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VOLUME II

BEFORE THE SECRETARY OF
THE UNITED STATES DEPARTMENT OF AGRICULTURE
AGRICULTURAL MARKETING SERVICE

In the Matter of Proposed Amendments: : Docket Number
to Tentative Marketing Agreements : : AO-14-A74, et al
and Orders : : DA-06-01

National Public Hearing
January 25, 2006
Sheridan Suites
801 North St. Asaph Street
Alexandria, Virginia 22314

BEFORE:

THE HONORABLE PETER M. DAVENPORT
U.S. ADMINISTRATIVE JUDGE
UNITED STATES DEPARTMENT OF AGRICULTURE

1 APPEARANCES:

On Behalf of United States Department of Agriculture:

2 Sharlene Deskins
Babak Rastgoufard
3 Jack Rower
Henry H. Schaefer
4 Jason Nierman
Erin Taylor

5 On Behalf of Agri-Mark:

6 John Vetne
7 Robert Wellington
Richard Langworthy
8 Dennis Schad
Jim Sleper

9 On Behalf of National Cheese Institute:

10 Steven Rosenbaum

11 On Behalf of Select Milk Producers, Continental Dairy
12 Products and Dairy Producers of New Mexico:

13 Benjamin Yale
Ryan Miltner
14 Kristine H. Reed

15 On Behalf of the Association of Dairy Cooperatives in the
Northeast:

16 Marvin Beshore

17 On Behalf of the National Cheese Institute:

18 Steven Rosenbaum

19 On Behalf of Upstate Farms and O-At-Ka Milk Cooperatives

20 Timothy Harner

21 On Behalf of Dean Foods:

22 Wendy Yoviene

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1 Day 2 - January 25, 8:30 a.m. MORNING SESSION

2 THE JUDGE: Good morning, ladies and
3 gentlemen. We are back in session. This
4 morning, rather than continue Mr.
5 Wellington's testimony, we have a number of
6 dairy farmers that have come in from
7 Pennsylvania, no little inconvenience to
8 themselves. And as I announced before, what
9 I would like to do is I would like to take
10 them at this time so that they can get back
11 to their other activities as rapidly as
12 possible.

13 So at this time, Mr. Tewksbury, if
14 you want to come forward.

15 Mr. Tewksbury, do you have a prepared
16 statement?

17 MR. TEWKSBURY: Yes, I do, sir.

18 THE JUDGE: If you would, I would
19 like to have four copies given to the
20 hearing reporter. And then, if there are
21 other copies, we can make them available to

1 the other individuals.

2 MR. TEWKSBURY: Why don't I give all
3 the copies, the extra ones, to someone --
4 the people here at the table here.

5 MS. DESKINS: We'll help you
6 distribute them.

7 Whereupon,

8 ARDEN TEWKSBURY,
9 having been first sworn by the judge, was
10 examined and testified under oath as follows.

11 THE JUDGE: Tell us your name and, if
12 you would, spell your last name for the
13 hearing reporter.

14 THE WITNESS: My first name is Arden,
15 A-R-D-E-N. And the last name is Tewksbury,
16 T-E-W-K-S-B-U-R-Y.

17 [Whereupon, Exhibit 30 was marked
18 for identification by the judge.]

19 THE JUDGE: Mr. Tewksbury, your
20 statement has been marked as Exhibit 30, if
21 you wish to read your statement into the

1 record at this time.

2 THE WITNESS: Yes, Your Honor. And
3 before I start my testimony, I would like to
4 just speak to the USDA for a minute, okay.

5 There are a lot of dairy farmers
6 that did not know this hearing was going on.
7 And I know it was in the Federal Register,
8 and I know that there is a news release put
9 out. I have a copy of it. But I think that
10 when there is going to be a hearing that
11 could have at least an adverse effect upon
12 our dairy farmers' prices, that maybe these
13 dairy farmers should receive a notice as
14 well.

15 Evidently, it was not time enough to
16 get it into the bulletins. So if that is not
17 going to take place, I think the dairy
18 farmers themselves should be notified. I
19 think they, too, are interested parties in
20 this hearing procedure.

21 STATEMENT FOR THE RECORD OF ARDEN TEWKSBURY

1 Mr. Chairman, my name is Arden
2 Tewksbury. I reside at RR#2, Box 165,
3 Meshoppen, Pennsylvania. I have been a
4 dairy farmer all my life in the Meshoppen
5 area. Recently, I moved many of my animals
6 to Faithopity Farms located at 492 Cemetery
7 Road, Berwick, Pennsylvania (Columbia
8 County).

9 Currently I am associated with the
10 farm in different ways. The farm is owned
11 by two sisters and two brothers. They are
12 currently milking 450 cows

13 The owners installed a DeLaval rotary
14 milking parlor in 1996 to enable them to milk
15 their animals on a timely basis. A computer
16 system has been installed that tabulates the
17 cows' production on a daily basis. The
18 computer also gives Faithopity owners other
19 valuable information

20 The owners grow all their forage used
21 on the farm using about 1,500 acres of land.

1 The best part of this operation is
2 that all the work done on the farm is done
3 entirely and strictly by family members.
4 There is no outside help used and certainly
5 there are no illegal immigrants used on the
6 farm.

7 Presently I serve as Manager of the
8 Progressive Agricultural Organization which
9 is headquartered at my residence.

10 In the past I have been associated in
11 different capacities with the Pennsylvania
12 Farmers Union, the Pennsylvania State
13 Grange, the Regional Cooperative Marketing
14 Agency, the North East Interstate Dairy
15 Compact, the Northern Tier Milk Cooperative,
16 and for many years with the former Eastern
17 Milk Producers Dairy Cooperative.

18 My appearance today at this hearing
19 is being made on behalf of the Progressive
20 Agricultural Organization, Faithopity Farms,
21 and other organizations that we have

1 attached to our testimony. And the names of
2 those organizations are on the back. They
3 are Farm Wives United from North Java, New
4 York; Tioga Valley Milk Co-op, Tioga,
5 Pennsylvania; Family Farm Defenders in
6 Madison, Wisconsin; American Raw Milk
7 Association in Wauna Key, Wisconsin;
8 Pennsylvania Farmers Union from Mifflintown,
9 Pennsylvania; National Family Farm Coalition
10 in Washington, D.C.; and South Auburn Grange
11 in Susquehanna County, Pennsylvania.

12 These organizations have all endorsed
13 our appearance here today

14 We oppose any amendment that would
15 increase the make allowance of manufactured
16 milk at the expense of the dairy farmers.
17 Actually, I have a problem in finding proper
18 language in any Federal Agriculture Act that
19 calls for dairy farmers to pay for a
20 substantial amount of the cost of converting
21 milk to manufactured milk products.

1 When Order Reform took place on
2 January 1st, 2000, I wrote an editorial
3 entitled, "Order Reform - A Processor's
4 Dream." With order reform, dairy farmers
5 shipping milk to a milk handler that had been
6 regulated by former Order 2 have seen their
7 hauling cost triple, and now almost
8 quadruple. These farmers still pay a
9 substantial amount of money for advertising
10 milk and milk products.

11 However, the granddaddy of
12 everything was when the dairy farmers in
13 Federal orders were compelled to pay for the
14 make allowance. Any further increase in
15 make allowances charged to dairy farmers
16 would be very detrimental. Certainly, at
17 Faithopity Farms, we know what this would
18 mean to our bottom line.

19 I realize the dairy processing
20 business can be a little rough at times.
21 But, let me say, it gets darned rough for

1 the dairy farmers most of the time

2 Please remember that dairy farmers are
3 also experiencing extreme increased cost for
4 the fuel used on their farms. But these
5 costs are only part of the problem.

6 Dairy farmers are also being whacked
7 by higher costs for almost everything they
8 purchase. But, you know what, the dairy
9 farmers don't have a sugar daddy to reach
10 out and help with them with this accelerated
11 cost.

12 Instead of this hearing to take more
13 money from dairy farmers, we should be
14 having a hearing to price raw milk
15 differently.

16 We should have a formula to price raw
17 milk fairly to the dairy farmers, and to the
18 processor, and then to the consumers.
19 Something is wrong when I see a certain
20 national brand of butter selling for over \$4
21 per pound and I know that dairy farmers have

1 paid for the majority of the cost for
2 converting that milk into the butter.
3 Something is wrong when cheese companies
4 continue to use imported milk protein
5 concentrate in making cheese. To complicate
6 it more, I have been told by store owners
7 that under the WIC program, cheese
8 containing milk protein concentrate cannot
9 be made available to the recipients.

10 Something is wrong when I find a
11 gallon of milk in Monticello, New York,
12 selling for \$4.39 per gallon.

13 Mr. Chairman, if things are that
14 rough in the processing business, then how
15 has Leprino Foods surfaced from a small
16 operation in Colorado to become the large
17 manufacturer of mozzarella cheese

18 How then has a large pizza maker in
19 Michigan become an owner of national sports
20 franchises like baseball, hockey and
21 whatever else?

1 My understanding is that if the make
2 allowance was not charged to dairy farmers,
3 then in August 2005 the Class III price
4 would have been approximately \$16.14 per
5 pound instead of \$13.60. Class II would have
6 been approximately \$15.63 a hundredweight
7 instead of \$13.95, and the Class IV price
8 would have been approximately the \$15.12
9 instead of the \$13.44. The higher
10 manufacturing price would have meant a
11 higher Class I price also. If everything
12 stayed equal, the Class I price of August
13 2005 in Boston would have been \$20.26 instead
14 of \$16.95.

15 Certainly these figures show that
16 dairy farmers are not receiving their fair
17 share of the market price.

18 Pro Ag feels there are sufficient
19 reasons why there should be no increase
20 charged to dairy farmers for the make
21 allowance.

1 The dairy farmers just don't have a
2 direct way to recover their cost of
3 production for producing milk.

4 In closing, I want to point out that
5 in Pennsylvania, the Pennsylvania Milk
6 Marketing Board has been establishing an
7 over-order premium on Class I milk for
8 nearly 18 years. Currently this premium is
9 \$1.90 per hundredweight. However, 35 cents
10 per hundredweight of the \$1.90 is paid to
11 dairy farmers to compensate for higher costs
12 to transport milk from the farm to the
13 marketplace. This applies only to Class I
14 milk that is used in Pennsylvania.

15 The fact that the Pennsylvania Milk
16 Marketing Board can use dairy farmers'
17 increased cost to justify higher prices,
18 then I think it's time that the USDA and the
19 United States Congress take adequate steps
20 in developing a new pricing formula to price
21 raw milk.

1 Thank you, sir.

2 THE JUDGE: Mr. Tewksbury, you also
3 have attached to your statement an exhibit.
4 Would you just tell us generally what that is
5 --

6 THE WITNESS: Yes, that is --

7 THE JUDGE: -- and where it came
8 from.

9 THE WITNESS: Thank you, sir. That
10 is a price announcement that was sent out by
11 the Pennsylvania Milk Marketing Board which
12 has marked an over-order premium of \$1.90.
13 And then there is a footnote halfway down the
14 page that illustrates that 35 cents of that
15 \$1.90 is to compensate dairy farmers for
16 accelerated hauling costs.

17 THE JUDGE: And then the last page of
18 that exhibit, you indicated before is the
19 list of organizations which have supported
20 your testimony here today?

21 THE WITNESS: Yes, sir.

1 THE JUDGE: Very well.

2 Further questions of this witness?

3 Ms. Deskins.

4 MS. DESKINS: Judge Davenport, I have
5 some questions.

6 EXAMINATION

7 BY MS. DESKINS

8 Q. Thank you for testifying, Mr.
9 Tewksbury. I just wanted to clarify
10 something. You said that you are the
11 manager of the Progressive Agricultural
12 Organization?

13 A. Yes.

14 Q. How many members does that have?

15 A. We have signed up over 1,200 members
16 into the organization, mainly in about 30
17 some counties in Pennsylvania, some in New
18 York and a few New Jersey.

19 Q. Are they all dairy farmers?

20 A. No, 75 percent of them are dairy
21 farmers. And we also have business people

1 who have pledged their support behind us,
2 also.

3 Q. And how long has this organization
4 been around?

5 A. We started in February, 1991.

6 Q. Now, also, you listed several other
7 organizations that are endorsing your
8 testimony?

9 A. Yes.

10 Q. I'm just going to go through this
11 list. Can you just give me an idea of how
12 big the organization is and then, also, how
13 many members would be dairy farmers? The
14 first one you listed is Farm Wives United?

15 A. Yes, Farm Wives United is in New
16 York State. And I can't really tell you how
17 many members they have, ma'am, but I do know
18 that the ones we have worked with have all
19 represented dairy farmers, and they have
20 been at hearings that we have had and
21 testified.

1 The American Raw Milk Producers
2 Association would be all dairy farmers.
3 Again, I don't have the number of the
4 organization.

5 The Family Farm Defenders would be
6 mainly dairy farmers.

7 The National Family Farm Coalition
8 is made up of about 33 or 34 different
9 organizations across United States. A lot of
10 them are dairy farmers, but not all of them
11 are dairy farmers.

12 South Auburn Grange is a mixture of
13 probably about 150 different people, dairy
14 farmers, interested consumers that have gone
15 with us to Washington to march and everything
16 else because they don't think the dairy
17 farmers are getting a fair shake.

18 Q. Okay. And then, also, you said you
19 are opposed to the make allowance because it
20 is going to increase the cost to farmers.
21 Can you think of any proposal for make

1 allowance that would not increase the cost to
2 farmers, any changes that could be proposed
3 that wouldn't cause --

4 A. Well, let me say this. I was one of
5 the people, for whatever reason, that was not
6 aware the hearing was being held until the
7 middle of last week. We finally got all the
8 proposals off from the Internet and we had
9 some time to go over them, but the ones that
10 I read and went over, most of the -- most of
11 the time was by Agri-Mark. And I don't know
12 if there are other proposals that would raise
13 the make allowance without hurting our dairy
14 farmers or not. But I know one thing, that
15 our dairy farmers just cannot continue to
16 see their cost of hauling milk continue to
17 accelerate. And if this make allowance is
18 geared to lower the Class III and IV prices,
19 that certainly is going to have an adverse
20 effect upon the dairy farmers' prices.

21 And I read in some of the proposals

1 where that was. I even read some place, in
2 Agri-Mark, I think, where it was stated that
3 things have been happening as -- as --
4 unduly enhance the Class III price. If
5 that's true, why, that means that -- I guess
6 they think the price should be lower, and
7 that would have an adverse effect our upon
8 our dairy farmers.

9 I mean, I have been around a lot in
10 co-ops and everything. I know the problems
11 in marketing. I know there are problems.
12 But we have just got to come down to
13 something different than thinking we can,
14 I'm going to use the word thinking we can
15 take the money away from the dairy farmers
16 to solve the problem.

17 Q. And another question for you. On
18 Faithopity Farms, are you a part of that
19 farm?

20 A. I'm a consultant with the farm.

21 Q. And do you have your own separate

1 operation?

2 A. I have some animals there, yes.

3 Q. Okay. And don't give away any
4 trades secrets, but approximately how many
5 cows do you own?

6 A. Of my own, I have between 25 and 30
7 animals left.

8 Q. But you are still a separate
9 business? You're just --

10 A. Yes. I'm just there with them on
11 that basis.

12 Q. And then, also, just in terms of
13 this table that you have attached, you got
14 this from the Commonwealth of Pennsylvania
15 Milk Marketing Board?

16 A. Yes, ma'am.

17 Q. Okay. And did you get this from
18 their web page?

19 A. It was sent to me directly by the
20 marketing board officials.

21 Q. And is it accurate, to the best of

1 your knowledge?

2 A. It always has been.

3 Q. Thank you. I have no further
4 questions, but I do believe Mr. Rower might
5 have some questions for you. Thank you.

6 EXAMINATION

7 BY MR. ROWER:

8 Q. Good morning, Mr. Tewksbury.

9 A. Good morning, sir.

10 Q. My question concerns the size of
11 your dairy farm. We are required by law to
12 consider whether there are implications in
13 our rule-making process that would indicate
14 to us whether or not what we do has an
15 impact on small businesses, large businesses.
16 To get an idea of that, we need to ask
17 whether your dairy farm produces 500,000
18 pounds of milk per month, your 25 cows?

19 A. No, I do not.

20 Q. You do not. And your revenue is, on
21 an annual basis, below \$750,000; is that

1 correct?

2 A. A little bit below it, yes.

3 Q. Okay. I would guess so. We just
4 need to get a benchmark, and I appreciate
5 that.

6 A. I understand. I understand.

7 Q. The farm your family operates,
8 though, produces significantly more than
9 that.

10 A. Yes.

11 Q. And do they produce more than
12 500,000 pounds a month?

13 A. They are right in that neighborhood.
14 The unique part of that operation is, okay,
15 it becomes -- is that there are four -- four
16 owners there directly. They consolidated
17 everything together and put it under one --

18 Q. Operation.

19 A. -- one name. This way, they can cut
20 down on use of machinery, help and
21 everything.

1 So while grouped together, it looks
2 like it's way up there. Yet, when you bring
3 it down and realize it's four owners in
4 there with their families, then it's not
5 near as large as it appears. But, yes, that
6 much milk is produced, yes.

7 Q. Thank you very much.

8 A. Yes.

9 Q. I don't have any other questions.

10 THE JUDGE: Other questions? Mr.
11 Miltner.

12 EXAMINATION

13 BY MR. MILTNER:

14 Q. Mr. Tewksbury, thank you for --

15 THE JUDGE: Identify yourself,
16 please, Mr. Milton.

17 MR. MILTNER: Ryan Miltner, and I
18 represent Select Milk Producers, Continental
19 Dairy Products Cooperatives. We oppose the
20 changes in the make allowances.

21 BY MR. MILTNER:

1 Q. I want to thank you for coming to
2 testify today, Mr. Tewksbury. Mr. Tewksbury,
3 I didn't recall seeing you at the hearing
4 yesterday. Were you here for any of the
5 hearing?

6 A. No, I was not. At least two of our
7 people, three of our people, milked cows
8 last night. And I started 9 o'clock last
9 night picking them up and went around the
10 circle in northeastern Pennsylvania and got
11 down here at 5:30 this morning. These people
12 have not had any sleep, along with myself. I
13 have done that before, but these people have
14 walked away from their farms during the
15 night. We went through snowstorms and
16 windstorms to get here. And unfortunately,
17 we're going to leave town as soon as we can
18 because there's some bad weather forecast up
19 in our area again.

20 Q. Okay.

21 A. But, no. That's a long way to get

1 around to answering your question but, no, I
2 was not here.

3 Q. And the reason I ask is because
4 there were some numbers presented yesterday,
5 and I can share those with you, and I want
6 to ask you some questions about them.

7 A. Okay.

8 Q. First, though, I did not see in your
9 statement that it says where your dairy farm
10 markets its milk. And if I missed that, I'm
11 sorry. But are you affiliated with a co-op?

12 A. Not at the present time. The milk
13 all I'm talking about is marketed through
14 Reddington Farms in Whitehouse, New Jersey.

15 Q. Is that milk pooled on a Federal
16 order?

17 A. Yes, it is.

18 Q. Federal Order 1?

19 A. Yes.

20 Q. Okay. The Market Administrator's
21 Office was kind enough to prepare some

1 analysis for us yesterday, and it was
2 admitted to the hearing in Exhibit 13 so
3 everyone else can refer to it. And on page
4 7 of that exhibit, in Federal Order 1, they
5 estimated that under the various scenarios
6 that are in the hearing notice, that I
7 assume you -- you have had a chance to look
8 at the hearing notice?

9 A. Yes.

10 Q. Even short notice as it was?

11 A. Yes.

12 Q. And they estimated that over the
13 past two years, if these new make allowances
14 were in place, the blend price for Order 1
15 would fall by between 26 and 45 cents a
16 hundredweight.

17 A. I understand that's the figures that
18 have been used, yes.

19 Q. Okay. For your dairy farm, what
20 does a loss of that magnitude mean?

21 A. Well, you know, not only -- okay,

1 you asked me about the 26 to 45. You put
2 that on the pounds of milk that you referred
3 to, it's a substantial loss to these --
4 especially to the Faithopity Farm because
5 that's their -- that's their sole purpose of
6 -- of income. It's going to be -- it's
7 going to be a real hardship to them.

8 And I understand that cheese prices
9 dropped in Chicago yesterday besides, which
10 just means our prices will be going down all
11 the more. So it will mean -- it's hard
12 enough for them now, and drops like that at
13 one time is pretty hard to swallow.

14 Q. Do you think it would affect the
15 ability of those four families to continue
16 dairy farming if we were looking at losses
17 of that magnitude?

18 A. I think that they would continue to
19 farm because they are the salt of the earth.
20 They have gone through a lot of hardships.

21 [Pause.]

1 Excuse me. Even to the point

2 where --

3 MS. DESKINS: Your Honor, could --

4 THE WITNESS: I'll be okay.

5 MS. DESKINS: You okay?

6 THE WITNESS: Yes -- to where one of
7 the owners suffered a severe stroke two years
8 ago at the age of 45, and he is practically
9 incapacitated. And that's why we are we are
10 trying to help out even more with them on
11 some of these problems. That's why we
12 represent them and try to negotiate premiums
13 or whatever we can do. And I don't know how
14 much more they can take when you take one of
15 the main -- when one of the main spark plugs
16 is taken out. And then any further decrease
17 in prices, it's going to be a hardship.

18 BY MR. MILTNER:

19 Q. And --

20 A. And I apologize for --

21 Q. You don't need to apologize.

1 The impact, the real impact of these
2 changes in make allowances, it has an impact
3 on your farm and, I assume, also the other
4 dairy farm members of Pro Ag and the other
5 groups that you have testified about?

6 A. Yes. That's why they all have
7 endorsed our testimony today.

8 Q. I thank you again for driving down
9 in bad weather, and good luck to you. Thank
10 you.

11 A. Well, I'm accustomed to it, but I
12 hate to drag other people through the same
13 adversity. They wanted to come, and we went.

14 THE JUDGE: Other questions?

15 Thank you, Mr. Tewksbury.

16 THE WITNESS: Thank you.

17 THE JUDGE: You may step down.

18 Exhibit 30, unless there is an objection,
19 will be admitted into evidence at this time.

20 [Whereupon, Exhibit No. 30 was
21 received in evidence.]

1 THE JUDGE: Ms. Hall. Do you also a
2 have a statement?

3 THE WITNESS: Yes, I do.

4 THE JUDGE: In other words, can you
5 give me a copy and copies to the hearing
6 reporter. I need one, and she needs four.
7 And Ms. Deskins will help you pass the
8 others out.

9 Whereupon,

10 DONNA HALL,
11 having been first sworn by the judge, was
12 examined and testified under oath as
13 follows.

14 THE JUDGE: Give us your name,
15 please.

16 THE WITNESS: My name is Donna Hall,
17 H-A-L-L.

18 [Whereupon, Exhibit No. 31 was
19 marked for identification by the judge.]

20 THE JUDGE: Very well, Ms. Hall, I
21 have marked your statement as Exhibit 31.

1 Are you prepared to read it into the record
2 at this time?

3 THE WITNESS: Yes, I am, Your Honor.

4 THE JUDGE: Please do so.

5 THE WITNESS: Your Honor, thank you
6 for the opportunity to speak here today.

7 STATEMENT FOR THE RECORD OF DONNA HALL

8 A. My name is Donna Hall. Our family
9 operates a dairy farm business in Lycoming
10 County, Pennsylvania. I am speaking today
11 as a dairy farmer and as a member of
12 Progressive Agriculture Organization (Pro
13 Ag), Pennsylvania Farmers Union (PFU), and
14 National Family Farm Coalition's Dairy
15 Subcommittee (NFFC). With the support of Pro
16 Ag, Pennsylvania Farmers Union, and NFFC, I
17 am speaking to oppose the Agri-Mark proposal
18 to increase the make allowance.

19 This is the third time I have written
20 my testimony. The first time I ripped it up
21 because I didn't have enough facts. The

1 second time I ripped it up because I had too
2 many facts. So this time it's simply from my
3 heart. I don't need 10 pages of facts that
4 could be right or wrong, interpreted,
5 misinterpreted, or skewed to suit whomever.

6 After over 40 years of dairy farming
7 and always being required to be ever more
8 efficient in order to survive, my husband,
9 Eugene, and I have no one who wants to
10 continue dairy farming. Our family is
11 typical of thousands who love our way of life
12 but are disappearing. Why?

13 Today we may have only about 60,000
14 dairy farm businesses left in the whole
15 United States, and we're losing about 5,000 a
16 year. Why? Could it be because tired
17 farmers are also just plain tired of taking
18 whatever is doled out to us for our raw
19 products and paying out whatever is asked for
20 whatever we need to stay in business

21 It is long past time for a change.

1 Farmers need to receive what they rightfully
2 deserve, which is a cost of production and
3 some profit. Fairness.

4 What recourse do farmers have when
5 all of our costs go up and our incomes go
6 down? We can't get it out of the
7 marketplace, like co-ops should be doing.

8 If we try to produce more to increase
9 our incomes, we get paid less for our milk.
10 We can't seem to win.

11 If you can, tell me, how will our
12 dairy farmers survive?

13 As one of the interested parties who
14 I believe should have been properly notified
15 about this hearing and given ample time to
16 prepare our testimonies, I am again asking
17 you to turn down the petitioners' request.
18 This would require to petitioners to also
19 become ever more efficient and use their
20 powers to get their profits from the
21 marketplace.

1 When considering all the petitions
2 and testimonies presented, I'm asking you to
3 please think dairy farmer instead of just
4 Agri-Mark, Land O'Lakes, IDFAs and so forth
5 whenever increased costs and lower incomes
6 are mentioned.

7 The farmers' money well is going dry.
8 Besides, without farmers, what will we need
9 co-ops for?

10 Oh, by the way, is Agri-Mark even a
11 co-op? Or is it Agri-Mark a Delaware
12 corporation? What effect will California's
13 response to an increase have? Will the
14 petitioner simply return for another make
15 allowance?

16 We need a different pricing system.
17 How about 608c(18)? The Agricultural
18 Marketing Agreement Act of 1937 clearly
19 intended for our nation's farmers to be
20 protected and consumers to have a safe,
21 secure and adequate food supply, not unsafe,

1 illegal MPC and so forth.

2 Will all continue as is at our peril?

3 I repeat, any nation that cannot feed itself
4 is not free.

5 Thank you all for your time and
6 consideration. Thank you, Your Honor.

7 THE JUDGE: Do we have questions of
8 this witness? Ms. Deskins.

9 EXAMINATION

10 BY MS. DESKINS

11 Q. Good morning. My name is Sharlene
12 Deskins. I'm with the USDA Office of General
13 Counsel, and I have a couple questions for
14 you.

15 A. Okay.

16 Q. I just want to get an idea, where in
17 Pennsylvania is Lycoming County?

18 A. It's located in the central part of
19 Pennsylvania. Williamsport, Pennsylvania, do
20 any of you know Williamsport?

21 Q. Uh-huh.

1 And also, you talked in your
2 statement about farmers need to seek what
3 they rightfully deserve, which is a cost of
4 production and some profit?

5 A. Yes.

6 Q. How would the proposed change in the
7 make allowance, do you believe, affect your
8 cost of production?

9 A. Well, it seems to be that they are
10 trying to cover their production, their costs
11 and their profit loss at our expense. That's
12 the way I interrupt everything that I have
13 read. I am no expert, as everybody else is
14 here, maybe. I'm just a simple dairy farmer
15 that understands that we are not getting it,
16 somebody else is.

17 Q. I'm just trying to understand. How
18 do you think this is going to impact your
19 cost of production? Is it going to increase
20 it, decrease it? What do you think?

21 A. It is going to be taking out of our

1 profit because if this goes through, as I
2 understand it, it won't simply affect Class
3 II and III, or Class III and IV, rather, but
4 I think it will have an impact on I and II,
5 also.

6 And I think there is going to an
7 impact, also, because California, well, how
8 are they going to respond? Is that going to
9 effect a further call for a make allowances
10 in the future?

11 We have to do something different.
12 This isn't working for us. It is not working
13 for us, and perhaps it's not working for you,
14 either, if you can't get your profit.

15 But right now, I'll tell you what.
16 What really makes me angry is when I see
17 Wal-Mart telling Land O'Lakes or someone
18 else, we don't want your butter, we don't
19 want your butter because you don't meet our
20 price. We have got to change this system so
21 the money gets back to the farmers and you

1 guys can do a decent job at processing and
2 providing it to the consumer. But we have to
3 work together. It's not just us or you, it's
4 everything that needs to be changed and
5 fixed. This isn't working. This is not
6 working.

7 Q. I noticed on here, you are a member
8 of some of the same organizations as Mr.
9 Tewksbury?

10 A. I sure am.

11 Q. Do you have any idea what the size
12 of Pennsylvania Farmers Union is?

13 A. Right now I do not. But I will tell
14 you one thing. We speak for our farmers.
15 And most of our members are farmers, unlike
16 one of the biggest farm organizations in the
17 country, which I also did work for before,
18 legislatively and in policy development. So
19 we are sincere, no matter what the size. And
20 we are speaking for our farmers.

21 And I am on National Family Farm

1 Coalition's Dairy Subcommittee. We have
2 telephone conference calls a couple times a
3 month, at least. We work on dairy issues.
4 And this is hard for us because we take the
5 time away from our dairies to do this work
6 because we care enough about what's happening
7 to our dairy farmers in this country. We
8 are disappearing.

9 It used to be, in '97, I think there
10 was enough, maybe, to fill Penn State's
11 Beaver Stadium. Now we are down to 60,000,
12 maybe. This is disastrous.

13 And if you guys think that you can do
14 without us or you can get your milk some
15 place else, you'd better think again. Even
16 Mexican immigrants, their kids do not want to
17 farm. It's already been stated, they don't
18 want to farm. Why? Why put up with what we
19 have to put up with?

20 You know, I had -- the day I was
21 trying to get my testimony around with short

1 notice, I had to call the vet. I had to get
2 up in the morning and call the vet. We had a
3 cow that had a twisted stomach. We had to
4 have her operated on. And it was her first
5 calf effort. Valuable animal. Then we had
6 another cow that calved and didn't clean, and
7 we have -- right now she may not make it.
8 But anyway, I have a vet expense there.

9 And then I had to go and I had to
10 get my testimony around. I almost didn't
11 come. And somebody says, no, you have got
12 to go, just go and tell it, tell it like it
13 is. So that's why I'm here, telling you
14 guys like it is. We need this change
15 because you can't get along without us. If
16 you don't have our milk, you can't do
17 anything, either. So we both have to -- we
18 have to work together and make changes.
19 This is not working.

20 Q. And do you think there is any change
21 that could be made where you could --- that

1 you would be comfortable with?

2 A. Sure, there are changes to be made,
3 but I -- I cannot give you those changes
4 because I -- I know smarter men than me that
5 we work with, if they could have been here
6 today, which they couldn't, they had other
7 engagements, they could have given you the
8 answer just like. That there are proposals,
9 there are things that we have studied at the
10 National Family Farm Coalition and Pro Ag and
11 Farmers Union. We have studied these things.
12 There are different avenues to take. There
13 are different solutions. But I can't give
14 you the answers today.

15 I am a simple dairy farmer speaking
16 from my heart without facts, without figures,
17 whatever.

18 Q. Mrs. Hall, I think this is going to
19 be my last question. I noticed on here you
20 said you didn't have ample notice of this
21 hearing --

1 A. No, I did not.

2 Q. -- and not enough time to prepare?

3 A. No.

4 Q. Is there any information that --
5 they have something called "official notice."
6 Is there any information that you would like
7 the court to take notice of? If you could
8 give us, say, a web page or a book, we could
9 put that into the record if you didn't have a
10 chance to get to --

11 A. Well, I'll tell you what. As few
12 dairy farmers as there is today and with this
13 being of such importance to us, because it's
14 our survival, it is our survival, I think
15 that every dairy farmer should be notified,
16 every dairy farm business.

17 And we are businesses. We put back
18 into our communities. We are not just dairy
19 farmers, we are businesses. So I think
20 everyone should be notified before anything
21 like this. If they want to come, they can.

1 That's -- you know, we don't need a room
2 full of processors and people that use our
3 raw products here today, we need a room full
4 of farmers, also. We need more
5 representation, and we did not have ample
6 time.

7 I could have maybe done different,
8 but I know everybody else has facts and
9 figures; you didn't need my facts and
10 figures. And like I said, they can be
11 interpreted, misinterpreted. Figures can --
12 they can lay on paper and do whatever, you
13 know. So that's where I am today. I'm here
14 to tell you, we have to change things.

15 Q. Thank you. I don't have any further
16 questions.

17 A. Thank you.

18 THE JUDGE: Mr. Rower.

19 EXAMINATION

20 BY MR. ROWER:

21 Q. Good morning. I'm Jack Rower with

1 AMS Dairy Programs. Thank you for coming
2 this morning.

3 A. You are welcome.

4 Q. How large is your dairy farm?

5 A. We have just under 500 acres. We
6 have a little under 500 acres.

7 Q. How many cows do you milk?

8 A. How many cows? Right now I think we
9 are milking 68 head of cattle. And we do not
10 want to milk more.

11 Q. So your production is less than
12 500,000 pounds a month?

13 A. Oh, sure, it is. But here is the
14 point I want to make. In Pennsylvania, we
15 have thousands of dairy herds the size of
16 ours. We have very few large herds. And
17 this is one thing that makes Pennsylvania
18 unique. We also support a tourist industry.
19 I brought pictures to show some of the
20 people from National Family Farm Coalition
21 today. I have those pictures back there. I

1 can show you a picture of our farm. You
2 take these small family farms out of
3 Pennsylvania, and you are going to destroy
4 tourism because I don't care -- it's not
5 just Lancaster County, it's all over the
6 state of Pennsylvania.

7 If you want to see my farm, I'll
8 show you. But we are important because we
9 are thousands of farms instead of just some
10 farms in a small area that are into
11 pollution. If you get too many animals in
12 one spot, you have got problems. You draw
13 out of the groundwater. You can pollute the
14 groundwater. You can pollute there. You
15 have problems with odor. You have problems
16 with people.

17 With Pennsylvania's situation, where
18 our farms are dispersed, it is unique. And
19 we don't have a problem with disease as much
20 because they are out there, widespread. I
21 don't think that any program to help dairy

1 farmers like Pennsylvania is now proposing,
2 they have a -- our governor and our
3 Secretary of Ag, whom I know, Denny Wolf, is
4 proposing something to help our farmers to
5 become more efficient. And they may be
6 helping, like, I think, 17 or 20 a year.
7 What's that do for the other thousands?

8 So efficiency is not the end all and
9 be all. We can be so efficient. And that's
10 why I'm still here today. We have been
11 dairy farming, I think -- we started raising
12 our own calves and creating our own herd,
13 worked our own way up. We didn't get a farm
14 given to us. We did it the hard way, in
15 1963. We actually started milking in '65.
16 So we are still here. And if we weren't
17 efficient, we wouldn't be here.

18 But the fact is that we are hurting.
19 It is very hard to buy things like health
20 insurance and a lot of the other problems
21 that you guys have today. We don't have a

1 big retirement because we keep it invested.
2 And every dollar we have, the milk check
3 comes in, it goes to the bank. And where
4 does it go? It goes right back out to pay
5 all the bills.

6 So this is what you are also
7 destroying.

8 You are not just destroying, you know
9 what I mean, dairy farms, you are destroying
10 businesses that put back into their
11 communities. So we have to change what's
12 going on here today. We cannot have this
13 happen all the time.

14 Farmers -- like I said, the money
15 well is going dry. You are getting rid of
16 your sources. You are not going to -- you
17 are not just hurting us, you are going to be
18 hurting yourselves.

19 Q. Thank you very much.

20 A. Thank you.

21 THE JUDGE: Other questions? Yes,

1 sir. Mr. Yale.

2 EXAMINATION

3 BY MR. YALE:

4 Q. Good morning. Ben Yale on behalf of
5 Select Milk and the Continental Dairy
6 Products and Dairy Producers of New Mexico.
7 Again, I want to thank you for coming. I
8 know the sacrifices you guys make to do
9 this.

10 Let me see if I can -- I would
11 assume, in your role in the family
12 operations, that you handle the checkbook?

13 A. Sure do.

14 Q. And I'll bet you can tell me pretty
15 quick what 10 cents a hundredweight does for
16 you one way or the other. Am I right?

17 A. Well, it sometimes makes a
18 difference whether you can pay a bill or not,
19 I can tell you that.

20 Q. And with 25 cents a hundredweight
21 change in your price on the negative, can you

1 kind of describe to us what kind of impact
2 that would have and the changes you would
3 have to make in your operation?

4 A. Well, I might have to turn out the
5 lights. My light bill is a thousand dollars
6 a month.

7 Q. Do you have any paid labor on your
8 farm?

9 A. We have a family operation. We work
10 the farm together. And as I stated, I don't
11 think our children are interested at all in
12 continuing.

13 Q. But with the 25 cents, there is no
14 -- it just comes out of your own pay,
15 there's -- there are no employees?

16 A. No, it comes out of our pay. That
17 is right.

18 Q. And if the price drops 25 cents, are
19 there any savings that come to you on the
20 other end? I mean, do the feed prices drop
21 or the vet prices drop or anything like

1 that?

2 A. I wish they would.

3 Q. That's all I have. Thank you.

4 THE JUDGE: Other questions of this
5 witness? Thank you, Ms. Hall. You may step
6 down.

7 MR. ROWER: Judge Davenport, one
8 last question.

9 THE JUDGE: I'm sorry.

10 THE WITNESS: Sure.

11 EXAMINATION

12 BY MR. ROWER:

13 Q. Could you tell me where your milk is
14 pooled, ma'am?

15 A. Well, I think it's on Order 2. Am I
16 right, Arden?

17 Q. On the Northeast Order?

18 A. Yes, Northeast Order.

19 Q. And are you a member of a
20 cooperative?

21 A. No, and I would like to tell you a

1 little about that.

2 Q. Thank you.

3 A. I have had a distrust of co-ops for
4 many, many years. I had two unfortunate
5 circumstances, which I got out of. And until
6 recently, we were shipping milk
7 independently to Farmland, which was
8 Parmalat that went bankrupt. We stuck with
9 Parmalat that went bankrupt because we felt
10 it was important to keep independent
11 producers. So we stuck with them. Then they
12 reverted back to Farmland because of the
13 financial arrangement that the bankruptcy
14 court had.

15 So right now we are shipping to
16 Farmland. But last summer, we turned over
17 400 -- over 400 independent dairy businesses
18 were turned over to DMS, which is an arm of
19 DFA, without our knowledge or consent. We
20 received a letter in the middle of the
21 month, around the 15th, I believe. And it

1 stated that as of the first of the month,
2 now, we were with DMS. Now, I don't think
3 that that's right, and I have spoken my mind
4 about that.

5 So right now, we are with DMS. I
6 never signed a contract with them, and I will
7 not sign a contract with them. And they
8 better not try to force me into DFA.

9 So I do not like what is currently
10 happening with DFA. There is a federal
11 antitrust suit against them with, I think, 18
12 to 20 or more states investigating. And
13 personally, I hope they are broken up. I
14 think we need to change that situation, too,
15 because our dairy co-ops have become too
16 large. They are not working for the members.
17 That's us.

18 I have had members go to their
19 meetings, different co-op meetings, and ask
20 what their salaries were because we had
21 mentioned that maybe we should tie the milk

1 price to the CEOs' or the board members'
2 salaries. Maybe that would work. Maybe we'd
3 end up with more money that way. And they
4 very flatly told the member that asked that
5 it was none of her business.

6 So I do not think that the co-ops
7 are doing their job. They are too large.
8 They are more like corporations. They should
9 have to disclose more information to their
10 members. There should be more openness. And
11 like I said, I hope that this does happen and
12 they are broken up. I hope that something
13 is changed. We need to get control back into
14 the hands of the farmers for the benefit of
15 the farmers and then work with whoever
16 markets our milk.

17 Q. Thank you very much. Thank you for
18 coming. I appreciate it.

19 A. You're welcome.

20 EXAMINATION

21 BY MS. DESKINS:

1 Q. I just want to clarify one thing.
2 You used an acronym, DMS. Can you say what
3 that stands for?

4 THE JUDGE: DMS.

5 THE WITNESS: Dairy Marketing
6 Service. And you want to hear another one?
7 I never have any problems much, I only had a
8 problem or two with Farmland or Parmalot all
9 the time I shipped out there, all those
10 years. Since DMS took over, I have had
11 problems every month, every month. I have
12 called and I have gotten them taken care of.
13 I have also called our Pennsylvania Milk
14 Marketing Board, okay? There was also other
15 farmers that received the same butterfat, all
16 of us received 3.43.

17 Now, here is 3.43 down the line
18 here. Now, how does it get in a computer at
19 3.43 here and all of us like this? Between
20 303087 and 303500, there was multiple
21 problems with our butterfats. And some of

1 these butterfats were all on farmers' trucks
2 that happened to be making a noise against
3 DMS, okay?

4 Now, I'm not saying that it happened
5 on purpose, but how does this happen when the
6 butterfats are all this 3.43 or 3.65 and then
7 the protein and the other components are
8 different? So I complained to our milk
9 marketing board, okay? So I have received
10 other problems every month since we have
11 been with them. You call that efficiency? I
12 don't. I don't call it efficient to have
13 mistakes. And I don't call it efficient for
14 some of the things that's happening, okay?

15 I don't want to go into any more
16 detail. I could tell you what happened this
17 month, but I'm keeping this to myself.

18 Q. Thank you.

19 A. You are welcome.

20 THE JUDGE: Other questions?

21 Thank you, Ms. Hall.

1 THE WITNESS: Thank you.

2 THE JUDGE: May I hear from Mr.

3 Carlin?

4 Whereupon,

5 GERALD CARLIN,

6 having been first sworn by the judge, was

7 examined and testified under oath as

8 follows.

9 THE JUDGE: Tell us your name and

10 spell your last name for the hearing

11 reporter.

12 THE WITNESS: Gerald Carlin,

13 C-A-R-L-I-N.

14 [Whereupon, Exhibit 32 was marked

15 for identification by the judge.]

16 THE JUDGE: Mr. Carlin, I have marked

17 your statement as Exhibit 32. Are you

18 prepared to read it into the record at this

19 time?

20 THE WITNESS: Yes.

21 THE JUDGE: Please do so.

1 STATEMENT FOR THE RECORD OF GERALD CARLIN

2 THE WITNESS: Thank you, Your Honor,
3 for the opportunity to speak today. My name
4 is Gerald Carlin. My wife, children and I
5 own and operate a 60-cow dairy farm in
6 Susquehanna County, Pennsylvania.

7 The outcome of this hearing will
8 have a direct impact on my business and on
9 every dairy farms in the Federal orders. My
10 farm is already struggling to make ends meet.
11 Like the processors, I have increased health
12 insurance costs as well as increased fuel and
13 energy costs. In addition, fertilizer and
14 steel costs have skyrocketed. Also, there
15 have been increases in property taxes, farm
16 insurance, vet costs, animal medicines and
17 more.

18 In spite of added cost, farm milk
19 prices, averaged out over the past 25 years,
20 have remained basically flat. It is,
21 therefore, deeply disturbing that Agri-Mark

1 has petitioned USDA for higher make
2 allowances, which would reduce milk price to
3 dairy farmers who are already struggling

4 According to the analysis of Dr.
5 Kenneth Bailey, Penn State University, the
6 expected increases in the make allowances
7 could reduce farm gate prices by 25 to 46
8 cents per hundredweight. On my relatively
9 small dairy farm, this would mean a
10 reduction of \$3,000 to \$5,500 a year in milk
11 income per year. This certainly makes me an
12 interested party. The average dairy farm in
13 the United States could lose \$6,500 to
14 \$12,000 a year, which makes every dairy
15 farmer in the Federal orders an interested
16 party, and every one of them should have
17 been notified about this hearing.

18 Any increases in processor costs
19 should be passed on to their customers.

20 Retail dairy product prices are at 183
21 percent of the 1982 to '84 baseline

1 according to "Dairy Market News." There is
2 room in these prices to absorb added
3 processor costs. To put these costs on the
4 backs of dairy farmers who have no way to
5 pass them on is immoral and deeply offensive.

6 Let me say that I am not opposed to
7 dairy processors making a fair profit.

8 However, I will note that Agri-Mark and
9 Upstate Dairy Cooperatives, Incorporated,
10 plaintiffs in the St. Albans Cooperative
11 Creamery, Incorporated, et al., Plaintiffs,
12 vs. Dan Glickman, Secretary of Agriculture,
13 Defendant, case withdrew their case after
14 USDA adopted Option 1A.

15 U.S. District Judge William Sessions,
16 III had cited Dan Glickman for failure to
17 consider dairy farmers' cost of production
18 in the milk marketing formula. Judge
19 Sessions made clear in his opinion and order
20 that "this court looks to the direct
21 language of the statute to determine the

1 sufficiency of the Secretary's consideration,
2 which makes no mention of indirect
3 consideration being adequate in meeting the
4 requirements of 608c(18). The record shows
5 no direct consideration of regional costs in
6 feed, feed availability, or other region
7 specific economic factors." Judge Sessions
8 also noted that "the court finds the
9 Secretary's Final Order and Decision
10 violates Congress's mandate under the 1937
11 Agriculture Marketing Agreement Act (AMAA).

12 The fact that co-ops, including
13 Agri-Mark and Upstate Farms dropped this case
14 without resolution of the cost production
15 issue strongly indicated to me their lack of
16 concern for their membership's getting paid
17 cost of production. It also shows a
18 disregard for the Capper-Volstead Act, which
19 established a co-op's right and
20 responsibility to fight for fair farm milk
21 prices for their membership.

1 In December 2000, USDA released a
2 Tentative Decision on Proposed Amendments
3 for Class III and IV Pricing. Once again,
4 USDA ignored the mandates of 7 U.S.C.
5 608c(18), maintaining that Class III and IV
6 prices "are such prices as will reflect the
7 aforesaid factors" [General Findings (b)].
8 This is nonsense. Of course, the co-ops
9 block voted the referendum through. In light
10 of these past actions, I think that it is
11 obvious where the petitioners' real
12 interests are. It goes against economic
13 fairness to pass increased operating costs
14 backward to the supplier. All through our
15 economy, increased costs are passed on to the
16 customers. Passing costs on seemed to work
17 before Order reform and should work again.
18 Passing costs backward will cause undue
19 economic hardship to the very farmers on whom
20 processors rely and make fresh local milk
21 even scarcer.

1 Furthermore, the current system
2 affords additional benefits to processors who
3 use imported dairy ingredients to increase
4 yield since they are paid a make allowance on
5 end product. It seems that this will also
6 render USDA milk production figures
7 exaggerated and unreliable.

8 Before any action is taken on make
9 allowances, USDA must abide by 7 U.S.C.
10 608c(18) "to assure a level of income
11 adequate to maintain productive capacity
12 sufficient to meet anticipated future needs,
13 and be in the public interest." A drive
14 around rural America certainly reveals that
15 the current economic plan for agriculture has
16 brought once proud and beautiful farms into
17 disrepair and is causing farm kids to turn
18 their backs on farming.

19 Dairy farmers don't need gimmicks.
20 We need fair prices. USDA already has the
21 data on total economic costs for dairy

1 farmers. Now they need to act. Cost of
2 production for dairy farmers is not a just
3 good idea, it is the law.

4 I added a few notes at the end. Like
5 everybody, the other farmers here, I didn't
6 have much time to work on it. And my
7 business is really tying me down all during
8 the day from 4:00 or 6:00 in the morning
9 until 8:30 or 9:00 at night. I worked on it
10 afterwards. And anyway, I added this on at
11 the end.

12 THE JUDGE: The appendix is, in other
13 words, just a footnote --

14 THE WITNESS: Just an add-on because
15 it was put on after we copied the other
16 testimony.

17 THE JUDGE: And you have also
18 included a chart which reflects the
19 cheese-related indices. Can you tell me
20 where that came from?

21 THE WITNESS: Well, the source is the

1 Bureau of Labor Statistics. John Bunting put
2 it in a graph form. And what that does is
3 show dairy farm price.

4 I assume it's the price per pound
5 that cheese processors make.

6 THE JUDGE: The upper axis is the
7 price, the other is the year?

8 THE WITNESS: Yes.

9 THE JUDGE: And you have included,
10 also, the next page is an extract from the
11 statute?

12 THE WITNESS: Yes, that is the
13 Section 608c(18).

14 THE JUDGE: And then the last page
15 appears to be something from "Dairy Market
16 News" from December 26th through 30th.

17 THE WITNESS: Yes. And that gives
18 the dairy product prices --

19 THE JUDGE: And did you --

20 THE WITNESS: -- percentages compared
21 to the 1982 to '84 baseline.

1 THE JUDGE: Did you extract that from
2 the "Federal Dairy Market News"?

3 THE WITNESS: Yes, this is a direct
4 copy from that.

5 THE JUDGE: Questions of this
6 witness?

7 EXAMINATION

8 BY MS. DESKINS:

9 Q. Good morning, Mr. Carlin. My name
10 is Sharlene Deskins. I'm an attorney with
11 the USDA Office of General Counsel.

12 You mentioned a report from a person
13 named Kenneth Bailey?

14 A. Yes.

15 Q. Can you give us, if you know, what
16 the full name of the report is?

17 A. I think it's something to the fact
18 that "USDA to Hold Hearings on Make
19 Allowances," was the name of the report. It
20 was just published. I think I got a hold of
21 it a week ago. It's been within the last

1 couple of weeks it was published.

2 Q. Do you know where it was published?

3 A. It was published online, I assume.

4 Q. Do you have a web page for it?

5 A. No, I don't have that with me.

6 Q. And you said the man's name was
7 Kenneth Bailey. Could you spell that for
8 the record?

9 THE JUDGE: It's in the statement,
10 Ms. Deskins.

11 MS. DESKINS: We don't have a copy of
12 the statement.

13 THE JUDGE: I'm sorry. It's Dr.
14 Kenneth, K-E-N-N-E-T-H, Bailey, B-A-I-L-E-Y,
15 Penn State University.

16 THE WITNESS: It's in the testimony.

17 MS. DESKINS: We don't have a copy of
18 that. There's only copies enough for the
19 judge and the court reporter.

20 THE WITNESS: Oh.

21 MS. DESKINS: I don't have any other

1 questions.

2 THE JUDGE: Very well. Other
3 questions? Mr. Miltner.

4 EXAMINATION

5 BY MR. MILTNER

6 Q. Ryan Miltner on behalf of
7 Continental Dairy Products and Select Milk
8 Producers.

9 Mr. Carlin, thanks again for coming
10 up to offer your testimony today. You -- in
11 your statement you said that there was lost
12 income for dairy farmers of about \$3,000 a
13 year, and I didn't hear the full amount. Can
14 you just let me know what that number was?

15 A. \$3,000 to \$5,500 based on just over
16 1.2 million pounds.

17 Q. Okay. And you have approximately 60
18 cows on your dairy?

19 A. Right.

20 Q. What does a loss of that magnitude
21 mean to your dairy and your family?

1 A. Well, it means a lot of worn-out
2 equipment continues to be worn out and
3 dangerous and not being able to update like I
4 should and, of course, the additional stress
5 of maybe getting further behind on bills or
6 something like that.

7 Q. When you say getting further behind,
8 do you mean that there would be bills that
9 you would either not be able to pay or you
10 would have to delay payment?

11 A. Delay payment.

12 Q. Okay. And eventually, would that
13 mean that you would reach a point where there
14 would be bills that would be severely
15 overdue?

16 A. Well, unlike the federal government,
17 I can't keep running up the tally, yes.

18 Q. You are not issuing bonds or
19 anything like that?

20 A. No.

21 Q. I want to talk a little bit about

1 your energy costs on the farm. You said that
2 energy that you have to pay to keep your
3 operation going, those prices have increased.
4 Do you have any idea off the top of your head
5 how your electric or natural gas or propane
6 bills compare this year compared to a couple
7 years ago?

8 A. Electric is a little higher. I'm
9 going to guess in the 10 to 15 percent range
10 higher than a few years ago. Propane and
11 natural gas is not much of an issue for me.
12 I do heat entirely with wood, the household,
13 and the barn is all electric. So I do use
14 very little propane or natural gas.

15 Q. Okay.

16 A. Of course, that does affect
17 fertilizer prices a lot, though, propane and
18 natural gas.

19 Q. How do your fertilizer prices
20 compare?

21 A. About 25 percent higher than two

1 years ago, at least.

2 Q. Do you purchase diesel fuel for your
3 operation for crops or anything?

4 A. Yes.

5 Q. How do your diesel prices compare?

6 A. I believe they're up about -- about
7 double what they were four years ago,
8 probably 80 percent higher than they were two
9 years ago.

10 Q. And those energy costs are all
11 additional costs to your operation that you
12 didn't have a couple years ago?

13 A. Right.

14 MR. MILTNER: I don't have anything
15 further, Your Honor, although I think I may
16 have a site to Dr. Bailey's report, and if we
17 could check with Mr. Carlin and maybe offer
18 that into the record, maybe not in the next
19 few minutes here, but after the break.

20 THE JUDGE: Very well.

21 MEMBER OF THE AUDIENCE: Your Honor,

1 I have one copy of Dr. Bailey's report, if
2 that would be helpful.

3 MR. MILTNER: Maybe we can confer,
4 Judge.

5 THE JUDGE: See if we can possibly
6 get some copies made.

7 [Whereupon, counsel conferred.]

8 MR. MILTNER: Well, we'll offer it
9 and let the judge decide.

10 THE JUDGE: Mr. Vetne.

11 MR. VETNE: John Vetne, counsel for
12 Agri-Mark. I don't have any problem with
13 providing for the record the web page
14 citation to Ken Bailey's report. I have it
15 on speed dial, or the equivalent, of my
16 computer. But I do have a problem with the
17 contents of that report, those reports, which
18 are varied, and any analysis or fact being
19 incorporated in the record without being able
20 to examine Dr. Bailey. He has useful
21 analysis that somebody might be able to look

1 at and incorporate in their own thoughts, but
2 as far as his facts and his methodology, his
3 data, that is not part of the record now.
4 Providing the Internet site doesn't make it
5 part of the record, and I hope that there is
6 no implication that it will.

7 THE JUDGE: Your objection will be
8 noted.

9 Other questions of this witness?

10 Thank you, Mr. Carlin. You may step
11 down.

12 Ms. or Mrs. Cochran.

13 MR. RASTGOUFARD: Before we proceed
14 with the next witness, I don't think Exhibit
15 31 or 32 have been entered into the record.

16 THE JUDGE: I did admit 31. However,
17 32 should be admitted at this time.

18 MR. RASTGOUFARD: Thank you.

19 [Whereupon, Exhibit No. 32 was
20 received in evidence.]

21 THE JUDGE: Ms. Cochran's statement

1 will be marked as Exhibit 33.

2 [Whereupon, Exhibit No. 33 was
3 marked for identification by the judge.]

4 Whereupon,

5 BRENDA COCHRAN,
6 having been first sworn by the judge, was
7 examined and testified under oath as
8 follows.

9 THE JUDGE: Please be seated. Would
10 tell us your name and spell your last name
11 for the hearing reporter.

12 THE WITNESS: My name is Brenda
13 Cochran, C-O-C-H-R-A-N.

14 THE JUDGE: Very well. Ms. Cochran,
15 you have prepared a statement which I have
16 marked as Exhibit 33. Are you prepared to
17 read it into the record at this time?

18 THE WITNESS: I am, Your Honor.

19 THE JUDGE: Very well, why don't you
20 do so.

21 THE WITNESS: My name is Brenda

1 Cochran. My husband and our children own and
2 operate a 200-cow dairy farm in Tioga County,
3 Pennsylvania. I am here today to speak on
4 behalf of my own family and on behalf of the
5 multiple thousands of American dairy farming
6 families who, even now, know nothing at all
7 about this hearing because we farmers who
8 will be so adversely affected by Agri-Mark's
9 proposed increase in dairy processors' make
10 allowances were not considered worthy for
11 notification as interested parties. This
12 preposterous fact alone is outrageous but
13 its atrocity pales in comparison to the
14 infuriating position taken by the named
15 parties advancing this proposed reduction in
16 dairy farmers' milk checks.

17 It is middleman dairy processors who
18 are boldly advancing such a nefarious scheme
19 that assumes we farmers, who produce the raw
20 milk they need for the operation of their
21 plants, somehow owe them money from our

1 hard-earned milk checks to cover their
2 bottom lines. Why are these dairy product
3 manufacturers not securing their cost
4 increases from their customers who buy their
5 finished dairy products? What is more
6 shocking, however, is the role being played
7 in this money scam by the dairy cooperatives
8 who allege to represent their farmers' best
9 interests. In fact, the dairy cooperative
10 hirelings, who masquerade as advocates for
11 the farmers, in fact, are working to bankrupt
12 us and completely eliminate our dairy farming
13 culture as we have known it. This is exactly
14 what will happen if any effort to reduce our
15 milk checks is approved, and this will not
16 please the American consumer who continues to
17 strongly support fair milk prices for their
18 dairy farmers.

19 Agri-Mark suggests that "antiquated
20 cost data from 1998 to 2000" as the basis for
21 current make allowances is inadequate to

1 cover their rising business costs, yet the
2 farmer members of their co-op labor under
3 milk prices that do not even approximate the
4 real basic farm costs to produce the milk in
5 the first place. These cooperatives are
6 fighting here for their plant profit margins,
7 whining for higher cost of production for
8 dairy processing plants, seeming to believe
9 that the "efficiency, economy of scale" model
10 of business they have forced on dairy farmers
11 for the past two decades should somehow not
12 apply to their businesses. Perhaps they
13 should run their plants the way we farmers
14 have been obligated to run our farms during
15 this era of "get more efficient." That would
16 be interesting.

17 Higher fuel costs are impacting on
18 all dairy farm inputs. Skyrocketing health
19 insurance premiums also affect farmers, too,
20 many of whom cannot afford any health
21 insurance at all. And no co-op has

1 addressed that fact by negotiating higher
2 prices for farmers as they are supposed to be
3 doing in the marketplace under the
4 Capper-Volstead Act. Why do these co-ops
5 even exist if not to set a fair price for
6 dairy farmers' milk at the farm? Instead, as
7 rapacious parasites, they pass on higher
8 hauling costs to captive farmers with no
9 adjustment in our milk prices. The farmer is
10 coerced to advertise for the dairy
11 processors' finished product, so it seems
12 these freeloaders feel free to come back
13 again and again and again to take more and
14 more from the farmer until there will no
15 farmers left to provide American consumers
16 with an adequate supply of fresh, local
17 milk.

18 Agri-Mark disparages the new way
19 milk is priced as far as how it determines
20 make allowance for dairy processors. Yet
21 this co-op and its supporters have done

1 nothing to push the USDA to follow through
2 on Federal Judge William Sessions' ruling in
3 the very case Agri-Mark and Upstate Farms
4 supported, St. Albans Cooperative Creamery,
5 Inc., et al., v. Dan Glickman, Secretary of
6 Agriculture. Judge Sessions insisted that no
7 federal milk pricing formula was to be
8 implemented without first factoring for the
9 basic cost to produce the milk as mandated by
10 the 1937 Agricultural Marketing Agreement Act
11 (AMAA). Agri-Mark feigns concern for the
12 plight of the dairy farmer in considering the
13 inevitable drop in milk price we will suffer
14 under their recommended make allowance
15 increases by pointing out that without
16 adjustments plants will close. In fact, they
17 should be honest and say that plants will
18 close when there are no more farmers and that
19 will happen because no one wants to pay dairy
20 farmers what it really costs to milk cows.
21 While plants close for a variety of reasons,

1 it is the dairy plant who should be paying
2 to haul the milk to their processing
3 facility, not the farmer. Under the current
4 stick-it-to-the-farmer milk transportation
5 fee system, dairy processors have no
6 incentive to site their plants either in the
7 traditional dairy regions where farmers
8 currently milk the cows or near the
9 communities where the dairy products are
10 used.

11 The petitioners cry that they cannot
12 wait any longer for relief, yet the short
13 notice of this hearing has given few of us
14 sufficient time to examine or analyze the
15 far-reaching impact the petitioners' request
16 will have on the other class prices. Until
17 dairy farmers receive consideration for their
18 rising production costs, any increase in
19 profits or make allowances will unfairly
20 negatively impact on dairy farmers' income,
21 seriously affecting our ability to pay

1 creditors, plant and harvest crops, care for
2 our cattle and for our families.

3 This insolvency will have an
4 inevitable ripple effect in our rural
5 communities, pulling down our agribusiness
6 providers who are already struggling with
7 open accounts from too many years of low milk
8 prices and bad weather. My farm alone, using
9 figures provided by Penn State's dairy
10 economist, Ken Bailey, is projected to lose
11 annually from \$7,500 to over \$13,000 if this
12 larcenous scheme is approved. That
13 financial loss will severely handicap our
14 family's farm. Granting the petitioners'
15 request for a make allowance adjustment at
16 the expense of dairy farmers in the Federal
17 order system will serve only to unleash a
18 reaction from California, whose make
19 allowance formulas are allegedly the reason
20 the petitioners have requested a reduction in
21 dairy farmers' milk prices.

1 Frankly, what everyone needs to
2 acknowledge is that the current milk pricing
3 system called "Order Reform," (which, by the
4 way, was block voted in by many of the same
5 dairy co-ops who are now petitioning for make
6 allowance increases) is hurting dairy farmers
7 and processors. Left as it is much longer,
8 it will eventually hurt consumers, who will
9 be left with no domestic dairy
10 infrastructure. The Federal Order Reform was
11 an inherently stupid and unfair way to price
12 milk from its dark inception, and it should
13 be discarded for a new system that gives fair
14 consideration to all parties: fair to dairy
15 farmers who care for the cows and the land,
16 fair for processors whose skills provide us
17 with the finished dairy products we all need,
18 and for the consumers who depend on both
19 dairy farmers and dairy processors for their
20 food. It is time to stop the infighting and
21 accept the fact that the current system is a

1 failure and a disgrace to our American
2 values. Until a remedy is implemented, the
3 greatest unfairness is falling on the
4 powerless dairy farmers for whom few are
5 speaking, in spite of the clamor we hear
6 emanating from the petitioners.

7 Again, I implore you not to grant
8 this request to increase the make allowance.
9 Justice is long overdue for America's
10 hardworking dairy farming families.

11 THE JUDGE: Questions of this
12 witness? Ms. Deskins.

13 EXAMINATION

14 BY MS. DESKINS:

15 Q. Sharlene Deskins with USDA. Good
16 morning.

17 A. Good morning.

18 Q. You put in your statement that you
19 didn't have sufficient time to examine the
20 far-reaching implications of this proposal.

21 I understand that, but do you think you could

1 give an estimate, your estimation of what you
2 think this proposal will do to you?

3 A. I think it will ruin us because we
4 are already marginal from the years and years
5 of living under order reform. I mean, order
6 reform, how our milk is priced, gives no
7 consideration to what it really costs to get
8 the milk. I mean, we are producers of raw
9 milk. We are the ones who handle the cows,
10 and we are the ones who plant the crops. And
11 we are the ones who have consideration from
12 our local businesses. I mean, we don't
13 produce the milk alone. We have got a whole
14 pyramid of people in our communities who
15 depend upon us to fight for a milk price out
16 here so they can stay in business.

17 Q. I don't have any other questions.

18 EXAMINATION

19 BY MR. RASTGOUFARD:

20 Q. Babak Rastgoufard, USDA Office of
21 the General Counsel. I know most of the

1 people in the room don't have a copy of your
2 statement, but I noticed in your statement
3 you referred to efficiency. You placed it in
4 quotation marks. I didn't know if you could
5 just describe for us what you mean by
6 efficiency when you place it in quotation
7 marks.

8 A. It's basically punitive. I don't
9 think there is any reasonable businessman
10 who does not believe that efficiency is
11 necessarily a good for his business. But we
12 cannot get any of these representatives to
13 talk to us about anything but get more
14 efficient or get out.

15 You know, and what I'm talking about
16 is like this make allowance. I really don't
17 understand it. I have people in my community
18 and in my associations, and I have a son in
19 my own family who would love to have had
20 sufficient time to analyze it. And I am
21 blessed to have a family member who could

1 have, if he had been properly informed of the
2 timing, to look at it.

3 But when you have to pay your bills,
4 you have to go out every day and milk these
5 cows, and no one wants to talk to you about,
6 hey, my fuel bill is up, the artificial
7 inseminator costs more, the DHI costs more,
8 we are all paying more for fuel -- I mean,
9 the estimation here of the loss, \$7,500 to
10 over \$13,000, I mean, that would be my
11 health insurance.

12 Just this past month, thanks to fuel
13 costs, certainly not grain prices, because
14 our grain farmers are just being scourged,
15 because of fuel prices, my feed company
16 increased -- I order four formulas a month.
17 All four formulas in two weeks went up 12 to
18 \$21 a ton. For my farm that means just like
19 that, in two weeks, I'm going to have to
20 come up with \$2,000 more just for grain.

21 Because my community has suffered

1 four years of terrible weather conditions, my
2 farm has yet, over the past four years, to
3 complete the harvest of all our crops. Our
4 crops have been ruined, and this has
5 necessitated our going out into the community
6 and buying surplus forage from other
7 farmers. So I'm paying extra forage just
8 because I don't have it. All those farmers
9 are passing extra costs that they are
10 experiencing in their harvest on to me, you
11 know, so where do we go?

12 If we go to our co-ops, if we go to
13 the USDA, if we go to Congress, it's we don't
14 need your farm. Why else would we have lost
15 90 percent of our dairymen since this
16 implementation of a policy that we don't need
17 local farmers?

18 MR. RASTGOUFARD: Thank you.

19 THE JUDGE: Other questions. Yes,
20 ma'am.

21 EXAMINATION

1 BY MS. REED:

2 Q. Good morning, Mrs. Cochran.
3 Kristine Reed with Yale Law Office. We met
4 sometime ago, I think. We are here today
5 representing dairy farmers that are also
6 opposed to the changes that have been
7 proposed in this hearing.

8 You talked a little bit about costs
9 that your farm has experienced generally and
10 increases, in particular, in some of those
11 costs over the last several years. Have you
12 also had increases in hauling costs?

13 A. Yes. Yes, we have.

14 Q. How does your farm respond,
15 generally speaking, to continued increases
16 in all areas, not just hauling?

17 A. Prayer, first of all. I feel that
18 it is nothing short of miraculous that we
19 are still in business. And, number two,
20 cutting out other management that -- you
21 have to prioritize -- that may be most

1 important to you, but you have to view it as
2 nonessential because the money is not in the
3 milk check. And we definitely fall in the
4 category of the marginal open accounts.

5 Q. At some point, do you believe there
6 will come a time that these increased costs,
7 particularly if these make allowance
8 increases are adopted by the Department, that
9 your farm will just no longer be able to
10 withstand those kinds of hits?

11 A. Absolutely, because it seems to us
12 -- and I am just speaking as a layperson. It
13 just seems to us there is no fire wall
14 between us and what they can do to us. I
15 mean, they are paying more for fuel, so
16 they'll just take it out of the milk checks.

17 It certainly -- I'll tell you, if it
18 went to a farmer vote, they'd vote no,
19 because when a farmer has a choice between
20 losing his family farm and saying, hey, I
21 need a higher milk price, he wants that

1 higher milk price. I'm sure you cannot get
2 -- the majority of dairymen right now, if
3 they could do a secret ballot themselves, no
4 block voting, secret ballot, they would not
5 want to see an increase in any of their
6 deductions. They want that milk check in
7 its entirety because, I mean, you know, I
8 know we are not supposed to say the "P"
9 word, but some of us are old enough to
10 remember parity.

11 And maybe that's a pricing system
12 that should not be mentioned. Maybe it is
13 not something that we can go back to. But
14 clearly, cost of production is something that
15 all businesses understand. And basic costs
16 are not the same as total economic costs. We
17 are not asking them to guarantee us a profit.
18 These are not, as far as I'm concerned,
19 profit margins. These are basics.

20 You know, I have got cattle that
21 need improved housing. They're not getting

1 it. So we are not talking about a profit
2 where I can go back and make a capital
3 investment. We're talking about paying the
4 vet, the feed bill, the DHI, my taxes.

5 Q. You are talking about having a farm
6 that will continue to survive as an
7 operating farm into the next year?

8 A. For the next generation, whether
9 it's my children or -- I have a large family.
10 I have 14 children. And right now I have
11 only nine left on the farm; of the nine, two
12 who, at one time strongly wanted to farm, are
13 very negative, not because they don't have
14 the farming skills or the interest, they are
15 sick of what is absolutely unjust. Of the
16 children who left, two definitely were also
17 targeted on their own to be farmers, and they
18 had to give it up.

19 I mean, it's like Mrs. Hall said. I
20 mean, we are the nursery of the next trained
21 generation of farmers. This is crazy. We

1 have got all the knowledge. My husband
2 comes, both sides of his family, from
3 generations of dairy farmers. When he is
4 gone and his children are gone, that
5 knowledge is lost.

6 Q. You mentioned that you and your
7 husband, your farm, has about 200 cows?

8 A. Yes.

9 Q. Are you a member today of any
10 cooperative?

11 A. We are now a member of Middlebury
12 Cooperative Milk Producers. In the past we
13 have shipped our milk to Friendship.

14 Q. A recurring theme that we have heard
15 this morning in the producer testimony is
16 that there are a lot of concerns that you
17 folks out in the farm, on the farms, know of
18 a lot of other farmers who are just recently
19 finding out and, in some cases, finding out
20 too late to actually make arrangements to be
21 here for this hearing. How did you actually

1 become aware of the hearing?

2 A. I became aware of it through my
3 contacts in my organization. Otherwise, I
4 would not have known about it. And I would
5 say that the majority of the dairy farmers I
6 know in my community still know nothing. And
7 yet, even if they had known something about
8 it, they don't have time to study it. We
9 cannot assume that they are able to search
10 out the postings in the government records.

11 I know that all dairy farmers get a
12 milk check. And it seems to me that since we
13 all get paid in the milk check, any important
14 announcement could be put into the milk
15 check.

16 Q. I appreciate your testimony and your
17 being here today. Thank you.

18 THE JUDGE: Mr. Beshore.

19 EXAMINATION

20 BY MR. BESHORE

21 Q. Marvin Beshore. Good morning, Mrs.

1 Cochran.

2 I want to talk about loss
3 minimization. If, in spite of your views and
4 the views of others, the Secretary of
5 Agriculture were to find it necessary to
6 change the make allowances, increase them,
7 but it could be limited to Class III and
8 Class IV milk, which is about 35 percent in
9 Order 1, and not be applied to Class I and II
10 prices, would you favor that as at least a
11 minimization of the reductions that they have
12 to have?

13 A. No, Mr. Beshore, I would not because
14 I have always subscribed to the basic belief
15 that we are producers of raw milk. And when
16 my vet comes in or my feed man, he doesn't
17 say, okay, I'll price this percentage of cows
18 at a Class I feed price, Class II, III, IV.
19 Everything that we put into those cows
20 produces milk. What the processor does with
21 that milk after he buys it is his business.

1 And I guess that sounds like a
2 simplistic answer, and maybe it's somewhat
3 arrogant because I'm not able to understand
4 the complexities of what's out there, but I
5 just honestly believe that is an obtuse way
6 to price milk.

7 And if you do have some factor that
8 triggers back to the farm what's going on in
9 the marketplace or at the plant, at the very
10 least I want my cost considered, because
11 right now if it seems to me that if I -- I
12 can prove on paper that I'm spending more
13 for property taxes, liability insurance,
14 health insurance, feed, fertilizer, seed,
15 everything, okay, where am I going to be able
16 to prove that the punitive effect of the make
17 allowance is a definable cost, because they
18 are taking it out from the value of my milk
19 before I ever get that check. So how can I
20 tabulate that this is a legitimate cost of
21 doing business?

1 I mean, even with the, what I feel,
2 is a very unfair, unconstitutional charge,
3 the advertising fee, at least I can see it
4 printed. I don't like it, I think it's
5 awful, and I hope some day it goes away. But
6 it's printed. Where will I see that the
7 profits or the make allowance is within the
8 cost of production for me so then maybe I can
9 get them to raise my price to cover my
10 increased make allowance factor?

11 Q. Okay. Thank you.

12 THE JUDGE: Other questions?

13 Thank you, Ms. Cochran.

14 Ladies and gentlemen, it looks like
15 it's about five minutes of 10. At this time
16 we'll take a 10-minute break, and let's take
17 come back at 10 after 10:00.

18 [Whereupon, the hearing recessed
19 at 9:53 a.m. and reconvened at 10:10 a.m.]

20 THE JUDGE: We are back in session at
21 this time. Mr. Miltner.

1 MR. MILTNER: Ryan Miltner, Your
2 Honor. And there was a website that Dr. Ken
3 Bailey at Penn State posts some reports on
4 that was referenced in some of the farmer
5 testimony earlier this morning, and I wanted
6 to provide that address for record.

7 THE JUDGE: Very well.

8 MR. MILTNER: Okay. It is
9 <http://dairyoutlook.aers.psu.edu>. So we have
10 that, and then we --

11 THE JUDGE: Let's go one more time,
12 please.

13 MR. MILTNER: Sure. It's
14 dairyoutlook.aers.psu.edu.

15 MR. BESHORE: I would just like to
16 note our joinder in Mr. Vetne's objection to
17 that being taken as evidence.

18 THE JUDGE: With the website, it
19 appears that we will not need a copy of the
20 publication, if that resolves your objection.

21 MR. BESHORE: No, my objection is to

1 the taking into evidence of the publication
2 on the website as if it were testimony,
3 expert testimony. It's got opinions,
4 conclusions, etc. Dr. Bailey is not here,
5 and it should not be taken as if he were.

6 THE JUDGE: Well, it will be taken
7 for whatever evidence or for whatever weight
8 the secretary wishes. In other words, it is
9 merely being provided as a reference to the
10 testimony that was given.

11 At this time we also have one
12 additional individual which I'm taking out of
13 order. We have Joe Logan with us at this
14 time.

15 Whereupon,

16 JOE LOGAN,
17 having been first sworn by the judge, was
18 examined and testified under oath as
19 follows.

20 THE JUDGE: If you would, spell your
21 last name for the hearing reporter.

1 THE WITNESS: My last name is spelled
2 L-O-G-A-N.

3 [Whereupon, Exhibit No. 34 was
4 marked for identification by the reporter.]

5 THE JUDGE: Very well, Mr. Logan, you
6 have prepared a statement which I have marked
7 as Exhibit 34. Are you prepared to read it
8 into the record at this time?

9 THE WITNESS: Yes, Your Honor.

10 THE JUDGE: Please proceed.

11 STATEMENT FOR THE RECORD OF JOE LOGAN

12 THE WITNESS: Good morning. Thank
13 you. My name is Joe Logan. I am here
14 representing dairy farmer members of the
15 National Farmers Union.

16 Dairy producers and dairy processors
17 are partners, each dependent upon one
18 another. However, both, not just simply one,
19 must sustain profitability to achieve a
20 healthy dairy industry. Farmers receive no
21 effective assurance of profitable milk prices

1 under the Federal order system, and our
2 question is, why should processors be given
3 special treatment? The Farmers Union opposes
4 the proposals outlined by USDA to increase
5 the make allowance for processors because we
6 believe that it gives a distinctly
7 inequitable advantage to processors and will
8 be economically harmful to producers.
9 Increased energy prices in 2005 have taken
10 their toll on everyone across the country,
11 and it is neither reasonable nor justifiable
12 to craft a remedy for one segment of our
13 industry at the expense of another.

14 Let's take a look, if you would, at
15 the income and expense situation, a snapshot
16 for producers, if you would indulge me. USDA
17 has estimated 2005 net farm income will be
18 \$71.5 billion. That's down \$11.1 billion
19 from the 2004 estimate, which is a 13.5
20 percent decrease in net farm earnings from
21 2004 to 2005.

1 Now, with regard to expenses, the
2 total production expenses for 2005 are
3 estimated to rise 5.8 percent, to a total of
4 \$221.9 billion. This includes all purchased
5 inputs, with especially dramatic increases in
6 energy and fertilizer costs.

7 Now, that 5.8 percent increase
8 equates to a \$12 billion increase in
9 expenses, making it the largest annual
10 increase seen since the \$20 billion increase
11 in 1979.

12 The rising cost of energy-based
13 inputs and increasing interest expense will
14 account for 60 percent of those increases in
15 2005.

16 Now, according to ERS, fuel, lube
17 and electricity costs have cost Ohio dairy
18 farmers -- have increased for Ohio dairy
19 farmers 45.9 percent between 2004 and 2005.

20 Now let's take a snapshot of the
21 statutory authority. The Agricultural

1 Marketing Agreement Act of 1937 requires in
2 Section 608c(18) that the secretary should
3 establish milk pricing according to the
4 following language. "When the national
5 parity price for milk does not adequately
6 reflect the price of feeds, the availability
7 of feed supplies and other economic
8 conditions which affect market supply and
9 demand for milk in the marketing areas to
10 which the marketing agreement order relates,
11 he shall fix such prices as will reflect such
12 factors, insure sufficient quantity of pure
13 whole system milk, and be in the public
14 interest."

15 We believe that the current milk
16 pricing policy being followed by USDA fails
17 to take into account dairy producers'
18 production costs as a factor to determine and
19 adjust the value of milk. The scope of the
20 public interest concerning the dairy industry
21 today has also taken on new meaning. Public

1 interest no longer involves only a fluid milk
2 supply. A dramatic increase in our
3 consumption of processed dairy products
4 demonstrates this to be true. American
5 consumers now rely upon manufactured dairy
6 products as well as fluid milk to be ready
7 available in stores at reasonable prices.

8 The USDA's Federal Milk Marketing
9 Order Program has in the past viewed milk
10 used in the manufacturing products of butter,
11 cheese and nonfat dry milk as reserve milk.
12 Today this milk has as much importance and,
13 arguably, as much value to the consumer as
14 milk utilized in the fluid market.

15 A milk pricing system that is
16 balanced requires that dairy product prices
17 and producer's cost of production and the
18 plant's cost of production, or the make
19 allowance, all be given consideration when
20 determining the value of milk. Each of these
21 items should send signals to one another in a

1 free market environment so that proper
2 adjustments can be forthcoming. The current
3 milk pricing -- in the current milk pricing
4 system, one of these entities seems to be
5 getting unfair consideration. If the current
6 proposal is accepted, the make allowance may
7 be set at a level which may allow the
8 processing segment of the industry to be
9 unconcerned with those market signals.

10 A dairy industry that is truly
11 balanced and market-oriented should be the
12 goal of any milk price system. However,
13 market signals need to flow in both
14 directions, toward both the producing and
15 processing sectors of the industry for that
16 goal to be realized. Economic and marketing
17 conditions are an important element.
18 However, the current USDA Class III and
19 Class IV pricing formulas based strictly upon
20 dairy product commodity prices lack a full
21 acknowledgment of the economic and marketing

1 factors on the producer side of the
2 equation.

3 The main factors involved in
4 establishing USDA current producer milk
5 price formulas are the dairy product price,
6 the product yield and the plant's make
7 allowance. The dairy product prices
8 fluctuate according to economic and marketing
9 conditions. The product yield also
10 fluctuates substantially due to changes in
11 formulation or other quality factors,
12 including cheese moisture content and milk
13 component composition. The remaining factor
14 is the processor's make allowance.

15 The dilemma for USDA's milk price
16 formulas as they relate to the plant make
17 allowance is that a make allowance is a
18 fixed number applied to a highly variable
19 equation. Under USDA's proposal to increase
20 processor make allowances with all three
21 scenarios proposed by USDA, all Federal

1 order class and blend prices fall. The U.S.
2 all-milk price falls and the dairy product
3 prices increase. With all three scenarios,
4 both producers and consumers are losing.

5 Under Scenario No. 1, producer
6 revenue falls by \$72 million per year.

7 Under Scenario No. 2, producer revenue falls
8 by \$140 million per year. Under Scenario No.
9 3, the producer revenue falls by \$207
10 million on average per year.

11 Now, we believe that these estimates
12 may be dramatically understated -- may
13 dramatically understate the revenue losses
14 to the farmer in that they may fail to
15 account for the compounding effect of Class
16 I, or Class III and IV prices impacting
17 Class I and Class II prices. But under no
18 scenario proposed does producer price
19 revenue increase.

20 Now, farmers are the only segment of
21 this economic network that does not have the

1 ability to pass increased production costs
2 forward. Farmers are price takers, we are
3 not price makers. And while the make
4 allowance for processing may need some
5 adjustment, it should not be done strictly at
6 the expense of the producers.

7 Producers should be paid for milk
8 based on the class of product for which it
9 is used. Now, if milk is turned into nonfat
10 dry milk and then is, in turn, used to make
11 cheese, we believe that the producer should
12 be paid based on its cheese value. The USDA
13 may need to implement some procedures for
14 further verification as products flow through
15 the system.

16 The National Farmers Union proposes
17 that Class III and Class IV make allowances
18 be established in a market-oriented fashion.
19 The cheese, dry whey, butter and nonfat dry
20 milk make allowances should have a base make
21 allowance set by the weighted average of

1 manufacturing costs determined by the USDA
2 Rural Business Cooperative Service and
3 adjusted on an annual basis. The cheese and
4 whey base allowances should be adjusted
5 according to the relationship between cheese
6 versus whey powder reference price and the
7 producer's cost of production. The butter
8 and nonfat dry milk base allowance are to be
9 adjusted according to relationship between
10 the butter-nonfat powder reference price and
11 the producer's cost of production.

12 This make allowance proposal is
13 directed by market conditions, which the
14 current formula lacks or ignores. The
15 current formula forces all market price
16 volatility on to the producer's milk pay
17 price. The challenge for USDA is to develop
18 a system that will equitably consider the
19 profits for processors and producers to give
20 each the proper market signals and
21 incentives to produce a healthy supply of

1 dairy markets and a healthy overall market.
2 Linking may allow producers' costs and
3 prices -- linking the make allowance to
4 producers' cost and prices will help USDA
5 insure a sustainable system for future
6 generations.

7 Thank you, Your Honor. I'll take
8 any questions that you may have.

9 THE JUDGE: Questions of this
10 witness? Mr. Yale.

11 EXAMINATION

12 BY MR. YALE:

13 Q. Benjamin F. Yale on behalf of Select
14 Milk Producers, Continental Dairy Products,
15 Dairy Producers of New Mexico. Good
16 morning.

17 A. Good morning.

18 Q. Do you still operate a dairy farm?

19 A. Actually, my brother, Tom, operates
20 the active dairy farm. I raise some dairy
21 heifers for him and farm.

1 Q. And you still have an interest in
2 the dairy operation?

3 A. Absolutely.

4 Q. And you grew up on a dairy farm?

5 A. Fifth generation, yes. I was an
6 active dairy farmer for 25 years.

7 Q. And that farm is located where?

8 A. In northeastern Ohio.

9 Q. In Trumbull County?

10 A. Trumbull County, that is correct.

11 Q. And that is -- and do you know where
12 that milk is marketed?

13 A. That milk is currently marketed out
14 of a Reiter Dairy. It used to go to Akron.
15 Now a lot of it goes to Springfield and,
16 actually, some go to other processing plants
17 in the region.

18 Q. So you are not a member of a co-op?

19 A. They have not been members of
20 co-ops. I was a member of the DFA co-op for
21 many years and its predecessor co-ops.

1 Currently not members of a co-op.

2 Q. And do you know if they receive any
3 premium over the blend price for their milk?

4 A. A modest quality premium.

5 Q. You talked about the requirements
6 under 608c(18) and the cost of feed and the
7 like. In your opinion, does the cost or the
8 prices of cheese, for example, does that
9 reflect the cost of feed at the farm, at the
10 dairy farm that you operate or your brother
11 operates?

12 A. In a short word, no. Actually, USDA
13 ERS estimates total cost of production for
14 dairy farmers to be in the vicinity of
15 \$18.68 in 2004, I believe, for which the
16 most recent figures are available.

17 Obviously, the dairy prices languish far
18 below that.

19 Q. And you indicated you raise heifers,
20 I believe?

21 A. Yes.

1 Q. And I take it that you sell them,
2 right?

3 A. Yes.

4 Q. And do you index the price of your
5 heifers off the price of cheese?

6 A. No, those markets operate
7 independently, although there is a distant
8 relationship.

9 MR. YALE: I don't have any other
10 questions.

11 THE JUDGE: Thank you. Other
12 questions?

13 EXAMINATION

14 BY MR. RASTGOUFARD:

15 Q. Babak Rastgoufard, USDA. I just
16 have a couple questions for you regarding the
17 National Farmers Union.

18 A. Sure.

19 Q. Do you happen to know the size of
20 that organization?

21 A. Nationwide, about 250,000 members.

1 Q. And do you know what percentage or
2 what number of members are dairy farmers?

3 A. Actually, I cannot give you that
4 number at this point. We could get that back
5 to you if you need it.

6 MR. RASTGOUFARD: No other questions.
7 Thank you.

8 THE JUDGE: Other questions of this
9 witness? Mr. Beshore.

10 MR. BESHORE: Yes.

11 EXAMINATION

12 BY MR. BESHORE:

13 Q. Marvin Beshore, Mr. Logan. Did I
14 understand your testimony -- and I didn't
15 have a copy of your statement available.
16 Did I understand your testimony to be that
17 you thought that the economic impact
18 statement published with the proposed rule
19 did not reflect the impact on Class I and II
20 prices?

21 A. I have anecdotally seen and heard

1 some analysis which project the loss to
2 dairy farmers to be dramatically beyond
3 those figures that are published. And I
4 infer from that that they may not included
5 the relationship between the impact that
6 Class III and IV prices would eventually
7 impose upon Class I and II.

8 Q. Were you here at the hearing
9 yesterday at all?

10 A. No, I just got here today.

11 Q. If I were to suggest to you that the
12 detailed data that the USDA officials placed
13 in the record concerning that analysis show
14 that it did include impact upon Class I and
15 II prices, would you be willing to accept
16 that?

17 A. Well, I have seen data over the
18 years from USDA and other analytical
19 agencies that has been true, and I have seen
20 data from USDA that has not proven to be.
21 So I guess my inclination would be increased

1 to accept that.

2 Q. Okay. If it were possible for
3 changes in the make allowances to be done in
4 a way that it did not impact Class I and II
5 prices and insulated those prices from the
6 changes, would you support that limit on the
7 price effect on dairy farmers?

8 A. We would appreciate the gesture.
9 But on behalf of dairy producers that are
10 already producing milk and putting it on the
11 market at far below the cost of production,
12 no, we could not in good conscience accept
13 that.

14 Q. It is not enough? Is that the
15 problem?

16 A. Well, once again, we cannot support
17 an effort and a structure that is designed
18 to hold harmless one segment of the industry
19 while it causes great harm and injury to
20 another segment.

21 Q. Do you understand blend pricing

1 under the Federal order?

2 A. Yes, I think so.

3 Q. And do you understand that all
4 producers, regardless of where their milk
5 is, are affected by reductions in every
6 class price?

7 A. With the exception of California,
8 sir.

9 Q. Right. In the Federal order system
10 which --

11 A. Right.

12 Q. Okay. And so, if price reductions
13 were -- well, you understand that changes in
14 the make allowance could change and reduce
15 Class I and II prices?

16 A. Yes.

17 Q. And, therefore, prices on all uses
18 of milk, right?

19 A. Absolutely.

20 Q. But if were structured so that the
21 impact was only on Class III and IV and,

1 therefore, the reduction on the blend prices
2 to all farmers, not just one segment, but
3 all farmers was less, wouldn't that be a
4 more desirable outcome?

5 A. I understand that would mitigate the
6 negative effect on dairy farmers. But
7 nevertheless, it would still be an effort,
8 in our view, to hold harmless one segment of
9 the industry at the expense of another
10 segment of the industry.

11 Q. Who is being held harmless other
12 than the --

13 A. Well, the processors with that make
14 allowance.

15 Q. So you would rather have the dime or
16 20 cents loss than half that or a third of
17 that?

18 A. Say that again, please.

19 Q. Well, if there is going to be -- you
20 prefer -- if there is going to be a
21 reduction in blend prices to all dairy

1 farmers in the Federal order system --

2 A. Yes.

3 Q. -- okay, you'd prefer it to be 20
4 cents than 10 cents? Is that your
5 testimony?

6 A. No, that's not my testimony.

7 Q. Okay. Thanks.

8 THE JUDGE: Mr. Yale.

9 EXAMINATION

10 BY MR. YALE:

11 Q. There was another line of questions
12 I forgot to ask. The size of the producers
13 that tend to be members of the Farmers
14 Union, how would you characterize the size of
15 those?

16 A. Generally speaking, the National
17 Farmers Union represents the so-called
18 family farms, perhaps a bit more modest in
19 size than the national average. Now, that
20 said, many of our members are large farmers
21 as well with many thousand cows.

1 Q. The impact of a quarter a
2 hundredweight in pricing, does that have --
3 would you see that as an impact on the small
4 farmers that are members of the Farmers
5 Union?

6 A. I would see that as having an
7 enormous impact. I mean, when we are
8 operating a business which has a very limited
9 to zero and, in many cases, a negative
10 margin, a quarter a hundredweight, a penny a
11 hundredweight, a dime a hundredweight makes a
12 huge difference.

13 Q. I see. So you say you have been
14 dairying for 25 years and have obviously been
15 in the dairy country before that. You do
16 look older than 25. That was what I was --

17 A. A bit.

18 Q. When prices come down like that,
19 what impact do you see that happening in the
20 country in terms of the dairy farm people and
21 the like? I mean, is it noticeable?

1 A. Oh, absolutely. I grew up in a
2 neighborhood that was predominantly dairy
3 farmers, many dairy farmers up and down the
4 road. And frankly, since 1978, we have had
5 a constant downgrading in prices. At that
6 time, prices were floored at \$13.68 or
7 something of that nature, and now dairy
8 farmers are lucky to see that on the
9 average, so yes. And that has -- we have
10 seen that decimate communities across the
11 state of Ohio and across the nation.

12 Q. There is testimony that's given, and
13 you have heard it, I'm sure, over the years.
14 They say if prices go down, there is loss of
15 production. Loss of production means that
16 the supply/demand tilts back in favor of
17 producers, demand rises the prices up and,
18 you know, that production gets a higher
19 price.

20 How is it that production is lost in
21 the country due to low prices?

1 A. Well, actually, that mechanism that
2 is common in most other aspects of other
3 industries is not as common in agriculture,
4 and certainly not in dairy. And that, I
5 believe, is the case because farmers in
6 general, and dairy farmers especially, are
7 very highly leveraged. In other words, they
8 have mortgages. They have families to feed.
9 They have college funds, medical bills, etc.
10 to pay, and they need to generate X dollars
11 of income. And if the price of milk falls,
12 they need to put on a few more cows and
13 produce a few more units of production in
14 order to make those payments.

15 So we don't see that supply/demand
16 factor repeated in agriculture like we do in
17 other industries.

18 Q. But production does go down with
19 reduced prices, right?

20 A. Actually, we have not seen that as a
21 historical dynamic that we can rely on.

1 Q. Right, and the overall production
2 tends to grow, but in some areas it -- I
3 mean, when production does go down, how is it
4 done? Is it because they sell the cows and
5 slaughter them, or what happens?

6 A. Yes, when production goes down in a
7 given area, normally what you'll see is the
8 small, family type farmers, usually the elder
9 farmers, will give up the ghost or they will
10 be liquidated forcefully, and those cattle
11 will then go down the road to another farm
12 somewhere else.

13 Q. So the effect of lower prices ends
14 up being fewer producers? Is that a fair
15 statement?

16 A. The effect of lower prices is fewer
17 producers and, in some cases, communities
18 that are in dramatic decline.

19 Q. Just one follow-up on a question
20 that Mr. Beshore had asked you. You said
21 that one segment of the industry should not,

1 you know, get a guaranteed profit or, I mean,
2 I'm kind of paraphrasing, while the farmers
3 have to take a loss. Are you referring to
4 the fact that the cheese manufacturers or
5 those processors under this scenario where
6 the Class I and II is changed, that they
7 still get relief, but the farmers don't get
8 any relief for their costs? Or what were you
9 meaning by that statement?

10 A. Well, an increase in the make
11 allowance is a withdrawal from the pool.
12 That pool then is allocated to dairy farmers.
13 So, in our view, a reduction in the total
14 amount available in the pool is a reduction
15 in dairy prices to farmers, and so we view
16 any increase in the make allowance as a
17 decrease for farmers.

18 Q. You say it comes out of the pool.
19 Where, then, does the money go?

20 A. Well, that make allowance money
21 would be allocated to the processors.

1 MR. YALE: I have no further
2 questions. Thank you.

3 THE JUDGE: Other questions?

4 Thank you, Mr. Logan. You may step
5 down.

6 Mr. Vetne, at this time it looks like
7 we have gone through some of the independent
8 testimony. Do you wish to put Mr. Wellington
9 back on or would you rather -- at this time
10 we also have the option of putting Dr. Ling
11 back on.

12 MR. VETNE: I would suggest that we
13 get Dr. Ling back on and out of the way so we
14 can have continuity in the testimony.

15 THE JUDGE: I trust that you mean
16 just get his testimony out of the way.

17 MR. VETNE: Let's hear from Dr. Ling.
18 Whereupon,

19 DR. CHARLES LING,
20 having been previously sworn by the judge,
21 was examined and testified under oath as

1 follows:

2 THE JUDGE: Good morning, Dr. Ling.

3 You are still under oath.

4 I have a statement which Ms. Deskins
5 has handed to me. It will be marked as
6 Exhibit 35.

7 [Whereupon, Exhibit No. 35 was
8 marked for identification by the judge.]

9 THE JUDGE: To the extent not
10 previously already admitted, we now have 34
11 exhibits in evidence, and then this one under
12 consideration at this time.

13 [Whereupon, Exhibit No. 34 was
14 received in evidence.]

15 EXAMINATION BY MS. DESKINS

16 Q. Dr. Ling, did you put in the back of
17 room copies of Exhibit 35?

18 A. Did I --

19 Q. Did you put in the back of room
20 copies of Exhibit 35?

21 A. Yes.

1 Q. And, Dr. Ling, for the record, could
2 you identify --

3 THE JUDGE: Ms. Deskins, why don't we
4 wait just a little bit so people can see the
5 copies, and then we can go into what they
6 actually mean.

7 It looks like everyone has one now.

8 MS. DESKINS: Yes, sir.

9 BY MS. DESKINS:

10 Q. Dr. Ling, could you identify for the
11 record what Exhibit 35 is.

12 A. It's Table 1, Cooperatives and
13 Plants by Location Participating in the USDA
14 Rural Development Cooperative Programs Dairy
15 Product Plant Cost Technical Assistance
16 Project, 1998 and 2004 Data.

17 Q. And can you explain to us why you
18 brought this exhibit in today?

19 A. This is in response to Mr. Yale's
20 request yesterday. It is to -- he wanted to
21 see the plants that participated in 1998 and

1 2004.

2 Q. And were there any other requests
3 made of you yesterday?

4 A. I believe his associates requested
5 that high and lows, the highs and low range
6 of the cost, that we provide it.

7 Q. Are you able to respond to that
8 request at this time?

9 A. I have to decline to provide that
10 data. The reason is co-op, when they give
11 me the permission to testify, they allow me
12 to use aggregates or averages. If I provide
13 high/low ranges of individual cost items,
14 those items, those ranges are neither
15 aggregates nor averages. And in any case, I
16 should not go beyond what I have put in
17 Exhibit 18 that was approved by the agency.

18 MS. DESKINS: Okay. Thank you, Dr.
19 Ling. I would move for the admission of
20 Exhibit 35.

21 THE JUDGE: Very well. Exhibit 35

1 will be admitted.

2 [Whereupon, Exhibit No. 35 was
3 received in evidence.]

4 THE JUDGE: Is there -- excuse me.
5 Mr. Rower.

6 MR. ROWER: Thank you, Judge.

7 EXAMINATION

8 BY MR. ROWER:

9 Q. Jack Rower, AMS Dairy Programs.
10 Good morning, Dr. Ling.

11 A. Good morning.

12 Q. In your plant cost analysis, did you
13 notice that larger plants tend to have lower
14 production costs than smaller plants in the
15 population of plants that you were looking
16 at?

17 A. Without looking at the data, I
18 wouldn't be able to give you that general
19 statement because there are so many factors
20 going into, you know, price and cost.

21 Q. So that is not just eminently

1 apparent from looking at the data and from
2 remembering this morning?

3 A. No. I mean, from my memory, I don't
4 --

5 MR. ROWER: Okay. Thank you very
6 much, Doctor. That's my questions. Thank
7 you.

8 THE JUDGE: Other questions? Mr.
9 Yale.

10 EXAMINATION

11 BY MR. YALE.

12 Q. Good morning, Dr. Ling.

13 A. Good morning.

14 Q. Thank you very much for preparing
15 this. I just want to make sure -- I want to
16 make some assumptions off of your statement,
17 off this exhibit, but I thought maybe I
18 ought to ask your permission before I do.

19 A. Okay, before you go on --

20 Q. Okay.

21 A. -- I want to say that this should

1 supersede what I said yesterday in response
2 to your question about location of plants
3 because when I responded to your questions,
4 I responded out of my memory, so it might
5 not be complete or accurate.

6 Q. Looking at that, it looks like you
7 were pretty close, so -- and the good news
8 is that it's typed up. I wrote mine down
9 from the stand, and I can't read them last
10 night anyhow. So it's not something I can
11 read.

12 What we can do with this data is
13 that we can safely say that by comparing --
14 you have 1998 -- you have a header, 1998
15 Data, and then a header, 2004 Data, right?

16 A. That is correct.

17 Q. And I could draw a line down between
18 those two, and I can -- if a plant appears
19 on the right side, under the 2004 data, but
20 it was not on the left side, under the 1998
21 data, I can say that this is -- this was

1 new, this was a new plant or new data that's
2 been added to the operation, right? It was
3 not used in 1998 at all? I can safely say
4 that?

5 A. That is correct.

6 Q. Okay. And vice versa, that if shows
7 up in 1998 and not 2004, that it was not
8 available in 2004?

9 A. That is correct.

10 Q. All right. So -- and not asking for
11 any additional information that you have to
12 come back or anything, but if you know, does
13 -- these additional plants that came on or
14 show up in 2004, did they also appear in
15 some prior years, like 2002 and 2003, or are
16 they mostly new for 2004?

17 A. Well, some are new, like, you know,
18 some are newly acquired, so yes.

19 Q. Right. And you haven't personally
20 visited all these plants or done an
21 inspection of their operations?

1 A. Back in the '80s and early '90s I
2 made a point of visiting every plant. But
3 since then, I didn't make many trips out to
4 the plants because we want to save taxpayers
5 money so we can have tax cuts.

6 Q. Okay. We could have a long
7 discussion on that, but I think it's not
8 relevant to this hearing.

9 Very good. That's all the questions
10 I have.

11 Thank you again for providing this
12 information.

13 THE JUDGE: Other questions of this
14 witness?

15 Very well, Dr. Ling. Thank you.
16 You can step down.

17 Mr. Vetne.

18 Whereupon,

19 ROBERT WELLINGTON,
20 having been previously sworn by the judge,
21 was examined and testified under oath as

1 follows.

2 THE JUDGE: Mr. Wellington, you are
3 still under oath.

4 THE WITNESS: Yes, sir.

5 MR. VETNE: Your Honor, I have no
6 further direct at this time. I may have
7 redirect later.

8 THE JUDGE: Very well. Is there
9 cross of this witness? Mr. Yale?

10 EXAMINATION

11 BY MR. YALE

12 Q. Benjamin F. Yale on behalf of
13 Select, Continental and Dairy Producers of
14 New Mexico. Good morning, Bob.

15 A. Good morning.

16 Q. I would like to start off with a
17 couple questions. One of the plants that is
18 owned by Agri-Mark now is Cabots, if I'm not
19 --

20 A. We have three plants. We own one in
21 Cabot, Vermont, yes.

1 Q. Yes, Cabot, Vermont.

2 A. Yes.

3 Q. Right. And is it fair to say that
4 Cabots has a reputation of producing a
5 high-quality cheese?

6 A. Yes, it does.

7 Q. In fact, cheeses?

8 A. Yes.

9 Q. A number of different varieties?

10 A. Primarily, they are all
11 cheddar-based varieties, but yes.

12 Q. Right. And the trade name "Cabot"
13 is routinely used to add value to that
14 product in its marketing throughout --
15 really, throughout the world, right?
16 Doesn't it market cheese throughout the
17 world?

18 A. On occasion.

19 Q. It's not a routine international --

20 A. We sell a pound in England, and then
21 we tout it as an international company --

1 Q. Oh, okay.

2 A. -- but --

3 Q. I remember being told it was
4 internationally sold, so --

5 A. At times, it is, on occasion, but
6 basically it's a national -- we are at
7 national distribution now.

8 Q. Right. And in looking at your
9 website for Cabot, I noticed that it has --
10 again, most of these, I do believe, are
11 cheddars or American style cheeses.

12 A. Yes.

13 Q. But a wide variety of things, sharp
14 cheeses and various stages of sharps,
15 seriously sharp, extra sharp, flavored
16 cheeses, chipotle, pesto, sundried tomato, a
17 number of those varieties, right?

18 A. Yes.

19 Q. Now, are those cheeses produced at
20 your plant at Cabot?

21 A. It depends on the particular cheese.

1 Most of our cheese is actually produced at
2 Middlebury. If you look at our sharp or
3 extra sharp or a variety like that, that's
4 just cheddar cheese that is just aged a
5 longer period of time.

6 Q. Yes.

7 A. And there's a lot of cost, of
8 course, involved with that. But most of
9 that is made at our Middlebury plant. Our
10 other varieties could be made at Cabot. It
11 depends on if we have or want to -- if we
12 need to make more cheese or whatever, are not
13 -- some varieties, you almost have to make
14 at Cabot, such like if you are going to make
15 a tomato basil. You are putting extra
16 ingredients in, and you need an open vat to
17 do that. So we have the open vat to put the
18 tomato basil in.

19 Q. These cheeses, these varieties I
20 mentioned, you know, I think as indicated by
21 Dr. Ling's just recent testimony and

1 yesterday, that Cabots is listed as one of
2 the plants that has participated in this
3 cooperative plant cost survey, right?

4 A. Yes.

5 Q. And are these cheeses included in
6 that survey?

7 A. The production of cheeses at the
8 plant is included in the survey. We tried
9 to remove any additional costs that would be
10 involved from the survey costs. We tried to
11 follow Charlie's instructions in regard to
12 that.

13 Q. Are -- does Cabot sell any cheese --
14 or let me rephrase that. Do you report --
15 does Agri-Mark, first of all, report any
16 product to NASS for the NASS product
17 surveys?

18 A. Yes, we report nonfat dry milk
19 powder.

20 Q. Nonfat dry. Do you report any
21 cheeses?

1 A. No.

2 Q. And butter?

3 A. We haven't reported butter in quite
4 a period of time.

5 Q. What about dried whey?

6 A. No, we don't make any standard dried
7 whey with regard to that. We do, by the
8 way, we have purchased butter from people who
9 do report in the NASS. I think we referred
10 to cheese on occasion.

11 Q. Now, in the selling and the
12 marketing of these cheeses from Cabot's, are
13 those sold routinely in 40-pound blocks?

14 A. Oh, no, not at all.

15 Q. They tend to be in, like, 10-pound
16 loaves?

17 A. Most of cheese is sold in consumer
18 type packing.

19 Q. Off-cut and wrapped at Cabot?

20 A. It's a separate facility at Cabot,
21 but it is located at Cabot.

1 Q. And these products that -- are sold
2 at prices higher than the NASS survey price?

3 A. We have to because the costs are so
4 much higher than the cost of making cheese
5 at the NASS survey -- the cost, rather, of
6 the marketing and all the storage and
7 everything else that goes on in that
8 process.

9 Q. At Table 3 of your statement, you do
10 a -- some form of an abbreviated, for want
11 of a better term, profit and loss statement?

12 A. I wouldn't call it profit and loss.
13 It is an impact statement of looking where
14 our costs are at right now that we put
15 together for Dr. Ling's study. And then we
16 compared that with the current make
17 allowances to show that difference that we
18 are experiencing in our plants.

19 Q. Now, you show an impact of \$15
20 million, almost \$15.5 million on operations
21 for 2004 under this scenario. Is this a

1 loss that's actually reported on the books
2 of Agri-Mark?

3 A. Not reported in that particular
4 form. The fact that we can't -- we don't
5 recover our costs of making the product,
6 that becomes a loss or, at least, a loss to
7 that sector of that production.

8 Q. And is this a number that is
9 reported internally as a loss within
10 Agri-Mark?

11 A. We do keep track of what our costs
12 are. That made it easier to do Charlie's
13 study as well as the Cornell study. And we
14 know what the make allowance is, so we know
15 what the impact on our total operations of
16 inadequate make allowances. So we do keep
17 track of the impact on that.

18 Q. Are these plants actually reporting
19 operating losses?

20 A. To --

21 Q. To -- I mean, first of all, are they

1 separately -- are they a separate operating
2 entity in which you have enterprise
3 accounting for each of the plants?

4 A. Oh, yes. That's a good point. Yes,
5 actually, they are. We separate our
6 Agri-Mark business out from our Cabot
7 business so we can keep track of those two.
8 And so, at our Agri-Mark business, we are
9 responsible for making the products. And
10 then we transfer them at a cost, basically at
11 the CME level, to Cabot so we can keep track
12 of those costs. And if we look at our
13 Agri-Mark costs over time, lately -- well,
14 this year, probably our aggregate losses are
15 9 or \$10 million because of that.

16 Q. And that includes the -- is Cabot's
17 also operating at a loss?

18 A. Cabot, this year -- is about
19 breaking even in the past. It usually
20 operates, we hope -- we have a lot of assets
21 involved, and we have spent a lot of money

1 on marketing and inventory so it would make a
2 profit. This year, it's been a struggle to
3 do that.

4 Q. But the added value for these
5 specialty cheeses and stuff that is sold at
6 Cabot's in the Cabot plant, it's not in the
7 other plants? You don't pass on -- in other
8 words, if you made cheddar at Middlebury and
9 shipped it to Cabot's and they cut and
10 wrapped it and sold it as one of their
11 specialty cheeses at a higher price,
12 Middlebury only gets the credit at the CME
13 price?

14 A. Right.

15 Q. They don't get the credit of any
16 added value that's done at --

17 A. Oh, no, they don't get any credit
18 from the other side.

19 Q. But at the end, it shows up in the
20 Agri-Mark books once it filters all the way
21 to the top or bottom or however --

1 A. Oh, at the bottom, absolutely.

2 Q. Okay. Now, in this analysis, there
3 is some assumptions that aren't shown here.
4 And let ask you, I want to ask you a
5 question about that. One of those is the
6 yield. What yield does Agri-Mark get on its
7 cheese production out of a hundred pounds of
8 milk, approximately?

9 A. A little less than 10 pounds, I
10 believe.

11 Q. Do you know what the implied yield
12 is under the Federal order formula?

13 A. The implied yield, I believe, is
14 somewhere around 97, but it also implies a
15 very high amount of whey butter coming out
16 of that and whey powder, higher than it
17 would have. We actually get a higher yield
18 from cheese, but then we don't make as much
19 whey butter, and we don't make as much whey
20 powder.

21 Q. You have a higher butterfat yield

1 than the -- or butterfat recovery than what
2 the Federal order formula --

3 A. Yes, we do.

4 Q. Now, in Dr. -- well, let me take
5 another step. You are, I'm sure, being in
6 the dairy industry all these years, you are
7 aware of the "Dairy Market News," right?

8 A. Yes.

9 Q. And do you read that from time to
10 time or look at it or --

11 A. Pretty much every week when it comes
12 out.

13 Q. Now, one of the things that's
14 reported on a weekly basis in "Dairy Market
15 News" are wholesale selling prices of
16 different cheeses other than the straight
17 CME and the like, right?

18 A. I have seen them, yes.

19 Q. And then they have a report from
20 different regions. For example, in the
21 Northeast, in the one that we have marked as

1 Exhibit No. 17, there is an indication of
2 prices for 10-pound prints and cheddar
3 single daisies and cheddar 40-pound blocks.
4 Do you ever look at those prices?

5 A. I don't because my end of the
6 business really is looking at the
7 farmer-related issues and the general price
8 levels that are there, forecasting prices.
9 I don't look at the details of those, no.

10 Q. What is a 10-pound print?

11 A. Basically, it's -- my understanding
12 -- I don't do that end of the business, but
13 a 10-pound print is a 10-pound block of
14 cheese that will be sold. And then usually,
15 each person you sell it to will cut it up in
16 whatever form they want to cut it.

17 By the way, I would say, it's
18 probably good to say early on that some of
19 the detail questions like this, we are going
20 to have Richard Langworthy, who is in charge
21 of operations, coming on. And I can give

1 you my best estimate, but he is very
2 knowledgeable of that.

3 Q. But you won't squirm if I don't ask
4 you these questions.

5 A. No Agri-Mark people squirm.

6 Q. I appreciate that, and I'll try to
7 defer to him. Thank you for making that
8 reference.

9 But one of the things that I noticed
10 in this -- and again, it's reported in
11 "Dairy Market News."

12 And one of the problems with dairy is
13 that there's all kinds of numbers out there.
14 We have heard already, with a couple
15 witnesses, almost a plethora of make
16 allowances. You know, you have got 1998. We
17 have got 2004. We've got with ROI. We've
18 got the administration. We've got the
19 California. We've got the efficient, large
20 California. We have got the small, lesser
21 efficient California and the like.

1 I want to approach something else
2 here just to show you something that deals
3 with impact on Table 3. In -- I think you
4 would agree, would you not, that the cheeses
5 sold are Cabot's are -- I think you've said
6 they are higher than the NASS price, right?

7 A. The product we get for it?

8 Q. No, that you sell out of Cabot's,
9 that that price is sold at Cabot's. And it
10 sells cheese at prices per pound at a higher
11 rate than the NASS price that's reported?

12 A. Sure, because we have much higher
13 costs than --

14 Q. Sure. I understand that. And one
15 way to determine the cost of a plant,
16 another way to do that is to take your
17 product that you sell and multiply that
18 times a -- you know, a price per pound, an
19 average price per pound. And then you can
20 subtract that -- you can take that out and
21 subtract out the value of the milk, and you

1 can kind of get a gross margin in there
2 between what the product sold for and what
3 you paid for the raw milk, right?

4 A. You can certainly make that
5 calculation.

6 Q. Right. Now, if you look -- Dr.
7 Ling, for his 40 -- for his study, reported
8 for the 40-pound blocks that the yield for
9 those plants reported was 10.7 pounds per
10 hundred pounds of milk. Do you see that?

11 A. I don't have it with me. To be
12 honest with you, I didn't even look. Wait a
13 minute. Maybe I did bring Charlie's report
14 with me. [Reviewing.]

15 Yes, I do see that.

16 Q. So if you note in the -- and I can
17 get you the exhibit. You can look if there
18 is a question that you have. But in the
19 Northeast, under the cheeses reported at
20 page 7 of this exhibit, for example, the
21 price, average price in December that they

1 listed for the Northeast -- and I understand
2 that there is a lot of slop in that. I mean,
3 the prices -- some sold less than that, and
4 some of them more, and these are estimates.
5 It's not a technical survey, but it gives
6 some indication -- indicated a price of
7 \$1.76, \$1.77 per pound.

8 Now, if you took that price times
9 the 10.7, you would get a gross value of --
10 I'm going to set up this scenario, and then
11 I'm going to ask you a question. You would
12 get a gross value of \$18.91. The Class III
13 price for that month was \$13.57 with an
14 implied gross margin of about \$5.34, or about
15 50 cents a pound.

16 Now, I'm not asking you to agree
17 with me on those numbers because I know what
18 the answer would be, that you would think
19 that you make a 50 percent make. But my
20 question is that when we look at what truly
21 is the make allowance, don't we need to do

1 more of a mass balance and look at the gross
2 sales that are coming out of the plant and
3 look at the raw costs of the milk, and the
4 difference between those is the make, not
5 sitting down here and trying to build up
6 tables of labor and wages and the like?
7 Would you agree with that?

8 A. No, I think the make is how much it
9 costs to manufacture.

10 Q. And one way to obtain that is to
11 take the gross sales and subtract out the
12 raw --

13 A. But the gross sales isn't a
14 manufacturing cost.

15 Q. But you can come up with a gross
16 margin by doing that, can you not?

17 A. You can come up with gross margin,
18 but there are so many other things in that
19 margin other than cost --

20 Q. I understand that?

21 A. -- that I don't think it relates

1 back to the manufacturing cost.

2 Q. But it reflects back to the
3 profitability or the lack of profitability of
4 a plant. And that is what you are here
5 about, is your profitability of your plant,
6 not the make allowance. The make allowance
7 is your proxy to get you to a profitable
8 plant. But what you are interested in is a
9 profitable plant, right?

10 A. No. Now, we -- whether we make a
11 profit or loss at our facilities, it's going
12 to have to be a level on where we are
13 relative to average efficiency relative to,
14 gosh, we put \$10 million a year into
15 marketing our products to try to get a better
16 price. All those things will lead to
17 profitability.

18 We are trying to say -- we have a
19 choice here. We could make the products
20 ourselves or, like I said -- let's take
21 butter, for example. We bought butter from

1 people in the NASS. And so, we could take
2 that butter and do it that way, and then we
3 wouldn't have to worry about a make
4 allowance. But we'd prefer to take our milk
5 and provide a market for our members and for
6 other farmers. Particularly on butter, we
7 provide a market for a lot of farmers around
8 the Northeast.

9 You know, that's our issue, and
10 that's our concern in doing that.
11 Profitability is an entirely unrelated issue
12 in regard to this.

13 Q. Okay, let's talk about that. In
14 other words, you are having to make choices
15 in terms of what Agri-Mark does and how it
16 does it, right?

17 A. Every business does, yes.

18 Q. Every business does, right. And you
19 are now in a situation where a choice to
20 continue to operate plants under the current
21 regimen is, in your position, the way you

1 look at it, is not cost effective?

2 A. Right now, that -- given what the
3 make allowances are, yes, that is true.

4 Q. Okay. So is the issue that you are
5 focusing on at Agri-Mark an issue that is
6 one that is being -- that plants, for
7 example, in the Southwest are facing?

8 A. I would say to a great extent, yes.
9 I mean, besides just looking at the cost
10 factor, you know, we also have to look at
11 providing markets for milk. And I guess
12 those plants probably do, too. I'm not
13 familiar with it.

14 Q. But are they facing the same kind of
15 economic choice because of the make
16 allowances in setting markets than you are?
17 Can you testify for a fact that, for
18 example, in the Southwest, that they need
19 this extra make allowance in order for them
20 to maintain a market for their producers?

21 A. No, I can't, and I would say they

1 may not. I mean, I'm aware of a new plant in
2 the Southwest coming on that may be the
3 largest plant in the country. Maybe their
4 make allowance tends to be smaller than
5 ours. I don't know. But, no, I can't
6 testify about Southwest information because I
7 just don't have --

8 Q. All right. So -- but the proposal
9 that you are making and you are supporting,
10 you are asking the Department to change
11 these prices throughout the country, is that
12 right?

13 A. Yes, I am. And our numbers will be
14 a piece of that, but they're not -- I'm not
15 asking them to go to our make allowances on
16 this, so --

17 Q. But -- and I understand that, but
18 you are proposing a reduction in Class III
19 prices throughout the country or Federal
20 order program?

21 A. No, the impact on the Class III

1 price will depend on what happens to the
2 price of cheese on the make allowance. If
3 the price of cheese was held constant, yes,
4 it would lower the price.

5 Q. Or if the price that producers are
6 paid is indexed to the Class III price,
7 directly indexed to the Class III price,
8 their price --

9 A. When you mean index, you mean the
10 Class I --

11 Q. Plus or minus Class III. If the
12 price sold to a cheese plant is plus or
13 minus Class III, Class III is the index and
14 --

15 A. If that's their arrangement, then
16 mathematically I guess that would be the
17 case.

18 Q. All right. So then, the reduction
19 in the Class III formula would have an
20 impact in the reduction in their price
21 because their index is reduced?

1 A. If they are based on the Class III
2 price, yes.

3 Q. And how is it -- assume for a moment
4 that this is case in the Southwest, okay?
5 Let me just -- I'm not asking you to --

6 A. You might want to put someone from
7 the Southwest on so we don't have to assume
8 something.

9 Q. Well, I'm going to ask you a
10 technical question with that assumption.

11 A. I just hate the word or definition
12 of assume, but I will try to help you.

13 Q. Yeah, at least half of it I don't
14 like.

15 So with that in mind, how can you --
16 I know how you are trying to justify a
17 reduction in or a change in the make
18 allowance in the Northeast, because of your
19 particular market situation. But how can
20 you justify, that to solve your problem in
21 the Northeast, that the producers in the

1 Southwest need take a significant reduction
2 in the prices they receive for the milk they
3 sell into cheese?

4 A. Well, I think that certainly the
5 cost of making cheese in the Southwest
6 should be taken into consideration. I
7 believe we have, or we tried to, at least.
8 And then once those costs are made, I -- the
9 impact on producers, it's unfortunate. None
10 of us want to see the producer price fall.
11 However, if the price is not adjusted, our
12 concern is that the plants will not be able
13 to stay in operation.

14 I can say that for our plants. I
15 can't say for the Southwest plants. It may
16 be an entirely different situation in the
17 Southwest, which is something that I think
18 your witnesses are welcome to show.

19 Q. But you would agree, would you not,
20 that the need that your members and
21 producers in the Northeast would provide the

1 butter, you know, you have the butter plant
2 and the like, for a market there is not one
3 that is shared by the producers of the
4 Southwest?

5 A. I would think all producers need a
6 market.

7 Q. I mean that particular market, the
8 particular markets that you are -- the plants
9 that you are trying to maintain.

10 A. I don't think so, but I don't know
11 that. We don't operate in the Southwest. I
12 very rarely even go there, so.

13 Q. I'll have to bring you down.

14 A. Well, perhaps that would be a nice
15 trip.

16 Q. Now, you indicated that you are
17 going to have somebody speak on behalf of
18 the plant?

19 A. Yes.

20 Q. Okay. So we are going to save some
21 of these questions for him.

1 A. Thank you.

2 Q. You are welcome.

3 Are you going to have any of your
4 members testify?

5 A. No. That's -- that's why they hire
6 me to do that.

7 Q. In your proposal, as taken fully, is
8 that it has the impact of reducing the price
9 for Class I and Class II milk, is that
10 correct?

11 A. With my proposal, unfortunately,
12 that will also be an impact.

13 Q. Now, let me back up on to another
14 question. Does Agri-Mark purchase any raw
15 milk from other than its members for any of
16 its plants?

17 A. Oh, yes, we do.

18 Q. And are those routinely -- I'm not
19 looking for specific amounts, but do you
20 purchase any of that milk at higher than a
21 Class III or IV price?

1 A. Routinely, yes, we do. It's a
2 competitive situation in the Northeast. In
3 the last few months we have had to lower
4 those prices because we have had these
5 losses, and our members are getting reblends
6 of losses, continuing reblends, so we
7 couldn't justify paying outside milk coming
8 in. So the whole premium level is affected.

9 But technically, we normally end up
10 doing that because there is a competitive
11 situation for milk, and we try to maintain
12 that competitive relationship.

13 Q. So the value of Class III milk in
14 that market, at least between plants or
15 plants purchasing it, is higher than the
16 Class III price? The competitive value --

17 A. Not anymore, it isn't because of the
18 make allowances. But in the past, has it
19 been at times? Yes, it has.

20 Q. In the recent past, has it?

21 A. Probably in the last two years or

1 so. Prior to the last two years, that --
2 yes, it was. It was -- it was some
3 premiums, they usually tended to be far less
4 than Class I premiums, for example. But in
5 order to obtain the milk from farmers and be
6 competitive, you have to charge more because
7 if you don't, you are going to lose the milk
8 out to other players in the marketplace.

9 Q. So from producer standpoint, you
10 know, in the equation of buying and selling
11 milk, from the producer standpoint, they are
12 viewing their milk more valuable than what
13 the product yield formula the Department is
14 saying that it's worth. Is that a fair
15 statement?

16 A. I think the producers you had this
17 morning clearly believe their milk is worth
18 more than that, and I would say most farmers
19 do. No farmer right now is happy with the
20 prices of milk. And, in fact, I even had
21 farmers back in 2004 who had higher -- that

1 felt they had higher costs.

2 I mean, there's an old adage that I
3 was once told by an extension agent that,
4 you know, most farmers believe that the cost
5 of producing the milk is always a dollar
6 higher than the price, so whatever that
7 price is. But farmers -- I don't know too
8 many happy farmers in regard to price.

9 Q. I understand. But you were
10 mentioning that the competitive situation in
11 your marketplace to acquire milk from farms
12 or nonmembers, whatever source that was, is
13 that you felt that you had to pay the Class
14 III price plus some additional money in order
15 to acquire that milk?

16 A. Yes.

17 Q. And is that not a classic definition
18 of what the value of that particular milk is
19 because it's between a willing buyer and
20 seller and --

21 A. Okay. Keep something in mind,

1 though. One of the reasons we do that is
2 because we do have a value-added business
3 that earns us additional money, so we can
4 take some of that money and apply it in that
5 direction. If we were making commodities
6 products, we perhaps wouldn't be able to do
7 that. So we have some opportunities there
8 because our members have invested \$40
9 million in equity and \$150 million in
10 assets.

11 Q. Well, let's --

12 A. So that's to benefit everybody.

13 A. That's a great point. I want to
14 bring that up. That formula that we use in
15 the federal is basically a base commodity
16 formula, right?

17 A. Yes.

18 Q. It's a proxy for coming up with a
19 Class III price, but it doesn't necessarily
20 represent what any plant anywhere in the
21 country is selling its cheese for or

1 yielding for its cheese or the cost to
2 produce that cheese, right?

3 A. No, it's the exact opposite, in
4 fact. My understanding is the NASS survey
5 of hundreds of plants as -- as to what their
6 actual price is. So I think it's a very
7 real price with regards to most plants and
8 most cheese.

9 Q. For those plants that sell and
10 report -- but your plants don't report to
11 the NASS on the cheese?

12 A. No, but we compete with those people
13 who do. And we also view that as an
14 alternative way to buy our cheese.

15 Q. But the make allowances that you
16 reported are not the make allowances
17 reported to produce a commodity cheese
18 that's sold on NASS?

19 A. Well, we did our best to try to get
20 to our basic cheese production loss, and we
21 used Charlie's instructions to get to that

1 level. But, I mean, our plant could very,
2 very -- any one of our plants could
3 participate in the NASS if we didn't have a
4 value-add business. But because our plants,
5 you know, tend to be smaller -- a lot of
6 that is because of the region we operate, the
7 age of the plants, things like that -- our
8 costs do tend to be higher, absolutely.

9 Q. When we were talking about prices of
10 non-members, or your members, are you paying
11 near a blend price or -- on the actual
12 checks that go out to your members?

13 A. Right now we have just had to
14 institute a 30-cent assessment based on the
15 losses from last year that are continuing,
16 so the net amount received by producers is
17 going out of the blend.

18 Q. By 30 cents or --

19 A. Probably a little less than that,
20 Ben, because we do collect Class I premiums.
21 And so, we try to distribute that to members

1 as best we can. Most of that goes in the
2 form of quality premiums because most
3 farmers -- it's one thing to lower -- if we
4 had a base premium, every member was getting
5 something, a premium, but once you start
6 paying quality premiums, most farmers feel
7 they have earned those quality premiums, and
8 it is very difficult to weigh.

9 So we take our Class I premiums and
10 we try to blend them across. I think the net
11 amount is the reduction below the blend that
12 farmers receive, but it may be to the extent
13 of 10 or 15 cents, right? But it's also -- I
14 need to point out one thing. It also is
15 likely to be at 30 cents below their neighbor
16 who is not an Agri-Mark member.

17 Q. So outside of Agri-Mark, many of the
18 plants are paying a blend price or higher?

19 A. The Class I plants certainly are.
20 There may be some co-ops who are reblending
21 or -- there isn't -- there isn't a whole lot

1 of manufacturing plants that provide milk
2 directly from producer. We know, for
3 example, that the Class I plants are, and
4 that's often the area where we have to try
5 to be competitive to keep our milk supply.

6 Q. Now, if the Department were to adopt
7 your proposal, how would that affect your
8 price to your producers as compared to the
9 blend?

10 A. The 30 cents represented the losses
11 that we had. And so, that will actually
12 continue for probably a good part of this
13 year because they represent last year's
14 losses. But current losses would no longer
15 continue. And then, at that point, our
16 farmers would probably be paid closer to what
17 their neighbors are getting.

18 Q. In terms of their relationship to
19 the blend?

20 A. Yes.

21 Q. But the overall blend would also be

1 reduced?

2 A. Right, that would be -- that cost
3 would now be shared among all producers
4 instead of just my members.

5 Q. And you indicated that, you know, I
6 think, that it's the case for the most part
7 that you have balancing plants. Those
8 balancing plants have some extraordinary
9 costs, right?

10 A. Yes.

11 Q. Is your powder plant one that you
12 actually will shut down for periods
13 throughout the year or does it operate most
14 of the year?

15 A. It operates all year long. A powder
16 plant is, of course, most needed in the
17 spring flush period when we've got additional
18 milk production. But also, a powder plant is
19 needed, for example, on the weekends, where
20 Class I operating plants -- most Class I
21 plants in our area do not operate seven days

1 a week; they operate either five or six. So
2 on Sunday, suddenly our plant goes from
3 having no milk to full. If there is a
4 holiday, for example, might be a three-day
5 weekend in the fall, then our plant may
6 operate for two or three days during that
7 period.

8 But that may be something, also,
9 that Mr. Langworthy probably should address.

10 Q. You indicated that you have Class I
11 premiums. Part of those Class I premiums is
12 to cover some of those costs of balancing
13 those plants, is it not?

14 A. We receive premiums that are
15 competitive out there, and some of them --
16 unfortunately, some of the money goes to
17 cover that. It's -- there is a cost to it,
18 but there is also -- of the plant, but there
19 also is a benefit to having the plant. It's
20 a benefit to the whole marketplace by trying
21 to maintain some over-order premiums that are

1 higher.

2 Q. You indicated in page 3 of your
3 testimony that the amount of cheese
4 utilization has dropped dramatically?

5 A. Yes.

6 Q. Is this because of a structural
7 shift in the national dairy market, that
8 production of cheese in the Northeast is
9 declining and that milk is going more into
10 national markets either in the Northeast or
11 in the Southeast?

12 A. No, I don't believe so. We have had
13 milk production shift in 2004 going down, but
14 now we are bouncing back up again, and the
15 milk is not coming back into the cheese
16 plants, the cheese plants aren't taking it.
17 I noted in my testimony that powder, for
18 example, is now absorbing more of that milk.
19 It's not only becoming a Class I balancer,
20 it's balancing total milk supplies in the
21 past that it hasn't done.

1 Q. Now, at the bottom -- I want to just
2 move along in your testimony -- you mention
3 this situation with the powder and the NASS
4 survey, and there was an agreement to add an
5 energy surcharge, so you sold it and reported
6 it. And then it seemed to come back to bite
7 you because it showed up and went to
8 producers and didn't go to the plants. Is
9 that a fair statement?

10 A. Yes.

11 Q. So that issue is not only one of
12 make, but it is also an issue of the method
13 of capturing the price of the product, right?

14 A. It's the method of capturing the
15 price of the product? It's -- if we could
16 exclude some of those additional costs, for
17 example, in the NASS price, then we wouldn't
18 be here, because we tried to do that. But
19 the NASS, understandably, from their point of
20 view, wants to grab the entire price that's
21 paid.

1 Q. I understand that. But maybe -- but
2 there -- by changing the price -- you know,
3 there are three parts to the price formula,
4 the price series that allows for the make
5 and the yield that is paid. But if the price
6 series were adjusted, for example, to allow
7 you to exclude energy costs or energy
8 surcharges that you are able to pass on, then
9 you would have been able to offset or
10 mitigate some of your increased energy costs
11 without passing that on to the producers,
12 right?

13 A. Yes. You could do this in two
14 different ways. You could do the make
15 allowance in the Federal order, or we could
16 make a set adjustment to the NASS price and
17 decrease the NASS price by a certain amount
18 of money. In a way, USDA already impacts the
19 NASS price by adding 3 cents to the barrel
20 price to cheese before they make their
21 calculation.

1 I mean, that's another way to do
2 that. But we thought that it was easier to
3 directly approach it. Since make allowance
4 is supposed to represent the manufacturing
5 cost, we should be talking about that change
6 in manufacturing cost and then insert it in
7 the formula accordingly.

8 Q. Moving on in your discussion of the
9 whey products on page 4, you are making a lot
10 of whey protein concentrates?

11 A. Yes, we make whey protein
12 concentrate, 80 percent protein. We do on
13 occasion, I believe, make 40 percent at
14 times, but we generally don't make any whey
15 protein -- I'm sorry, whey powder. But
16 that's also something -- I don't mean to keep
17 pointing to Mr. Langworthy, but he can tell
18 you exactly what we do there.

19 Q. Okay, and we'll discuss those costs
20 with him.

21 Do you make any whey protein

1 isolates?

2 A. I don't believe we do. Oh, we make
3 lactoferrin, which is a very, very small
4 amount of product from it. And please ask
5 Mr. Langworthy the details about lactoferrin.
6 That's a complicated issue.

7 Q. The costs, and I think we would all
8 probably agree, to create whey protein
9 concentrates is a much different and a higher
10 cost than just to make a dried whey powder?

11 A. Oh, absolutely.

12 Q. And presumably, there is a yield or
13 a return on the other side to justify --

14 A. There is a higher price to it.

15 Q. Right.

16 A. That's why, you know, we didn't put
17 any numbers in on Charlie's survey on that.
18 We didn't think that was appropriate. And I
19 used some of our numbers there, for example,
20 on our ROI, GNA and others, to try to get at
21 those numbers. But ours are much higher, and

1 nationally, they're much higher.

2 Q. Well, let's talk about the Ling
3 study. Based on this exhibit that we just
4 had, which is, what, 35?

5 THE JUDGE: Yes, sir.

6 BY MR. YALE:

7 Q. There is a significant change in the
8 number of participants in the plants --

9 A. Yes.

10 Q. -- from 1998?

11 A. 1998.

12 Q. Were you part of any effort to lobby
13 or get other plants to sign up to this study?

14 A. I believe I was the effort.

15 Q. You were the effort?

16 A. Yes. Would you like me to go into
17 it in more detail?

18 Q. Yes.

19 A. Okay. Sure. We felt that the
20 fairest way to affect the -- to calculate the
21 make allowances was to redo Charlie's study

1 and then use that and the California numbers,
2 update what USDA had used before. So the
3 first thing we needed, we needed to make sure
4 Charlie's study was done.

5 And my intention in doing Charlie's
6 study was to have as many plants as possible.
7 So I went over the information for the last
8 seven or eight years I had handy in my office
9 and looked at all co-ops who had participated
10 in Charlie's study.

11 So I contacted all those co-ops and
12 said, would you be willing to participate in
13 this study again? And the ones who said yes
14 are listed on the list.

15 Some, like Bongards Dairy, they're
16 not owned by co-op. California, I didn't
17 want to repeat the same problems from last
18 time, so I didn't contact anybody in
19 California.

20 And then I contacted Charlie, and I
21 said, Charlie, are you willing to do this?

1 And he said, well, he was, but in his role,
2 he has to be contacted by the co-ops, asking.

3 So I said, well, I will be
4 contacting you and I will talk to these other
5 co-ops. So we all contacted Charlie and,
6 hence, how the procedure began.

7 Q. And your goal was to come up with a
8 different make allowance?

9 A. Our goal was to come up with a
10 realistic one representing our current costs,
11 yes, it was.

12 Q. In 2002, I think it was, the
13 Department came out with the final, final
14 decision on the Class III and IV make --

15 A. Might have been April 1st of 2003,
16 but --

17 Q. Well, maybe that was when it was.

18 A. When it was effective, yes.

19 Q. There was a lawsuit filed to
20 challenge the final decision. Do you recall
21 that?

1 A. I don't recall that, but I can't say
2 it didn't happen.

3 Q. Agri-Mark hasn't participated in any
4 lawsuits to challenge any of the decisions
5 modifying the make allowances or yields?

6 A. No, not that I'm -- I don't believe
7 so. I guess after this morning we got in
8 enough trouble for being in the hearing, the
9 one in 2000, with Option 1A and 1B. But,
10 no, we haven't as far as I'm aware. And I
11 would be aware. I'm just --

12 Q. I couldn't recall. That's why I was
13 asking the question.

14 A. Yes. I don't believe so.

15 Q. The -- you talked a little bit ago
16 about the Class III or the -- I'm sorry, the
17 cheese and the 3 cent barrel to block
18 conversion. And you use that on page 5 as an
19 argument to basically ignore the larger
20 plants in California for the blend of the
21 pricing because they tend to be making

1 500-pound barrels or 640 blocks, right?

2 A. Well, not so much in California that
3 I made the argument. I was really making the
4 argument in regard to Dr. Ling's studies. He
5 has the price for all cheese, and then he has
6 for cheddar cheese. And because there is
7 block and barrel in the all cheese, we think
8 that probably that's -- that's probably the
9 difference, for the most part, between the
10 block group only and the total cheese group.

11 So what I did was I said, okay, if I
12 know that the block group, how much that
13 costs, and I know the total group, how much
14 they cost, I just found the difference and
15 said, okay, the plants who are in the all
16 cheese but who are not in the block cheese,
17 okay, what are their costs? And they were
18 exactly 3 cents lower than the block cheese
19 plants.

20 From that 3 cents, and knowing there
21 were -- a lot of them were barrel plants, I

1 surmised that that, maybe, is the reason that
2 they are 3 cents lower and, indeed, USDA adds
3 3 cents to the cost. That was my logic in
4 doing that.

5 Q. But the NASS survey includes
6 barrels?

7 A. It includes barrels. And then the
8 Department adds 3 cents to it before they do
9 their calculation.

10 Q. Right.

11 A. Yes. And I believe the 3 cents was
12 supposed to reflect the price difference
13 relative to manufacturing. At least, that
14 was my understanding.

15 Q. Now, in the -- this idea of blending
16 these two tables together --

17 A. Which table?

18 Q. I mean the two studies, the Ling
19 study and the California.

20 A. Yes.

21 Q. You would have to agree, would you

1 not, that there are some major differences
2 between the two studies in terms of who they
3 are performed on, what their purpose is, and
4 how the studies are done?

5 A. Yes, there are. Unfortunately,
6 there's not a whole lot of other
7 alternatives. But, yes, there are
8 differences.

9 Q. For example, in California, when we
10 had the young lady yesterday testify that
11 they do the auditing to make sure the numbers
12 -- and Dr. Ling just basically takes the
13 numbers as he has them, right?

14 A. Right. We think at some point in
15 the future USDA should have a formula in
16 there that is audited by the Market
17 Administrators and accomplishes the same type
18 of goal. But unfortunately, they don't have
19 that right now.

20 Q. And they deal with a block barrel
21 differently than USDA does, right?

1 A. I believe, but I don't know a whole
2 lot about California pricing. But that's my
3 understanding.

4 Q. As I understood, her testimony was
5 -- and correct me if you understood it
6 differently -- was that they look at what
7 those costs are in terms of the packaging
8 and labeling associated with the 40 pounds
9 versus the barrel and make an adjustment to
10 the barrel cost. But they handle it
11 differently than the USDA does, right?

12 A. Okay. Whatever the record shows. I
13 don't know that much about it.

14 Q. But the cost of the barrels in the
15 640s, we don't even consider 640s in the
16 Federal system, right?

17 A. The cost of the -- the price of
18 640s?

19 Q. Yes, the pricing of 640s is not part
20 of our formula, right?

21 A. I believe it is not included in the

1 NASS piece, as far as I know.

2 Q. Right. It may or may not have been
3 included in the Ling study, you don't know?

4 A. I guess he did say something about
5 640s, and -- but I don't -- he has a
6 footnote relative to 640s, so I believe it
7 is.

8 Q. The California plant also includes
9 proprietary claims study, right?

10 A. I guess so.

11 Q. And your study doesn't include any
12 proprietary claims?

13 A. No. Once again, it was the
14 cooperative service; we used a study that
15 was already available. We think that in the
16 future, if there is a survey being done, it
17 should be all plants, or at least a random
18 sample of all plants, of all size plants.

19 Q. There are procedures involved in
20 California that are not in Ling. For
21 example, they actually go out and inspect

1 the operation and get a feel for how things
2 move to follow the cost as well. And Dr.
3 Ling indicated, for saving taxpayer's
4 dollars, he doesn't make those planned
5 visits, so he is not able to tie in an
6 actual, physical inspection with the numbers.

7 A. That is the case.

8 Q. Right. The plants in California,
9 they also reported a significant difference
10 in the yield in those plants?

11 A. Well, I'm a little concerned. The
12 intent of Charlie's study was to try to get
13 at the cost piece. And so, this 10.7 yield
14 looks really weird to me.

15 I don't have a lot of confidence in
16 Charlie's numbers. He didn't go in and look
17 at how much milk went in, how much cheese.
18 You know, he just said how much milk do you
19 get in the plant, how much cheese do you get
20 back, and then calculated a yield. I don't
21 know what else is going on at that plant. I

1 don't know if they are getting in condensed
2 product. I don't know if they are using,
3 God forbid, MCP, milk protein concentrate.
4 They could do that very easily.

5 And if that's the case, then they are
6 getting a yield not from producer milk but
7 from others.

8 I don't know. And I would -- it's a
9 shame. Maybe Charlie should have gone after
10 me again because I would have asked him does
11 he have a lot of confidence in those.

12 Someone may have asked that. Perhaps the
13 record shows that.

14 Q. But the study that he has provided
15 indicates they made, that allowances,
16 averages that he's averaged out from all your
17 17 cheese plants, I think it is, that yields
18 a -- what he reports as a 10.7 yield,
19 however he got that, that that's what it
20 says, right?

21 A. Yes, but I'm just saying that at the

1 hearing that established the current yields
2 under the Federal order, we had elaborate and
3 lengthy testimony about those yields, and we
4 had people who went in and looked at those
5 yields. We had experts such as Dr. David
6 Barbano from Cornell and others. So we have
7 a lot of confidence in those yields that
8 were in that formula. This number is a
9 secondary number that I'm just concerned
10 about using it to that extent.

11 Q. Well, let me bring the point,
12 though, is that if I wanted to make a plant
13 that yielded 9.5 or 9.8 9.9, whatever the
14 yield is, comply to the formula, those costs
15 to produce a commodity cheese at that yield
16 may be at a lower make than one to produce
17 one at 10.5, because there are added costs
18 associated with getting those higher yields.
19 You would agree with that, right?

20 A. No, I don't know if there's higher
21 costs in getting to that higher yield. I

1 mean, I don't know what the costs are. If
2 there are any MPCs, does that add a lot of
3 costs by putting some bags in the vat? I
4 don't know. We don't do it. So I couldn't
5 answer that question.

6 Q. Or if they brought in equipment to
7 recycle the whey butter and get a higher
8 butterfat recovery in the processing of
9 cheese than the 90 percent, would --

10 A. There might be. I want to make it
11 clear, though, we get a higher butterfat
12 recovery, but we never recycle the butter.
13 We just happen to get that piece, but --

14 Q. That's fair. But the point is,
15 though, is that the make allowance, can you
16 really divorce the make allowance from the
17 yield?

18 A. I think the make allowance, the
19 yield was already considered in detail. If
20 -- I think if you are going to use a 10.7
21 yield, you really need to go in and look at

1 a lot more details.

2 Can you divorce the two? No, and
3 that's why the original hearing looked at in
4 great detail both issues.

5 Q. Right. But what we don't know by
6 this information is that, of those make
7 allowances, whether or not -- I'll give you
8 this issue, that whether or not a higher make
9 allowance that this 2004 study shows as
10 compared to 1998 also accounts for a higher
11 yield. We don't know that, whether that's
12 the case or not, right?

13 A. Because I don't -- I would have to
14 say yes because I don't know what the true
15 yield is. But we don't see yields of basic
16 cheddar cheese technology changing
17 dramatically from there unless you were to
18 do something that -- at least, most cheddar
19 cheese plants that I'm aware of don't put in
20 -- let's say block cheddar. I don't know of
21 any block cheddar that uses MPCs to make

1 cheese like, for example, an Italian cheese
2 plant would do. But perhaps Mr. Langworthy
3 would be aware of some in his operation
4 experience.

5 Q. Now, as we continue to talk about
6 yields, you said there was extensive
7 testimony about yields and everything. Are
8 you aware of the butter price, the yield that
9 was calculated for the butter and the
10 formula and the final decision and the shrink
11 that was applied to that?

12 A. I was aware of it back then, but
13 with all these other numbers I'm dealing with
14 right now, I couldn't recall it.

15 Q. Are you a numbers person?

16 A. I used to be when my memory was a
17 lot better.

18 Q. So you wouldn't be able to talk
19 about that shrink issue?

20 A. No.

21 Q. On your nonfat dry milk, do you

1 produce dry buttermilk?

2 A. Yes, on occasion.

3 Q. Is that something that your cohort
4 will be able to talk about?

5 A. Yes, I think he can talk more about
6 that. In fact, I think probably it's more
7 than on occasion. I think we do other
8 things, but I think on a general basis, we
9 have to do something with it.

10 Q. And dried buttermilk is not
11 accounted for in the pricing formula, is
12 that right?

13 A. In terms of the yields of powder and
14 butter, it might be. I'm not sure. There
15 is nothing that says dried buttermilk or the
16 prices of dried buttermilk, but I believe
17 they did account for the fact that there are
18 some solids that have some value and they
19 factor that into the equation. I just don't
20 know what that factor is.

21 They don't allow you anything free

1 under the Federal orders.

2 Q. Well, we are not so sure of that.

3 A. Well, we're pretty sure these days.

4 Q. Going back to this weighted average
5 that you want to use between the two and the
6 different yields, let's -- let me create a
7 hypothetical. Let's say that you have two
8 plants of approximately equal size, and one
9 has -- that each of them have their own make
10 allowance and each of them have their own
11 yield. Should not the make allowance be
12 adjusted to the yield so that there is an
13 equation between the two for purposes of
14 this pricing formula?

15 A. Should the make allowance be
16 adjusted to the yield? I think every plant
17 has their own separate yield and make
18 allowance, but I think that's already done in
19 the Federal order. That's why we went in and
20 used a -- basically, if I recall right, we
21 used sort of an engineering approach to get

1 to that yield.

2 So, I mean, I think that the
3 averages on what a plant should be getting
4 under certain tests is already factored in
5 there. I mean, should we -- should
6 everybody have a different Class III price
7 based on yield and --

8 Q. That wasn't my question. My
9 question is, in deriving the formulas that
10 you propose, you want to take the RBCS
11 numbers and you want to take the California
12 numbers, or portions of each of those,
13 40-pound blocks --

14 A. Right.

15 Q. -- and then do a weighted average
16 between the two?

17 A. Yes.

18 Q. And my question is, should you not
19 also have to reflect that each of those have
20 different yields at those make allowances
21 and weight that as well?

1 A. I would have to think about that.
2 Like I said, I think there already is a
3 yield portion in the Federal orders. And I
4 don't know if it's different from
5 California. I mean, in our real-world
6 situation, what we would have preferred to do
7 is actually go in and look at just Federal
8 order plants and not look at California at
9 all because we're dealing with Federal order
10 pricing. And then this wouldn't be an issue
11 because the Federal orders used a yield
12 factor in regard to that.

13 But I also believe that the Federal
14 orders use a yield factor that wasn't unique
15 to Federal orders, it was unique to
16 manufacturing of that product. Whether
17 California uses something different on that,
18 I don't know. But we are not proposing
19 doing that.

20 Q. I want to get into the area of --
21 I'm kind of switching gears from talking

1 about yield and stuff and talking about the
2 impact of this price.

3 As you have explained that you had
4 this difficult situation in the Northeast
5 where the -- for whatever the reasons are,
6 avoidable, unavoidable, good, bad or
7 whatever, your cost to produce, according to
8 you, is higher than what the make allowance
9 allows for under the Federal order formula,
10 right?

11 A. We specifically had that in the
12 Northeast, but I believe there will be other
13 proponents that --

14 Q. I understand, but we are talking
15 about doing the Northeast.

16 A. Yes.

17 Q. And part of that, is it not -- isn't
18 this not the case, that there has been this
19 ongoing structural shift in the dairy
20 industry nationwide, both in terms of where
21 the milk is produced, where the plants are

1 located, the size of the plants, the size of
2 the producers, their relationships to the
3 markets, that there is this structuring going
4 on? And whenever there is that kind of
5 structuring, there are going to be areas
6 that tend to benefit from it, and there are
7 areas that are going to lose. And
8 historically, they tend to be the older
9 areas, such as the Northeast, as opposed to
10 the others.

11 I mean, does that sound like a
12 general -- I mean, do you agree or disagree
13 or have any comment on that statement?

14 A. Things change is sort of a summary
15 of what you said, and things change, but I'm
16 not sure if those changes have a lot of do
17 with the make allowance. But things do
18 change.

19 Q. Well, that's my point. That's where
20 I want to head, is that is this change in the
21 make allowance truly going to, long-term,

1 benefit the Northeast and, generally and
2 specifically, Agri-Mark? And let me point
3 this out, is we had some producers testify,
4 and I think honestly --

5 A. Absolutely.

6 Q. -- that a reduction in 25 or 30 or
7 40 cents is going to have an impact on their
8 ability to maintain their operations. And I
9 think you would agree with that, right?

10 A. Oh, I think that -- that initial
11 impact -- when this first goes into effect,
12 I don't even disagree that that's probably
13 going to be the impact, at least for, you
14 know, a couple months.

15 Q. Right.

16 A. Over time, I think what USDA has said
17 will be correct.

18 Q. Right.

19 A. Initially, yes.

20 Q. And would you not also agree that
21 you still have a significant number of the

1 traditional sized farms with the older
2 operators in your area and in your
3 membership?

4 A. Yes, but their -- keep in mind,
5 their price also moves for a lot of
6 different reasons. Yesterday, I believe, at
7 the exchange the block of cheese price went
8 down 40 cents, which will probably result in
9 a 40-cent price, and that's terrible for
10 farmers.

11 Q. I understand. But I'm just talking
12 about -- we are talking about the one that
13 we are involved in. I can't --

14 A. No, but you are talking about what
15 is the impact of a drop in the farmer price,
16 and I'm saying any impact is terrible with
17 regard to the farmer price --

18 Q. Right.

19 A. -- and there's a lot of causes for
20 that impact.

21 Q. I understand, but we're talking

1 about the cause of -- this hearing has the
2 potential of having its own cause,
3 independent of the others. And my question
4 is, is that are you not, in its own way,
5 having kind of a law of unintended
6 consequences if you are going to create an
7 exodus of production of producers in the
8 Northeast that speeds up this structural
9 change, not necessarily to the benefit or
10 Agri-Mark or its plants?

11 A. Well, it certainly -- if we don't
12 correct this right now, our farmers are
13 bearing that cost right now.

14 Q. Right.

15 A. So they have -- they have this
16 30-cent reblend. So our farmers are going
17 to go out -- either go out faster for the
18 same reasons those people went out for.
19 They are impacted the exact same. So, you
20 know, they could go out or they are going to
21 leave our organization. And then we won't be

1 able to support our plants and do other
2 things.

3 So our members are already being
4 impacted by that. And I think that if we
5 lose -- if we don't correct this, it sends a
6 signal that the Federal orders --
7 manufacturing in the Federal orders creates
8 a serious problem, and maybe you should move
9 out to the Southwest where there are some
10 alternatives. And, you know, as plants
11 leave, farmers are going to have fewer and
12 fewer opportunities for their milk.

13 And, I mean, nobody likes a low
14 price, but there is something worse than a
15 low price, and that's no price. And that's
16 if nobody wants your milk, you have got to go
17 searching all the over the place, it creates
18 disorderly marketing, it increases
19 transportation costs, which could be far
20 above 30 cents, depending on where the milk
21 has to move.

1 So there is a law of unintended
2 consequences whether you do something or not.
3 That's part of the problem.

4 Q. And I guess the answer to the
5 question is that we may or not totally solve
6 all the problems, but we may create or speed
7 up -- once we get away from just the issue
8 of Agri-Mark and we look at the market, it
9 could have an impact on the market?

10 A. Well, absolutely, it could have an
11 impact on the market. You know, right now we
12 have a serious problem, a direct problem
13 that we think we have been able to measure
14 or at least attempt to measure on what's
15 going at Agri-Mark and, we believe, some
16 other manufacturers.

17 Q. And you would agree that that, at
18 least by your testimony, is a regional issue
19 to the Northeast?

20 A. It certainly is a regional issue. I
21 believe it's further than that, but

1 definitely to a regional. In fact, I would
2 just add to that, I believe it is a regional
3 issue in the Northeast, a regional issue in
4 the Northwest and the Southwest and the
5 Southeast and Central. I believe it's just
6 an impact that I think everybody is
7 impacted, but I can tell you what our
8 impacts are for the Northeast. I can
9 document that.

10 Q. I think we are about to wrap up
11 here. I'm a lawyer that said that, so be
12 careful.

13 A. I see you have two other colleagues
14 here, so I'm very careful.

15 Q. You, at the end of your testimony,
16 stated you wanted to have an interim
17 decision. You still -- you have asked for
18 an expedited --

19 A. Yes.

20 Q. -- and a decision without a
21 recommended decision. You want to be able

1 to go to a final order or at least an
2 operative decision from the Department as
3 quickly as possible, right?

4 A. Yes.

5 Q. You are not, by using the word
6 interim, suggesting -- or maybe I shouldn't
7 say that. Let me phrase it this way.

8 You are still hoping that the
9 Department has, with this hearing record,
10 the opportunity for subsequent comments for
11 them, if necessary, to make adjustments under
12 this hearing record to that interim decision
13 if something is less than perfect? Or do
14 you want it just to be over with, the hearing
15 done and nothing further?

16 A. It's sort of like this testimony. I
17 would like it to be over as quickly as
18 possible.

19 Q. Completely?

20 A. Completely. But, however, we
21 recognize that the Department needs to do

1 what they need to do. We have asked the
2 Department to do something that is not
3 typical. It is not unusual. They have done
4 it in the past. But it is not something
5 that's normally their procedure.

6 So it is going to be up to their
7 view. We just want relief from this as soon
8 as possible and the fastest way possible.
9 Now, if they want further comments, I don't
10 have an issue with that.

11 Q. You have indicated, and I think over
12 the years you have always indicated that
13 Agri-Mark and you, personally, have strong
14 support for the Federal order program?

15 A. Oh, absolutely.

16 Q. If the effect of this decision in
17 some regions is to call producers to
18 consider whether they want to continue the
19 Federal orders program in their area or
20 possibly terminate because it's no longer to
21 their benefit, do you see that as a benefit
22 in your area or not?

23 A. It depends on the area involved.
24 For example, I guess there was an order voted
25 out in Utah area that had no impact that I'm
26 aware in our area. I wouldn't want any other
27 group hurt, of course. I mean, our goal is
28 not to hurt anyone.

29 If it was -- if we voted out, for
30 example, in Ohio or the Appalachian, I don't
31 think that would be the case. But if it
32 were, sure, that could have an impact.

33 Q. So it's proximity to your market
34 that --

35 A. I think basically on that. But
36 also, we feel if the Department does not do
37 this, that that yields to disorderly
38 marketing and other things that they really
39 -- they need to do, and that's why -- often
40 why orders decisions are all or nothing in a
41 situation.

42 Q. I have no other questions. Thank
43 you.

44 THE JUDGE: Very well. It looks like
45 it's about 5 of 12. So we'll take our lunch
46 recess at this time. Let's be back at 1:25.

47 [Whereupon, the hearing recessed
48 at 11:53 a.m. and reconvened at 1:23 p.m.]

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JANUARY 25 - DAY 2 - AFTERNOON SESSION

THE JUDGE: We are back on the record. Are there additional questions of Mr. Wellington? Yes, sir. Mr. Rosenbaum.

MR. ROSENBAUM: Good afternoon, Mr. Wellington.

THE JUDGE: Would you identify yourself again for the record, please.

Ladies and gentlemen, let's have some order, please.

MR. ROSENBAUM: I'm Steven Rosenbaum appearing for the National Cheese Institute.

EXAMINATION

BY MR. ROSENBAUM

1 Q. Now, Mr. Wellington, I wanted to
2 follow up to some questions you were asked by
3 Mr. Yale in his examination.

4 Now, if I understand your proposal
5 correctly, you are not asking that the make
6 allowances be based upon Agri-Mark's own
7 costs; is that correct?

8 A. No, it would just be a factor within
9 those costs, but not based upon our costs.

10 Q. And when you say that Agri-Mark would
11 be a factor in those costs, you would be a
12 factor insofar as your plants were one of the
13 many participants in the Rural Business
14 Cooperative Survey; is that correct?

15 A. That is correct.

16 Q. And other than that -- well, let me
17 start that again. And so, to the extent that
18 you submitted your costs, those would be
19 weighted based on your production just like
20 everybody else?

21 A. Correct.

1 Q. And the fact that you are proponents
2 does not itself carry any greater weight to
3 your costs than any other plant the
4 Department surveys, is that right?

5 A. That is correct.

6 Q. And if you could just take your
7 testimony, please, which is Exhibit 29 -- and
8 I'm going to be flipping back between Table 3
9 and Table 7, so maybe you could just sort of
10 have those both handy.

11 A. Yes.

12 Q. Now, Table 3 sets forth, sort of in
13 the middle of the page, a row called, Total,
14 correct?

15 A. Now, which -- okay, yes.

16 Q. Actually, there are two of them.
17 But about the middle of the page, above where
18 it says FNMO manufacturing allowance, above
19 that there is something called, Total,
20 correct?

21 A. Yes.

1 Q. And those -- with respect to cheese,
2 butter and nonfat dry milk, those represent
3 Agri-Mark's own -- essentially your own
4 costs of make, is that correct?

5 A. Yes.

6 Q. All right. And I believe you
7 testified with respect to whey powder, that
8 in fact is not your cost, that's just --
9 because you don't really make whey powder as
10 such, correct?

11 A. That is correct.

12 Q. So that your cost -- your cost of
13 make for cheese is 22.8 cents per pound,
14 correct?

15 A. Yes.

16 Q. And then flipping over to Table 7,
17 the make allowance that you are proposing is
18 set forth in Table 7, correct?

19 A. Yes.

20 Q. And that you are proposing a make
21 allowance for cheese of 18.1 cents, correct?

1 A. Yes.

2 Q. So even if your proposal is
3 accepted, the make allowance that you will be
4 entitled to, in fact, will not cover all of
5 your costs, correct?

6 A. That is correct.

7 Q. You will be reducing your losses but
8 not eliminating your losses, correct?

9 A. Correct.

10 Q. And similarly, for butter, your cost
11 of make for butter is 21.1 cents, whereas
12 the make allowance that you, yourself, are
13 proposing is only 15.4 cents, correct?

14 A. That is correct.

15 Q. And similarly, for nonfat dry milk,
16 your cost of make is 21.2 cents, and you are
17 proposing a nonfat dry milk make allowance of
18 19.7 cents, correct?

19 A. Yes.

20 Q. And so, in all three cases the make
21 allowances are not sufficient to cover your

1 costs, correct?

2 A. Yes.

3 Q. Now, do I understand correctly that
4 the make allowances that you are proposing
5 follows the same essential methodology that
6 was used to set make allowance in 2000,
7 namely, it reflects a weighted average of
8 the cost in the California survey and the
9 costs of the -- in the Rural Cooperative
10 Business survey, correct?

11 A. Yes, although there's some subgroups
12 in California that are used a little bit
13 differently.

14 Q. Because you think that there is data
15 that now allows you to have more of an
16 apples to apples comparison than previously?
17 Is that --

18 A. Well, it's more of you look at the
19 size of the plants. We were considering
20 those. We actually said, given the size of
21 the butter plants, that perhaps we should

1 use all the butter instead of just the high
2 cost. That actually works against us, but
3 we thought that was fair. And powder on
4 powder we thought that, given the large
5 powder plants, that we would use the medium
6 cost ones by themselves because they were
7 much better representatives of a fairer cost.

8 Q. Now, the make allowances that you
9 are proposing, that would be sufficient to
10 cover the costs of essentially the weighted
11 average plants, so to speak. Is that right?

12 A. Yes.

13 Q. So that sort of by definition, even
14 if your proposal is accepted, half of all
15 the production will be at a price that's not
16 sufficient to cover their costs, correct?

17 A. That is correct, just like ours
18 wouldn't be sufficient, yes.

19 Q. And that's the same with the system
20 today, correct?

21 A. Yes.

1 Q. So that the -- that's the same as
2 the concept behind those that were set back
3 in 2000, correct?

4 A. Yes. Our intent was to copy that
5 concept.

6 Q. Okay. And if, in fact, the data
7 here is correct as to what the make
8 allowances -- well, let me rephrase that.
9 Your proposed make allowances reflect what
10 the data suggest are the actual costs,
11 correct?

12 A. Yes.

13 Q. And even if they are accepted, as
14 you just said, only half of the production
15 will be -- will have its costs covered by
16 these make allowances, correct?

17 A. Yes.

18 Q. So it must be that if today's make
19 allowance is something way, way in excess of
20 50 percent of production, it is at a level
21 that's not sufficient to cover true costs,

1 correct?

2 A. That's what our belief is, yes.

3 Q. Well, assuming the accuracy of the
4 California and RBCS data, that has to be the
5 case, correct?

6 A. Yes.

7 Q. Because, by definition, that data
8 suggests even with these higher prices that
9 you are supplying for the make allowances,
10 you are still only going to cover only half
11 -- only half of the production will be able
12 to cover their costs, correct?

13 A. Yes.

14 Q. So considering the fact that the
15 current make allowances are, as you show in
16 Table 7, in every case materially lower than
17 you are proposing, then the percentage of
18 the plants that are not currently covering
19 their cost just has to go up and up,
20 correct?

21 A. Yes, it does.

1 Q. Now, a question -- let me switch,
2 then, to, if I could, Mr. Ling's chart that
3 -- Dr. Ling's chart, excuse me, that he
4 introduced this morning, Exhibit 35. Do you
5 have a copy of that?

6 A. Oh, of this morning's?

7 Q. Yes, this is the list of the plants
8 that were covered by the survey.

9 A. Yes, actually I do. Yes, I do.

10 Q. And let me focus, perhaps, just a
11 question as to cheese. And I just want to
12 sort of run down the geographic regions that
13 are covered by the survey because there were
14 some questions asked this morning as to
15 whether or not the data is really
16 representative or not.

17 There obviously is coverage in the
18 survey for plants in the Northeast. Those
19 are your own plants, correct?

20 A. Yes.

21 Q. And then there are also, as I count

1 them, eight plants from the Midwest, Upper
2 Midwest, Wisconsin, Minnesota, Iowa, correct,
3 Missouri?

4 A. Yes.

5 Q. And --

6 A. From two different co-ops.

7 Q. All right. And then questions were
8 asked about the southwestern United States.

9 In fact, there is a cheese plant in
10 Lovington, New Mexico, that's a participant
11 in the survey, correct?

12 A. Yes.

13 Q. And then there is also participation
14 -- oh, and I'm sorry. I said Upper Midwest.

15 I think I left out in my count the two
16 Wisconsin plants further down.

17 A. Right.

18 Q. So it's actually, I think, 10 plants
19 from the Upper Midwest, if I'm counting
20 correctly now. Is that right?

21 A. I would have to do the count myself.

1 I think there are nine.

2 Q. All right. Well, nine or ten.

3 A. Yes.

4 Q. And then you have three plants from
5 the Pacific Northwest, correct?

6 A. Yes.

7 Q. And that's, of course, just from the
8 RBCS survey, correct?

9 A. Yes.

10 Q. Because then, in addition, 98
11 percent of the production in California is
12 also is covered by the California survey,
13 correct?

14 A. Yes.

15 Q. And that also works into the make
16 allowance equation, too, correct?

17 A. Correct.

18 Q. You are somewhat familiar, I'm sure,
19 with cheddar cheese and cheese production, in
20 general, around the country, correct?

21 A. Yes.

1 Q. Is this representative and a sample
2 of the cheese production in the United
3 States, given the geographic diversity of
4 coverage here.

5 A. I think it is. We attempted do
6 that. There was no one left out of Dr.
7 Ling's study who had participated, like I
8 said, in the last 10 years. We approached
9 everybody to say, could you participate. We
10 were not intending to try to pick a group or
11 anything else. We just wanted the largest
12 population available to give, you know, the
13 best idea of what the cost would be for the
14 Department.

15 Q. Do you think you achieved that?

16 A. We hope so. We believe so.

17 Q. Let me switch now to the subject of
18 yield. You were asked a few questions about
19 that, correct?

20 A. Yes.

21 Q. You actually were the person who

1 asked Dr. Ling to perform the new make
2 allowance survey, correct?

3 A. I was the initial person. Each
4 person had to ask Dr. Ling separately, but I
5 was the first one.

6 Q. I take it you did not ask him to
7 perform a yield study, correct?

8 A. No, not at all.

9 Q. And he did not perform a yield
10 study, did he?

11 A. No, I think he just collected pounds
12 and -- pounds of milk and pounds of product.
13 I don't -- you know, you would have to
14 adjust it for a lot of other factors.

15 Q. Okay. And you participated in the
16 2000 hearing at which the current pricing
17 formulas were set for Class III and IV,
18 correct?

19 A. Yes, I did.

20 Q. And do you recall that there were a
21 number of food scientists who appeared and

1 testified in great deal detail as to the
2 appropriate calculation of your factors?

3 A. Yes. That's why I mentioned that
4 Dave Barbano, I believe, was one of them.
5 He's probably the premier person in our
6 minds with regard to that. And that's why I
7 -- I said it was sort of an engineering
8 approach to doing it. It wasn't looking at a
9 survey of plants, it was saying what should
10 be the plan.

11 Q. And as you understand what Dr. Ling
12 was doing when he has his number -- he does
13 have a yield number in his data, correct?

14 A. Yes.

15 Q. Now, from your understanding of how
16 he approached his study, would he have taken
17 into account, for example, farm to plant
18 losses?

19 A. No, they were not included, as far
20 as I know.

21 Q. And if you took into account farm to

1 plant losses of milk, does that lower the
2 yield?

3 A. Yes.

4 Q. And, in fact, is that something that
5 was taken into account by USDA when it
6 actually was looking at yield issues?

7 A. Yes, it was.

8 Q. And similarly, did -- when Dr. Ling
9 did his analysis, as you understand it, was
10 he standardizing per hundredweight the 3.5
11 percent butterfat, 5.7 percent other solids
12 and 2.9 percent protein?

13 A. No, he was not.

14 Q. And is, in fact, that
15 standardization reflected in the current
16 price formulas?

17 A. Yes.

18 Q. And is it the case that, in fact, in
19 this country, for example, the average milk
20 produced in this country has a butterfat
21 level higher than 3.5 percent?

1 A. Yes.

2 Q. And so, when you standardize to 3.5
3 percent, does that have the effect of
4 lowering the yield?

5 A. Yes, it does.

6 Q. And that's something that was, once
7 again, addressed back in 2000 when people
8 were actually testifying about yield issues?

9 A. Yes, it was. But even more
10 importantly, in that decision we went to
11 component pricing. So now anyone who gets
12 these higher, more protein, more milk that
13 might result in a higher yield, are paying
14 for it already to the Federal order.

15 MR. ROSENBAUM: That's all I have.
16 Thank you.

17 THE JUDGE: Thank you. Other
18 questions of this witness? Yes, sir.

19 EXAMINATION

20 BY MR. HARNER

21 Q. Good afternoon. My name is Tim

1 Harner, H-A-R-N-E-R. I'm general counsel of
2 Upstate Farms Cooperative, and at this
3 hearing I'm representing both Upstate Farms
4 and O-At-Ka Milk Cooperative.

5 First, Bob, I would like to thank
6 you for all your hard work preparing this
7 proposal that Upstate Farms and O-At-Ka
8 support. And I would just like to explore a
9 bit all the balancing services that
10 Agri-Mark provides.

11 And in your testimony, you got into
12 that somewhat, but could you please expand on
13 what services Agri-Mark's plants provide,
14 especially West Springfield, in balancing?

15 A. Basically, our primary balancing is
16 at West Springfield with butter and powder.
17 In my Table 9 of the plant I tried to reflect
18 that by how much additional milk goes in in
19 the springtime versus all, at least on a
20 percentage basis. I think if you look at it,
21 it was like three times as much milk, or at

1 least nonfat dry milk powder. So not only do
2 we balance milk, we balance milk components,
3 which is crucial.

4 Our cheese plants do some type of
5 balancing. They do basically a balance of
6 producer milk supplies. If you looked at
7 the pattern of our cheese plants, they pretty
8 much match the milk pattern, which is what
9 you find at cheese plants. Although on
10 occasion, when there is additional milk, and
11 particularly in springtime, if our balancing
12 plant in West Springfield is full, then our
13 cheese plant will make -- usually more
14 cheese than what we would normally like to
15 make in order to handle the milk.

16 Q. And do you know approximately how
17 much member equity is invested in West
18 Springfield?

19 A. In West Springfield? That's a tough
20 question. In terms of the active value,
21 maybe -- I hate to refer - keep referring

1 things to Mr. Langworthy, but we have a
2 total amount of equity of about a little
3 less than 40 million now from our members.
4 And of our four plants, I would say probably
5 a value of about maybe 20 million, 15 or 20
6 million. A lot more -- a lot more than 15
7 and 20 million.

8 Q. All right. I saw the thumb pointing
9 upwards in costs. Thank you very much.

10 THE JUDGE: Other questions? Mr.
11 Schad.

12 EXAMINATION

13 BY MR. SCHAD

14 Q. Good afternoon, Bob.

15 A. Hi, Dennis.

16 Q. Dennis Schad, Land O'Lakes. A
17 couple questions for you.

18 First of all, in response to a
19 question from attorney Yale yesterday, or
20 today, you said that -- you were talking
21 about if a dairy farmer's price was indexed

1 at a Class III price as a result of this
2 hearing, would that dairy farmer's price
3 change and lower. And I believe you said
4 this morning that that would be true, given
5 that the Class III price was constant. Is
6 that true?

7 A. If the Class III price was constant,
8 yes.

9 Q. Would you change your answer if that
10 dairy farmer had a participation in the
11 profits of the plant in which his milk was
12 being delivered to?

13 A. Actually, that's a very good point.
14 Yes, I would.

15 Q. Would you expand on that.

16 A. Okay. It's a situation where, if a
17 farmer could already be bearing those costs,
18 like our farmers have a 30-cent basic
19 reblend, and so if this was put into effect,
20 that 30-cent reblend were to disappear and
21 then be replaced by this, so you wouldn't

1 have any decline in that particular market.

2 Q. Also, you just answered, and I
3 believe I got it correct, from Mr. Rosenbaum
4 a question relative to the cost of the
5 weighted average survey and the Agri-Mark
6 costs. Is it true that the -- your proposal
7 for make allowances for each of the
8 commodities is actually less than the RBCS
9 weighted average as a consequence of
10 bringing in the California prices?

11 A. I believe it is. I would have to go
12 back and look at the specific numbers, but I
13 believe that's the case.

14 Q. Yes, the record will show that
15 that's true for butter powder and cheese.

16 Are you -- there was some
17 questions yesterday relative to Dr.
18 McDowell's study. Do you have a copy of --

19 A. I don't have his --

20 Q. -- Exhibit 28?

21 A. Exhibit 28? Thank you.

1 Now I have a copy.

2 Q. Okay. I believe that Chart A-2,
3 Scenario 1, was the one that was being
4 addressed yesterday, but any of the charts
5 will do. The point was brought out by
6 Attorney Miltner yesterday that there, on the
7 bottom line, producer revenue being a
8 negative number.

9 MR. VETNE: The appendix is Exhibit
10 2.

11 THE WITNESS: Could you say that
12 again?

13 MR. SCHAD: It is Exhibit 2. Okay,
14 it's Exhibit 2, I'm sorry, so the record is
15 clear.

16 THE WITNESS: What table am I looking
17 at, Dennis?

18 MR. SCHAD: It would be Table A-2,
19 Scenario 1, is the one I'm looking at.

20 THE WITNESS: I have it.

21 BY MR. SCHAD:

1 Q. And it gives you the U.S. producer
2 income difference on the bottom line. So if
3 you look at 2005-2006, we are looking at a
4 number that would be negative one five eight?

5 A. Yes, I see that.

6 Q. And it was represented yesterday
7 that that would be the number of dollars that
8 would be out of producer income in year one,
9 and there would be a year two, three and
10 four.

11 I guess my question would be, where
12 would those dollars go?

13 A. Those dollars would go to the
14 manufacturing plants in the higher make
15 allowance.

16 Q. Would some of those manufacturing
17 plants be cooperatives and that they would
18 be, in fact, going to other dairy farmers?

19 A. Yes.

20 Q. So that the cumulative amount, when
21 you are looking at dairy farmers' income in

1 the aggregate, is not the addition of all of
2 these because some of these dollars are going
3 back to other dairy farmers?

4 A. Yes, that's true.

5 Q. So would you characterize this as
6 rather -- rather than taking money from
7 dairy farmers, shifting the costs between
8 dairy farmers?

9 A. Yes, it would be. And, in fact, you
10 can even look at some of the outlying years,
11 it could be a positive impact because if our
12 -- if the manufacturing costs were to stay
13 where they are right now at these high
14 levels, which we anticipate they probably
15 will, that without this correction, our
16 members would be losing probably \$158 billion
17 every year or, in fact, more than that,
18 really.

19 Q. Your members would be losing?

20 A. The manufacturing sector would be
21 losing, including our members. Thank you.

1 Q. And as a last question, does
2 Agri-Mark buy and sell cream?

3 A. Yes.

4 Q. What are the normal terms of trade
5 when you buy and sell cream?

6 A. It's a percentage of the butter
7 price.

8 Q. From multiple --

9 A. Multiples, right. Multiples, yes.

10 Q. Thank you much.

11 THE JUDGE: Other questions? Mr.
12 Rower.

13 EXAMINATION

14 BY MR. ROWER

15 Q. Jack Rower, AMS Dairy Programs.
16 Good afternoon, Mr. Wellington.

17 A. Good afternoon.

18 Q. Nice to see you again.

19 In your prepared statement in Exhibit
20 29 --

21 A. Yes.

1 Q. -- you had mentioned that there was
2 a Sorrento plant that had closed in Orange
3 County, New York, a Sorrento cheese plant,
4 right?

5 A. In Goshen, which is Orange County.

6 Q. Right. Exactly.

7 Do you know if Sorrento is still
8 manufacturing cheese?

9 A. The company or the plant?

10 Q. The company.

11 A. The company is, yes.

12 Q. Do you know where they relocated to
13 or where those operations might have gone?

14 A. I don't know specifically where they
15 went, no.

16 Q. Did they go west?

17 A. I believe they did. I know they do
18 additional milk cheese production out there.

19 Q. Thank you. In your prepared
20 statement, again Exhibit 29, you discuss Dr.
21 Ling's calculation of whey costs --

1 A. Yes.

2 Q. -- from the data that was presented?

3 And did I understand correctly that
4 you are suggesting that we should give less
5 weight to the value of that set of numbers
6 than we should to cheese, butter, nonfat dry
7 milk?

8 A. Yes. We have concerns about those
9 particular numbers, not so much to, you know,
10 are they credible numbers, because we believe
11 that the people who put them in put them
12 under the terms that they were asked to do.
13 But we are concerned about how those numbers
14 are used, were they including all the costs.
15 Just when we look at those numbers compared
16 to California numbers, the discrepancy is so
17 large that we have a concern for that.

18 Plus, the type of plants that are
19 involved in Dr. Ling's study tend to be
20 larger plants. And my understanding is --
21 and we should be getting some more

1 information on the record in the future --
2 that they are plans that collect whey from a
3 number of plants in the vicinity. And the
4 transportation cost of bringing in that whey,
5 which can amount to several cents a
6 hundredweight, are not included in that.

7 So we think that's left out some
8 costs. Plus, the whole methodology of whey
9 accounting is a little different. Butter and
10 cheese and powder, everyone has been doing
11 for a long time, so we have a lot of
12 confidence in those. That's why we think
13 those are important.

14 Whey, we are disturbed by that, so we
15 felt that needs further study. The
16 Department has commissioned with Cornell
17 University to do some methodology with
18 further study. And in fact, regardless of
19 the result of this hearing, we will be
20 talking with Professor Stevenson there and
21 saying this is an area where we think there

1 is a weakness and that we need to take a
2 closer look at in the future.

3 So we do say -- in fact, we are
4 really saying give no weight to that and use
5 the nonfat dry milk powder plus, which is
6 what we suggested -- what the Department did
7 the last time around.

8 Q. I have a quick question about
9 Agri-Mark's operations. Your operations are
10 largely unionized, is that right, in Vermont
11 and New York?

12 A. No, actually, one of our plants is
13 unionized, and the other three are not.

14 Q. Okay. In reviewing the California
15 data, it seemed that many of the plants in
16 California are highly unionized, have large
17 fringe benefits that Ms. Reed mentioned on
18 the record earlier. And we were curious with
19 respect to costs.

20 To your knowledge, in the Southwest,
21 do plants there that operate under union

1 contracts change butter --

2 A. I'll be honest with you. I don't
3 know. But I can tell you this. We only have
4 one plant that's unionized. But we actually
5 have -- we have fairly good benefit packages,
6 so maybe the other plants aren't so inclined
7 to be unionized.

8 You've got to keep in mind, when
9 there's unions out at an area -- I hope this
10 doesn't get me in trouble, but when there's
11 unions out at an area, they -- we are on the
12 record -- tend to -- when you are looking at
13 it, if you don't give a sufficient amount of
14 benefits, okay, well, then rightfully so,
15 the employees would say, hey, maybe we should
16 be unionized or something.

17 Q. So you are saying you have to be
18 competitive?

19 A. What we really have to be is
20 competitive.

21 Q. By the way, how many employees does

1 Agri-Mark have?

2 A. All total, between Agri-Mark and
3 Cabot, we have about 900. But actually, Mr.
4 Langworthy has a table that he can put on the
5 record with that, with the exact number of
6 plants.

7 Q. So we'll get all this on the record?

8 A. The exact number.

9 Q. Thank you.

10 Henry Schaefer is going to have some
11 questions for you.

12 EXAMINATION

13 BY MR. SCHAEFER

14 Q. Henry Schaefer with USDA Dairy
15 Programs.

16 Good afternoon, Bob.

17 A. Good afternoon.

18 Q. On page 4 of your testimony, you
19 indicated on there that the manufacturing
20 allowances in the Federal orders are
21 intended to cover the cost of making the

1 product. And then, in your discussion with
2 Mr. Rosenbaum a few minutes ago, you
3 indicated, of course, that your costs are not
4 entirely covered. Your statement in there
5 does not indicate that you intend for the
6 make allowances to cover a hundred percent of
7 the costs of these plants.

8 A. Well, we would certainly like that,
9 Dave, but we recognize that if you do that,
10 you are also going to be -- the plants that
11 have lower costs, then they would be making
12 substantial amounts of money. I think the
13 order can address that. But in the past,
14 and what the Department has decided to do is
15 look at the weighted average.

16 If you ask me, I think the simple
17 average is probably fairer, to a degree. And
18 I talk a little bit about that in my
19 testimony, so I won't elaborate. But we
20 basically are recommending weighted average
21 even though it doesn't cover our costs

1 because it was way that was used before, and
2 we thought that was a way that the industry
3 could rely upon and the Department had found
4 acceptable in the past.

5 Q. You also had mentioned in your
6 testimony about subsidizing the rest of the
7 market --

8 A. Yes.

9 Q. -- by the -- your not being able to
10 make money from your plants. Would you
11 explain in a little more detail how you
12 arrived at that conclusion and what you mean
13 by subsidy in that circumstance.

14 A. Right. What we are basically
15 paying, because we can't -- because the
16 manufacturing allowance under the orders
17 doesn't cover the manufacturing costs, they
18 don't cover our costs, and they don't cover
19 the average costs, as we tried to show here,
20 that it ends up with a Class III price that
21 is actually higher by the amounts that we

1 have shown than it would have been.

2 And so, we now have a higher Class
3 III price that goes into the Federal order
4 pool. In our mind, because it doesn't
5 represent the true value, it is enhancing the
6 pool. We are basically subsidizing the pool
7 that goes to all farmers, independent farmers
8 and our own farmers, by the way. But by
9 doing that, we are basically subsidizing the
10 pool, and that's where the subsidy is coming
11 from.

12 Q. Okay. Thank you

13 On Table 4 of your testimony, where
14 you calculate how you arrived at your
15 proposed make allowances, if we just go down,
16 let's say, to the cheese computation there
17 and kind of look at what those numbers are --
18 I think everybody knows, but I thought it
19 would be a good idea to clarify -- your
20 weighted average cost under the RBCS, you
21 have got RBCS there first of one fifty-one;

1 that does not include the electricity and the
2 fuel, I take it?

3 A. No, no, that does include them.

4 Q. That does include them? Are you
5 then adding in the electricity and the fuels
6 --

7 A. No.

8 Q. Okay.

9 A. What I did was there, later on in
10 that calculation, toward the bottom, where I
11 did a fuel cost adjuster, I wanted to make
12 sure that cost information was on this
13 worksheet table. I really should have -- as
14 I looked at it later, I thought I should
15 have indented that.

16 Actually, what I added is, I think,
17 the weight average cost of \$.151. And then I
18 skip down to the DFA -- no, I'm sorry, the
19 CDFA return on investment of .008, add the
20 CDFA administration, and if you look at that,
21 that sums to the 18 cents. There's a

1 rounding, I think, involved. It sums 18.

2 Q. And then you added in -- farther
3 down there, then you added in the marketing
4 which we used in the prior decisions to the
5 total of that --

6 A. That is correct.

7 Q. -- when you got your average between
8 the two of them --

9 A. Yes.

10 Q. -- the RBCS and the CDFA?

11 And then, on your fuel adjuster, you
12 talked about using two indexes, and you have
13 got a 6 percent here. Are you looking at
14 just taking a change from one year to the
15 next in that index? So if the index in year
16 one is one fifty, and the index in year two
17 is one sixty, you would just calculate that
18 percentage change? Is that how you are
19 arriving at this 6 percent?

20 A. Yes, yes, yes.

21 Q. And you think that fairly represents

1 the change that we would have versus starting
2 the index in some other year, because I
3 believe you indicated that index's base
4 period in '88?

5 A. That's how I calculated it. I
6 thought that would be a fair representation
7 of it. But I would have to think about --
8 that's how it was done.

9 Q. Okay. And then we've had a few
10 questions on Table 3, and I thought I would
11 just spend a few minutes on that one as well.
12 And, for instance, on your cheese there you
13 have got your cost per pound, and you have
14 got your Middlebury, Chateaugay and Cabot
15 plants. That's the cost for those three
16 plans, correct, that you would have submitted
17 to Dr. Ling?

18 A. Yes.

19 Q. Okay. And the ROI and the
20 administration is just -- is that your ROI,
21 the administration and marketing costs?

1 A. Yes.

2 Q. Also in your testimony, you
3 indicated the loss of Class III milk in the
4 Northeast. During that time period that you
5 looked at, 2004 and 2005, was there
6 significant quantities of milk not cooled
7 that would have influenced that data compared
8 to times that all the milk was pooled?

9 A. In 2004, there was some Class III
10 pooling that occurred, but not in 2005. Or,
11 well, I'm not aware of 2005.

12 Q. So that maybe a better indicator of
13 the Class III numbers in that market or
14 cheese production in that market would come
15 from NASS information dairy products or
16 something like that?

17 A. Perhaps. Clearly, for just 2004,
18 that would be true. 2005, like I say, I'm
19 not sure that the pooling that occurred that
20 year, I don't -- the price distortions were
21 not such in the Northeast that I don't

1 believe there was any significant pooling, if
2 there was any.

3 So I think our 2005 numbers are
4 pretty good there. But if there was another
5 source of information that would also show
6 that, that's fine with us.

7 Q. Okay. I have nothing further.
8 Thank you, Bob.

9 THE JUDGE: Other questions?

10 MR. YALE: I have got some
11 follow-up.

12 THE JUDGE: Mr. Rosenbaum, are you
13 coming up?

14 MR. ROSENBAUM: I'm not standing up
15 to ask questions.

16 THE JUDGE: Very well. Mr. Yale.

17 EXAMINATION

18 BY MR. YALE:

19 Q. You have Table 3 in front of you --

20 A. Yes, I do.

21 Q. -- of your testimony?

1 A. Yes.

2 Q. Let me start by this question. The
3 components of milk in the vat, in other
4 words, the amount of fat and the amount of
5 protein in the vat, correlates to the
6 efficiency -- you know, the higher the
7 component values, you are going to have a
8 more efficient make in the cheese, are you
9 not?

10 A. You are going to have higher yield.

11 Q. Higher yield.

12 A. Some of it depends on the proportion
13 of fat and protein. If you have got the
14 correct proportion, I would say it lends to
15 efficiency.

16 Q. But the cost to fill the vat and the
17 starters and all the things that are
18 necessary to make a vat of cheese as far as
19 labor and the like are basically the same
20 regardless of the components that make up
21 that fat, right?

1 A. I would think so, but that also
2 would be another question for Mr. Langworthy.
3 But I would think so.

4 Q. Okay. So the question that I have,
5 first of all, dealing with your table, and
6 you indicate that you produce X number of
7 pounds of cheese. Was that made from 3.5
8 percent butterfat and 3.1 percent true
9 protein?

10 A. No, it was not. We tend to have
11 higher butterfat and protein tests. First,
12 the average producer milk is generally higher
13 than that, particularly on butterfat. But
14 also, we have higher protein and butterfat
15 tests. We tend to in Vermont, for example,
16 and some of the other areas.

17 Q. Do you buy any cream for your cheese
18 plant?

19 A. Buy any cream for our cheese plant?
20 I don't believe so.

21 Q. Do you buy powder or skim milk for

1 your cheese plant to fortify the butterfat?

2 A. To fortify the butterfat? I don't
3 believe we do, but Mr. Langworthy would
4 definitely know.

5 Sorry, Dick.

6 Q. Did you guys travel separately or --

7 A. No, but generally I would say I
8 don't believe we buy cream because we have
9 whey cream at the end, okay. And on the
10 powder side, I know we don't standardize
11 into a vat with powder for cheddar cheese.
12 So I'm just saying I don't want to answer a
13 question when I have an expert here --

14 Q. That's fair.

15 A. -- to go into the details.

16 Q. But my question is that it comes
17 down to this, is that looking at this Table
18 3, we cannot tell what components went in the
19 amount of producer milk to yield these
20 pounds, right?

21 A. No, you cannot.

1 Q. And we also don't know -- there is a
2 question about farm to plant shrink, right?

3 A. Yes.

4 Q. And we have nothing in the record to
5 indicate what your farm to plant shrink is
6 that would yield -- that eventually goes into
7 this cheese, do we?

8 A. No, we didn't feel that was an issue
9 for this hearing. I believe we put
10 something in back for the 2000 decision, but
11 I don't remember what it was.

12 Q. And you make a point that there was
13 expert testimony about the making of cheese
14 at that hearing and the yields, right?

15 A. Yes.

16 Q. And you made several references to
17 Dr. Barbano?

18 A. Yes.

19 Q. And do you recall that Dr. Barbano
20 felt that the 90 percent butterfat yield was
21 way too low, that it should have been at

1 least 94 or 95 percent? Do you remember
2 that?

3 A. I remember there was some question
4 on that. And in fact, our yield is higher
5 than that, probably 92, 93 percent.

6 Q. So there was some expert testimony,
7 but it wasn't incorporated into the decision,
8 right? We have a 90 percent butterfat
9 recovery in the current formula.

10 A. That's true. But also, the
11 Department, I think, made an adjustment on
12 that because I think they thought that if it
13 was extra butterfat, we would put it back
14 into the vat. And in fact, we don't do that.
15 And then they turned around and said, okay,
16 well, then we are going to price that at the
17 whey butter price and -- I'm sorry, no, we
18 are going to price that at the Grade AA price
19 when the value is whey butter. And so, that
20 actually created a problem.

21 I actually had a proposal of the

1 three that I put in, and the Department chose
2 not to hear that. They just chose to hear
3 this one, which is fine with us because we
4 need something very focused.

5 Q. Another thing that Dr. Barbano
6 criticized, if you recall -- he provided a
7 mass balance, did he not, in his
8 presentation?

9 A. I don't recall that part.

10 THE JUDGE: Just a minute, Mr. Yale.

11 MR. BESHORE: Your Honor, if I
12 might, I want to object at this point to any
13 further examination about this issue which,
14 as Mr. Yale -- the very first statement made
15 on the record of this hearing, Mr. Yale
16 noted and objected to the fact that the
17 yield factors are not part of the hearing.

18 We have been patient and tolerant
19 and let him rove around the edges here, but
20 we are never going to get done if we
21 litigate all these things that are not part

1 of the hearing.

2 MR. YALE: Your Honor, we believe
3 that the make allowances that they are
4 talking about are a function of the yield
5 and that if they are going to enter a make
6 allowance and not discuss the yield that
7 they are a function of, then it is not an
8 accurate number, and I have a right to
9 explain that

10 Also, this particular witness has
11 made it very much a point on
12 cross-examination by NCI's attorney, Mr.
13 Rosenbaum, about how great it was that Dr.
14 Barbano testified as to issues and how it was
15 relevant, and I want to point out to the
16 record that there were key elements of his
17 testimony that have been ignored and that
18 are relevant to this discussion.

19 And we are not going to -- you know,
20 we still think they are all part of one and
21 you can't separate the two. And if we cannot

1 discuss those, then the hearing itself
2 becomes arbitrary and capricious. If the
3 Department wants to ignore the questions and
4 answers, they can do that. But I think we
5 have a right to put that into the record.

6 THE JUDGE: I'll give you some
7 latitude, but it does appear to me that some
8 of these questions are much more suited to a
9 technical expert such as Mr. Langworthy as
10 opposed to this witness.

11 MR. YALE: And we are going to get
12 there, but I want to talk about for a minute
13 the situation with Dr. Barbano.

14 THE JUDGE: Well, let's --

15 MR. YALE: And I'll try to keep it
16 short. And I think I have tried to do that
17 throughout this hearing, considering the
18 issues involved, and there is a tremendous
19 amount of money involved in this.

20 BY MR. YALE:

21 Q. Mr. Wellington, I want to go back.

1 Do you recall whether Dr. Barbano presented a
2 mass balance analysis to determine the cost
3 of producing milk in yields?

4 A. No, I don't, not in detail.

5 Q. You are not providing a mass -- do
6 you know what I mean by mass balance?

7 A. Not really.

8 Q. Is this another question I need to
9 ask --

10 A. Well, I mean, if you are talking
11 about -- if by mass balance you are saying
12 what comes in and what comes out --

13 Q. Right, and you account for
14 everything --

15 THE JUDGE: He's asked and answered
16 that question.

17 MR. YALE: Okay.

18 BY MR. YALE:

19 Q. But I want to get back -- this Table
20 3 does not tell us what your yield is, does
21 it?

1 A. No, it doesn't tell what the yield
2 is. But I'm thinking that the yield may not
3 even be that big a factor because this comes
4 out with production per pound of product.

5 If you have more yield, then you have -- it
6 doesn't affect your production per pound for
7 product. It doesn't -- you are already
8 calculating -- I'm sorry, not production.

9 You are already calculating your make
10 allowance per pound. So if there is a change
11 in the yield, it affects your make allowance
12 per pound.

13 So, I mean, I think that sort of
14 neutralizes, to some extent, the yield issue
15 if there is one.

16 Q. Now, is it your position that in
17 establishing Class III prices, the Department
18 is to ignore competitive forces in the field
19 that involve the prices that plants pay for
20 milk?

21 A. I don't think it's a question of

1 ignoring it. You can't -- you need to look
2 at pieces that are involved here. And to the
3 effect that, for example, if this is not
4 corrected, over-order premiums that are out
5 there would fall, that offsets some of the
6 things that they are saying about the impact
7 of these proposals, that doing nothing
8 increases the price, and I wanted to make
9 sure the Department was aware of that.

10 So I would say that you have to look
11 at various pieces that are involved in that.
12 But the bottom line for this is that the
13 Department should be looking at what is the
14 true manufacturing cost to get to a true
15 value of Class III milk.

16 Q. And that's the point that -- let me
17 propose a hypothetical to maybe illustrate
18 what I think you are saying. Let's say that
19 you have a plant -- you have two plants that
20 are competing for a supply of milk, and the
21 manufacturing under the Federal order

1 program tells us that, based upon the prices
2 of cheese and the yield that they have
3 implied and the make allowance, that the
4 Class III price ought to be \$12, because
5 that's really what we are talking about,
6 right?

7 A. Yes.

8 Q. Okay. But the competitive market is
9 that in that area, for whatever reason, to
10 get that milk, the plant has to pay \$12.50 to
11 get the milk.

12 A. Right.

13 Q. What is the value of the milk in the
14 marketplace?

15 A. The minimum value should be the \$12
16 you spoke about. The order is supposed to
17 go after what the minimum value is.

18 Q. So --

19 A. You are allowed to pay more. You
20 either can't pay less because they're
21 proprietary or, in a competitive situation,

1 it's makes it difficult to pay less if you
2 are a cooperative.

3 Q. But let's take it the other way.
4 And this is where, frankly, I thought you
5 were going to come with your testimony
6 today, or yesterday and today, and you
7 didn't. And let's say that the formula says
8 it's \$12. The milk is ready available at
9 \$11. Should the Department consider that in
10 determining the value of milk in that
11 marketplace?

12 A. Well, obviously, the minimum -- if
13 the minimum price is \$12, the Department
14 should hopefully have minimum prices that are
15 reflective in the marketplace. If there is
16 not, there is some other problem.

17 I mean, part of the problem is we are
18 putting milk into our plant because we can't
19 -- if there is distress milk out there, for
20 example -- I mean, if we can't afford to put
21 surplus milk into West Springfield because we

1 can't cover the cost of the product, well,
2 then, there may be milk out there for \$11.
3 We think that's probably a disorderly
4 marketing condition.

5 Q. Let's take it another step. In your
6 testimony, you have made the statement in
7 here that we need to be looking at some of
8 the smaller plants, not getting too biased by
9 larger western plants, in establishing these
10 make allowances.

11 Is that a fair --

12 A. Yes, that's true. Consider both.

13 Q. So if we have a situation where the
14 Department is setting a minimum price based
15 on an end product pricing that allows the
16 smaller, less cost effective plants -- and
17 I'm not going to say inefficient because they
18 are not necessarily inefficient, just less
19 cost effective due to their particular size
20 -- that if it sets it for that, but the more
21 efficient plants are able to pay for their

1 milk, isn't that really an indication that
2 the Department should be looking at that
3 value of the milk and not the value of the
4 plants in the lesser, the smaller --

5 A. No, because once again, I think that
6 the purpose of the Department to set minimum
7 prices. That's why there is something called
8 over-order price, because if the marketplace
9 can bear additional returns back to farmers,
10 that's great. But the orders are minimums.
11 You can't -- you know, you are not supposed
12 to be able to pay farmers less. You want to
13 have some level of price integrity.

14 Q. In fact, that's one of the issues,
15 isn't it, is that what good is a Federal
16 order if it reduces the price of the value of
17 milk to producers compared to what the market
18 is?

19 A. Well, we think there is a lot of
20 good to the Federal orders besides that.
21 But, I mean, one of the issues is to have

1 something about price integrity,
2 particularly on class prices, that these are
3 prices that the people who are paying this in
4 regard to price integrity can, you know,
5 afford to, you know, at least have a shot at
6 breaking even.

7 If you are paying this Class III or
8 Class IV price, if from day one the milk
9 comes into the plant and you are losing
10 money, the price integrity goes out the door.

11 That's one of the things we know, we
12 feel strongly that the Federal order should
13 address.

14 And Federal order is good for a lot
15 of things. Recording information is just one
16 piece. Setting the price is another big
17 piece. There are a lot of very valuable
18 things that the order does, as I know you
19 agree.

20 MR. YALE: I have no other
21 questions.

1 THE JUDGE: Other questions of this
2 witness? Mr. Vetne.

3 EXAMINATION

4 BY MR. VETNE

5 Q. John Vetne, counsel for Agri-Mark, on
6 redirect. Let's go to some of Mr. Yale's
7 last questions because they are fresh in
8 your mind.

9 The cheddar cheese included in the
10 pricing formula now, the NASS survey, and the
11 allowance for making cheddar cheese, that's a
12 commodity product, correct?

13 A. Yes.

14 Q. There are other cheeses to varying
15 degrees that are not commodity products that
16 are also Class III specialty products that
17 are not included in the survey, and no
18 attempt was made to determine the price of
19 those products?

20 A. That is correct.

21 Q. As a commodity product, cheddar

1 cheese and the resulting Class III price is
2 designed to be a market-clearing price for
3 milk going into cheese?

4 A. That is my understanding, yes.

5 Q. In fact, if the market value of milk
6 -- I think implied in one of the questions
7 that Mr. Yale asked, if the market value of
8 milk is greater than the Class III price, the
9 market value is what is going to get paid,
10 not a lower Class III price?

11 A. Yes.

12 Q. Handlers adjust to the marketplace
13 whenever they can or whenever they have to?

14 A. Yes.

15 Q. The one place, however, that you
16 cannot adjust is at increased manufacturing
17 costs because when you try to pass those on
18 for commodity cheddar cheese, it increases
19 the survey price, and the cost increase that
20 you attempt to capture comes right through
21 you into the pool?

1 A. Right. Particularly for those
2 commodity people, but effectively for about
3 everybody out there. It's a circular
4 approach.

5 Q. Within the universe of milk going
6 into various Class III cheeses, would you
7 agree that there are probably a variety of
8 values to the buyer and a variety of values
9 from region to region?

10 A. Oh, absolutely.

11 Q. Would you agree it is not -- in your
12 opinion, that it is not the function of the
13 order to set the average value of Class III
14 in all those uses, but to set a
15 market-clearing price for one of those uses?

16 A. Yes, and we believe the primary use
17 is cheddar cheese.

18 Q. And market factors apply to produced
19 prices above that on occasion?

20 A. Yes, and that's a good thing for
21 producers.

1 Q. So if someone were to examine an
2 effect on producers from increasing the make
3 allowance and thereby reducing the Class III
4 price, the marketplace response would include
5 premiums paid for other uses of milk and
6 other cheeses?

7 A. And other cheeses, yes.

8 Q. And, in fact, prior to Federal order
9 reform, the Class III price was one that
10 provided a variable manufacturing allowance.
11 Isn't that the case?

12 A. Yes, the Minnesota-Wisconsin price
13 series.

14 Q. And the difference between the
15 selling price of cheese and the survey pay
16 price to dairy farmers varied from month to
17 month and place to place?

18 A. Yes, it did.

19 Q. And what is different now is that
20 handlers cannot respond to marketplace
21 factors by making those variations in their

1 pay prices because you are constrained by the
2 Federal order as to what you must pay
3 regardless of the marketplace?

4 A. Yes, that's true. If we had the
5 Minnesota-Wisconsin price series right now,
6 we wouldn't be here because the
7 Minnesota-Wisconsin price series' intent was
8 to address the issues. The handlers in
9 Grade B milk out in the Minnesota-Wisconsin
10 area would pay farmers the amount based upon
11 the competitive situation there, but also
12 would return a level that should be at least
13 break even or profitable for them.

14 So if their manufacturing costs went
15 up, while the cheese price was totally
16 constant, they would return less to farmers
17 to cover those additional costs, and then so
18 the Class III price would have fallen as a
19 result automatically. And, you know, we
20 wouldn't be here at a hearing saying, you
21 know, can we get this. It would have been

1 adjusted in the marketplace already.

2 We are a function of the type of
3 pricing that we have today, and it's
4 unfortunate we can't do a Minnesota-Wisconsin
5 price series.

6 Q. You talked about cheese plant
7 closings in the Northeast, particularly in
8 New York and Vermont. That provides fewer
9 marketing options for Agri-Mark and other
10 Northeast producers?

11 A. Yes.

12 Q. Have there been occasions in the
13 past when Agri-Mark has been unable to find
14 capacity in the Northeast and had to
15 transport milk to distant places?

16 A. Yes, there has.

17 Q. Would you give some illustrations of
18 places where it would have gone.

19 A. We have sent milk out to western
20 Pennsylvania. Farmers' Cheese is a group out
21 -- a plant out there. We have sent some milk

1 to Ohio and Wisconsin, at times. Usually, it
2 is during a flush period when there is just
3 so much milk out there. It might be -- it
4 wouldn't be for the entire year, but it might
5 be for selected times of the year.

6 Q. And to the extent any plant in the
7 Northeast decides to close because of
8 marketplace factors, you would have more milk
9 that would have to make such a journey?

10 A. We would have more milk, and some
11 others would have a lot more milk.

12 Q. And when you put milk on such a
13 journey, who picks up the transportation tab
14 from the Northeast for New England to Ohio
15 and western Pennsylvania?

16 A. Well, Agri-Mark and our farmers
17 would do so.

18 Q. And what typically are you able to
19 sell the product for delivered to such plant
20 in that kind of transaction?

21 A. Well, milk going out there is

1 distress milk. You have to find a home. We
2 are only bringing it out there because we
3 have no other place for it. And usually, the
4 people that are receiving it recognize that.
5 So you're usually -- not only are you paying
6 transportation costs, you are usually getting
7 a price that can often be a dollar or two or
8 \$3 a hundredweight less than what that cost
9 price, so a substantially lower value.

10 Q. That milk is being sold to a handler
11 in a transaction that is not price regulated
12 between you and the buyer by the USDA?

13 A. Correct.

14 Q. On the other hand, the milk is part
15 of the pool, so you have to account to the
16 pool at the Class III price?

17 A. Yes.

18 Q. And in the Northeast, you can't
19 readily be pooled at such a low --

20 A. Correct.

21 Q. So you account to the pool. The

1 pool then gets the benefit of -- you used the
2 term subsidy. The pool gets that \$2 as
3 though you had received that benefit, but you
4 had received \$2 less?

5 A. Yes.

6 Q. In the Northeast in the last seven
7 years, since the time of the last survey, has
8 there been a -- you referred to a reduction
9 in cheese capacity. Has there also been a
10 change in the nature of ownership and
11 operation of the remaining cheese plants?

12 A. Yes, there has.

13 Q. Would you describe that.

14 A. The plants that are remaining tend
15 to be more owned by cooperatives. We are
16 probably a classic example of that. Our
17 Middlebury, Vermont, plant was formerly owned
18 by Kraft, and they made Swiss cheese there.
19 And then about 1991, I believe, 1990 -- I
20 guess it was later on, maybe 1993, 1994,
21 Kraft decided that they were going to close

1 down that plant. And they offered to sell it
2 to us as a Swiss cheese operation. They were
3 closing it because there was a lot of Swiss
4 cheese in the market.

5 And so, we were -- you know, it was
6 unlikely we were going to continue to make
7 Swiss cheese. So we ended up having it
8 converted to a cheddar cheese plant, and we
9 kept it open as a cheddar cheese plant.

10 And the same thing happened two years
11 ago with Valio, which is a Finnish co-op,
12 which was effectively proprietary and viewed
13 as such here, sold to McCadam Cheese up in
14 Chateaugay, New York. And they decided they
15 were going to leave. And so, their plant was
16 going to close. And so, we talked with
17 them, and we were able to purchase the plant
18 and keep the plant open.

19 We had a fair amount of our member
20 milk that was going in there, plus a lot of
21 milk in the north country, New York, going

1 in. And we thought it would be better for
2 the marketplace to keep that plant there.

3 Q. Prior to ownership by Valio of that
4 plant, was it owned by Dean Foods?

5 A. Yes, it was owned by Dean Foods.

6 Q. Mr. Yale asked you about premiums
7 that you pay for milk from sources other than
8 Agri-Mark going into your cheese plant. He
9 asked you a few questions about that.

10 Is it not case that cheese plants
11 customarily pay something more for the
12 incremental extra loads in addition to their
13 regular supply?

14 A. Most of the time, yes.

15 Q. And if you were able to acquire milk
16 for Class III at less premium or no premium
17 or below class, what would that do to the
18 premium structure you were able to negotiate
19 for other classes?

20 A. Well, it means that if -- if you can
21 get it for less than class or even not class,

1 it means that there is extra milk floating
2 out there in the marketplace. Usually, that
3 milk, before someone is going to get class or
4 below class, they are going to peddle it
5 around to everybody. And that's going to
6 lower the premium level for all classes of
7 milk that are out there, so the general
8 premium level will decline.

9 Q. Something I wasn't sure I
10 understood, so I want to have it clarified.
11 You talked about enterprise accounting
12 between Cabot and Agri-Mark. Let me see if I
13 understand correctly. Milk that's going for
14 processing cheddar cheese, and your
15 enterprise accounting is on Agri-Mark's books
16 through receipt through the vat and into the
17 block and -- or whatever unit --

18 A. Right.

19 Q. -- as fresh cheese. And at that
20 point, it goes to Cabot for whatever value is
21 added by aging and packaging and so forth.

1 Am I correct?

2 A. Yes.

3 Q. So what goes on Agri-Mark's books is
4 essentially the same commodity as that
5 included in the other cheese plant surveys
6 and similar to that other kind of cheese
7 that's being included in the NASS for prices?

8 A. Yes, we separated that out because
9 we felt it was important -- not only our
10 board of directors but our farmers felt it
11 was important that, when we purchased the
12 Cabot business, that we keep track of
13 whether Cabot was making or losing money and
14 how our endeavors were doing at that point.

15 It's -- I think that accounting also
16 is probably the reason why Agri-Mark is the
17 chief proponent, because with that accounting
18 we saw this problem starting to build over a
19 year ago on the Agri-Mark side. And when we
20 pinpointed what it is, we started going
21 around to the industry, saying, folks, there

1 is a problem here.

2 So I think that was helpful, at
3 least, in us getting to a hearing, having
4 that accounting so you could separate out the
5 two. A lot of companies don't necessarily do
6 that.

7 Q. The surveys that are employed as
8 part of the price formula and are proposed to
9 be employed include both small and large
10 plants, correct?

11 A. Yes.

12 Q. And your cheese plants are in the
13 category among the smaller cheese plants in
14 the survey?

15 A. I would say, clearly, that's the
16 case with Cabot plant and the McCadam. Cabot
17 is much smaller. I think Cabot plant may
18 have been the smallest. And then McCadam
19 plant is less than the average size. I
20 think the Middlebury -- I'd have to look at
21 the size, but I think it's -- it's probably

1 in the same area. Might be a little less.

2 Q. And in your experience, is it
3 generally true that a smaller cheese plant
4 has greater cost per pound of cheese than a
5 large plant?

6 A. It has less pounds to spread over a
7 fixed cost and, yes, it does.

8 Q. I think you said that, even with
9 this proposal, more than half the plants, not
10 more than half the production of them, more
11 than half the plants will still not be able
12 to recover their costs?

13 A. Right, because the intent of having
14 a weighted average that -- you are at the 50
15 percent point on milk volume. So half the
16 volume can cover it, half -- half can have
17 cost above and half below. But because you
18 are doing a weighted average now and smaller
19 plants tend to have a higher cost, you now
20 have more plants, a larger number of plants
21 in that group that cannot cover the cost.

1 Q. You are aware that there are many
2 small businesses that operate small cheese
3 plants around the country?

4 A. Yes.

5 Q. So the effect of doing nothing would
6 rationally, logically be felt more adversely
7 by a larger number of small businesses than
8 the effect of doing nothing on the largest
9 cheese plants?

10 A. Relative from the average cost, I
11 would say yes.

12 Q. And the benefit, although it
13 wouldn't be full cost recovery, the reduced
14 burden of regulation would be felt more by
15 small business cheese plants than by the
16 largest?

17 A. I think proportionately, yes. I
18 think it would be felt by everybody involved
19 because I don't know if anybody is making
20 their cost right now where they are at, even
21 if they are the largest plants. But

1 generally, I would say yes.

2 Q. And Table 4 in Exhibit 29, where you
3 have the energy adjuster?

4 A. Yes.

5 Q. I think Jack Rower asked you a
6 question about that, somebody. You employed
7 an index there where the base period was
8 1988. I think you agreed with that.

9 However, the only thing you are
10 measuring in Table 4 for the energy adjuster
11 line is the change in energy prices between
12 19 -- I mean, between 2004 and 2005?

13 A. Right.

14 Q. It is only that component of the
15 energy cost. The baseline for this purpose
16 is 2004 energy prices, and the adjustment is
17 for what has increased in those energy
18 components from 2004 to 2005?

19 A. That is correct.

20 Q. And based on the Department of
21 Energy projections, that's pretty close to

1 what they project it to be for the next
2 couple years?

3 A. Actually, I think it is probably low
4 relative to what we have seen. We tried to
5 be very conservative.

6 Q. Thank you.

7 A. If I could just add, I did hesitate
8 in regard to that question because I was
9 thinking if the base here made a difference.
10 I don't think it does in the comparison, but
11 I wasn't sure.

12 Q. Okay. Do you have anything else you
13 want to add that I forgot?

14 A. No, I think we have covered
15 everything.

16 Q. Okay. Thank you.

17 THE JUDGE: Other questions? Mr.
18 Yale.

19 MR. YALE: Just one follow up.

20 THE JUDGE: Promise?

21 MR. YALE: Promise.

1 EXAMINATION

2 BY MR. YALE

3 Q. Small business. Are you claiming
4 that Cabot's and your cheese plants are small
5 business enterprises under the Regulatory --

6 A. No, no, we would not be in that
7 category.

8 MR. YALE: I'll keep my promise.

9 THE JUDGE: Yes, sir. Thank you.

10 Other questions? Very well, Mr.
11 Wellington, you may step down.

12 Mr. Rosenbaum, maybe at this time it
13 might be a good idea to ask if we could have
14 your two witnesses.

15 MR. ROSENBAUM: Your Honor, I would
16 like to do that, but before I call a witness
17 I have a matter I need to raise with Your
18 Honor that I think has the potential for some
19 critical importance.

20 As Your Honor knows and as the rules
21 provide, and quoting 900.4(A), "the notice of

1 hearing shall define the scope of the hearing
2 as specifically as may be practicable," which
3 essentially means that you can't consider a
4 proposal unless it's been listed in the
5 hearing notice.

6 The hearing notice here is very plain
7 that we are to take evidence on a proposal
8 seeking to amend Class the III and Class IV
9 formulas, manufacturing allowances. And the
10 hearing notice also states in as plain words
11 as possible -- and I'm paraphrasing, but this
12 is on page 546 of the Federal Register --
13 while the proposal, talking about the
14 Agri-Mark proposal, seeks to amend the
15 product pricing formulas used to price Class
16 III or Class IV milk, changes in these
17 formulas also would affect the prices of
18 Class I and Class II milk.

19 And that's said on page 546 and said
20 again on page 552.

21 The reason that is said, and is

1 accurately said, is because while we are
2 talking here about changing the make
3 allowances for Class III and Class IV prices,
4 that automatically also changes the Class I
5 and II prices because the Class II price is
6 the Class IV price plus 70 cents, the
7 so-called differential, Class II
8 differential. And the Class I price is the
9 higher of the Class III or IV price plus the
10 fixed differential, the so-called Class I
11 differential.

12 I would note that USDA's econometric
13 model contained in the hearing notice,
14 Exhibit A, assumes that any changes in the
15 make allowance would also affect the Class I
16 and II prices, which is quite accurate. And
17 Exhibit 13, which is the exhibit put in by
18 another USDA representative yesterday, makes
19 the exact same assumption quite correctly, in
20 our estimation.

21 Now, why am I bringing this all up,

1 Your Honor? Because there is nothing in the
2 hearing notice whatsoever suggesting a) that
3 we are going to consider changes in the Class
4 I or Class II differential; b) that we are
5 going to consider changing the Class I or II
6 price formulas; or c) that we are going to
7 consider changing the relationship between
8 Class III and IV, on the one hand, and Class
9 I and II on the other. That is the say, the
10 fact that Class II will be Class IV plus 70
11 cents, and Class I will be the higher Class
12 III or IV plus the fixed differential set
13 forth in the order.

14 I am extremely concerned -- and
15 therefore, no one -- there are lots of people
16 who would be extraordinarily interested if
17 any of those three proposals were on the
18 table. For example, ice cream companies who
19 are Class II would be very interested if
20 there were to be a change in the formulas for
21 Class II milk.

1 And yet I know from looking out in
2 the room that -- I know none of the large ice
3 cream companies are here, as an example. And
4 there is no reason they should be.

5 I'm very concerned by Mr. Beshore's
6 questioning. And I let it go at the time
7 because he was asking dairy farmers
8 questions, and I try not to interrupt them.
9 But he asked questions to the dairy farmers
10 saying, well, what if we change the Class III
11 and Class IV make allowances, which is the
12 very thing we are talking about here, and
13 appropriately talking about here, because
14 it's the only thing that's covered by the
15 hearing notice. But we didn't carry those
16 changes forward to Class II and Class I.

17 In other words, what if we decided to
18 change the Class I and II pricing formulas?
19 What if we decided to change the Class I and
20 II differentials?

21 What if we decided to change the

1 relationship between Class III and IV and
2 Classes I and II?

3 The problem is, Your Honor, none of
4 those things are noticed, and those cannot be
5 considered at this hearing. And for that
6 reason, Your Honor, testimony or proposals
7 along those lines which may be forthcoming
8 are utterly inappropriate.

9 And I am asking Your Honor, pursuant
10 to Your Honor's power at 900.6(B), to rule
11 that there can be no evidence, there can no
12 proposals suggesting any of those changes.

13 Now, Your Honor, I raise this because
14 I don't want anyone to -- because people need
15 to know what's happening here. I will point
16 out that this is -- that this exact same
17 kind of thing came up when we had the 2000
18 hearing. Someone tried to take the stand and
19 testify about what actually was a lot closer
20 to the existing hearing proposal but actually
21 wasn't one, which was for a separate Class

1 III butterfat price.

2 I stood up and objected to that
3 testimony. My objection was sustained by the
4 administrative law judge.

5 Ironically, USDA notwithstanding that
6 objection, it initially purported to put in a
7 separate Class II butterfat price, and we --
8 a number of people in the industry went to
9 court and were successful in having that
10 thrown out.

11 As the judge said in that case,
12 "there was no proposal to create a separate
13 Class III butterfat price," and while the
14 secretary had the right to make proposals, if
15 she hadn't done so, she had not given fair
16 notice to the industry.

17 Your Honor, there has been no notice
18 provided to the industry here with respect to
19 any proposal, as I say, to do any of three
20 things: to amend the Class I or II
21 differentials; b) to change the relationship

1 between Class III and IV, on the one hand,
2 and I and II, on the other; or c) to change
3 the Class I and II price formulas. And
4 therefore, testimony, proposals that would
5 encompass any of those changes should not be
6 allowed.

7 And I wanted to get this out on the
8 table so that someone doesn't appear -- try
9 to appear on Thursday or Friday and try to
10 put this in or that we don't get further
11 questioning on this issue.

12 But my motion is to exclude any such
13 questioning or proposal as being clearly
14 beyond the scope of the hearing notice.

15 THE JUDGE" Very well. Your
16 objection will be noted.

17 MR. ROSENBAUM: And if someone does,
18 Your Honor, try to take the stand and
19 provide that, such testimony --

20 THE JUDGE: I'll allow you to renew
21 your motion at that time.

1 MR. ROSENBAUM: All right, Your
2 Honor. Thank you. But I would note that it
3 is, of course, within Your Honor's power
4 expressly provided to exclude such testimony
5 and proposals, not merely to note my
6 objection.

7 THE JUDGE: Very well.

8 MR. ROSENBAUM: As I mentioned the
9 last time this issue -- not this precise
10 issue, but the last time the kind of issue
11 arose, the administrative law judge, in our
12 mind entirely properly, granted the motion
13 and excluded it.

14 As I say, it's not -- from our
15 perspective, there is no cure, you know, to
16 allow the evidence in over our objection
17 because obviously, the whole problem --

18 THE JUDGE: Well, obviously --

19 MR. ROSENBAUM: -- from our
20 perspective is that people are not here who
21 would be here, etc.

1 THE JUDGE: At the same time, Mr.
2 Beshore's line of questioning was not
3 objected to at that time.

4 MR. ROSENBAUM: Your Honor, he asked
5 two questions to dairy farmers, and I have
6 said I let that pass. It is hard for me to
7 jump up in the middle of cross-examination,
8 but it seemed to me that at this -- there's
9 been no formal proposal made at this point,
10 and I --

11 THE JUDGE: Well, right now we are
12 going down the road on the proposals that are
13 before us.

14 MR. ROSENBAUM: That's right, Your
15 Honor, and I think -- and I felt it incumbent
16 upon me -- the proposal before us is Proposal
17 No. 1, Your Honor. That's the only proposal
18 before us.

19 THE JUDGE: Well, that plus the
20 general proposal which is in all notices
21 which allows USDA to give certain

1 modifications to conform with the general
2 nature of the proposal being considered.

3 MR. ROSENBAUM: Well, that's right,
4 Your Honor.

5 But nonetheless, that's been
6 interpreted, and the litigation I mentioned
7 confirmed that is not a catchall allowing
8 anything and everything to come in.

9 THE JUDGE: I didn't say it was. I
10 said subject to that additional proposal.

11 MR. ROSENBAUM: My only point is
12 that I -- Your Honor's point is well taken
13 and accurate.

14 My only observation is that that is a
15 narrowly applied power based upon --

16 THE JUDGE: At the same time, the
17 purpose of all of these hearings is to gather
18 information. If, as a general matter,
19 information comes in that the approach taken
20 on the proposal under consideration is
21 faulty, then that evidence certainly may be

1 taken into account in rejecting the proposal.

2 MR. ROSENBAUM: Well, I appreciate
3 that the USDA can consider whether or not to
4 accept Proposal No. 1 or not.

5 My objection is for the contemplation
6 at this hearing of something that is not part
7 of Proposal No. 1.

8 They can -- USDA can decide to do
9 proposal No. 1 or not, as the case may be, as
10 the evidence supports. But that does not
11 provide, obviously, carte blanche for them to
12 do something in addition to Proposal 1 that
13 is not fairly encompassed within the scope of
14 that proposal.

15 MS. YOVIENE: Your Honor, I would
16 like to make my appearance for Dean Foods
17 Company. My name is Wendy Yoviene,
18 Y-O-V-I-E-N-E. I also move with Mr.
19 Rosenbaum that you exercise your authority
20 under part 900 to preclude any testimony
21 about the issues of decoupling, which

1 essentially is an issue about whether the
2 Class I differential is going to be changed.

3 Dean Foods, as a Class I milk
4 processor, will be affected by this. But
5 when the proposals came out back in November,
6 the chief proponents, Agri-Mark and IDFA,
7 through the Cheese Institute, specifically
8 cited in their letter that they were only
9 asking to deal with the issue of make
10 allowances. And we relied on that.

11 And then the notice of interested
12 parties came out, and that was a couple weeks
13 later. Let's see if I can find that.
14 November 15th. So the letter came out in
15 October. Then USDA issued a Notice to
16 Interested Parties, which I can hand out. I
17 would like to have it marked as an exhibit.
18 It's not yet an exhibit in the record.

19 THE JUDGE: Very well.

20 MS. YOVIENE: [Handing out
21 documents.]

1 I would like to ask that that Notice
2 to Interested Parties be premarked as Exhibit
3 36, and I will be asking for its submission.

4 THE JUDGE: It is so marked.

5 [Whereupon, Exhibit No. 36
6 was marked for identification by the judge.]

7 MS. YOVIENE: But in this notice, on
8 December 15th, the Department specifically
9 said -- and I have lost my copy.

10 The Department specifically said, and
11 I quote, "Consideration is being given to"
12 -- and I underscore -- "limit a public
13 hearing to reconsideration of the
14 manufacturing allowances for cheese, whey
15 powder, butter and nonfat dry milk powder
16 only."

17 Then, if you turn to page 2, the
18 Department indicates that there is an
19 opportunity before the hearing notice
20 actually goes out to discuss with the
21 Department personnel the various proposals.

1 So during that time, various
2 interested parties went to the Department and
3 talked with them and got confirmation that
4 the hearing was going to either -- you know,
5 suggested or supported the limits of the
6 scope of the hearing.

7 MR. BESHORE: Your Honor, I have got
8 to object to testimony, in essence, from the
9 podium with respect to prehearing
10 conversations with departmental personnel
11 obviously for the purpose of, you know,
12 embedding in the record, you know, reliance
13 or the truth of those conversations. I mean,
14 there are all kinds of conversations that go
15 on with the Department and departmental
16 officials prior to these hearings.

17 If they are to be the subject of, in
18 essence, the factual upon which rulings are
19 to be made, we are opening up a huge
20 Pandora's box --

21 MS. YOVIENE: I can shortcut this.

1 MR. BESHORE: -- of issues.

2 MS. YOVIENE: I can shortcut this.
3 I'm not offering that as testimony or for the
4 truth of the matter. I think it's a proper
5 inference that there was a chance for
6 discussion, and the Department then issued a
7 hearing notice that specifically limited the
8 proposal to just change the make allowances.
9 And therefore, I stand on that.

10 THE JUDGE: Very well.

11 MS. DESKINS: Judge Davenport, maybe
12 I can help to try to resolve this.

13 THE JUDGE: Well, let's -- as I
14 understand what is before me at this time, we
15 only have Proposal 1, and that's all we have
16 heard testimony about at this point.

17 So Mr. Rosenbaum has raised his
18 objection to make sure that, in other words,
19 I am limiting my consideration or, in other
20 words, the presentations that are heard.

21 I have also indicated, too, that, in

1 other words, if we start getting into areas
2 like that, then he certainly may renew his
3 objection, as may you, counsel.

4 MS. YOVIENE: My quandary, Your
5 Honor, is that I have an expert witness that
6 I would bring in to address these issues who
7 is currently in Phoenix, Arizona, and is
8 calling me hourly, trying to figure out her
9 schedule. And it's because -- she is in
10 Phoenix, Arizona, because the notice of
11 hearing was limited, and so we didn't need
12 her.

13 And so, I'm asking Your Honor to make
14 a ruling that the hearing will be limited
15 to --

16 THE JUDGE: Well, you are asking me
17 to rule upon a hypothetical which I don't
18 have before me at this time. In other words,
19 it is entirely possible that some parties
20 present may seek to advance another
21 proposal. But in other words, that has not

1 been brought.

2 And as such, I haven't been able to
3 rule on whether or not it is within the scope
4 of the notice.

5 MS. YOVIENE: If I may sit down for a
6 moment after I ask for another exhibit to be
7 marked and maybe let the other parties speak,
8 because I know Mr. Beshore was standing up
9 here wanting an opportunity.

10 THE JUDGE: As is --

11 MS. YOVIENE: Maybe we can resolve
12 this.

13 THE JUDGE: As is Mr. Yale.

14 MS. YOVIENE: Yes. But first, I
15 also reference the letters of request of the
16 chief proponents of the proposal, one from
17 Agri-Mark, one from IDFA, from the National
18 Cheese Institute. And then there were a
19 number of other supporting letters from
20 proponents that were also posted on USDA's
21 website. These all came off of USDA's

1 website.

2 I would like to have them marked, and
3 then I would like to move for the admission
4 of this exhibit and Exhibit 36.

5 THE JUDGE: Very well. Let's mark
6 them sequentially.

7 MS. YOVIENE: I think they can be
8 marked as one exhibit. They are stapled
9 together.

10 THE JUDGE: Very well. That will be
11 Exhibit 37.

12 [Whereupon, Exhibits No. 36 and
13 37 were received in evidence.]

14 MS. YOVIENE: I do have additional
15 legal argument, but perhaps it's best to let
16 the other folks speak to you first.

17 THE JUDGE: I think you'll have your
18 chance.

19 MR. YALE: Your Honor, Benjamin F.
20 Yale on behalf of Select Milk Producers,
21 Continental Dairy Products and Dairy

1 Producers of New Mexico. We are joining them
2 in this objection and motion because, you
3 know, we think that it does expand and it
4 creates an incredible quandary in proceeding
5 further.

6 And I understand Your Honor's dilemma
7 because, in a sense, you are not aware of
8 what we know is about to come out. And the
9 timing of the witnesses is starting to throw
10 us because we are going to have witnesses
11 come on and leave because of scheduling that
12 may happen before this proposal is out there.

13 We understand that National Milk is
14 going to propose this decoupling of Class I
15 and Class II.

16 And so, I think maybe the appropriate
17 way is to have a motion in the form of a
18 motion in limine that can be done in advance
19 so that there is notice to the parties that
20 we can proceed one way or the other.

21 And there is a -- it is an extremely

1 important practical aspect. I mean, Ms.
2 Yoviene explains one difficulty, getting a
3 witness out here. We have several witnesses
4 that we would end up calling and bringing out
5 ourselves if that ends up being the issue.
6 And we'd ask to put on the ones that we do
7 have in that issue.

8 And it really is -- let me just
9 share, is that the relationship, as explained
10 by Dr. McDowell yesterday, was that -- is
11 that the make allowances change, everything
12 flows up and down, one, two, three and four.
13 And his scenario reflects that. The
14 economic analyses reflect that.

15 But when you decouple it, it does
16 some strange things. And we need to be able
17 to know whether we are going to be able to
18 address those.

19 So I think, in efficiency, a ruling
20 by Your Honor at this point, I think would be
21 a very efficient way to handle it.

1 THE JUDGE: Very well. Ms. Deskins
2 was about to see if she could shed some
3 additional light on the subject.

4 MS. DESKINS: After hearing what Mr.
5 Yale said, is it possible to have National
6 Milk make the proposal? And then, once it is
7 on the record, some rulings could be made.
8 But I agree with Your Honor that, until
9 something is actually put on the record,
10 there is nothing to rule on or object to or
11 do anything.

12 So if National Milk has a proposal,
13 perhaps they could be asked to make it now,
14 and then the -- the discussion we had would
15 be relevant to something that's actually
16 being proposed.

17 THE JUDGE: Mr. Beshore.

18 MR. BESHORE: I'm not representing
19 National Milk but, of course, Dr. Cryan is
20 here and has been here from the beginning,
21 and he has testimony and he will present it.

1 And I expect the cooperatives I represent who
2 are members of National Milk will be
3 supporting that position.

4 Just a couple of comments on, you
5 know, the premature comments we have had from
6 counsel here.

7 The notice of hearing, like all
8 notices of hearings, has within the
9 statement, the modifications of the
10 proposals are within the notice of the
11 hearing, okay? That has been construed by
12 the courts not too long ago, in a Seventh
13 Circuit case which a number of us have been
14 involved in, to say that the industry is on
15 notice to issues which might come up.

16 The hearing should not be controlled
17 by representation of parties as to what their
18 plans were or anticipations were with respect
19 to the hearing. Modifications are open at
20 this hearing. And in addition, I would say
21 -- and this is very important with this

1 issue, that the status quo of the industry --
2 the status quo of regulations is always on
3 the table in a hearing necessarily.

4 Any departures -- the whole issue is
5 whether the status quo should be changed.
6 And if a modification of a proposal, in
7 essence, maintains the status quo in part,
8 it's certainly within the scope of the
9 hearing.

10 So whenever Dr. Cryan chooses to
11 testify or be called, if there is testimony
12 that someone wants to object to, of course, I
13 think that would be the time.

14 There are no procedures, by the way,
15 for motions in limine or for people to be
16 required to submit in advance what they
17 intend to present. The hearing notice is
18 there, and we all know --

19 THE JUDGE: Parties were, of course,
20 invited to submit proposals.

21 MR. BESHORE: That's right.

1 THE JUDGE: Ms. Yoviene.

2 MS. YOVIENE: I just wanted to
3 address Mr. Beshore's comment that everything
4 is on the table. And he said it in light of
5 the Alto Dairy case, which is the Seventh
6 Circuit case where Judge Posner was the chief
7 author. The case citation is 336 F.3d 560.

8 I quote Judge Posner when he says,
9 "Through this gobbledegook" -- you know, he
10 says, "Though this is gobbledegook to an
11 outsider, insiders such as the plaintiff
12 would realize that the focus of the
13 proceeding was beyond their eligibility to be
14 pooled with the Mideast producers (that is
15 what being pooled on the Mideast order
16 means)."

17 My point in citing that is that Judge
18 Posner, who cited the D.C. Circuit case for
19 the proposition that notice is adequate if
20 the parties were on -- could logically
21 conclude that the different issues being

1 raised in the hearing were the logical
2 outgrowth of the proposal.

3 And what I'm suggesting and arguing
4 to Your Honor is that Judge Posner recognizes
5 that even the industry insiders had an
6 opportunity to look at the notice, and the
7 notice gave some information.

8 And a significant portion of the
9 industry that's here, while there is not a
10 lot of other industry that's here, has said
11 the gobbledegook that we looked at, Your
12 Honor, for Proposal 1, when you put it
13 together with the chief proponents' letters,
14 when you put it together with the Notice to
15 Interested Parties, when you put it together
16 with the hearing notice and you put it
17 together with the preliminary and economic
18 analyses that USDA put together, says that
19 decoupling, changing Class I differentials
20 and all these other issues that are not
21 about change in make allowances are not on

1 the table, not the logical outgrowth.

2 THE JUDGE: Very well. Having said
3 that, it looks like it's time for an
4 afternoon break.

5 [Whereupon, the hearing recessed
6 at 2:56 p.m. and reconvened at 3:10 p.m.]

7 THE JUDGE: Back on the record.

8 Mr. Rosenbaum, before you get
9 started, you and Ms. Yoviene have raised an
10 issue.

11 As you know, I do not have anything
12 before me at this time which is not within
13 the notice. It is my understanding that
14 such information may well be presented. But
15 until such time as it is, I'm not really
16 prepared to look at it and to rule on

17 And so, once that's done, in other
18 words, I will give you an expeditious ruling
19 at that point. My inclination is that if it
20 is not fairly within the scope of the notice,
21 then I am going to exclude that proposal and

1 testimony.

2 MR. ROSENBAUM: Thank you, Your
3 Honor.

4 MS. YOVIENE: May I just interrupt
5 for a moment?

6 THE JUDGE: I think you just did.

7 MS. YOVIENE: We are having a little
8 difficulty hearing you in the back.

9 THE JUDGE: Very well. I'll try to
10 talk a little louder.

11 MR. BESHORE: Your Honor, Mr.
12 Carlson has now taken the stand and is
13 prepared to give his testimony. He has a
14 written statement which I would ask be marked
15 as Exhibit 38.

16 THE JUDGE: Very well, it is so
17 marked.

18 [Whereupon, Exhibit No. 38 was
19 marked for identification by the judge.]

20 Whereupon,

21 RODNEY CARLSON,

1 having been first sworn by the judge, was
2 examined and testified under oath as
3 follows.

4 THE JUDGE: Please be seated and
5 spell your last name for the hearing
6 reporter.

7 THE WITNESS: My name is Rodney
8 Carlson, C-A-R-L-S-O-N.

9 EXAMINATION

10 BY MR. ROSENBAUM:

11 Q. Mr. Carlson, could you please read
12 your testimony.

13 STATEMENT FOR THE RECORD BY RODNEY CARLSON

14 A. My name is Rodney Carlson. I am
15 Corporate Director of Milk Procurement for
16 Lactalis American Group. Our corporate
17 headquarters are located at 2376 South Park
18 Avenue, Buffalo, New York 14220.

19 Two of the companies within the Group
20 are makers and marketers of cheese. Sorrento
21 Lactalis, Incorporated, produces and markets

1 Italian cheeses while Lactalis USA,
2 Incorporated, produces and markets European
3 cheeses such as Feta, Brie and Camembert.
4 Cheese is produced in five plants. Three of
5 these plants purchase milk from regulated
6 handlers, and another plant is an unregulated
7 area but does pay producers on the basis of
8 Federal order Class III prices.

9 Lactalis American Group supports the
10 proposal to update the Class III and Class IV
11 make allowance. We also support the
12 testimony of Bob Yonkers from the National
13 Cheese Institute.

14 While we do not make cheddar cheese,
15 we are very aware, and we have experienced
16 the cost increases cheese manufacturers have
17 been subject to since the 1998-99 time frame
18 used as the base for the existing make
19 allowances. For example, in the one plant
20 that has been relatively consistent in its
21 operation for the past seven years, we have

1 seen a 14 percent increase in the average
2 cost of producing a pound of mozzarella
3 cheese from 1999 to 2005. This increase has
4 happened even as we increased production in
5 this plant by closing other plants and
6 consolidating operations. The plant capacity
7 was increased by over 25 percent during that
8 time in order to decrease unit costs by
9 taking advantage of efficiencies of a larger
10 scale operation. We have budgeted a 16
11 percent increase in production costs per unit
12 in 2006 as compared to 2005.

13 Examples of some input cost increases
14 during the past six years include: Average
15 natural gas costs increased 167 percent
16 comparing 1998 annual average costs to 2005
17 average annual costs. When comparing
18 December 2005 natural gas costs to 1998
19 annual average cost, the increase is 309
20 percent. The cost for a kilowatt hour of
21 electricity in December of 2005 was 22

1 percent higher than the average cost in 1998.
2 Even water costs have increased by 69 percent
3 since 1998. Labor costs have increased 46
4 percent even as the number of employees has
5 been reduced. Wage rates are up 37 percent
6 from 1998 to 2005 but medical insurance costs
7 are up by 97 percent during that same time
8 period. Retirement benefit costs have risen
9 by 259 percent in those same seven years.

10 The cost of producing a pound of
11 whey at the Buffalo facility has increased 32
12 percent during that time period of time.

13 As Dr. Yonkers states in his
14 testimony, the current situation cries out
15 for prompt resolution. Emergency conditions
16 do exist in the manufacturing segment of our
17 industry. We urge the Secretary to omit a
18 recommended decision and proceed to implement
19 an amended or interim order with all due
20 haste.

21 Thank you for the opportunity to

1 address these issues.

2 MR. BESHORE: At this point, I would
3 move Exhibit 38 into evidence, Your Honor.

4 THE JUDGE: So admitted.

5 [Whereupon, Exhibit No. 38 was
6 received in evidence.]

7 MR. ROSENBAUM: And the witness is
8 available for cross-examination.

9 THE JUDGE: Very well. Questions of
10 this witness? Ms. Deskins.

11 EXAMINATION

12 BY MS. DESKINS

13 Q. Sharlene Deskins with USDA Office of
14 Counsel. I notice in your statement you put,
15 "Emergency conditions do exist in the
16 manufacturing segment of our industry."

17 I was wondering if you could tell us
18 what would happen if the Secretary should put
19 this change in if they don't find it's an
20 emergency?

21 A. It is going to make the losses in

1 the manufacturing segment of the industry
2 continue to mount. Whether that will mean
3 plants will end up being closed, whether some
4 organizations will file for bankruptcy, it's
5 hard to say. But I can imagine those kinds
6 of things happening if this issue isn't
7 addressed rather quickly.

8 Q. Also, you put in here examples of
9 costs that have been increasing over the
10 years. Is the increasing costs what you
11 consider emergency conditions?

12 A. Yes.

13 Q. Is there anything else you would
14 consider to be an emergency condition?

15 A. Well, the increasing costs and the
16 inability for us to increase our margins
17 because of the circular pricing methods
18 that's in the Federal order program today.
19 Those are the issues.

20 Q. Thank you.

21 THE JUDGE: Other questions? Mr.

1 Yale.

2 EXAMINATION

3 BY MR. YALE

4 Q. Afternoon, Rodney

5 A. Hi, Ben.

6 Q. Where -- Ben Yale on behalf of
7 Select Milk Producers, Continental Dairy
8 Products and Dairy Producers of New Mexico.

9 You indicated there were five plants.
10 Can you tell me where they are located?

11 A. One plant is located in California,
12 one in Idaho, two in Wisconsin, and one in
13 Buffalo, New York.

14 Q. And does the one in Buffalo, New
15 York, produce cheese?

16 A. Yes.

17 Q. What styles of cheeses?

18 A. Mozzarella and provolone.

19 Q. So the Italian --

20 A. Yes, Italian style.

21 Q. And the two in Wisconsin?

1 A. The two in Wisconsin, one produces
2 the European style cheeses, specialty
3 cheeses. The other one is spreadable
4 cheeses.

5 Q. And then the one in Idaho?

6 A. Mozzarella.

7 Q. And then California?

8 A. Again, it's the specialty cheeses.

9 Q. Now, Idaho -- or first of all,
10 California has its own pricing system, and
11 they are subject to that system, right? That
12 plant is, right?

13 A. Correct.

14 Q. And by your testimony, as I
15 understand, they do not participate in this
16 price survey that was testified about
17 yesterday because they don't produce any
18 cheddar?

19 A. That is correct.

20 Q. Now, Idaho is -- the Western Order
21 has been voted out, so there is no longer any

1 regulation, particularly in Idaho, but is the
2 plant itself, does it pool on any, like the
3 Northwest, Pacific Northwest or the Central
4 Order?

5 A. No.

6 Q. And your plant in Buffalo; is it
7 pooled on an order or is it subject to the
8 state order? How does it --

9 A. It is not pooled on any order, but
10 we buy regulated milk at that facility. Or
11 milk from regulated handlers. Let's put it
12 that way.

13 Q. And the two plants that are in
14 Wisconsin, are they pooled on Order 30?

15 A. Again, no, they are not pooled, but
16 buy milk from regulated handlers.

17 Q. Now, by buying from regulated
18 handlers does not mean they have to pay a
19 minimum price, right?

20 A. Only if you want the milk.

21 Q. Well, if the -- that's a fair

1 situation because that's what the market
2 value is, right?

3 A. That's what competitive pressure is
4 a result of, yes, sir.

5 Q. Right. I mean, you have been -- and
6 we don't want to get into years, but you have
7 been in the industry for a long time?

8 A. Thank you.

9 THE JUDGE: He's also more than 25,
10 Mr. Yale.

11 THE WITNESS: Yes.

12 MR. YALE: We were working together
13 when we were six.

14 BY MR. YALE:

15 Q. And there was a period in the early
16 '80s, you know, where we had nationwide,
17 really, but even in the Mideast and Ohio, we
18 had tremendous volumes of milk that had no
19 home. Is that --

20 A. That is correct.

21 Q. And you worked at that time for a

1 cooperative, I believe?

2 A. Yes, I did.

3 Q. And although you wish to sell milk
4 at the class price, there is a lot of milk
5 that was sold below class, right?

6 A. There was, during that time frame, a
7 lot of milk sold at distressed prices, that
8 is correct.

9 Q. Right, because that was what the
10 market conditions were that allowed that,
11 right?

12 A. Correct.

13 Q. And it is the same situation when
14 you are buying from a regulated handler.
15 They can get the regulated price now only
16 because the market conditions are such that,
17 like you said, that's the price you have got
18 to pay to get the milk?

19 A. True.

20 Q. And have you ever had a situation on
21 a spot basis or otherwise to purchase milk at

1 less than class price?

2 A. Ask the question --

3 Q. Have there been occasions purchasing
4 from these regulated handlers on a spot
5 basis, maybe even to purchase milk at
6 distressed prices or lower than class?

7 A. There have been occasions when milk
8 has been offered at lower prices, yes.

9 Q. Do you have your own producer base?

10 A. Not in Buffalo, no.

11 Q. And what about in Wisconsin?

12 A. No.

13 Q. And Idaho?

14 A. Yes.

15 Q. And you have established your own
16 pricing formula for the milk you purchase in
17 Idaho?

18 A. Yes.

19 Q. Sometimes individually negotiated,
20 sometimes on a broad basis?

21 A. No. We always do it on a broad

1 basis. We treat all producers alike. And at
2 this point, all of our Grade A producers are
3 -- the pricing is based on Class III,
4 Federal order Class III prices.

5 Q. So it is Class III plus or minus
6 some basis?

7 A. That is correct.

8 Q. So those producers in Idaho, if
9 there is a reduction in the Class III price,
10 would see a reduction in their price?

11 A. I expect so.

12 Q. Now, you have, however, the ability,
13 depending on the length of your contracts
14 with those particular producers, to change
15 the basis of that Class IV, right, to reflect
16 your manufacturing costs?

17 A. Yes.

18 Q. And why isn't that the answer since
19 you are not regulated as opposed to
20 supporting a change in the --

21 A. Because we compete with milk that is

1 pooled in different Federal order markets,
2 and the competition is basically paying a
3 Class III price, and we want to be
4 competitive in our pay prices.

5 Q. Now, you made the comment of the
6 circularity of the mass and the formula, the
7 fixes, the margin and the Class III price,
8 that you are not able to recoup it out of the
9 marketplace. Is that a fair assessment of
10 your --

11 A. Yes.

12 Q. But you are not making cheddar
13 cheese, right?

14 A. That is correct.

15 Q. You are making specialty cheeses?

16 A. We are making Italian.

17 Q. Italian cheeses?

18 A. Yes.

19 Q. And those prices are not reported to
20 NASS?

21 A. That is correct.

1 Q. So you could negotiate prices
2 however you wished to negotiate them based
3 off of your basis with the CME and not
4 necessarily have to worry about it coming
5 back to affect you in the NASS, right?

6 A. That's true.

7 Q. The -- as a result of these changes
8 in market conditions and prices that you have
9 indicated, are your plants no longer
10 operating as profitable plants?

11 A. I can't say for all of the
12 facilities if that's true, but at least in
13 the one that I -- we did the study on, that
14 is true.

15 Q. And is this an older plant?

16 A. It is an older plant, but it has
17 been upgraded internally many times.

18 Q. Now, just recently, I would say
19 within the last year, Sorrento had some other
20 plants out here, is that not correct?

21 A. That is correct.

1 Q. And what did you do with those
2 plants?

3 A. We had a plant in Goshen, New York,
4 and we closed that plant a year -- just over
5 a year ago.

6 Q. Now, you mentioned in your testimony
7 some consolidation that went on. Did you
8 consolidate those?

9 A. We did bring some of that production
10 capacity into Buffalo. We also increased
11 production capacity in Idaho to make up for
12 some of the loss of production in the Goshen
13 facility.

14 Q. And one of your jobs is milk
15 procurement, right?

16 A. That is correct.

17 Q. And comparing the milk supply in
18 Idaho with the milk supply you had around
19 Goshen, is the one growing and the other one
20 not, or not as much, or how would you
21 describe --

1 A. The milk supply in Idaho is growing,
2 growing -- has been growing at double digit
3 percentages over some period of time. When
4 we closed the plant in Goshen, milk
5 production in that area had been declining
6 for something like 14 straight months in a
7 row. And, yes, it just got very expensive to
8 procure an adequate supply of milk for that
9 plant.

10 Q. Because the less supply right there
11 created a demand that your local bases just
12 got more than you could afford to do?

13 A. Well, it was one of the factors.

14 Q. One of the factors, among others?

15 A. Yes.

16 Q. Where you had to go further to get
17 the milk?

18 A. Or our suppliers did.

19 Q. Right. And this is just the nature
20 of -- somebody said we are just dealing with
21 change. That's just the nature of the

1 industry, right?

2 A. It's always in a state of flux.

3 Q. Have you had any -- with your
4 producers in Idaho, does Sorrento arrange for
5 the hauling of the milk or is it the
6 producer's responsibility?

7 A. Sorrento arranges for the hauling of
8 the milk for almost all the producers.

9 Q. And you pass that hauling cost on to
10 the producers?

11 A. Yes, sir.

12 Q. And with a rise in diesel prices or
13 other prices, have you passed on additional
14 costs to them?

15 A. Yes, sir.

16 MR. YALE: I have no other
17 questions.

18 THE JUDGE: Other questions

19 If there are no other questions, Mr.
20 Carlson, you may step down.

21 THE WITNESS: Thank you very much.

1 MR. ROSENBAUM: Steve Rosenbaum,
2 National Cheese Institute. At this time I
3 would like to call Richard Scheuerman to the
4 stand, please.

5 THE JUDGE: Very well. Mr.
6 Scheuerman. Thank you.

7 [Whereupon, Exhibit No. 39
8 was marked for identification by the judge.]

9 THE JUDGE: Mr. Scheuerman's
10 statement has been marked as Exhibit 39.
11 Whereupon,

12 RICHARD SCHEUERMAN,
13 having been first sworn by the judge, was
14 examined and testified under oath as
15 follows.

16 THE JUDGE: Please be seated, tell us
17 your name, and spell your last name for the
18 hearing reporter.

19 THE WITNESS: My name is Richard
20 Scheuerman. The last name is
21 S-C-H-E-U-E-R-M-A-N.

1 EXAMINATION BY MR. ROSENBAUM

2 Q. Mr. Scheuerman, could you please read
3 your statement.

4 A. Sure.

5 STATEMENT FOR THE RECORD

6 BY RICHARD SCHEUERMAN

7 A. My name is Richard Scheuerman. I am
8 the president and CEO of Alto Dairy
9 Cooperative. Alto is a Wisconsin-based
10 co-op, owned by the farm families from across
11 the state and the upper peninsula of
12 Michigan that provide our cheese operations
13 with over 1.5 billion pounds of milk
14 annually. We operate two cheese plants in
15 Wisconsin and pool our milk in Order 30. In
16 these plants we convert our member milk into
17 200 million pounds of commodity and specialty
18 cheese. Our cheese and its associated
19 byproducts are distributed nationally through
20 food service, industrial and retail markets.
21 Alto has 500 hard-working employees. The

1 largest of our two cheese plants in Waupun,
2 Wisconsin, is the largest cheese plant east
3 of the Mississippi.

4 The health of the U.S dairy producers
5 is tied directly to a healthy dairy
6 processing industry. Our ability to convert
7 their milk into quality product is in turn
8 dependent on our ability to earn a fair
9 return on the investments we employ in that
10 conversion process. As the leader of a
11 cooperative, it is very important to me that
12 the milk pricing system treats both processor
13 and producers fairly. It is clear to me that
14 current make allowances tip the balance
15 towards producers and to the disadvantage of
16 cheese manufacturers.

17 I am testifying today in support of
18 the proposal introduced by the Agri-Mark and
19 the National Cheese Institute to adjust make
20 allowances. Like most cheesemakers, the cost
21 of milk represents between 85 percent and 90

1 percent of our total costs. As you know,
2 these make allowances used to price this
3 milk are at least five years old. During
4 this time, the nondairy ingredient cost of
5 cheese manufacturing has risen significantly.
6 Some examples include the cost of natural
7 gas, which has almost tripled in the last
8 three years. Energy cost increases show up
9 in many other cost elements, including
10 packaging film, cleaning chemicals and
11 freight surcharges on inbound and outbound
12 goods. Similarly, medical premiums also
13 have risen by 44 percent in the last three
14 years, despite making health plan changes
15 that reduce coverage. The total impact of
16 these inflationary increases, even after
17 significant productivity initiatives, is an
18 increase in Alto's cost of production of over
19 3 cents per pound. We currently produce
20 cheese at a cost significantly higher than
21 the make allowances in today's Class III

1 formula.

2 I worry daily about the member and
3 employee families that rely on Alto for their
4 livelihood. Our ability to provide our
5 members a long-term home for their milk and
6 our employees with a long-term source of
7 income is dependent on being able to produce
8 our products profitably. We work hard to
9 control our non-milk costs, but are pressured
10 like all industries by rapidly escalating
11 utility, wage and benefit costs. While we
12 increase efficiencies every day and leverage
13 the size of our manufacturing facilities,
14 these industry-wide cost pressures along with
15 the shrinking milk-to-cheese spread which
16 resulted from the last round of dairy reform
17 have made earning an adequate return on our
18 member's equity very difficult, if not
19 impossible. We announced that our
20 cooperative lost money in our last fiscal
21 year.

1 I urge USDA to move swiftly and
2 decisively to provide immediate relief to the
3 U.S. cheese processing industry. At current
4 margins, many companies will measure their
5 future in months instead of years. If cheese
6 companies are not permitted to be financially
7 solvent, then the long-term outlook for
8 producers will be equally bleak.

9 Thank you for your consideration.

10 MR. ROSENBAUM: Your Honor, I would
11 move Exhibit 39 into evidence.

12 THE JUDGE: Admitted.

13 [Whereupon, Exhibit 39 was
14 received in evidence.]

15 MR. ROSENBAUM: And Mr. Scheuerman
16 is available for cross-examination.

17 THE JUDGE: Questions of this
18 witness? Ms. Reed.

19 EXAMINATION

20 BY MS. REED:

21 Q. Good afternoon, Mr. Scheuerman.

1 Kristine Reed, Yale Law Office, here on
2 behalf of Select Milk Producers, Continental
3 Dairy Products and Dairy Producers of New
4 Mexico.

5 I want to draw your attention to
6 Exhibit 35, which was the sheet that Dr. Ling
7 prepared --

8 A. Yes.

9 Q. -- for us and testified to earlier
10 today. I notice that your Alto, Wisconsin,
11 plant and Black Creek, Wisconsin, plant were
12 included in the 1998 data with the survey
13 that was prepared at the last hearing.

14 I also noticed that you have no
15 plants that were included in the 2004 data.
16 Is that accurate?

17 A. That's true.

18 Q. Why is that?

19 A. I think I would attribute to a
20 misunderstanding because I was not aware that
21 we needed to contact Dr. Ling to provide our

1 information. I think we would have been
2 expected to be contacted to provide that
3 information. And it was not malicious. We
4 have provided data to Mark Stevenson for the
5 Cornell study. So we would be happy to
6 provide your data if asked to do so.

7 Q. You would be happy to provide it for
8 the record in this hearing?

9 A. No, I would be happy to provide it
10 to be incorporated and aggregated with the
11 other data. I respect Agri-Mark's
12 willingness to share their proprietary
13 information, but I'm not as willing to do
14 that for the betterment of the business.

15 Q. Okay.

16 You said you have two cheese plants.
17 Could you tell me about your products at each
18 of those plants.

19 A. Sure. Both of our plants, the large
20 one in Waupun, Wisconsin, and a small
21 facility in Black Creek, Wisconsin, are both

1 capable of making American and Italian-style
2 cheeses. Right now our product is -- is
3 mostly Italian-style cheeses because they are
4 more profitable to manufacture and market.

5 Q. And do you currently make commodity
6 cheddar?

7 A. We make very, very little. We do
8 have the capability in our Black Creek
9 facility to make 40-pound blocks, but we only
10 make it when customers to whom we supply the
11 mozzarella request the cheddar as well.

12 Q. Thank you. Nothing further.

13 THE JUDGE: Other questions of this
14 witness? Mr. Beshore.

15 EXAMINATION

16 BY MR. BESHORE:

17 Q. Good afternoon, Mr. Scheuerman.

18 A. Good afternoon.

19 Q. Just a question or two about some of
20 the cost inputs that you have cited and the
21 cost increases which you have helped document

1 for the record.

2 The -- as a cooperative, I'm sure
3 you are aware that some of these costs that
4 are experienced at the plant level are simply
5 experienced at the farm level?

6 A. [The witness nodded.]

7 Q. Is that yes?

8 A. Yes, that's a yes.

9 Q. Okay. Thank you.

10 A. Sorry.

11 Q. Okay. And I just wanted to explore
12 one of them that you mentioned and Mr.
13 Carlson mentioned, medical costs. Of course,
14 every farm family has a need for medical
15 insurance, as do your employees, correct?

16 A. [The witness nodded.]

17 Q. Is that yes?

18 A. Yes.

19 Q. You need to not nod but respond
20 verbally.

21 A. Yes, sir, that is correct.

1 Q. Thank you.

2 A. Okay.

3 Q. And when you indicate that Alto has
4 been able to reduce coverage, in essence, is
5 that like by increasing employee co-pays or
6 something of that nature?

7 A. It is primary through offering
8 higher deductibles and higher co-pays for
9 drugs and office visits.

10 Q. So that the employee is sharing more
11 of the total cost of medical insurance with
12 --

13 A. That's right.

14 Q. -- with the employer?

15 A. In addition to paying insurance
16 premiums, right.

17 Q. Now, a self-employed dairy farmer --

18 THE JUDGE: As a matter of
19 clarification, is this because of what
20 products are offered by the insurance company
21 or is this your company's option?

1 THE WITNESS: This was a conscious
2 decision to reduce the cost of premiums.

3 BY MR. BESHORE:

4 Q. Now, for your owners, your farmer
5 members, self-employed dairy farmers, they
6 have got to share that all within themselves.
7 I mean, they have to absorb at their family
8 level the cost both as employer and employee
9 of the family health insurance?

10 A. That is correct.

11 Q. That's all I have.

12 A. We as employers have to induce our
13 employees to work at our facility as opposed
14 to someone -- we need to offer competitive
15 payback just so that we can staff our plants.

16 Q. I understand fully. Thank you.

17 THE JUDGE: Other questions?

18 Very well. Thank you, sir.

19 THE WITNESS: Thank you.

20 THE JUDGE: Mr. Rosenbaum, are those
21 the witnesses that you have at this time?

1 MR. ROSENBAUM: Those are the two I
2 had to get on now.

3 THE JUDGE: Very well. Thank you,
4 sir.

5 MR. Vetne, it looks like it might be
6 time for Mr. Langworthy.

7 MR. VETNE: Yes.

8 THE JUDGE: Mr. Vetne, this statement
9 has --

10 [Whereupon, Exhibit No. 40
11 was marked for identification by the judge.]

12 Whereupon,

13 RICHARD LANGWORTHY,
14 having been first sworn by the judge, was
15 examined and testified under oath as
16 follows.

17 THE JUDGE: Please be seated and
18 spell your last name for the hearing
19 reporter.

20 THE WITNESS: Richard Langworthy,
21 L-A-N-G-W-O-R-T-H-Y.

1 THE JUDGE: Mr. Vetne.

2 EXAMINATION

3 BY MR. VETNE:

4 Q. John Vetne for Agri-Mark.

5 Mr. Langworthy, you have a prepared
6 statement with some details about Agri-Mark's
7 operations?

8 A. I do.

9 Q. And that includes your experience
10 and resume?

11 A. It does.

12 Q. Proceed, please.

13 STATEMENT FOR THE RECORD

14 BY RICHARD LANGWORTHY

15 A. My name is Richard Langworthy. I
16 serve as Senior Vice President of
17 Manufacturing Operations for Agri-Mark Dairy
18 Cooperative. I have served in that capacity
19 since 1995. Prior to that, I was a Senior
20 Vice President at H. P. Hood from 1989 to
21 1995 managing several divisions, including

1 the Empire Cheese Group. From 1977 to 1989
2 I worked for Agri-Mark and its predecessor
3 cooperative serving as Senior Vice President
4 of Marketing and Commercial Operations.
5 From 1969 to 1977 I was employed by the New
6 York-New Jersey Market Administrator's
7 Office, where I served as Chief of Research
8 and Cooperative Relations.

9 I earned a Bachelor's Degree of
10 Science majoring in Agriculture Economics at
11 Cornell University and a Master of Science
12 also in Agriculture Economics from the
13 University of Connecticut.

14 Agri-Mark owns and operates two
15 cheese plants, one in Middlebury, Vermont,
16 and another in Chateaugay, New York, as well
17 as a cheese and other dairy products plant
18 in Cabot, Vermont, and a butter-powder plant
19 in West Springfield, Massachusetts. I
20 directly oversee these operations, and the
21 plant managers of each facility report to me.

1 Proposal No. 1 is such a crucial
2 issue to Agri-mark that we hoped it would be
3 useful to USDA in their decision-making
4 process if the hearing record includes direct
5 information and testimony from someone who
6 has direct day-to-day responsibility for
7 operations and product manufacturing costs.

8 The manufacturing allowances
9 currently in place in the Federal orders were
10 based upon information that included
11 Agri-Mark information from 1998. Actual
12 costs per unit of product increased at our
13 operations and continued to climb from 1998
14 forward, albeit at a slower rate of increase
15 initially. The cost increases moved up more
16 rapidly in 2004 as the costs of employee
17 health insurance skyrocketed. Energy prices
18 increased substantially in 2004 and have
19 continued to rise. As noted by the recent
20 U.S. Department of Energy announcement,
21 energy prices are expected to be even higher

1 in 2006.

2 Agri-Mark plants have taken many
3 steps to increase efficiency and lower any
4 costs possible. Since 1998, these steps
5 included:

6 1. Installing a step-down transformer at
7 Agri-Mark's cheese plant at Middlebury,
8 Vermont, to permit buying lower cost
9 high-voltage electricity directly from the
10 grill.

11 2. Drilling water wells at Middlebury to
12 avoid purchase of more costly city water.

13 3. Pre-buying forward priced energy when
14 prices warrant.

15 4. Participating in energy savings
16 programs with respective electric companies
17 in New York, Massachusetts and Vermont that
18 share costs in updating to more efficient
19 motors, lighting and refrigeration equipment.

20 5. Installed larger enclosed vats, more
21 efficient block forming towers with automatic

1 bag presenters, automatic boxers and robotic
2 palletizers at the Cabot, Vermont, facility
3 to reduce labor costs.

4 6. Purchase bulk commodity cleaning
5 chemicals to reduce cost.

6 7. Consolidated purchasing power of
7 multiple plants to control costs.

8 8. Extensive safety training programs to
9 control workmen's compensation costs.

10 9. Restructured supervision and
11 management by consolidating job
12 responsibilities of the West Springfield,
13 Massachusetts, plant to reduce costs.

14 10. Expanded recovery and reuse of water
15 at all plants to reduce water sewer cost.

16 However, even greater efficiency and
17 efforts to keep costs as low as possible have
18 not been able to compensate for the increase
19 in most costs.

20 Table 1 shows Agri-Mark's 2004 costs
21 as reported in the RBCS study for each of our

1 four plants as well as the weighted average
2 RBCS cost.

3 Costs continued to rise in 2005 and
4 2006, particularly those involving energy or
5 containing energy products as components
6 (such as certain cleaning supplies, plastics,
7 packaging, etc.). Agri-Mark energy costs
8 included in our 2004 costs more likely
9 reflect 2003 energy prices since we pre-buy
10 most of our oil and propane whenever
11 possible. However, during 2005, it became
12 more costly and difficult to pre-buy energy.
13 When pre-buy contracts are available now,
14 they are usually at rates even higher than
15 current high prices. Table 2 shows the rates
16 and change in Agri-Mark's annual average
17 energy costs for oil, propane and natural gas
18 at Agri-Mark manufacturing plants from 2001
19 to 2005 as well as locked in pre-bought rates
20 for some parts of 2006.

21 Table 3 shows the cost of electricity

1 and other energy sources per pound of product
2 at our plants in 2003, 2004 and 2005 as well
3 as the change during that period.

4 Table 4 indicates health insurance
5 costs paid by Agri-Mark for 1998 through
6 projected 2006. The number of employees and
7 cost per employee are also shown as well as
8 the percentage change in costs per employee

9 Compared to our average cost and cost
10 increases experienced in recent years, we
11 believe that the Proposal No. 1 provides a
12 conservative value for manufacturing costs,
13 but does allow our facilities to operate
14 without sustaining the multimillion-dollar
15 losses that they are currently incurring.

16 Table 5 shows the cost of moving whey
17 solids from Agri-Mark's Cabot and Chateaugay
18 plants to our central whey processing
19 facility which is part of our Middlebury
20 cheddar cheese plant. When converted from a
21 pound of whey solids to a pound of whey

1 powder, the costs per pound are \$.0189 for
2 Chateaugay and \$.0313 for Cabot whey.

3 I would be happy to respond to any
4 questions that USDA or others have in regard
5 to this information or Agri-Mark's
6 manufacturing costs.

7 Q. John Vetne, counsel for Agri-Mark.

8 On the bottom of page 2 of your
9 statement, the text describing Table 5, the
10 costs that you express there for whey, 1.9
11 cents and 3.1 cents, those are -- they only
12 reflect the portion of the per- pound or
13 calculated per-pound whey solids cost of
14 loading and transporting whey from Chateaugay
15 and Cabot, is that correct?

16 A. That is correct.

17 Q. Those are not whey processing costs;
18 those are part of the costs to the chief
19 plant of converting whey and, in this case,
20 that includes a transportation component?

21 A. Just the logistics of getting it

1 loaded out of the plant where the cheese is
2 produced, delivery to our whey processing
3 plant.

4 From my understanding yesterday from
5 Dr. Ling's testimony, he picked up in his
6 data the cost of receiving whey from other
7 plants. But that is shipping cost and not
8 receiving costs.

9 Q. Okay. But his data does not include
10 a transportation component from plants that
11 make cheese but don't produce whey powder?

12 A. That is correct.

13 MR. VETNE: The witness is
14 available.

15 THE JUDGE: Do you wish to move that
16 into evidence?

17 MR. VETNE: Yes, we do. Exhibit 40.

18 THE JUDGE: Very well. Exhibit 40
19 will be admitted into evidence at this time.

20 [Whereupon, Exhibit No. 40 was
21 received in evidence.]

1 THE JUDGE: Questions of this
2 witness? Mr. Yale.

3 EXAMINATION

4 BY MR. YALE:

5 Q. Good afternoon.

6 A. Good afternoon.

7 Q. Ben Yale for Dairy Producers of New
8 Mexico, Continental Dairy Products and Select
9 Milk Producers.

10 One of the things I forgot to ask
11 Bob, and I think you can probably answer it
12 as well, what type of products do you make at
13 the Chateaugay plant?

14 A. There are two cheese lines at the
15 Chateaugay plant. One is straight cheddar
16 and Jack. The other line is the Euro line,
17 primarily muenster but also havarti and
18 lapi.

19 Q. Do you report the sales of the
20 cheddar to the NASS survey?

21 A. Yes.

1 Oh, excuse me. I'm sorry. I
2 misspoke. I thought you were asking if I
3 reported it to Dr. Ling. Not to the NASS
4 survey, no.

5 Q. And as I understand Bob Wellington's
6 testimony, that some of that -- that the
7 cheddar is made available to Cabot for cut
8 and wrap or other retail --

9 A. That is correct.

10 Q. If you would, look at this Table 1
11 on the back of your document.

12 You have been in the cheesemaking
13 business for how long? A long time? I mean,
14 you don't have to give specific years.

15 A. Yes, quite a long time.

16 Q. You are not a cheesemaker or cheese
17 master?

18 A. I am not.

19 Q. But at the Cabot plant, you -- that
20 plant is known to produce and, by my own
21 pallet I can confirm, some pretty

1 high-quality cheese, is that correct?

2 A. That's correct.

3 Q. And to make quality cheese, there is
4 a difference in what goes in to make a
5 high-quality cheese such as that and that
6 what we sometimes call a commodity-grade
7 cheddar. Is that not correct?

8 A. There's some nominal difference but
9 not great differences.

10 Q. There is more concern on controls
11 and quality and quality ingredients and
12 management, though, to insure more consistent
13 product than with the commodity cheddar,
14 right?

15 A. I think you would probably find the
16 same level of controls in cheddar cheese that
17 you find in efficient processed cheese. It
18 would just be a different standard.

19 In other words, processed cheese
20 might have higher moistures, and we have got
21 to control that moisture because it's put

1 away for a long time, and pH's.

2 Q. Right. And those things come with a
3 cost?

4 A. Once you train people to do it right
5 and they do it right every day, there is not
6 a great deal of additional cost.

7 Q. But the products that are produced
8 at -- as you indicate, none of these plants,
9 Middlebury, Cabot or Chateaugay, none of
10 those products are considered for the NASS
11 survey of cheddar prices, right?

12 A. None of them are reported to NASS.

13 Q. Your butter plant in West
14 Springfield, is that just straight butter?
15 Is there any specialty butter, any printing,
16 any added-value products?

17 A. It's a large printing operation as
18 well as a turning operation.

19 Q. Does Cabot sell butter with its
20 brand name like it does its cheese?

21 A. It does.

1 Q. And does the name Cabot bring an
2 added value to the product?

3 A. It does.

4 Q. And that's an intellectual property
5 value. It is not one necessarily that comes
6 out of the cost of the make?

7 A. All of the value is after the bulk
8 butter is produced in terms of marketing
9 trade level and consumer level, maintaining
10 sales force, differentiating the product with
11 packaging and other fanciful things. Any
12 value added is beyond the time it comes off
13 the churn in the bulk form.

14 Q. At your West Springfield plant, you
15 also produce nonfat dry milk. Do you produce
16 any dried buttermilk?

17 A. We do.

18 Q. And the cost of that is similar to
19 the cost to produce the nonfat dry milk?

20 A. Similar.

21 Q. Now, on your whey condensing, your

1 whey processing, I think based upon what Bob
2 said, you are not producing any of this 34
3 percent dried whey or anything of that
4 nature, is that right?

5 A. No, the two pieces of data for Cabot
6 and for Chateaugay concentrate wet product
7 off the vats. At Cabot, we run it through
8 an RO and interrupt it at 18 percent solids
9 and ship it to a processing center. At
10 Chateaugay, we fractionate and ship WPC for
11 further processing at Middlebury as well as
12 permeate.

13 That permeate would be brought up to
14 something over 40 percent solids, and that's
15 applied to the cost per unit as well.

16 Q. So this 12 cents that's reported
17 here for Chateaugay, that is the cost to
18 remove it and take it to Middlebury?

19 A. No, that's the in-plant cost of
20 local filtration to separate the protein and
21 the -- the deproteinized whey or permeate and

1 the cost of evaporation of the permeate at a
2 later date, which shows the cost here at
3 Table 5, shows the cost of transporting it
4 to the Middlebury plant.

5 Q. So what is the concentration at this
6 plant, at Chateaugay?

7 A. A little over 40 percent.

8 Q. So then the processing, when it goes
9 to Middlebury, is it further fractionated
10 into different whey proteins or is it just
11 the -- does it go through a dia-filtration or
12 other process to further concentrate it?

13 A. You are ahead of me. It goes
14 through dia-filtration at that point and
15 brings the protein up to 80 percent.

16 Q. And in some cases, you actually do
17 some whey protein isolates?

18 A. The only fraction that we are
19 isolating at this point is lactoferrin.

20 Q. Even at the Middlebury plant you are
21 not producing the 34 percent dried whey?

1 A. No, we don't make -- we don't dry
2 any whole whey in the company.

3 Q. Well, will you agree that one of the
4 problems that pricing the cost of processing
5 whey is the fact that there is multiple end
6 products that come out of the dried whey?
7 The cheese -- we talked about cheddar as
8 defined as, you know, a certain component,
9 38 percent moisture and, you know, size and
10 package. But whey doesn't quite have that
11 standardization, is that correct?

12 A. There are more kinds of cheese than
13 there are kinds of whey, but --

14 Q. Well, I'm talking about compared to
15 cheddar for costing purposes.

16 A. I would say that to the extent that
17 the whole whey is used in the Class III
18 formula, that the proper way to look at it is
19 a drying up whole whey component as the basis
20 because those of us in the Order, it's a very
21 large component, the price which is based on

1 that whey price that is reported by NASS.

2 Q. And basically, the process is to
3 take the whey and to dry it to that point?

4 A. I --

5 Q. Or to take the whey that comes off
6 and just to dry it for purposes of the dried
7 whey for the NASS, and that is the price?

8 A. That is correct. We take it off the
9 vats and evaporate it, crystallize it, dry it
10 and package it.

11 Q. But those who take it off the vats
12 and proceed directly into other
13 concentrations may not be able to provide the
14 type of information that would be relevant
15 to a discussion on what it takes to take it
16 off and just dry it to that and package it.
17 Is that correct?

18 A. I would agree with that.

19 Q. Do you know what we mean by the term
20 mass balance?

21 A. I've got a rough idea.

1 Q. That's not something you use
2 internally in your plant?

3 A. We do.

4 Q. You do? And how do you -- in your
5 rough way, how do you define mass balance?

6 A. Say, in operations of a cheese and
7 whey plant, for a number of different
8 purposes, say budgeting, you need to come up
9 with where your milk is going to be, and you
10 start taking that apart and the various
11 products you are going to make. And then --
12 and you take that down to the byproducts, the
13 finished products and -- and then balance
14 your -- to your operation.

15 Q. The key word there is balance, isn't
16 it, to make sure that all of the components
17 have -- all the raw products have been
18 accounted for, all the byproducts and
19 products accounted for and the processes in
20 between, so that you can make sure that all
21 costs have been identified?

1 A. That is correct.

2 Q. As well as all opportunities to
3 market products?

4 A. Not necessarily at the plant level.

5 Q. Did you participate in preparing the
6 information for Dr. Ling?

7 A. The information came from our
8 finance records. An operation analyst who
9 reports to me directed the finance people in
10 preparing the data, yes.

11 Q. And was that put together as a part
12 of the process of a mass balance?

13 A. No, it was put together on the basis
14 of the instructions that were given by Dr.
15 Ling, or RBCS.

16 Q. And did you know at the time that
17 you were doing that that one of the purposes
18 of this process would be used to provide
19 testimony for purposes of changing make
20 allowances in Federal order hearings such as
21 this?

1 A. I don't recall the timing of that,
2 whether that -- I believe that data was done
3 prior to the notice of this hearing.

4 Q. I understand before the notice of
5 the hearing. My question was, did you put it
6 together with the idea in mind that at some
7 point it might be used for the purposes of
8 setting make allowances in a hearing such as
9 this?

10 A. It was put together with the
11 knowledge that it had been used at a previous
12 hearing and was part of the basis to come up
13 with make allowances.

14 Q. Did you make any presentations
15 yourself to USDA about the need for a
16 hearing?

17 A. I did not.

18 MR. YALE: One moment, Your Honor.

19 BY MR. YALE:

20 Q. You did not make any -- dealing with
21 your Tables 1 through 5, you are not making

1 any representations of what the cost of
2 producers have to produce the milk are, do
3 you?

4 A. No, I do not.

5 Q. And are you involved in any of the
6 -- I mean, in your part of the plant
7 manager, do you get involved in any of the
8 procurement of the milk?

9 A. I do not. Well, only to the extent
10 that we are buying outside milk
11 occasionally.

12 Q. Are you finding that you are having
13 to go further afield to purchase milk from
14 outside?

15 A. In the northernmost parts of our
16 operating area, that's been the case.

17 Q. And has that added additional cost
18 to the milk?

19 A. It has.

20 MR. YALE: I don't have any other
21 questions, Your Honor.

1 THE JUDGE: Other examination? Ms.
2 Deskins.

3 EXAMINATION

4 BY MS. DESKINS:

5 Q. I'm Sharlene Deskins with the USDA
6 Office of General Counsel. I just wanted to
7 clarify these tables that you have at the
8 back. You prepared all of them yourself?

9 A. I did.

10 Q. And all of this is from Agri-Mark
11 data?

12 A. It is.

13 MS. DESKINS: That's all the
14 questions I have.

15 THE JUDGE: Other questions?
16 Very well. Thank you, sir. You may step
17 down.

18 MR. VETNE: Your Honor, John Vetne.
19 The next witness for the proponent coalition
20 will be John Schad from LOL.

21 THE JUDGE: Mr. Vetne, it looks like

1 Mr. Schad has one exhibit which has 12 pages.
2 There are also Tables A through K. Should
3 they all be marked as one exhibit or should
4 we have two exhibits?

5 MR. VETNE: I think it would be
6 convenient to do two -- they are separately
7 stapled - if that's all right.

8 THE JUDGE: Actually, mine aren't
9 stapled at all.

10 MR. VETNE: His testimony would be
11 the next exhibit, and his tables would be the
12 following one.

13 THE JUDGE: Very well. It will be so
14 marked. His statement will be Exhibit 41,
15 and the tables will be Exhibit 42.

16 [Whereupon, Exhibits No. 41
17 and 42 were marked for identification by the
18 judge.]

19 Whereupon,

20 DENNIS J. SCHAD,
21 having been first sworn by the judge, was

1 examined and testified under oath as
2 follows.

3 THE JUDGE: If you would, spell your
4 last name for the hearing reporter.

5 THE WITNESS: My name is Dennis J.
6 Schad, S-C-H-A-D. And I have a statement,
7 and I'll start with that.

8 STATEMENT FOR THE RECORD OF DENNIS SCHAD

9 My name is Dennis Schad and I am here
10 to testify on behalf of Land O'Lakes,
11 Incorporated. My business address is 405
12 Park Drive, Carlisle, Pennsylvania. I hold
13 a bachelor's degree in history from the
14 College of William and Mary and a Masters in
15 Business Administration from Virginia Tech.
16 I have worked for Land O'Lakes and its
17 predecessor cooperatives for 25 years, and
18 my current title is Director of Regulatory
19 Affairs. Prior to this assignment, I have
20 held positions in the cooperatives'
21 marketing and transportation departments. I

1 have testified at numerous Federal and state
2 milk marketing order hearings and before the
3 agriculture committees of several state
4 legislatures.

5 Land O'Lakes (LOL) is a dairy
6 cooperative with over 4,000 dairy farmer
7 member-owners. The cooperative has a
8 national membership base, whose members are
9 pooled on six different Federal orders. Land
10 O'Lakes owns numerous cheese plants and a
11 butter/powder plant. These plants are
12 regulated under the Federal orders.

13 I testify today in support
14 of Agri-Mark's proposal to update the
15 manufacturing cost indices used to determine
16 powder, nonfat dry milk powder, cheese and
17 dry whey powder.

18 Background of Determining Class Prices.

19 Through the informal rule-making
20 process of Federal Order Reform and the Final
21 Decision of the 2000 Class III and IV

1 hearing, USDA developed a process to
2 determine class prices. This process that
3 sets Class III and IV prices replaced the M-W
4 and the Basic Formula Price Series.

5 Theoretically, Class III and IV prices are
6 now the residual of the market price of a
7 commodity (butter, nonfat dry milk, cheese
8 or whey) less the cost of converting milk to
9 that commodity.

10 Determining the class prices starts
11 with the NASS price series, which describes
12 commodity-specific products, cheddar cheese
13 in 40-pound blocks and 500-pound barrels;
14 butter in 25-kilogram and 68-pound boxes and
15 nonfat dry milk and whey in "bag, tote or
16 tanker sales." NASS reports the total price
17 received at plants for these commodities.
18 During the last few years, Dairy America, a
19 nonfat dry milk selling marketing
20 agency-in-common, increased its selling
21 price of NFDM in recognition of increased

1 energy costs. Naively, Dairy America
2 believed that a line item energy surcharge
3 would not be captured in the NASS survey and
4 the surcharge could be passed back to the
5 manufacturing plant. In actual practice,
6 NASS captured the Dairy America energy
7 surcharge in its reporting of the selling
8 price of nonfat dry milk.

9 The manufacturing allowance is fixed;
10 any increases to the selling price to capture
11 increased costs are reported to NASS and all
12 dairy farmers, regardless of whether their
13 marketing organization incurred the costs,
14 benefit from the higher class prices.

15 The second step of the process is to
16 determine the cost of converting milk to the
17 commodity whose price is quoted in the NASS
18 survey. The Department is scrupulous in
19 making sure that commodity manufacturing
20 costs are tied to the product described by
21 the NASS survey. For instance, in the

1 Federal Order Reform process and the Final
2 Rule from the 2000 hearing, USDA subtracted
3 the butter packaging cost from the RBCS
4 survey and substituted the CDFA butter
5 packaging costs. The reason for the
6 substitution was that the CDFA costs better
7 reflected the costs of bulk butter, while the
8 RBCS cost represented the cost of packaging
9 print butter. The NASS butter price reports
10 the market selling price of bulk butter.

11 The residual of this calculation is
12 the Class III or Class IV price. The price
13 is designed to be the minimum regulated price
14 for the commodity. Additionally, USDA
15 defines the Class IV price to be the market
16 clearing price and explicitly adds a
17 component for balancing costs in the make
18 allowance for Class III and Class IV.

19 Background of the Current Make Allowance
20 Calculation.

21 The Federal Order Reform and 2000

1 Class III and IV final decisions set forth a
2 process to determine make allowances. USDA
3 averaged the costs of cooperatively owned
4 manufacturing plants with the costs reported
5 the -- to by the plants regulated by the
6 California Department of Food and Agriculture
7 (CDFA). The costs at the cooperatively owned
8 plants are reported by the Rural Cooperative
9 Business Service of USDA (RBCS).

10 Manufacturing costs were presented at the
11 2000 hearing by other interested parties.
12 However, USDA found them lacking in either
13 specificity or design.

14 For the Final Decision of the 2000
15 hearing, USDA combined the weighted average
16 of all California cheese plants with the CBS
17 weighted average to set the make allowance
18 for cheese to be used in the Federal orders.
19 For nonfat dry milk, the weighted average of
20 the two lower cost subgroups of the CDFA
21 survey were combined to set the nonfat dry

1 milk make allowance to be used in the Federal
2 orders. For butter, USDA combined the
3 highest cost subgroup of the California
4 butter plants with the RBCS weighted average
5 to set the butter make allowance. For whey,
6 USDA adopted a make allowance of \$.159,
7 reflecting a higher drying cost compared to
8 nonfat dry milk and the NCI reported cost.

9 USDA recognized that the RBCS survey
10 did not include all the relevant
11 manufacturing costs. To approximate the
12 costs associated with return on investment
13 and general and administrative costs, USDA
14 added to the RBCS costs the reported ROI or
15 G&A costs from the appropriate CDFA group or
16 subgroup. Additionally, USDA added a \$.0015
17 cost per pound to the RBCS and CDFA costs as
18 an estimate of the marketing costs.

19 Charles Ling of RBCS has testified
20 earlier relating to the inadvertent error
21 contained in the calculation of the make

1 allowances from the 2000 hearing. The RBCS
2 Survey from 2000 that was presented at that
3 hearing included two butter and two nonfat
4 dry milk plants that were located in
5 California. The 2000 Manufacturing Cost
6 Annual, published by CDFA, stated that 99.5
7 percent of the butter and 98.9 percent of
8 nonfat dry milk produced in California was
9 manufactured by plants included in the
10 survey. Obviously, these two California
11 butter and powder plants were included in
12 both the RBCS and CDFA surveys.

13 Page A of LOL Exhibit 42 is the 1998
14 Dairy Product Plant Costs, as reported by
15 RBCS at the 2000 hearings. That's also
16 Exhibit 19 of this hearing.

17 Page B of LOL Exhibit 42 is the 1998
18 Dairy Product Plant Costs, as revised by CBS.
19 This report excludes the California butter
20 and powder plants. That's Exhibit 20 of this
21 hearing.

1 Page C of LOL Exhibit 42 is the
2 Calculation of the Butter Make Allowance,
3 using the data from Page A.

4 Page D of LOL Exhibit 42 is the
5 Calculation of the Butter Make Allowance
6 using the data from Page E.

7 Page E of LOL Exhibit 42 is the
8 Calculation of the Nonfat Dry Milk Allowance,
9 using the data from page A.

10 Page F of LOL Exhibit 42 is the
11 Calculation of the Nonfat Dry Milk Make
12 Allowance, using the data from page B.

13 Page G of LOL Exhibit 42 is the
14 Calculation of the Nonfat Dry Milk Make
15 Allowance, using the data from Page B and
16 with an alternative CDFA weighting.

17 When the California plants are
18 excluded from the RBCS survey, the resulting
19 make allowance calculation increases. Had
20 the RBCS evidence in the 2000 hearing been
21 correct, it is arguable that the current

1 butter make allowance would be 11.95 cents
2 (LOL Exhibit 42, page D) instead of the
3 current 11.5 cents per pounds, and the nonfat
4 dry milk make allowance might be 14.22 cents
5 (LOL Exhibit 42, page F) instead of the
6 current 14 cents per pound.

7 Additionally, had this evidence been
8 available to USDA at the 2000 hearing, the
9 Department may have decided to weight the
10 California information differently. The
11 Final Decision states:

12 "The basis for using the two
13 lower-cost groups of California plants is
14 that the mid-cost group is of a similar size
15 as the group included in the RBCS survey, and
16 that the lowest-cost California group has a
17 very similar total cost to the mid-size
18 group."

19 That's cited in Federal Register,
20 Vol. 67, No. 216, November 7th, 2002 page
21 67,921.

1 And I'll say that this is a reference
2 to the nonfat make allowance.

3 Given this revised evidence, the
4 Department may have concluded that the
5 average RBCS plant size of 29.1 million
6 pounds was not as comparable to the average
7 Group II CDFA powder plant; and that the new
8 RBCS cost of \$.1711 per pound might have
9 resulted in a different weighting selection.

10 LOL Exhibit 42, page G, shows the make
11 allowance calculation had the Department
12 chosen to weigh the RBCS costs with the
13 weighted average of all the CDFA powder
14 plants. Such a calculation would have set
15 the current nonfat dry milk make allowance
16 at \$.1451 instead of the current 14 cents
17 per pound.

18 USDA Should Include Balancing Costs in the
19 Make Allowances.

20 In the Final Decision regarding
21 market service payments in the Northeast

1 Order for balancing costs, USDA has made it
2 clear that the Class III and Class IV make
3 allowances include recognition for the costs
4 of balancing. To that point the Secretary
5 stated:

6 "The Class III and IV Final Decision
7 that adopted product price formulas for all
8 Federal milk marketing orders, including the
9 Northeast Order, gave specific recognition
10 to the costs associated with balancing in
11 the make allowance factor for setting the
12 Class III and Class IV milk price. ADCNE's
13 exception is not persuasive. As already
14 stated, the Class III/IV pricing formulae
15 include a factor to offset the cost of
16 balancing performed by butter-powder
17 plants."

18 Cited from the Federal Register/Vol.
19 70, No. 19, January 31st, 2005, page 4,953.

20 The costs of balancing the market are
21 real. At the Federal Order 1 Market Service

1 Hearing, Land O'Lakes submitted testimony
2 regarding its plant utilization at its
3 Carlisle facility (Land O'Lakes Exhibit 42,
4 page K). That table illustrates the
5 function of a balancing plant to the market.
6 In August 2001 the Carlisle plant had
7 deliveries of total milk solids at 50 percent
8 of capacity and only nine months later, in
9 May 2002, the plant received total milk
10 solids at a hundred percent of its capacity.
11 As stark as this comparison is, monthly data
12 actually mask the daily and weekly balance --
13 strike that. As stark as this comparison is,
14 monthly data actually mask the daily and
15 weekly balancing demands.

16 Fixed costs on a per-unit basis at a
17 balancing plant are high. They are built to
18 handle the demands of the highest day's
19 balancing and rarely are they filled to that
20 level for a sustained period. In most
21 businesses labor is considered a variable

1 expense. The firm can add or lay off workers
2 as the workload changes. Labor at a
3 balancing plant is treated as a fixed cost.
4 The employees are highly trained and mobile.
5 Reducing the work force to accommodate
6 fluctuating milk receipts opens the
7 balancing plant to the risk of being
8 understaffed at a critical time.

9 The Secretary acknowledged the
10 balancing function within the butter make
11 allowance when he opted for a weighting
12 calculation that resulted in a Federal milk
13 marketing order make allowance greater than
14 the RBCS adjusted weighted average cost.
15 However, the nonfat dry milk weighting choice
16 resulted in a 14 cent Federal order make
17 allowance when the RBCS adjusted weighted
18 average cost was \$.1530 per pound. In lieu
19 of its stated recognition of the costs borne
20 by some to balance the markets, the Secretary
21 might have made a different weighting

1 decision for nonfat dry milk in 2000 had the
2 Department known that the real weighted
3 average RBCS cost was \$.1711 per pound. Land
4 O'Lakes Supports the Agri-Mark Proposal.

5 Land O'Lakes owns and operates many
6 dairy plants within the United States. Among
7 them are two that are included in the RBCS
8 survey. They are the butter/powder plant at
9 Carlisle, Pennsylvania, and the cheese/whey
10 plant in Kiel, Wisconsin. Both plants were
11 also included in the RBCS Survey presented at
12 the 2000 hearing. The costs supplied to
13 RBCS were costs related specifically to
14 manufacturing the commodity product that is
15 contained in the NASS surveys. As all know,
16 Land O'Lakes markets value-added, branded
17 cheese and butter products. Except for
18 butter packaging costs (which was adjusted
19 out by USDA in 2000), specific efforts were
20 made to exclude any costs from the RBCS
21 survey related to the marketing of our

1 branded products.

2 In 2003 Land O'Lakes chose to finance
3 a portion of its business through the sale
4 of bonds. As these bonds are currently
5 traded on the open market, Land O'Lakes is
6 subject to the regulations promulgated by
7 the Securities and Exchange Commission
8 regarding insider trading. Simply put, Land
9 O'Lakes can make no material statement
10 regarding its operations unless the
11 cooperative makes this information available
12 to the general public. For that reason, I
13 must be somewhat circumspect regarding
14 specific information about our operations.
15 Land O'Lakes participated in the RBCS
16 surveys, an aggregating process which allowed
17 for our anonymity. With that said, I can
18 make some general statements about our
19 various operations.

20 On a unit cost basis, Land O'Lakes'
21 costs at its Carlisle butter plant are up

1 dramatically compared to our 1999 costs.
2 While our butter plant capacity utilization
3 has increased, our per-unit cost against
4 almost all categories increased over the
5 five-year period.

6 The same is true at our Carlisle
7 powder plant. Against virtually all
8 categories, the unit costs were greater in
9 2004 compared to 1999. While the total
10 pounds produced were greater in 2004, the
11 percentage of plant capacity declined in 2004
12 compared to 1999. This is due to a plant
13 expansion at Carlisle during 2000.

14 The per-unit costs at our cheese
15 plant in Kiel increased only marginally
16 compared to 1998. There are two obvious
17 reasons for this per-unit achievement in an
18 environment of increasing costs. First, Kiel
19 is an old plant with lower than average
20 depreciation expenses. And secondly, Kiel
21 experienced a large increase in volume

1 through the plant during the period.

2 Increased volumes and minimal plant
3 investment drove the unit cost equation at
4 the plant.

5 RBCS did not report on whey costs in
6 2000, so there can be no comparison with the
7 current reported RBCS whey drying cost. Land
8 O'Lakes' cost of drying whey in 2004 is less
9 than the average cost reported by RBCS.

10 While our costs are fairly presented, we do
11 not think them representative of industry
12 norms. The whey drying operation at Kiel
13 dries the whey produced at the Land O'Lakes
14 cheese plants in Kiel, Denmark and Greenwood,
15 Wisconsin.

16 Denmark and Greenwood ship their
17 condensed whey to Denmark for drying, which
18 allows -- I'm sorry. Strike that. Denmark
19 and Greenwood ship their condensed whey to
20 Kiel for drying, which allows Kiel to run at
21 almost 100 percent capacity. The cost of

1 evaporation activity at Kiel was determined,
2 and that cost was used as the proxy for
3 evaporating costs at Denmark and Greenwood.
4 We have not had the time to test the validity
5 of that assumption. Nevertheless, the
6 per-unit efficiency of the whey drying
7 activity at Kiel is dependent on the
8 three-plant system that has evolved in that
9 area, and we believe it is not
10 representative of the industry norms.

11 Recommendations for CDFA and RBCS Weighting.

12 Land O'Lakes supports the
13 recommendations of Agri-Mark relating to the
14 weighting of the various groups and
15 subgroups of the CDFA survey with the RBCS
16 survey. In the Final Decision USDA used the
17 criteria of relative plant size, comparable
18 per-unit costs and a recognition of balancing
19 costs as the criteria for choosing the
20 appropriate California group or subgroup to
21 combine with the RBCS survey in a weighted

1 average calculation. While it may be
2 expeditious to use the same group, subgroup
3 weightings as used in 2000, Land O'Lakes
4 recommends that USDA apply its 2000 criteria
5 to the 2004 realities. One reason for this
6 recommendation is the fact that the RBCS
7 evidence at the 2000 hearing was in error,
8 and had the Department had the correct RBCS
9 information, it may have weighted the cost
10 data differently.

11 Butter: Land O'Lakes recommends that
12 USDA combine the RBCS weighted average cost
13 with the California weighted average cost for
14 all butter manufacturers (LOL Exhibit 42,
15 page H). The average RBCS plant produced 36
16 million pounds in 2004, while the average
17 California plant ran 48 million. Adjusting
18 for packaging and applying the California
19 ROI and G&A costs plus the marketing expense
20 of \$.0015 per pound, the adjusted RBCS cost
21 was \$.1714 and the California cost adjusted

1 for marketing expense was \$.1383 per pound.

2 The weighted average of the two groups was

3 \$.1515 per pound. Land O'Lakes recommends

4 that USDA weight these two groups because

5 the average plant size is comparable.

6 Additionally, the result of the weighted

7 average is very close to the current

8 California make allowance for butter.

9 Nonfat Dry Milk: Land O'Lakes

10 recommends that USDA combine the RBCS

11 weighted average nonfat dry milk cost with

12 Group II of the CDFA survey (LOL Exhibit 42,

13 page I). The average production of the RBCS

14 group, 31 million pounds, is closer to any of

15 the other subgroups of the California survey

16 (Group II is 59 million pounds). Adjusted

17 for ROI and G&A and marketing expense the

18 RBCS weighted average cost is \$.1932, while

19 the CDFA Group II adjusted cost is \$.1748.

20 The current California make allowance for

21 nonfat dry milk is more than half a cent

1 below the most recent weighted average cost
2 and -- let me read that again, please. The
3 current California make allowance for nonfat
4 dry milk is more than one-half cent below the
5 most recent weighted average cost and 2 cents
6 below the Group II average cost. Of all the
7 commodities in question at this hearing,
8 nonfat dry milk plays the strongest role in
9 clearing the market of excess milk. Powder
10 plants balance the markets and nonfat dry
11 milk is characteristically the first product
12 offered to the CCC. For these reasons, Land
13 O'Lakes recommends that USDA use the CDFA
14 Group II nonfat dry milk series as the
15 weighting factor, which would provide a make
16 allowance of \$.1867 per pound.

17 Cheese: For this hearing RBCS
18 offered two cheese groups, an all cheese
19 group and a 40-pound block group. The CDFA
20 cheese survey reports the costs for 40-pound
21 blocks. In the CDFA survey, the three

1 plants that processed 500-pound barrels or
2 640-pound blocks had packaging and packaging
3 labor costs for 40-pound blocks substituted
4 for its reported costs. I cite the
5 California Manufacturing Cost Annual, 2004,
6 CDFA, Table 1, Sections 4 and 5, page 8.
7 For that reason, Land O'Lakes believes the
8 relevant comparison for cheese is the RBCS
9 40-pound block survey and the CDFA weighted
10 average cheese survey (LOL Exhibit 42, page
11 J). While the Group II cheese plants were
12 closer to the RBCS average production, the
13 cost per pound between the two groups were
14 too great for comparison purposes. The
15 adjusted RBCS cost was \$.1814 and the
16 adjusted unit cost for the weighted average
17 CDFA was \$.1784. The weighted average of
18 the two is \$.1794, which correlates well
19 with the current California make allowance of
20 \$.1710 per pound.

21 Whey: The Final Decision used the

1 NCI whey cost data to determine the current
2 make allowance for whey. At the hearing
3 there was persuasive testimony that the cost
4 of whey drying is greater than the cost of
5 drying nonfat dry milk. This is the first
6 time time RBCS has released a survey of whey
7 drying costs. The weighted average cost of
8 drying whey, as reported by RBCS, is \$.1155,
9 while CDFA reports a cost of \$.2673 per
10 pound. The average RBCS plant produces
11 about 10 million pounds per year while the
12 average California plant produces 31 million
13 pounds. These data are counterintuitive.
14 Land O'Lakes recommends that USDA consider
15 setting the whey make allowance based on a
16 value above the nonfat dry milk allowance.
17 We are informed that others will provide data
18 relating to the incremental cost of drying
19 whey compared to nonfat dry milk.

20 Summary and Conclusions.

21 Land O'Lakes recommends that the

1 Department increase the butter make allowance
2 by \$.0365 per pound, nonfat dry milk by
3 \$.0467 per pound and the cheese by \$.0144 per
4 pound. For whey, Land O'Lakes recommends
5 that USDA set a make allowance above the cost
6 of drying nonfat dry milk and at a rate
7 consistent with the testimony and
8 recommendations of Northwest Dairymen's
9 Association and Leprino Foods. We recognize
10 that this request represents a 31.7 percent
11 increase in the butter make allowance; a 33.4
12 percent increase in the nonfat dry milk make
13 allowance; and an 8.7 percent increase in the
14 cheese make allowance. We also point out
15 that the testimony today represents an
16 updating of cost over a six-year period.
17 Additionally, the evidence presented in the
18 2000 hearing contained an error, so it is
19 quite reasonable to conclude that the make
20 allowances for butter and powder have been
21 understated during the entire period.

1 In the last make allowance hearing,
2 IDFA spent considerable time arguing that the
3 Department should attempt to err on the high
4 side when calculating the make allowances.
5 While Land O'Lakes is a major manufacturer of
6 butter, powder and cheese within the Federal
7 order system, it is also a cooperative. Our
8 dairy farmer member-owners rely on a milk
9 price for their living and they also expect
10 that their investment in manufacturing assets
11 brings a return. I would recommend to the
12 Secretary to be like Goldilocks and get the
13 make allowance "just right." Given that the
14 CCC clears the market of excess butter,
15 powder and cheese, it would be to no one's
16 advantage in the industry to set a
17 commodity's make allowance so high that milk
18 flows to producing that commodity
19 irrespective of external market signals. On
20 the other hand, setting make allowances too
21 low discourages investment and the assets

1 needed to clear the market on a daily,
2 seasonal and annual basis. The costs of
3 maintaining market balancing facilities must
4 be borne by the market, not only the owner of
5 the facilities.

6 Land O'Lakes is well aware of the
7 class price decreases that will follow from
8 our support of the Agri-Mark proposal is 46
9 cents in the Class III price and 51 cents in
10 the Class IV. While Land O'Lakes' membership
11 isn't happy about the changes, they recognize
12 that they are currently paying for these
13 increased plant costs while the larger
14 producer market avoids them by not owning
15 plants. We also recognize the longer-term
16 and more expansive analysis provided by USDA
17 in the Notice of Hearing.

18 USDA's three scenarios offer insights
19 into the producer price impacts of the
20 changes in make allowances. Scenarios 2 and
21 3 increase the cheese make by 3.5 cents from

1 current levels) and 5 cents (from current
2 levels), which is far above our proposed
3 increase of 1.44 cents. All three USDA
4 scenarios increase the butter make at 4.11
5 cents, which is also above our proposed
6 change of 3.68 cents. Additionally, we
7 propose to increase the nonfat dry milk make
8 by 4.67 cents and the whey make allowance by
9 5.27 cents compared to USDA's scenarios of
10 an increase of 2.15 cents on nonfat dry milk
11 and 1.59 cents on whey.

12 USDA's scenarios give us an idea of
13 how varying the cheese make allowance impacts
14 producer prices and a bit of an idea of how
15 changing the other makes will impact producer
16 prices.

17 We would expect the impacts of
18 Agri-Mark's proposal on producer milk prices
19 to fall within the ranges estimated by the
20 USDA. Like the USDA estimates, we would
21 expect the impact on class prices to be

1 largest immediately following the changes in
2 make allowances. In accordance with the
3 Department's model we would expect the
4 wholesale product prices to increase and get
5 passed along to producers through the
6 classified pricing formulas. We would not
7 anticipate the longer term impact of our
8 proposed changes to far exceed the price
9 impacts on the all milk price estimated by
10 USDA in Scenarios 2 and 3. We must also
11 point out that any impacts to producer blend
12 prices by decreased Class I prices would be
13 mitigated by the MILC program, which is not
14 factored into the USDA analysis.

15 In anticipation of questions
16 regarding Land O'Lakes' financial conditions,
17 I present the following. During year 2004
18 the Dairy Foods division of Land O'Lakes
19 reported pretax earnings of \$16.4 million.
20 That amount includes the operations of the
21 cooperative's value-added and industrial

1 divisions. While Land O'Lakes has a policy
2 of not reporting in detail of its individual
3 plant operations, I can say that each of our
4 butter, powder and cheese plants included in
5 the RBCS survey lost money in 2004, even
6 given the fact that the average selling or
7 transfer price at each of the -- that should
8 read three plants, was above the NASS average
9 for the year and assuming no -- I'll say that
10 again, and assuming no procurement costs
11 were allocated to the plant. Even though
12 whey operation reported a profit, the
13 cheese-whey operation reported a loss; and
14 the favorable transfer price between the
15 Denmark and Greenwood plants and Kiel was
16 very likely an important factor in Kiel's
17 whey profitability.

18 Need for Emergency-Expedited Decision on
19 Updating the Cost Indices.

20 The testimony given today highlights
21 the increase in costs incurred by butter,

1 powder, cheese and whey plants since
2 1998-1999, when USDA last set make allowances
3 based on the manufacturing costs of those
4 years. Additionally, the defect in testimony
5 presented at 2000 further highlights the need
6 for the Department to update the butter and
7 powder make allowances based on the most
8 recent cost surveys because there is a
9 question whether those make allowances are
10 currently in error. We request that the
11 Department issue a rule without a recommended
12 decision.

13 Land O'Lakes wishes to thank the
14 Secretary and his staff for the expedited
15 manner in which this hearing was called look
16 forward to a timely decision.

17 With your indulgence, I'll just walk
18 through the exhibits. As I said, Page A is
19 an exhibit that was formerly 19.

20 Page B is Exhibit 20.

21 Page C is a calculation of the final

1 rule make allowance from the 2000 hearing
2 using the information from page A, which was
3 the testimony presented.

4 Page C is the -- I'm sorry. Strike
5 that. Page D is the calculation had USDA
6 used the same weighting system and the
7 revised cost from RBCS. At the bottom you'll
8 note that it's \$.1195 as opposed to \$.115
9 for the butter make allowance.

10 Page E is the calculation of the
11 current nonfat dry milk make allowance from
12 Page A. \$.1406 at the bottom is rounded
13 down to 14 cents.

14 Page F is the same calculation using
15 the same weight in California's RBCS with the
16 revised cost data from Page B. And again,
17 you'll note the \$.1422.

18 Page G is a calculation that the
19 Department may have chosen to use a different
20 subgroup of California to weight. Had they
21 had all the information and had they chosen

1 the entire California weighted average, this
2 is \$.1450, which is a feasible solution.

3 Page H is a calculation for the
4 butter make allowance for this hearing using
5 California ROI and G&A as additions to the
6 RBCS. Note at the bottom 31.7 cents
7 difference in this make allowance from the
8 other. And just as a point, current
9 California make allowance for butter is
10 \$.1560, and CDFA reports that that price,
11 when related to the manufacturing cost of
12 the year that this related to, covers about
13 65 percent of the state's butter.

14 Exhibit I is nonfat dry milk make
15 allowance, a calculation of Agri-Mark
16 supported by Land O'Lakes' recommendation.
17 Note that the current California make
18 allowance is \$.1520 and, at the time that was
19 instituted, covered 67 percent of the state's
20 nonfat dry milk.

21 J is the recommendation for a cheese

1 make allowance. Note that when California
2 instituted the \$.1710 it covered about 79
3 percent of California's cheese at the time.

4 K, which at the bottom right you'll
5 note that it's also Exhibit 17, Table 5 of
6 the hearing in the Northeast. I guess it was
7 the year 2003 -- 2002. And it notes on a
8 total solids level the capacity of the
9 Carlisle plant and the monthly percentage of
10 capacity.

11 That concludes my testimony, if there
12 are any questions.

13 THE JUDGE: Mr. Vetne.

14 EXAMINATION

15 BY MR. VETNE:

16 Q. Mr. Schad, your testimony and
17 recommendations combine the data from 2004
18 from California and the RBCS data from 2004
19 produced by Dr. Ling.

20 Do you also believe that the final
21 make allowance to apply, hopefully, in 2006

1 and forward should also include an adjustment
2 to reflect the very high increased costs of
3 energy between 2004 and 2005?

4 A. Our position, Land O'Lakes' position
5 on that is that we want the most timely
6 resolution to this. If updating energy costs
7 to 2005 lengthens the process of getting a
8 result, then we would say no. And we note
9 that we only submitted costs for 2004.

10 I'll say up front now that, because
11 Land O'Lakes has yet to release any numbers
12 on its profitability of its operations for
13 year 2005, I can't say anything about year
14 2005.

15 Q. Okay. Can you say this much, that
16 Land O'Lakes' costs for energy inputs are
17 likely to be close to those experienced by
18 other industries in the same region of the
19 country, changes in Land O'Lakes' costs for
20 energy inputs?

21 A. Sure. I would think that you could

1 go to an outside source and you could see
2 that the cost for natural gas or electricity
3 in our Wisconsin or Pennsylvania plants are
4 comparable to other people --

5 Q. To other industries in those states?

6 A. Yes.

7 Q. Thank you.

8 THE JUDGE: Other questions of this
9 witness?

10 Mr. Miltner.

11 EXAMINATION

12 BY MR. MILTNER:

13 Q. Ryan Miltner for Select, Continental
14 and Dairy Producers of New Mexico. Good
15 afternoon, Mr. Schad.

16 A. Good afternoon.

17 Q. I have some preliminary questions
18 about Land O'Lakes based on your statement.
19 You have 4,000 dairy farmer member-owners?

20 A. Correct.

21 Q. Where are those producers located?

1 A. As I said, we are a national dairy
2 cooperative. We have members in California.
3 We have members in the Upper Midwest, which
4 would include Minnesota, Wisconsin, Iowa,
5 the Dakotas. We also have dairy farmer
6 members in the Northeast, which would be New
7 Jersey, a few in New York, Pennsylvania,
8 Maryland, Delaware, Virginia, West Virginia.

9 Q. Of the 4,000, do you have any guess
10 as to how many would be categorized as small
11 businesses under USDA regulations?

12 A. No.

13 Q. You mention in your statement that
14 your members are not pleased at the prospect
15 of lower Federal order prices. Is that a
16 general statement that you are making or have
17 there been communications between the
18 cooperative and the membership at meetings or
19 surveys or anything like that?

20 A. That's a general statement. As I
21 said before, dairy producers are never happy

1 about lower costs, I mean lower prices.

2 However, they also recognize that the current
3 make allowance system places a cost on their
4 operations.

5 Q. The implied statement in your
6 statement in that concept is that your
7 members are willing to trade off lower prices
8 for increased plant profitability?

9 A. The answer to that is yes, and the
10 answer is they are willing to trade off on
11 having their costs incurred individually for
12 -- and have it spread across the entire --
13 spread across the market.

14 Q. But you are making that as a general
15 statement not based on any conversations,
16 surveys or meetings you have had with your
17 producers?

18 A. That's right.

19 Q. Do you have any producers who are
20 members of Land O'Lakes who would testify?

21 A. I would like to revise, that the

1 board of directors are fully cognizant of
2 what we are doing and they support the
3 action. So, yes, our dairy farmer leaders
4 know what we are doing, and yes.

5 Q. Are any of your producers, board of
6 director members or otherwise, going to be
7 testifying at the hearing?

8 A. No.

9 Q. In your statement, you testified
10 that member milk is pooled on six different
11 orders?

12 A. That is correct.

13 Q. Do you know off the top of your head
14 which of those six orders?

15 A. Federal Order 1, Federal Order 5,
16 Federal Order 33, Federal Order 30, Federal
17 Order 32 and Federal Order 7.

18 Q. Predominantly those orders that are
19 in the eastern half of the country with the
20 exception of Florida?

21 A. Well, and the Midwest.

1 Q. Okay. But the easternmost orders,
2 not -- in other words, not in 131, not in
3 126, not in 124?

4 A. Correct.

5 Q. Okay. You make a general statement
6 that Land O'Lakes has a number of plants,
7 cheese plants and one -- a butter powder
8 plant, is that correct? You only have one
9 butter powder plant?

10 A. We have a butter powder plant in
11 California in addition to the one in
12 Pennsylvania.

13 Q. The California plant, is that part
14 of the CDFA survey?

15 A. Yes, it is.

16 Q. Your numerous cheese plants, how
17 many cheese plants does Land O'Lakes operate?

18 A. I mentioned them all. I believe
19 there's three of them. Oh, and I guess
20 there's Melrose. So it would be four. There
21 are four, the three of them I mentioned,

1 Kiel, Greenwood, Denmark, and the other one
2 is Melrose.

3 Q. Can you provide for us the products,
4 the specific cheeses that are manufactured at
5 each of those plants?

6 A. Probably not.

7 Q. The Greenwood plant, does it produce
8 predominantly cheddar type cheese?

9 A. Specialty cheese, as I understand,
10 goes to dispenser, a cut-and-wrap operation.

11 THE JUDGE: Mr. Schad, you are
12 tapering off as you --

13 THE WITNESS: The Greenwood plant, as
14 I understand it, manufactures specialized
15 cheeses that go to a dispenser cut-and-wrap.

16 BY MR. MILTNER:

17 Q. And the Kiel plant, is that
18 predominantly cheddar type cheeses?

19 A. That's exclusively cheddar in
20 40-pound blocks.

21 Q. How about the Denmark?

1 A. Italian cheeses.

2 Q. Exclusively Italian cheeses?

3 A. To my knowledge.

4 Q. And the Melrose plant?

5 A. Melrose would have cheddar and also
6 specialty cheeses, Parmesan.

7 Q. In what state is the Melrose?

8 A. Minnesota.

9 Q. Minnesota.

10 If I recall, Exhibit 35 is the
11 updated information for Dr. Ling.

12 THE JUDGE: That is correct.

13 BY MR. MILTNER:

14 Q. And Land O'Lakes is listed as a
15 participant in the RBCS survey for both 1998
16 and 2004. There is a plant in, is it Perham,
17 Minnesota, is that how --

18 A. That is correct.

19 Q. -- listed in '98 and not in 2004?

20 A. That is correct.

21 Q. Is that plant closed or --

1 A. That is correct.

2 Q. And the only cheese plant that's
3 listed in the 2004 data is the plant in Kiel?

4 A. That is correct.

5 Q. Is there a reason that the Melrose
6 plant, in particular, was not included in the
7 RBCS data?

8 A. Because it's not -- product mix was
9 -- wasn't exclusively cheddar. We tried to
10 represent our costs relevant -- at a plant
11 relevant to the products that are listed in
12 the NASS survey.

13 Q. So the Parmesan cheeses and the like
14 couldn't satisfactorily -- to your
15 satisfaction, separate those costs?

16 A. We felt we would be giving better
17 data from a plant that was exclusively
18 cheddar in 40-pound blocks.

19 Q. Does Land O'Lakes participate in the
20 NASS surveys at all?

21 A. Yes. Our Carlisle plant, nonfat dry

1 milk would be reported on NASS. And Kiel,
2 the whey would be reported on NASS. And
3 there are some cheddar cheeses sold out of
4 Kiel, also, that's reported on NASS.

5 Q. Only some of the cheddar cheese?

6 A. Yes. Some of the cheddar cheese is
7 transferred internally and used in
8 value-added products.

9 Q. The NASS survey, it's a voluntary
10 survey, right? There is no obligation for
11 Land O'Lakes to participate in the survey?

12 A. I don't know the answer to that
13 question. We report. Whether we are
14 required to or do it voluntarily, we report.

15 Q. Do you report all of the eligible
16 40-pound block sales that Land O'Lakes makes?

17 A. Sure.

18 Q. At the bottom of page 2 of your
19 statement, you talk about some problems that
20 Dairy America had in trying to add an energy
21 surcharge on to some powder sales?

1 A. Yes, I know the reference.

2 Q. I'm sorry?

3 A. I know the reference.

4 Q. Okay. If NASS were to change its
5 reporting to permit the exclusion of energy
6 surcharges or other type surcharges in their
7 reports, would that be a solution in Land
8 O'Lakes' mind for the problem that they face?

9 A. I don't think so, no. I heard that
10 question asked of Bob Wellington earlier. I
11 like the simplicity in that all costs are
12 included in NASS. I would hate to have a
13 situation where some costs are excluded.

14 And the reason that I say that is if
15 you -- if you are running a powder plant and
16 you have a backlog of inventory, someone may
17 go to a customer and tell them that they will
18 sell you powder at a price -- they would mix
19 the two together in a way that would be
20 uncompetitive. I think the idea that all of
21 the -- all of the product prices go back to

1 the dairy farmers, less the fixed make
2 allowance, is the preferable way for the
3 Federal order to operate.

4 Q. Even given the cyclical effect or
5 the cumulative effect that the NASS surveys
6 have, as you pointed out in your statement?

7 A. I'm not sure what you're referring
8 to.

9 Q. Well, you said that if you add an
10 energy surcharge on it and drove the price of
11 milk up, in that situation it got fed back
12 into the pricing formula.

13 A. That is correct.

14 Q. Even given that shortcoming?

15 A. The solution is to address the make
16 allowances, not the NASS survey.

17 Q. Okay.

18 Toward the end of your statement you
19 make a comment about impacts to blend prices
20 by decreased Class I prices being mitigated
21 by the MILC program.

1 A. Yes.

2 Q. You'll note that it's not factored
3 into the USDA analysis. However, the MILC
4 program has expired, correct?

5 A. Yes, and -- agreed. However, I
6 believe that it may have still have legs.

7 Q. And it may not?

8 A. It may still.

9 Q. But even so, that would only account
10 for, depending on what version of the bill
11 may or may not get passed, 35 to 45 percent
12 of those farm losses, correct?

13 A. Yes, I -- I don't say to the extent
14 that it would mitigate that; I only point out
15 that it would.

16 Q. And only at the block and Class I
17 price of sixteen ninety-four?

18 A. That's very correct. That's true.

19 Q. The rest of those producer losses,
20 as we talked about yesterday, may not be
21 recoverable by producers?

1 A. I would rather characterize it as
2 the differences in class prices. I'm not
3 sure that it -- that you can call it all
4 producer losses, given my colloquy with Mr.
5 Wellington earlier that some of those numbers
6 that are reported are actually are producer
7 losses but only targeted to those producer
8 groups that own manufacturing plants.

9 Q. And those producer groups that do
10 not own manufacturing plants or are located
11 in geographic regions that do not share the
12 problems that Land O'Lakes and Agri-Mark
13 might be experiencing, these would all be
14 fresh and real losses to them, correct?

15 A. Yes.

16 MR. MILTNER: Nothing further, Your
17 Honor. Thank you.

18 THE JUDGE: Other questions?

19 Go ahead. Identify yourself, please.

20 MR. SLEPER: Jim Sleper from Land
21 O'Lakes.

1 EXAMINATION

2 BY MR. SLEPER

3 Q. Dennis, just to clarify a couple of
4 questions asked of you a second ago, I guess
5 --

6 THE JUDGE: Excuse me, Mr. Sleper.
7 Would you spell your name for the hearing
8 reporter.

9 MR. SLEPER: Jim, J-I-M, Sleper,
10 S-L-E-P-E-R.

11 THE JUDGE: Thank you.

12 MR. SLEPER: Thank you.

13 THE JUDGE: Sorry.

14 BY MR. SLEPER:

15 Q. Again, just to clarify a couple of
16 the questions, a question was directed to
17 you in terms of you having daily contact or
18 weekly contact or some sort of contact with
19 producers. You are in contact with field
20 representatives, are you, correct, on a
21 pretty regular basis and you know whether or

1 not --

2 A. [The witness nodded.]

3 Q. -- if I can go ahead and finish --
4 whether producers on --

5 THE JUDGE: Lets's ask one question
6 at a time, and let him give us an audible
7 response.

8 MR. SLEPER: Sure.

9 THE WITNESS: Yes.

10 MR. SLEPER: We need a little levity
11 in this thing, anyway, huh?

12 BY MR. SLEPER:

13 Q. You are also involved with regular
14 meetings in terms of our directors, delegates
15 and so forth as well?

16 A. Yes.

17 Q. In Exhibit 35, it was mentioned
18 about the Perham facility. Do you have
19 recollection -- this is kind of a minor point
20 -- recollection that Land O'Lakes did sell
21 that particular facility not too long ago?

1 A. Yes, that's true.

2 Q. Help me out in terms of -- let's
3 talk Carlisle for just a second. And in
4 terms of balancing and the role that Carlisle
5 balances the Northeast, would you say that
6 during the last, say, four years, or at least
7 three of the last four years there have been
8 some very phenomenal weather events that has
9 caused milk production to decrease in the
10 Northeast?

11 A. Yes. We had ongoing drought, and we
12 were followed with a year of an overabundance
13 of rain so that we had forage problems which
14 --

15 Q. I think it's in your -- the last
16 page, I think it's page K of Exhibit 42, I
17 believe it is.

18 A. Yes.

19 Q. You go through some volumes of, I
20 believe it's 2000, 2001?

21 A. Yes.

1 Q. Would you just characterize how,
2 say, 2003, 2004, those two particular years
3 or any other years, how the volumes came into
4 Carlisle?

5 A. 2002 was a -- from a total volume
6 standpoint with pretty good year. 2003, it
7 fell quite a bit. 2004 was a bit of a
8 rebound, but it is still -- I would
9 characterize it on a yearly basis as
10 definitely under capacity or under any level
11 of adequate capacity.

12 Q. If I made a statement such as if the
13 entire Northeast decreased by, say, 1
14 percent, would you say that Carlisle receipts
15 would decrease by much greater than a 1
16 percent?

17 A. Yes, 10 to 12 times as much, I would
18 say.

19 Q. I think you were here earlier with
20 some discussions of plants closing in the
21 Northeast, correct?

1 A. That is correct.

2 Q. Why does LOL have a balancing
3 facility in the Northeast? I mean, help me
4 out. What particular function does that
5 facility play for our dairy producers as well
6 as others?

7 A. Well, it's a balancing facility in
8 that it absorbs the daily seasonal, monthly
9 variations in both producer supply of milk
10 and sales.

11 Q. But do you also agree that it plays
12 a primary role in Class I access for our
13 producers as well as balancing the Class I
14 market, especially the Northeast?

15 A. If the question is, does milk go out
16 of Carlisle during the short season go to a
17 Class I market --

18 Q. No, I'm just stating, would you
19 agree that Carlisle provides a major
20 balancing function for the Class I market of
21 the Northeast?

1 A. I thought I said that. Yes.

2 Q. Okay. Just clarifying.

3 I know you can't talk in terms of
4 profits of each plant and that sort of thing.
5 You mentioned that in your testimony. But I
6 think you could be able to say -- let's use
7 Carlisle as an example. Has Carlisle made
8 money during the last several years?

9 A. No, sir.

10 Q. If USDA would make a change in the
11 make allowance as what we are being proposed
12 today, would you say that that change would
13 cause Carlisle's profits or the negative to
14 go to a profit, beyond red line to black
15 line, in other words?

16 A. No, it wouldn't. The costs are
17 above the weighted average at both plants,
18 given that we won't even get the weighted
19 average because it will be blended in with
20 the California. It will make things easier,
21 but it won't take us to a black position.

1 Q. Thank you, Dennis.

2 THE JUDGE: Mr. Schaefer.

3 EXAMINATION

4 BY MR. SCHAEFER:

5 Q Henry Schaefer, USDA.

6 A. Hello, Henry.

7 Q. Welcome, Dennis.

8 Just one quick I -- think we may have
9 a typo here. On page 10 of your testimony,
10 and in the very last paragraph down there,
11 where you talk about the class price
12 decreases that will follow from our support
13 of Agri-Mark's proposal. I agree with the 46
14 cents. That's what Mr. Wellington had in his
15 testimony. In fact, he actually had two
16 numbers, 43 and 46. But the Class IV one of
17 51 cents, I believe Mr. Wellington had 55.
18 Is that what you intended?

19 A. I would -- yes. The answer to that
20 is yes.

21 Q. Okay. Thank you very much.

1 A. Thank you.

2 THE JUDGE: Other questions? Mr.
3 Yale.

4 EXAMINATION

5 BY MR. YALE:

6 Q. Thank you. Ben Yale for Select,
7 Continental Dairy Products and Dairy
8 Producers of New Mexico.

9 I want to follow up on Jim Sleper's
10 question dealing with the balancing. In page
11 5 of your testimony, you mentioned that the
12 Department needs to consider balancing costs
13 in setting the Class III and IV prices. Is
14 that -- that's your statement, right?

15 A. That is correct.

16 Q. So is it your statement that -- are
17 balancing costs regional in nature or are
18 they -- for the market, or they a national
19 issue?

20 A. I think they can be both.

21 Q. What of your costs at Land O'Lakes

1 at Carlisle are national?

2 A. Insofar as we -- we have told
3 members that on a -- on a particular day we
4 have had milk from not only our own region
5 but milk as far away as Florida and far away
6 as Maine and as far away as Indiana.

7 Q. And do you get paid for that
8 service?

9 A. Do I get paid for that service?

10 Q. Not you but Land O'Lakes.

11 A. I pay for milk.

12 Q. You pay for milk? Okay. Let me
13 restate the question. Do you buy that milk
14 at the full minimum price?

15 A. On the longest day, probably yes and
16 no. If I'm talking about three different
17 sources, I'm not -- I would say that at
18 least one of them is probably less than
19 class.

20 Q. For milk to come that far, it's
21 distress for those markets, right?

1 A. I would assume so.

2 Q. And in your experience with
3 distressed milk, they are willing to --
4 obviously, they want as much as they can, but
5 at this point the minimum price isn't the
6 criteria, it's getting the best price?

7 A. And not all milk that travels that
8 distance is distressed milk.

9 Q. But my question comes down that the
10 -- the proposal that you are making would
11 reduce -- would increase make allowance and,
12 relative to particular commodity prices,
13 reduce the producer's return nationwide,
14 including the Southwest?

15 A. I agree.

16 Q. Okay. And if the Southwest has
17 dealt with and handled its balancing costs,
18 why should it take a reduced price so that
19 you can handle the balancings cost in the
20 Northeast?

21 A. As I said earlier, that Land O'Lakes

1 joined with a group, ADCNE, to argue that
2 balancing costs should be a regional issue,
3 and the Department rejected that notion.

4 Q. Maybe we need to agree with you that
5 it's a --

6 MR. SLEPER: Where were you when we
7 needed you?

8 MR. YALE: I wasn't asked.

9 One second, Your Honor.

10 BY MR. YALE:

11 Q. Are you going to -- Mr. Sleper was
12 asking about field service, and there is
13 communication with producers and stuff. Are
14 there any Land O'Lakes producers going to
15 come and testify in favor of your proposal?

16 THE JUDGE: Asked and answered.
17 Previously asked and answered.

18 MR. YALE: That's fair enough.
19 Thank you. I have nothing else.

20 THE JUDGE: Very well. Other
21 questions?

1 Very well, it's a little after 5:00.

2 We are going to recess for the day. We'll go
3 off the record at this time.

4 [Whereupon, the hearing adjourned
5 at 5:11 p.m.]

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