined with corresponding efforts on the
11 marketing side in order to create new demand
12 for those new products in their own rights,
13 thus expanding the total market for food and
14 beverages.

15 We believe it is wise, however, to
16 be respectful of the generations of dairy
17 producers and marketers who have dedicated
18 their entire working lives to the development
19 and maintenance of consumer confidence in milk.
20 The current definition of milk already allows a
21 great latitude for processors to supplement or
22 remove dairy derivatives from milk products and
23 any further broadening of this definition or
24 interpretation only serves to signal the
25 industry that any fractionation or

1 J. Logan - Direct Testimony

2 recombination of dairy-derived ingredients can
3 pass as a milk product.

4 In our view, the proposals under
5 consideration would seriously undermine the
6 accumulated store house of consumer confidence
7 in milk products and at the same time the
8 proposals would encourage processors to
9 incorporate a wider array of dairy-derived
10 compounds into products marketed as milk.

11 The domestic dairy processing
12 industry has already demonstrated a voracious
13 appetite for low cost imported dairy
14 ingredients, so let's not allow the industry's
15 quest for low cost supplements undermine the
16 consumers' confidence in fluid milk.

17 The primary purpose of the Federal
18 Milk Marketing Order Program is to provide
19 American consumers with reliable, safe supplies
20 of wholesome milk while assuring producers
21 uniform marketing standards, fair weights and
22 measures.

23 The proposals under consideration
24 would breach the compact with both consumers
25 and producers by allowing the inclusion of milk

1 J. Logan - Direct Testimony

2 protein concentrates, caseinates and whey
3 proteins.

4 These compounds are understood to
5 have functional and nutritional characteristics
6 which are different from those of fresh milk,
7 so consumers must be justifiably concerned.
8 Domestic dairy producers, meanwhile, would find
9 themselves competing for the local fluid milk
10 market with ingredients from all corners of the
11 world and some produced under all imaginable
12 sanitary and phytosanitary standards.

13 Beyond the betrayal of consumers and
14 dairy producers, these new proposed rules could
15 potentially expose taxpayers to additional
16 liabilities under the Federal Dairy Price
17 Support System by encouraging additional dairy
18 ingredient imports.

19 In summation, the Ohio Farmers Union
20 has no problem with new product development,
21 but we do have problems with trying to market
22 those new formulations under the name plate of
23 milk. As mentioned before, jeopardizing the
24 long established perception of milk as a fresh,
25 pure wholesome beverage would be

1 J. Bunting - Direct Testimony

2 counterproductive for consumer confidence and
3 for the economic viability of domestic
4 producers. We would urge no change to the
5 statute.

6 JUDGE DAVENPORT: Are there
7 questions of this witness? Apparently there
8 are none. Mr. Logan, thank you for appearing
9 and giving us your statement. You may step
10 down. Mr. Bunting, why don't you come forward
11 at this time. Please tell us your name and
12 spell your last name for the hearing reporter.

13 MR. BUNTING: John Bunting,
14 B-U-N-T-I-N-G.

15 (Exhibit No. 28 was marked for
16 identification.)

17 JUDGE DAVENPORT: Mr. Bunting,
18 I have marked your statement as Exhibit No. 28.
19 Are you prepared to read it into the record?

20 MR. BUNTING: Yes, I am.
21 Thank you, Your Honor.

22 JUDGE DAVENPORT: Please
23 proceed.

24 -----
25

1 J. Bunting - Direct Testimony

2 JOHN BUNTING3 a witness herein, having been first duly sworn,
4 testified as follows:5 MR. BUNTING: My name is John
6 Bunting. I am a dairy farmer in Delaware
7 County, New York, and I also write for a dairy
8 publication. Today I'm testifying on behalf of
9 the National Family Farm Coalition in
10 opposition to amending the definition of fluid
11 milk.12 The NFFC was founded in 1986 and
13 represents family farms and rural groups in 30
14 states whose members face the challenge of
15 deepening economic recession in rural
16 communities caused primarily by low farm milk
17 prices and the increasing corporate control of
18 agriculture. The dairy subcommittee has
19 members from coast to coast.20 NFFC has taken an active role in the
21 dairy protein debate. NFFC submitted testimony
22 to the U.S. International Trade Commission
23 hearings on dairy proteins. NFFC submitted a
24 citizens' petitions to the Food and Drug
25 Administration (FDA) in April of 2004

1 J. Bunting - Direct Testimony

2 requesting the Food and Drug Administration to
3 notify state and federal regulators of GRAS
4 requirements of milk protein concentrates.

5 The context of this hearing is
6 particularly troubling in that it represents a
7 significant step backwards in the nearly
8 100-year struggle in an effort to gain public
9 confidence in the quality of dairy products.
10 Indeed, the language of 7 USC 608(c)18 states
11 the need to "insure a sufficient quantity of
12 pure and wholesome milk."

13 In 1934, under *Nebbia versus New*
14 *York State*, the United States Supreme Court
15 clearly stated that milk was clothed in public
16 interest. The court wrote "Thus, understood,
17 'affected with a public interest' is the
18 equivalent of 'subject to the exercise of
19 police power.'"

20 From the very beginning, the use of
21 milk protein concentrate has been a flagrant
22 violation of the public's interest and the rule
23 of law. In spite of the widespread usage,
24 there is no GRAS (generally recognized as safe)
25 for MPCs.

1 J. Bunting - Direct Testimony

2 According to the FDA, under Sections
3 201(s) and 409 of the Act, and FDA's
4 implementing regulations 21 CFR 170.3 and 21
5 CFR 170.30, "The use of a food substance may be
6 GRAS either through scientific procedures or
7 for a substance used in food before 1958,
8 through experience based on common use in
9 food."

10 MPCs were not used in food prior to
11 1958 and, therefore, subject to scientific
12 procedures in determining GRAS. Under a
13 Freedom of Information request response to me
14 on August 13, 2003, the FDA stated "We have
15 searched our files and find no responsive
16 information for the scientific studies" --

17 JUDGE DAVENPORT: No is not
18 present on your text.

19 MR. BUNTING: I'm sorry.
20 That's a typo, I'm certain. Let me find it in
21 the accompanying document. It will be there,
22 the statement from FDA.

23 JUDGE DAVENPORT: But that
24 should read "no" responsive information?

25 MR. BUNTING: Yes, it should,

1 J. Bunting - Direct Testimony

2 and there is a letter from FDA included. I'm
3 sorry.

4 JUDGE DAVENPORT: Very well.

5 MR. BUNTING: Let me start
6 with that again. "We have searched our records
7 and find" -- and this is a typo because I
8 omitted the no -- "no responsive information
9 for the scientific studies on human safety and
10 consumption of ultrafiltered milk/milk protein
11 concentrate."

12 There is one very good reason for
13 this. There is no definition for milk protein
14 concentrate. Nothing can be studied
15 scientifically which cannot be defined.

16 U.S. Customs made an attempt to
17 define MPCs and failed. In September 2002,
18 National Milk Producers Federation petitioned
19 customs for a definition. In Customs decision
20 we read:

21 "Many of the comments contend that
22 your position which limits coverage of the Note
23 to products produced by ultrafiltration is not
24 supported by the language of the Note. These
25 comments point out that when Congress was

1 J. Bunting - Direct Testimony

2 drafting the Note, it could have used
3 restrictive language to achieve the result you
4 urge. However, this was not done.

5 "These commenters state that in the
6 food industry the term "milk protein
7 concentrates" is commonly used to refer to a
8 wide variety of products of varying
9 composition. These products are manufactured
10 to specifications to render them suitable for
11 specific end uses in the food industry. In
12 addition, they point out that certain milk
13 protein concentrates are obtained by a
14 combination of ultrafiltration and blending
15 while other products contain milk proteins that
16 are isolated from milk by other processes such
17 as precipitation. They contend that products
18 containing 40 percent or more protein by weight
19 have more protein than milk and are thus milk
20 protein concentrates.

21 "They also note that if Congress
22 intended the provision to be limiting to the
23 total milk proteinate that was the subject of
24 previous Customs ruling, it would have enacted
25 the broad language of Additional Note 13 and

1 J. Bunting - Direct Testimony

2 would not have set the milk protein threshold
3 as low as 40 percent.

4 "Upon consideration of the petition
5 and the comments submitted, Customs agrees with
6 the comments received that the Note does not
7 restrict MPCs to any particular method of
8 manufacture. Rather, the note speaks to any
9 complete milk protein concentrate which
10 contains a specific protein percentage by
11 weight.

12 The use of the term 'any' suggests
13 that a broad rather than restrictive reading of
14 the Note was intended. The Note does not
15 require that the protein be complete which
16 according to the note requires that it contain
17 casein and lactalbumin.

18 However, the Note neither requires
19 that the protein be in the same proportion as
20 they are found in milk, nor does it specify
21 relative percentage of the protein components.
22 It only requires that the source of the protein
23 be milk, that casein and lactalbumin be present
24 and that they constitute 40 percent or more by
25 weight of the product." That's the end of the

1 J. Bunting - Direct Testimony

2 quote from Customs.

3 Clearly, the dairy industry wants to
4 be totally free and unrestricted in calling
5 anything it so chooses MPCs. Clearly, then we
6 are not talking about amending any definition
7 of milk. This hearing is in reality about
8 eliminating any definition of milk in the
9 interest of processor profit.

10 Under GRAS regulations, FDA allows
11 individual determination for each product
12 produced. This is not done because the sole
13 purpose of MPC use is because processors profit
14 from use of low cost ingredients. To test each
15 product would severely reduce or eliminate
16 profit. Therefore, all MPC use is a
17 reprehensible violation of the rule of law.

18 Making this matter even worse is the
19 tacit complicity of FDA in MPC use. While FDA
20 correctly states use of MPCs in standardized
21 products is illegal, they say use of MPCs in
22 nonstandardized products is allowed. FDA fails
23 to mention that GRAS certification is required
24 in nonstandardized products.

25 Certainly industry could correct

1 J. Bunting - Direct Testimony

2 this problem by clearly defining MPCs and
3 running scientific studies. The fact that this
4 could be done and has not been done suggests
5 that there may, indeed, be a dark unsafe side
6 to MPCs.

7 In addition to the troubling
8 disregard for GRAS regulations, these proposals
9 require the abandonment and tossing out of
10 Grade A pasteurized milk ordinance (PMO). The
11 PMO requires:

12 "Each dairy farm, milk plant,
13 receiving station, milk tank truck cleaning
14 facility and transfer station whose milk or
15 milk products are intended for consumption
16 within, of or its jurisdiction, and each bulk
17 milk hauler/sampler who collects samples of raw
18 milk for pasteurization, for bacterial,
19 chemical or temperature standards and hauls
20 milk from a dairy farm to a milk plant,
21 receiving station or transfer station and each
22 milk tank truck and its appurtenances shall be
23 inspected by the regulatory agency prior to the
24 issuance of a permit."

25 USDA Foreign Agricultural Service

1 J. Bunting - Direct Testimony

2 trade database lists over 40 countries which
3 have imported Chapter 35 dairy proteins which
4 casein, caseinates and casein MPCs.

5 Do those proposing the use of these
6 dairy-based products such as MPCs and
7 caseinates really expect farms in Belarus, the
8 Ukraine and the Peoples Republic of China will
9 be inspected by a qualified U.S. agency? That,
10 of course, would be preposterous.

11 M-A-83 Grade A powdered dairy blends
12 as ingredients, et cetera requires "If a
13 powdered blend is to be used as an ingredient
14 in the production of a Grade A product from an
15 IMS listed plant, the blend must be labeled
16 'Grade A' and the plants where the Grade A
17 dairy powders are manufactured and the facility
18 where the powder is blended and packaged must
19 have an acceptable IMS listing."

20 How do the proponents of these
21 proposals or USDA propose to guarantee that
22 powdered dairy blends and ingredients will be
23 sourced from PMO-approved sources?

24 From "nutrient content claim" to
25 labeling to the PMO definition of "concentrated

1 J. Bunting - Direct Testimony

2 milk," all of these and more would have to be
3 thrown out if the proposals advocating the use
4 of high protein products are incorporated into
5 the USDA Federal Milk Order rules and
6 regulations.

7 Anyone who might suggest limiting
8 these ingredients to only domestically-produced
9 products is sadly ignorant of the power of the
10 WTO (World Trade Organization). Rules
11 promulgated by the WTO are not as likely to be
12 ignored as U.S. rules.

13 Finally, there is the bottom line.
14 The federal orders are about payment. In the
15 May 2005 issue of Progressive Dairyman, Elvin
16 Hollon, a DFA vice president spoke of this
17 hearing.

18 The article said, referring to the
19 statement by Hollon, "The main emphasis is on
20 new forms of milk protein, like milk protein
21 concentrate that are used to create new fluid
22 products. Hollon says that if a farmer's milk
23 is to be used to make a product that competes
24 with Class I, then the farmer should be paid
25 for Class I."

1 J. Bunting - Direct Testimony

2 What farmers and where? All
3 indications are that MPCs cannot be paid
4 profitably in the U.S. MPC would dictate the
5 use of imported MPCs. Is anyone thinking
6 farmers in India or New Zealand would be
7 getting blend price for their milk?

8 Furthermore, as Mr. Hollon must
9 surely know, the domestic MPC-producing
10 Dairiconcepts plant in Portales, New Mexico
11 pays Class IV price for MPC production. The
12 USITC report Conditions of Competition For Milk
13 Protein Products in the U.S. Market,
14 investigation No. 332-453, mentions several
15 advantages of the Portales plant and says "Even
16 with these advantages, purchasers of MPC from
17 the Dairiconcepts facility still pay a premium
18 over the price of imported MPCs to provide the
19 facility with a return that is equivalent to
20 the return on SMP."

21 In reality, the bottom line is to
22 have MPCs accepted as just good old milk which
23 they are not. These proposals are merely
24 continuation of the deception associated with
25 the use of MPCs.

1 J. Bunting - Direct Testimony

2 A recent example of the deception is
3 found in a U.S. patent application, and I give
4 the number, which proposes the use of MPCs to
5 make cheese. We find not once but twice,
6 "Other GRAS (generally regarded as safe)
7 ingredients common to cheese-making process may
8 be added at any suitable stage."

9 Despite widespread claims, the
10 safety of MPCs to this day, they are not GRAS
11 and MPCs are not milk and have no place in the
12 definition of milk.

13 To summarize, I speak in opposition
14 to all proposals which would classify as Class
15 I (fluid) ingredients in the use of dairy-based
16 beverages which do not currently meet Federal
17 Milk Order requirements for 6.5 percent nonfat
18 dairy solids.

19 Milk protein concentrate does not
20 meet FDA safety rules under GRAS specifications
21 as legal food ingredients. Milk protein
22 concentrates are caseins, which are not
23 manufactured to any degree in the United States
24 are imported in vast quantities. The sources
25 of these foreign dairy ingredients do not meet

1 J. Bunting - Direct Testimony

2 U.S. Pure Milk Ordinance standards for Grade A
3 farm, plant and milk truck haulers, nor do
4 various daily personnel from such nations
5 comply with U.S. PMO rules.

6 If USDA were to implement these
7 proposals, there would be a revenue outflow
8 from the Federal Milk Order revenue pools to
9 foreign dairy producers.

10 If the USDA were to implement these
11 proposals, the Department would be in violation
12 of its legislative mandate to provide pure and
13 wholesome milk. Milk in the form of illegal
14 MPCs and foreign-sourced dairy ingredients that
15 do not comply with the U.S. pure milk ordinance
16 and FDA's GRAS specifications can be neither
17 pure nor wholesome.

18 By all reason and logic, it is a
19 farce that USDA should even elevate these
20 issues to the level of a National Federal Milk
21 Order Hearing. Thank you.

22 JUDGE DAVENPORT: Thank you,
23 Mr. Bunting. Are there any questions of this
24 witness? Mr. Wilson?

25 -----

1 J. Bunting - Cross - by Mr. Wilson

2 CROSS-EXAMINATION

3 BY MR. WILSON:

4 Q. Todd Wilson, USDA. Good morning.
5 Just one clarification if I could, please. On
6 page 6, your third bullet you said there would
7 be a general outflow of federal approval to
8 foreign dairy producers. Could you further
9 explain that?

10 A. Certainly. Let me say that there
11 have been situations in the northeast in which
12 if a state inspector were to go to Canada and
13 approve farm facilities and manufacturing
14 facilities, those producers within that
15 according to the Federal Order Administrator,
16 Erik Rasmussen would be eligible for a blend
17 price. That's where I'm getting that from. I
18 assume that Mr. Rasmussen knows what he is
19 talking about. Canada is the logical source of
20 the outflow, but we do have USDA inspection in
21 New Zealand as well, so it could in all
22 possibility go there. Does that clarify it?

23 Q. Yes, thank you. The last sentence
24 of the first paragraph on page 4 says this
25 hearing is in reality about eliminating any

1 J. Bunting - Cross - by Mr. Wilson
2 definition of milk in the interest of processor
3 profit. As far as I can deduce from the
4 proposals, all of the proposals are still
5 defining a fluid milk product in the
6 definition; is that correct?

7 A. The point I was making on that,
8 Mr. Wilson, is if there is no definition of
9 MPCs and MPCs are an allowed ingredient in
10 fluid milk, then, therefore, by extension it
11 would be eliminating any definition because the
12 main component could not be defined. Did I
13 make that clear?

14 Q. No.

15 A. Let me try it from another angle.
16 If you add an ingredient that has no standard,
17 no known quantity such as MPCs, no agreed upon
18 definition as an acceptable part of what is
19 defined as milk, you have to that extent
20 eliminated a definition of milk. You would
21 have to, in my opinion, first clearly define
22 MPCs to be a specific understood product with a
23 standard of identity that is widely and broadly
24 understood and no variation in order to include
25 MPC in Class I definition. Did that clarify

1 J. Bunting - Cross - by Mr. Wilson
2 it?

3 Q. I believe so. Thank you.

4 JUDGE DAVENPORT: Other
5 examination of this witness? Very well. Thank
6 you, Mr. Bunting, for your testimony. You may
7 step down. I see that Mr. Beshore is out.
8 Mr. Yonkers, how long do you think your
9 testimony is going to take?

10 MR. YONKERS: 15 minutes.

11 JUDGE DAVENPORT: Very well.
12 Why don't you come forward at this time. Tell
13 us your name, please.

14 MR. YONKERS: Robert Yonkers,
15 Y-O-N-K-E-R-S.

16 JUDGE DAVENPORT: Very well.
17 Mr. Yonkers, I have marked your statement as
18 Exhibit No. 29. Are you prepared to read it
19 into the record at this time?

20 MR. YONKERS: Yes, I am.

21 JUDGE DAVENPORT: Please
22 proceed.

23 (Exhibit No. 29 was marked for
24 identification.)

25 -----

1 R. Yonkers - Direct Testimony

2 ROBERT YONKERS3 a witness herein, having been first duly sworn,
4 testified as follows:5 DIRECT TESTIMONY6 MR. YONKERS: This testimony
7 is submitted on behalf of the Milk Industry
8 Foundation or MIF which has over 100 member
9 companies that process and market about 85
10 percent of the fluid milk and fluid milk
11 products consumed nationwide.12 As buyers and processors of milk,
13 the members of MIF have an important interest
14 in this hearing. Most of the milk bought and
15 handled by MIF members is purchased under the
16 Federal Milk Marketing Orders promulgated
17 pursuant to the Agricultural Marketing Act of
18 1937 also known as the AMAA.19 I am Dr. Robert D. Yonkers, chief
20 economist and director of policy analysis with
21 the International Dairy Foods Association, an
22 umbrella organization of which MIF is a
23 constituent. I have held that position since
24 June of 1998.

25 I hold a Ph.D. in agricultural

1 R. Yonkers - Direct Testimony

2 economics from Texas A&M University, a Master's
3 Degree in dairy science from Texas A&M in 1981
4 and a Bachelor of Science Degree in dairy
5 production from Kansas State University in
6 1979. I have been a member of the American
7 Agricultural Economics Association since 1984.

8 Prior to taking my current position
9 at IDFA, I was a ten-year faculty member in the
10 Department of Agricultural Economics and Rural
11 Sociology at The Pennsylvania State University
12 where I was employed for nine years.

13 At Penn State, I conducted research
14 on the impacts of changing market conditions,
15 alternative public policies and emerging
16 technologies on the dairy industry.

17 In addition, I had statewide
18 responsibilities to develop and deliver
19 extension materials and programs on topics
20 related to dairy marketing and policy. I have
21 written and spoken extensively on economic
22 issues related to the dairy industry, and I
23 have prepared and delivered expert witness
24 testimony to state legislatures and to
25 Congress.

1 R. Yonkers - Direct Testimony

2 This hearing was called to consider
3 a number of proposals that would amend the
4 definition of fluid milk product in federal
5 order regulation. Milk used to make fluid milk
6 products is classified under the federal orders
7 as Class I milk which carries the highest
8 regulated minimum price.

9 USDA first requested additional
10 comments and/or proposals regarding the fluid
11 milk product definition of August of 2003 in
12 response to a petition received from Dairy
13 Farmers of America.

14 On September 19, 2003, MIF submitted
15 comments to USDA indicating its opposition to
16 holding a hearing based on the lack of data and
17 analysis necessary to justify any change in the
18 regulation.

19 USDA extended the deadline for
20 interested parties to submit comments to
21 January 30, 2004. This time the National
22 Producers Federation joined with MIF to file
23 joint comments to USDA requesting that no
24 hearing be held citing the lack of information
25 about the market for beverage products

1 R. Yonkers - Direct Testimony
2 containing milk and other dairy-derived
3 ingredients.

4 Again, the USDA extended the
5 deadline for submitting comments this time to
6 September 30, 2004 and, again, National Milk
7 Producers Federation joined with MIF to request
8 that USDA not hold a hearing noting that
9 initiating the formal rule-making process
10 required to amend federal orders without
11 further data and analysis may compromise the
12 effectiveness of the resulting decision. USDA
13 again extended the deadline for comments to
14 January 31, 2005 and subsequently issued a
15 hearing notice governing this hearing.

16 Consistent with our position on this
17 issue from the start, MIF opposes any change to
18 the fluid milk product definition because the
19 proponents of the proposals contained in the
20 hearing notice have failed at this hearing to
21 provide data and analysis that would
22 demonstrate the need for any change at this
23 time.

24 MIF's philosophy toward proposed
25 amendments to the federal order system can be

1 R. Yonkers - Direct Testimony

2 simply stated. MIF believes that the
3 proponents of such amendments carry the burden
4 of coming forth with solid data and analysis
5 demonstrating both the need for a change and
6 that the proposed amendment will address that
7 need. Anecdotal evidence or broad suppositions
8 do not suffice.

9 USDA has itself adopted this
10 approach to federal order amendments. A good
11 example is the proposed rule issued in Milk in
12 the Texas Southwest Plains Marketing Areas,
13 Dockets Nos: A0-231-A56 and A0-210-A48 and
14 DA-88-110 published June 16, 1988 at 53 FR
15 22499, addressing and rejecting a proposal to
16 amend a federal order with respect to the
17 producer-handler exemption.

18 Although the proponents asserted
19 that the exemption created a significant unfair
20 advantage, USDA noted that "The existence of
21 large producer handler operation merely implies
22 that the conditions for disorderly and
23 disruptive market conditions may exist."

24 MIF similarly notes that the mere
25 existence of beverages that contain milk and

1 R. Yonkers - Direct Testimony

2 other dairy-derived ingredients does not prove
3 that these products either compete with
4 beverages that meet the existing fluid milk
5 product definition nor that such competition
6 has a negative impact on the market for fluid
7 milk products or producer revenue under
8 existing federal order regulations.

9 In the producer-handler decision,
10 USDA went on to note that mere "concern over
11 the potential of a large handler who may have
12 the ability to become a producer-handler does
13 not provide a sufficient basis for a regulatory
14 change."

15 Applying this lesson here, it seems
16 clear that the proponents of any change to the
17 fluid milk product definition must demonstrate
18 using actual data and analysis that products
19 not meeting the current fluid milk product
20 definition are having an impact on the market,
21 not merely that they may have the potential to
22 do so. Without such data and analysis, there
23 cannot be a sufficient basis to justify a
24 regulatory change.

25 USDA in the producer-handler

1 R. Yonkers - Direct Testimony

2 decision made another apt observation, pointing
3 out that "not sufficient time has elapsed
4 between the time that pure milk acquired
5 producer-handler status and when the hearing
6 was held" to evaluate the economic impact.

7 MIF has similarly and consistently
8 maintained that the market for beverages
9 containing milk and dairy-derived ingredients
10 is in its infancy noting in the January 30,
11 2004 letter to USDA that "At such time that
12 study and experience provide a more conclusive
13 basis for redefinition of Class I products, the
14 dairy industry can ask the department to
15 address the issue."

16 USDA's decision in the
17 producer-handler decision to which I have
18 referred is only one example of the approach to
19 decision making that should be applied here.

20 For example, in its 1998 decision
21 rejecting proposals to establish a price floor,
22 USDA concluded that "The data contained in the
23 record of the public hearing in this proceeding
24 provide no basis to expect that an adequate
25 supply of milk for fluid use will not be

1 R. Yonkers - Direct Testimony

2 available nationwide. Therefore, the record
3 does not support adopting the proposal which
4 would encourage more milk."

5 Again, USDA placed the burden on the
6 proponents to come forward with hard data and
7 analysis justifying the change and in its
8 absence declined to adopt the proposed order
9 amendment. Milk in the New England and Other
10 Marketing Areas, Dockets No. A0-14-A68,
11 DA-98-01 published June 12, 1998 at 63 FR
12 32147. Similarly, proponents of changes to the
13 fluid milk product definition in this hearing
14 have failed to demonstrate any need to do so.

15 Let me be more specific as to the
16 data and analysis that I or any other dairy
17 economist would need to see before determining
18 whether an economic change in the fluid milk
19 definition were needed.

20 One, a quantification of the market
21 share held by beverages which do not fall under
22 the current fluid milk product definition but
23 would be included under any proposed change.
24 Speculative conjecture of the hypothetical
25 potential for such products to gain significant

1 R. Yonkers - Direct Testimony

2 market share in the future is not sufficient.
3 There has been no quantitative market data
4 demonstrating that beverage products not
5 meeting the current fluid milk definition have
6 a significant market share. Without such
7 information, there can be no analysis of the
8 competitive impact that such products are
9 having on the market for beverages which meet
10 the existing fluid milk product definition.

11 Two, an analysis of the cross-price
12 elasticity of demand between beverages which
13 meet the existing fluid milk product definition
14 and beverages which would meet any of the
15 proposed changes to the fluid milk product
16 definition. This is the necessary economic
17 test to determine whether two such product
18 types are truly in competition with each other
19 as substitutes in the marketplace. Such
20 competition is a prerequisite to reaching any
21 conclusion regarding whether other products are
22 being placed at an unfair competitive
23 disadvantage or whether disorderly marketing
24 conditions exist.

25 Merely looking at how the two

1 R. Yonkers - Direct Testimony

2 products are packaged or where in the retail
3 store they are sold is not sufficient to
4 demonstrate that products compete in the
5 marketplace.

6 I believe the data necessary to
7 perform this analysis could have been obtained
8 and analyzed by the proponents at least with
9 respect to some of the products that would be
10 reclassified as fluid milk products under the
11 proposed amendments.

12 Even if the fact that no empirical
13 evidence of such cross-price elasticities has
14 been presented at this hearing were due to the
15 lack of data necessary to conduct such an
16 analysis, this would simply demonstrate that
17 the market share of those products is just too
18 small today to warrant regulatory attention.

19 Three, an analysis of the own-price
20 elasticity of demand for those beverages. The
21 most obvious economic test to determine the
22 impact of a regulatory change which would
23 change the cost of ingredients used in
24 beverages with milk and dairy-derived
25 ingredients is to study how economic agents

1 R. Yonkers - Direct Testimony

2 react to such a change.

3 The first inquiry would address
4 empirical evidence of the impact of consumer
5 response to the increased cost of the
6 product--in economist's terms, own-price
7 elasticity of retail demand. That inquiry
8 would be necessary to assess the impact of the
9 regulatory change on the pool specifically,
10 would the positive impact on pool revenues
11 resulting from a higher minimum price for raw
12 milk more than offset by the decline in sales
13 of the product resulting from the higher price
14 for the product.

15 One would also need to assess the
16 higher regulated price on the ingredient
17 formulation of the product. This requires
18 empirical analysis of the input substitution
19 between dairy and non-dairy ingredients in
20 those beverages.

21 Once again, the issue is whether the
22 positive impact on pool revenues resulting from
23 a higher minimum price for raw milk would be
24 more than offset by the decline in use of dairy
25 ingredients in the product because of the

1 R. Yonkers - Cross - by Mr. Yale
2 higher price for the dairy ingredients.

3 Without such an analysis, there can
4 be no credible testimony regarding the impact
5 on producer revenue at federal order minimum
6 class price from the proposed regulatory
7 change.

8 Analyzing the economic impact of
9 changing the fluid milk product definition
10 requires actual market data and empirical
11 analyses, not simply conjecture and
12 speculation. Those data and analyses have not
13 been presented at this hearing. There is,
14 therefore, no justification for changing the
15 fluid milk product definition at this time.
16 Thank you. That concludes my statement.

17 JUDGE DAVENPORT: Examination
18 of this witness? Mr. Yale?

19 -----

20 CROSS-EXAMINATION

21 BY MR. YALE:

22 Q. Good morning. Ben Yale for Select
23 Milk and Continental Dairy Products. You talk
24 in terms of economic data to make a change.
25 Are you suggesting that if there is a term

1 R. Yonkers - Cross - by Mr. Yale
2 within the order in which there is a potential
3 of ambiguity or a lack of clarity that the
4 Department cannot hold a hearing to take
5 testimony to clarify the use of a term that it
6 has already determined to be economically
7 justified?

8 A. That's a long question. I don't
9 believe my testimony was that USDA had no right
10 to call this hearing. MIF asked USDA not to
11 conduct a hearing because we did not believe
12 there was sufficient data and analysis to be
13 presented on the record to justify a change.

14 Q. Forget the hearing. Are you saying
15 that after a hearing, the Department cannot
16 based upon the testimony at the hearing make a
17 change simply to clarify a term within an order
18 in which the economic justification for that
19 term had already been justified at a prior
20 hearing?

21 A. Are you saying USDA should consider
22 prior hearing testimony and evidence in making
23 a change now? I'm not quite sure of your
24 question.

25 Q. Let's go back. On the proposal from

1 R. Yonkers - Cross - by Mr. Yale

2 National Milk to set the standard from 6.5
3 percent nonfat solids to 2.25 percent protein
4 and based on their testimony, that's just the
5 protein portion of the nonfat solids that that
6 is, in fact, a clarification reflecting current
7 technology of an already economically-justified
8 position that the Department has already
9 previously adopted that basis of defining fluid
10 milk, so my question is: Do you have to have
11 an economic analysis to justify a clarification
12 of a term already in use by the regulations and
13 already established?

14 A. I don't know where in the current
15 fluid milk product definition or Class I
16 definition the term "protein" appears, so I
17 would consider this a change but let me go on.

18 MIF believes that any regulatory
19 change has a burden on the industry. Any
20 regulatory change will have at least some
21 burden on the industry and, therefore,
22 regulatory changes should not be made unless
23 there is a clear problem that the change is
24 designed to address and there is clear evidence
25 that the proposed change will address that

1 R. Yonkers - Cross - by Mr. Beshore
2 problem in the marketplace.

3 Q. The question of whether there is a
4 clear change or not ultimately is the
5 Department's to determine?

6 A. Absolutely.

7 MR. YALE: I have no other
8 questions.

9 JUDGE DAVENPORT: Mr. Beshore?

10 -----

11 CROSS-EXAMINATION

12 BY MR. BESHORE:

13 Q. Marvin Beshore for Dairy Farmers of
14 America. Good morning, Dr. Yonkers. You have
15 cited one prior USDA decision, but I noted that
16 you did not cite any classification decisions
17 of the Department to support your contention
18 with respect to what type of data they need.

19 A. No, I did not.

20 Q. There are none, are there?

21 A. I didn't review classification
22 decisions. I reviewed decisions that I thought
23 were very relevant about demonstrating a need
24 for a change.

25 Q. How about the most recent

1 R. Yonkers - Cross - by Mr. Beshore
2 classification decision, the most recent I can
3 think of relating to the appropriate
4 classification for evaporated and condensed
5 canned milk? Are you familiar with that
6 decision?

7 A. I would attend the hearing.

8 Q. You're aware that that decision
9 resulted in the finding that the classification
10 of those products should be changed?

11 A. Yes.

12 Q. There was no testimony or evidence
13 in that hearing about the cross-price
14 elasticity of demand between those products and
15 any other products in either of their present
16 category which is Class 3 or the proposed
17 category which is Class IV, was there?

18 A. I would agree with that. In
19 addition, there was absolutely no testimony
20 during that hearing that would oppose the
21 change. USDA on the hearing record only had
22 evidence to suggest making a change. No one in
23 the industry opposed making a change. I don't
24 know why they wouldn't when there was no one
25 there opposing the change.

1 R. Yonkers - Cross - by Mr. Vetne

2 Q. So if someone comes in and raises
3 their hand I'm against such as your clients or
4 your organization might be economically
5 affected, then these criteria kick in. Is that
6 your position?

7 A. I don't think so, no.

8 Q. Was there any evidence in that
9 classification decision or hearing about the
10 own price elasticity of demand for those
11 products which were being reclassified?

12 A. I don't recall that there was.

13 MR. BESHORE: Thank you.

14 JUDGE DAVENPORT: Mr. Vetne?

15 -----

16 CROSS-EXAMINATION

17 BY MR. VETNE:

18 Q. John Vetne for H.P. Hood.
19 Dr. Yonkers, you refer to the desirability of
20 own price and cross-price elasticity studies in
21 the context of consumer behavior to changes in
22 price; correct?

23 A. Yes.

24 Q. In the paragraph immediately
25 following that on page 6, you talk about

1 R. Yonkers - Cross - by Mr. Vetne
2 analysis of input substitution between dairy
3 and non-dairy ingredients in those beverages
4 which is essentially analysis of either cross
5 price or own-price elasticity of processors or
6 manufacturers as consumers of ingredients
7 produced by others?

8 A. Yes. The normal consumer demand is
9 conducted at the retail level because that's
10 where our data is. You could also conduct this
11 at an intermediate step in this case at the
12 processor level and their demand for inputs in
13 products which can be substituted.

14 Q. In the following sentence, one
15 issue, as you see it, is the positive impact on
16 pool revenues from a higher minimum price for
17 raw milk would be more than offset by the
18 decline in the use of dairy ingredients. Maybe
19 this is the simple converse which follows from
20 your testimony, but would you maintain that any
21 important consideration in classification or
22 reclassification would be to measure demand of
23 dairy-derived ingredients and the impact that
24 would have on producer revenue in the price of
25 Class III or Class IV products from which other

1 R. Yonkers - Cross - by Mr. Cryan
2 classifications follow?

3 A. In order to demonstrate a reason for
4 changing classification, yes.

5 MR. VETNE: Thank you.

6 JUDGE DAVENPORT: Other cross
7 of this witness? Dr. Cryan?

8 -----

9 CROSS-EXAMINATION

10 BY MR. CRYAN:

11 Q. Roger Cryan, National Milk. Good
12 morning, Bob.

13 A. Good morning.

14 Q. My first question is: Is your
15 applied economic policy and analysis somewhat
16 speculative or conjectural because it
17 necessarily looks forward to the potential
18 impact of a change in policy?

19 A. Are you talking about policy
20 analysis or are you talking about --

21 Q. The kind of economic analysis that's
22 necessary to consider the impacts of a policy
23 change.

24 A. None of my testimony addressed
25 policy change, just regulatory change.

1 R. Yonkers - Cross - by Mr. Cryan

2 Q. Isn't that a policy change -- Okay,
3 then regulatory. Isn't most applied economic
4 analysis, most applied economic regulatory
5 analysis somewhat speculative or conjectural
6 because it projects into the future the impact
7 of a change in regulation?

8 A. The type of analysis I'm looking for
9 as an economist to determine whether two
10 products are substitutes are not looking into
11 the future. They are based on existing data in
12 the marketplace. USDA in the past has rejected
13 potential market impacts and look to
14 demonstrated actual market impacts at the time
15 of the hearing in making a decision.

16 Q. Do you believe that's appropriate
17 that federal regulation never looked forward to
18 potential impacts?

19 A. I think the federal order regulation
20 when it was put into the effect looked at the
21 impact that regulation would have on the
22 marketplace. Changing those regulations would
23 have significant -- any regulation -- has
24 impacts on the economic agents in the
25 marketplace. It should not be done without

1 R. Yonkers - Cross - by Mr. Cryan
2 analysis of what problem is being addressed by
3 the regulatory, definition of what problem is
4 being addressed and then analysis of how the
5 proposed change will address that situation.

6 Q. So federal order amendments should
7 never prevent problems, they should only fix
8 problems?

9 A. In the past USDA has made those
10 changes to fix existing problems in the
11 marketplace. I'm not sure I'm aware of
12 situations where USDA has made a significant
13 regulatory change in anticipation of something
14 that will change in the future.

15 Q. Do you agree with that?

16 A. Yes. I agree that they should focus
17 on demonstrated impact. You can't predict. I
18 agree. You cannot predict what is going to
19 happen. You cannot predict what technologies
20 will come along in five years from now.

21 Q. You say in your testimony that one
22 of the things that would be necessary is
23 quantification of the market share held by
24 beverages which do not fall under the current
25 fluid milk product definition but would be

1 R. Yonkers - Cross - by Mr. Cryan
2 included under any proposed change. You say
3 that data should be part of the record in order
4 to address the problem that exists on the
5 market?

6 A. Yes.

7 Q. What if that data is proprietary?

8 A. There have been other cases where in
9 federal order hearings that data has been
10 proprietary and others have found ways of
11 finding data and put in the market and people
12 that actually testify about their experience in
13 the marketplace.

14 Q. You also indicate that -- Your
15 testimony stated that one of the things that
16 should be on the record for this type of a
17 decision is an analysis of the own-price
18 elasticity of demand for those beverages. What
19 if the class of products that would be
20 reclassified or potentially reclassified
21 consists of a single product which price has
22 never changed?

23 A. Well, this price may never change
24 but the price of fluid milk, are you implying
25 that it never changes either because --

1 R. Yonkers - Cross - by Mr. Cryan

2 Q. Can you establish an own-price
3 elasticity or demand for a product whose prices
4 never change?

5 A. No.

6 Q. So in such a case, you should not
7 make a decision no matter how large the share
8 of market?

9 A. If there is evidence presented,
10 there is a single product in the market is the
11 only product in that category and its price
12 never changes, you would have to look at other
13 economic analysis, and I didn't imply that the
14 department should not also consider other
15 economic analysis, consumer survey research
16 which has been presented during this hearing,
17 but you're right. You cannot do an own price.

18 You can do cross-price elasticities
19 because relative prices are changing in the
20 marketplace with other beverages unless those
21 other beverages such as fluid milk products
22 that meet the current definition never have
23 their price change either, but I don't believe
24 that's the case.

25 Q. Let's talk about cross-price

1 R. Yonkers - Cross - by Mr. Cryan
2 elasticity now. Aside from what is already on
3 the record, comments that are already on the
4 record about potential difficulty of developing
5 those types of models, let's consider a
6 situation where a new product is introduced and
7 it has attributes, it has most of the same
8 attributes of a larger category of products and
9 they are both in -- the quantity and demand for
10 that product is really associated with a sort
11 of a structural change and folks moving from
12 one subcategory to another subcategory. Is
13 information about that, is the process of
14 structural substitution or one subcategory to
15 another going to be captured by consideration
16 of cross-price elasticities?

17 A. Between those two categories of
18 beverages, sure. If people are moving between
19 those products, that will be captured in the
20 demand system analysis. If you specify model
21 correctly, sure it will be.

22 Q. If it's a new product that has been
23 introduced and people are adopting the new
24 product because of a particular attribute that
25 is essentially the primary attribute that they

1 R. Yonkers - Cross - by Mr. Cryan
2 demand once it's available, isn't that
3 something of a structural change in the demand
4 rather than the kind of demand that can be
5 modeled as part of a matrix of demand?

6 A. My testimony about the need for
7 cross-price elasticities is to demonstrate that
8 products are substitutes in the marketplace
9 and, therefore, under the federal orders, the
10 dairy ingredients used to manufacture those
11 products should have equal product costs. In
12 your case, are you talking about a demand
13 expansion for the category in which case there
14 is no product substitution? It's an entirely
15 new product?

16 Q. I'm talking about a shift in the
17 demand structure. If the new product is
18 introduced and that leads to a fundamental
19 shift in the demand structure in terms of the
20 allocation of the demand between the
21 traditional subcategory and the new
22 subcategory, the nature of that shift cannot
23 necessarily be captured in the model of
24 cross-price elasticities, can it?

25 A. It can be captured in a consumer

1 R. Yonkers - Cross - by Mr. Cryan
2 demand systems analysis with proxy variable to
3 measure the change in taste and preferences.
4 Is that what you're getting after is that
5 consumers have a substantive change?

6 Q. Right.

7 A. But if that is also causing them to
8 substitute the new product for the existing
9 product, that will still show up in that
10 cross-price elasticity or some interaction
11 between the prices of either of those products
12 and the proxy variable you're going to use for
13 taste and preference and a variable in that
14 model.

15 Q. The type of information that would
16 be captured by that variable is something like
17 information about what degree folks are just
18 changing their preference substituting one
19 subcategory for another for what types of uses
20 they are putting it to and what type of
21 switching they are doing between products.

22 A. Again, I didn't say this is the only
23 data, the only type of analysis USDA should
24 base its decision on, but in order to determine
25 if two products are substitutes economically as

1 R. Yonkers - Cross - by Mr. Cryan
2 a trained economist, we need to have this type
3 of information.

4 Q. Let's talk about substitution then.
5 If you have two sets of customers one of whom
6 swears by skim milk and the other set swears by
7 whole milk and let's say it may not be
8 unreasonable to imagine a set of customers who
9 goes to the store and finds only whole milk and
10 just refuses to buy it because there is an
11 attribute to that product that they won't
12 accept. Does that mean that skim milk should
13 not be in Class I?

14 A. Because it's not on the shelf?

15 Q. Does the fact that there are folks
16 that are a large number of people --

17 JUDGE DAVENPORT: Dr. Cryan,
18 what is the relevance of this particular line
19 of questioning?

20 MR. CRYAN: This is relevant
21 to the nature of --

22 JUDGE DAVENPORT: The perfect
23 question is: How is this going to assist the
24 administrator in making a decision?

25 MR. CRYAN: This will help the

1 R. Yonkers - Cross - by Mr. Cryan
2 administrator understand that products do not
3 necessarily have to be economic substitutes for
4 them to be justified as being in the same
5 class. Is that acceptable?

6 JUDGE DAVENPORT: Well, I'll
7 permit it for a few more questions, but I think
8 we are getting pretty far afield from what
9 Mr. Yonkers' position was.

10 MR. CRYAN: Well, I will defer
11 to the staff and ask them if they feel that's
12 the case and if they would, I'll shut it down.
13 Would that be appropriate if we ask them?

14 JUDGE DAVENPORT: You
15 certainly may address the question to the
16 representatives that are here.

17 MR. CRYAN: Is this line of
18 questioning pertinent, to your thinking?

19 MR. STEVENS: Garrett Stevens,
20 Office of General Counsel, U.S. Department of
21 Agriculture. Your Honor, I think that we are
22 over here agreeing with your assessment of the
23 situation and that there may be a way to get
24 through it a little faster without dwelling on
25 it to the extent we have to this point so I

1 R. Yonkers - Cross - by Mr. Tosi

2 would leave it at that.

3 JUDGE DAVENPORT: In other
4 words, Dr. Cryan, it's not my intent to muzzle
5 you or to curtail your right to
6 cross-examination of the witness, but it is at
7 a point where, in other words, I think the
8 points have been belabored and Dr. Yonkers'
9 position has been clearly set forth. There is
10 an opportunity post hearing if there is an area
11 of lack of clarity that you certainly may give
12 additional comments at that time.

13 MR. CRYAN: That's fine. I'm
14 done. Thank you.

15 JUDGE DAVENPORT: At this time
16 I'm going to declare the lunch recess.

17 (At this juncture, a luncheon
18 recess was taken.)

19 JUDGE DAVENPORT: Is there any
20 additional cross for this witness? Very well.
21 Mr. Tosi?

22 -----

23 CROSS-EXAMINATION

24 BY MR. TOSI:

25 Q. Good afternoon, Bob. I want to

1 R. Yonkers - Cross - by Mr. Tosi

2 thank you for appearing at the hearing today.
3 Are you aware of any decisions that have been
4 issued by AMS or the Department, decisions that
5 were issued even though there were no
6 disorderly marketing conditions and that a
7 decision was issued changing certain things to
8 prevent the possibility of events happening
9 that would result in disorderly marketing
10 conditions?

11 A. I can tell you I did not review
12 every federal decision that has been made over
13 a time period, so I can't answer that question
14 and say yes or no because I don't know.

15 Q. If it turned out that there were a
16 significant number of those types of decisions,
17 would that be cause for us to reconsider the
18 advice or positions that you're taking here
19 with regard to doing extensive analyses on
20 things?

21 A. I would say if there were, then USDA
22 has been inconsistent in applying its rule in
23 the cases in which I cited, and I would hope
24 that you would have to resolve that
25 inconsistency, address what I have addressed in

1 R. Yonkers - Cross - by Mr. Tosi

2 my testimony.

3 Q. I want to throw a hypothetical
4 situation at you. Let's assume that there is
5 fluid milk, but there is a product called skim
6 milk that no one had ever thought about and
7 someone developed a way to take the fat out of
8 milk and we had this new product called skim
9 milk. Would you be of the opinion that before
10 we would class that that we should undergo the
11 extensive economic analysis that you're
12 suggesting here in your testimony before we
13 would decide what class that product would be
14 put in?

15 A. Can you tell me what you mean by
16 before we class that product? Are you saying
17 that the definition you would look at in the
18 regulation does not help you in classifying it
19 and you need to and there is no direction, you
20 can't classify that because of the regulation?

21 Q. Well --

22 A. I'm not quite sure what you mean by
23 when we class the product. When USDA
24 determines classification, they have a
25 regulation in place to go look at and either it

1 R. Yonkers - Cross - by Mr. Tosi
2 meets that definition or nothing, so I don't
3 know what else you could do but use the
4 regulation. I mean, that's the law. We all
5 have to operate under it. The only way to
6 change that regulation is through a hearing
7 process such as this as I understand it.

8 Q. In the event that there is some sort
9 of ambiguity or some gray area, if there were
10 no gray areas, it might be reasonable to think
11 that we wouldn't be here today having this
12 hearing?

13 A. I think USDA makes a determination
14 of how to interpret regulations on a regular
15 basis, not necessarily federal order
16 regulations but all regulations on a regular
17 basis and if someone in the industry disagrees
18 with that interpretation, there is recourse.

19 Under the 37 Act, there is recourse
20 to go through an administrative procedure and
21 ultimately through a court procedure. So USDA
22 always has to read regulations and come to a
23 legal determination. I'm not an attorney so I
24 can't do that. If anyone in the industry
25 disagrees with that, they have legal recourse

1 R. Yonkers - Cross - by Mr. Tosi

2 to pursue, it's my understanding.

3 Q. Let me throw another hypothetical at
4 you then. Let's assume that there is a new
5 product that someone has developed and it falls
6 within this little gray area that is kind of
7 hard to determine gee, is this fluid? Should
8 it be in Class I or should it be in Class II,
9 for example? Would it be correct that we would
10 look at the nature of your testimony here to
11 say that before we decide what class to put
12 that new product in that we should be
13 conducting analyses on the elasticity of demand
14 of that product, what its impact may or may not
15 be on producer revenue, what its impact may be
16 on overall consumption of dairy products or
17 fluid milk?

18 A. There is nothing in my testimony and
19 I don't believe I'm going to provide any answer
20 to your question about how you should interpret
21 regulations. I'm not going to do that. The
22 regulations are as they are written. I don't
23 disagree that USDA when faced with a situation
24 that's not considered when the regulation was
25 written does have to make a determination and

1 R. Yonkers - Cross - by Mr. Tosi

2 then industry participants who feel that you
3 have made that determination incorrectly have
4 legal recourse.

5 Q. Are you of the opinion based on the
6 products that you are aware of that USDA has
7 made proper determinations in all cases?

8 A. I'm here representing MIF and MIF
9 has not come to any conclusions about that, to
10 my knowledge. I don't believe we have policy
11 on how you're interpreting that.

12 Q. On page 6 of your prepared
13 statement, referring to Item No. 3 which is
14 your statement on analysis of own-price
15 elasticity of demand for those beverages. Your
16 last sentence reads "Without such analysis,
17 there can be no credible testimony regarding
18 the impact on producer revenue at federal order
19 minimum class prices from the proposed
20 regulatory change."

21 What relationship then -- I take
22 away from this that what you're saying is
23 somehow the impact on producer revenue needs to
24 somehow be considered with respect to
25 determining form and use of a product, and I

1 R. Yonkers - Cross - by Mr. Tosi
2 don't understand if that is what you're doing
3 or if that is what you're suggesting how you
4 take form and use and separate that from the
5 economics of what may result from a difference
6 in deciding if a product goes into Class II or
7 Class I?

8 A. I'm not sure I'm happy you asked
9 that question or sorry you asked that question,
10 Gino. I think the individual classification
11 decision is looking at individual trees. The
12 forest is what the order system is designed to
13 do.

14 My understanding through my training
15 and study of the dairy industry is that there
16 was a time when there was not a sufficient
17 supply of milk to meet the requirements for
18 fluid milk products what we now know as Grade
19 A.

20 One reason to attract that milk was
21 because for farmers it cost money to actually
22 make those changes on the farm, so you needed
23 to have a system in place that put more money
24 to those farmers that did convert to Grade A
25 and serve that market for those products.

1 R. Yonkers - Cross - by Mr. Tosi

2 If you start going backwards and
3 making decisions that take money away from
4 that, what is the purpose of having
5 classification? If you don't need the money
6 now to attract producers to the Grade A
7 production system and to the Class I market,
8 why are you doing this.

9 When I say I'm not sure I'm happy or
10 unhappy, I could answer that question for an
11 awfully long time, Gino, but I would hope that
12 USDA in this hearing and in all hearings would
13 not get so focused on a narrow technical issue
14 that they ignore broader issues around why we
15 are doing the regulation. What is the whole
16 purpose of having classification? Here is an
17 aspect of classification that could go against
18 the reason we have it, in fact, the
19 classification decision would result in less
20 producer revenue.

21 MR. TOSI: I think I
22 understand your answer. Thank you very much.
23 I appreciate your patience.

24 JUDGE DAVENPORT: Other
25 examination of this witness? Very well. Thank

1 M. Suever - Direct Testimony

2 you, Dr. Yonkers. You can step down.

3 Mr. Vetne? Do you want to bring your witness
4 up?

5 MR. VETNE: Yes.

6 JUDGE DAVENPORT: Please tell
7 us your name and have a seat.

8 MR. SUEVER: My name is Mike
9 Suever representing H.P. Hood.

10 JUDGE DAVENPORT: Mr. Suever,
11 you have prepared testimony to read; is that
12 correct?

13 MR. SUEVER: Yes, I have.

14 (Exhibit No. 30 was marked for
15 identification.)

16 JUDGE DAVENPORT: Mr. Vetne,
17 that has been marked as Exhibit No. 30.

18 MR. VETNE: Thank you.

19 -----

20 MIKE SUEVER

21 a witness herein, having been first duly sworn,
22 was examined and testified as follows:

23 DIRECT EXAMINATION

24 BY MR. VETNE:

25 Q. Can you supplement your prepared

1 M. Suever - Direct Testimony

2 testimony by giving us a little bit of your
3 professional and educational experience?

4 A. I am a 1980 graduate of the Ohio
5 State University with a degree in food
6 technology, dairy technology. I have worked in
7 the dairy industry since that time in a number
8 of functions. I participated in state and
9 local hearings since the mid-1980's on and off
10 again.

11 Q. And that participation includes
12 participation as a witness and participation as
13 an attendee?

14 A. Yes, it does.

15 Q. As we said, you have a prepared
16 statement. Proceed with that, please.

17 MR. SUEVER: Thank you. I am
18 Mike Suever, senior vice president of R&D,
19 Engineering and Milk Procurement for H.P. Hood,
20 LLC. H.P. Hood, LLC, its Crowley Foods
21 Division and its Kemps, LLC subsidiary own and
22 operate a number of milk processing and
23 manufacturing plants in the eastern United
24 States and the midwest.

25 Hood produces a full line of fluid

1 M. Suever - Direct Testimony

2 milk, traditional Class II products and
3 specialty products. Hood-packaged fluid milk
4 is distributed throughout the east and midwest.
5 Several manufactured and specialty products
6 produced by Hood and its copackers are
7 distributed nationally.

8 H.P. Hood's position in a nutshell:
9 As stated in my letter of January 31, 2005 to
10 Deputy Administrator Coale which contained
11 Hood's proposal for this hearing, our primary
12 view is that no change is needed to current
13 regulations. The fluid milk product definition
14 should not be amended to include more dairy
15 products in the Class I category nor any new
16 dairy beverage unless it competes directly and
17 substantially with conventional fluid milk
18 sales.

19 However, if USDA decides that an
20 amendment of the rule is necessary, Hood's
21 Proposal No. 5, as modified, provides express
22 standards for an administrative conclusion that
23 a dairy beverage with less than 6.5 percent
24 nonfat milk solids competes with and displaces
25 Class I fluid milk sales and that product may,

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2 therefore, warrant Class I classification.

3 Hood is withdrawing Proposal No. 6.

4 Our position at this hearing is
5 based on several axioms. Number one, the
6 development and marketing of new dairy products
7 is good for the dairy industry and for the
8 consuming public. Two, new product innovation
9 is very expensive. Three, creating higher raw
10 ingredient costs discourages product
11 innovation.

12 Four, high raw ingredient costs
13 encourages manufacturers to reformulate and
14 seek lower cost, non-dairy substitutes. Five,
15 consumers respond to price increases by reduced
16 purchases. Six, milk producers respond to
17 higher farm milk prices by an increase in milk
18 production. Seven, increased milk production
19 produces lower farm milk prices.

20 Reclassification of some beverages
21 as proposed in this hearing would affect a very
22 small volume of milk, so any enhancement of
23 producer blend prices would be negligible at
24 best and probably short-lived as explained by
25 Dr. Stephenson.

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2 On closer examination it is likely
3 that farm milk prices will be reduced by these
4 proposals. Current marketing order rules
5 stifle dairy product innovation and development
6 by capturing in the fluid milk definition
7 products that are not fluid milk.

8 Proposals at the hearing would
9 further discourage new product innovation and
10 encourage use of non-dairy ingredients in
11 beverages. These consequences are damaging to
12 the industry, damaging to producers and
13 damaging to the interests of the consuming
14 public.

15 As a matter of public policy and
16 economic reality, USDA should do all it can
17 through the Federal Milk Order System to
18 encourage product innovation and create new
19 demand for producer milk.

20 Class I milk should be limited to
21 products that contain at least 8.25 percent
22 milk solids not fat entitled to be packaged and
23 labeled as "milk" as defined by the FDA in 21
24 CFR 131.110 and those fluid milk substitutes
25 that compete directly and substantially for

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2 fluid milk sales, consistent with economic
3 reasoning and regulatory policy underlying
4 classified price discrimination.

5 Carb Countdown was developed and is
6 marketed by H.P. Hood as a dairy beverage
7 option for consumers who would not otherwise
8 consume fluid milk.

9 As a processor of fluid milk, Hood
10 does not wish to pursue regulations that would
11 damage its producer-suppliers or to encourage
12 consumers to buy nonmilk beverages instead of
13 fluid milk.

14 Rather, by offering innovative
15 beverages with dairy ingredients, we hope to
16 regain or retain part of the market share that
17 the dairy industry has lost or would lose to
18 non-dairy beverages and to attract consumers
19 that would not otherwise pick up a carton of
20 milk at the grocery store. It was with these
21 objectives in mind that Hood developed and
22 introduced a new dairy beverage called Carb
23 Countdown.

24 Carb Countdown is a low-carbohydrate
25 beverage containing milk ingredients. It is

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2 produced by Hood in New York, Virginia,
3 Connecticut and by copackers in the west.

4 Less than 6.5 percent of the
5 finished product weight of the product is
6 nonfat milk solids representing only 75 percent
7 of the nonfat total milk solids required in the
8 FDA standard beverage milk. Carb Countdown
9 cannot, therefore, be packaged and labeled as
10 "milk."

11 As displayed on the ingredients
12 panel, the milk-derived ingredients in Carb
13 Countdown are fat free milk or ultrafiltered
14 fat free milk, cream, calcium caseinate, whey
15 protein isolate and buttermilk.

16 Carb Countdown was designed to
17 appeal to people who were not buying milk or
18 were intending to reduce milk consumption
19 because of milk's relatively high carbohydrate
20 content. Milk carbohydrates are sugars
21 contained in milk lactose which makes up the
22 largest part of nonfat milk solids in producer
23 milk.

24 By removing lactose through
25 ultrafiltration or by adding dairy ingredients

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2 that contain little lactose, Carb Countdown is
3 offered with only three to four grams of
4 carbohydrates per eight-ounce serving. Fluid
5 milk contains 12 grams or more of carbohydrates
6 representing more than one-half of the initial
7 daily carbohydrate allowance under many of the
8 low carbohydrate diet plans.

9 H.P. Hood, like others in the food
10 and dairy industry, observed several years ago
11 that sales of fluid milk and other high
12 carbohydrate foods were decreasing due to the
13 growing number of people on low carbohydrate
14 diets. Consumer surveys cited in the August
15 issue of Dairy Foods Magazine last year
16 reported that 11 percent of the population are
17 following a low carbohydrate diet and 20
18 percent of the population has tried a low
19 carbohydrate diet since 2002.

20 Carb Countdown was developed and
21 intensely marketed to this population group who
22 were likely to eliminate fluid milk from their
23 diet. An example of this marketing strategy is
24 shown in Attachment A. Two story boards are
25 included showing our TV commercials.

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2 Consumer responses in e-mails and
3 letters to Hood, samples of which are compiled
4 in Attachment B reveal that Carb Countdown has
5 reached the target population and produced
6 sales of the dairy beverage to people who were
7 intending to eliminate conventional fluid milk
8 from their diets or had stopped buying fluid
9 milk all together.

10 Hood thus produced a value-added
11 product that provided a market for milk and
12 milk-derivative ingredients that would have
13 otherwise been disposed of in surplus products
14 depressing producer prices.

15 Not only does Carb Countdown appeal
16 to a limited group of consumers who would not
17 otherwise buy milk, it also does not compete
18 directly with FDA-standard beverage milk on
19 price.

20 Unlike filled milk in the 1960's,
21 Carb Countdown is significantly more expensive
22 than fluid milk on the grocery store shelf
23 because it is significantly more costly to
24 produce regardless of classification, so there
25 is no cost incentive to select Carb Countdown

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2 as a substitute for milk.

3 Carb Countdown is a Class II product
4 in California as are all dairy beverages that
5 do not meet FDA or state standards of identity
6 for milk. Although it contains less than 6.5
7 percent nonfat solids from milk and milk
8 derivative ingredients, Carb Countdown has been
9 treated by the market administrators as a Class
10 I product in the federal orders.

11 To accomplish this, USDA now counts
12 as part of the nonfat milk solids for the
13 purposes of the 6.5 percent SNF standard milk
14 derivative ingredients -- such as calcium
15 caseinate, whey protein isolate and whey
16 protein concentrate -- that were previously
17 treated as non-milk ingredients, Attachment C.

18 Additionally, USDA applies an SNF
19 equivalent and skim milk equivalent formula to
20 dairy ingredients in Carb Countdown and
21 attributes to the product all solids in milk
22 that have been used to produce some of Carb
23 Countdown's milk-derived ingredients rather
24 than simply measuring milk solids in the
25 content of the package.

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2 This interpretation, we believe, is
3 contrary to the plain meaning of Section
4 1000.15 and is the subject of ongoing
5 litigation. We are not here to litigate that
6 interpretation in another forum but to preserve
7 Class II classification in the future for Carb
8 Countdown and other beverages Hood may develop
9 to bring consumers back to dairy foods and away
10 from soft drinks or other beverage alternatives
11 or keep consumers from abandoning milk
12 beverages in the first place.

13 Criteria for Class I Classification
14 and Price Discrimination: Fluid milk demand
15 traditionally has been considered by USDA
16 economists to be relatively inelastic to
17 changes in the price of consumer products. The
18 relative inelasticity of demand for packaged
19 fluid milk and relative elasticity of demand
20 for dairy products is one of the primary
21 reasons the dairy industry and government
22 regulators have applied price discrimination
23 for raw milk in the form of classified pricing.
24 USDA has explained this in its final Federal
25 Milk Order Reform Decision, 64 FR 16026 at page

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2 16102, April 2, 1999.

3 "The elasticity of demand for the
4 various dairy products is significantly
5 different creating different consumer responses
6 to changing prices for various dairy products.
7 The federal milk orders have attempted to
8 address these issues through classified
9 pricing. This system allows a higher price to
10 be applied to milk used for Class I uses due to
11 the inelastic demand for Class I products."

12 In order to protect the integrity of
13 the Class I price discrimination and maintain
14 Class I sales, USDA has included in Class I
15 classification milk beverages thought to be
16 substitutes for FDA-standard beverage milk and
17 which thereby displace or cannibalize fluid
18 milk sales.

19 For example, filled milk was
20 introduced in the 1960's as a substitute for
21 whole milk in which milk fat was replaced by
22 vegetable fat. It apparently displaced fluid
23 milk sales by using cheaper fat ingredients and
24 being offered to consumers at a price below
25 fluid milk price.

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2 Filled milk was expressly included
3 as Class I use in the fluid milk definition
4 prior to federal order reform and is
5 incorporated in the current definition 7 C.F.R.
6 1000.15. Filled milk is no longer produced in
7 the Federal Milk Order system 64 Federal
8 Register at 16122.

9 The reasons for including certain
10 fluid milk substitutes as Class I products were
11 explained in the so-called Nourse Committee
12 Report to the secretary in 1962:

13 "The principal reasons for including
14 milk and its related milk by-products in Class
15 I is that because of sanitary requirements,
16 transportation costs, and other reasons
17 supplies tend to be limited to a relatively
18 local milkshed. Further, the consumer demand
19 for these products is such that relatively high
20 prices can be charged without substantially
21 reducing the quantities that will be absorbed
22 by the market. Together, these factors provide
23 sufficient reason for the inclusion of these
24 products in the high-priced classification.

25 "Furthermore, the extent to which

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2 closely related fluid products may be
3 substituted in consumption for fluid whole
4 milk, the exclusion of these from the same
5 category as whole milk would serve to reduce
6 the degree of inelasticity of demand since the
7 existence of substitutes for any product has an
8 effect of increasing the sensitivity or
9 responsiveness of buyers to changes in the
10 relative prices of any particular product and
11 of its competitor.

12 "For this reason, the successful
13 introduction of a new competitive product such
14 as a sterile concentrated milk in a local
15 market would be expected to result in an
16 increase in elasticity of demand for locally
17 produced fluid milk supplies, as well as a
18 reduction in the level of demand."

19 Report to the Secretary of
20 Agriculture by the Fluid Milk Order Study
21 Committee (April 1962) Part II, Section 1,
22 pages 5 to 6, reproduced in "publications" on
23 the CPDMP website at cpdmp.Cornell.edu.

24 In 1970 and 1971, USDA conducted
25 three regional hearings to provide more

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2 uniformity in product classification producing
3 decisions in 1974 at 39 Federal Register 8202
4 (March 4, 1974), 39 Federal Register 8712
5 (March 6, 1974) and 39 Federal Register 9012
6 (March 7, 1974).

7 In these decisions, USDA applied the
8 Nourse Committee theories to refining products
9 to be included in Class I use by examining
10 product substitution and competition.

11 Milkshakes were included in Class II because
12 they competed for consumer dollars with frozen
13 desserts rather than fluid milk. Infant and
14 dietary formulas were excluded from Class I
15 because they are "specialized food products
16 prepared for a limited use and do not compete
17 with other milk beverages consumed by the
18 general public."

19 Likewise, beverages with less than
20 6.5 percent nonfat milk solids were "not
21 considered as being in the competitive sphere
22 of traditional milk beverages." 30 Federal
23 Register at 8715. A national hearing in 1990
24 produced additional but minor refinements to
25 the fluid milk definition. 58 Federal Register

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2 12633, 12634-35 (March 5, 1993). The current
3 definition in 7 CFR 1000.15 contains the same
4 6.5 nonfat milk solids standard as pre-reform
5 definitions.

6 I summarize this history to emphasis
7 two related objectives underlying Class I
8 classification. First, Class I classification
9 is intended to enhance or stabilize producer
10 prices by price discrimination for only the
11 most price inelastic dairy products.

12 Second, only milk beverages that are
13 clear substitutes for Class I products by
14 direct competition with fluid milk should also
15 be considered eligible for Class I treatment to
16 maintain the first objective. The corollary
17 principal is that dairy products that do not
18 directly and substantially compete with
19 conventional fluid milk products should not be
20 in Class I use. Class I classification should
21 also be avoided if demand for the product is
22 relatively elastic or if Class I classification
23 would not enhance producer prices.

24 Classification of Dairy Beverages to Class I
25 Will Not Enhance Producer Prices.

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2 Although it may be tempting to
3 conclude that the inclusion of any dairy
4 beverage product in Class I will benefit
5 producers by increasing milk prices, that would
6 be an erroneous and shortsighted conclusion.

7 Rational examination of economic and
8 marketing reality demonstrates, we believe,
9 that Class I classification of dairy beverages
10 that are not milk will discourage development
11 of new products in the first instance, have
12 little impact on the producer prices if the
13 products were nevertheless developed and that
14 the effect on producer prices will be negative
15 rather than positive.

16 The expense and risk of new product
17 research and development and the potential use
18 of alternative non-dairy ingredients are
19 important factors in any decision to classify
20 beverages as Class I fluid milk.

21 New product research and development
22 includes several costly stages: (1) concept
23 scrutiny, (2) feasibility study, (3) costing
24 and ingredient sourcing (4) prototyping, (5)
25 test marketing and (6) commercialization. The

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2 product developer hopes over time to recapture
3 these costs in the marketplace of the product.
4 This, of course, is more difficult if high raw
5 product prices drive up consumer prices and
6 discourage consumers from trying the product.

7 The odds of success, however, are
8 weighted heavily against new food products even
9 without regulatory disincentives. Few new food
10 products survive beyond two years after first
11 commercial sale.

12 A May 12, 2005 article by the
13 University of Georgia College of Agriculture
14 and Environmental Sciences in the publication
15 Georgia Faces reported 80 percent of 15,000 new
16 products introduced each year are withdrawn
17 within two years causing food industry losses
18 of four billion dollars.

19 The volume of milk in Class II dairy
20 beverages is very small representing only a
21 fraction of the 12 percent of Class II use
22 reported by USDA for 2003 to be in the "other
23 food products" which includes miscellaneous
24 cream products, commercial food processing use
25 such as soup, candy, bakery products as well as

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2 dairy beverages.

3 Data assembled in the table attached
4 to Mr. Rourke's testimony, Exhibit No. 12 shows
5 that only 0.19 percent of the total Class II
6 use in 2004 came from dairy beverages that are
7 Class II because they contain less than 6.5
8 percent NFMS and an additional 0.11 percent of
9 total Class II use was from Class II
10 yogurt-based beverages.

11 Researchers at Cornell have
12 concluded that reclassification of new dairy
13 beverage products from Class II to Class I
14 disregarding other market responses is likely
15 to affect producer prices by less than one cent
16 per hundredweight.

17 The volume of milk in Class I
18 beverages that are not traditional fluid milk
19 products is also small, representing only 0.8
20 percent of total Class I product disposition in
21 2003 as reported in the annual Federal Milk
22 Order Statistics publication. Data for 2004
23 assembled by Mr. Rourke in Exhibit No. 12
24 similarly reveal only 0.53 percent of Class I
25 sales in products consisting of non-milk dairy

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2 beverages.

3 Further, as described in a recent
4 study by Cornell University entitled
5 "Assignment of New Products Under Classified
6 Pricing: A Conceptual Dynamic Model of Class
7 Assignment Outcomes" and in testimony by
8 Dr. Stephenson at this hearing, Class I
9 assignment of current Class II dairy beverage
10 products is likely to produce lower weighted
11 average returns to producers in the long run,
12 particularly if demand for new products is
13 highly elastic as is usually the case.

14 The Cornell study assumed that new
15 products are actually produced and marketed as
16 Class I products. The damage caused by failure
17 to develop new dairy products and by artificial
18 limitations on market expansion for milk
19 derivative ingredients due to regulatory
20 disincentives is also substantial but probably
21 not measurable.

22 H. P. HOOD'S PROPOSAL

23 While we believe that no change is
24 needed to, or justified for, the current fluid
25 milk definition, our proposal seeks to strike a

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2 balance incorporating the foregoing principles
3 and to control damage to processors and
4 producers.

5 We have slightly modified our first
6 proposal, Proposal 5 in the hearing notice as
7 described in our letter of May 24 to Deputy
8 Administrator Coale, Attachment D to my
9 testimony. Additionally, we withdraw Proposal
10 6 and will not present supporting testimony.

11 Proposal 5 would continue to focus
12 on whether a milk beverage competes directly
13 and substantially with FDA-standard fluid milk
14 products and provides some criteria for
15 measuring that competition potential. These
16 criteria include:

17 (1) Whether the product is eligible
18 to be labeled as "milk" under FDA standards of
19 identity. Whether called "milk" or not on the
20 product label, if a milk beverage contains at
21 least 8.25 percent nonfat milk solids as
22 required by FDA, it presumably competes
23 directly with fluid milk beverages. We observe
24 that California follows this criterion by
25 classifying dairy beverages, i.e., beverages

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2 not meeting FDA or state standards of identity
3 for "milk" as Class II products, including Carb
4 Countdown.

5 (2) Whether the price of the product
6 to consumers at the retail level is comparable
7 or below retail prices for conventional milk
8 products and thereby encourages product
9 substitution.

10 This is an important factor in
11 direct competition and substitution analysis.
12 If the retail price of a dairy beverage is in
13 excess of prices for conventional fluid milk
14 products, it is unlikely that consumers will
15 purchase the dairy beverage as a substitute for
16 milk. If the price is equal or less than fluid
17 milk prices as may have been the case for
18 filled milk in the 1960's, Class I
19 classification may be necessary to preserve
20 fluid milk sales to protect producer revenue
21 from such sales.

22 (3) Whether the product is promoted
23 or advertised in a manner intended to create
24 product substitution by consumers.

25 This factor allows USDA to use

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2 manufacturer's own promotional strategy to
3 support Class I classification. Presumably, a
4 dairy beverage marketed in a manner to induce
5 consumers to buy that product where they would
6 otherwise buy fluid milk will, in fact, create
7 product substitution as intended by the
8 manufacturer.

9 (4) Whether the product is packaged
10 and displayed to consumers in a manner
11 substantially similar to conventional milk
12 products.

13 This behavior, we believe, may play
14 a small role in a final determination of
15 product substitution in combination with price,
16 promotion, advertising and consumer perception.

17 Product placement may have no impact
18 on fluid milk displacement or substitution
19 because consumers who would not otherwise buy
20 conventional fluid milk are also drawn to the
21 dairy case for beverages such as soy milk and
22 calcium fortified orange juice.

23 (5) Whether there is significant
24 consumer feedback that indicates consumers are
25 substituting the product for conventional milk

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2 products.

3 This factor is a test of consumer
4 behavior and perception. The relevant fact is
5 that consumers are, in fact, buying a dairy
6 beverage when they would otherwise buy fluid
7 milk. This would reveal product substitution,
8 if significant, tend to support a case for
9 Class I classification.

10 Conversely, if consumers indicate
11 that they are buying a dairy beverage such as
12 Carb Countdown because they are intending to
13 reduce or eliminate fluid milk from their diets
14 in any event, the purchase of dairy beverage,
15 whether described by consumers as a milk
16 "substitute" or "alternative" to milk, does not
17 displace fluid milk sales and is not a product
18 substitution for purposes of classified pricing
19 economics.

20 If direct and substantial
21 competition with beverage milk is found by
22 these standards, Class I classification may be
23 justified. However, in order to avoid some of
24 the raw ingredient cost disincentive for new
25 product development under other proposals,

1 M. Suever - Direct Testimony

2 Hood's proposal incorporates a distribution
3 threshold that must be exceeded before a new
4 product will be classified as Class I. This
5 would allow predictability of classification
6 assumptions through the test marketing and
7 early commercialization stage of new product
8 development.

9 If a new dairy beverage is developed
10 and contains less than 6.5 percent nonfat milk
11 solid (however "milk solids" may be construed),
12 the product innovator should be assured that
13 Class I classification will not occur under the
14 foregoing criteria notwithstanding evolving
15 evidence of product substitution unless and
16 until distribution of the product reaches a
17 point of competitive significance. We have
18 selected three million pounds of distribution
19 in a federal milk marketing area as the measure
20 of such significance.

21 Finally, we believe that no
22 processor should be uncertain about whether raw
23 milk costs will be retroactively increased or
24 be faced with an audit adjustment applicable to
25 many months in the past for a new product on

1 M. Suever - Direct Testimony

2 which USDA has not yet issued a classification
3 ruling.

4 Decisions of the Secretary on a
5 number of issues including Class I price and
6 butterfat differentials demonstrate the damage
7 and disorder that retroactive pricing may
8 produce. Our experience with Carb Countdown
9 confirms this.

10 USDA Dairy Programs issued its Carb
11 Countdown classification decision March 2004
12 but applied that decision retroactively to
13 distribution of the product in 2003. This
14 resulted in a large and unexpected bills from
15 the market administrators and severely upset
16 our understanding about product classification
17 under which we developed and initially marketed
18 the product.

19 Our proposal, therefore, shifts the
20 burden on USDA to make a prompt, written
21 classification determination before a new dairy
22 beverage that otherwise falls below the 6.5
23 percent milk solids nonfat milk standard may be
24 classified as Class I.

25 CONCLUSION

1 M. Suever - Direct Testimony

2 Dairy and milk ingredient technology
3 have clearly changed in the course of a few
4 decades and even a few years. However, the
5 basic laws of economics that underlie the
6 classified pricing system have not been
7 amended.

8 Price discrimination by higher Class
9 I prices can only work for milk used in
10 products for which demand is relatively
11 inelastic: conventional fluid milk products.
12 Knee-jerk classification of beverages as Class
13 I whether applying a straw test, a pour test or
14 a protein test will harm producers, processors
15 and consumers.

16 Before any dairy beverage perceived
17 to compete with and displace sales of fluid
18 milk is classified as Class I, a rational
19 determination of direct and substantial
20 competition and product substitution should be
21 made. That is what we propose and ask the
22 Secretary to adopt if any rule amendments are
23 to be made. That concludes my testimony.

24 BY MR. VETNE:

25 Q. Mr. Suever, Hood's primary position

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2 is retention of the current fluid milk product
3 definition in Section 1000.15 of the general
4 provisions; correct?

5 A. That is correct.

6 Q. And that position is combined with
7 your perception that USDA is applying that
8 section of the rules in a manner not currently
9 permitted by the rules?

10 A. That is my belief.

11 Q. Earlier in this hearing, an exhibit,
12 Exhibit No. 14C was introduced which purports
13 to be a Power Point presentation on a study of
14 some sort for Dairy Management, Inc. which also
15 has a heading on the exhibit prepared for DFA
16 January 13, 2005. Let me ask if you at some
17 point after January 13, 2005 became aware that
18 such a study or presentation had been made?

19 A. We had heard that a presentation was
20 made.

21 Q. Did you hear also that it applied
22 specifically to Hood's product Carb Countdown?

23 A. That was our understanding.

24 Q. After hearing that, did you make an
25 effort, did Hood make an effort to secure a

1 M. Suever - Direct Testimony

2 copy of the material that had been presented?

3 A. Yes. Our public relations consumer
4 affairs department tried to get ahold of that
5 report.

6 Q. As a result of those efforts, were
7 you provided with something representing to be
8 that report?

9 A. We were provided with a Power Point
10 presentation dated April of this year.

11 Q. When did you receive that?

12 A. Within the last six weeks.

13 Q. Is the Power Point presentation that
14 you received identical to the content of
15 Exhibit No. 14C?

16 A. Based on my review, it is not
17 identical.

18 MR. VETNE: Your Honor, if you
19 recall, on behalf of Hood, I objected to the
20 receipt of Exhibit No. 14C in the first
21 instance based on its reliability and the
22 unavailability of the underlying narrative
23 study as well as the details of the study.

24 We are put in a difficult position
25 here in presenting rebuttal that we don't think

1 M. Suever - Direct Testimony

2 should be in the record to something that we
3 also don't feel should be in the record, but to
4 the extent that the Secretary considers and
5 weighs Exhibit No. 14C, I would offer as the
6 next consecutive exhibit, although somewhat
7 reluctantly, as I described the Power Point
8 presentation that was mailed to H.P. Hood.

9 JUDGE DAVENPORT: Rather than
10 marking it separately, Mr. Vetne, why don't we
11 make that the next letter attachment to
12 Mr. Suever's testimony.

13 MR. VETNE: Mr. Nightingale is
14 passing out some copies. We have a few
15 available. It would be attachment E to Exhibit
16 No. 30 so 30E.

17 BY MR. VETNE:

18 Q. Mr. Suever, you have in front of you
19 a copy of the document now marked 30E. Is that
20 the Power Point presentation that you were sent
21 upon request?

22 A. Yes, it is.

23 Q. And it was the Power Point
24 presentation, although it has a date of April
25 of 2005, that you received after requesting the

1 M. Suever - Direct Testimony

2 presentation that was made on January 13, 2005?

3 A. Yes.

4 Q. By the way, at the bottom of that
5 document, there is something in writing
6 referring to the date January 13, 2005. Do you
7 know whose writing that is?

8 A. When it was sent to us, it had that
9 notation.

10 Q. Among others, can you identify a few
11 differences in Exhibit 30E from the exhibit
12 marked 14C?

13 A. The order and presentation are
14 different, but also some of the concluding or
15 summary statements are also different.

16 Q. Did Hood either before or after
17 receiving Exhibit No. 30E request a copy of the
18 narrative study report and/or underlying data
19 from DMI or anybody else?

20 A. We contacted DMI after reviewing the
21 Power Point presentation asking for the
22 supporting documentation both the IRI data that
23 is referred to, as well as the NPD study that
24 is noted in this Power Point presentation.

25 Q. The NPD study being the exhibit

1 M. Suever - Direct Testimony

2 marked as 14D, the one that followed this?

3 A. We only can assume that given that
4 it wasn't provided to us.

5 Q. In both cases, the underlying data
6 in the report were not provided?

7 A. That is correct, whether from BMI or
8 from the initial gatherers of the survey
9 information who we contacted.

10 Q. Do you have any further remarks you
11 care to make before people ask you questions?

12 A. I do not.

13 MR. VETNE: Your Honor, I
14 request that Exhibit No. 30 with its
15 Attachments A through E be received.

16 JUDGE DAVENPORT: Mr. Beshore?

17 MR. BESHORE: I would object
18 to Attachment B of Exhibit No. 30. I don't
19 have any objection to the remainder of the
20 exhibit including Attachment E.

21 JUDGE DAVENPORT: State the
22 basis for your objection.

23 MR. BESHORE: The basis for
24 the objection is that it's a collection of
25 e-mails. I'm not questioning the authenticity

1 M. Suever - Direct Testimony
2 of the e-mails, but this is the second current
3 proceeding in which parties have attempted to
4 present information for the record for the
5 Secretary by assembling e-mails sent from
6 people out there, consumers or whatever. They
7 are hearsay statements that are offered for the
8 truth of those statements. The declarants are
9 unknown and, of course, unavailable and it is
10 just not the manner in which we should be
11 building or proliferating the record here, and
12 I object to its receipt.

13 JUDGE DAVENPORT: Response to
14 that, Mr. Vetne?

15 MR. VETNE: Yes. I would like
16 to ask the witness a couple of questions before
17 I respond further if that's all right.

18 JUDGE DAVENPORT: All right.

19 BY MR. VETNE:

20 Q. Mr. Suever, does Hood have a system
21 whereby consumers may respond and comment
22 directly to Hood concerning its products?

23 A. We have both an e-mail system
24 available on the Internet as well as an 800
25 number.

1 M. Suever - Direct Testimony

2 Q. Are these data that you regularly
3 assemble and compile as part of your business
4 records and rely on in your evaluation of your
5 products?

6 A. It certainly is.

7 MR. VETNE: Your Honor, this
8 is not the type of data that the rules of
9 practice would exclude because it is not the
10 type upon which a responsible person is
11 accustomed to rely. In fact, this witness has
12 indicated that it would be his business and in
13 the responsibilities of his business, he relies
14 on them. They are a collection and part of the
15 business records. They meet that standard
16 certainly more than either Exhibit No. 14C or
17 14D.

18 MR. BESHORE: Your Honor, I
19 think the last statement is preposterous to
20 suggest that anonymous e-mails are more
21 reliable than studies done by known reputable
22 firms such as --

23 JUDGE DAVENPORT: Reaching
24 that particular point, I don't think it's
25 necessary to do. In other words, this is the

1 M. Suever - Cross - by Mr. Cryan
2 type of material which is not necessarily
3 indicative of anything more than the fact that
4 there are responses that have been received and
5 a collection has been made of them.

6 For that reason, the Administrator
7 certainly would give them whatever weight he
8 sees fit such as he is willing to do with
9 respect to this exhibit, so the objection is
10 overruled. In other words, they will be
11 admitted for whatever weight the Administrator
12 chooses to give them.

13 MR. VETNE: Thank you, Your
14 Honor. The witness is available for questions.

15 JUDGE DAVENPORT: Examination
16 of this witness?

17 -----

18 CROSS-EXAMINATION

19 BY MR. CRYAN:

20 Q. First of all, Mike, on behalf of
21 National Milk, we believe that Carb Countdown
22 is a positive product per se, and we wish you
23 success with it.

24 A. Thank you.

25 Q. You're welcome. My question is

1 M. Suever - Cross - by Mr. Cryan
2 either to you or Mr. Vetne were discussing the
3 comparison of these two Power Point
4 presentations. One of you said that the
5 underlying numbers were different. I didn't
6 see any underlying numbers that were any
7 different.

8 A. What I suggested is that the order
9 or sequencing of the charts and so on are in
10 different order, but I'm not aware that the
11 numbers themselves differ. But the conclusion
12 pages in one is different than the conclusion
13 or summary in the other.

14 Q. Yes, I see that. Would you say that
15 the two sets of conclusions could be
16 interpreted as a different way of looking at
17 the same, essentially the same conclusion?

18 A. I don't know what went behind those
19 that made one determination from looking at
20 data versus the other. Apparently it's the
21 same. DMI apparently took -- and I can only
22 infer or assume that DMI took a basic amount of
23 data from IRI and NPD that they have noted here
24 and come to two different conclusions.

25 Q. I hope you would agree with me that

1 M. Suever - Cross - by Mr. Cryan
2 the most important thing about either of these
3 would have to be the numbers, that the
4 department and the administrator will have to
5 come to their own conclusions about what the
6 numbers mean?

7 A. Unfortunately, they are probably
8 going to have the same difficulty that I had
9 given they don't have nor do I have access to
10 the core data and have not been provided with
11 it.

12 JUDGE DAVENPORT: Neither have
13 I. Thank you.

14 MR. CRYAN: Thank you.

15 JUDGE DAVENPORT: Mr. Beshore?

16 -----

17 CROSS-EXAMINATION

18 BY MR. BESHORE:

19 Q. Thank you. Marvin Beshore for Dairy
20 Farmers of America. Good afternoon,
21 Mr. Suever.

22 A. Good afternoon, sir.

23 Q. Do you have available to you Exhibit
24 No. 14B?

25 A. I don't have it.

1 M. Suever - Cross - by Mr. Cryan

2 Q. I can give you mine.

3 A. Thank you.

4 Q. Exhibit No. 14B you have in front of
5 you now; correct?

6 A. Yes.

7 Q. Do you recall that when Dr. Cryan
8 testified?

9 A. I do.

10 Q. I'm not an economist. I don't think
11 you're an economist either; right?

12 A. I am not.

13 Q. If we think about classification
14 here just from a nontechnical economist
15 perspective and sort of as a matter of common
16 sense, if you take your product Carb Countdown
17 and you look at the array of products on
18 Exhibit 14B and you're just going to try to
19 figure out which group the product is more
20 similar to, is it more similar to Yoo-Hoo or to
21 the fluid milk products?

22 A. In my direct testimony, I suggested
23 a five-step approach that the Department should
24 utilize in order to help them come to that
25 determination.

1 M. Suever - Cross - by Mr. Cryan

2 Q. I'm asking you to take a different
3 approach. I'm asking you to just look at the
4 sets of products represented on 14B which is a
5 group of beverages presently in Class II
6 because they have less than 6.5 percent nonfat
7 milk solids and Class I products. I'm just
8 asking you to just apply some common sense and
9 intuition to those two sets of products.

10 On the one hand, you have
11 Frappucino, Yoo-Hoo, Folgers Jakata, 80 &
12 Sunny, Raging Cow. On the other hand, you have
13 Lactate 100, Hershey's chocolate milk, whole
14 milk, reduced fat milk, skim milk. Which group
15 is Carb Countdown most similar to?

16 A. Your preface was that the category
17 in the lower section was predicated on an
18 assumption that all of those products were less
19 than 6-1/2 percent?

20 Q. Well, they are all Class II.

21 A. Since I have stipulated in direct
22 that Carb Countdown is also less than 6-1/2
23 percent, I would say that my product would fit
24 with the Class II products.

25 Q. If you don't have any knowledge of

1 M. Suever - Cross - by Mr. Cryan
2 the chemical composition of the products, you
3 have Starbucks, you have all of those Class II
4 products and you have the milks and lactate, et
5 cetera on the other side, which is it more
6 similar to?

7 A. I would say the Carb Countdown two
8 percent chocolate product from a case profile
9 if I were a consumer picking up that product
10 versus the Raging Cow product, I would say they
11 were virtually indistinguishable from a flavor
12 perspective if I knew nothing else about the
13 product.

14 Q. Well, you don't know the flavors.

15 A. I just suggested that I had tasted
16 the product and that they were both chocolate
17 products. I would say that they were virtually
18 indistinguishable from one another as a
19 consumer.

20 Q. Because they were both chocolate.
21 So it's your testimony here today to this
22 secretary that when you assemble those two
23 groups of products, Carb Countdown is more like
24 the Class II group than the Class I group?

25 A. You're attempting to refocus my

1 M. Suever - Cross - by Mr. Cryan

2 direct which, in fact --

3 Q. Yes, I am. This is cross.

4 A. Which, in fact, listed five
5 different levers that we suggest that USDA
6 would use to help them make the determination,
7 not just a single attribute. We are suggesting
8 five different attributes to help them
9 collectively make a determination.

10 Q. I was trying to infuse a sixth
11 there, maybe some common sense. Can we work
12 with that?

13 A. In my dealings over 25 years with
14 USDA, I have always assumed that they used
15 common sense in making a determination, so I
16 assumed that the sixth one was already present.

17 Q. If we just isolate that one and use
18 it, are you still sticking with Carb Countdown
19 in Class II?

20 A. Yes, sir.

21 MR. BESHORE: Thank you.

22 JUDGE DAVENPORT: Mr. Beshore,
23 by virtue of looking at this again, I see that
24 what I did previously was mark the other
25 exhibits A through D. Instead they really

1 M. Suever - Cross - by Ms. Carter
2 should be C through E at this point.

3 (Discussion held off the
4 record.)

5 JUDGE DAVENPORT: Is there
6 other examination of this witness? Ms. Carter?

7 -----

8 CROSS-EXAMINATION

9 BY MS. CARTER:

10 Q. Good afternoon. Antoinette Carter
11 with the USDA. Just for clarification
12 purposes, you indicate that you support leaving
13 the current definition unchanged in terms of
14 the 6.5 nonfat milk solid standard?

15 A. That is correct.

16 Q. In your prepared statement, you
17 suggest that -- and I can try to find the
18 page -- on page 9 you state or indicate that
19 FDA 8.25 percent nonfat milk solid standard be
20 used by USDA. Could you clarify? There seems
21 to be an inconsistency in terms of what you're
22 stating in your prepared statement.

23 A. I will attempt to clarify. It is my
24 intent by making notation of that to FDA
25 standard of identity that the department would

1 M. Suever - Cross - by Ms. Carter
2 utilize the 8.25 percent somewhat as a flag for
3 products that are in the realm of what FDA
4 standard of identity have indicated as a Class
5 I product, but that the 6.25 percent would
6 still be the threshold that USDA could utilize.

7 The 8.25 percent was simply meant to
8 be a flag that it would start to look at the
9 other five levers that I have suggested in my
10 direct so that it would start collecting data,
11 looking at information because a product
12 fitting into this profile, therefore, may at
13 some time or may specifically move into
14 something that the Department is going to be
15 asked to make a determination on.

16 Q. You listed a number of criteria, if
17 you will, that USDA would have to include in
18 terms of an analysis of a new product in making
19 the classification determination. How do you
20 envision if your proposal is adopted it being
21 administered?

22 A. When having conversations with your
23 department, a number of times in conversation I
24 was asked other than a specific criterion of a
25 test, if you will, solids test in this case, if

1 M. Suever - Cross - by Ms. Carter

2 that's not sufficient, what other tests or what
3 other criteria should the department utilize.

4 What I tried to do in my direct is respond by
5 giving five different levers, if you will, that
6 the Department could utilize in helping to make
7 a determination when something is in question.

8 Q. The information that would be
9 included in that analysis, would that be
10 something that, say, if you're using a product
11 that H.P. Hood is experiencing, would the
12 handler be providing that information to USDA
13 at the time that they are requesting that the
14 product determination be made or what do you
15 envision happening?

16 A. I think I tried to deal with that a
17 little bit in that I have asked or suggested
18 that we have a cooling off period, if you will,
19 or a period of time where a new product is
20 given a Class II classification while data is
21 being collected both by the processor or
22 handler as well as USDA. So I tried to deal
23 with that opportunity to collect information,
24 real live market data by virtue of this warming
25 in period, if you will.

1 M. Suever - Cross - by Ms. Carter

2 Q. Generally when products are
3 classified by USDA prior to the product
4 entering the market, a lot of the information
5 that is included in those five steps is not
6 available for at least some period of time
7 after that product has been on the market, so I
8 guess we are having a difficult time
9 understanding just how we could implement your
10 proposal as it is proposed.

11 A. Again, when meeting with your
12 department, it became clear to me that simply
13 the solids nonfat test standard or threshold
14 was not the only criteria and there was form
15 and use that was being evaluated or used to
16 make determination and there was other
17 criterion that was described to me that played
18 a role specifically in the determination by the
19 department about Carb Countdown.

20 Because of those questions and
21 concerns that the Department had, again rather
22 than trying to deal with theoretical market
23 conditions or circumstances, I have suggested
24 this period of time to collect live data in the
25 market, and it would then be the responsibility

1 M. Suever - Cross - by Mr. Wilson
2 of the processor-handler and the Department to
3 evaluate these five criteria and make a
4 determination at the end of that period as to
5 whether the product still fits the category
6 that it was originally classified at or should
7 be reclassified at that time.

8 MS. CARTER: Thank you.
9 That's all I have right now.

10 JUDGE DAVENPORT: Other
11 examination? Mr. Wilson?

12 -----

13 CROSS-EXAMINATION

14 BY MR. WILSON:

15 Q. Todd Wilson, USDA.

16 A. Good afternoon, sir.

17 Q. Good afternoon. In some of your
18 testimony, you indicated that your product is
19 marketed to people that would not necessarily
20 be buying milk?

21 A. Or had turned away from milk.

22 Q. Or had turned away from it?

23 A. Yes.

24 Q. Should that be a determination?

25 A. We believe so, yes, and I have

1 M. Suever - Cross - by Mr. Wilson

2 indicated that in my direct.

3 Q. Are you aware of a product by the
4 name of Lactaid?

5 A. I am.

6 Q. Do you know if it's a fluid milk
7 product?

8 A. It is currently classified as fluid
9 milk, Class I milk.

10 Q. So it's a fluid milk product. Is
11 that product marketed to a specific consumer in
12 a similar fashion that Carb Countdown is
13 marketed to a specific consumer?

14 A. They are both targeting different
15 consumer groups, but they are targeting
16 consumer groups. But they have different
17 attributes, different characteristics and
18 different fundamental makeup.

19 Q. Would the consumer groups that are
20 drinking Lactaid, in your opinion, be drinking
21 milk if Lactaid was not available?

22 A. I suspect not.

23 Q. Just for clarification, in
24 Dr. Stephenson's scenarios that you had
25 mentioned, you have a copy of Exhibit No. 23?

1 M. Suever - Cross - by Mr. Wilson

2 A. Yes, I do.

3 Q. Table 6, second page from the end,
4 could you tell me if there is a product
5 somewhere on there that Carb Countdown
6 resembles?

7 A. Carb Countdown would resemble the
8 La Cart.

9 Q. The class used calculation, Roman
10 numeral I as in Class I, it's my understanding
11 that with this scenario, this maximized
12 producer revenues by being in Class I for this
13 particular product?

14 A. That's what I heard under his
15 testimony, yes.

16 Q. Beginning on page 8, if I understand
17 your testimony, the last paragraph you said
18 that Class I designation would likely produce a
19 lower weighted average return to producers. Am
20 I misunderstanding or confused?

21 A. What I indicated is that it would
22 likely produce lower weighted average returns
23 over the long run, and that's cumulative
24 returns not specifically related to that
25 product or how it's classified but to also take

1 M. Suever - Redirect - by Mr. Vetne
2 into consideration milk derivatives, milk
3 ingredients that would be impacted as well.

4 Again, my focus in looking at this
5 study and citing it was that I was looking at
6 the producer farm gate price which is a blended
7 price, not just a specific Class I component.

8 MR. WILSON: That all I have.
9 Thank you.

10 JUDGE DAVENPORT: Other
11 examination? Mr. Vetne?

12 MR. VETNE: Just a little bit
13 of redirect.

14 -----

15 REDIRECT EXAMINATION

16 BY MR. VETNE:

17 Q. Mr. Suever, Todd Wilson asked you
18 some questions about a product called
19 "Lactaid." Is that a product that is processed
20 and sold by H.P. Hood?

21 A. By exclusive license, yes.

22 Q. Is that a product that is labeled as
23 milk, sold as milk and meets the FDA standards
24 of identity for milk?

25 A. Yes, in all counts.

1 M. Suever - Redirect - by Mr. Vetne

2 Q. The list of criteria you propose to
3 put in the regulations, it's your intent that
4 they apply to products that contain less than
5 6.5 percent solids nonfat?

6 A. That was my intention, yes.

7 Q. It's your intention in including
8 those to refer to products the container of
9 which and the content of which is less than 6.5
10 percent solids, not fat?

11 A. The material in the container
12 itself, yes.

13 Q. Which describes Carb Countdown?

14 A. That is correct.

15 Q. Carb Countdown is other than Class I
16 because USDA has applied criteria such as these
17 to up-classify it notwithstanding the content
18 of the package; is that correct?

19 A. That's my understanding in a lengthy
20 conversation with the Department, yes.

21 Q. You proposed in Hood's second
22 preferred proposal, the first proposal is no
23 change, but the Hood second proposal is to give
24 the Department express authority in the rules
25 to do in the future that which they do now

1 M. Suever - Redirect - by Mr. Vetne
2 without express authority?

3 A. That's correct.

4 Q. Let me ask you about Lactaid. You
5 produce both Carb Countdown and Lactaid?

6 A. We do.

7 Q. And one is specifically marketed
8 towards consumers that are lactose intolerant.
9 That is Lactaid; correct?

10 A. Yes.

11 Q. And the other contains lactose and
12 is marketed to a different population group?

13 A. Correct.

14 Q. Since the introduction of Carb
15 Countdown, how have your Lactaid sales fared?

16 A. Our Lactaid sales have continued to
17 grow at almost double digit figures.

18 Q. At one point you refer to your
19 proposal or the existing rule as the 6.25
20 percent. Was that an error? The current rule
21 reads 6-1/2 percent?

22 A. Yes. That was an error on my part.

23 Q. In reading your testimony, you made
24 one correction, and that was in reference to
25 the story boards you made at Burrell. Did you

1 M. Suever - Redirect - by Mr. Vetne
2 intend in your narrative to make any other
3 specific corrections?

4 A. Not intentionally.

5 MR. VETNE: Thank you.

6 MR. NIGHTINGALE: Paul
7 Nightingale, general counsel for H.P. Hood. I
8 want to clarify a point that was discussed
9 earlier in Mr. Suever's testimony.

10 There is a handwritten notation on
11 the DMI presentation that we had received that
12 has been introduced into evidence here and that
13 handwritten notation is actually my own
14 handwritten notation. I wrote that on this
15 document believing that that was the date of
16 the meeting. I don't know if it was or wasn't.
17 I just wanted to clarify that point for the
18 record.

19 MR. SUEVER: It was present
20 when I received it.

21 MR. NIGHTINGALE: From me,
22 right.

23 BY MR. VETNE:

24 Q. I have given away all of my copies
25 of Exhibit No. 30D. 30D is the story board

1 M. Suever - Recross - by Ms. Carter
2 that was provided to Hood. Is one of the
3 conclusions that was not in the Exhibit No. 14
4 package that is in the material that is
5 provided to you that is different a conclusion
6 that the new low carb milk beverages recently
7 introduced appear to have retained milk
8 consumption among low carb dieters?

9 A. That is expressly noted, yes.

10 Q. That was either expressly or
11 inadvertently omitted from whatever is in the
12 Exhibit No. 14 package?

13 A. It was not present in Exhibit No.
14 14.

15 MR. VETNE: No further
16 questions.

17 JUDGE DAVENPORT: Ms. Carter?

18 -----

19 RECROSS-EXAMINATION

20 BY MS. CARTER:

21 Q. If I can direct your attention to
22 page 11 of your prepared statement, the first
23 full paragraph just to clarify, under the
24 standard No. 5, is it my understanding that in
25 order for a product to be classified as Class

1 M. Suever - Recross - by Ms. Carter

2 I, its distribution would have to exceed three
3 million pounds?

4 A. Again, I was focusing on products
5 that were less than 6-1/2 percent solids nonfat
6 so for products that fit that category, yes.

7 Q. What is the basis for justification
8 for that three million pound statement?

9 A. The USDA finding of fact related to
10 producer-handlers utilize the three million
11 pound threshold as something that wasn't overly
12 burdensome or significant in the marketplace,
13 and that's where I pulled the three million
14 pounds from.

15 Q. Just to clarify, you indicate
16 distribution in a federal milk marketing area.
17 You mean in a single federal milk marketing
18 area or combined distribution in federal milk
19 marketing areas?

20 A. A as in singular.

21 MS. CARTER: Thank you.

22 JUDGE DAVENPORT: Is there any
23 other examination of Mr. Suever? That being
24 the case, let me call upon Mr. Alby and
25 Ms. Taylor.

1 S. Taylor - Direct Testimony

2 MR. ALBY: Good afternoon,
3 Your Honor. My name is Jon Alby. I'm senior
4 staff attorney for Leprino Foods Company.
5 Appearing on behalf of Leprino Foods Company
6 today, we have one witness, Sue Taylor, who is
7 an expert in dairy policy area and will be
8 reading a statement after a few preliminary
9 questions and introductory remarks.

10 JUDGE DAVENPORT: Very well.
11 Ms. Taylor, your statement has been marked as
12 Exhibit No. 31.

13 MS. TAYLOR: Thank you.
14 (Exhibit No. 31 was marked for
15 identification.)

16 -----
17 SUE TAYLOR
18 a witness herein, having been first duly sworn,
19 was examined and testified as follows:

20 DIRECT EXAMINATION

21 BY MR. ALBY:

22 Q. Mrs. Taylor, can you state your
23 position with Leprino Foods Company?

24 A. I'm currently the vice president of
25 dairy policy and procurement for Leprino Foods.

1 S. Taylor - Direct Testimony

2 I have led the dairy policy and procurement
3 efforts for Leprino since 1995.

4 Q. Can you briefly describe the Leprino
5 Food Company's operations?

6 A. Leprino is a mozzarella manufacturer
7 with nine plants located within the United
8 States. Six are regulated in the federal order
9 system or receive milk regulated by the federal
10 order system. Three are located in the State
11 of California.

12 One of the reasons that I'm
13 appearing here today is those plants in the
14 process of cheese making also generate whey and
15 the whey that's generated will all be impacted
16 regardless of the source in terms of in the
17 marketplace by some of the decisions coming out
18 of this hearing.

19 Q. Could you also again explain your
20 experience and role as vice president of dairy
21 policy and procurement of Leprino?

22 A. Sure. My responsibilities cover a
23 broad area that generally would be considered
24 part of dairy economics. That's the policies
25 of use, procurement issues, market analysis,

1 S. Taylor - Direct Testimony

2 forecasting.

3 Prior to my position at Leprino
4 which, again, I joined in 1995, I had worked in
5 a few other positions that also were related to
6 policy and procurement.

7 I shifted over to this side of the
8 industry in 1989 working at Sorrento Foods as a
9 dairy economist/production analyst through
10 early 1992. Then I had a dairy economics
11 consulting business from 1992 through 1994.

12 JUDGE DAVENPORT: Counsel, it
13 looks like some of this is being covered by her
14 statement and it's a little different format.
15 Why don't you just let her read her statement.

16 MR. ALBY: Will do, Your
17 Honor. I wanted to break it up a bit.

18 MS. TAYLOR: My thought
19 actually was to not read that first page of the
20 statement.

21 JUDGE DAVENPORT: Very well.

22 MS. TAYLOR: Just as far as
23 the balance of what is covered in the expertise
24 area is that my background is actually
25 agricultural education, both a Master's and a

1 S. Taylor - Direct Testimony

2 Bachelor's with a heavy focus in agricultural
3 economics. I will start reading my statement
4 them from page 2.

5 -----

6 DIRECT TESTIMONY

7 MS. TAYLOR: In the face of
8 rapidly advancing technologies and the chilling
9 effect that Class I regulation has on the use
10 of dairy ingredients in many existing and new
11 product formulations such as non-traditional
12 dairy beverages, Leprino believes that it is
13 time to refocus the Class I fluid milk product
14 definition on beverage milk and those products
15 that directly compete with beverage milk.

16 To best achieve that change, Leprino
17 supports the adoption of many of the concepts
18 embodied in Proposal #5 (Hood). Specifically,
19 we support defining Class I products as those
20 products that fit the standards of identity for
21 milk and cultured buttermilk and those products
22 that substantially compete with those products.

23 Alternatively, if the current Class
24 I definition structure is maintained, Leprino
25 supports the exclusion for nutritional drinks

1 S. Taylor - Direct Testimony

2 (Proposal #10) and supports the exclusion of
3 products containing 20% or more yogurt
4 (Proposal #9).

5 If the department does not grant the
6 exclusions for nutritional drinks and beverages
7 containing 20 percent or more yogurt, Leprino
8 strongly opposes the adoption of the protein
9 standard to replace the SNF standard.

10 The issue of defining Class I fluid
11 milk products is very complex. The current
12 definition casts the net broadly ("fluid milk
13 products in fluid or frozen form...that are
14 intended to be used as beverages") and then
15 provides specific exclusions. These exclusions
16 include eliminating products for composition
17 (fat above 9 percent or SNF below 6.5 percent)
18 and concentration levels.

19 Additionally, specific products
20 (evaporated milk, sweetened condensed milk, and
21 "formulas especially prepared for infant or
22 dietary use (meal replacements) that are
23 packaged in hermetically-sealed containers) are
24 specifically excluded. Several exception
25 terms, such as "formulas prepared for dietary

1 S. Taylor - Direct Testimony

2 use" and "hermetically-sealed containers" lack
3 clarity.

4 Unintended consequences are being
5 generated by the existing Class I definition in
6 the current environment of fractionation and
7 packaging technology advances. Some parties to
8 this hearing contend that one unintended
9 consequence is the potential classification of
10 low carb drinks that resemble milk and are
11 marketed directly against milk as Class II
12 products.

13 While I do not dispute that
14 conclusion, I believe there is a more troubling
15 second unintended consequence that has the
16 potential of reducing producer revenues to a
17 much greater extent than the omission of low
18 carb milk-like products from Class I.

19 Specifically, I am concerned about
20 the dampening effect the existing definition
21 has on the demand for dairy ingredients in what
22 I will term non-traditional beverages and
23 smoothie type products. These products do not
24 resemble milk and are not marketed directly
25 against milk but represent significant markets

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2 for dairy ingredients.

3 Increasingly, products are being
4 engineered from ingredients that did not even
5 exist ten years ago. In the case of dairy,
6 they products have benefitted from the
7 technological advances with the development of
8 more highly specialized fractions that can be
9 effectively marketed into a broader set of food
10 applications than ever before.

11 Whey protein manufacturers have made
12 substantial progress in addressing the heat
13 stability concerns that had historically been a
14 limiting factor in whey protein applications.
15 Cornell and other universities have also made
16 progress fractionating milk prior to
17 manufacturing products.

18 They have shown, for example, that
19 it is possible to extract the milk serum
20 proteins prior to cheese making. The milk
21 serum proteins are what we think of as whey
22 proteins once the milk has undergone the
23 cheese-making process.

24 Concurrent with the advances in
25 technology in dairy, advanced fractionation

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2 technology has been applied across a broad
3 spectrum of ingredients resulting in an almost
4 exponential growth in ingredient options.

5 In many cases, the fractionation has
6 contributed to the reduction or elimination of
7 unfavorable attributes of specific ingredients,
8 resulting in many new ingredients that compete
9 more effectively across a broader spectrum of
10 applications.

11 Determining the classification of
12 dairy products by specific component levels has
13 become increasingly difficult in light of these
14 advances in fractionating technology. It is
15 also much riskier. I believe that the current
16 definition has a chilling effect on dairy
17 ingredient demand that extends far beyond what
18 is known by the Department or the industry.

19 Based upon discussions that I had
20 with beverage marketers as part of my
21 consulting business prior to joining Leprino, I
22 believe that product formulators are
23 constraining their use of dairy ingredients in
24 products that would otherwise be classified as
25 Class I in order to avoid both the regulatory

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2 burden and the increased costs associated with
3 the production and marketing of Class I
4 products.

5 While this concerned me ten years
6 ago, it is of much greater concern today
7 because of the significantly larger market
8 opportunity that is being constrained.

9 Additionally, proposals before the
10 Department to replace the SNF standard with a
11 protein standard are likely to establish even
12 further constraints, particularly as it relates
13 to smoothies, products containing yogurt and
14 the nontraditional beverage category.

15 The difficulties with the current
16 definition are evidenced by recent challenges
17 to its application. The 15(a) administrative
18 appeal proceeding regarding the classification
19 of low carb milk-like products and the changes
20 in procedures implemented by the Department in
21 recent years to include whey ingredients in the
22 calculation of the SNF content of beverages for
23 the purposes of determining whether a beverage
24 is a Class I or Class II product reflects the
25 challenge.

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2 Additionally, I have been told by
3 Department staff that the current application
4 of the Class I definition criteria to
5 nontraditional beverages is inconsistent.

6 My understanding is that these
7 non-traditional beverages are generally not
8 currently priced as Class I, either because the
9 inclusion of dairy ingredients has been
10 constrained to fall below the 6.5 percent SNF
11 limit or because the Department has considered
12 their volumes to be de minimus and has not
13 pursued their regulation as Class I products.

14 However, I am concerned that
15 adoption of a protein standard in the absence
16 of a clarification in the definition that would
17 ensure an exception for these products could
18 result in the regulation of some of these
19 beverages as Class I.

20 While our corporate concern is
21 centered on the impact on the market demand for
22 dairy ingredients including whey proteins, I
23 also would contend that producers net a lower
24 overall price under the current definition or
25 the NMPF proposal than would be achieved if the

1 S. Taylor - Direct Testimony

2 Class I definition was narrowed.

3 Our opposition to the replacement of
4 the SNF standard with a protein standard is
5 rooted in our concern that the modification as
6 NMPF proposes (Proposal 7) will only exacerbate
7 the problem discussed above as it relates to
8 demand for whey proteins unless additional
9 exclusions are also adopted.

10 The NMPF proposal has been
11 characterized as an updating in the accounting
12 under the orders to reflect advances in
13 fractionation technology. Although the
14 proponents of this proposal have stated that
15 they do not intend that products currently
16 priced as Class II be moved up to Class I, that
17 is not the likely practical effect.

18 The methodology used by NMPF to
19 develop the new protein criteria translates the
20 existing SNF criteria to a protein criteria
21 based upon the protein to SNF ratio in raw
22 milk. To the extent that products close to the
23 6.5 percent SNF threshold contain a higher or
24 lower protein to SNF ratio than does raw milk,
25 those products may be shifted between Class I

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2 and II under the NMPF proposal.

3 It is logical to assume that protein
4 beverages have a higher protein to SNF ratio
5 than does raw milk. Consequently, protein
6 drinks using dairy ingredients will likely be
7 moved from Class II to Class I under the NMPF
8 proposal.

9 Additionally, many smoothie products
10 are currently formulated at less than 6.5
11 percent SNF to maintain a Class II
12 classification but contain significant
13 quantities of whey protein.

14 Therefore, I would expect many of
15 these products to be moved from Class II to
16 Class I under the proposal. A more thorough
17 understanding of the products that would be
18 impacted under the proposal is necessary to
19 understand the demand implications for dairy
20 ingredients in those products.

21 The products that I am most
22 concerned about include beverages that would
23 not be confused with milk. These beverages are
24 being marketed as sport or protein drinks or
25 smoothies.

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2 The manufacturers of these typically
3 highly flavored products can choose between
4 dairy and non-dairy ingredients without
5 substantially impacting the identity of the
6 product.

7 While my primary concern is rooted
8 in negative impacts on whey and whey product
9 demand, a similar case could be made for other
10 dairy ingredients. However, my testimony will
11 focus specifically on the potential impact on
12 whey and whey products.

13 Product developers consider many
14 factors when selecting ingredients to be
15 incorporated in product formulations. These
16 factors include the functionality, the
17 contribution of each ingredient to the end
18 product characteristics, and cost, among other
19 things. In many cases, several alternative
20 ingredients can be used to provide the desired
21 nutritional or functional profile.

22 Whey and whey products compete with
23 several non-dairy ingredients in product
24 formulas. Under the proposals that would adopt
25 a protein compositional standard, the

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2 competitive position of high protein whey
3 fractions, such as whey protein concentrates
4 and isolates, would be most highly impacted.

5 Proteins are generally added to
6 foods or beverages for their contribution to
7 the nutritional profile of the finished product
8 or to enhance the structure and mouth feel.

9 The most commonly referenced
10 competitive ingredients tend to be soy-based,
11 whether they are soy protein concentrates or
12 soy protein isolates. These are the most
13 likely substitutes for whey proteins in
14 applications where they are being used for
15 their protein contribution.

16 However, many other ingredients such
17 as wheat protein isolates and vital wheat
18 gluten/isolates can also be substituted to
19 achieve the desired protein contribution.
20 Several different ingredients can be
21 substituted for whey proteins that are being
22 used to provide structure and mouth feel.

23 An expanding family of hydrocolloids
24 can substitute for whey protein to achieve
25 desired structure and mouth feel. These

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2 products can be used individually or in
3 combination with starches and gums. Product
4 developers are very skillful in combining these
5 proteins in developing products.

6 The competitive issues facing the
7 whey complex are becoming more acute over time
8 as improvements are made in alternative
9 ingredients. Soy historically has been
10 criticized for its beanie flavor and its use in
11 beverages has been limited to highly flavored
12 products that were capable of masking the
13 flavor.

14 However, with the more recent
15 development of low flavor soybeans and improved
16 refining techniques, flavor is becoming less of
17 a constraint on soy use. Most every marketer
18 of soy proteins now market low flavor protein
19 with reduced beanie flavor. Archer Daniels
20 Midland, Dupont, Solae, and Central Soya are
21 just a few of these companies.

22 Several protein drinks already
23 contain substantial volumes of soy protein.
24 St. Louis-based Solae and Yoplait in France
25 have recently announced the introduction of soy

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2 in a new yogurt being marketed in France with
3 health claims touting both the dairy and soy
4 benefits.

5 Beyond the functional considerations
6 in selecting ingredients, an important
7 additional factor in selecting ingredients to
8 be used in a particular formulation is the
9 cost.

10 Cost considerations include the
11 direct procurement costs and any costs
12 associated with regulation. The regulatory
13 costs include payment obligations into the pool
14 and the costs incurred to satisfy reporting and
15 other requirements of the order. The impact of
16 this regulatory burden should not be
17 underestimated.

18 Companies that have not historically
19 been subject to Federal Order regulation find
20 the reporting/audit requirements to be
21 extraordinarily burdensome and the Federal
22 Order System complicated and difficult to
23 understand.

24 From discussions during my
25 consulting years that I had with marketers of

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2 products that had the potential of being Class
3 I products, I found that non-dairy companies
4 tend to have a visceral reaction regarding the
5 potential burdens. These discussions often
6 concluded with a point that classification as a
7 Class I product would result in the product
8 losing viability.

9 In such situations, the product
10 formulators were sent back to the lab to
11 reformulate the product using other ingredients
12 to ensure that the product did not fall within
13 the definition of a Class I product.

14 The Department must be cautious not
15 to establish a regulatory disadvantage for
16 dairy ingredients that will result in reduced
17 market demand. Given the wide array of
18 alternative ingredients, an increase in cost or
19 regulatory burden would do just that and more
20 than offset any incremental gains realized by
21 producers as a result of Class I classification
22 for such products.

23 To provide some insight regarding
24 the impact of the proposals on existing
25 products, I purchased a limited number of

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2 products from two stores in Denver.

3 Two smoothie-type products (Odwalla
4 and Naked) were purchased from a health food
5 store. These products were located in
6 refrigerators placed on end caps on aisles away
7 from the dairy section. The other six products
8 were purchased from a nutritional supplement
9 store that notably did not sell milk.

10 Although they were refrigerated at
11 the point of sale to allow for immediate
12 consumption, these products are all shelf
13 stable at room temperature. To clarify, that
14 comment refers to the sports beverages. The
15 Odwalla and Naked are not shelf stable in
16 temperature. The products selected are all
17 marketed as sport or high protein beverages.
18 Some include dairy ingredients and some do not.

19 Leprino targets applications using
20 vegetable proteins (soy and wheat), caseins,
21 and milk protein concentrate as potential
22 markets for whey proteins. With recent
23 advances in technology, whey protein could be
24 formulated into all of these products.

25 However, it is relevant to review

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2 the classification of these products presuming
3 that a protein composition criteria, such as
4 that proposed by National Milk (NMPF) is
5 adopted.

6 Since insufficient data is available
7 on the nutrition panel to segregate the portion
8 of the protein that is from dairy-derived
9 ingredients and because we view the entire
10 protein composition to be a dairy protein
11 opportunity, it is instructive to review the
12 potential protein usage within each product.

13 Based upon the nutritional panel
14 data, I estimated the protein percent in each
15 of these products. I assumed 28.35 grams of
16 protein per ounce and divided the ounces of
17 protein by the fluid ounces of finished
18 product. I did not have the specific gravities
19 of the products so could not be more precise,
20 but I believe the methodology is materially
21 accurate.

22 The following table summarizes the
23 estimated protein and current sources of
24 protein for the eight products. This table, by
25 the way, is frank for low protein percent and

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2 high protein percent.

3 The lowest protein product that we
4 have is the Accelerade Fruit Punch. It has
5 whey protein isolate in it as its source of
6 protein. The estimated protein is 1.8 percent
7 so it would clearly not be a Class I product
8 under any of the proposals that we are talking
9 about today.

10 The Odwalla Super Protein has 4.4
11 percent protein and currently they are getting
12 that protein from soy sources, soy milk and soy
13 protein isolate.

14 The Naked product has 6.2 percent
15 protein and that is sourced from a combination
16 of whey protein concentrate and soy protein
17 isolate.

18 The Atkins Advantage Shake is 6.4
19 percent protein from a combination of calcium
20 caseinate and whey protein concentrate.

21 The Isopure is 7.1 percent protein
22 and that is from a whey protein isolate. The
23 GNC Pro Performance Protein is 8.0 percent
24 protein, currently just a soy protein isolate
25 source.

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2 The EAS Myoplex is 8.7 percent
3 protein, combination of sources from milk
4 protein concentrate, calcium caseinate and whey
5 protein isolate.

6 Finally, the Met-RX Ready-to-Drink
7 40 is 9.4 percent protein from a combination of
8 milk protein concentrate, milk protein isolate,
9 calcium sodium caseinate and hydrolyzed wheat
10 protein.

11 Based upon the protein compositional
12 criteria alone (putting aside for the moment
13 the Class I exception for products in meal
14 replacements in hermetically-sealed
15 containers), all products on the above list
16 with the exception of Accelerade would be
17 classified as Class I if they used only
18 dairy-derived proteins under the National Milk
19 proposal. Yet, none of these products could be
20 confused with standard of identity milk by
21 consumers.

22 Consumers of these products are
23 purchasing the products for their performance
24 benefits, such as fuel for an endurance event,
25 as a recovery drink, or for muscle building or

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2 other health benefits. Therefore, it is
3 unlikely that these products are displacing
4 milk sales.

5 Manufacturers of these products
6 would have several options in response to a
7 Class I classification. Of course, one
8 alternative would be to formulate with dairy
9 proteins regardless of regulatory impact.

10 Although we believe that dairy
11 protein is superior to non-dairy protein, my
12 experience has been that product developers
13 would more likely formulate around the
14 regulation to ensure the product was not
15 classified as Class I than be subjected to the
16 regulations.

17 A second alternative under NMPF's
18 proposal would be to source all of their
19 protein as whey protein and avoid an obligation
20 to the pool. It is unclear to me, however,
21 whether the reporting requirements would still
22 apply since the product would still be a Class
23 I product.

24 Certainly, the burden of reporting
25 production or distribution of the product would

1 S. Taylor - Direct Testimony

2 likely be sufficient to discourage using whey
3 proteins as the sole protein source even if the
4 manufacturer had no pool obligation.

5 If there were no reporting
6 requirement, whey protein would be on par with
7 non-dairy proteins but would have a regulated
8 advantage over other dairy ingredients.

9 A third, and I believe most likely,
10 alternative would be use dairy-derived proteins
11 up to slightly less than 2.25 percent threshold
12 and use non-dairy protein sources for the
13 balance of the protein needs.

14 The foregone opportunity for dairy
15 protein would range from 49 percent of the
16 protein in the Odwalla Super Protein to up to
17 76 percent of the protein demand for the Met-Rx
18 RTD 40.

19 It is this third scenario that harms
20 the industry. Ultimately, no one wins in this
21 third scenario other than producers of
22 non-dairy ingredients that displace dairy's
23 market share.

24 To the extent that the demand for
25 whey proteins is constrained by new product

1 S. Taylor - Direct Testimony

2 developers limiting use in order to avoid a
3 Class I classification, the overall returns
4 from the whey and lactose complex are lower
5 than they otherwise would be.

6 These lower returns would result in
7 a shift in production from whey fractions to
8 sweet whey. The sweet whey market is a
9 delicate market and is subject to substantial
10 price swings when supply and demand is
11 imbalanced.

12 For example, the NASS whey price
13 dropped \$0.1472 (over 50% from \$0.2868 down to
14 \$0.1396) during the 18-month period from
15 January 2002 to June 2003 under pressure from
16 demand displacement from the animal feed
17 sector. As demand recovered, prices recovered
18 to just shy of \$0.30 within a year thereafter.

19 Each penny change in whey prices
20 moves the Class III price by 5.86 cents.
21 Therefore, a 15-cent price swing on sweet whey
22 moves the Class II price by 88 cents per cwt.

23 Assuming the 30.92 percent Class III
24 utilization in the Orders in 2004, a penny
25 reduction in whey price translates into a

1 S. Taylor - Direct Testimony

2 1.8-cent reduction in the uniform price.

3 However, to the extent that Class III prices
4 move Class I prices, the negative impact on
5 producer milk prices is amplified.

6 At the 43.41 percent Class I
7 utilization in 2004, the penny reduction in
8 whey prices equates to a 2.6-cent reduction in
9 the uniform price. So a penny reduction in
10 whey prices reduces uniform prices by 4.4 cents
11 per hundredweight in total.

12 My estimate of the direct impact on
13 the uniform price of narrowing the Class I
14 definition (ignoring the impact on the Class
15 prices due to changes in whey prices already
16 noted above) is that in 2004 the uniform price
17 would have decreased by 0.5 cents per
18 hundredweight.

19 This estimate was calculated by
20 multiplying the 43.61 percent 2004 Class I
21 utilization published in the Federal Order
22 Statistics by the 0.30 percent of Class I
23 utilization attributed to yogurt-based
24 beverages in the department exhibit (Exhibit
25 12). Based on this calculation, 0.13 percent

1 S. Taylor - Direct Testimony

2 of total pool milk is impacted by moving
3 yogurt-based beverages from Class I to Class
4 II.

5 The price difference between Class I
6 and II for 2004 is approximated to be \$3.70 per
7 hundredweight. Therefore, the impact of moving
8 yogurt-based beverages from Class I to Class II
9 is a reduction of 0.47 cents per hundredweight
10 on the blend price.

11 While this small number might be
12 surprising, it is not illogical. As I have
13 already noted, I believe that manufacturers of
14 non-traditional beverages have largely
15 formulated around the Class I threshold as have
16 many smoothie manufacturers.

17 I have not attempted to estimate the
18 impact of the constraints on whey protein
19 demand under the current or proposed Class I
20 definitions. Similarly, I have not estimated
21 the impact on nonfat dry milk or other dairy
22 ingredients that are also impacted by the same
23 constraints on Class IV prices (and therefore
24 on Class II prices). This is because data is
25 not available quantifying the foregone demand

1 S. Taylor - Direct Testimony

2 under the regulations.

3 However, I fully expect that the
4 increased opportunities for whey proteins and
5 other dairy ingredients that will be unleashed
6 by the removal of these nontraditional
7 beverages and smoothies from the threat of
8 Class I classification will offset the
9 reduction in Class I revenue by many fold.

10 The Class I fluid milk product
11 definition has significant impacts on dairy
12 ingredient demand. Many references have been
13 made at this hearing to the formulation of
14 products in a fashion that results in them
15 dropping into Class II.

16 This reformulation is accomplished
17 by displacing dairy ingredients with non-dairy
18 ingredients. Therefore, not only is the pool
19 missing out on Class I revenue that was
20 intended to be captured under the current
21 definition, but the diminished dairy ingredient
22 demand due to the reduction in dairy ingredient
23 use results in lower whey and dry milk prices
24 that translate into lower prices across all
25 classes.

1 S. Taylor - Direct Testimony

2 I do agree that products competing
3 directly with drinking milk need to be put on a
4 comparable regulatory footing with drinking
5 milk. Therefore, products that can be confused
6 with milk and are directly marketed against
7 milk should be classified as Class I. However,
8 I do not believe the nontraditional beverages
9 and smoothies fall into this category.

10 Therefore, Leprino believes that it
11 is time to refocus the Class I fluid milk
12 product definition on beverage milk and those
13 products that directly compete with beverage
14 milk.

15 Alternatively, if the current Class
16 I definition structure is maintained, Leprino
17 supports the exclusion for nutritional drinks
18 (Proposal 10) and supports the exclusion of
19 products containing 20 percent or more yogurt
20 (Proposal 9).

21 If the Department does not grant the
22 exclusions for nutritional drinks and beverages
23 containing 20 percent or more yogurt, Leprino
24 strongly opposes the adoption of the protein
25 standard to replace the SNF standard.

1 S. Taylor - Cross - by Mr. Yale

2 MR. ALBY: Thank you,
3 Ms. Taylor. I believe that concludes our
4 testimony.

5 JUDGE DAVENPORT: Is there
6 examination of Ms. Taylor? Mr. Yale?

7 -----

8 CROSS-EXAMINATION

9 BY MR. YALE:

10 Q. Benjamin F. Yale for Select Milk
11 Producers and Continental Dairy Products. Good
12 afternoon.

13 A. Good afternoon, Mr. Yale.

14 Q. I want to turn to your table on page
15 6 and it goes on to 7. Based upon your
16 understanding of the National Milk Producer's
17 proposal, the question I have is -- and then I
18 want to go through each of these products --
19 the Accelerade that uses whey protein isolate.

20 A. That would be Class II.

21 Q. What about Odwalla?

22 A. If it were formulated with dairy
23 proteins, it would be Class I.

24 Q. But it's formulated with not dairy
25 proteins now; right?

1 S. Taylor - Cross - by Mr. Yale

2 A. No, but as I stated in my precursor
3 to this table, we will get the entire protein
4 composition of these beverages as a potential
5 market for dairy ingredients. My point is that
6 we are constraining that marketplace by having
7 the regulations in place with a protein or an
8 SNF limitation.

9 Q. Have you had any discussions with
10 the makers of Odwalla about using milk
11 proteins?

12 A. I have not in my role. I'm not in
13 the sales side.

14 Q. Would the soy protein isolate be
15 replaced by whey protein isolate or a casein
16 protein; do you know?

17 A. I suspect it could be replaced by
18 either one.

19 Q. Do you know what the ratio would be?

20 A. No, I don't specifically.

21 Q. Is there a reason, for example, that
22 the soy protein -- You don't know what the soy
23 protein isolate is?

24 A. No.

25 Q. So you don't know whether it would

1 S. Taylor - Cross - by Mr. Yale
2 be replaced by a whey protein or a casein
3 protein?

4 A. No.

5 Q. But as it stands now formulated, it
6 is not a Class I product, is it?

7 A. As it stands formulated, none of
8 these are Class I products.

9 Q. And you don't know if they were to
10 use soy proteins whether they would use whey
11 proteins and to the extent they would use whey
12 proteins?

13 A. Can you repeat that?

14 Q. I said you don't know if they did
15 use milk proteins what amount of those would be
16 whey proteins?

17 A. No, I do not.

18 Q. With the Naked, currently as it's
19 formulated, is that Class I or Class II?

20 A. Currently as it is formulated, it
21 would be Class II.

22 Q. Again, with the soy protein isolate,
23 you don't know whether that isolate is
24 comparable to a whey protein or a casein
25 protein?

1 S. Taylor - Cross - by Mr. Yale

2 A. No, I do not.

3 Q. If it were a whey protein that it
4 was replacing, then it would still remain Class
5 II, right, under the proposal?

6 A. If the product only used whey
7 protein, it would still be pushed into Class I
8 because any product that has greater than 2-1/4
9 percent protein under the national milk
10 proposal would be a Class I product.

11 Q. But it would have no pricing -- As
12 you said, it might have some reporting, but it
13 has no pricing obligation?

14 A. Correct, if the National Milk
15 proposal were adopted as they have proposed.

16 Q. The next one with the calcium
17 caseinate and the whey protein concentrate, do
18 you know what the mix is between the calcium
19 caseinate and the whey?

20 A. No. On all of these products, I was
21 working off the product labels that wouldn't
22 give specific formulations.

23 Q. Depending upon how much is calcium
24 caseinate, this may be I or II, right, but we
25 don't know?

1 S. Taylor - Cross - by Mr. Yale

2 A. Correct.

3 Q. Then the Isopure, that's the
4 situation where that is using whey protein
5 entirely; right?

6 A. Right. I suspect if you ignore the
7 fact that probably you could argue this is a
8 nutritional product in a hermetically-sealed
9 container that it would just based on
10 composition be a Class I.

11 Q. Why would that be?

12 A. Because it would have greater than
13 6.5 percent SNF from dairy sources at the
14 moment.

15 Q. But, again, not having any pricing
16 obligation?

17 A. I'm rather unclear under the current
18 implementation of regulations by USDA. As I
19 mentioned in my testimony, my understanding is
20 that they have been inconsistent in their
21 implementation, but I believe in a close
22 reading -- Again, I think they are exempt from
23 Class I because of the container if it's a
24 nutritional product, but otherwise it would fit
25 under the current regs that would be a Class I

1 S. Taylor - Cross - by Mr. Yale

2 product.

3 Q. One way to correct that would be
4 just simply to say that there would have to be
5 some non-whey protein among the protein, some
6 casein proteins in that plus, at least some
7 before the Class I were triggered; right? If
8 the requirement was that there at least be some
9 non-whey dairy proteins rather than to trigger
10 it, that would take care of that, would it not?

11 A. Yes, it would, but the challenge
12 with that situation is, for example, we had a
13 product that the formulator wanted to use some
14 caseins because of the functional attributes
15 and there was a need for additional protein and
16 that additional protein if they used whey
17 protein would trigger it above 2-1/4 percent,
18 that casein portion would have implications and
19 would still push that formulator to move over
20 to a non-dairy protein to supplement the base
21 level.

22 Q. The theory is there. I agree with
23 your theory, but for Isopure they have
24 indicated they don't want any casein proteins?

25 A. In this case, yes.

1 S. Taylor - Cross - by Mr. Yale

2 Q. Over to the GNC, again it's a soy
3 protein isolate. You don't know whether that's
4 a whey protein isolate comparable or not?

5 A. Right. I do not know the specific
6 compilation.

7 Q. What is your understanding of the
8 vegetable and wheat isolates? Do they tend to
9 be replaceable by whey protein isolates or
10 other protein isolates?

11 A. In my conversations with product
12 developers, they generally have said that they
13 would replace whey protein with soy protein so
14 with the whey protein concentrate at presumably
15 similar levels, but I don't have the expertise
16 to really comment on that beyond the comments
17 that have been given to me by those R&D folks.

18 Q. You're not a dairy chemist or have
19 an education in dairy chemistry?

20 A. No, I do not.

21 Q. Not to say you might not be smarter
22 than them, but you just don't have that
23 ability. I don't want you to think my
24 assumption is that you don't know what you're
25 talking about, but just that you're not an

1 S. Taylor - Cross - by Mr. Yale

2 expert.

3 In fact, what is the potential of
4 casein protein isolates? How often do you even
5 see that or hear about that?

6 A. Casein itself can be concentrated.
7 Just normal casein can be concentrated at
8 levels that are comparable to whey protein
9 isolate so I have never heard of the term
10 "casein isolate," but I think in terms of the
11 density, it's comparable.

12 Q. But it's not commonly done at this
13 point?

14 A. I believe that some of the
15 caseinates are close to the 90 percent purity
16 level.

17 Q. Of a particular protein?

18 A. Yes. 90 percent casein is my
19 understanding. There are variations in the
20 composition of caseins.

21 Q. Casein, it depends on how you count,
22 it can have a number of proteins, four or more
23 proteins; is that right?

24 A. Yes. There are several different
25 subparticles within casein or subproteins

1 S. Taylor - Cross - by Mr. Yale

2 within case in.

3 Q. I won't ask the names.

4 A. Thank you.

5 Q. Again, this EAS, the milk protein
6 concentrate, that one potentially would be a
7 Class I product if depending again on the
8 percent that is the whey protein as opposed to
9 the milk protein concentrate; right?

10 A. That's correct.

11 Q. And the same for the Met-Rx?

12 A. That's correct.

13 Q. Do you know what the market for whey
14 proteins used in beverages such as this is as a
15 percentage of the total whey market?

16 A. I do not and other observation is
17 that currently that market may be somewhat
18 constrained by formulation and response to the
19 current regs.

20 Q. Are you aware of any studies or done
21 any market research or aware of anybody that
22 has done any that indicate that -- I have a
23 couple of questions regarding market research
24 in which the classification for the use of whey
25 protein to be classified, they are used to

1 S. Taylor - Cross - by Mr. Yale
2 classify products as Class I would, in fact,
3 impact the whey price as reported by NASS.

4 A. The overall whey demand which is
5 impacted by its potential abuse in beverages or
6 any other use does get reflected in the overall
7 price level of whey as collected by NASS.

8 Q. But you don't know what that level
9 of impact is?

10 A. No, I do not.

11 Q. When you mention here on page 8 that
12 it's a 15-cent movement in whey, do you have
13 any evidence that would prove that this
14 proposal of National Milk will create a 15-cent
15 movement in the whey price?

16 A. No, I don't, and I did not intend to
17 relay that in my testimony. In the 15-cent
18 swing comment, I was illustrating that whey is
19 a relatively delicate market with demand that
20 if it falls off much at all can result in some
21 very significant swings. I do not know what
22 the price impact would be on changing the
23 regulations that would allow more whey products
24 into beverages or restrict them more so.

25 MR. YALE: I have no further

1 S. Taylor - Cross - by Mr. Yale
2 questions.

3 JUDGE DAVENPORT: Other
4 examination? Mr. Vetne?

5 -----

6 CROSS-EXAMINATION

7 BY MR. VETNE:

8 Q. John Vetne for H.P. Hood. Page 5
9 hydrocolloids, my first introduction to that
10 word. Is that a protein ingredient, first of
11 all?

12 A. I have a definition that I have
13 written down if you would like me to read that.
14 It can be a protein. Generally it can be any
15 range of other ingredients as well. It can
16 tend to give form and structure to the food.
17 It could be starches, gelling agents.

18 Q. Do any of the ingredients that may
19 be part of that family when tested produce
20 nonprotein nitrogen?

21 A. I do not know.

22 Q. When Leprino manufactures and
23 markets whey ingredients to consumers, say whey
24 protein concentrate, do you make standard
25 formulations, company standard formulations of

1 S. Taylor - Cross - by Mr. Yale

2 whey protein concentrate?

3 A. Yes. We have several different
4 products we offer.

5 Q. 40 percent, 50 percent protein, that
6 kind of thing?

7 A. Yes. The most common would be WPC
8 35, WPC 48 and variations off of that.

9 Q. In those common formulations, do you
10 have a tolerance for allowance of protein in
11 the product plus or minus something?

12 A. There would be standard deviation
13 variances, yes.

14 Q. What would that commonly be?

15 A. I don't know.

16 Q. Is the 35, 48 whatever the
17 percentage on the package, is that a measure of
18 true protein or what we call total protein that
19 includes nonprotein nitrogen?

20 A. I do not know.

21 Q. You're aware, are you not, that the
22 protein in the producer of milk when measured
23 as total protein includes a nonprotein
24 nitrogen?

25 A. That's true.

1 S. Taylor - Cross - by Mr. Yale

2 Q. And the true protein is ordinarily
3 derived not by testing measures but by
4 arithmetic measure with a common relationship
5 between total protein and true protein?

6 A. My understanding is that
7 historically that's true. I have also been
8 told, and I'm not an expert in this area, that
9 some of the newer machines are actually seeing
10 true protein rather than total protein.

11 Q. Do you know if those newer machines
12 can distinguish between whey protein and casein
13 protein?

14 A. I do not.

15 Q. Do you know if they can distinguish
16 between dairy protein and non-dairy protein?

17 A. I have been told that some can.
18 There is also more sophisticated lab techniques
19 that they can distinguish.

20 Q. The more sophisticated lab
21 techniques that you're referring to, they are
22 not ones that can be done for a few pennies a
23 sample, are they?

24 A. No. They would typically be
25 electrophoresis.

1 S. Taylor - Cross - by Mr. Beshore

2 Q. If a tester is using the nitrogen
3 method for protein, are there food ingredients
4 that you're aware of that produce nitrogen that
5 might be mistaken for protein when it doesn't
6 come from protein at all?

7 A. That's outside my expertise.

8 MR. VETNE: Thank you.

9 JUDGE DAVENPORT: Mr. Beshore?

10 -----

11 CROSS-EXAMINATION

12 BY MR. BESHORE:

13 Q. Marvin Beshore for Dairy Farmers of
14 America. Good afternoon, Ms. Taylor. On page
15 8, your net producer impacts calculation, I
16 wanted to make sure that I understand this.
17 Your first sentence you say "My estimate of the
18 direct impact on the uniform price of narrowing
19 the Class I definition" -- skipping the
20 parenthetical -- "the uniform price would be
21 decreased by 0.5 cents per hundredweight" and
22 you go on to elaborate on that.

23 That's based, as I understand it,
24 upon the assumption that all current Class I
25 yogurt products would be reformulated to avoid

1 S. Taylor - Cross - by Mr. Beshore
2 continuing Class I classification and would be
3 dropped into Class II?

4 A. No. Actually, this is an
5 explanation of if the department were to adopt
6 my suggestion that they narrow the Class I
7 definition to be only essentially milk and
8 products that compete with milk and they remove
9 the liquid yogurts from Class I, this would be
10 the impact. It would be a reduction in the
11 uniform price of a half cent.

12 Q. What all was assumed in your
13 narrowing then? Is that assuming like going to
14 the end of your testimony that the yogurt
15 exclusion, products containing 20 percent or
16 more yogurt would be adopted, Proposal 9 and
17 also Proposal 10? Is that part of your
18 assumption?

19 A. My assumption is that they would
20 take my preferred option which is it would
21 exclude all yogurt products that are currently
22 in Class I that John Rourke in his exhibit
23 listed as yogurt-based beverages.

24 Q. Basically your calculation is just
25 to take the yogurt-based beverage volumes of

1 S. Taylor - Cross - by Mr. Beshore
2 Exhibit No. 12 that John Rourke put in, take
3 them out of Class I and put them into Class II?

4 A. Yes. The balance of my proposal
5 that we also narrow it so these other drinks
6 will also fall out of Class I. My
7 understanding is right now generally they are
8 not in Class I, so it would have no impact on
9 the current pool so that analysis was not a
10 separate analysis.

11 Q. If we turn back to page 7 of Exhibit
12 No. 31 in your text after the chart relating to
13 the products, you say based upon the protein
14 compositional criteria alone, all products on
15 the above list other than Accelerade could be
16 classified as Class I or would be only if they
17 used dairy-derived proteins under the National
18 Milk proposal. If they used dairy-derived
19 proteins only and the National Milk proposal is
20 adopted, but there is a parenthetical there
21 "putting aside for the moment the Class I
22 exception for products in meal replacements in
23 hermetically-sealed containers." You put that
24 aside, but you never put it back in, did you?

25 A. The reason why I felt that it was so

1 S. Taylor - Cross - by Mr. Beshore
2 important to look at the impact of your
3 proposal absent the meal replacement in
4 hermetically-sealed container exception is
5 because there is such confusion around those
6 issues and as in any hearing, the department
7 may adopt part of your proposal but not all of
8 your proposal .

9 For example, if they did do
10 something to the language that would eliminate
11 that protection effectively, I wanted them to
12 understand what the impact would be if they
13 were going just looking at composition alone.

14 Q. But it's your testimony, and I think
15 if I understood, you maybe your responses to
16 Mr. Vetne earlier on the first question, that
17 presently the majority of the products that you
18 bought in the health food stores and have
19 discussed here, they are considered Class II
20 because they are meal replacements or meal
21 supplements as Mr. Alexander testified and in
22 hermetically-sealed containers?

23 A. That is my belief. I have not
24 consulted with USDA on that.

25 Q. With respect to Proposal 7, why

1 S. Taylor - Cross - by Mr. Beshore
2 wouldn't the nonpricing of sweet whey or a
3 sweet whey proxy for that product -- In terms,
4 that means the same thing as whey for cheese
5 making?

6 A. Sweet whey I typically think of as
7 referring to the finished product where the
8 lactose portion, sugar portion has not been
9 separated from the protein portion. Whey I
10 think of generically as the fluid coming off of
11 that.

12 Q. Where you have a proposal, Proposal
13 7, that would not price whey that comes from
14 the cheese-making process and would price all
15 other dairy protein sources, why is it that a
16 great advantage to those of you such as your
17 company who are marketing whey from the cheese
18 making process?

19 A. To the extent that the formulator is
20 comfortable only including whey protein and no
21 other dairy sources, then it would be a great
22 benefit. It would give whey protein an edge or
23 whey products an edge over other dairy
24 ingredients.

25 However, if there was a reason for

1 S. Taylor - Cross - by Mr. Beshore

2 them to need the casein portion of the protein
3 in that formulation, then they would still be
4 sensitive to other dairy sources that might
5 trigger them above the threshold. I think that
6 there is enough likelihood that many products
7 will want a combination of proteins, casein and
8 whey protein, and I'm not comfortable just
9 taking advantage of your gift.

10 Q. But the products would have to be
11 those that avoid the exclusion of meal
12 replacements. For instance, as long as the
13 exclusion for meal replacements in
14 hermetically-sealed containers is continued,
15 let's assume the present administration of
16 those products that you have in front of you
17 continue. There is absolutely no pricing risk
18 whatsoever in using whey in its products;
19 correct?

20 A. In these specific products, but
21 there is a range of other functional foods that
22 are being developed that may fall beyond this
23 over time that may not fit that exclusion of
24 meal replacement.

25 Q. Other than yogurt beverages which

1 S. Taylor - Cross - by Mr. Beshore
2 there has been a lot of testimony and data with
3 respect to those volumes whether some of them
4 are presently Class I and some of them are
5 presently Class II, other than those
6 beverages -- By the way, in those beverages the
7 they exemption for pricing would be a big plus,
8 would it not, in that market?

9 A. I would expect so.

10 Q. Other than those beverages and other
11 than the ones you have in front of you here,
12 what is the other market we are talking about?
13 What other products?

14 A. I can't tell you off the top of my
15 head.

16 Q. Do you have an idea?

17 A. More and more food developers are
18 going toward functional food products whether
19 they are something that's --

20 Q. Beverages. What other categories or
21 classes of beverages are we talking about where
22 there might be regulatory problems?

23 A. There could be, for example, soda
24 drinks that have protein added. Whether the
25 department would determine those to be

1 S. Taylor - Cross - by Mr. Beshore
2 nutrition drinks, I think, is a very cloudy
3 area.

4 Q. Are you aware of any presently -- By
5 the way, was whey an ingredient in the now no
6 longer marketed Swerve product; do you know?

7 A. I don't know.

8 Q. Are you aware of any of that soda
9 drink category with protein, dairy protein
10 additives that is presently being marketed in
11 substantial volumes?

12 A. I'm not aware of anything that is
13 specifically on the market. I am aware of some
14 products that, for example, Cornell in their
15 refinery process has shown to various companies
16 that they are using milk serum proteins, so
17 they have been separated prior to cheese
18 making. They don't have some of the asthmatic
19 activity that you normally get in whey
20 proteins. I also tasted a cola that was
21 indistinguishable to my palate from Coke, but
22 it was equivalent protein to milk.

23 Q. Is it being marketed today?

24 A. Not that I'm aware of.

25 MR. BESHORE: Thank you.

1 S. Taylor - Cross - by Mr. Tosi

2 JUDGE DAVENPORT: Other
3 examination? Mr. Tosi?

4 -----

5 CROSS-EXAMINATION

6 BY MR. TOSI:

7 Q. Thank you for appearing at the
8 hearing. I just have a couple of questions.
9 What is a functional food? You use that term a
10 couple of times, and I'm not sure exactly what
11 context to put that in.

12 A. There is probably a more precise
13 definition that I'll give you. My
14 understanding though is that they are foods
15 that are designed for a very specific benefit,
16 generally a health benefit and some of them may
17 be addressing particular health issues, but
18 they are still mainstream foods.

19 Q. Could you give like an example of
20 something that might currently be out there?

21 A. Off the top of my head, I can't
22 think of the specifics. I hear the term quite
23 a bit as you're out and about at industry
24 meetings. I know that on the product
25 development side, it's something that not only

1 S. Taylor - Cross - by Mr. Tosi
2 has been a focal point, but my understanding is
3 there are a number of products out there, but
4 quite honestly I have not paid enough attention
5 to the specific foods they are talking about to
6 give you an answer. I could if you would like
7 elaborate on that in the post-hearing brief.

8 Q. It's up to you. I just wasn't sure
9 of the context in which to interpret that term.
10 In light of your concerns about why that may
11 cause certain products that are currently II to
12 move up to Class I, would you be in support to
13 the extent that we are touching on the gray
14 areas here between Class I and Class II to give
15 the department a little discretion in making a
16 determination of whether or not something
17 should be in Class I or II?

18 A. Yes. In fact, under my suggestion
19 that we narrow things down in identifying Class
20 I as strictly essentially standard of identity
21 milk and those things that are significantly
22 competing against it, that would require
23 department discretion.

24 Q. In that regard then, are you
25 suggesting that our 6-1/2 percent nonfat solid

1 S. Taylor - Cross - by Mr. Tosi
2 standard as a fluid milk product that's
3 currently included in the fluid milk product
4 definition and that currently differs from what
5 FDA says the standard of identity for milk is,
6 are you saying that we should, that our
7 standard for a fluid milk product definition
8 should be the FDA 8-1/4 percent solids not fat?

9 A. I have not done all of the studies
10 to identify what parameters. You have some
11 variation around that 8-1/4 percent, but I
12 suspect that the lower threshold would be
13 something greater than 6-1/2 percent, yes.

14 Q. Then I'm not sure. How does that
15 narrow or give the department discretion? It
16 seems like you're giving it less discretion to
17 handle new products that come out of making
18 this determination. I'm at a loss here.

19 A. What you would do is, first of all,
20 you wouldn't be focused as much on the
21 compositional threshold. If you looked at the
22 range of these products, in my mind there is no
23 reason to give somebody incentive to buy this
24 (indicating) over this (indicating), but your
25 6-1/2 percent would say this (indicating) is

1 S. Taylor - Cross - by Mr. Tosi

2 Class I. This (indicating) is Class II.

3 I think we need to be very narrowly
4 focused in what we call Class I and restrict it
5 to drinking milk and some of the other things
6 that you specifically have identified the
7 cultured products. Flavored milk I would
8 consider part of that.

9 Various variations on the fat levels
10 of drinking milk as well would be Class I and
11 those products that directly compete against
12 that. So if somebody would go back to a filled
13 milk kind of product where it's a vegetable oil
14 substitution, obviously that should also be
15 included.

16 However, in terms of other new
17 products that are somewhere between a classical
18 milk drink and some other innovation, I would
19 put those into Class II.

20 Q. Getting back to allowing the
21 department some discretion of making fine
22 distinctions here, you held up the product
23 that's red in color versus the one that's
24 bluish in color. If one by compositional
25 standards would meet the fluid milk product

1 S. Taylor - Cross - by Mr. Tosi
2 definition and the other one that's II, do you
3 think it would be appropriate to give the
4 department some discretion to, for example, say
5 the blue one which meets the fluid milk
6 definition literally would not be classified as
7 a fluid milk product?

8 A. My proposal is that we don't have
9 the regulations written in Class I definition
10 that then would essentially put the overhang on
11 the formulators' mind as to which direction the
12 department would classify a product that would
13 be like in the case of these kind of products,
14 that would be very clear that we are only
15 talking about milk products so that then the
16 formulators don't from the start make sure that
17 they reduce the dairy ingredients.

18 Q. If there should be a question that
19 the department ends up with -- excuse me -- if
20 it turns out that there is a new product that
21 comes out and we are in this gray area about
22 how to classify, would you be of the opinion
23 that the overriding factor should be form and
24 use in determining classification?

25 A. Yes, but I believe I would define

1 S. Taylor - Cross - by Mr. Tosi
2 use more narrowly than what has been defined
3 recently by the Department. Use would be those
4 things that are used in direct competition to
5 drinking milk.

6 Q. A hypothetical will be my last
7 question to you. If there are people that buy
8 regular milk and use it only on cereal and
9 consume it as a food as they would cereal and
10 there are other people who buy fluid milk only
11 to drink as a beverage, how is the Department
12 supposed to differentiate use in something
13 like that?

14 A. It's a practical application. I
15 don't think the department needs to
16 differentiate every sub use of a particular
17 person, but the predominant use of the
18 population, I think, is sufficient.

19 MR. TOSI: Thank you, Sue.
20 Thank you for your patience.

21 JUDGE DAVENPORT: Mr. Wilson?

22 -----

23 CROSS-EXAMINATION

24 BY MR. WILSON:

25 Q. Todd Wilson, USDA. Good afternoon,

1 S. Taylor - Cross - by Mr. Wilson

2 Sue. I appreciate you being here and maybe
3 answer some of these questions. I think you
4 had mentioned that maybe at least one of those
5 products might meet the current 6.5 percent
6 standard. Would you consider that product as
7 that 6.5 standard has been written about in
8 prior decisions was intended to exclude
9 competitive sphere type products that did not
10 compete?

11 A. I'm sorry. The competitive what?

12 Q. Sphere, the competitive nature of
13 the products. We are talking about that blue
14 product?

15 A. Right.

16 Q. Would you consider that to be in
17 direct competition with what you call
18 traditional milk?

19 A. I would not.

20 Q. One other question, and I had asked
21 this earlier, and I hope you can answer it with
22 your knowledge. When you talk about in your
23 written statement on page 3 the ability of
24 possibly in the future and maybe even currently
25 of being able to fractionate the serum proteins

1 S. Taylor - Cross - by Mr. Wilson
2 from the whey proteins prior to the
3 cheese-making process, do you know that the
4 ability to be able to distinguish if that serum
5 protein or that whey protein, if the whey
6 protein is then dried into a powder, can that
7 be marketed as whey powder or maybe it's not
8 even happening?

9 A. I'll try to clarify a little bit on
10 the question and let me know whether I'm going
11 in the wrong direction, but the process that
12 Cornell has been working on with their refinery
13 model would separate the casein from the milk
14 serum proteins.

15 The milk serum proteins are the same
16 proteins that end up as whey proteins after
17 they have gone through cheese making and if I
18 understand the direction you're going, I
19 believe your question is whether if you were to
20 dry the milk serum protein and dry the whey
21 protein whether you would be able to
22 distinguish between the two; is that correct.

23 Q. You're saying the milk serum protein
24 and whey proteins are really the same?

25 A. Yes. The milk serum protein after

1 S. Taylor - Cross - by Mr. Wilson
2 it has gone through cheese making, and my
3 understanding is that, yes, you could
4 differentiate the two, but I'm not sure of the
5 sophistication of the test that's required
6 because my understanding is that there is a
7 slight chemical difference between the two,
8 whereas, the activity on the whey protein has
9 been picked up through the cheese-making
10 process.

11 I know that in terms of applications
12 on serum protein is perceived to have a broader
13 application than the whey protein, so I would
14 presume based on that that, yes, you could
15 analytically determine whether that protein is
16 milk serum protein or whey protein.

17 Q. Do you foresee industry growing in
18 that possible new product?

19 A. I think it's an exciting area. My
20 opportunity to view this process was a workshop
21 where in combination some of the folks from the
22 food science department and some of the folks
23 from the dairy markets and policy group at
24 Cornell invited some folks from the industry
25 and just tried to brainstorm what the potential

1 S. Taylor - Cross - by Mr. Wilson
2 was, what the potential applications were.

3 Cornell had been going through this
4 process just in a very small pilot plant
5 situation at the time. This was probably about
6 two years ago, so some folks might have
7 advanced since then.

8 There were certainly a number of
9 companies there that had a fair amount of
10 advanced fractionation technology. My
11 understanding at the time was in Europe it is
12 being used.

13 One of the questions I think in its
14 application here in the United States is
15 whether the standard of identity would allow
16 you to still call the cheese that is made from
17 milk that has had the milk serum proteins
18 separated first, still call it by the standard
19 of identity name. So that's long term one of
20 the things that will impact on how quickly that
21 market grows.

22 Q. Do you know if there is currently a
23 market -- On page 6, the middle paragraph if I
24 read this correctly, this is saying whey
25 protein could be formulated into all of these

1 S. Taylor - Cross - by Mr. Wilson
2 products. Are you saying that whey protein
3 concentrate 80 could be formulated to be
4 combined with nonfat dry milk into a blended
5 specialty product that would be marketed in the
6 marketplace?

7 A. There are any range of products that
8 could be developed and even within the whey
9 protein group there are many variations, many
10 fine refractions that companies have advanced
11 into that are customized for particular
12 applications; but whether you market these as
13 self standing whey protein components or
14 whether you combine them with another
15 ingredient, for example, nonfat dry milk, they
16 could be marketed either way.

17 Q. Do you know if on product labeling,
18 for instance, the products you have, and I
19 don't know which one this is up there, but the
20 Atkins Advantage Shake, in your table beginning
21 on page 6, it lists calcium caseinate and whey
22 protein concentrate. I'm assuming that's on
23 the label?

24 A. Yes.

25 Q. Could that be a blended powder? Can

1 S. Taylor - Cross - by Mr. Wilson
2 the identification on the label, will it
3 include the components of a blended portion of
4 an ingredient?

5 A. That is out of my expertise, but I
6 will observe that as I read through each of
7 these labels, there were several that had a
8 name for a protein blend and then in
9 parentheses listed the individual protein
10 sources. So my suspicion is that they still
11 need to list the individual sources even if
12 they have created a blend.

13 Q. On the same table, whenever there is
14 more than one protein source, are they listed
15 by majority percentage?

16 A. That's my understanding as far as
17 the rank order, but the percentage is not
18 listed on the label and I did include them on
19 this table in the same order that they were
20 included in the label.

21 MR. WILSON: Thank you very
22 much, Sue.

23 JUDGE DAVENPORT: Other
24 examination? Dr. Cryan?

25 -----

1 S. Taylor - Cross - by Mr. Cryan

2 CROSS-EXAMINATION

3 BY MR. CRYAN:

4 Q. Good afternoon, Sue.

5 A. Good afternoon.

6 Q. Ms. Taylor, according to your
7 proposal, if a product had less than 6-1/2
8 percent nonfat solids that was competing
9 effectively in terms of form and use with fluid
10 milk, would it be reasonable for the department
11 to classify it as a Class I product?

12 A. Yes. Under my preferred proposal,
13 the primary criteria would be whether it
14 competes directly with fluid milk and whether
15 it could be confused by consumers as fluid
16 milk, yes.

17 Q. In another topic, if Proposal 7 was
18 adopted and whey wasn't priced, would you
19 expect that a processor that used whey, a whey
20 protein to produce something like this would be
21 able to document to the satisfaction of the
22 market administrator that they have used whey
23 by use of things like past records and invoices
24 and what not?

25 A. I suspect they would, but as I

1 S. Taylor - Cross - by Mr. Cryan
2 mentioned in my testimony there is almost a
3 visceral reaction to the level of regulation
4 and reporting that's required under the Federal
5 Order System so even that requirement could
6 keep people from using the whey products.

7 Q. You were concerned also if they are
8 using milk protein concentrates, if the product
9 became Class I and they file a handling report
10 and deal with pool obligations that that would
11 be a strong disincentive as well; is that
12 right?

13 A. Yes. It would be a disincentive for
14 any dairy ingredient.

15 Q. How would that change if, for
16 example, the Department developed something
17 like a Class I ingredient classification or dry
18 ingredients that could be priced at Class I at
19 the manufacturing plant and then incurred no
20 future obligation from the handlers that use
21 it?

22 A. The trade in these dry products is
23 so complex while the product goes through
24 distributors, brokers. I think it's next to
25 impossible to be able to classify it by end use

1 S. Taylor - Cross - by Mr. Cryan
2 of the dry product.

3 Q. That could be at the option of the
4 manufacturer?

5 A. Could you further elaborate?

6 Q. The idea would be that a
7 manufacturer of milk protein concentrates or
8 even nonfat dry milk or some subcategory of dry
9 ingredients could identify a volume of milk
10 used to produce a milk equivalent or some form
11 of a Class I dry ingredient that would then
12 lead to plant without any future obligation, if
13 a processor could demonstrate that they were
14 using those products, but there would be no
15 future obligation, no additional obligation
16 with respect to the pooling?

17 A. I would still go back to the
18 complexity of the marketing distribution chain.
19 If I understand, you're laying out if something
20 that occurs but not to get into essentially
21 prepaying the obligation and some who did not
22 and how you trace back through that product.

23 I think it still would force some
24 oversight on the ultimate end user, and it's
25 that oversight that I think positions dairy at

1 E. Tipton - Direct Testimony

2 a disadvantage to other ingredients where they
3 don't have to be encumbered by reporting the
4 regulation.

5 MR. CRYAN: Thank you.

6 JUDGE DAVENPORT: Other
7 examination? Thank you, Ms. Taylor. You may
8 step down.

9 (Short recess taken.)

10 JUDGE DAVENPORT: Mr. Tipton,
11 why don't you come forward at this time.

12 (At this juncture, the witness
13 was sworn in.)

14 JUDGE DAVENPORT: You are E.
15 Linwood Tipton?

16 MR. TIPTON: Yes, sir.

17 JUDGE DAVENPORT: Very well.
18 Mr. Tipton, you have a statement which I have
19 marked as Exhibit No. 32. I understand that
20 you have a request that it be entered into the
21 record as if fully read; is that correct?

22 MR. TIPTON: Yes, sir. I have
23 two statements.

24 JUDGE DAVENPORT: So there is
25 actually two statements. I would still mark

1 E. Tipton - Direct Testimony

2 them all collectively as Exhibit No. 32. Do I
3 have any objection to Mr. Tipton's request that
4 his statement be entered into the record as if
5 read?

6 MR. BESHORE: I don't have any
7 objection.

8 JUDGE DAVENPORT: Very well.
9 Mr. Beshore has no objection. Mr. Yale?

10 MR. YALE: No objection, Your
11 Honor.

12 JUDGE DAVENPORT: Mr. Vetne?

13 MR. VETNE: None.

14 JUDGE DAVENPORT: Mr. Harner?

15 MR. HARNER: No objection.

16 JUDGE DAVENPORT: Mr. Yonkers?

17 MR. YONKERS: No objection.

18 JUDGE DAVENPORT: Dr. Cryan?

19 DR. CRYAN: No objection.

20 JUDGE DAVENPORT: Very well.

21 Madam Reporter, we will transcribe this, both
22 statements, 32 and 32A as if fully read into
23 the record.

24 (Exhibit Nos. 32-32A were
25 marked for identification.)

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E. Tipton - Direct Testimony
STATEMENT OF E. LINWOOD TIPTON
CHAIRMAN AND CEO
THE TIPTON GROUP, INC.

The companies on whose behalf I am appearing take the following positions relative to the issues raised in this hearing:

1. They support continuation of the requirement that a product must contain by weight at least 6.5 percent nonfat milk solids to be included in Class I.
2. They support the classification of yogurt and kefir in Class I, whether in liquid drinkable form or a more viscous spoonable form and whether combined with juices or other foods or not.
3. They support continuing to exclude from the Class I definition "formulas prepared for infant feeding or dietary use (meal replacement) that are packaged in hermetically-sealed containers."
4. They support adding the following types of products to be excluded from the Class I definition when packaged in hermetically-sealed

1 E. Tipton - Direct Testimony

2 containers: Formulas for snack replacement;
3 high protein drinks; beverages that contain
4 alcohol and are licensed by the Treasury
5 Department; and packaged milk products
6 formulated and labeled for animal use.

7 5. They oppose all proposals not consistent
8 with the above positions including: (a) The
9 reduction or elimination of the 6.5 percent
10 minimum nonfat solids standard; (b) The
11 addition of a protein standard along with the
12 6.5 percent nonfat milk solids standard, or the
13 replacement of the 6.5 percent standard with a
14 protein standard; (c) The inclusion of whey in
15 applying the 6.5 percent nonfat solids minimum.

16 6. They oppose using as a basis for
17 classifying products in Class I "any products
18 containing milk or milk products that are
19 intended to be used as a stand-alone beverage."

20 Before proceeding to testify on the
21 issues involved in specific proposals, I want
22 to provide the context in which any decisions
23 coming from these proceedings should be made.

24 The Federal Milk Order's classified
25 pricing system is confronted with unstoppable

1 E. Tipton - Direct Testimony

2 driving forces of change that must be
3 recognized and addressed in any decisions
4 coming from this proceeding. We believe the
5 facts will support and justify a continuation
6 of the current classification criteria with
7 some added clarity and the specific exclusions
8 from Class I of a few specific formulas and
9 products that do not compete with beverage
10 milk, but do nevertheless, utilize significant
11 quantities of dairy farmers milk and
12 dairy-derived ingredients.

13 Among the driving forces of change
14 are: A continuous decline in fluid milk
15 consumption in the face of strong competition
16 from a broad range of other alternative
17 beverages such as water, juice, soft drinks,
18 teas, sports drinks and many new beverage
19 market entrants.

20 The exponential growth of
21 competitive alternative beverages, the
22 substantial advertising and promotion budgets
23 of highly branded beverages and changing
24 concepts of "healthy drinks" are forces to be
25 recognized and addressed. The availability of

1 E. Tipton - Direct Testimony

2 substitute and alternative beverages has
3 resulted in milk sales being much more
4 responsive to price changes than in earlier
5 years.

6 Quantum advances in ingredient
7 technology often make fractionations and
8 derivatives of milk's components more
9 functionally desirable than the base component
10 from which it was developed. Whey protein
11 technology has spawned a growing global market
12 for various whey protein products, many of
13 which are now used in sports drinks and other
14 high energy drinks and products.

15 The forces of ingredient technology
16 make it increasingly difficult to draw a
17 distinction about when a beverage might be
18 considered a dairy product by consumers and
19 when it would not. The competitive set for
20 milk is not dependent on whether the competing
21 product contains a modicum of some
22 dairy-derived ingredient.

23 Soft drinks with no added
24 dairy-derived ingredients are the most potent
25 competitive alternatives and water and juices

1 E. Tipton - Direct Testimony

2 are taking market share away from milk as well.

3 However, USDA has no authority to
4 regulate these highly competitive alternative
5 products. USDA needs to be very careful and
6 avoid creating situations that will make the
7 use of non-dairy ingredients more attractive
8 than dairy-derived ingredients.

9 USDA should apply an "acid test" to
10 all proposals and suggestions offered during
11 this proceeding. This test is whether the
12 proposal or suggestion increases the demand for
13 the product in question and will it increase or
14 decrease the demand for milk-derived
15 ingredients. Proposals or suggestions that
16 fail this test should be rejected.

17 USDA should include among its
18 objectives and goals: Permitting and
19 encouraging development of drinkable products
20 that contain dairy ingredients and provide
21 specific benefits to consumers for specific
22 purposes and uses; are available to consumers
23 in outlets and distribution channels where
24 currently milk is often not available; and are
25 positioned and formulated to provide specific

1 E. Tipton - Direct Testimony

2 nutrients or nutritional profiles to meet
3 specific groups of consumers' needs.

4 The dairy and food industries and
5 USDA should be pursuing courses of action that
6 will expand the consumption of milk and
7 drinkable products that contain dairy-derived
8 ingredients. This is the course for expanding
9 and growing the market for dairy farmers' milk
10 and its components.

11 However, we fear that some are
12 approaching this proceeding with a desire and
13 intent to erect barriers, create difficulty and
14 generally make it more difficult for
15 non-traditional drinkable products containing
16 dairy-derived ingredients to be marketed.

17 Although a number of potential
18 reasons have been offered over the years in
19 support of classified pricing, only one really
20 captures the truth. Price classification under
21 Federal Milk Orders was designed to obtain
22 higher revenue to producers than they would
23 have received without classified prices.

24 However, there now exists
25 substantial doubt that classified pricing is or

1 E. Tipton - Direct Testimony

2 can, in fact, enhance producer revenues.
3 Increasingly, the loss of revenue from lost
4 sales resulting from the higher Class I price
5 is offsetting the additional revenue generated
6 from the higher price.

7 In fact, new price responsiveness
8 measures (elasticities) show that the sales of
9 many products included in the Class I category
10 actually produce less revenue for dairy farmers
11 than they would if included in a lower price
12 class.

13 Among the Class I products to which
14 this statement applies are: Flavored milk in
15 gallon containers; both white and flavored
16 milks in half gallon containers; fat-free milk
17 in gallons and all fat levels of milk in half
18 gallons, including whole milk.

19 Federal milk classification pricing
20 is a government regulatory form of a general
21 economic pricing theory known as price
22 discrimination. This economic business
23 caption--price discrimination--applies to the
24 process of charging different prices in
25 separate markets, i.e., one higher and one

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2 lower, for identical products, which is what
3 Federal Milk Orders do.

4 Milk used for drinking (beverage
5 milk/Class I) is priced higher than milk used
6 to produce other products such as butter,
7 cheese, and other so-called manufactured dairy
8 products, although the milk used in all the
9 products is the same and is used in each of the
10 classes interchangeably.

11 As already stated, the purpose of
12 classified pricing is to generate more total
13 revenue for dairy farmers than would be
14 possible if all the product (milk) was sold at
15 one price. However, in order to generate more
16 total revenue, two conditions must be present.
17 There must be a difference in how customers in
18 the different markets respond to the prices,
19 and the lower-priced product cannot be
20 substituted for the higher priced product.

21 First, foremost and basic to the
22 whole concept, there must be a difference in
23 how customers respond to the differing prices
24 in the separate markets.

25 If customers in one market accept

1 E. Tipton - Direct Testimony

2 the higher prices without significantly
3 decreasing consumption, or at least not
4 changing their consumption as much as they
5 would in the other market, more total revenue
6 can be generated by increasing the price in the
7 markets where the response is less and charging
8 lower prices in the markets where customers
9 react more negatively to the higher prices.

10 This economic principle is the basic
11 tenet of Federal Milk Marketing Orders
12 classified pricing. The government holds that
13 total dairy farmer revenues can be increased by
14 charging a higher price for milk used for
15 beverage milk (Class I, market 1) than milk
16 used for other purposes (manufactured dairy
17 products/market 2) because they contend
18 consumers will decrease their consumption of
19 beverage milk less than they will decrease
20 their consumption of other products if those
21 prices were higher. This, we submit, is
22 unlikely in today's beverage market and
23 especially in the case of certain products that
24 do not meet the federal standards of identity
25 for milks but contain some dairy-derived

1 E. Tipton - Direct Testimony

2 ingredients and are often positioned for
3 specific segments of the market.

4 The second necessary rule for
5 successful price discrimination is that the
6 lower priced product cannot be substituted for
7 the higher priced product. Why would anyone
8 pay the higher price, at least for very long,
9 if the lower priced product were available? It
10 is raw milk of the same quality, healthfulness,
11 nutritional content, etc. It is
12 indistinguishable. It is the same milk, often
13 from the same farm, some is simply used for
14 beverage milk and the other is used for other
15 products. No one would pay the higher price in
16 such a circumstance--unless forced to do so.

17 To meet the criteria that the lower
18 priced milk cannot be substituted for the
19 higher priced milk, the federal government has
20 become the "enforcer." Its extensive,
21 complicated and heavily enforced rules prevent
22 the lower priced milk from being substituted
23 for the higher priced milk. The government
24 traces virtually every pound of milk from the
25 farm to the consumer at an enormous cost per

1 E. Tipton - Direct Testimony

2 year.

3 Additionally, the costs incurred by
4 dairy companies to create and maintain detailed
5 records of how the milk is used is also very
6 high.

7 Is the first criteria for price
8 discrimination/classified pricing being met?
9 The answer is probably not, but even more
10 importantly, is it even in the interest of
11 dairy farmers to continue this antiquated
12 72-year-old federal program of price
13 discrimination? The only reason to keep a
14 classified pricing system is if it, in fact,
15 enhances producer revenues. There is now
16 substantial doubt that it does.

17 If producers or the government did
18 not think price discrimination/classification
19 increased producer revenues, it would not be
20 used. But now new data and the greatly
21 changing beverage market raises very serious
22 doubts that dairy farmers get any more revenue
23 by pricing raw milk in different classes.

24 The new data reveals that for many
25 Class I products the higher Class I prices

1 E. Tipton - Direct Testimony

2 result in lower total revenues for that product
3 because of the large decrease in sales.

4 Total sales of fluid milk have
5 declined from the previous year in six of the
6 past eight years and at the end of 2004 were
7 three percent below 1999's sales, and per
8 capita sales of fluid milk have declined every
9 year since 1983 at a rate of about one percent
10 per year. This is not a new trend.

11 Fluid milk sales have simply not
12 kept pace with the rest of the beverage market.
13 Fluid milk is losing market share consistently
14 and regularly. Competing products are gaining
15 share daily. Bottled water sales now exceed
16 milk sales, as does coffee, and soft drinks.
17 Milk and beer sales are about the same.

18 New consumer responsiveness data
19 shows that most beverage milk products are
20 considerably more price responsive than
21 previously assumed and many are even more
22 responsive to price changes than the lower
23 priced products in Class II and Class III.

24 Price elasticities are the
25 traditional measure of price responsiveness.

1 E. Tipton - Direct Testimony

2 In the context of this testimony, it should be
3 noted that in order to increase revenues by
4 practicing price discrimination/classification,
5 there must be a difference in the elasticities
6 for the higher priced milk and the lower priced
7 milk.

8 Currently, there is a huge
9 discrepancy between historical measures of
10 price elasticities and more recent data. USDA,
11 in its most report to Congress dated July 2004
12 on the nation's generic promotion programs
13 contended that the retail price elasticity for
14 fluid milk was -0.098, meaning a 1.0 percent
15 increase in the retail price of fluid milk is
16 estimated to reduce per capita sales of fluid
17 milk by only 0.1 percent. This differs greatly
18 from two recent studies.

19 These new analyses show a very wide
20 range of elasticities for various fluid milk
21 products and even find a composite elasticity
22 for fluid milk that is nearly eight times
23 higher than that reported by USDA.

24 Dr. Oral Capps, Jr., of Texas A&M
25 University concludes that: "Historically there

1 E. Tipton - Direct Testimony

2 has been a void of information with respect to
3 elasticities of demand for fluid milk products.
4 Most of the information available was based on
5 analysis of all milk. Importantly, these
6 analyses often did not take into account the
7 competitive forces at work in the marketplace,
8 where milk comes in many forms and package
9 sizes. In fact, in a recent report to Congress
10 dated July 1, 2003, the own-price elasticity of
11 demand for fluid milk was reported to be -0.085
12 (Note: The July 1, 2004 report estimates
13 -0.098). The marketplace reality, according to
14 this project, is that for individual milk
15 products demand is not nearly so inelastic, and
16 for many products is, in fact, elastic."
17 (Presentation by Dr. Oral Capps, Jr., Southwest
18 Dairy Marketing Endowed Chair, Texas A&M
19 University, Managing Partner, Forecasting and
20 Business Analytics, LLC, in January 2004, at
21 the International Dairy Foods Association's
22 Dairy Forum in Boca Raton, Florida).

23 To illustrate his point, Dr. Capps
24 found that the elasticity for gallons of white
25 milk was -0.5597 (basically a one-percent

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2 increase in price results in nearly 0.6 drop in
3 consumption-still inelastic but six times less
4 inelastic than USDA reports); for gallons of
5 flavored milks Dr. Capps reports an elasticity
6 of -1.2092--quite elastic; for half gallons he
7 reports -1.7383 for white milk and -2.1063 for
8 flavored milk--both highly elastic. (Note:
9 When the elasticity exceeds one, an increase in
10 price will decrease consumption more than
11 proportionate to the price increase and total
12 revenues will be less.)

13 Dr. Capps found the demand for
14 carbonated soft drinks, bottled water and
15 juices/drinks were all quite elastic also. He
16 also found that carbonated soft drinks are
17 strong substitutes for both white and flavored
18 milk. He found that the elasticity of branded
19 milk in gallons was nearly one for one, i.e., a
20 one-percent change in price brought a
21 one-percent change in sales in the opposite
22 direction; private label milk in gallons was
23 about 1 to 0.6.

24 In all cases, the elasticities were
25 found to be less inelastic than previously

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2 believed and in many cases they were elastic.
3 Dr. Capps calculated elasticities for milks of
4 differing fat levels and also found the
5 individual elasticities to be much greater than
6 previously reported. (Presentation by Dr. Oral
7 Capps, Jr., Southwest Dairy Marketing Endowed
8 Chair, Texas A&M University, Managing Partner,
9 Forecasting and Business Analytics, LLC, in
10 September 2004, at BevExpo in Tampa, Florida.

11 Dr. Leigh Maynard at University of
12 Kentucky, using weekly data similar to that
13 used by Dr. Capps but from an earlier time
14 period found similar results. (Maynard, L.J.
15 and Dr. Liu "Fragility in Dairy Product Demand
16 Analysis," American Agricultural Economics
17 Association annual meeting, Nashville, TN,
18 August 1999).

19 As noted previously, Class I milk
20 sales have been in decline for many years. One
21 has to raise the question as to whether
22 continuing this system might be a serious error
23 in public policy.

24 It seems entirely likely that with
25 the burgeoning introductions of alternative

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2 drinks and competing beverages that consumers
3 are much more responsive to milk prices than
4 they were for decades past.

5 Additionally, it seems totally
6 logical that consumers do not perceive all
7 Class I products to be equal in satisfying
8 their needs, and therefore, react differently
9 to prices in making decisions.

10 Maybe flavored milk sales have not
11 grown as significantly as many may have
12 expected because the elasticities are high
13 (-1.2 for gallons and -2.1 for half gallons),
14 or maybe these higher elasticities apply to all
15 smaller size packages. I think this may well
16 be the case.

17 Clearly, extending Class I pricing
18 to beverages that are not milk under the state
19 and federal rules but contain only limited
20 amounts of milk-derived ingredients and/or
21 drinkable products that have not heretofore
22 been included in Class I is not appropriate
23 based on what has happened to fluid milk sales.

24 USDA has an obligation to producers,
25 processors and consumers to thoroughly study

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2 and evaluate the changes that are occurring in
3 the beverage market and whether its policy of
4 charging a higher price for all milks consumed
5 as beverages really helps dairy farmers or
6 whether changing the rules to include still
7 more products which are not even milk is dairy
8 farmers' best interest.

9 Additionally, USDA needs to
10 seriously evaluate whether dairy farmer
11 revenues will be increased or decreased if the
12 Class I definition is changed to encompass
13 beverages that contain only small amounts of
14 dairy-derived ingredients. We believe dairy
15 farmer revenues are more likely to be reduced
16 than increased and the demand for the
17 components of milk will be reduced also.

18 Drs. Charles Nicholson, Mark
19 Stephenson and Andrew Novakovic, professors at
20 the Department of Applied Economics and
21 Management at Cornell University, Ithaca, New
22 York, have modeled the market dynamics of
23 introducing new milk-based beverages.

24 They conclude that there is little
25 net additional revenues to be generated for

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2 dairy farmers by classifying these new
3 milk-based beverages in Class I. We believe
4 this is the case also. Efforts to capture more
5 products containing less than 6.5 percent
6 nonfat milk solids in Class I should be
7 rejected.

8 Although there is growing evidence
9 that it may no longer be in dairy farmers' best
10 interest to have classified milk pricing, that
11 is not an issue before this proceeding.

12 We have provided extensive
13 elasticity data related to fluid milks to make
14 the point that USDA should not adopt new rules
15 to extend classified pricing to new products
16 that contain limited amounts of milk-derived
17 ingredients because they are perceived to be
18 competitive with Class I milk.

19 To attempt to extract a Class I
20 price on the small amount of milk-derived
21 ingredients contained in coffee drinks, or
22 juice and milk or yogurt blends is a
23 substantial overreach and can only be viewed as
24 a protectionist action.

25 The protectionist advocates believe

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2 that classifying these type products in Class I
3 will deter their development and make them less
4 competitive with milk, thereby increasing
5 producer revenues from beverage milk. It is
6 not based on sound economic analysis. We
7 believe dairy farmer revenues will likely be
8 reduced by such protectionist action.

9 If such actions are taken by USDA,
10 it is highly likely that the products that now
11 contain some dairy-derived ingredients will be
12 reformulated to minimize, if not eliminate,
13 milk-derived ingredients by substituting
14 non-milk ingredients such as soy. The
15 technologies are now readily available to make
16 non-dairy ingredients fulfill functions similar
17 to those of dairy-derived ingredients.

18 Not only are class price issues
19 driving food formulators to use non-dairy
20 ingredient sources, but also the record keeping
21 and reporting requirements and presenting
22 records for audits by market administrators are
23 added burdens that many food processors would
24 prefer to avoid. This is another incentive to
25 use non-dairy ingredients.

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2 Additionally, the Food and Drug
3 Administration, through its Federal/State
4 Cooperative Milk Program is considering changes
5 to its dairy-specific health and sanitary
6 inspection programs so beverages that contain
7 some dairy-derived ingredients and are similar
8 to milk in their use would be subject to FDA's
9 "Grade A" milk requirements. This would limit
10 dairy ingredients used in such products to
11 those meeting the "Grade A" inspection
12 requirements, which from a practical
13 standpoint, would eliminate use of many
14 imported ingredients that are now very widely
15 used, as they do not meet FDA's "Grade A"
16 requirements.

17 This could include casein and
18 caseinates, concentrated proteins and other
19 fractionated components and nutrients contained
20 in milk including some that are not available
21 in significant quantities from domestic
22 producers.

23 This is yet another incentive for
24 food formulators to use non-dairy ingredients
25 in these new products. Higher costs, more

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2 recordkeeping and administrative burdens, and
3 special regulatory inspection requirements are
4 likely to reduce the use of dairy ingredients
5 in these type products, again, leaving less net
6 revenues for dairy farmers.

7 There are a number of new products
8 containing some milk-derived ingredients that
9 have been introduced to the market in the past
10 couple of years that have fallen short of food
11 processors' goals and expectations. Some have
12 been withdrawn from the market. There are no
13 beverages containing under 6.5 percent nonfat
14 solids that have gained significant share of
15 the market.

16 Among some of the products to have
17 received a lot of press in the dairy industry
18 are Nestle Choglit (no longer on the market),
19 Coca Cola's Swerve (only limited distribution),
20 Cadbury's Raging Cow (only limited
21 distribution), Atkins' Advantage Shake (only
22 limited success), and several brands of
23 Smoothies, a blend of juice, kefir and/or
24 yogurt.

25 Only Starbucks' Frappuccino has

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2 lasted and obtained limited market penetration.
3 However, Frappuccino is not a product that
4 competes with or is substituted for milk.
5 Nearly 75 percent of Frappuccino is consumed as
6 an "a.m." or "p.m." snack. It contains less
7 than 6.5 percent by weight of milk-derived
8 ingredients. It is not positioned in the
9 marketplace as a competitive alternative to
10 milk.

11 The top four reasons cited by
12 consumers as to why they buy this product is
13 that it is portable, it is an indulgence/a
14 treat, it is a change of pace, and it is fun to
15 drink. It is most frequently consumed in a
16 vehicle, with consumption at home placing
17 third.

18 It is displayed in the
19 non-carbonated beverage section of the soft
20 drink aisle or the cold case of most grocery
21 stores. It is clearly a snack product and not
22 an alternative to milk beverage.

23 Another product, Cadbury's Yoo-hoo,
24 has been on the market for many years but has
25 only achieved meager penetration. In fact, the

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2 6.5 percent standard was inserted primarily to
3 exclude this product from Class I.

4 USDA has a long history of
5 responsibly addressing issues under Federal
6 Milk Orders that reflect major changes in
7 markets or operations and has avoided making
8 significant changes to the program in response
9 to short-term market phenomena. Making a sea
10 change decision on this issue at this time is
11 unwarranted and premature.

12 The companies on whose behalf this
13 statement is made support the continuation of
14 the 6.5 percent nonfat solids requirement
15 currently contained in the orders with some
16 added clarity as to how it is to be
17 administered.

18 The USDA decision that first
19 contained the 6.5 percent nonfat milk solid
20 standard is instructive: "The 6.5 percent
21 nonfat milk solids standard is used to exclude
22 from the fluid milk product definition those
23 products which contain some milk solids but
24 which are not closely identified with the dairy
25 industry, such as chocolate flavored drinks in

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2 "pop" bottles.

3 These composition standards are
4 chosen so as to conform as closely as possible
5 to the water, solids and butterfat content of
6 those products specifically listed in the fluid
7 milk product definition, i.e., the traditional
8 milk beverages. It is intended that these
9 standards apply only to milk products and only
10 to such products that are being marketed for
11 consumption in fluid form.

12 In determining whether or not a milk
13 product in fluid form falls within the
14 composition standards of the fluid milk product
15 definition, such standards should be applied to
16 the composition of the finished product in its
17 finished form, not to the composition of the
18 product on a skim equivalent basis.

19 A new product not intended for
20 beverage use might contain in its finished form
21 somewhat more than the maximum total solids
22 specified for a fluid milk product under the
23 adopted composition standards. On this basis,
24 the product would not fall within the fluid
25 milk product definition. Application of the

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2 composition standards to this product on a skim
3 equivalent basis, however, could result in the
4 product meeting such standards and thus being
5 defined as fluid milk product.

6 As pointed out by producers in their
7 exceptions, applying the compositions standards
8 to products in the form in which marketed could
9 exclude from the fluid milk product definition
10 a new concentrated fluid product that is
11 intended to be consumed as a beverage only
12 after reconstitution.

13 For the present time, however, the
14 composition standards should be applied to a
15 product in its finished form. A refinement of
16 such standards may be appropriate once there
17 has been an opportunity to evaluate their
18 applicability under actual market conditions.

19 It should be noted that under the
20 adopted classification provisions, accounting
21 for a new product on other than a skim
22 equivalent basis would be limited solely to
23 determining whether or not the product meets
24 the composition standards of the fluid milk
25 product definition. For all other purposes

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2 under the order, the product would be accounted
3 for on a skim equivalent basis.

4 In applying the 6.5 percent nonfat
5 milk solids standard, it is intended that this
6 standard apply to such solids in any form
7 except sodium caseinate." (39FR8714-8716,
8 March 6, 1974).

9 It is clear and specific that the
10 6.5 percent nonfat milk solids standard is to
11 be applied on a weight basis to the composition
12 of the product in its finished form and not to
13 the composition of the product on a skim
14 equivalent basis. This is an important
15 distinction and is the concept we support. We
16 oppose calculating compliance with the 6.5
17 percent standard on a milk equivalent basis.

18 The 1974 decision has not been
19 changed. It has now been the rule for 31
20 years. These provisions were explicitly
21 reviewed again during the 1998-2000 so-called
22 Federal Milk Order Reform process and was
23 explicitly reconfirmed in the 1999 final rule.

24 "4f. CLASS I MILK

25 In this final decision, Class I milk

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2 includes all skim milk and butterfat contained
3 in milk products that are intended to be
4 consumed in fluid form as beverages, with
5 certain exceptions.

6 These exceptions include: Plain or
7 sweetened evaporated or condensed milk, milk
8 that is used in formulas especially prepared
9 for infant feeding or meal replacement if such
10 products are packaged in hermetically-sealed
11 containers, and any product that contains by
12 weight less than 6.5 percent nonfat milk
13 solids." (Excerpt from USDA's printed copy of
14 the 1999 final rule)

15 Retention of these provisions was
16 not inadvertent nor for lack of attention.
17 USDA formed several committees to review
18 certain provisions of federal orders and make
19 recommendations for the Secretary's
20 consideration.

21 The Federal Order Reform
22 Classification Committee recommended the
23 elimination of the 6.5 percent nonfat milk
24 standard, but it was not adopted, and it was
25 not adopted for good reason. If eliminated, it

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2 would have left enormous discretion to USDA.
3 The requirement that a product must have at
4 least 6.5 percent nonfat solids provides clear
5 parameters and definition, both very important
6 to a regulatory program such as this.

7 The 6.5 percent nonfat milk standard
8 is as appropriate today as it was in 1974. It
9 establishes a definitive level of nonfat milk
10 solids that distinguishes which beverages
11 containing milk-derived ingredients are Class I
12 and which are not.

13 It is important, however, that the
14 measurement of whether the 6.5 percent standard
15 has been exceeded continue to be by weight of
16 the finished product. It is a clear and
17 concise rule that can be easily understood and
18 followed. It allows the inclusion of all forms
19 of nonfat milk solids to be measured and
20 included in the determination.

21 It has been proposed that a milk
22 equivalent rule be used to determine whether
23 the nonfat milk solids exceed or fall below the
24 6.5 percent standard. A milk equivalent rule
25 is complicated, difficult to understand and

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2 comprehend and is not as precise. It would
3 exclude some milk components depending on how
4 it is applied or it could double count some
5 components, again depending on how it is
6 computed.

7 Milk contains many major components
8 and nutrients. Therefore, to calculate milk
9 equivalency when the various components are
10 included in varying amounts in a finished
11 product would double count and overstate the
12 milk equivalency.

13 As an example, if a product contains
14 caseinates, whey isolate, lactose and calcium,
15 and if the standard is based on the amount of
16 milk required to produce the amount of each
17 component in the milk, the milk equivalency
18 could be four times the appropriate amount.

19 Some of the proposals in the hearing
20 notice would replace the 6.5 percent nonfat
21 solids standard with a protein standard.
22 Companies supporting this testimony are opposed
23 to such a change.

24 One of the proposals would
25 substitute 2.25 percent milk protein for the

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2 6.5 percent nonfat milk solids standard. This
3 is not appropriate for several reasons.

4 Some say the two standards are
5 equivalent to each other, but this is not the
6 case. Protein is only one of the components in
7 milk. The 2.25 percent protein standard is
8 equivalent to the amount of protein in skim
9 milk containing 6.5 percent nonfat solids,
10 according to USDA standards for calculating
11 equivalencies. (i.e. skim milk contains 9.0
12 percent nonfat solids. 34.44 percent of that
13 9.0 percent is protein, so the protein in 6.5
14 percent nonfat solids is 2.25) Using only one
15 nutrient, protein, as the standard provides a
16 significantly different result than using
17 nonfat milk solids.

18 The 6.5 percent nonfat milk solids
19 standard encompasses all milk-derived
20 components. The standard simply says that if a
21 product contains 6.5 percent or more nonfat
22 milk-derived ingredients, it would be Class I,
23 and if less than 6.5 percent, it would not.
24 Milk-derived nonfat solids could be composed of
25 any one or more of all the components of milk.

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2 They are not required to be in the same
3 portions as they are normally contained in skim
4 milk.

5 If a 2.25 percent standard replaces
6 the nonfat milk solids standard in order to
7 avoid Class I classification, the amount of
8 milk protein would be limited to a fairly low
9 level that would qualify as a good source of
10 protein, but products containing 10 grams of
11 protein, the minimum amount required to make a
12 nutrient claim of "high," "rich in," or
13 "excellent source of protein" would be Class I.

14 Using the 6.5 percent nonfat milk
15 solids standard would permit the high protein
16 claims to be made and would further stimulate
17 the market for concentrated dairy proteins.

18 There is a great deal of
19 experimentation with the use of whey proteins
20 especially in sports drinks. The development
21 of special high protein drinks should be
22 encouraged and not be limited simply because of
23 a regulation inserted in the rules primarily to
24 protect milk against competition from other
25 parts of the beverage industry. Dairy proteins

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2 are important components of milk and their use
3 should be strongly encouraged, not discouraged.

4 The dairy industry has shackled
5 itself with regulations, definitions and
6 multiple restrictions that impede innovation
7 and creation. Innovation and creativity are
8 the foundation for effective competition and
9 competition is the stimulating force of market
10 growth. Leveling the playing field through
11 laws and regulations is the enemy of growth and
12 profitability.

13 The 6.5 percent nonfat milk solids
14 standard should not be changed and limited
15 effects of a 2.25 percent milk-derived protein
16 standard should not be included.

17 Kefir and yogurt are similar
18 products in that they are fermented by
19 culturing with the use of living
20 microorganisms. Kefir, low fat kefir and
21 nonfat kefir are defined under the cultured
22 milk products section of the Code of Federal
23 Regulations, whereas yogurt has its own
24 standard of identity.

25 Currently, beverage forms of these

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2 products, if they contain 6.5 percent nonfat
3 milk solids are Class I. If they contain less
4 than 6.5 percent in nonfat milk solids or if
5 they are not for drinking, they are Class II.

6 Both yogurt and kefir are often
7 combined with other liquids such as fruit
8 juices, purees, water and other ingredients to
9 provide a specific taste and texture. These
10 mixes are sometimes marketed using the name
11 "smoothie" and in such cases yogurt or kefir
12 are identified as ingredients or as a product
13 containing two foods such as fruit juices and
14 kefir or yogurt.

15 Cultured dairy products are one of
16 the fastest growing segments of the dairy
17 industry, about five percent per year and
18 yogurt and kefir are anchoring the growth. We
19 believe yogurts that are combined with other
20 foods and water provide an excellent
21 opportunity for dairy farmers to expand the use
22 of dairy ingredients and should not be burdened
23 with the additional costs of Class I
24 classification.

25 Based on a number of factors, it is

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2 clear that drinkable kefir and yogurt are not
3 milk and do not compete with fluid milk. Both
4 have the characterizing bacterial cultures that
5 milk does not have, and these cultures have
6 therapeutic benefits to the body such as
7 contributing to gastrointestinal health,
8 improved immunity and lower cholesterol. They
9 are not consumed in lieu of milk or as a
10 substitute for milk.

11 In the case of kefir, it is not
12 bought as a beverage to be consumed with food
13 but rather as a snack or meal replacement
14 specifically because of the probiotic cultures
15 and the hunger satiation feeling it provides
16 due to its viscosity.

17 These products are frequently not
18 sold in the same section of the store as milk,
19 they have a substantially different texture and
20 taste profile and are typically packed in
21 containers that are intended to be consumed "on
22 the go" in a single serving.

23 Consumers choose kefir and yogurt
24 culture beverages for different occasions and
25 taste reasons than when consumers elect to

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2 purchase fluid milk. In light of these
3 distinct differences, kefir and yogurt should
4 be classified in Class I for all uses.

5 Proposal No. 3 would replace the
6 requirement that special products that are
7 excluded from Class I be packaged in
8 hermetically-sealed containers with new
9 language--"packaged in containers that are
10 shelf stable at ambient temperatures."

11 Virtually all, if not all, of the
12 special formulas currently excluded from Class
13 I or proposed for exclusion are subject to
14 FDA's thermally processed low-acid foods
15 regulation (21 CFR113).

16 These regulations require all such
17 foods with a finished equilibrium pH greater
18 than 4.6 to be aseptically processed and
19 packaged in hermetically-sealed containers. As
20 a result, we are not certain that the newly
21 proposed language would in reality include any
22 packaging material or process not covered by
23 FDA's low acid food regulations.

24 We support continued use of the
25 current criteria that is known terminology and

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2 consistent with the FDA's terminology and
3 regulations. The only additional products that
4 the new language might apply to are foods
5 (beverages) with a pH of 4.6 or lower that
6 would have sufficient acidity to be outside the
7 low acid food regulations.

8 Prior to the 1974 decision on
9 classification, all fluid milk products that
10 were packaged in hermetically-sealed glass or
11 can containers were excluded from Class I. In
12 the 1974 decision, USDA changed these
13 provisions and concluded that all fluid milk
14 products whether sterilized or unsterilized
15 should be included in Class I.

16 However, at that time USDA
17 specifically concluded "Evaporated milk and
18 condensed milk sold for home use are intended
19 primarily for cooking purposes. They are not
20 consumed normally as a beverage. Infant and
21 dietary formulas which are being sold in
22 hermetically-sealed glass or all metal
23 containers are specialized food products
24 prepare for a limited use. Such formulas do
25 not compete with other milk beverages consumed

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2 by the general public. Similarly, fluid
3 products containing only a minimal amount of
4 nonfat milk solids are not considered as being
5 in the competitive sphere of the traditional
6 milk beverages." (39 FR8715)

7 The Federal Order Reform Rule of
8 1999 continued the exemption and it now reads
9 "formulas especially prepared for infant
10 feeding or dietary use (meal replacement) that
11 are packaged in hermetically-sealed
12 containers."

13 Notwithstanding this long history of
14 classification of meal replacement products in
15 Class II, one of the proposals submitted for
16 the hearing would do away with the specific
17 meal replacement exclusion. There is no basis
18 for doing this.

19 Although we believe the phrase
20 "dietary use" includes meal replacement
21 products such as Slim-Fast, a product of
22 Unilever United States and a party to this
23 testimony, we urge USDA to continue to specify
24 meal replacements as a food exempted from Class
25 I. Slim-Fast products are a prototype of the

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2 meal replacement exclusion.

3 Slim-Fast observes the following
4 criteria for the development of its products,
5 each of which reaffirms their identity as a
6 meal replacement distinct from milk and other
7 beverages: Formulated meal replacement
8 products are intended for use as part of a
9 weight control diet; when substituted for
10 normal meals, they help maintain adequate
11 nutrition while reducing overall caloric
12 intake; meal replacements are formulated to
13 supply about one-third of the daily value for
14 essential vitamins and minerals; meal
15 replacements are formulated to supply at least
16 20 percent of the daily value for protein per
17 serving; meal replacements are formulated to
18 supply a good source of fiber; and meal
19 replacements drinks are labeled with
20 instructions that a drink be consumed in place
21 of one or two meals per day.

22 In many areas outside of milk
23 pricing, the law does not treat Slim-Fast as a
24 beverage. For example, of the 11 states that
25 have mandatory bottle deposit laws for beverage

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2 containers (which add a deposit amount, usually
3 five to ten cents per container that is
4 refundable upon return of the used container
5 and are intended to reduce solid waste and
6 litter), none require such deposits for
7 Slim-Fast or other similar meal replacement
8 products.

9 Finally, AC Nielsen, which tracks
10 market data for every product sold in a grocery
11 store, tracks Slim-Fast in the weight loss
12 category along with diet pills and other
13 similar products specially formulated to aid in
14 weight loss.

15 The example of Slim-Fast clearly
16 demonstrates the wisdom of the meal replacement
17 exclusion that has been a part of USDA
18 regulations for 31 years and which should be
19 preserved.

20 Those companies on whose behalf this
21 testimony is being given support the
22 continuation of the longstanding exemptions for
23 formulas for infant feeding and dietary use
24 (meal replacement).

25 They also support expanding the

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2 types of products excluded to not only exclude
3 both dietary uses and meal replacements but
4 specifically identify other types of special
5 formulas that are specialized food products
6 prepared for a limited use.

7 We suggest that FDA's requirements
8 for foods for special dietary use provide a
9 good framework to discuss this suggestion.
10 Section 411(c)(3) of the Federal Food, Drug and
11 Cosmetic Act defines special dietary use as a
12 particular use for which a food purports or is
13 represented to be used. These divide into
14 three categories which we call clinical,
15 supplemental and sole source.

16 Clinical: Supplying a special
17 dietary need that exists by reason of a
18 physical, physiological, pathological or other
19 condition, including but not limited to, the
20 conditions of disease, convalescence,
21 pregnancy, lactation, infancy, allergic
22 hypersensitivity to food, underweight,
23 overweight or the need to control the intake of
24 sodium.

25 Supplemental: Supplying a vitamin,

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2 mineral or other ingredient for use by humans
3 to supply the diet by increasing the total
4 intake.

5 Sole Source: Supplying a special
6 dietary need by reason of being a food for use
7 as the sole item of the diet.

8 Given this regulatory structure, we
9 suggest the following exclusions:

10 Formulas especially prepared for
11 infant feeding--a continuation of the current
12 regulations;

13 Formulas especially prepared for
14 meal, snack replacement--meal replacements are
15 currently excluded from Class I, and we suggest
16 that snack replacements be added to this
17 phrase. There are an increasing number of
18 dietary recommendations that urge consuming
19 smaller amounts of food at a given eating
20 occasion but consume these smaller amounts more
21 frequently. As a result, many meal replacement
22 products also include items for snacks to
23 replace meals;

24 Formulas especially prepared for
25 high protein drinks and have a protein content

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2 greater than ten grams per serving. The level
3 established by FDA in 21 CFR 101.54(b) that
4 must be met for a product to be called high
5 protein;

6 Beverages that contain alcohol and
7 are licensed by the Federal Tax and Trade
8 Bureau, U.S. Department of the Treasury and;

9 Packaged milk products that are
10 specifically formulated and labeled for animal
11 use.

12 We believe none of these products
13 compete with or would replace sales of fluid
14 milk beverages. They would simply be additive
15 and create opportunities to use additional milk
16 components.

17 Whey, a by-product of cheese
18 production has become a highly versatile source
19 of protein for many foods, some of which are
20 drinkable. Dairy farmers are paid for the milk
21 from which the cheese is made that in turn
22 generates the whey, when it is purchased by the
23 cheese processor. It is unnecessary and
24 inappropriate to try to collect the Class I
25 differential when it is used in various drinks.

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2 Many sports drink formulations use
3 whey proteins. These products are highly
4 acidic and contain various juices, water,
5 vitamins and other minerals. Often they do not
6 contain any other dairy component. They are
7 not substitutes for fluid milk beverages and
8 cannot be considered to be competitive with
9 milk. We believe the appropriate treatment is
10 to exclude whey and whey products from the
11 determination of the 6.5 percent nonfat milk
12 solid standard.

13 We believe USDA should classify in
14 Class I only specifically defined products,
15 either those that are federally standardized or
16 are otherwise specially identified and defined.

17 However, USDA has for a number of
18 years used the undefined and nebulous criteria
19 of "products intended to be consumed as
20 beverages." Beverages are not defined in
21 actual orders so the present language allows
22 great latitude and discretion in the officials
23 administering the program.

24 However, new criteria is being
25 proposed -- "intended to be used as a

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2 stand-alone beverage." Although "intended to
3 be used as a beverage" is quite unspecific, the
4 word "beverage" has a common and usual meaning
5 that has been ascribed to it over time and, of
6 course, is cited in virtually all dictionaries.
7 A stand-alone beverage has no history of use or
8 meaning. It is unclear what value is added by
9 the creation of this new terminology or which
10 products would be captured by it that are not
11 now covered by the current language. We oppose
12 using such an undefined and indefinable
13 criteria.

14 In conclusion, given recent trends
15 in sales of Class I milk, we believe USDA's
16 policies should be focused on promoting growth
17 and innovation, especially in terms of new
18 products within the dairy category. Any
19 efforts to expand the reach of Class I will
20 have the opposite effect likely prompting
21 reformulation with non-dairy ingredients and
22 driving up the costs of products which new
23 research shows to be increasingly price
24 sensitive.

25 We believe the development of new

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2 dairy-based products and those containing
3 dairy-derived ingredients are not a threat to
4 be met with new regulation but are, in fact, an
5 important part of the dairy industry's ability
6 to compete with the alternative beverages over
7 which USDA has no authority.

8 We urge the Department to recognize
9 these forces in the marketplace and not
10 overreact by increasing the cost and regulatory
11 burden on those trying to bring the benefits of
12 milk and its components to consumers through
13 new products they desire.

14

15 ADDITIONAL STATEMENT OF E. LINWOOD TIPTON

16 Although I have already presented a
17 statement on behalf of Lifeway Foods as well as
18 others, Lifeway Foods has requested that I
19 present additional testimony on their behalf
20 specific to their proposal for the Class II
21 classification of kefir.

22 Over 80 percent of the kefir sold in
23 the United States is produced and marketed by
24 Lifeway Foods, a family-operated business in
25 Morton Grove, Illinois. Kefir competes

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2 directly with yogurt and should be in the same
3 class, Class II, as yogurt for all uses.

4 Kefir is a cultured dairy product
5 similar to yogurt. Both products have
6 characterizing bacterial cultures which
7 consumers buy based on the probiotic cultures'
8 various health benefits that are otherwise
9 absent in milk.

10 The viscosity of kefir is very
11 similar to yogurt. Some yogurts are a little
12 more viscous than kefir and some are less.
13 Kefir is within the range of viscosities of
14 yogurt.

15 Kefir, like yogurt, is not usually
16 consumed with a meal except for breakfast.
17 Both kefir and yogurt's snack usage is large.
18 Most kefir as in the case with yogurt are
19 sweetened.

20 The acidity of kefir and yogurt are
21 about the same. Kefir and yogurt are
22 competitive products which can be substituted
23 for each other at various eating occasions. We
24 strongly urge USDA to put kefir in Class II,
25 the same class as yogurt.

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2 Kefir-cultured beverages are
3 beverages that contain the standardized
4 ingredient kefir (or a reduced fat version)
5 fruit juice or puree, water and/or other
6 ingredients to provide a specific taste and
7 viscous texture.

8 Currently, beverage forms of these
9 products if they contain 6.5 percent nonfat
10 milk solids are Class I. If they contain less
11 than 6.5 percent nonfat milk solids or if they
12 are not for drinking, they are Class II.

13 Both yogurt and kefir are often
14 combined with other liquid such as fruit
15 juices, purees, water and other ingredients to
16 provide specific taste and texture. These
17 mixes are sometimes marketed using the name
18 "smoothie" and in such cases yogurt or kefir
19 are identified as ingredients or as a product
20 containing two foods, e.g. fruit juices and
21 kefir or yogurt.

22 Cultured dairy products are one of
23 the fastest growing segments of the dairy
24 industry, about five percent per year and
25 yogurt and kefir are anchoring the growth. We

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2 believe kefir and yogurts that are combined
3 with juices, other foods and water provide an
4 excellent opportunity for dairy farmers to
5 expand the use of dairy ingredients and should
6 not be burdened with the additional costs of
7 Class I classification.

8 Based on a number of factors, it is
9 clear that drinkable kefir and yogurt are not
10 milk and do not compete with fluid milk. They
11 are not consumed in lieu of milk or as a
12 substitute for milk. These products are
13 frequently not sold in the same section of the
14 store as milk, they have a substantially
15 different texture and taste profile and are
16 typically packed in containers that are
17 intended to be consumed "on the go" in a single
18 serving.

19 Consumers choose kefir and yogurt
20 culture beverages for different occasions and
21 taste reasons than when consumers elect to
22 purchase fluid milk. In light of these
23 distinct differences, kefir and yogurt should
24 be classified in Class II for all uses.

25 Finally, while kefir and yogurt do

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2 have some distinct qualities, they are clearly
3 both cultured products so while we strongly
4 urge the Class II classification of both
5 products, it is also clear that these two
6 should be placed together in the same class.

7 Due to the similarities that exist,
8 if one were to be placed in Class II and the
9 other in Class I, that would be a clear
10 competitive advantage for the Class II product
11 and not merited by the facts given their
12 similar composition.

13 In conclusion, I want to return to
14 the theme of my earlier statement regarding my
15 feeling that for the U.S. dairy industry to
16 thrive in the coming years, as I believe it
17 can, USDA must embrace policies that encourage
18 growth and innovation in the development of
19 dairy products and products containing dairy
20 ingredients.

21 Cultured dairy products are one such
22 category where great opportunities exist and
23 most especially for kefir, so I hope the
24 Department will look at the issues relating to
25 yogurt and kefir and see that the interests of

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producers and processors are truly aligned when these products are placed in a more competitive position and not shackled by regulations which, however well-intended, have the effect of dampening the prospects for this category. Thank you.

JUDGE DAVENPORT: Due to the late hour and the length of the exhibit, it would be best if we postpone the examination of this witness until tomorrow morning. That being the case, this might well be an appropriate time for us to recess.

Let's just briefly recap what I have at least remaining. It's my understanding that we would have the cross-examination of Mr. Tipton tomorrow morning. We would also have Mr. Hollon back on the stand, and I also have Mark S. Roberts who is here for Hormel Foods and a cross-examination as well as Mr. Wilson.

Are there any other parties or individuals or entities that need to be heard from? That being the case, let's make that the tentative order of arrangement for tomorrow

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morning. We will recess at this time until
8:00 tomorrow morning.

(Whereupon, the above-entitled
matter was concluded at 4:50 p.m., this date.)

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C E R T I F I C A T E

I hereby certify that the proceedings and evidence are contained fully and accurately in the stenographic notes taken by me on the hearing of the within cause and that this is a correct transcript of the same.

Cheri A. Redlinger
Professional Court Reporter