UNITED STATES DEPARTMENT OF AGRICULTURE

BEFORE THE SECRETARY OF AGRICULTURE

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I N D E X

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E X H I B I T S

EXHIBIT NO.	MARKED	RECEIVED
Exhibit 35	1338	1391
Exhibit 36	1338	1391
Exhibit 37	1503	----
Exhibit 38	1536	1538

P R O C E E D I N G S

8:30 a.m.

THE COURT: -- November 18th. This is day five of our hearing, and before we call the first witness of the day, anything anyone needs to bring up? Ms. Deskins?

MS. DESKINS: Judge Hillson, yesterday Mr. Rower quoted from a book, and just for the record, we'd like to say what the book was so that people know.

THE COURT: Well, this is his college textbook from 1966?

MS. DESKINS: This is college textbook from 1966. It's called Industrial Production Models, by Sven Dano, spelled --

MR. ROWER: Sven.

MS. DESKINS: Sven, spelled S-v-e-n, and then D-a-n-o.

THE COURT: And what am I supposed -- you just noting that for the record --

MS. DESKINS: Yes, because --

THE COURT: -- that that was the book he was talking about?

MS. DESKINS: Right.

THE COURT: Okay. Maybe you'll increase sales of the book for the first time in 40 years. I don't know.

MR. UNIDENTIFIED: Don't we have some instruction about why he kept it, Judge (phon.)?

THE COURT: Some people just can't throw things away.

MR. UNIDENTIFIED: Can't throw anything away?

MR. ROWER: Because I'm a dull guy (phon.).

MR. UNIDENTIFIED: Oh, no, I wouldn't say that.

THE COURT: Okay. Are we going to call -- is Mr. Van Dam going to be the first witness this morning?

MR. MARSHALL: Yes, Your Honor, we believe that Mr. Van Treek, whom we were willing to yield to is not here. So I believe by the consent of the opponents and --

THE COURT: Okay. Is there anyone else here who has -- who's going to be here only today who needs to testify today?

(No response)

THE COURT: I see no response. So Mr. Van Treek shows up or whatever, I'll squeeze him in, but --

MR. MARSHALL: I should've identified myself for the record. This is Doug Marshall with Northwest Dairy Association. And Mr. Van Dam is approaching the witness table, and I might add that there are copies of his prepared testimony in the back of the room that were not there last night. So people may want to get that if they haven't already, and I have copies for the front table here.

THE COURT: Thank you.

MR. MARSHALL: There is his prepared testimony, and there are tables, which I'd like to have marked as separate exhibits.

THE COURT: So you want his written testimony marked, is that what you're saying? Okay. Let me see. The last one I have was 34, so I'm going to mark as the written testimony, Exhibit 35 and the tables Exhibit 36.

(Exhibit Nos. 35 and 36 were marked.)

THE COURT: Mr. Van Dam, if you could raise your right hand.

WILLIAM C. VAN DAM

having been first duly sworn, was examined and testified as follows:

THE COURT: Please state your name, then spell it for the record.

THE WITNESS: My name is William C. Van Dam. That's W-i-l-l-i-a-m, C., V-a-n, separate word, D-a-m.

EXAMINATION

BY MR. MARSHALL:

Q. Mr. Van Dam, please proceed to read your prepared testimony.

A. "My name is William C. Van Dam. I am testifying today on behalf of Northwest Dairy Association, which is usually referred to as NDA. In addition, Tillamook County

Creamery Association, Farmers Cooperative Creamery, and Northwest Independent Milk Producers have authorized NDA and me to express their support for Proposal No. One. And in addition, not written in here, Inland Northwest Dairy in Spokane has also authorized me to express their support of Proposal No. One.

"Background information about NDA. NDA is a cooperative association which acts as a handler in the Pacific Northwest federal order market, Order 124. NDA markets on behalf of 603 producers as milk has traditionally been associated with the Pacific Northwest Order. Therefore, the provisions being considered at this hearing are of vital interest to NDA.

"NDA's the parent company of WestFarm Foods, which operates three class one bottling plants in Order 124. These plants are in Seattle, Washington, Portland, Oregon, and Medford, Oregon. NDA also operates four milk manufacturing plants within Order 124. These plants, all in Washington, are Chehalis, Issaquah, Lynden and Sunnyside.

"NDA has no direct connection with the Arizona/Las Vegas market order, Order 131, and does market the milk of any producers located in that area. NDA does, however, experience two factors in common which -- with Order 131 that create a bond between the two areas. First, both Order 131 and 124 border on different parts of the largest dairy state in this country, California. California has its own statewide order, and therefore is not subject to regulation by federal orders. The interface with the statewide order is both interesting and potentially troublesome to NDA, as was shown by Arizona witnesses at the Phoenix phase of this hearing.

"Second, Order 131 appears to be the order with the highest volume of producer/handler milk in the federal order system, and Order 124 is the second highest. It is the second factor that caused NDA to request a joint hearing on this issues of Order 124 of 131.

"Proposals number one and number three, regulation of producer/handlers with over three million pounds of class one sales per month, general statement. NDA cannot conceive of a valid argument that justifies the exemption from pooling of a producer who is among the largest three percent of all producers in the entire marketing area. The exemption from classified pricing of any handler who operates a bottling plant that is as large and as efficient as the plants of regulated handlers is equally unjustifiable.

"The fact that the cows and the plant are owned by the same entity does not make the current exemption fair to regulated handlers or to pool handlers -- pool producers.

"NDA has repeatedly and consistently voiced concern that the producer/handler exemption for larger operations posed a threat to orderly markets, and provided select competitors in the market with advantages that cannot be defended or sustained. These comments cannot have been missed by producer/handlers, and we certainly feel that they have been adequately forewarned of our concern and the potential for changes in the rules.

"The concept and exemption of producer/handlers has a history as long as that of the federal orders. The present exemption may have been appropriate for circumstances that pertained at the time the concepts of classified pricing and pooling were introduced seven decades ago. Dairies were much smaller then, and producers who bottled their own milk numbered in the hundreds and probably in the thousands. Home delivery was the standard, and stores were smaller and not organized into chains.

"In the 1930s it was judged politically impossible to implement these new concepts if all producers who bottled their own milk were included. At that time, there was no such thing as a producer/handler who had a significant portion of any sizeable market, and they were not the primary cause of the ruinous competition that was disrupting the marketplace.

"They were, however, numerous and as a group, they did not see any advantage to being in a pool. Therefore, as a practical and as a political matter, they had to be exempted to get the early orders up and running. The exemption is an accident of history that has survived to this day in spite of the substantially changed circumstances of milk marketing in the federal order markets.

"Revision to Proposal No. One. NDA is the proponent of Proposal No. One, which pertains to the Pacific Northwest order. There are some changes to language that we would like to offer consistent with the revisions being proposed in Order 131."

And at this point, I would like to skip the next four pages, to page six. What we have there -- have entered into the record is the exact language that is being proposed. It is exactly the same as that proposed for 131. It was done in conjunction with DFA. Our language and our reasons are consistent -- oh, and with UDA and Mr. Berde. We worked as a committee in putting this together, so without repetition on this thing, we will move to page six. Right in the middle of the page there --

Q. Excuse me, Mr. Van Dam.

A. Yes.

Q. While we're talking about the proposal which --

and its form, yesterday were you present yesterday during Mr. Hollon's testimony?

(No response)

BY MR. MARSHALL:

Q. Were you present yesterday --

A. Yes. Yes, I was.

Q. -- during Mr. Hollon's testimony? You heard him suggest that he would ponder certain potential changes to that language --

A. Yes, I did hear that.

Q. Has that pondering been finalized?

A. No, the pondering has not been finalized.

Q. But it may be that at some point that we will have additional changes to --

A. Yes, they were interesting issues, and they didn't yield to ready solutions.

Q. Thank you. Proceed to read your testimony.

A. In the middle of page six there.

"These changes were developed in coordination with representatives of United Dairymen of Arizona and Dairy Farmers of America. In its prepared testimony, DFA's witness explains the intent behind this proposal in the form of a revised proposal number three for Order 131. We agree with these comments. We feel that consistency between the two orders is appropriate, although perhaps not essential.

"Our testimony today will be directed toward the situation as it exists in Order 124, but it is the example of what is happening in Order 131 that most clearly illustrates what could happen in any order.

"My exhibit. I have prepared an exhibit which contains a series of tables. It is attached to the copies of my prepared testimony which are available for participants at this hearing."

So anybody that hasn't picked them up, there in back there. It is ready-marked as Exhibit No. 36.

"I will describe each table in the exhibit as I go through my testimony.

"Producer/handlers of Order 124. Table -- Exhibit 36, Table 1 is a set of data comparing the numbers of producers and volume of milk produced by both producer/handlers and normal pool producers. The volume data for all producers is that gathered and reported by NAS. The data related to producer numbers comes from the county statistics reported by the market administrator's office, as does the data related to production and number of producer/handlers. The data was taken from these sources to eliminate any impact of de-pooling in market boundaries.

"The table is largely self-explanatory, and I will expound on just a few points. First the similarities. In the 13 years represented in this table, there was a total increase in production of 21 percent by pool producers and 22 percent by producer/handlers. That's from 1990 to 2002.

"The number of producers decreased at very similar rates. The pool producer count decreased by 49 percent, and while that of producer/handlers decreased 53 percent. It would appear that the overall economic pressures impacted both groups in similar ways.

"Second, the differences. The most obvious difference between the pool producer and the producer/handler is in average size of operation. The average pool producer markets approximately 833,000 pounds of milk a month, while the average producer/handler produces 2,627,000 pounds of milk a month. The average producer/handler is more than three times bigger than the average pool producer, and their dairy farms are among the largest in the entire Pacific Northwest market area.

"Additionally, the trend line for the last seven years, 1995 to 2002, is that the average producer/handler is growing in size faster than the average pooled handler." I think I meant pooled producer there.

Q. Did you mean --

A. I know I did.

Q. -- average pooled producer?

A. Yeah, average pooled producer. There's no handler data on this table.

"Small business. With the above background then, I would like to point out that the public policy considerations to support small business overwhelmingly argue for insuring that the producer/handler exemption does not injure the 933 pooled producers who are, as far as we know, mostly within the definition of small business. It may be that the potentially regulated producer/handlers also are within the definition of small business. However, we point out that many of the smaller regulated plants fit into this definition also.

"The producer/handler advantage. NDA concurs with the procedure used in prior hearings that analyze the producer/handler advantage by looking at the difference between the class one price and the blend price. A regulated handler does pay the class one price. If a producer/handler were to do an economic analysis to accurately measure the success of the plant and distribution part of his operation, he would value the milk used in his plant at the classified price in the order because that reflects the value of the milk cost of his regulated competitors.

"Even if this calculation resulted in a loss that would show -- resulted in a loss, it would show management how their plant measured up to the competition. If the producer/handler were operating his business with the concept of maximizing his income, this would be a number of great interest.

"In exactly the same manner, the dairy farm portion of the operation should measure its success against the blend price in the market. The blend price is real. It is available to the producer/handler, should he choose to sell his plant or otherwise become subject to regulation. The manager of the dairy farm will, or should anyway, insist that he gets at least that price in calculating his own performance. I should add that many years ago, I worked for a while for a producer/handler, and my analysis used the approached just outlined.

"These two values of milk, one to the plant and one to the farm, are obviously different prices. Assuming the producer/handler uses some form of enterprise accounting, this difference in value would be a third source of income or profit. One that exists solely because the producer/handler -- of the producer/handler exemption in the order.

"The other two profit centers are the dairy farm and the milk processing and distribution. Of the three, I can assure you that only one of them, the producer/handler exemption is the likely to always be profitable.

"Exhibit 36, Table 2 calculates the difference between the two milk values each year from January through -- January 2000 through October 2003 with the assumption that 100 percent of a producer's -- producer/handler's milk is sold as class one. The average difference for the 46 months included in this time period is $1.79 per hundredweight, which works out to 15.4 cents per gallon of milk.

"The blend price used in this table is the actual, reported price. The variation in the spread from year to year is related to, (a) very significant differences in class three and class four prices, which because of the higher of class one pricing will tend to push the class one price higher, while at the same time the lowered -- the lower priced of class three or four will reduce the blend price, and (b) de-pooling opportunities when taken will always reduce the volume of the higher priced of class three or four pool, which in turn will lower the blend price.

"Exhibit 36, Table 2(a) is the same calculation, except in this case, we have adjusted the class one usage to 85.5 percent achieved by producer/handlers in the Pacific Northwest order in the three full years, 2000 through 2003. The 85.5 percent number is from Exhibit 3 --

Exhibit 36, Table 3, which adds to the reported route distribution sales by producer/handlers, the sales of surplus bulk milk used as class one to unregulated areas, Alaska, as reported in the market administrator's Exhibit 7, Table 6, which was prepared as our request.

"For the purposes of this table, we balanced the pool for the producer/handler with 14.5 percent of their milk assigned a value equal to the lower of class three or class four. This was done in spite of the fact that the same MA exhibit, which reports the usage of producer/handler surplus milks shows that approximately half the surplus was either used in his plant as class two or was moved to plants that reported its usage as class two.

"The intent of Table 2(a) is to show the worst possible likely producer/handler blend price. Even this worst case scenario leaves the producer/handler advantage -- leaves a producer/handler advantage of $1.33 per hundredweight, or 11.4 cents per gallon. I and others who have experience in selling packaged milk to wholesale accounts know that even 11 cents is an incredible advantage. This is a business where normal competition causes business to change hands for fractions of a cent per gallon. The 11.4 cent worst case cost advantage held by the producer/handler is many times bigger than the price difference that separates traditional, regulated competitors.

"There is simply no possible way for the regulated handler to compete with the prices that the producer/handler could, and often does, offer. This advantage is far bigger than that needed to acquire new business, and by this I mean, that a producer/handler does not need to use even a significant portion of his advantage to get new business. He just needs to be a bit lower than the competition. The balance of the advantage remains his margin, profit if you will, that goes to the producer/handler.

"Dan McBride of NDA, among others, will testify concerning competitive milk pricing by producer/handlers. Quite often the price quoted to customers by producer/handlers is much lower than what is needed to meet the competition. To the extent, this reflects the advantage producer/handlers enjoy from not being regulated. We contend that this is an arbitrary wasting of an economic benefit designed by Congress to be available to all dairy producers in the market-wide pool.

"It is disturbing to see that some of the quotes we have seen are for prices as much as 45 cents less per gallon than the prices quoted by regular handlers when federal order prices are high. That is considerably more than the advantage available to the producer/handler. If this is indeed happening, the producer/handler is netting less than the blend price that would be paid to a pooled producer. This flies in the face of normal pricing and marketing logic.

"One explanation of such low pricing may be that the producer/handler is buying a long-term customer through fixed price contracts that do not increase at times, like the present, when class one price mover (phon.) is high. This is really not a satisfactory answer because every producer knows what the currently classified pricing umbrella is. It may also be explained by the fact that there are so many producer/handlers in Order 124 that they are competing among themselves for the limited business available.

"We conclude that this pricing is an excellent example of the kind of price competition that occurs in the absence of regulation, and which gave rise to the concept of disorderly marketings. Indeed, this hearing record is already demonstrated enough disorderliness that the secretary should act to put a stop to it.

"The dollars available to the producer/handler, whether kept or wasted, exists because of the milk pricing laws designed to improve the income of all producers. The Agricultural Marketing Agreement Act calls for these funds to be 'distributed equally.'" That was in quotes. "Distributed equally among all producers, rather than squandered in competitive excess. It is very difficult to reconcile the existing, unequal distribution of class one premium income with the language and the clear intent of the order programs enabling legislation.

"Balancing costs. One of the primary justifications given for the current exemption is that producer -- that the producer/handler must bear the full costs of balancing his milk supply without burdening the pool producers. Federal order theory then permits the exemption as long as the producer/handler does not shift a balancing burden to the regulated producer and to the plants in the pool. The reasoning is that since the producer/handler does not share its class one proceeds with other producers, then in all fairness, he should not then be allowed to shift to those producers any of the costs of balancing his own milk supply.

"NDA contends, and the evidence submitted shows, that the way producer/handlers market today, most do and almost always will use the pool to balance their milk supply. This goes beyond the obvious fact that by selling to distributors or to stores that carry milk from regulated handlers, the regulated market is there to fulfill any shortage they may have.

"Another very important point in understanding this issue is to consider the incentive that exists for the producer/handler to avoid selling any surplus milk to a manufacturing plant. It is a fairly standard procedure for a manufacturing plant that is willing to purchase surplus milk to pay the seller the lowest of class three or class four. If manufacturing plants are full, they will often pay even less than the lowest class price. This gap can be as big as $3 a hundredweight.

"Producer/handlers become very innovative in avoiding this cost, for that is what they judge it to be, a cost. We know that it is common for producer/handlers to sell surplus milk to regulated handlers, thus displacing pooled milk and pushing the balancing burden back onto the pool. There is no evidence whatsoever that any producer/handler considers it an obligation to make sure that he has paid the full costs related to the sale of his surplus milk.

"We define surplus milk for a producer/handler as that milk above his own bodily needs. To understand this number, we asked the MA's office for a report that shows the disposition of producer/handler surplus milk since January 2000. The result is Table 6 in the MA's Exhibit No. 7.

"To avoid the impact of restricted data on the report, I calculated percentage based only on the full year of 2001 and year-to-date for 2003. The resulting disposition of producer/handler surplus milk was, 27 percent of it went to class one, sales to other bottlers, 52 percent went to class two, used in ice cream or sold to class two plants, and only 21 percent was used as class three or class four combined.

"To the extent a producer/handler's milk is sold anywhere but a manufacturing plant, it will always replace a sale that would otherwise have been made by a pooled producer or his cooperative. Even though the producer/handler's sale to a bottling plant would be down allocated to class four or class three, it still backs out pooled milk of that plant into the pool balancing plants, contradicting the principle that a producer/handler balances his own supply."

The ice machine's behind me.

"Current rules allow the sale of surplus producer/handler milk to regulated handlers, even though the rest of the pool balances that sale. Unfortunately, that issue is not directly before this hearing.

"I also want to point out that the down allocation rules do not fully protect the pooled producers. If the bottler buys enough from a producer/handler that some is allocated to class two, this removes class two differential dollars from the market-wide pool. And if some is allocated to class one, the pool receives only the difference between class one and the blend price, not the full class one differential.

"As Dan McBride will testify from his experience, some producer/handlers sell their surplus to an unregulated bottling plant in Alaska that also buys from NDA. By selling to class one or class two bulk milk uses in Alaska, the producer/handler has also taken away from the pooled producers who would otherwise be supplying that market, the entire value of the class one or class two differential. And again, the burden of handling his surplus has been shifted to the pooled producers, violating once again one of the primary assumptions justifying the producer/handler exemption.

"Loss of class one sales to the pool. Classified pricing was introduced into the law to protect dairy farmers from the effects of unstable and mostly low milk prices caused by milk handlers fighting for market share with low prices. Older observers may remember what were dubbed 'the milk wars.' Classified pricing did stabilize the prices, but caused a second war over who would get to serve the markets with the highest valued class one milk.

"To correct the abuses that occurred, the pooling and equal distribution of the premium generated was added to the marketing plans. And except for an occasional hiccup, the concept worked well to achieve the stated objectives.

"The amount of dollars that do not make it to the PN -- Pacific Northwest order pool because of the producer/handler exemption are significant. The best measure of this is the line called 'Producer/Handler advantage' shown on Exhibit 36, Table 2. If the volumes of class one sales now in the hands of exempt producer/handlers were put back into the pool, along with the matching milk production, the net gain to the pool would be the class one price, less the blend price paid to the producer/handler.

"Exhibit 36, Table 4 shows the dollars taken from the PNW order pool by all producer/handlers in the three previous, full years. In calculating this number, we have included the non-pool sales of surplus producer/handler milk as class one. If the larger producer/handlers were regulated, then all sales to Alaska would once again be from regulated sources, and would add to the class one volumes in the PNW order.

"The table shows in excess of $4 million worth of premium dollars, do not appear in the pool each year. Approximately 70 percent of this is taken from the pool because the activities of those producer/handlers who are larger than the proposed three million pound limit. The net impact on the pool blend price is approximately four cents per hundred weight.

"NDA believes it is contrary to the stated purposes of the Agricultural Marketing Agreement Act to allow this amount of class one premium dollars to be concentrated in the hands of so few producers, producer/handlers, instead of being equally distributed to all producers through pooling.

"Uniform handler prices. Fundamental milk pricing theory and the law hold high the concept of the uniform handler prices. It simply cannot be argued that this exists when one type of competitor, the producer/handler has a competitively sized plant that is not subject to classified pricing. Paul Arbuthnot, formerly president of Sunshine Dairy in Portland, Oregon has previously testified how difficult, impossible really, it can be to compete with a producer/handler.

"The threat to federal order milk pooling. Of far greater importance than the four cent reduction in pooling is the principle involved and the potential upheaval in our industry if these proposals are not adopted. A basic tenant of federal orders is the equal sharing of class one proceeds. This concept is the very heart of federal orders.

"We are concerned that the presently unlimited producer/handler exemption can and will be used to drain our pool of its class one dollars. As the larger producers in our market begin to be aware of a pool dwindling gradually toward a blend of manufacturing milk only, they may follow the example of those who are producer/handlers and will begin to bottle and distribute milk. They will be unregulated and will compete vigorously for their share of the market.

"Certainly this competition will cripple the competitive position of the regulated handlers, and in time, will drive them out of the marketplace, or more likely, force them to force the producers supplying them with milk to sell their milk at less than class one prices. These are exactly the conditions that existed 70 some odd years ago that led to the laws setting up the federal orders.

"The worry about the threat to the federal order system is not new. What is different at this time in both the Phoenix and the Seattle markets is that some have actually taken advantage of the exemption to a degree that so impacts the market that others will be tempted to follow. The result is a self-financing juggernaut that can use its unregulated advantage to strip all the large volume accounts from the regulated handlers.

"I know from my personal discussions with -- that the interest level among larger producers is very high. I am aware of a large producer in Oregon who has openly discussed the possibility of becoming a producer/handler, and I know from conversations with producers that others have at least considered the possibility.

"The economic incentive is high for a producer who may see a potential gain of $1.73 per hundredweight. A high volume discount store will also drool over the opportunity to share some of this gain in order to price milk even lower at retail. The parties cut out of this game are the regulated handler and the pooled producer. But as they become less competitive, their best solution may be to join them if they can't beat them. And as this trend accelerates, the pooled class one dollar amounts decline, and gradually, what the rest of the producers can gain from the federal order system diminishes.

"The Arizona model can be repeated (phon.) in any federal order. People watch, and they learn. Unless the producer/handler exemption loophole is plugged or at least limited now, the future of the federal order is very bleak indeed.

"The case for the three million pound limit. A producer/handler is both a producer and a handler. In establishing the three million pound limit, we considered the impact of the limit on each part of the operation.

"In the Pacific Northwest market during May 2002, there were only 22 producers out of a total of 933 producers whose production volume exceeded three million pounds for the month. This number of 22 comes from the analysis of hauling charges and producer milk by location and size range of production, Pacific Northwest and Western federal orders, May 2002, staff paper 02/03, published November 2002, page 13, Tables a-5 and a-6, Seattle Market Administrator's office, by Chris Warner (phon.).

"These 22 producers represented only 4.4 -- no, 2.4 percent of all producers. In May 2003 or Table 1 of the market administrator's Exhibit No. 8, the three largest producer/handlers have average class one sales of 4.7 million pounds. By definition, these three producer/handlers will have production that at least equals and more likely exceeds, their class one sales. So the three large producer/handlers will join the other 22 producers that produce in excess of three million pounds per month and will be among the largest three percent of all producers in the Pacific Northwest order.

"Others will present evidence at this hearing of the cost advantages of the larger dairy farms. There is no point in repeating that evidence. The salient point is that there is absolutely no reasonable basis to continue to grant an exemption to producers who already have economies of scale on their farms, that only three percent of the other producers in the market can match.

"Compared to a pooled producer of the same size, the producer part of the producer/handler operation has not one penny of extra cost just because the operation also happens to own and operate a plant. In fact, in many cases the producer who is also a handler has a significant cost advantage in that many, but not all, producer/handlers have the dairy farm located on the same property as the plant, and therefore have no raw milk hauling costs.

"Farms producing more than three million pounds per month are typically very efficient. It makes no sense to give them a regulatory advantage that is not available to smaller farms.

"Handler. The right size at which to include the handler part of the producer/handler operation in the pool is not as clear as the producer's side. The plants of producer/handlers, even those over the proposed limit, are not bigger than 97 percent of the regulated plants in the market.

"The choice of three million pounds for the limit has an intuitive and a political side to it. The political side is that the three million pound number first circulated among proponents because Congress chose to exempt plants smaller than that from the 20 cent per hundredweight assessment for the processor funded promotion program. We understood the goal was not to burden smaller plants with that 20 cent assessment and that the three million pounds was the size below which Congress felt the burden to -- would be unfair or excessive.

"More importantly, after careful review of available data, we find that the three million pound threshold has solid economic support for the purposes of both the congressional assessment and the issues at this hearing. As noted earlier, NDA's subsidiary, WestFarm Foods, operates three class one bottling plants in Order 124. This provides a wealth of actual detailed data from which to draw comparisons of size versus operating costs.

"Only one of those plants runs at volumes close to the three million pound level, and Mr. Dan McBride in following testimony will share the details of the study of that plant.

"The points of this study that are most important to our discussion are the numbers generated within WestFarm Foods are quite similar to those presented earlier at this hearing by Mr. Carl Herbine at the extremes. That is, for the smallest and for the largest plants, there -- they match up well. The WestFarm Foods data clearly support a cost trend line that shows costs decrease as plant size increases.

"Number two, the difference between the data groups is that the WestFarm Foods study indicates that costs decrease more quickly than is indicated in the Herbine exhibit. Our data shows that somewhere past 2.5 million pounds of volume per month, cost per unit, begin to drop dramatically.

"The cost decrease per gallon of product from 2.5 million pounds per month to one that does three million per month is approximately ten cents a gallon. This data shows that at about three million pounds, the cost savings at the plant offset the producer/handler advantage of 11.4 cents shown in Table 2(a) of my exhibit.

"In our view, the purpose of the three million pound limit is to establish a size beyond which it is no longer reasonable to exempt a producer/handler. The three current producer/handlers that exceed the three million pound limit average 4.7 million pounds of class one sales. As shown in the MA's Exhibit 8, Table 2, the average size of these operations already exceeds the average size of the smallest third, that's six plants, of the regulated plans -- regulated plants in Order 124 by more than 750,000 pounds per month. There is no reason to exempt these plants based on their small size.

"To illustrate this point further, we have used the limited market information available to us to estimate the bottling volumes of the smallest 20 plants in the Pacific Northwest order and rank their estimated volumes from smallest to largest."

I won't read every one of these into the record. You can see the breakdown on that, and you'll notice over to the right, we give the regulatory status, whether they're producer/handler or not.

I will read the notes that are associated with this. The notes say that Vitamilk went out of business in August. That's of this year. Norman Brook went out of business in September of this year, and I believe -- yeah, it was in October, Country Morning Farm in Othello had a fire which destroyed its plant, and we have no knowledge of whether they're going to rebuild or not. So there are substantial changes going.

"We include them because all three of these are included in the market administrator's exhibits for this hearing. I would like to emphasize that these are only rough estimates. The MA's office has available to it the accurate information needed to rank the plants in the Pacific Northwest order, and we urge them to verify these numbers for the order formulation branch if that is permitted. For our purposes at this hearing, however, these estimates are sufficient to demonstrate the point that producer/handlers are not necessarily the smallest handlers.

"We conclude from our ranking that the two largest of the producer/handler plants are larger and presumable for that reason, more efficient in bottling than eight fully regulated plants, and nine if you include Vitamilk. The smallest of the producer/handlers that would be regulated by our proposal, Mallory's Dairy, would be larger than two fully regulated plants and about the same size as WestFarm Foods plant at Medford, which is owned by producers cooperatively.

"There's no reason to exempt the producer/handler plants based on their size or their being a small business. To demonstrate that hypothetically, note that if the largest company in the Northwest, Microsoft, were to buy one of the producer/handler operations, it would still be a producer/handler and still be exempt from regulation.

"Alternatively, when a tiny bottler like Valley of the Road (phon.) does business without its own cows, it is fully regulated. This is not about small business. It is about a competitive equity and the statutory principle of uniform pricing. Small, regulated plants deserve a level playing field.

"NDA suggests that in determining the appropriate threshold for regulation, the fundamental policy that should govern USDA's thinking is the requirement that uniformity and pricing found in section -- 7 USC Section 608(C)(5)(a) which reads in pertinent part: 'Such prices shall be uniform as to all handlers, subject only to adjustments for: (1) volume, market, and production differentials customarily applied to the handlers subject to such order, (2) the greater quality of the milk purchased, and (3) the locations at which delivery of such milk or any use classification thereof is made to such handlers.

"That price regulation on producer/handlers as within the secretary's authority is clear from Section 608(C)(5)(c) which reads, 'In order to accomplish the purposes set forth in paragraph (a) and (b) of this subsection, providing a method for making adjustments in payments as among handlers (including producers who are also handlers) to the end that the total sums paid by each handler shall equal the value of the milk purchased by him at the prices fixed in accordance with paragraph (a) of this subsection.'

"In our view, the uniform pricing goal in Section (A) should be accomplished as suggested under Section (C). The smaller handlers properly receive an exemption which clearly is an adjustment of sorts based on volume, to the end that the total sum paid by each handler approximates the class values. Specifically, NDA believes that the evidence in this hearing will show that producer/handlers below three million pounds have inefficiencies in processing that raise their overall costs to the point where they, in reality, have no cost advantage over a regulated plant, even with the 20 cent promotion assessment that also gets added when a plant exceeds three million pounds per month.

"On the other hand, producer/handlers with greater volumes have processing costs that are similar to regulated plants, so there's no justification for avoiding uniform pricing in their case. The marketing activities of a producer/handler does not begin to have disorderly impact on the marketplace until the dock costs of the producer/handler are lower than those of the regulated handler. The evidence shows that this occurs when the producer/handler's volume crosses the three million pound per month of bottling volume.

"To summarize our argument, we suggest that the volume of producer/handlers is a relevant consideration for exemption or regulation. And in determining the volume level, the key consideration should be to insure, insofar as possible, uniformity in milk costs between producer/handler plants and the regulated plants after consideration of such additional volume of related costs as higher processing costs, the 20 cent per hundredweight promotion assessment, or anything else. We submit that a producer/handler whose volume exceeds three million pounds per month can compete effectively on the level playing field even though fully regulated.

"Another point worth noting is that the largest producer/handlers represent about 70 percent of the total class one sales of the nine producer/handlers. Adoption of this size limit would reduce the portion of the market's total class one sales held by exempt producer/handlers to about three percent, which we can accept as a not disruptive volume of class one sales. Thus, the proposed level of regulation accomplishes another primary purpose of the milk order program, that of preventing disorderly markets.

"Disorderly markets. The current unlimited exemption of producer/handlers has led to disorderly market conditions. The goal of preventing disorderly markets is one of the key concepts of the federal order system, along with uniformity of pricing as discussed above.

"The federal orders have prevented disorderly markets in part through the adoption of market-wide pooling. During the early years of the federal orders, other approaches were tried, including individual handler pools. That approached was discarded because it led to competition among producers to compete for access to the more favorable handler pools.

"I note that the analysis I use above to derive producer/handlers' regulatory advantage based on utilization is essentially the analysis of a handler pool with only one producer. For all the reasons that individual handler pools create disorderly markets when they involve many producers, the same result can occur when a handler pool contains only one large producer instead of many small producers.

"Disorderly marketing among producers can occur in either the market for raw milk or in the market for bottled milk. NDA producers own three bottling plants in the Pacific Northwest market, as noted above, and they compete with individual producers who do business as producer/handlers. When they compete in the wholesale market, we have the classic situation of competition among producers for the class one market. Albeit, a competition in the form of bottled milk versus bulk milk. Even though it is cooperative producers who own a plant, competing with the individual producer/handlers who own their plant, it is still competition among producers for the class one market.

"It's a similar disorderly market situation which needs to be remedied in the same way as was competition between handler pools. That is, by regulations which put all the producers into a market-wide pool to create a level playing field. The traditional approach to disorderly marketing of bulk milk has been to bring producers, and we propose that this should include producer/handlers, into the market-wide pool. At the same time, this addresses the problem of the non-uniform pricing among handlers, which the exemption for producer/handlers creates for regulated, bottling plant operators.

"In the example I have used, I describe disorderly marketing among producers by citing competition between a producer/handler and a producer own, that is, cooperatively operated bottling plant. Taking this a step further, however, when those disorderly markets occur, there is little difference between the negative impact on a pooled producer who ships to a proprietary plant compared to the negative impact on a producer who ships to a cooperatively owned plant, other than the amount of investment that may be at risk by the cooperative member.

"This can be seen by the recent closure of Vitamilk Dairy in Seattle, which we believe is at least in part the result of competition from large producer/handler plants in Washington State. The producers who shipped to that proprietary plant lost their market, and may enjoy less favorable market opportunities in the future. I make the latter statement because those producers now have the choice of shipping to NDA or to DFA, and from what we understand, based on our discussions with these producers, they will have a greater hauling cost with either cooperative, and they will have no opportunity with either cooperative to market under the free farm label program that had returned a bonus to them.

"In our view, their demise was a result of several factors. One was competition from producer/handlers, which the management of Vitamilk Dairy has discussed with me and with NDA personnel many times over the years, and testified to earlier in this hearing. There were other factors as well, including the consolidation of the grocery chains, which limited market opportunities for them. But when that consolidation occurred, they, that's Vitamilk and WestFarm Foods, both focused on the remaining market, much of which is handled by independent distributors.

"In both our case and Vitamilk's, the distributors typically buy cheap gallons from the larger producer/handler plants to sell along with a full line of products from the regulated plants from whom they also buy products. Dan McBride's testimony will further document how that occurs.

"NDA respectfully submits that this is evidence that the producer/handler exemption creates competitive harm by undercutting regulated plants. We also respectfully submit that this harm is the direct consequence of a competitive environment which is disorderly, as exempt producer/handlers cut price in order to take and maintain that business.

"We respectfully submit that this disorderly price competition pits one group of producers, exempt producer/handlers, against another group, those in the pool. Finally, we respectfully submit that this fact pattern is as clear a case of disorderly market conditions as any fact pattern previously found in any prior decisions by the secretary that remedied disorderly markets, and that the solution is to bring the larger producer/handlers into the market-wide pool.

"Proposal two, same size packages with similar label limitation. NDA supports the wording and concept of proposal two. The limitation proposed, however, speaks to just one of a variety of ways that a producer/handler can take advantage of the regulated handlers to, in effect, balance his milk supply.

"A -- the producer/handler in this situation addressed by this rule simply bottles gallons of milk in his own label until the milk supply is used up. If the amount delivered was not enough volume for the store, and it was surely planned that demand would exceed supply, the store's other milk supplier, a regulated plant, would delivery enough gallons in a similarly labeled package to fill the store's needs. In this way, the producer/handler could always clear 100 percent of his milk at near class one prices in a single package size while the regulated handler would then deliver all the other milk products plus have some sales of gallons.

"The store mentioned in the previous paragraph could just as well have been a distributor who buys from multiple sources. Mr. Dan McBride of NDA staff will in testimony following mine describe exactly how this is occurring.

"A critical point that a regulator must consider is that a producer/handler is not limited to finding traditional, full product line customers that can effectively market to a limited -- but can effectively market to a limited portion of sales to a customer. The portion invariably will be the largest volume, most easily bottled package, the gallon.

"The overall problem is not solved by this proposal. The same trick can be accomplished nearly as effectively by using different labels, and it will be an endless task to keep the rules coming fast enough to keep up with the variations that could occur.

"Outright prohibition of the sales of gallons only is one logical conclusion of such a rule, but that would be such an infringement on normal business affairs, that it would quickly be judged a regulatory over-reach. Indeed, as a business strategy, a regulated handler may decide to specialize in the high volume gallon trade. In the scope of business competition, this is a legitimate market ploy that only touches the regulatory realm when done by an exempt party who by so doing enriches himself at the expense of the regulated handlers and all pool participants.

"Along the same line of thought, USDA is urged to contemplate the economic incentive that creates -- that exists for the creation of additional gallons only producer/handlers. Producers continue to grow in size as do stores. The investment required to build and equip a simple gallons only plant is not large compared to the existing investment already in place by either a dairyman or the store.

"When the return on investment of this contemplated investment is calculated for a large dairyman, the investment pays a handsome dividend, even if the producer/handler had to give up a portion of the potential advantage. It is clear from past decisions of USDA that they see their role as one of reacting to actual events instead of to potential events.

"At this time, there are two instances where available loopholes are being used in ways that make a mockery of milk price regulation. First, of course, is Sarah Farms in Arizona and its remarkable growth. The second instance is not a producer/handler exemption as we normally understand the term. USDA is urged to consider the actual event of a new plant operating in Yuma, Arizona that has been built to take advantage of a loophole exemption from classified pricing and pooling.

"In that case, the loophole is the inability of the state of California to regulate under its state order milk processed outside the state, but sold into California. The exemption that this plant found is for all intents and purposes exactly the same as the exemption available to a producer/handler. The economics are powerful. The model has been established. It is probably not a coincidence that the owner of this new plant is, in fact, the largest producer/handler in America.

"In the view of NDA, the best and most rational course is to end the exemption for those whose market size -- whose size makes them a threat to render moot the concepts at the heart of milk regulation, classified pricing and pooling.

"Proposal number four, double-dipping. NDA urges the implementation of the concept recently incorporated in several other orders, Order 30, 33, 124, and 135, which effectively prevents the simultaneous pooling of milk in the California state-wide pool and in the federal order. The change should be adopted consistently across all orders. The language proposed for this hearing meets this suggestion, and its adoption is encouraged.

"In order to save time at this hearing and to avoid repetition of testimony given at previous hearings, NDA requests that official notice be taken of the testimony and findings, recommendations and final decision of the previous federal order hearings related to this topic.

"Proposal number five, conforming amendments. NDA, as always, supports the need to make necessary adjustments to the marketing agreements.

"This concludes my prepared testimony. Dan McBride will offer additional testimony on behalf of NDA."

Q. Thank you, Mr. McBride -- excuse me, Mr. Van Dam. As you know, Mr. McBride will be testifying shortly, but I'd like to take advantage of the fact that we had some interest expressed in earlier questioning of other witnesses to maybe ask you a few more questions to help address some of those questions that have been asked of other witnesses.

Before I do ask you those other questions, though, I think it would be useful -- I should've done this earlier before you began your prepared testimony. It would be useful to have you explain a little bit about your background and experience in the dairy industry. Would you tell us a little bit about your formal education, please?

A. My formal education is a bachelors degree from University of California at Davis in agricultural economics, with animal husbandry as my minor, and then after I was in the service for two years, ten months and 15 days, I went to Cornell University and got my masters degree in agricultural economics with a minor in agricultural policy.

Q. Okay. And have you worked in or around the dairy industry for all of your professional career?

A. My entire professional career has been with the dairy industry.

Q. You grew up in the dairy business, too, didn't you?

A. I was born and raised on a dairy in Southern California.

Q. Do you have relatives who are currently in the dairy producing side of the industry?

A. Consider number of relatives who are in the producing side of the industry.

Q. And do you -- and from that relationship, do you have good sense of dairy production and some of the issues involved in -- that face producers?

A. Certainly do. Yes, I certainly do.

Q. Tell us about your career since Cornell. I noticed you mentioned on page seven that you once worked for a producer/handler. What other types of positions have you held within the dairy industry?

A. Immediately out of school, I went to California and became the general manager of the League of California Milk Producers and represented producers in the state pooling plan. That was our primary plan. It was brand new then. That was back in 1969, so it had just been implemented. So that organization, I worked for them for a while.

Left there to go to work for what was then Petaluma Cooperative Creamery, which is now -- what then became California Cooperative Creamery, which is now part of DFA.

Left there to go to Clover Stornetta Farms (phon.) where I was part owner with five other fellows, former employees of the coop, and stayed there for seven years. So I was a distributer. I was vice-president in charge of finance. Did the bookkeeping and things like that for that company.

Q. What kind of business was Clover Stornetta?

A. It's a milk distributor. It's a relatively small one. It has -- plant is located in Petaluma, California. It was previously owned by Cal-Coop, and they decided to sell it after their plant burned to the ground. And so I became part of a group that bought it.

Left there and went and had my own cheese factory for a little while. That was -- up until then my career was going upward. That was a very bad step backwards. I owned a small cheese plant in Pleasanton, California. We'll just leave it at that. It was an unpleasant experience.

From there I went to work for a producer/handler in California, Chase Brothers in Oxnard, California for a number of months. Then went to work for DCCA in California where --

Q. Who was DCCA?

A. Dairyman's Cooperative Creamery Association in Tulare, California, which is now part of Land O' Lakes. For them I was -- at least my final position there was a marketing manager, but that meant mostly selling powdered milk.

Q. What kind of business was -- were DCCA in at that point in time?

A. DCCA was in -- very large in their cheese plant, making cheese for Kraft. Very large drying plant, drying a lot of milk. We took -- on real good days in the spring, we'd take in ten million pounds of milk a day into that plant. A large volume of that was reloaded on trucks and shipped into the L.A. market for the class one market.

From there I went up to Washington where I worked for a while for Dairy Marketing Services, a small company that owned a cheese plant up there and a bottling plant, both of which have since been shut down.

Q. Up where?

A. In Mount Vernon, Washington, north of here 60 miles or so. From there I went -- was hired by Symploc (phon.) -- well, Symploc Company and I, but a great big Symploc Company, a very small I, bought a cheese cut and wrap operation that was subsequently closed in Mount Vernon and moved to Idaho.

I moved with it and became the general manager of the dairy division of Symploc Company. That involved being the -- also the direct manager of the Swiss Village Cheese Plant.

When Symploc found that I nor anybody else could not make money making cheese, I no longer worked for him. And then he sold the cheese factory to Sorrento-Lactalis (phon.), so it's no longer in his system any more.

And then in the years since then I've been operating as a dairy consultant living in Meridian, Idaho, and that's what I'm doing at this time.

Q. In connection with your consulting business then, do you work with individual producers as well as with folks like Northwest Dairy Association?

A. I certainly do. I operate in pretty much the full range of things that are of interest to dairymen and they're willing to pay me for working on, including some production problems, some manure management problems, and some looking into the future what they might do.

Q. I noticed on page 13 of your testimony that you refer to the fact that producers -- larger producers have economies of scale and that are farms producing more than three million pounds per month, are typically very efficient. Have you been on such farms, and do you have knowledge of that efficiency that you were testifying to?

A. Yes, I do. I do get on a lot of farms of this size. That's my -- by far the biggest part of my clientele are the people who are of this size. And in addition to that, during my consultancy period there, I was the general manager of the Northwest Milk Marketing Federation, a milk pricing organization. And during that five years that that was operating, I managed to pay visits to every, single one of the regulated handlers in the Pacific Northwest market and almost all of the producer/handlers. I've been on these dairies. I've seen how they operation, you know. From general appearances, you can see that these places are

extremely well run. Their production per cow is high.
Q. Which places are you referring to?
A. Just about all the big ones I've been on, but the --
Q. (Indiscernible)
A. -- producer/handlers included, producer/handlers in this market area. They are good producers.
Q. You've never seen their balance sheets, have you, or their operating statements?
A. No, I haven't.
Q. So you're making a judgment as a observer of the dairy industry that those are efficient operations?
A. Yes, I would.
Q. Were you here yesterday for Dr. Terry Smith's testimony?
A. Yes, I was.
Q. In your view and in your experience, are the things that he was testifying to about economies of scale real, and do they comport with what you've observed in the real world?
A. Yes, they comport perfectly with what I observed out there and his observations were, in my judgment, absolutely right on.
Q. I noticed on page eight of your testimony where you were discussing Table 2, and the worse case scenario as

you described --

A. Uh-huh.

Q. -- leaving producer/handler with a blend of different utilizations. I'd like to ask you a few questions about that. In view of some of the issues that have been raised with other witnesses yesterday, and in view of the fact that there appears to be some interest in it, first of all, understand correctly that this Table 2 is hypothetical?

A. Yes, it is.

Q. We talked, and I guess I'm referring to Table 2(A) as well as Table 2 --

A. Equally hypothetical.

Q. In a situation -- in a hypothetical situation where -- are you aware of any situations where producer/handlers have sold excess milk that they didn't need to regulated bottling plants?

A. Yes, I am aware of that.

Q. Were you aware that that practice goes on?

A. Yes.

Q. In that situation, are you aware that under the federal order system, there would be some allocation of that receipt by the regulated plant. There would be some allocation of that milk received from the producer/handler to a classification of use?

A. Yes, that's known as down allocation.
Q. In a scenario like that, then if the handler had any milk that was classified as three or four, which is possible, that would illustrate -- that would be as illustrated in Table 2(A) where there were some class three or four utilization shown. You're not showing any class two allocation here. In your experience and your knowledge of the federal order system, would the plant receiving such milk -- the regulated plant receiving such milk from producer/handlers pay a compensatory payment on any allocation to class one?
A. Yes, on class one, they would pay a compensatory payment equal to the difference between class one and the blend price.
Q. How about if the use is down allocated to two or to three or to four?
A. No payments at all. And in the case of class two, there -- the class two premium is lost to the pool.
Q. So this is a very imperfect model then of what the real economics may be to a producer/handler operation?
A. Absolutely. It is only intended to put together what we feel is a very conservative, worst case scenario. I believe that in almost all cases, but obviously not in every case, they will do substantially better than what my model here shows.

Q. Let's talk a little bit about balancing costs. You might recall -- were you here yesterday for Mr. Hollon's testimony?

A. Yes.

Q. And did you hear his testimony that balancing costs are typically not part of the federal order pricing scheme?

A. I have to correct myself. I wasn't here for his actual prepared testimony. I was here for his questioning. My flight had been canceled in the morning. So I did not hear that part, but I agree with the statement.

Q. In your knowledge then, balancing costs are not part of a orders pricing scheme?

A. Right. That is correct.

Q. Typically then in federal order analysis, are federal order prices assumed rather than actual prices including such things as balancing costs?

You have a puzzled look on your face --

A. Yeah, the puzzled look is because you're going to need to rephrase that one. I --

Q. -- rephrase the question.

A. I probably agree with you, but.

Q. Is it typical in federal order analysis to use federal order pricing rather than exact numbers that might include such factors as balancing costs?

A.   Yes, that's true. You use just the federal order announced price because -- and you -- and in this kind of work, we don't even adjust it for fat and solids content and things like that, that would really adjust the prices that producers pay or get, that handlers pay or producers get. This give it a very good sense of what is happening, though, and illustrates the case correctly.

Q.   So if there are balancing costs within the marketplace that are assessed to producer/handlers for selling class three or four products -- selling milk that's classed by this class three or four to organizations like ours, those would not necessarily be part of what you were trying to analyze here then?

A.   No, they were not, and I sort of assumed in a way by being so cautious on the values I did use.

I should add in response to your statement is that there will be plenty of opportunity for opponents to enter testimony, if I am substantially wrong in that assumption.

Q.   Did you participate and were you present during the hearing in April '02 regarding the Western Order market hearing held in Salt Lake City?

A.   Yes, I was there for the whole hearing.

Q.   Yesterday Mr. English asked some questions of Mr. Hollon about that hearing. Do you recall those questions?

A. Yes, I do. I was here for that.

Q. I'd like to ask you to address the same issues since he's not here. Could you describe briefly the issue involving a bulk tank proprietary unit and its use of small bottling plants to achieve its pooling goals?

A. Yes, the -- that was a case of two small bottling plants located in south central, I guess, south central Idaho, and those two plants were working in concert with a proprietary bulk tank handler unit. And what they were doing is, they were pumping milk in -- bringing -- delivering milk into those small plants, pumping out three quarters of it in order to use that entire volume to qualify additional volumes of milk for pooling, because during most of the stretch of time we were looking at them, the advantages of being in pooling were very, very high. And so everybody was striving to find ways to do it.

What was particularly interesting about that finding -- well, first of all, at the hearing the people who operated these plants admitted readily that they were not paying full class one price for the milk they were actually bottling, which was an interesting revelation. And that became part of the basis of the findings from that hearing when the net provisions of the plan and the entire bulk tank proprietary unit were thrown out of the order because the result of those positions was a -- was plants, competitive plants in that market paying less than the uniform price for their milk. Very interesting finding.

Q. Is -- do you see any parallels between what was going on there and a exempt producer/handler operation?

A. Well, I certainly do. It's exactly the same net result. There are people out there bottling milk who are not paying the uniform price for their milk. That was the finding then, and that is what's going on here.

Q. On page 12 of your prepared testimony in the section called, "The Threat to Federal Order Milk Pooling," you described vigorous competition for the remaining -- for the class one sales within the market. Would that be the kind of competition that you observed both at the hearing and in your own experience as a resident of Idaho, was going on then?

A. Yes, it certainly was, and it's actually more than vigorous. It probably would be defined as predatory because the small plants needed to get their class one volume up to a level at which the bigger cheese plant could pool more milk. It was driven by something more than just the desire to sell class one milk. It was driven by a desire and a need to have more class one sales to qualify more milk. Vigorous may not even be a strong enough word.

MR. MARSHALL: Okay. Well, Mr. Van Dam, I appreciate your being here on behalf of NDA today. I make you available to any questions that any other parties may have.

THE COURT: Shall we take our break now, our morning break?

MR. UNIDENTIFIED 1: That would be fine, and I'd also suggest that if any of the proponents want to use this testimony, we'd just as soon follow them rather than proceed.

THE COURT: Okay. I don't -- I --

MR. UNIDENTIFIED 1: I don't know if they have any. I don't know. If they do, that's fine.

MR. UNIDENTIFIED 2: I'm sorry, I didn't hear the --

MR. UNIDENTIFIED 1: I mean, our preference would be if any of other proponents want to, you know, work with his testimony before we cross, that would be (indiscernible)

MR. UNIDENTIFIED 3: Nothing needs to be added, but when you said --

THE COURT: I don't know what people are going to ask, so I --

MR. UNIDENTIFIED 1: That's fine.

THE COURT: I'm just going to generally follow this methodology unless there's a good reason not to.

MR. UNIDENTIFIED 1: You know, a break would be great.

THE COURT: Okay. Let's take a 10 minute -- well, make it a 15 minute break. Okay. We'll come back at 10:00 o'clock, 15 minute break.

(Off the record at 9:45 a.m. and reconvened at 10:00 a.m.)

THE COURT: Okay. We're back on the record, and it's time to -- for -- people have questions of Mr. Van Dam.

Who's -- who would like to go first? Don't forget to identify yourself.

BY MR. BESHORE:

Q. Yes. Marvin Beshore for Dairy Farmers of America.

Mr. Van Dam, I'd like to pursue just a bit your discussion of the affect on pool of utilization of surplus milk by producer/handlers for class two.

A. Okay.

Q. Okay. And you discussed that in your testimony, and there are exhibits which -- Table 6 of one of the market administrator's exhibit, which was prepared for Mr. Marshall. I don't have the exhibit number.

THE COURT: Before you go on, Mr. Beshore, I just realized. These documents that were marked, but they were never introduced into evidence. Can I assume, Mr. Marshall, you want Exhibits 35 and 36 admitted into evidence?

MR. MARSHALL: Yes, this would be the time to ask that. Thank you.

THE COURT: Okay. And I don't hear any objection, so Exhibits 35 and 36 are admitted into evidence.

(Exhibit Nos. 35 and 36 are received.)

THE COURT: Sorry about that, Mr. Beshore. Just wanted to remember that.

MR. BESHORE: No problem. Thank you.

EXAMINATION

BY MR. BESHORE:

Q. Mr. Van Dam, you've -- you're aware, I think you've pointed out, that close to 50 percent of the surplus milk of producer/handlers goes to class two usages according to the market administrator's data.

A. That is correct.

Q. Okay. In fact, on the butter fat side, it's -- I haven't done the arithmetic, but it's more like 75 or 80 percent, I think.

A. I certainly would believe that based on the products it goes to, but I have not done that calculation either.

Q. In any event, those numbers are in Table 6 of the exhibits submitted by Mr. Mykrantz at Mr. Marshall's request. Now, to the extent that pool milk is displaced from class two utilization in the order, do you have an opinion based on your knowledge of this marketplace, what usage that pool milk likely is diverted to?

A. Okay. Well, what happens within a market is that as milk comes from a new source, a producer/handler goes into a plant that displaces automatically milk back into the cooperative plants. They're going to keep their higher paying plants as full as they can, and so by definition, this extra milk gets forced into the lowest possible class use. In the current class market, that would be class four.

Q. Okay. So when that occurs, as you've testified, the market loses the 70 cent per hundredweight difference between the class four price and the class two price, correct?

A. Absolutely.

Q. Okay. And that's a -- when the producer/handler milk, which is non-pool milk goes into that class two use, it's a dead weight loss to the pool of about 70 cents per hundredweight, correct?

A. Correct.

Q. And the pool handler, who may be acquiring that surplus milk from producer/handlers has no obligation to the pool on that milk, correct?

A. As I understand it, that's correct.
Q. Okay. And you testify there's no compensatory payment required on class two as there is on class one, correct?
A. There is none.
Q. So there's quite a marketing opportunity available there for pool handlers to acquire milk for class two utilization at an unregulated price?
A. Precisely.
Q. Okay. And, in fact, the exhibits would indicate that -- you know, that that option, you know, is pursued -- takes place in this marketplace from -- in terms of the utilization shown for class two of the producer/handler surplus?
A. That's correct.
Q. Okay. That loss to the pool, you haven't attempted to calculate their --
A. No, I have not. It's -- relative to the class one premiums lost, it's pretty small. Nonetheless, it's there, and it does happen, and it is a violation of the uniform pricing.
Q. Well, in any event, it's 70 cents per hundredweight --
A. Yes.
Q. -- times whatever the utilization -- whatever the

volumes of milk and butter fat used for those --

A. Right.

MR. BESHORE: -- purposes. Okay. Thank you.

THE COURT: Anyone else have any questions?

MR. YALE: I'd be glad to call my next witness (indiscernible) I apologize (indiscernible)

THE COURT: It's okay, Mr. Yale.

MR. YALE: Unfortunately, the issue is (indiscernible) more than one form.

MR. UNIDENTIFIED: I want to follow up on this --

THE COURT: You need to identify yourself.

EXAMINATION

BY MR. YALE:

Q. Benjamin F. Yale on behalf of Smith Dairy Farms, Etteline Dairy, Mallory's Dairy.

I want to follow up on this class two discussion.

How much milk is going into a pool plant and displacing class two in a pool plant in the Pacific Northwest?

A. You want to know how much milk --

Q. From a producer/handler, I'm sorry. How much producer/handler milk is going into a pool plant in the Pacific Northwest and displacing class two that would -- that you mentioned here with -- this discussion with Marv Beshore --

A. Uh-huh. Well, the -- that is a number that's not available to me. Only you and your group would have that number. I only know the grand totals because of confidentiality requirements of the reporting. So I know the totals, and I know it's significant.

Q. Now, let's talk a bit about -- let me try to differentiate the types of class two that we're talking about. Let's assume that we have a producer/handler that producers ice cream. That's a class two produce, right?

A. That's certainly part of the numbers we got.

Q. All right. Now, let's assume also that there's a 7A plant that produces ice cream. Now, that 7A plant would pay the class one on its class one, and the class two on its ice cream, right? And then any other class milk, right?

A. That's the way it would work.

Q. All right. Now, example number one is, the producer/handler moves milk and sells it to the 7A plant.

A. Right.

Q. All right. Now, I think the discussion's been here today that this gets down allocated, right?

A. That's correct.

Q. Now, does the 7A plant have an obligation to pay that producer/handler that down allocated price?

A. No, there's no -- as far I know, there is no obligation establishing a price that has to be paid. It is exempt from pricing.

Q. That's right. So they could pay them $5 or $6 if the class four price is 10, right?

A. They certainly could.

Q. And, in fact, that's what WestFarm does, doesn't it? It pays its class -- for its class three and four that it purchases from producer/handlers a discount of a buck 50 or more per hundredweight, right?

A. That's my understanding, but Dan McBride knows the specifics --

Q. All right.

A. But there's a discount, but I -- you can't use $5. That's not the price either.

Q. Well, we -- we'll get to that.

A. Okay.

Q. But it -- they don't -- they can pay that lower price, right, and in fact the --

A. It is unregulated.

Q. So WestFarm purchases milk from producer/handlers at less than class prices, right?

A. Yes.

Q. And who benefits from that?

A. WestFarm Foods.

Q. And who owns WestFarm Foods?

A. The dairymen.
Q. So they got a benefit from that?
A. To the extent that that milk shows up at their plant, --
Q. All right.
A. -- they got a benefit.
Q. So let's take the next step. Let's say that this milk gets down allocated to the point that it's class two. There's still no obligation to pay the producer/handler the class two price, right?
A. There is not.
Q. And any difference between what they pay -- that WestFarm pays that producer/handler and what the producer/handler -- or what the -- WestFarm has to account to the pool for, WestFarm keeps, right? They --
A. Yes.
Q. Right?
A. Yes, sir, or anybody else.
Q. Or anybody else.
A. Right.
Q. Okay. Now, in -- the question I have right now is, because you do have privy to WestFarm's reports, right?
A. I do not.
Q. In preparation for this hearing, they haven't given you information about the amount of class two milk

that's been down allocated out of their plants from producer/handler purchases?

A. They have not.

Q. Isn't that the reason why, is because they haven't purchased any class two or had any milk allocated to class two?

A. I don't know. You'll have to ask Dan. Maybe he knows.

Q. So then why are we talking about milk coming from it into a plant and being allocated to class two if it isn't happening?

MR. UNIDENTIFIED: Objection, mischaracterizes his earlier testimony. He didn't say it was happening at WestFarm Foods. He said it was happening in (indiscernible)

THE COURT: He can answer the question if he knows the answer.

BY MR. YALE:

Q. All right. Let me ask this question. Are you aware of any 7A plant in the Northwest order purchasing milk from producer/handlers and in their reports to the MA, it gets down allocated to class two?

A. Yes.

Q. And who is that?

A. That was Umpqua Dairy (phon.). They're not doing

--

Q. Pardon?

A. -- it now, but they were.

Q. Who?

A. Umpqua Dairy.

Q. Umpqua Dairy. And when was --

THE COURT: You might want to spell that, because -- just for the.

THE WITNESS: U-m-p-q-u-a.

BY MR. YALE:

Q. And when was this?

A. Year and a half ago.

Q. And how do you know that?

A. I was told by the representative on Umpqua Dairy.

Q. And how much they allocate to class two?

A. They didn't tell me.

Q. They --

A. They have substantial mono-class two (phon.) in their plant. They have very little three and four. Plant losses only. They stopped doing it because it started reaching into the compensatory payments range, so I understand it. It must have been substantial, but I don't have the exact numbers. I just know it happened.

Q. Okay. But is -- and Umpqua Dairy is not doing that now?

A. They're not doing that now.
Q. All right.
A. As recently as a month ago, I talked with them, and they aren't doing it now.
Q. All right. Now, let's talk another second -- another issue here. Let's take the issue of the producer/handler who has class two at his farm or her farm.
A. Right.
Q. Okay. In fact, and I think in all my cases it's his and her farm, but at their farms, at their plants that they make class two, if by your proposal they become 7A plants because they exceed the three million, they would pay into the pool the class two price, right, for that amount of milk?
A. Correct.
Q. And they would withdraw from that pool the blend price, right?
A. Correct.
Q. And that blend price exceeds the class two price, right?
A. Correct. Probably, in most cases.
Q. Right. So the class two really is not a contributing factor to any erosion of producer income in the Pacific Northwest, is it?
A. Oh, it certainly is.

Q. How?
A. The 70 cents is not contributed. It's premium income above this -- the class three price, --
Q. But the --
A. -- and it's not there.
Q. But to get that from these producer/handlers, you'd have to pay a blend price to get it?
A. That's correct.
Q. So you'd have to pay more than you're getting back?
A. No, that's not true. On class two it might be true, --
Q. On class two --
A. -- but it's an overall pool.
Q. On class two?
A. On class one premiums, make that a very, very worthwhile move to make.
Q. All right. So let's talk about this class one premium and this move. You compute the impact if these three plants were made 7A plants, the total improvement to the price of producers in this order would be how much?
A. Four million dollars plus a few.
Q. And what's that come out, to hundredweight?
A. Four cents.
Q. Four cents. That a lot of money to a producer?

A. It adds up.
Q. Pretty important, right?
A. It adds up.
Q. And you're suggesting to the secretary here that this four sets is creating a disorderly -- it's part of a disorderly marketing situation, right?
A. I certainly am --
Q. They --
A. -- because of the $1.73, not the four cents.
Q. So, in other words, the fact that the producers are getting the money are not -- is irrelevant; is that what you're saying?
A. I certainly believe that the producers as a whole should share that four million dollars.
Q. On that four cents?
A. Yeah. Yes, that's correct.
Q. All right. And that it's important to get that amount of money to the producers, right?
A. Certainly is.
Q. Okay.
A. It is -- oh, sorry.
Q. Let me take a different line here for a moment.
You indicated that NDA owns WestFarm?
A. That's correct.
Q. All right. By the way, in the market, what

percentage of the producer milk in Order 124 goes -- is attributed to members of NDA?

A. It's in excess of 65 percent.

Q. Okay. Now, you have the WestFarm group, and they have plants, right?

A. Correct.

Q. Now, does NDA pay its members the blend price?

A. It bases all their pricing on the blend price. Their members in the Pacific Northwest order, but you're -- I think you're getting into an area that I am not as conversant with as -- I am not the appropriate one to ask that question. That's better given to Dan McBride.

Q. Okay.

A. But I know that they start their prices with the blend price.

Q. We may defer that line to him then. Thank you for saving us all some time this week, Bill.

Now, you spent a lot of time in your brief, or in your testimony, I'm sorry. Not the brief. Talking about efficiencies. Efficiencies at the farm, efficiencies at the plant. You testified on some Q and A from Doug Marshall about how you visited some large farms, and they're very efficient, and I think you said you even seen some of the PDs and are impressed that they're a state of the art and efficient, right?

A. Correct.

Q. All right. And as I understand that -- kind of reading, or maybe it's not even reading between the lines. I think you're suggesting that these efficiencies, these plants should be able to survive, and that they should not get any "benefit" from being a producer/handler, right?

A. Correct.

Q. Okay. So is this -- and then you're going to -- the deal is, is that they will pay -- under your scenario, they will pay more for their milk than they currently are?

A. That's correct.

Q. And the other producers will receive more milk out of the pool than they currently are, right?

A. I think you meant money out of the pool?

Q. What did I say?

A. Milk.

Q. Money. Milk is money, right?

A. In that case, I agree with what you said.

Q. All right. So they take money out of the pool, right? I mean, they get more money, right?

A. Correct, --

Q. Okay.

A. -- there's more money in the pool to be distributed across the pool.

Q. So in summary, really what you're saying is, is that we have efficient farms, efficiently supplying an efficient plant, that's efficiently supplying the public, and we're going to take money from that single enterprise that they're not currently paying, to pay to less efficient farms in the order and reduce their profitability so that the less efficient plants could be more competitive. Isn't that what you're talking about?

A. That is your way to characterize it. I don't see it that way at all.

Q. But isn't that really what's going on here, Mr. Van Dam, is that we have this efficiency in the system that has been derived, and by the way, these plants for decades, has derived this efficiency to move milk from the farm to the consumer --

A. And there's nothing in our proposal to keep them from doing that.

Q. Well, let's talk about that a minute. What is the economic impact? Everything else stays the same, tomorrow your proposal takes effect, --

A. Uh-huh.

Q. -- what is the economic impact on the average PD of these three PDs to the Pacific Northwest pool?

A. It would be large.

Q. It'll be large.

A. Yeah. At three million pounds, it would be approximately $52,000, as you did yesterday per month.

Q. And the average is 4.7 million, right?

A. That's correct.

Q. So it'd be 50 percent more than that, right, approximately?

A. Yeah, approximately. I know where you're going. That's fine.

Q. So about $78,000, right?

A. Somewhere in that neighborhood.

Q. So almost a million dollars a year?

A. Correct.

Q. And it's your position that these people owe the producers of the Pacific Northwest a million dollars a year?

A. Stated that way, I agree wholeheartedly with that.

Q. All right. Now what authority does the secretary have under the Act to require plants to pay for milk that they already own?

MR. BESHORE: Objection. Calling for a legal interpretation, inclusion of the Act.

MR. YALE: Your Honor, I want to read to you part of his testimony over here in page -- if I can find it -- I moved ahead of myself with my notes. He quotes the statute in his testimony. Bear with me a second, if I can have just a minute, I will find that section. Page 15. Okay.

He quotes, beginning at 15 and going on 16, the Act. I have a right to, if he's going to testify, to inquire what he knows of the Act, if he's willing to put himself --

THE COURT: Okay. I mean, I agree with Mr. Beshore that you're asking him what is really a legal question. But if you know the answer, I'll let you answer the question. If you don't know the answer, so state. Do you remember the question?

THE WITNESS: No, not sure we got to a question.

BY MR. YALE:

Q. All right. Well, the -- I think the question is, what is the legal authority for the secretary to require a plant that already owes -- owns the milk to pay to other producers a value for that milk?

A. The answer is clear. It's on page 16 on Section C. The paren. there says, "including producers who are also handlers."

Q. All right.

A. Unless the paren. means that you ignore that, it's clear.

Q. Did you prepare this testimony yourself?

A. I worked on all of it. I got some sections --

Q. Did you quote that --

A. -- from other people.

Q. Did you look up and see what the Act said that come up with that section that stated that?

A. I didn't look it up, but that's it.

Q. I'm going to read something that precedes the sentence under 7 USC Section 60C(5)(a), that precedes what you state here, and I want to know -- I want your -- I want to ask a question. I'm going to read it to you. And it talks about, shall provide, you know, minimum, or classes and so on and so forth, "providing for a method for fixing minimum prices for each use classification, which all handlers shall pay, and the time when payment shall be made for milk purchased from producers or associations of producers." And that's the phrase immediately prior to what you just quoted. Are you aware of that?

A. Sounds right. I don't see how it changes what I've got here, but you're getting into legalese that I'm not ready to debate with you.

Q. All right. Well, the question is --

MR. BERDE: Your Honor, my -- may I repeat the objection previously made, that Counsel is asking for a legal analysis and the legal authority, and I might add parenthetically that the exact question concerning authority has been previously decided over 40 years ago by two Circuit Court of Appeals cases in which the term "purchased from producers" was interpreted to mean "acquired for marketing," and the authority of a secretary has precisely been upheld to authorize the secretary to do exactly what that section provides.

THE COURT: That doesn't mean he can't ask him the question, Mr. Berde.

That was Mr. Berde, by the way.

MR. BERDE: But it is a legal analysis --

THE COURT: I agree with you 100 percent, and I told him if he knows the answer, he could answer it, understanding that it's actually more of a subject for the --

MR. BERDE: I understand.

THE COURT: -- for the briefs, for the post-hearing briefs.

MR. YALE: I'm leading up to a conclusion that gets us to there, Your Honor. I mean, because if you'll notice on page 16, he states, "The price regulation of producer/handlers within the authority is clear," and I want to get to his knowledge of why he says, as a witness sworn under oath, that it's clear.

THE COURT: I think you're entitled to ask those questions, and I will allow them.

BY MR. YALE:

Q. So were you aware, Mr. Van Dam, of that provision that it requires for prices for milk purchased from producers?

A. I have heard that before, because I've heard you before. It still appears to be clear to me in Section C that there is no exemption.

Q. Okay.

A. But not being a lawyer, it's not a legal opinion.

Q. Now, you -- there was some -- not testimony, it was questions, I think, by Doug Marshall about this, some kind of a supply plan in this deal over in Idaho where some people were able to basically just draw a lot of money out of the pool without really contributing to the market, right?

A. That's correct.

Q. Okay. Were those producers/handlers?

A. They were not.

Q. They were regulated plants, right?

A. They were regulated plants.

Q. And they were required as a regulated plant under the order to pay minimum prices for the milk which they used, right? That was the -- I mean, as a regulated plant, they were required to do that, right? Is there -- let me just rephrase. These were regulated plants. This -- I'm not trying to make a totally trick question here.

A. Yeah, and --

Q. But I think I see -- let me -- let's walk through this.

A. What was happening is, they were avoiding the real payments of the classified pricing, --

Q. Yeah.

A. Whether they were required their supply plant status or whatever status they had to make that a payment, I don't know, but they readily admitted they weren't paying it.

Q. I -- that was -- I saw the confusion. I wasn't trying to -- it wasn't a trick one, Bill. I was trying to make that point exactly, but they had an obligation already to pay minimum prices to the pool, right?

A. But they didn't do it.

Q. And they didn't do it by means of gaming this system, right?

A. Yes.

Q. Okay. But as it stands now, producer/handlers do not have an obligation to pay to the pool, right? That's why we're having the hearing.

A. They do not.

Q. Okay. And they have not in this order, almost from the beginning of its orders and its predecessors, that's --

A. That's been the history of all federal orders.

Q. Right. Okay. The 7A plants that are in this order, does Tillamook Cheese, on a regular basis, supply any of those with milk?
A. Yes, they do.
Q. The bottling plants, they have --
A. Yes.
Q. -- class -- and is that the same case for Farmers Cooperative Creamery?
A. Yes, they both do it through OMMF, Oregon Milk Marketing Federation --
Q. Okay. Well, that was my next question, that there is amongst all of you cooperatives in the Northwest, you've got a cooperative agreement for balancing -- qualification of plants and balancing of milk; is that right?
A. That's correct.
Q. All right. But in the delivery that Tillamook makes, does it have contracts of its own with any of these bottling plants?
A. Now you've just stepped over my knowledge line. I simply don't know how the details work.
Q. Okay.
A. I was much more conversant on that three years ago, but not as conversant now in the rules, and some of the agreements have changed. So I simply can't walk there.

Q. But isn't it fair to say that NDA, between its own plants and the other plants, supplies the vast majority of the class one plants -- 7A plants in the Pacific Northwest?

A. I tend to want to agree with that, but I simply don't know the numbers, so I can't --

Q. All right.

A. -- make a flat statement on the record that I do know. Save it for Dan. He'll know.

Q. Now, you're really helping him out.

A. Take notes, Dan.

Q. Now, in page two, first paragraph that's on that page, the last sentence, you -- "These comments could not have been missed by producer/handlers, and we certainly feel they have been adequately forewarned of our concern and the potential for changes in the rules," right?

A. Correct.

Q. Have you been going to -- has NDA or WestFarm been going to the customers of these producers/handlers and telling them that they intend to get the rules changes, so they have to pay more for their milk?

A. I absolutely do not know the answer to that question.

Q. I feel like we keep beating a dead horse on this one issue, but every time somebody brings it up, I feel like I've got to address it. You talk about when the rules existed back in the '30s, producer/handlers were small, right?

A. Correct, as all producers were.

Q. Everything was small in the '30s, wasn't it, as far as producers were concerned and milk and --

A. Correct.

Q. -- parties.

A. Small by standards we know today.

Q. Right. And -- but everything's relative, isn't it? I mean, we have larger producers than we had, so we have larger PDs. We have larger plants. All of that, right?

A. That's correct.

Q. So if you're going to take the argument that this act was intended to deal with small producers in the '30s, why does it -- or, producer/handlers, why can't that same argument apply to all entities within the marketplace? Why can't we have special rules for larger plants and multi-order plants than we do for the small, 7A plants.

A. I may not be directly responsive to your question. Nonetheless, I think I am going to answer your question. The order was not written to exempt the producer/handlers. It was a practicality in the economics and the politics of the situation then that exempted them.

They're still writing that, but the code itself was not written to exempt producer/handlers.

Q. It was to protect producers in marketing their milk to plants, right?

A. Right.

Q. But a producer that already owns the plant doesn't have to compete, does he?

A. But they were not exempted. It's a practicality that got them exempted, and it's sustained itself for a long time.

Q. Now, let's come to -- let's talk about this competition issue. NDA doesn't sell milk to the producer/handlers, right?

A. Not to my knowledge, but they could sell up to 150,000 --

Q. Right.

A. -- pounds to each one.

Q. A diminimous amount, you would agree, in the light of what we're dealing with --

A. Certainly. And certainly qualifies for that title for the three that are big enough.

Q. Right. The -- so they get -- they don't sell any, and so at the plant level, there's no competition between the farm, say Etteline owns, it's supplying its plant, and any other farmers at that plant for that milk, right?

A. For the bulk milk sale to them?

Q. Yes.

A. No, there is not.

Q. And where the competition comes in is at the retail level, right, or the wholesale package milk --

A. Wholesale package milk level.

Q. By the way, you -- there was some comments made that there -- you're still pondering some decisions, you know, in terms of some changes to language to answer in response to some questions --

A. In response to questions --

Q. Right.

A. -- raised yesterday.

Q. Right. Will we be able to see the results of that pondering soon, or do you know?

A. I don't know.

Q. Will it be before or after we have to testify about changes we don't know about?

A. I can't answer that either. They were not major issues that are going to change anything here. They're detailed kind of questions.

MR. YALE: I want you to -- bear with me one second.

(Pause)

MR. YALE: I apologize, Your Honor (indiscernible)

BY MR. YALE:

Q. You presented -- provided a table that talks about a 12-year change from 1990 to 2002. This is Table 1. I don't know what that exhibit number is.

A. 36.

Q. 36. Thank you. First of all, why did you choose a 12-year period?

A. The data I had available to me -- readily available to me reached back to 1990, that was -- didn't seem to be much point in going a whole bunch further back than that.

Q. Now, you have testified that there is a trend of a growing chair of producer/handlers in class one sales. The trend line is growth; is that right?

A. Did not say that.

Q. What did you say?

A. I said, this is total production we're looking at there, and that's what I was commenting on. I was comparing the total production levels of the producer/handler to the typical producer to see if we had some commonality and some differences.

Q. So it -- your -- it's not your testimony that the amount of milk going into class one with -- by

producer/handlers is growing in the market; is that right?
A. That's right.
Q. In fact, it starting to tend down, right?
A. I doubt that but.
Q. Well, let's look at your Table 1. Do you have that in front of you?
A. I have Table 1 in front of me.
Q. Okay. And it has -- Table 1 does -- Table 1 shows the total pounds of production for producer/handlers.
A. Correct.
Q. And what's the difference between 2000 and 2002; is it going up or going down?
A. It's down slightly.
Q. And you probably do not have available the exhibits from the market administrator that showed the in-area route disposition by handlers of the Pacific Northwest?
A. I do not have that with me.
MR. YALE: Do we have a copy -- I think it's Exhibit 6?
(Pause)
BY MR. YALE:
Q. Exhibit 7, and these are tables prepared by the market administrator. I want you to look at Table 1. Have you seen that table before?

A. The -- yes, I have.
Q. And it talks about the producer/handler's share of the class one in-area route distribution in the Pacific Northwest from 1998 to 2002, right?
A. That's correct.
Q. And you would agree, would you not, that in 2002, that the percentage is lower than it was in each of the two previous years, right?
A. That's what this table shows. I could add that when I saw that table, I was a little bit taken aback because it didn't match with what I understood to be the case, and that's when we discovered and stumbled across the fact that there was substantial sales to Alaska which, in effect, is class one sales, which is why I adjusted Table 2(a), or --
Q. Let's -- those class one sales existed prior to that, though, to Alaska?
A. They didn't. They weren't carried by the producer/handlers to the extent they were later.
Q. Yeah, but that doesn't -- the percentages, you would add it into the previous years in this one, so you'd still have the decline, right?
A. I don't think so.
Q. You can't just add it to 2002?
A. If I -- when I made the adjustment, I added it to

all of them. These -- this sales to Alaska were substantial.

Q. I understand, but let's talk about this for this table right here. This is in-area route distribution, right?

A. That's correct, --

Q. All right.

A. -- and it is down. I'll grant you that, Ben.

Q. And it's down in January to June of 2003, right, even more so.

A. I don't know.

Q. You don't -- but you've testified in your testimony that there's this growth of the presence in PD --

A. Ben, you asked me about this table.

Q. All right.

A. This table stops at the end of 2002. It is down slightly, .38 percent.

MR. YALE: We'll leave the record (indiscernible)

BY MR. YALE:

Q. But you would agree, would you not, that over the last three years there is no evidence of a growth of producer/handlers eroding class one sales in the Pacific Northwest, right?

A. I would agree that there's very little change in the level of class one sales by the producer/handlers in the Pacific Northwest order.

Q. And that since 2000, if any change, it's been down even -- although, maybe slightly, it has been down; is that right?

A. That's what the table shows, and that's approximately correct.

Q. Now, also on page seven, you -- I think we've talked about it, but I want to make sure that I've covered it all. We've got the 933 pooled producers who are, as far as we know, mostly within the definition of small business, right?

A. That's correct.

Q. And the impact we talked about earlier was the four cents a hundredweight?

A. Correct.

Q. Okay.

A. Four million dollars.

Q. And over -- okay. That's four million per year?

A. Four million for all producers.

Q. Right, per year?

A. Per year, yes.

Q. Right.

A. I'm sorry. I thought you --

Q. And all of that would come by payments from Etteline Dairy, Smith Brothers Farms, and --

A. Mallory's.
Q. -- Mallory's.
A. Well, they would be three million. They're 70 percent of the four million. Four million is the grand total of all of them. We're not going to regulate the other five or six, however many left.
Q. All right.
A. They're under three million.
Q. So I understand it then, is that the impact then, if you just regulate these three, is less than four million?
A. Yes.
Q. What is the impact of the regulation -- if you're --
A. 70 percent of the milk by producer/handlers is held by the three largest.
Q. So it would be 2.8 million?
A. Something like that, yes.
Q. Is the impact. So it'll be less than four cents?
A. Yes, it would be.
Q. And I guess four million to four, then 2.8 would be 2.8 cents, right, approximately?
A. Approximately. Still $2.8 million.
Q. Now, you made a statement in here that you were a producer/handler, or worked for a producer/handler at one

time, and I think it was in California?
A. That is correct.
Q. And they do not have the same regulatory systems we do here?
A. They certainly do not.
Q. In fact, the producer/handlers down there, they're not exempt unless they have PD quota, right?
A. Not sure that's technically correct, but that is how it works. They have quota, they've been issued quota based on the historical class ones sales with one adjustment some years later.
Q. Right. Do you consider yourself an expert on operation of producer/handlers based on that experience?
A. Don't know if that makes me an expert, but it sure gives me a lot more experience than a lot of people have had.
Q. Probably more experience than anybody that's testified so far, right? Do you know anybody that's testified in this hearing so far that's had more experience with a producer/handler than you?
A. Well, not at the levels that I've had that experience.
Q. And how long were you there?
A. Seven months.
Q. Seven months.

A. And I was a controller. I did the books for them.

Q. Okay. Now, did -- I didn't catch -- you -- what -- your degree is what, Bill? Did you get a ag. economy or --

A. Yeah, ag. economics.

Q. All right. And you took accounting?

A. You know, like all of us that go through econ. anything, --

Q. Right.

A. -- you have to do.

Q. Right. And did you do any courses in cost accounting?

A. Certainly did.

Q. All right. And you would agree, would you not, that -- or, let me ask you this. Other than this plant, did you ever get involved in discussions on how to allocate costs with different parts of an enterprise?

A. Oh, absolutely. I was the vice-president of financial of Clover Stornetta Farms, and we had a lot of that debate and do all the time.

Q. Right. Because there's never any real clear answer to that, right. I mean, there --

A. You know, there's -- but there's clear guidelines on how you do it, and you have to have some common sense --

Q. Right.
A. -- and a rational approach.
Q. Right. But in the board rooms around the country, there sometimes gets to be a lot of dispute over what common sense and what the guidelines are, but is -- there's -- right?
A. Especially currently.
Q. Yeah. And with a producer/handler situation that -- you don't know for a fact that -- well, let's just put it to these three, how they cost account for their milk, do they?
A. Certainly do not.
Q. Would -- I think you've testified the blend price is a very fluctuating price, right?
A. Yeah, the underlying prices fluctuate. So does the blend price.
Q. But a producer/handler doesn't really pay under the current situation a blend price for its milk, right, or does -- I mean, the farm side doesn't receive a blend price, right, and the plant doesn't pay a blend price, right?
A. That's correct.
Q. So what is the cost to that enterprise for that milk?
A. As I testified, if they do enterprise accounting

and would look at each part of their operation separately, the proper transfer price would be the blend price, and the proper pay price would be the classified price.

Q. It wouldn't be their cost of production?

A. No more than that is the way you measure a regular producer who is in the pool. His income is the blend price.

Q. But a producer/handler doesn't receive the blend price, he receives the price from the enterprise. Once it's -- the product is sold, right?

A. Well, certainly that's true, but if he's going to do enterprise accounting, understand how he fits in a market, he needs to apply the proper prices from the marketplace. They're very clear in a federal order market. You know exactly what the blend is. It's announced on a regular basis. You know exactly what the classified price is, because it is announced ahead of time.

Q. So it's NDA's position that producer/handlers need to change their accounting to use that as their transfer cost?

A. It's the NDA's position that the producer/handler should look at his enterprises on that basis to determine whether or not he can compete in the marketplace or not.

Q. If his cost of production exceeded the blend price, should he go ahead and treat it as if it -- cost was the blend and then make that the basis for selling his milk?

A. No, he'd make the classified price the basis for selling his milk, to the blend price. The blend price is how you measure your dairy enterprise, the cows. There's a difference between those two numbers, and that's your PD advantage.

Q. Assuming, of course, that your cost of production is less than or equal to the blend price, --

A. That is irrelevant.

Q. Well, --

A. It's irrelevant. Every producer in this state, that will determine whether they stay in business or not. It is not how they measure the income of their dairy cow operation.

Q. So your -- it's your testimony based upon all your years of experience that if a handler has milk and is selling it, that in a integrated operation from farm to the sale of the process product, that their sales price has to be based upon a blend price that they don't receive or pay, but not their cost of production?

A. That's not -- you know, you're trying to twist it. The sales price should be determined by the classified prices that are announced. That's what all their competitors, except other producer/handlers, pay. That determines what you sell it for. You measure the profitability or lack of profitability of your dairy cow operation based on the blend price, because that's what ever other dairyman gets.

Q. So it's your --

A. You can make money, you can lose money. It's a way to measure it, and it's the way you do enterprise accounting.

Q. So it's your testimony the producer/handlers based their sales price on the class one price?

A. That would be the logical thing for them to do, and at least they should measure their operation on that basis to know now they worked in the competitive world they exist in.

Q. And what happens when the class one price is less than their cost of production?

A. They lose money. They'll lose money on their dairy. That happens to everybody.

Q. Or they could sell their milk at a higher price, right?

A. Well, certainly, but that -- I'm -- we're only talking about how you measure your enterprise.

Q. Right.

A. Your response to it is why you measure it. You measure it so you can make an appropriate response.

Q. Is there anything in the rules that require a producer/handler to do the accounting on this basis?

A. There's none whatsoever. It's just the logical way to approach it, because you need to know how your operations measure up.

Q. Let's talk a minute about this transfer cost. How -- well, I'm going to pass that one through.

So I understand it, that in event -- in the period of time in which the cost of production -- I'm going to talk about from a plant standpoint in competing with other plants, plants that are 7A. It is your testimony that if that farm's cost of production, a producer/handler's cost of production exceeds the blend price, that that plant still has an advantage of the difference between the class one and the blend price? That's your testimony?

A. Not sure -- quite sure I followed what you're saying because you insist on using blend price as a cost of milk to the bottling plant, and it is the classified price that I suggest should be used to measure that. And it's enterprise accounting, and you're finding out what's profitable and what isn't.

Q. But you have testified that they have an advantage because they don't have to pay the classified price --

A. And they certainly do. All their competitors who are regulated pay the class one price.

Q. We've been through that. The producer/handler doesn't have to pay it, right?

A. That's correct.

Q. They have to pay -- or, is it your testimony they have to pay the blend price?

A. No.

Q. All right. I'm going to come back again to my question again. You have a producer/handler who purchases milk, and you've got a 7A handlers, and you're testifying today that that producer/handler has an advantage over that 7A handler, right?

A. That's correct.

Q. All right. And you have testified that that advantage is measured between the difference between class one and the blend price; is that right?

A. That's correct.

Q. But isn't the real reality is, is that for a single enterprise, the difference between any advantage would have to be between what their actual cost is and the class one, because they would not -- they are only paying that -- they're not paying themselves a blend price?

A. Yeah, we can go around that circle several more times if you want. My argument would be, you measure the enterprise of milking cows based on the over-based price. You make money or lose money. You measure your handler business based on the classified price, whether you make money or lose money. In between, you've got the advantage that either gets used up or doesn't.

Q. By over-base you meant the blend price? I didn't mean to send you back into your prior life, you know, to California.

A. I didn't want to think about that either.

MR. BERDE: I think the record should --

THE COURT: Mr. Berde, you got to identify yourself, and you got to speak through a microphone if you want to say --

MR. BERDE: The record should disclose that the witness -- Sydney Berde. The record should disclose the witness just corrected itself, and transcript may not disclose that. That is, he misstated, called the blend price the over-based price, and instead meant to say the blend price. I think Counsel will agree to that.

THE WITNESS: Oh, I agree. I thought I'd clarified it. Thank you for catching that, Ben and Syd.

You have to remember, Ben, that when I did this was at a California plant, so.

BY MR. YALE:

Q. We'll talk about California in a minute, based on your testimony. But for the moment, we're going to stay here.

Now, and maybe again, this is something else that you're going to pass on to a subsequent witness, but I want to ask the question. Have you done any analysis on the total volume of milk, packaged milk sales in Order 124 that have moved from a producer/handler -- I'm sorry, from a 7A plant to a producer/handler in the last three years?

A. From the 7A handler?

Q. Yes, to a PD.

A. No.

Q. Have you seen any table that has shown a shift of sales from a 7A plant -- in total. Not just individual sales, but in total. The total amount of sales that have transferred back and forth between a 7A plant and a producer/handler and a producer/handler and a 7A plant?

A. No, I have not.

Q. Now, you've been in the sales side of the product, right, over the years?

A. Correct.

Q. And producer, or customers come and go, right?

A. They do.

Q. And sometimes you lose them, and you never know why, but you lost them. Sometimes you know why and you lost them, but they just come, and then you also, you pick up other customers. That's the whole dynamic of a sales marketing team, right?

A. Pretty much, except we just about always knew why we lost them. That was a very, very important item to know in your marketing effort.

Q. Now, you -- in paragraph, on page nine in the middle, you make this statement. "We conclude that this pricing," and I think you were talking about, and you can correct me if I'm wrong, about the ability of a producer/handler to sell at whatever they want, and you got the class one, or the regulated --

A. Right.

Q. -- 7A plant, "that this is an excellent example, the kind of price competition that occurs in the absence of regulation, and which gave rise to the concept "disorderly markets." Indeed, this hearing record has already demonstrated enough disorderliness that the secretary should act to put a stop to it."

Now, what events, specific events of disorderly marketing have occurred?

A. Like we did before, Dan McBride is going to testify with the events, naming who the customers are --

Q. Okay.

A. -- and what's going on.

Q. Has any milk been dumped by NDA as a result of producer/handlers?

A. Going to have to leave that one to somebody else. I certainly am not aware of any milk being dumped any time in the last several years. So if I don't know that, I certainly don't know why it was dumped if it happened.

Q. On page -- you also talk about equal payments to the producers. That's really not -- the history of the act hasn't really always ensured the producers necessarily got equal payment, but the plants -- that there was an equal price at the plant level, right?

A. Yeah, the act calls for the distribution of the class one proceeds, I believe, it's equally to all producers or --

Q. What about a partially regulated plant?

A. Well, partially regulated plant does get regulated to the extent that they reach into that market --

Q. But their producers don't necessarily get the same price as the other producers in that market, right?

A. I believe that's correct because the producers are probably in another area. Nonetheless, it's distributed in an orderly basis.

Q. And we've also had orders and which had multiple plants, and we had individual handler pools within those orders, right?

A. Took a long time to eradicate those from the

system, but they're gone now.
Q. But there was a long history of them, right?
A. There was, until reform package came in.
Q. Till reform came?
A. Yeah.
Q. And under a federal order in which there was individual handler pools, you could have two handlers in that pool, and they'd each pay their producers a different plant blend, right?
A. Certainly.
Q. I want to go back to the topic -- I just want to make sure I understand, make sure I've got it covered. We talked about that down-allocation and the issue of milk going into a pool plant by a producer/handler. Have you computed simply on the issue of milk being sold by a producer/handler to a pool plant in Order 124 the amount of milk that has actually been sold to such 7A plants?
A. No, I have not. I don't have access to the data that could tell me that.
Q. Do you know -- so at that point, you don't know whether that's had an impact -- economic impact or to -- if it has, to what degree or how much; is that right?
A. That's correct.
Q. So based upon not knowing if there's an impact or how much that impact is, the secretary is to base a

decision in part upon that fact; is that part of your testimony?

A. Certainly. It does and did happen. The magnitude isn't as important as the principle.

Q. And free enterprise in America isn't a principle that's more important than some of these issues either?

A. Certainly not. If we're going to have a regulated system, and we do, it needs to be fair to everybody. If you want to give up on the regulated system, then you've got the basis of an argument.

Q. Were you part of the discussion in defining the marketing area for the Pacific Northwest during order reform?

A. I was not.

Q. Are you aware of anyone that had proposed that Alaska be included in that marketing area?

A. I'm not aware of that either way. Have no knowledge.

Q. The fact the secretary determined Alaska, either by default or intent. I would assume by default because it wasn't brought up, that Alaska is not included in the marketing area of the Pacific Northwest, right?

A. Uh-huh. That's correct.

Q. So the secretary has determined by that decision that sales in Alaska by distributing plants in Alaska, should not be shared with producers in the Pacific Northwest, right?

A. Doesn't strike me that's what he concluded. If they get their milk in the Pacific Northwest, then it's a class one sale. It should be shared.

Q. No, I mean, let's just talk about Alaska.

A. I am.

Q. All right. So if the milk comes from Alaska, and it's marketed in Alaska, the producer/handlers -- or producers in the Pacific Northwest have no right to the sale of those proceeds, right?

A. That's correct.

Q. All right. But it's your position that because -- notwithstanding that, that any sale outside of this marketing area should be regulated to limit producer handlers, right, or an advantage or whatever that may exist in selling that milk, right?

A. Go through that one again, Ben, because --

Q. All right. I'll withdraw it --

A. -- you're leading me somewhere that I'm not sure that I want to go.

Q. Well, that may be. I hope to lead you a lot of places you don't want to go.

A. I noticed that. It always starts with a smile.

Q. Let's start this again. The fact that Alaska's not part of the marketing area indicates the secretary did not determine the pooling of those sales important by themselves to the producer/handlers of the Pacific Northwest, right?

A. I'm not sure that was his reasoning, but he determined to leave it out. I'm not sure there was a lot more depth in it than that.

Q. And once you get into that unregulated market, it should be fair game to anybody that can supply that market because the secretary decided not to regulate it, right?

A. Secretary decided not to regulate it, but the milk is regulated in Washington and Oregon, and the Pacific Northwest order, and if it goes to class one, then it settles with the pool at class one. Not a whole lot of other use up there.

Q. Maybe the -- the response may be just to exempt those sales from the class one requirement under the order.

A. Why would producers in the Pacific Northwest want to do that?

Q. That -- and -- then they could also then include Alaska as part of the marketing area, right?

A. Could. Could stretch it out to that.

Q. But the intent of your proposal is, is that that sale would be included, right?

A. Yes.

Q. And it's also, as a part of your proposal, that in the event that they do not set the three million cap that the secretary still not allow them to sell milk into Alaska?

A. I didn't say that.

Q. Okay.

A. Because that's an unregulated sale, and it's unregulated sale. There's not much we can do about it.

Q. Okay.

A. Except to change that limit maybe, and bring it downward. I don't anticipate that happening either.

Q. Now, you on page 12 make a comment that you've had a produce -- come a -- or maybe, did you have the conversation with the large producer in Oregon, or you were just made aware of it?

A. No, I had the conversation with him.

Q. You had the conversation with him?

A. Yes.

Q. And --

A. On more than one occasion.

Q. And what was the context of that discussion?

A. Context was low prices.

Q. Isn't it true, Mr. Van Dam, that this producer was told that he had to join a market through NDA or else; then his response was, if I have to do that, I'll be a PD?

A. I have no idea if that's what the situation in a different conversation was. I know what my conversation was, and my conversation I came away from convinced, this man wanted to be a PD, and if he could find the proper markets, he would do it.

Q. And that's part of the other part of the equation we haven't talked about is that you have to have markets, right?

A. Certainly.

Q. And if you make that kind of investment, it has to be a long term market, right?

A. You would think so.

Q. And in your experience in selling packaged milk, how many long term markets are there out there?

A. In the business that I was in, there -- just about everybody was long term.

Q. And how do you define long term?

A. Well, the entire seven years I was there, most of them were customers the entire seven years, had been for some time before that, and I have no knowledge after that.

Q. Well, did they have a contractual obligation --

A. No.

Q. -- for a long term? That's what --

A. No contractual obligation whatsoever.

Q. That's my point.

A. Yeah.

Q. So that you make all this investment in a herd and a plant for a customer, you need a long term agreement, right, or you're taking a risk?

A. You're taking a risk. You don't get long term agreements very often.

Q. And isn't that another factor that contributes to the limitation of producer/handlers growing and being big in the way in which you've been describing?

A. Certainly. Not just the contract, the lack of markets. There has to be a market for the milk, or you can't do it.

Q. And to make that kind of investment with the sophistication, they need to have some assurance that that market's going to be there for some time?

A. That's right. Either assurance or a belief. Sometimes a belief is enough.

Q. Depends on how you -- well, depends on your banker, I guess.

And I want to go down through a list of bottling plants. Well, I thought I was. It doesn't really provide them as being bottled.

The bottling plants that exist in the class one -- or, the 7A plants that exist in Order 124 today, are they bigger today than they were three years ago, in general.

A. Many of them are much larger than they were. Others may be plugging along at about the same rate they've been for five years now. I simply don't know the details of that business.

Q. I believe that's another one for Mr. McBride. We'll see.

A. Yeah. He may have trouble with that one, too. There's a lot of proprietary information that is not readily available to us, but I'll leave it to him. You bet.

Q. Now, you testified you worked for some bottlers, actually worked for a bottling company?

A. Yeah.

Q. Okay. And --

A. Two of them.

Q. And the names of those were?

A. Clover Stornetta Farms.

Q. That was the PD?

A. No.

Q. Well, no, that was not the --

A. It's a regular regulated handler, --

Q. Right.

A. -- in Northbay, California.

Q. Okay.

A. And Chase Brothers Dairy, which was the PD --
Q. Okay.
A. -- down in Oxnard, California.
Q. And the first one you mentioned, and I'm not going to try to repeat its name.
A. Clover Stornetta.
Q. Clover Stornetta. Was that a small, medium, large plant?
A. Small verging on medium.
Q. And what's the range you define as a medium plant in that market?
A. We had -- the only number I can remember off the top of my head is, we had sales of 25 million back then annual.
Q. So that would mean a large plant would have to be much bigger than that?
A. Yeah.
Q. And what were the range or the size of the large plants?
A. I have no knowledge of what their volumes were.
Q. But it's not uncommon for plants to be in the 50 million pound range, bottling 40/50 million pounds?
A. Well, California's a big state, and got some real big plants. A lot of people there. Yeah, that wouldn't be terribly uncommon.

Q. Now, I think you're going -- there's going to be another witness that's going to talk about the plant costs for WestFarm Foods?

A. Yes, Mr. McBride.

Q. And all you know is whatever's been told to you. You don't know how they came up and won't be able --

A. I won't be able to answer the details, but if you want to talk about what I learned from looking at the graph, I've already got it in the testimonies.

Q. Okay. Now, on pages 14 and 15 you list a number of plants in a range -- I take it, by the way, you've done that to suggest the size range of the producer/handlers -- the larger producer/handlers in the Northwest, right?

A. Uh-huh. Yes.

Q. And the -- what's the source of this information?

A. Source of the information is sitting with a couple people that understand this market and doing our best guess, because we definitely wanted to illustrate the point that the larger producer/handlers are not the smallest plants in the market. And we put a proviso on there, you know. You people could fix these numbers, too, if you want. We think they're rational and reasonable.

Q. Now, is this supposed to be total production, or just the class one?

A. Just the class one. Our estimate of the volume going through the plants, class one. And you notice they're big time rounding in there, rather than trying to --

Q.   Yeah, I noticed that --

A.   -- get any more precise than that.

Q.   So you -- if the evidence were that, for example, Anderson were maybe nine or ten million, you have no reason to disagree with that?

A.   If there were evidence submitted to do that, yes.

Q.   Now, you indicate that these regulated plants aren't playing on a level playing field, right?

A.   That's right.

Q.   What prohibits any one of these plants from being a producer/handler?

A.   The requirement that they have to get that many cows and meet the criteria of being a producer/handler.

Q.   But that's not a regulator impediment. That is a business decision impediment, right?

A.   Definitely.

Q.   So it's the same rules. Anderson Dairy has the same rule as Mallory's.

A.   That's correct.

Q.   And they could decide we want to be a PD or not, right?

A.   They could.

Q. And they've decided not to be a PD, right?
A. They have.
Q. Huh?
A. They have decided to not be a PD.
Q. All right. And when they made that decision, you would assume that they knew that being a PD was an alternative, right?
A. If you're using Anderson Dairy, I know that they thought that.
Q. Okay.
A. They knew that.
Q. They've got --
A. I'm sure they all know it. They've all entered their heads, let's get our own cows.
Q. Right. Because they thought there was an advantage there, right?
A. They did.
Q. But after they did all the analysis, they didn't do it, did they?
A. They did not.
Q. And the reason for that, Mr. Van Dam is the fact that in the end, the advantage that you've tried to portray today doesn't really exist, does it?
A. Well, it's interesting that you bring up the point, because it is a point that I find interesting, and I

touched it in my testimony. And I call it a wasting of the advantage. I would agree with you that it appears that the producer/handlers do not take full advantage of the advantage they have. They do not price their milk as if they paid class one, and therefore they do not achieve class one.

Q.   But I'm talking about the handlers of this size that have chosen not to be PDs, have taken -- have given up an opportunity as well, right?

A.   Well, they have. You know, there's a second thought that goes there, and these --

Q.   What's that?

A.   -- believe that if they went ahead and did it, the rules would change, and they don't want to make that kind of an investment and have the rules changed on them.

Q.   Do you know for a fact that that's part of the decision?

A.   I know it is in at least -- well, one case I can think of clearly, vaguely think of another one, but that's -- I'm not sure of that one. I'm sure of one. I'm sure of two.

Q.   But they -- the -- they sit here -- the point is, is that the market forces, in actual play, not theory, but in actual operation is people make rational, business decisions based upon the rules in front of them, have

decided not to be a PD, but could be, right?
A. But there are some other sides that they could be, and some of them used to be.
Q. And they made the decision that that wasn't in their advantage economically, right?
A. That's correct.
Q. And that right there is the most compelling evidence, isn't it, that being a PD isn't what you represented it to be?
A. What have I represented it to be?
Q. That there's this advantage out there to these PDs.
A. Oh, there's no question the advantage is there. Whether they take advantage of it fully or not is a major question.
Q. But the field is level. I mean, the regulated handlers could be one, too. It's just as level, right? They've --
A. They --
Q. -- just decided to play by different rules.
A. It is not level.
Q. Why isn't it level?
A. Because they are not settling with the pool at the class one, class two, class three and four prices.
Q. But that's because the regulated handlers decided

that they wanted to be, but they didn't have to decide that?

A. No, they had -- they have to do it.

Q. Well, no, they --

A. They have decided not to be producer/handlers.

Q. That's my point. And that rule is level, and that everybody can be it, right?

A. No, not every can. I don't believe Safeway could do it. That might just -- that's just too much milk to try and put together. It is not a level playing field, competing against someone who does not pay the class one price.

Q. You say that Safeway's on a level playing field with Anderson?

A. Well, they're playing under the same rules. They're both settling in the class one price --

Q. -- so much larger, much more efficient.

A. That has nothing to do with it. The point is that the -- they settle in a system at the class one price. The cost of their milk into the bottle is the same. What they do after that is market forces entirely, completely.

Q. Then what difference does it make about the efficiencies? I mean, you've got all this evidence about the efficiencies of plants, so I guess that doesn't make any difference in the regulatory system?

A. No, it doesn't. The plant that's not efficient enough that pays the prices will lose money and go out of business. They have -- Vitamilk went out of business, a fairly efficient plant, but not enough volume going through it. Lots of factors involved.

Q. Well, let's talk about Vitamilk a minute. You mentioned that on page 17. How much volume of sales did they lose to PDs?

A. I have no way of knowing.

Q. Was it one load a day, was it one load a week, was it ten loads a day? Do you have any idea?

A. Still don't know.

Q. Do you know whether it's 1 percent or 100 percent?

A. Don't know that either.

Q. So how can you testify that it was a contributing factor to their determination as a business?

A. I spent hours with Mr. Teel, who is the owner and president of Vitamilk. And he regaled me repeatedly about the problems of trying to compete with the producer/distributors -- producer/handlers.

Q. Because isn't the real story with Vitamilk is, is that a huge portion of their sales was with a chain of stores?

A. My testimony says that.

Q. And that chain of stores was bought out by, I think, Kroger or Safeway, right?
A. Well, they had each of those happen.
Q. Yeah. And -- which have their own captive plants?
A. Correct.
Q. So that meant that Vitamilk no longer had a market, right, --
A. -- those two markets were lost.
Q. And those weren't lost to PDs, were they?
A. No, they weren't.
Q. And as -- those contributed to a huge percentage of their sales, right?
A. Don't know the numbers, but it's significant. I know that.
Q. Now, what you mentioned here is, is that the -- over here on the next page, there on page 18, the third -- second paragraph, the last sentence, and this again is talking about Vitamilk, right?
A. Yes.
Q. All right. And it says, "But when that consolidation occurred." Now, that's the consolidation of these chain stores with the Safeway and the Krogers, right?
A. Correct.
Q. All right. "They and WestFarm both focused on

the remaining markets." So I assume the WestFarm lost some sales to that as well?

A. I don't know that.

Q. Okay.

A. They may have been serving some of those accounts, --

Q. Okay.

A. -- but I don't know.

Q. And they both focused on the remaining market, much of which is handled by independent distributors. Isn't it true that prior to loss of -- through the consolidation that Vitamilk had told this -- these distributors and this smaller businesses, we don't want your business any more, either directly or by their pricing scheme, we don't want your business any more. And then when they needed their business, they came back, and the customers remembered the treatment they got before, and said, we're going to stay with who we got, that they had turned it over and gave it to the producer/handlers because that was all that was available to supply that market. Isn't that the case?

A. I have no knowledge whatsoever about your little bit of testimony there. None. I have not heard --

Q. Okay.

A. -- that, do not know that. I'm not even sure I believe it.

Q. But you do say -- you do suggest in here that they were coming back to that business. It wasn't part of their market before, right?

A. No, they -- what I'm saying is, they started concentrating on it because as business becomes unavailable, everybody left in the market must concentrate on --

Q. Right.

A. -- what business could be available.

Q. And that business at that time was already held by producer/handlers. It wasn't taken from them, it was already held by producer/handlers, and they came in and wanted to get it back, and they didn't get it, right?

A. I simply don't know -- have any knowledge of that either. I wasn't involved --

Q. So then your statement isn't based on a full knowledge of the facts that it was a -- the producer --

A. I don't even know that what you're saying are facts.

Q. Well, I'm talking about your facts. I mean, is there anything in --

A. My facts are good. This is what happened. They did have to concentrate on what business could be available.

Q. But you don't know what the competitive situation was before and after they decided to make that business --

A. No, I do not.

Q. And that makes a lot of difference, doesn't it, to determine whether or not the producer/handlers had an advantage or not.

A. It makes no difference to what I said. My point is the same. They had to concentrate on a piece of business that could be available.

Q. Yeah.

A. There's no point in trying to get a customer you can't get ever.

Q. And isn't it true that the one distributor that they lost to Etteline accounted for only one trailer load of milk per week?

A. Don't know.

Q. Well, let's put it -- if the evidence shows -- you have some idea of the size of Vitamilk, right?

A. Yes.

Q. All right. If Vitamilk lost just one trailer load of milk in its sales, would that be sufficient to have put it out of business?

A. You never know where the last straw is.

Q. But in general, would you expect that to be the result?

A. No, I wouldn't.
Q. All right.
A. On trailer load a day usually doesn't break a plant, but after other things happen.
Q. But one trailer load a week could be even less so, right?
A. Would be. The thing to keep in mind is that Vitamilk was a series of blows, and finally decided the business wasn't worth continuing.
Q. I want to go back to this issue on Alaska. Who -- do you know who supplies milk outside of the state of Alaska to the plants in Alaska?
A. I know that NDA supplies some of their supplies. I don't know for sure who else might be.
Q. And do you know what price they charge for it?
A. NDA? You'll have to ask Dan that. I don't know, but they do settle with the pool at class one on it.
MR. YALE: Rapidly going through my notes. That doesn't mean I'm going to be done. I mean, I'm just checking to make sure.
(Pause)
BY MR. YALE:
Q. Are you relying in any way on Carl Herbine's testimony?
A. Looked at his testimony, and made the conclusions

that we see here. So I did rely on it to that point.

Q. Did you provide any information to Carl Herbine for that testimony?

A. I did not.

Q. And in your preparation for your testimony, did you do any studies of PDs as a single enterprise -- I mean, complete studies in terms of the costs, the capital, the risks, the efficiencies, the inefficiencies, the regulatory impacts, anything at all?

A. I did no new studies. What I learned from Chase Brothers in Oxnard, I still have, but that's it.

Q. There's been some discussions in the industry in the last couple of months about the possibility of voting out an order because of some dissatisfaction with some pooling requirements, I think, in the Western order, and you're aware of that, right?

A. Yes, I am.

Q. All right. NDA is in a position to -- by itself to decide whether a proposed amended order is adopted or not, right?

A. Correct.

Q. All right. And is it NDA's position that the PD situation is such that so much disorderly marketing is created by producer/handlers that it would vote the order out if the secretary refuses to adopt the proposal that it made?

A. I simply can't comment on that.

Q. Now, I think we're done on the PD issue. I got -- I want to talk at the end of your testimony you bring up some other issues. You talk about California, and you talk about some pooling, just -- you characterize a situation as a loophole at page 19.

A. Yes.

Q. Okay. Isn't it true that the USDA and the interest in California came to an agreement, unintended maybe, but they came to an agreement that milk from out of California, shipped into California would not be subject to regulation?

Let me ask you this question. Are you aware of the fact that -- let me -- when were you in California? You weren't there in the '90s -- late '90s, were you? Were you aware --

A. No, hang on a second. Let me deal with the reasoning here. I think I left in 1991.

Q. Okay. So the Fair Act had passed, I guess, under -- some people called it the Unfair Act, but the Fair Act had passed. And we started order reform in '96, and California had an opportunity to come into the federal order; is that right?

A. That's correct.

Q. And California decided they did not want to have a federal order, right?
A. Correct.
Q. And they have a state order, right?
A. Correct.
Q. And do you understand that under the Interstate Commerce Clause that states are limited on how they can regulate product moving from one state to another?
A. Yes, I am.
Q. All right. So when California made the decision that they were just going to regulate it within their state, they intended, did they not, or accepted the fact or the risk, that they would not be able to regulate milk moving from out of California into their state, right?
A. Well, that's roughly correct. They were assuming the risk is what I would assume --
Q. Right.
A. -- determine.
Q. The risk, right.
A. Yeah.
Q. And at the same time and in that same period, the secretary considered decisions in terms of the size of the marketing area of the Arizona/Las Vegas market area, right?
A. I believe that's true.
Q. And proposals to include California were not

adopted, right?

A. That's correct.

Q. And it decided that producers in Arizona would not share in sales of milk, solely on the basis of sales into California, right?

A. Well, I don't know if they decided that, but that's what happened.

Q. That's what happened, right?

A. Yeah.

Q. Because they intended that this was the marketing area we're going to regulate. We're not going to regulate these other sales?

A. They can't.

Q. They can't.

A. Right.

Q. They could've, but they decided -- the federal government decided they weren't going to.

A. Because California decided they weren't coming in.

Q. -- didn't want to. Okay.

A. Yeah.

Q. So if the parties made that conscious decision, they have to live with that result, right?

A. For now they do. Obviously there's a reaction to every action, and the reaction is going on. Who knows where it's going to end.

Q. Right. But it wasn't a -- it's not so much a loophole. It is more of the gap in the regulation that the parties decided that they were going to take that risk?

A. That's how I define loopholes.

Q. Okay

A. Gaps in regulations.

Q. Okay. I want to move over into proposal number four. And I want to deal specifically with the California situation.

THE COURT: I'm going to just interrupt for a minute.

MR. YALE: Sure.

THE COURT: We've been going about an hour and -- what time is it now, an hour and a quarter. I was thinking maybe we should take a ten minute break, and then we'll continue until this witness is done. At that -- at which point we'll have lunch, unless -- or 1:00 o'clock, whichever comes first.

Okay. Because it's -- I'm just -- in the interest, I give -- he's been up for an hour --

MR. YALE: Oh, I think that's fair.

THE COURT: So we'll take a ten minute break, and then we'll continue with this witness until either this witness is done or until 1:00 o'clock, whichever comes first. At which point, we'll have lunch.

(Off the record and reconvened.)

THE COURT: Okay. We're back on the record.

I've just been told that Mr. Yale has no more questions. So I'll see who else has questions. Mr. Ricciardi, do you have questions.

MR. RICCIARDI: I do, Your Honor.

THE COURT: Will this be a good time?

MR. RICCIARDI: I'm ready to proceed whenever you're ready to proceed.

THE COURT: Come on up.

EXAMINATION

BY MR. RICCIARDI:

Q. Al Ricciardi on behalf of Sarah Farms.

Mr. Van Dam, you indicate in your testimony that you have -- NDA, excuse me, has no direct connection with the Arizona/Las Vegas market Order 131; is that true?

A. That's true.

Q. With regard to the testimony itself that was prepared, who assisted you in the preparation of that testimony?

A. I did most of it myself, but I had some input from Mr. Doug Marshall.

Q. Anyone else?

A. No, that's it.

Q. Okay. Anyone from UDA or Shamrock or anyone else provide you with any information?

A. Other than our collaboration on the wording that we -- in our proposals. That's where we limited our collaboration.

Q. Okay. You do not have any personal first-hand knowledge as to issues or events in Order 131, correct?

A. I do not.

Q. And you do not intend through the preparation of your testimony or the admission of your testimony to provide any direct information or knowledge regarding events that occurred in 131, correct?

A. That's correct.

Q. And you don't have any intention through your testimony to provide any information, because you don't have any, with regard to Sarah Farms, correct?

A. That's correct.

Q. Would you agree that based upon your experience, the fluid milk marketing channels in this country have been under-growing -- undergoing a rapid, structural change in the last three to four years?

A. Longer than that, but yes, it's continuing.

Q. And how has the channel been changing?

A. Consolidation is the most -- well, there's two major things occurring. Consolidation of chains into bigger chains that have their own milk plants, and therefore there's a fairly major shift in available market to the traditional handler. And the second one, obviously, the advent of Wal-Mart and the impact they have with their volumes.

Q. Wal-Mart is a warehouse store?

A. No.

Q. What is it?

A. Sam's Club would be a warehouse store. They own that one.

Q. Understand.

A. But they have more traditional, but very large superstores that they put together that command huge volumes.

Q. And so the -- in terms of the change in channels, what that means is that more of the fluid milk market has been moving to those type of stores, correct?

A. Correct.

Q. And that has occurred over the last four to five years?

A. Correct.

Q. When a business grows, one of the reasons for its growth may be that it produces a better product, correct?

A. That could be one of the reasons.

Q. One of the reasons may be that it's more

efficient than others in the industry?
A. That's correct also.
Q. One of the reasons may be that it has better customer relations, correct?
A. That could be also.
Q. It also may be that there's better service provided by that particular company?
A. That could be.
Q. It also may be that the quality of the product is better than its competitors?
A. That could be also.
Q. And that would be true in the milk industry also, correct?
A. Just as true there as other places.
Q. And I think you said in response to some questions from Mr. Yale that one of the reasons that people are regulated handlers -- more regulated handlers have decided not to explore the alternative to become a producer/handler is because of the concern that they might have, and I'll try to quote you, "that they don't want to make that type of investment and have the rules changed on them."
A. Correct.
Q. Now, with regard to the producer/handlers that do exist, including my client, Sarah Farms, they've already

made the investments to become a producer/handler, correct?
A. That's correct.
Q. They made all of the financial investments to go ahead and build dairies, correct?
A. That's correct.
Q. They've made the financial investments to build a processing plant, correct?
A. Correct.
Q. And now what you want to do is to change the rules on them essentially in the middle of the game, correct?
A. Absolutely.
Q. Okay. You gave some testimony regarding one the -- some of the reasons for establishing marketing orders. Do you remember some of that testimony?
A. Yes, I do.
Q. Okay. Some -- one of the other original reasons for establish the market orders was to protect farmers --
A. Correct.
Q. -- from monopsonistic pricing by channel firms.
A. Second to last word?
Q. Channel firms.
A. Channeled firms?
Q. Channel.
We talked about it before when I asked the

questions, and we're talking about consolidation in the industry, --

A. Okay.

Q. -- milk marketing channels, et cetera. Isn't it true that in the last five years also, in terms of the consolidation throughout the United States that companies like Dean Foods have established a larger and larger presence in various markets?

A. This is true.

Q. And, in fact, you're aware that Dean Foods controls about 30 percent of the dairy products in this country today?

A. Not clearly aware of that problem, but it is significant.

Q. Were you aware that there were some hearings by the Senate on the power of some of the monopsonistic companies, such as Dean Foods in the dairy industry recently?

A. No, not aware of those hearings.

Q. Would you agree with me -- actually, would you agree with Senator Lahey (phon.) that as a result of the changes, the dramatic changes over the last few years in terms of the growth of larger companies like Dean in this industry, that farmers are not getting a fair share of the retail price of the milk; would you agree with that?

A. No.

Q. Okay. Do you agree with Senator Lehigh that giant, corporate processors are taking in anti-competitive profits as they raise prices to consumers?

A. Not aware of that either, and I don't agree with it.

Q. You don't agree with that? Okay.

Is Dean -- does Dean Foods have any joint venture agreements with Northwest Dairy Association?

A. I really can't answer that. You're going to have to ask Dan that. I don't believe so, but I -- they might have some I don't know about. I doubt it.

Q. Does Land O' Lakes have any kind of either joint venture agreements or other agreements with Northwest Dairy Association?

A. Not aware of that either.

Q. I asked you in general. Let me be specific now. With regard to the information which is contained at the bottom of page 19 of your testimony, Mr. Yale had touched on it when he was talking to you about California.

You don't know who owns this new plant that you reference on the bottom of page 19, correct?

A. Yes, I do.

Q. Okay. You've seen the ownership papers?

A. No, haven't seen the ownership paper, but I know

who owns it.
Q. Okay. You've talked to someone directly who told you that they're the owner?
A. That's correct.
Q. Okay. With regard to this loophole, by the way, you were asked some questions by Mr. Yale. The actual loophole that you're talking about is the Federal Constitution, the Commerce Clause?
A. That's the one.
Q. Okay. So that's the one you want to plug up, we need to change the constitution; is that your position?
A. That would be difficult.
Q. Okay.
A. No, I -- but I like that term or phrase. That's clever that you came up with that. Give you points on that one.
Q. I feel so much better now.
A. I knew you would.
Q. Let me ask you a couple of other questions. With regard to the growth or non-growth of Sarah Farms since 1999, you do not have any direct, personal information as to either the size of the growth or the reason for the growth, correct?
A. Do not have personal information.
Q. You would agree with me that milk markets change

as any other market might change over time, correct?
A. That's correct.
Q. As competition comes in, a milk market might change?
A. Certainly.
Q. Okay. And the fact that there is additional competition doesn't necessarily mean that there is ultimately disorderly marketing, correct?
A. Just new competition does not generate disorderly marketing.
Q. Do you know how much money that Sarah Farms has as an investment in either the dairies or the processing plant?
A. I do not.
Q. Do you know how much money in investment that Mr. Hannigah and his wife have at risk with regard to those investments?
A. No, I do not.
Q. Okay. Would you agree with me in general that a newer processing plant will have better technology and therefore better efficiencies in terms of the production costs for milk?
A. Well, we certainly hope so. It doesn't always make it better, but it will be good.
Q. And it should be better than an older plant?

A. That, of course, depends on the level of investment in the older plants. Some of them do a marvelous job of staying current.

Q. But if you have an older plant where you have the decision as to whether or not you need to continually fix a problem, whether it be on the line, et cetera, you're going to run into a problem in terms of your cost, because the cost is going to increase as the line breaks down?

A. This is true.

Q. If you put in the investment for a new plant, however, and you get the technology and the efficiencies, you're going to hopefully reduce the cost of the product that you're selling, correct?

A. You would hope so.

Q. And there --

A. Although there is a capital cost to offset that.

Q. Understand. Once you take the capital costs, and you take that and reduce it, you're going to, over time, recapture it, and you're going to be able to have a higher profit?

A. That's the idea.

Q. Okay. And once you do that, then the decision can be reached whether or not you're going to capture the profit, or whether or not you may turn some of that profit over to your customers, correct?

A. That's correct.
Q. And that's an internal decision that any company can make, including a producer/handler?
A. Correct.
Q. Does the fact that a company like Dean Foods has so significant a size of the market, and therefore so significant strength in the marketplace, does that result in "ruinous competition" that is "disrupting the marketplace?"
A. Not that I'm aware of.
Q. So if Dean Foods, for example, captured 90 percent of a regional market in a federal order area, your testimony would be that that would not result in a disruption in the marketplace to the smaller producers, correct?
A. So long as there's a federal order regulation that marks the price difference between the two, they're unrelated issues.
Q. So --
A. I would be nervous about a 90 percent market penetration. I'm like you and everybody else, but in terms of a disorderly markets, as we use the term in the federal order system, that isn't going to create in and of itself disorderly markets.
Q. Is a consumer important in the federal order

system?

A. The consumer's ultimately the reason the federal orders exist.

Q. So the consumer is important?

A. The consumer is important.

Q. Is it ultimately the price paid by a consumer important in the federal order system?

A. The ultimately, long term price is, and the verification that the product will be there is.

Q. So adequate supply of fresh, fluid milk --

A. Right.

Q. -- at a quality fresh fluid milk product is one of the reasons for the federal order system, correct?

A. Part of the underlying assumptions that go into the federal order system to ensure an adequate supply of milk to the consumers of this country.

Q. Well, your testimony is, if you had market penetration of 50 to 70 percent by one, major company like Deans, which would ultimately result in potentially higher costs to the consumer for that product, that that would not cause any disruption in the marketplace as you define it?

A. Disorderly marketing as we define it for federal order purposes.

Q. Okay.

A. Yeah.

Q. What if we went to 90 percent?
A. Same answer.
Q. 100 percent?
A. Well, that would be interesting, but they will not be able to maintain that, --
Q. Okay.
A. -- because there will be competitors come in.
Q. At 100 percent market penetration, Deans in that region could charge whatever it wanted to?
A. Yeah, except they'll attract somebody.
Q. And that would not, in your opinion, based upon your testimony in which you're providing to the secretary in this hearing, cause any disorderly marketing?
A. Would not cause disorderly marketing of the type that causes problems in the federal order system, so long as the federal order's there, and the prices are set by the federal order.
Q. And is it your testimony that if we had a regulated production plant in the Northwest area that was inefficient, and that was, in fact, not producing at a level that it should based upon the economics involved, that that particular plant should be able to share in the efficiencies of a producer/handler if it went over three million pounds a month?
A. I'm not sure I followed you through that whole

thing. You want to try it again?

Q. Yeah. Let me see if I can do it better.

We're trying to talk about if -- and some of your testimony, at least, efficient markets, correct?

A. That's part of it, yes.

Q. Yeah. And what I'm trying to ask you is this. You have an inefficient production plant for whatever reason. It's older.

A. It's an assumption you're making. Go ahead.

Q. Okay. And then that's a hypothetical I'm giving to you.

Is it your testimony that even given its inefficiencies, that that plant should be able to share in the producer -- a producer/handler's output if it went over three million pounds a month?

A. And there is no impact there. That's why I'm puzzled with your question. The fact that a producer/handler would have to pay the classified price has zero impact on the inefficient plant that you've hypothesized, except to the extent that his competition now has -- is paying the same price he is. Otherwise he gets nothing from it.

Q. Couple of other questions. You don't -- in addition to having not a factual background of 131, you don't know about growth rates of producer/handlers over the last three years, correct?

A. Not in 131.

Q. Okay. And you don't know about the number of producer/handlers in 131, correct?

A. Other than the data I've seen, just like everybody else here.

Q. Okay. You don't know whether or not the growth is up or down for producer/handlers yourself, personally, correct, in 131?

A. Not myself, personally, although I know it's up.

MR. RICCIARDI: Okay. Nothing further. Thanks.

THE COURT: Okay. Mr. Cherry. Don't forget to identify yourself.

EXAMINATION

BY MR. CHERRY:

Q. Richard Cherry. Good morning, Mr. Van Dam.

A. Is it still morning.

Q. Oh. No, sir.

A. It didn't feel like it.

Q. Of NDA 603 producers, how many would you consider small businesses?

A. Well, we believe all of them are, except you just don't know the structures and whether they're part of something bigger, but gosh, it's a vast majority are small businesses.

Q. Okay. And of the 603 producers, what type of impact would these regulations have on these small businesses?

A. Well, other than improving their income by the 2.8 cents or 4 cents, whatever that number is, that would be the direct impact on them, but we have testified that there's a bigger issue having to do with the existence, the continued existence of the federal order system. That would have a major impact on them if the federal order system is lost.

Q. Thank you.

A. You're welcome.

MS. DESKINS: Sir, when you said that --

THE COURT: Identify yourself.

EXAMINATION

BY MS. DESKINS:

Q. Oh, I'm Charlene Deskins.

When you stated that there would be an increase of two to four percent for small producers, could you just tell us where you got that figure from?

A. Yeah, it's 2.8 to 4 cents per hundredweight, and that came from our tables and my discussion with Ben. And what it is, is the class one premium dollars that if these plants were regulated, they would have to pay into the pool some 4 -- well, it's 3 that would be regulated. Some $2.8

million a years into the pool that didn't exist before, and you just spread that money over the pool.

Q. Okay. That would only apply then just for Order 124?

A. 124, yes.

Q. Okay. I had a question for you on page three, and this is about the language that's been changed in the proposal.

A. Okay.

Q. Okay. My question is concerning -- I noticed that "ownership" has been deleted, and I'm just wondering, particularly on number two, if a producer/handler owned a process -- milk processing plant, and they leased it to someone, under this definition, they wouldn't have complete and exclusive control so they could still qualify for the producer/handler?

A. I'm sorry, I'm not quite staying with you on that question.

Q. Well, let's say you had a producer/handler, and let's assume he has two plants.

A. Uh-huh.

Q. He leases one.

A. Okay. Producer/handler has two plants.

Q. He leases one.

A. Uh-huh.

Q. He has the other one. Would he still be able to be a producer/handler under this definition?
A. By leasing it he is the person doing the leasing. He controls the plant through the lease. Then he would be a producer/handler. He could do that.
Q. And he --
A. It's got to be exclusive. I mean, the word "exclusive" is in there on purpose. You can't go lease a part of a plant and call yourself a producer/handler.
Q. But he leased the whole plant --
A. The whole plant. By the definitions we're proposing, that could count. It is the complete and exclusive control that counts here. Ownership gets a little nebulous, and we struck that even though ownership sounds like a cleaner, firmer word, it is not quite as easy to deal with.
Q. Well, I'm just wondering, because usually allotted commercial leases, when you lease it, the landlord doesn't have any control over those facilities any more, except to maybe come in to repair the roof.
A. Yeah.
Q. And I'm just wondering under this, if he leased it, you're saying he would still have control over it, even though he leased it to somebody else.
A. Okay. I think where we're getting confused is,

who's doing the leasing. I've got the producer/handler leasing the plant. You may have the producer/handler leasing it to somebody else.

Q. Right, the producer/handler leasing it to someone else.

A. Yeah, then he's going to lose -- he will lease it to somebody -- if he gives up complete and exclusive control and it's just an ownership position, I believe he can do that.

Q. Okay.

A. So long as he doesn't have anything to do with that plant.

Q. So if it's just a standard commercial lease, he --

A. Standard commercial lease, --

Q. He couldn't lease it --

A. -- he's leasing it to somebody else, long term, he has no control over it except to fix the roof as you say.

Q. Okay.

A. Yeah.

Q. That was my only question.

A. Okay.

THE COURT: Any -- go ahead, Mr. English. Mr. English was on his way up first.

EXAMINATION

BY MR. ENGLISH:

Q. Charles English for Shamrock Foods and Dean Foods Company.

You were asked a couple of questions by Mr. Yale about individual handler pools.

A. Yes.

Q. Prior to federal order reform, which took effect January 1 of 2000, there was one of 42 orders, 34 orders that had individual handler pools, still?

A. That's correct. They only existed in one of the orders.

Q. And that was the Upper Peninsula order?

A. I believe that's correct.

Q. And the Upper Peninsula was, you know, what we -- the part of Michigan that's not, you know, that is the peninsula, correct?

A. Correct.

Q. That's what the Upper Peninsula was. And there were a couple of -- there were two plants up there, right?

A. That's correct.

Q. And before that, that one last individual handler pool went out, effective January 1, 2000, were there any other orders to your knowledge for the past ten years that had individual handler pools on them?

A. Not to my knowledge. They'd been pretty much gone for a long time.

Q. And was the Upper Peninsula a large or significant order relative, say, to this order, the Pacific Northwest?

A. No, it's not.

Q. Was it a larger, significant order relative to the Arizona order?

A. No.

Q. And, in fact, of course, on January 1 of 2000, whatever entities had made investments in those facilities discovered that those investments were now no longer individual handler pools, correct?

A. Correct.

Q. That was a changing of the rules in the middle of the game, correct?

A. Absolutely.

Q. Not very uncommon in this industry, is it?

A. It's not. It happens.

Q. In fact, you testified earlier that there -- you were at the Idaho proceeding, and people had made various decisions and investments and USDA came along and said that that was disorderly marketing, and proposed to through out the proprietary bulk tank counter-provision, correct?

A. Correct.

Q. And that's a changing of the rule in the middle of the game, correct?

A. Rather significant change.

Q. And we have had a number of pooling hearings around the United States with respect to issues such as whether or not milk from a state marketing pool could be pooled simultaneously on a federal order, correct?

A. Correct.

Q. And also we have had, within the context of those proceedings, a number of changes to what constituted a pool producer or a pool plant, correct?

A. Correct.

Q. And that was changing the rules in the middle of the game, correct?

A. Correct.

Q. And that's just in the last couple of years, right?

A. Yep.

MR. ENGLISH: That's all I have.

THE COURT: Mr. Berde, did you have some questions?

MR. BERDE: I have some.

EXAMINATION

BY MR. BERDE:

Q. Mr. Van Dam -- Sydney Berde.

Mr. Van Dam, from your testimony, I take it you measure the compared -- the competitive advantage the producer/handler has by the difference between the class one and blend price, that he does not have to pay into the pool; is that correct?

A. Correct.

Q. Would that same, competitive advantage apply to any market in which producer/handlers operate?

A. Correct, it would.

Q. So it -- not necessarily unique. Your testimony is, it isn't necessarily unique to the Order 124 situation?

A. It applies to all producer/handlers in all markets.

MR. BERDE: Thank you.

THE COURT: Any more questions of this witness?

Mr. Marshall?

MR. MARSHALL: Thank you, Your Honor. A few questions on redirect. Doug Marshall with Northwest Dairy Association.

EXAMINATION

BY MR. MARSHALL:

Q. Well, Mr. Van Dam, it appears you and I are what's standing between this crowd and lunch. So let's --

A. You're in trouble.

Q. Let's be brief. Want to follow up on some of the line of questioning that you were getting from Mr. Ricciardi regarding Dean Foods. Do you remember that testimony?

A. Yes, I do.

Q. Is Dean Foods, to the best of your knowledge, active in the Order 124 market?

A. No, it is not.

Q. So you aren't familiar with any of those hypothetical situations that he was posing to you?

A. I am not.

Q. Let's talk hypothetically then about "A" handler that might have 80/90, even 100 percent of the class one market. I believe you testified that the concept of disorderly marketing conditions would not necessarily change -- be impacted, excuse me, let me rephrase that.

I believe you testified that such high market shares might not necessarily create conditions related to what traditionally the federal orders have called disorderly marketing conditions.

A. That's correct.

Q. Did you discuss these potential issues with NDA before your testimony?

A. Not specifically.

Q. So you were giving your opinion, not necessarily NDA's opinion --

A. Yes.

Q. -- on that. Let's go through some of the implications, though, of a handler having 90/100 percent of a market. Such a handler, if I understand the rules correctly, would have the control of the pooling base for an order, would they not?

A. In terms of earning pooling rights, the ability to pool, yes, they would, but the -- but if they get their milk from a cooperative who operates in that same market, then the control and the voting rights and that belong to the cooperative.

Q. Let's make sure we're talking about the same thing. Are you referring to the provisions of federal orders, known as the diversion limitations and associated pooling rules?

A. Yes.

Q. So in a situation where a individual handler, or for that matter, an individual cooperative were to control a high percentage of the class one sales, they would control the ability to pool on that order as well, would they not?

A. Yes, they would.

Q. Now, in your testimony, I believe you referred to the concept that at times it may be possible that people would find it advantageous to sell -- let me rephrase the question, it may be times when marketers of bulk milk may find it advantageous to sell below the class one price to class one handlers?

A. That's correct. That was the situation in Idaho.

Q. And was the issue in Idaho -- that's correct. Were referring to your testimony at the hearing in Salt Lake City in April of 2002. And was the purpose of that scheme that was being regulated -- was proposed to be reregulated to obtain pooling rights?

A. Yes.

Q. So there was a situation where the need to obtain pooling rights created disorderly marketing conditions?

A. That is correct.

Q. And can you conceive of a situation where the issues involving producer/handlers might create similar kinds of disorderly marketing conditions?

A. Yes, I certainly could envision that as the market gets smaller, because consolidation keeps sales from being available to the remaining, tradition handlers. They could easily be in a situation where there's not enough class one sales out there for them to get, to get producers qualified for the pool, and it could cause very disorderly conditions. as they try and find enough class one sales to stay pooled. a producer's qualified

Q. So the power of the pooling rules in making economic decisions, would you describe that as significant?

A. It's significant.

Q. That's what we saw in Idaho?

A. Yes.

Q. And that Idaho situation, would that have been a change of the rules for those who invested in those facilities?

A. It certainly was a change in the rules.

Q. And when the federal order -- if the federal order is voted out, will that also be a significant change --

A. That will be a very significant change.

Q. You were asked -- well, returning to the concept of the Pacific Northwest order here, rather than Idaho, based on your experience and your work with various handlers over the last few years, in your opinion, how competitive is the market in which bottling plants sell to their customers?

A. Very competitive.

Q. Could you explain in any detail or any further detail why you reached that conclusion?

A. From the visits with them, they were constantly complaining about the other guys trying to take their markets and pushing the prices down and not allowing them to maintain profitability. Those are just about always preceded by the comments about the consolidation and the lack of market available to the traditional handlers.

Q. You were asked a question by Mr. Ricciardi about a senate hearing, I believe, and a statement I believe he attributed to Mr. Lehigh about large profits being taken by processors. To the extent that that may be occurring, in your opinion, do you see any evidence that it's happening in the Pacific Northwest Order?

A. No, I do not.

Q. In your opinion -- well, we also refer you to one of the questions that you were asked by Mr. Cherry about the impact of his proposed regulations on small businesses, including those small businesses who might be dairy farmers who are members of Northwest Dairy Association. You identified some potential aspects of the proposed -- our proposal on small businesses. To the extent that producer/handlers are competing in the marketplace with a different cost structure because their exempt from uniform pricing. Could that also contribute to the highly competitive environment in which you have observed or testified to a few moments ago?

A. Yes, it certainly can.

Q. And I believe -- did you testified earlier that that was what was involved with about your discussions with Vitamilk Dairy?

A. Yes, it was.
Q. If the -- if all producer/handlers over three million pounds were competing on the same, uniform pricing level as regulated handlers, is it possible that that would impact positively --
A. A very good chance that it would.
Q. I haven't finished my question.
A. Uh-huh.
Q. Would that impact positively and since raising the price that is available to wholesale sellers of bottled milk?
A. Yes.
Q. It's possible?
A. Quite likely.
Q. And if so, would that benefit accrue in part to any producer who ships to a cooperative that owns all or part of a bottling plant?
A. Yeah, they would -- their position would improve based on improved profitability at their plant.
Q. Mr. Yale was asking you questions about the Vitamilk testimony which, of course, occurred at the Phoenix section of this hearing, and he asked you what might have been styled as a hypothetical question about losing just one trailer load of sales to one of his clients. Is it only the lost business that impacts market

price or a competitor?
     A.   Absolutely not.
     Q.   How else might Vitamilk have been impacted besides the loss of one trailer, or whatever, quantity of milk sales they actually lost, how else might have --
     A.   By --
     Q.   -- been affected by producer/handler competition?
     A.   By being forced to reduce your prices to keep business.
     Q.   You indicated having had the opportunity to be instructed by Mr. Jerry Teel at length about the challenges he was facing, and would he ever mention that kind of situation to you?
     A.   He certainly.
     Q.   Mr. Teel being the owner of Vitamilk Dairy?
     A.   Yes.
     Q.   I think there was a question you were asked. Again, it may have been hypothetical. I wasn't quite clear. It's going to be referenced to the Oregon producer who was considering becoming a producer/handler, that you refer to in your testimony, and I believe the question, if my notes are correct, that Mr. Yale -- a question Mr. Yale asked was whether he had been told that he had to market his milk through NDA. Based on your knowledge of that Oregon producer, do you know if he was told that? Is there

any reason to believe he was told that?
A. I do not believe he was told that, and if he was, he certainly didn't tell me.
Q. Does he market to NDA?
A. He does not.
Q. To whom does he market?
A. Farmers Cooperative Creamery.
Q. What other alternatives does he have where he is located?
A. He would have NDA as an alternative. He would have Portland Independent as an alternative, FCC where he is, and --
Q. Would there be any proprietary handlers in his market --
A. Oh, DFA, I'm sorry. Yeah, DFA.
Q. Any proprietary owned plants that are -- have their own producers in that Oregon area?
A. Well, the only one that I know of is Umpquah, which is pretty far away, but he has that alternative.
Q. Anybody near Clackamas, Oregon?
A. Yeah, there is another one.
Q. Oh, really?
A. Yeah, a fairly large outfit.
Q. Well, who would that be?
A. Safeway. Sorry about that.

Q. Some expert.

A. That's right.

Q. Again, just to clarify what may already have picked up in cross-examination. Mr. Yale was asking a question involving the Idaho plants in that hearing, and indicated in a question that they were required to pay the class one price, and I believe you answered, yes, that's correct. As you've thought about that, got any reason to reconsider that testimony?

A. Yeah, there's reason to reconsider that testimony, because there's special rules that apply in situations like that there, and the class one is actually paid by the proprietary plant rather than the supply plant. Supply plant was not required to pay class one, just settled with the proprietary plant. So the pool was clear with the class one price, but the plant itself did not have to pay the class one price.

Q. And was that -- were any of the proposals designed to directly address that situation? Any of the proposals in that earlier hearing --

A. Yes, there was a proposal in that hearing to specifically answer that. The department chose instead to eliminate the situation.

Q. So the parallel that you've drawn in your testimony to that situation -- let's go through the items.

Plant being operated by somebody?
     A.   Yes.
     Q.   Not required to pay the uniform price by the rules as they then existed?
     A.   That's correct.
     Q.   Resulting, and in fact, not paying the class prices, --
     A.   That's right, not paying it. Right.
     Q.   -- as they -- as was testified to; is that correct?
     A.   Correct.
     Q.   And the department found disorderly marketing conditions in that situation, coupled with, I guess I should've added, testimony at that hearing about the impact in the marketplace?
     A.   That's correct.
     Q.   Mr. Yale asked you a question, and I must confess, I was confused by the question. So I am asking what you meant in your answer to it. The question, I think, involved a situation where pool producers might compete with Etteline Dairy in some sale of bulk milk. So I want to understand what your understanding is. If you have a pool producer and Etteline Dairy -- well, in that potential competitive environment, can both of them be -- find themselves competing for sales to a regulated bottling

plant?

A. Yes, they could.

Q. And, in fact, that would be -- you testified that producer/handlers have, at times, sold to regulated bottling plants --

A. That's correct.

Q. -- an example of that competition. Can both pool producers and Etteline Dairy itself provide milk to the Etteline plant?

A. Except for the limit of the 150,000 pounds, which we're pretty much ignoring, they cannot.

Q. In fact, they could buy more than 150 million pounds if they chose, could they not?

A. Yeah, but then they'd lose their status as a producer/handler.

Q. It's a bright line over which they -- which they're aware they'd like to stay on the lower side?

A. Correct.

Q. Well, Mr. Van Dam, I think you've been up here a long time today, and I'm prepared to -- I've asked my last question, except to invite you. Is there anything else that you wanted to say to clarify any aspect of your testimony in this hearing?

A. No, nothing to add.

MR. MARSHALL: Thank you so much.

THE COURT: Let me see if anyone -- because you asked your last question -- go ahead -- Mr. Beshore has a question.

EXAMINATION

BY MR. BESHORE:

Q. I have one question. -- Marvin Beshore.

One question with respect to the language proposed on page three of your testimony, and I want to give you a copy of Exhibit 32, Mr. Hollon's testimony, and call your attention to page 19.

Okay. And so I want to compare the -- I want you to compare the language that Mr. Hollon proposed for Section (a)(2) on page 19 of Exhibit 32 with your proposed language in Section (a)(2) on page three of your testimony, which has been marked as Exhibit 35.

A. Right. It is obvious that we have left off part of a sentence in our copy, and if appropriate, I'll read it into the record.

Q. I'd like you to do that. Is it your testimony then that you would like to add at the end of part (a)(2) on page three of Exhibit 35, your proposal, some language that was inadvertently omitted?

A. Yes.

Q. Okay. And that language, after the word "operated," which is presently the last word --

A. Right.

Q. -- at the end of that would be what?

A. Needs to have added, "As the producer/handler's own enterprise and at its sole risk."

Q. Okay. And is it your intention then to make the language that you propose identical with that which Mr. Hollon proposed in -- and testified to in his Exhibit 32?

A. That is our intent.

Q. Okay. Now, just focusing on that language a second, because it has been the subject of some questions to you, in fact, from Ms. Deskins. The word "ownership" has been deleted. It's stricken through on there, correct?

A. Yes.

Q. And that allows a producer/handler the option of being the lessee of plant assets in this case.

A. True.

Q. But those assets must be held and as the language that you have now made clear, is intended to be part of your proposal at the producer/handler's own enterprise and at its sole risk, correct?

A. Correct.

Q. So that it can't share -- if it's leasing them and doesn't hold title to the assets, it still can't share the risk with anybody. It's got to be its sole enterprise and its sole risk?

A. Absolutely. That is the intent.
MR. MARSHALL: Okay. Thank you, Mr. Van Dam.
MR. UNIDENTIFIED: I have one.
THE COURT: Why don't you go, Mr. Berde?

EXAMINATION

BY MR. BERDE:
Q. Sydney Berde.
Bill, one of the handlers -- regulated handlers that you list is Anderson Dairy. Do you recall that?
A. That is correct.
Q. And you had some questions per Mr. Yale (phon.) about Anderson Dairy.
A. Yes.
Q. Do you recall whether Anderson Dairy receives own farm milk at its plant for processing?
A. It does.
Q. And do you know whether Anderson Dairy was once a producer/handler?
A. I do not recall.
Q. Are you aware that Anderson Dairy's producer/handler status was withdrawn pursuant to a 15(A) proceeding by the Secretary of Agriculture?
A. I was not aware of that, but I'd heard rumors to that effect. I believe it.
Q. Do you know whether Anderson Dairy operates dairy

stores through which he distributes some of its milk?

A. I do not believe he does, except there's one small store at his plant. He may have in the past.

Q. One small -- do you know whether at one time he attempted to retain producer/handler exemption by separating the ownership of that one store from his processing plant?

A. I'm sorry, I don't know.

MR. BERDE: Okay.

THE COURT: Mr. Yale, go ahead.

EXAMINATION

BY MR. YALE:

Q. I'll take the onus of being between us and lunch, and I'm very hungry, so it's going to be very quick.

A. Good.

THE COURT: I think there might be more after you anyway. Just a wild guess, but go ahead, Mr. Yale.

BY MR. YALE:

Q. Then it'll be their problem.

The - you mentioned this 2.8 to 4 cents. That's assuming that the producer/handlers, if they become fully regulated, that there aren't changes made in terms of their utilization or increased production to reduce their utilization, right? It just is -- is if it's right now, whatever they're producing right now marketing, right?

A. That's correct.

Q. So that in response to being regulated, they may add additional production to bring their utilization down in such a way that the -- when it all nets out, it could be less?

A. It certainly can. It's not a static world.

MR. YALE: Very good. Thank you.

MR. RICCIARDI: Mr. Van Dam, a couple of questions.

THE COURT: Please identify yourself.

MR. RICCIARDI: I will, Your Honor. I apologize. Al Ricciardi on behalf of Sarah Farms.

EXAMINATION

BY MR. RICCIARDI:

Q. Because I'm not sure because I listened to what Mr. Marshall asked you, and I need to make it clear in this record. Some opinions that you gave in your testimony are your personal opinions, and some opinions are on behalf of the Northwest Dairy Association; is that your -- is that what I understand?

A. The written testimony is the opinion of Northwest Dairy Association. Some of the answers to responses would appropriately be my own opinions.

Q. How do we figure that out?

A. If you ask me each time, you know each time.

Q. Okay. So it's -- I should've asked you each time, was this a personal opinion or Northwest Dairy Association --

A. The written material is the opinion of Northwest Dairy Association.

Q. Let me ask you about that point. Did -- was there a vote by the members that authorized you to give the written testimony?

A. Not to my knowledge, but you'll have to ask somebody else. I don't believe there was a vote on it.

Q. Did you -- did -- do any kind of a survey to see whether or not your members agreed with the opinions that you were going to give?

A. I did not do that, but Mr. Marshall went to a number of meetings with his member/producers and defined what he was going to testify to.

Q. He didn't testify -- well, he has testified --

A. No, I'm sorry, but I --

Q. You've -- you're testifying.

A. What my testimony was going to be.

Q. Okay. What about, did you clear with the Tillamook County Creamery Association, the Farmers Cooperative, and the Northwest Independent Milk Producers?

A. Yes, we did.

Q. When you say they authorized you, was there a vote again regarding the --

A. I have no idea how they handled that. They gave us written authorization to speak for them on proposal one -- to speak in support, speak in terms of their affirmative support of it.

Q. And that would be this proposed change to put a $3 million ceiling in so that producer/handlers would be regulated --

A. That was the -- that is the most important part of the proposal.

Q. But you would agree with me, would be a significant policy change by the department?

A. It would be a significant change.

MR. RICCIARDI: Okay. Thanks.

THE COURT: Anyone else.

(No response)

THE COURT: You may step down.

THE WITNESS: Thank you.

THE COURT: And it's 12:33. How much time do we need for lunch? I'm willing to listen to reason. Do you want an hour and a quarter or hour and a half? Hour?

MR. UNIDENTIFIED: Hour (indiscernible)

THE COURT: Okay. Let's make it an hour and a quarter because it's in between. Let's say at a quarter -- it's 12:30. Let's say at 1:45 we'll reconvene. Okay. And once again, when we reconvene, anyone who has to testify today who is leaving town and wants to get in today, please let me know before we start the next session.

See you at 1:45.

(Off the record at 12:30 p.m. and reconvened at 1:45 p.m.)

THE COURT: Okay. We're on the record.

It's afternoon, being the afternoon session on the 18th of November, and Mr. Marshall, you can call your next witness.

MR. MARSHALL: Calling Daniel S. McBride, Your Honor.

THE COURT: Okay. Mr. McBride, if you'll please raise your right hand.

DANIEL S. McBRIDE

having been first duly sworn, was examined and testified as follows:

THE COURT: Okay. And could you state and then spell your name for the record?

THE WITNESS: My name is Daniel S. McBride, M-c-b-r-i-d-e.

EXAMINATION

BY MR. MARSHALL:

Q. Mr. McBride, you've been here the last --

THE COURT: Did you want -- you said you wanted this marked --

MR. MARSHALL: We will want his exhibit -- his testimony marked as an exhibit, Your Honor, as marked prepared -- it's headed "Prepared Testimony of Daniel S. McBride."

THE COURT: Okay. I'm going to mark that at this point as Exhibit No. 37.

(Exhibit No. 37 was marked.)

MR. MARSHALL: I've been asked to remind myself that my name is Doug Marshall, and I'm with Northwest Dairy Association. And this is marked as Exhibit what, Your Honor?

THE COURT: 37.

MR. MARSHALL: Thank you.

BY MR. MARSHALL:

Q. Mr. McBride, you've been present the last few days and in the Phoenix hearing. You've heard testimony from Mr. Van Dam as our outside consultant. Would you explain how your testimony and his interrelate?

A. Bill was brought in as basically the outside expert. I work more with the day-to-day operations with NDA, and hopefully will be able to answer some of the more specific questions.

Q. And you've testified at federal hearings before and -- have you not?

A. Yes.

Q. So people can ask you any questions that they wish beyond your statement here, if it would be helpful.

I ask and invite you to read your prepared testimony.

A. "My name is Daniel S. McBride. I'm testifying today on behalf of Northwest Dairy Association, which is usually referred to as NDA. My title is Director of Milk Pricing Programs for NDA. I am responsible for coordinating all types of matters pertaining to federal orders, and have done so since leaving the market administrator's office to join the NDA staff in 1986.

"My role at NDA includes working with other departments of our organization that deal with marketing. For purposes of this testimony, I've relied my experience working with the group that markets the raw milk to regulated plants, including those NDA subsidiary, WestFarm Foods, WFF. I also have relied on my experience working with another group within WestFarm Foods that markets milk processed at our bottling plants, including the cost accountant for that group.

"Proposal No. One. NDA is a proponent of Proposal No. One, to revise the producer/handler provision of the Pacific Northwest marketing order limiting the exemption for producer/handlers to three million pounds of bottled milk sales per month. For purpose of this hearing, I have participated in a team which developed an in-house study of historical costs and production numbers at the WestFarm Foods Medford Bottling Plant. We developed the attached chart showing the cost per gallon at the various levels of capacity.

"The study was done over a ten year period using the gallons processed and the cost associated with the plant. The Medford plant has a capacity of 12 million pounds per month, and is currently processing four to five million pounds per month, and at times in the past, the volume of that plant has been below the three million pound per month level.

"In this study, plant costs include labor and overhead at the plant. It does not include packaging, marketing, or distribution costs. Nor does it include certain costs that are retained at the corporate or divisional -- division level in our cost accounting system.

"For confidentiality reasons, WestFarm Foods prefers not to release such details as to the degree of overhead charge or capital costs. This exhibit is offered simply to show the difference in variable costs between the plant processing less than three millions pounds per month inside, compared to the larger volumes of regulated plants.

"The points of this study that are most important to our discussion are the numbers generated within WestFarm

Foods Medford plant are quite similar to those prepared by Mr. Carl Herbine and testified at the Phoenix phase of this proceeding. Like his numbers, ours clearly support a cost trend line that shows costs decrease as plant size increases. The variable cost decreases on a per-gallon basis at the Medford plant, moves from less than three million pounds -- less than three million per month plant to processing over three million per month. That decrease in variable processing costs is in excess of ten cents per gallon. A five million pounds -- at five million pounds, the variable cost decrease an additional five cents per gallon.

"A plant below three million pounds per month on this scale has a disadvantage in the cost of processing of approximately the same amount as the advantage roughly 15 cents per gallon, which producer/handler exemption allows as was developed by Mr. Van Dam's earlier testimony. I would now like to discuss the impact producer/handlers have had in the Pacific Northwest Order 124 market, on WestFarm Foods, and our customers.

"During the past five years or so, producer/handlers have been becoming more aggressive in taking additional businesses -- business away from regulated handlers, including the three bottling plants at WestFarm Foods operates in the Pacific Northwest market.

"Producers/handlers are not fully regulated. They could sell product below the equivalent federal order class prices. Interesting, they sometimes offer multi-month fixed price contracts, which is something Congressional policy does not allow regulated bottling plants to do under the forward contracting program with producers, which are permitted for other classes of milk, but not for class one.

"Of the producer/handler group, only Smith Brothers has been involved in significant school milk sales in the past, but Etteline Dairy recently has put in a half pint machine and is supplying school milk to one of their distributors. This seems to represent an expansion of the traditional market of -- for producer/handler operations.

"WestFarm Foods supplies many milk distributors with all or a portion of the dairy products. These distributors, sometimes know as jobbers are independent businesses who buy consumer package dairy products from one or more sources and distribute them to various types of customers that they serve.

"I want to describe in this testimony how competition from producer/handlers has impacted that section of our business. Before doing so, it is important to note that since the Phoenix phase of this hearing, one of the producer/handlers in the market lost his plant in a fire. I refer to Country Morning Dairy near Othello, Washington in the central part of the state. We do not know if he plans to rebuild, but for purposes of this hearing, we will continue to view that operation as a competitor.

"The following summarizes the relationship between WestFarm Foods and its major distributors. Associated Grocers, based in Seattle, Washington, is our largest distributor, a wholesale grocery warehouse with distribution in Washington and Oregon.

"The dairy program -- their dairy program is built around the sales of WestFarm Foods products, but in recent years, that program has lost approximately one million gallons per year to Mallory's Dairy on gallons of milk. This occurred from one Oregon store owner who shifted four of his stores from the full participation in the Associated Grocers Dairy Program to direct purchase of Mallory's gallons.

"Three of the stores were lost about two years ago as follows: Food 4 Less in Salem, Shop N Cart in Albany, and Shop N Cart in Lebanon. These are all in Oregon. Total of approximately 750,000 gallons per year. About six months ago, that owner purchased the Shop N Cart in Woodburn, Oregon, which cost us another 250,000 gallons per year. Previous to the purchase of the Shop N Cart in

Woodburn, it was one of our top five volume retail stores through the Associated Grocers Program at the time that we lost the store.

"Dairy Value Distributing, Mt. Vernon, Washington. This Northwestern Washington distributor purchases gallons and half gallons and half pints of school milk from Etteline Dairy, a producer/handler, and purchases most of the rest of their products from WestFarm Foods. They were a spin-off of our former WestFarm Foods distribution network and were formed in 1997 by former employees when we closed our distribution branch in Mt. Vernon. Initially, they were mostly distributors of our Dairy Gold and other brands. However, that has changed. As a direct result, they told us of their ability to get cheaper product from Etteline. We were told that had they not done so, their competitor/distributors in the area would have bought from Etteline and would've had a competitive advantage over them.

"Iverson, Mt. Vernon, Washington, based in Northwestern Washington, is a distributor. This distributor purchases gallons of -- from Country Morning in Othello, Washington, a producer/handler, which uses the Dairy-licious (phon.) brand, and their smaller items from WestFarm Foods. Iverson's purchases gallons from Etteline, but switched to the Dairy-licious. Since the Country

Morning fire, they are purchasing their gallons from WestFarm Foods.

"Meadow Sweet, Seattle, Washington. They have historically not been a major Dairy Gold distributor, but buy some from us. Their major suppliers are Smith Brothers, also a producer/handler and Etteline. They also operate in the Portland market and supply Etteline producers into that market.

"Dairy Fresh, Olympia, Washington, are a primary distributor in Southwest Washington markets, currently buys no producer/handler milk.

"Arlon Wholesale in Walla Walla, in Eastern Washington, buys from WestFarm Foods and until recently from Country Morning in Othello, the Dairy-licious brand. Since the Country Morning fire, Arlon has purchased products from Inland Northwest Dairies.

"Terry's Dairy, Colville, Washington in Northeastern Washington, buys from WestFarm Foods, and until the fire, they also purchased Dairy-licious brand from Country Morning in Othello. Since the Country Morning fire, they've been purchasing their product from Inland Northwest Dairies.

"Only two of our long time distributor remain primarily distributors of our products. Jim Emenetto (phon.) and Gary White, both in Seattle. WestFarm Foods used to supply many of the other distributors with all of their dairy products, but now we are supplying many of them with just the items they cannot purchase from others. We have lost much of the gallon and half gallon businesses to producer/handlers.

"In addition to the distributor business described above, we also face producer/handler competition for direct delivery to major retail outlets. WestFarm Foods Oregon sales people have provided me with a list of 11 retail stores supplied by Mallory's who shares the store dairy case with WestFarm Foods or with the other traditional, regulated bottlers in Oregon, Alpanrose Dairy in Portland or Umpqua Dairy in Roseburg.

"The total, annual volume of these 11 stores was estimated by our area sales manager to be 940,000 gallons per year, roughly eight million pounds a year. Again this is direct competition for the same types of accounts that we and other traditional bottlers have historically served.

"Our sales people have told me that some of the producer/handlers obtain a competitive advantage from being able to offer a less volatile price than regulated handlers whose milk costs must reflect the volatility of the class one price mover. In our region, the federal order class one price -- our prices -- in our region when the federal order class one prices are low, producer/handler wholesale price tends to be about 15 cents a gallon lower than the WestFarm Foods price, but when the class one price rise, the difference can be as much as 45 cents per gallon.

"Our sales people indicate that Etteline hardly ever raises the price to their customers. In fact, they are -- there are indications that recently they went 16 month without a price change, thereby giving their customers an assurance of being able to maintain constant gallon price for many months.

"One of the issues that is in this hearing may be how producer/handlers balance their supply. At times, NDA supplies milk to the only bottler in Alaska, Matanooska Maid (phon.) at Anchorage. Alaska is outside any federal order marketing area, and so that plant is not a regulated plant.

"However, most of the other bottled milk to Alaska is supplied by pool plants regulated under the Pacific Northwest order. We are aware at times when producer/handler milk is available, Matanooska Maid purchases raw milk from producer/handlers. In this fashion, then excess producer/handler milk can be pushed back onto the pool, in this case, NDA by backing out our normal sales to Matanooska Maid.

"As the above demonstrates, producer/handlers in the Pacific Northwest market have become strong, direct competitors against our regulated WestFarm Foods bottling operations. They have hurt us in the marketplace. We believe that the same situation was a reason for the recent demise of Vitamilk Dairy in Seattle, a small, family-owned business that bottled, we estimated, about six to eight million pounds per month.

"Like the rest of the bottlers, Vitamilk was hurt by consolidation of the retail grocery industry, losing two of their chain customers when they were acquired by larger grocery chains who have their own bottling plants. That left Vitamilk, like WestFarm Foods, with a gradually increasing dependence on individual stores, smaller chains, and independent distributors.

"As we understand the marketplace, Vitamilk had five major distributors. In three of the five cases, Etteline supplied the gallons, Brinks in Billingham, Riverside in Burlington, and Glacier in Port Angeles. In the fourth case, Wilkinson Dairy in Central Washington, Country Morning supplied them -- supplied their gallons.

"We heard many times from the owner of Vitamilk, the producer/handlers were a major issue to -- for them. We know from our own experience that this must have been true. The intent of the foregoing testimony has been to demonstrate my belief that the larger producer/handlers in the Pacific Northwest market compete successfully against regulated plants, including ours and formerly Vitamilk's. We believe each of the producer/handlers mentioned, Smith Brothers, Etteline, and Mallory's each exceeds, or at least is getting close to the three million pounds per month threshold for regulation that NDA proposed in Proposal No. One.

"They have an advantage they are using successfully and unless proposal one is adopted, they will inflict more harm on regulated handlers in the future. I should add that as a supplier of raw milk, NDA feels pressured to lower our milk costs to WestFarm Foods and other raw milk customers. Of course, NDA has a substantial investment in the four WestFarm Foods bottling plants in the Order 124 and 135 markets, and in the end, we need to ensure that they are competitive.

"While competition from producer/handlers has not currently led NDA to subsidize any of our customer plants with below-order pricing, that is the likely next step if this unfair competitive situation is not resolved, because we need class one sales to ensure that our producers can remain pooled.

"It will make sense for us to subsidize class one market in order to fend off significant competitive challenge from producer/handlers. That would, of course, be the ultimate demonstration of disorderly market conditions. We urge the secretary to adopt proposal No. One so that situation does not occur."

Q. Thank you, Mr. McBride. Your prepared testimony, which is Exhibit 37, has appended to it a last page, which is entitled -- which is a graph entitled, "Plant Processing Costs Exclusive of Packaging," and it's not identified as to which plant that is. Could you do so for us?

A. Yeah. This is the information that we obtained, the history of our WestFarm Foods Medford plant.

Q. Okay. Might it be helpful to explain where Medford is?

A. Medford is in southern Oregon.

Q. And that would be a long ways away from the Portland market, would it not?

A. Yes.

Q. And in that situation, because of its distance, it's cheaper to run a small plant than it is a large -- than to haul milk from a large plant in Portland then-

A. Yes.

Q. -- would this be accurate?

There are a number of dots on the chart. One, two, three, four, five, six, seven, eight, nine, ten dots as I count them. What does each of those dots represent?

A. Basically those were -- are cost per gallon in the ten year period that we used to determine -- to develop the chart.

Q. And I would ask you to read the -- well, before we get to that, then what is the curve that is --

A. That is the --

Q. -- lining up between the dots?

A. Okay. That is the trend line that we -- that I inserted into the chart, and again, it's, you know, it's basically just the plant costs of labor and overhead.

Q. And I'd ask you to read the note at the bottom of that, --

A. Okay.

Q. -- well, on the -- below the chart on that --

A. Okay. For --

Q. -- page of your exhibit.

A. "For confidentiality reasons, WestFarm Foods prefers not to release such details as to the degree of overhead covered or capital costs. This exhibit is offered simply to show the difference in variable costs between plant -- between a plant processing less than three million pounds per month in size compared to larger volumes of regulated plants."

Q. In your prepared testimony, you identified a number of situations and where you or WestFarm Foods either had lost business to producer/handlers or was competing head-to-head with producer/handlers. As far as you've been advised in your work with the consumer product sales people, does any of those product -- have any of those sales been lost as a result of either poor quality or lack of service?

A. Not that they had mentioned.

Q. And did they indicate their belief as to what was the reason that they had lost that business?

A. They believed it was basically due to pricing.

Q. In Mr. Van Dam's testimony, he indicated that he had been asked by several organizations to express their support for Proposal No. One. Have you been asked to do so?

A. Yes.

Q. And please do so.

A. Wilcox Dairy Farms has authorized NDA to express their support for Proposal No. One in this hearing.

MR. MARSHALL: Thank you, Dan. Mr. McBride's available for cross-examination.

THE COURT: Who has questions for Mr. McBride?

MR. UNIDENTIFIED: We do, but (indiscernible)

THE COURT: If you're ready, Mr. Ricciardi, you can go -- oh, you going to go up, too? Someone go.

MR. UNIDENTIFIED: I was (indiscernible).

EXAMINATION

BY MR. MILTNER:

Q. Mr. McBride, my name is Ryan Miltner. I represent Smith Brothers Farms, Mallory's Dairy and Etteline Dairy.

I just want to go through your testimony and clarify some questions that I have. On page one you talk about your chart that you've developed, and you state that that's based on your Medford bottling plant?

A. Yes.

Q. How many bottling plants does WestFarm Foods operate in Order 124?

A. Three.

Q. And you selected the Medford plant over the other two plants?

A. Basically because it was an HDST plant and a -- and it was also the smaller, you know, relative size to the producer/handlers.

Q. I'm not familiar with that acronym, HDST?

A. Basically high -- I forget what it is, too. High temperature (indiscernible)

MR. UNIDENTIFIED: High temperature --

MR. MILTNER: High temperature short time, --

MR. UNIDENTIFIED: -- short time.

MR. MILTNER: -- is that what I heard? Okay. Thank you.

MR. UNIDENTIFIED: You're welcome.

BY MR. MILTNER:
Q. How many pounds per month are processed at the other two plants?
A. They'll vary basically. We've got about ten million pounds in the Portland plant, maybe roughly 25 million at our Seattle plant.
Q. If you were to take the processing costs for those larger plants and plot them onto this graph, would you expect the trend line to continue sloping downward?
A. I would.
Q. Would you be willing to provide us with your costs if you have them for those two plants?
A. I don't have them.
Q. Okay. You didn't calculate them?
A. No.
Q. The chart covers a ten year period, I understand?
A. Yes.
Q. And each of the dots, each of the points you've plotted on the chart represent one of those ten years?
A. Yes.
Q. Did you take the data for the entire year and then create a monthly average, or these represent one specific month out of those years?
A. Well, we took the information for an entire year.
Q. And then averaged it?

A. And I averaged it.
Q. Okay. Can you tell us which dot represents which year?
A. Guess I could. Now, the first dot is in 2000. Second dot is '99. Third dot is 2001. Next dot is 1998. Next dot is 2003. Next dot is 2004, and let me explain. These are our fiscal years, which run basically April through March.
Q. Okay.
A. The next dot is 2002. Then 1995, 1997, and 1996.
Q. I think maybe I missed the one between '03 and '02.
A. That was '04.
Q. Okay. How old is the Medford plant?
A. It's been around a long time. I'm not sure.
Q. When was the last time you updated the equipment at the Medford plant?
A. It's been updated, I think, within this ten year period.
Q. Okay. What is the mix of products produced at the Medford plant?
A. Basically we'll do gallons and half gallons.
Q. Are there any other products produced at that plant?
A. Once in a while they may do some whipping cream

or half and half.

Q. On page two you talk about an expansion of the traditional market of producer/handler operations. How do you define the traditional market for producer/handler operations?

A. I think traditionally they, you know, they used to basically be able to supply product right off of their farm to customers, and then they started, you know, supplying maybe some small stores.

Q. So anything other than sales off the farm itself and out of small stores, you would categorize as non-traditional sales --

A. Yes.

Q. -- for producer/handler?

In the same paragraph, you talk about Etteline Dairy having installed a half pint machine?

A. Yes.

Q. Do you have any knowledge as to the reasoning behind the installation of that machine?

A. I would assume it was to be able to supply the school business.

Q. Is it your testimony -- I read that paragraph as a whole, and it seems that you're indicating they installed that machine so they could expand their market -- expand their production. Is that what you're trying to convey to the secretary?

A. Yes.

Q. Do you have any factual basis to base the -- that conclusion that there was an expansion of production associated with the installation of that machine?

A. They installed the machine. They're supplying, you know, some of the -- one of the distributors with school milk.

Q. Is it possible that the installation of that machine was the result of shifting production from one packaged product to another or one account to another?

A. I don't know.

Q. In the next paragraph of your testimony, you talk about your independent distributors. You supply milk, as I understand it, to these independent distributors, and then they find an ultimate customer to purchase the product; is that correct? Am I (indiscernible)

A. Yes.

Q. Okay. I'm kind of new at this compared to everybody else here. So sometimes I'm not right.

The prices that these independent distributors charge to stores or to schools, does WestFarm have any influence over the prices that those distributors charge?

A. What they sell -- what they charge to the -- to their customers?

Q. Yes.
A. No.
Q. I mean, presumably they mark it up and make a profit, but other than -- I mean, there's no -- you have no control over -- your mark up is going to be set at a certain percentage or must be set at a certain percentage? You have no --
A. No.
Q. You wouldn't do that; that would probably cause other problems for you, I would guess.
What percentage of your distribution is done through independent distributors?
A. That I don't know.
Q. Do you have a rough idea?
A. I don't.
Q. More than half? Less than half?
A. I don't know.
Q. Okay. More than ten percent -- I mean, any idea -- can you give us any inclination? Is it a lot or a little?
A. I really -- I don't think it's, you know -- well, you know, it's hard to say because you've got a large -- you know, you've got Associated Grocery, which is our largest.
Q. Okay.

A. So what -- how much goes to there, I'm not --
Q. Okay. I mean, if you don't know, you don't --
A. I hadn't thought about that.
Q. If you don't know, that's fine. I can't make you know.
On page three, carrying over into page four, you've given us several summaries of some of your major -- and these are all independent distributors, correct?
A. Yes.
Q. Okay. Some of the interesting -- in the Dairy Valley Distributing bullet point, you mention that Dairy Valley Distributing was a spin-off of our former WestFarm Foods distribution network. So WestFarm once had their own distributors who were not independent employees of WestFarm?
A. We had distribution centers, you know, throughout the area, and then we would distribute those product to -- directly to customers.
Q. Okay. And in 1997 or somewhere about that time, you closed down that division?
A. We were closing down, you know, some of the distribution centers and consolidating, running more of the products right from our -- from the bottling plants.
Q. Okay. And so these former employees formed Dairy Valley Distributing, and your testimony is that after they

formed this, this was a -- that a customer of Dairy Valley Distributing got cheaper product from Etteline. Was this customer a customer of WestFarm Foods in-house distributing channel?

A. No, this was a customer of Dairy Valley.

Q. So before the spin-off, they were not a customer of WestFarm Foods?

A. That I'm not sure of.

Q. Okay. Are you familiar with Steve Harper?

A. I run into him once in a while.

Q. He's an employee of WestFarm Foods?

A. Yes.

Q. Okay. He -- as I understand, he set some of the prices that are charged to independent distributors, including Dairy Valley?

A. You know, he's probably responsible for the pricing.

Q. Okay. Isn't, in fact, true that this customer you reference left Dairy Valley Distributing because the price that WestFarm charged to Dairy Valley was increased disproportionately by Mr. Harper?

A. Class one prices moved -- well, fluctuate every month, so we --

Q. But you would expect --

A. -- will have to, you know, we have to -- we will move prices with the market.

Q. Do you -- you move them with the market. So if there were later testimony that suggested that the prices charged by, or set by Mr. Harper moved in the same direction as class one prices, but disproportionately in relation to those prices, would that -- is that plausible?

A. I'd have to look at the testimony.

Q. And if that happened to a customer of an independent distributor, wouldn't it be natural for them to look to a lower cost alternative that perhaps didn't try to exploit its customer base?

A. Again, I'd have to look at the -- what information you have.

Q. Okay. Next on your list is Iverson, another independent distributor, and it says that Iverson purchased its gallons from Etteline, and then switched to Dairy-licious. Do you have any idea when those gallons were purchased from Etteline?

A. I don't know the dates, no.

Q. No. Could've been 20 years ago?

A. I think it's probably a little more recent than that.

Q. 15? I mean, at some point if it's so far back it's kind of irrelevant to the decision we're trying to make, right?

A. Right, but like I said, I'm not sure how far back.

Q. Okay. So it could've been 20 years, you just don't know?

A. I do not know.

Q. Your testimony about Dairy Fresh that Dairy Fresh currently buys no producer/handler milk; is that correct?

A. Yes.

Q. Would it surprise you if I -- if it were revealed that they bought four loads a week from Etteline Dairy?

A. Well, it would, but, I mean, I'm relying on information that I get from the -- from our sales staff, and if they're buying milk.

Q. How current is that data you received from your sales staff?

A. Within the last, you know, couple months, --

Q. So they had --

A. -- since we started preparing for the --

Q. I didn't mean to interrupt you. I'm sorry

A. Since we've been preparing for the -- this hearing.

Q. So if they had been buying milk from Etteline Dairy for two and a half years, that would indicate that the data provided to you by your sales staff is perhaps inaccurate?

A. That would indicate that they weren't aware of the sales.

Q. But you're relied on their data in your testimony, right?

A. Yes.

Q. Is the information provided on Meadow Sweet also provided by your sales staff?

A. Yes.

Q. And they've informed you that Etteline products were being sold into the Portland market by Meadow Sweet?

A. Yes, they did.

Q. Did you verify that in any way?

A. Did I drive to Portland and check about the stores?

Q. I didn't ask you if you drove, I asked if you verified it.

A. No.

Q. So that could be wrong, you don't know?

A. Could be, I don't.

Q. So you're not making a representation that this is accurate?

A. I'm -- you know, presenting information that's given to me from our sales people.

Q. Okay.

A. I mean, if your clients can get up here and, you

know, tell us something different, then fine.
Q. They might.
On page four, this is the paragraph that begins with, "In addition to the distributor business." Your sales people again provided you a list of 11 stores supplied by Mallory's. You're making any testimony that there was a market that those stores somehow had displaced WestFarm products, that you lost WestFarm sales you once had in those 11 stores?
A. WestFarm and other handlers down there.
Q. Okay. Mallory entered those stores?
A. That was probably, you know, a year, year and a half ago.
Q. Year and a half ago?
A. Yeah, that's what I'm trying to remember what date.
Q. Do you know the name of those 11 stores?
A. I don't have a list up here. I know a lot of them were the -- were part of the Thriftway chains.
Q. Thriftway. Okay. It wasn't the Roth's chain? Is that the Roth's chain?
A. Well, I mean, it could be Roth's Thriftway.
Q. Okay. So if, in fact, Mallory's had been supplying those stores for the better part of 40 years, that would be -- that would not be consistent with the

information your sales staff provided you?

A. They could be providing them with a portion of their -- with their products, but, you know, I think here that basically it was a second label that went into those stores.

Q. Okay. In the following paragraph, you talk about indications that Etteline Dairy hardly ever raises the price to their customers. What indications did you have?

A. Again, relying on the information from the sales people --

Q. Same staff that's given you the other information we've talked about?

A. Yeah, there's -- I mean, there's a number of people that had, you know, collaborated on this.

Q. What are the -- which 16 months did they not move their prices? What period does that cover?

A. I think it's pretty -- the most recent period.

Q. The next paragraph, you talk about supplying milk to Matanooska Maid in Anchorage.

A. Yes.

Q. How often -- what's the frequency with which you supply that dairy?

A. During this time of year, you know, normal conditions we'd be supplying them with milk every week.

Q. How many months out of the year?

A. Seven or eight.
Q. Are those the normal sales to Matanooska you talk about later in your paragraph?
A. Yes.
Q. Okay. What is the price you charge Matanooska for the milk you supply?
A. My -- I don't have the prices, and again, that would be proprietary information anyway.
Q. Could be less than class price?
A. Doubt it.
Q. Could be much more than class price?
A. Possible.
Q. Could be double class price?
A. Doubt it.
Q. Doubt it. Let's say hypothetically, you did charge them twice class price, and there were another supplier of milk that would charge them one and a half times class price. If you were Matanooska, what would you do?
A. Hypothetically, why would they ever want to buy milk (indiscernible)
Q. Who else besides producer/handlers that you say supply milk to Matanooska and WestFarm Foods or NDA, who else are you aware of that regularly supplies milk to Alaska?

A. Well, we know Safeway has stores up there, and I believe Alford Myers (phon.) has some stores that --

Q. Who supplies to Matanooska?

A. That's bulk milk that they receive either from us or from producer/handlers.

Q. So if not for the producer/handlers, you would have a, I don't want to say monopoly. Maybe that is the right word. You would have a -- the sole ability to supply their plant, right?

A. They could go -- I mean, they could get the milk out of a Portland plant.

Q. Okay.

A. You know, someplace else, you know, other handlers.

Q. But absent a competitive environment, you could pretty well dictate a price for them?

A. We consider pricing. If they can get it cheaper, you know, I'm sure that's what they would.

Q. They'd probably do that.

On page five, there's some more talk about the Vitamilk, and you do talk about the -- some of their other problems -- some of the problems they have losing their large part of their market, but the -- first -- I guess, the second full paragraph talks about producer/handlers being a reason for the recent demise. Are you -- it's your

testimony that that is the primary reason for their demise?
A. It's a reason. I don't think I said primary.
Q. How did you obtain your information about Vitamilk's major distributors?
A. I had talked to Darryl Vander Pol.
Q. Okay. Are Brink in Billingham and Dairy Distributing in Billingham similar operations?
A. Similar in?
Q. I mean, are they -- I should say, are they distinct operations?
A. I believe they're independent distributors.
Q. Okay. Is it possible that Vitamilk didn't supply Brink, but they supplied Dairy Distributing?
A. It's possible.
Q. Don't know?
A. Don't know.
Q. Do you know how long Etteline has been supplying gallons to Riverside in Burlington?
A. No.
Q. Would it surprise you if that were 15 years?
A. I said I don't know.
Q. When Mr. Yale examined Mr. Van Dam, they talked about the net impact to producers in the -- their milk checks if these regulations were to be approved by the secretary. And somewhere between 2.8 and 4 cents per

hundredweight was kind of settled on, is what the impact would be on a per hundredweight basis. You're familiar -- you heard that testimony?

A. Yes, I did.

Q. Okay. One of the benefits you have as a coop is the ability to reblend expenses and potential loses against the income the coop receives, correct?

A. As a coop, yes, we have that ability.

Q. And you can reduce from the blend price received by your members in assessment to offset those expenses and loses, correct?

A. Correct.

Q. Is it true that up through September of this year that your coop had reblended ten cents per hundredweight against your producers as a result of your current labor troubles?

A. Want to say that again?

Q. Sure. Have you reblended a ten cent assessment against your producers?

A. For what period?

Q. I believe it ended this September, but that could be wrong. Maybe it's ongoing.

A. We did have a, you know, a work stoppage accrual that was assessed to the producers.

Q. And that cost your producers ten cents a hundredweight?

A. For a four month period, yes.

Q. What other assessments -- types of assessments might you make in the future against your producer's blend prices?

A. That's up to the board.

Q. Are there any assessments currently?

A. We have a nine and a half cent operating fund --

Q. Okay.

A. -- that is -- you know, that is assessed to all producers to offset the cost of the coop.

Q. Anything else?

A. They are being assessed the five cent CWTS assessment.

Q. Okay. Anything else?

A. Not that I can -- you know, they're going to be assessed, you know, if there's a quality assessment.

Q. How about a make allowance adjustment?

A. Is that October or November?

Q. I don't know. It's your letter. "Effective with" -- October, and this is a letter from Mr. Marshall. "Effective with the October milk proceeds, we will implement a five cent per hundredweight, FMMA will make allowance adjustment (phon.)."

A. Okay. Yeah, that would be effective with this check that's going out --

Q. Okay.

A. -- this week.

Q. And again, that impacts the returns received by your producers along with your work stoppage accrual, and any other assessments you make for losses your coop may incur, --

A. Is there --

Q. -- right?

A. -- a question there?

Q. I think I phrased it as a question. Those are losses against your producers, correct?

A. Yes.

MR. MILTNER: Just one moment, Your Honor.

(Pause)

MR. MILTNER: Your Honor, I apologize. I probably should have done this a few minutes ago, but I'd like to have marked as an exhibit a letter dated September 16th, 2003, on Northwest Dairy Association letterhead to NDA member producers in Whatcom County.

THE COURT: Okay. Do you have copies for the --

MR. MILTNER: I do.

THE COURT: That would be marked as Exhibit 38.

(Exhibit No. 38 was marked.)

THE COURT: Is this the document that you were just asking the questions on?

MR. MILTNER: Yes, it is.

THE COURT: Are there other people who need copies? I'm just curious. Should -- do you --

MR. MILTNER: We'll have to get some additional copies.

THE COURT: I mean, should we take a few minutes' Xerox break? I don't know --

MR. UNIDENTIFIED: -- won't take long to make --

MR. MILTNER: Sure. We'll get copies right away. If we want to take five minutes, we can get copies made.

THE COURT: All right. Because I don't know how many people would want them to follow along. So let's take five minutes while you make -- get some copies made.

(Off the record and reconvened.)

THE COURT: Okay. We're back on the record.

Go ahead, Mr. Miltner. We all have Exhibit -- what's been marked as Exhibit 38 now.

MR. MILTNER: 38 and if anybody does not have copies, there are additional copies on the back table.

BY MR. MILTNER:

Q. I think I just have one more question to follow up on your testimony, that there were 11 stores in the Portland area supplied by Mallory's Dairy, and you weren't sure if -- the identity of those stores. Do you know if those stores, the ones you're referring to, are still supplied by Mallory's Dairy?

A. I assume they are.

Q. Okay. But you're not -- you don't have knowledge definitively yes or no?

A. As of the first of the month, no, I don't know if they --

MR. MILTNER: Okay. Your Honor, I think we've identified No. 38. I'd like to move to have it admitted at this time.

THE COURT: Is there any objection?

(No response)

THE COURT: Exhibit 38 will be admitted into evidence.

(Exhibit No. 38 was received.)

MR. MILTNER: We don't have any questions -- any additional questions right now, Your Honor.

THE COURT: Okay.

EXAMINATION

BY MR. RICCIARDI:

Q. Al Ricciardi for Sarah Farms.

Mr. McBride, because we ran into this issue with Mr. Van Dam, let me clarify your testimony. Exhibit 37, your written testimony is on behalf of Northwest Dairy Association, correct?

A. Yes.

Q. There are no individual opinions in here?

A. No, not in the written testimony.

Q. Let me make sure of that. If you'll flip over to page five, that would be the fifth paragraph, beginning, "The intent of the foregoing."

Do you see that?

A. Okay.

Q. "The intent of the foregoing testimony has been to demonstrate my belief," et cetera. That should be our belief or the belief of Northwest Dairy Association?

A. Should be -- probably our belief.

Q. Okay. You also indicated during the course of your testimony that you had been authorized, I guess, is the best word that we're going to use, to speak on behalf of Wilcox Dairy in support of the proposal?

A. Yes.

Q. Okay. Mr. Wilcox is here in the room today, correct?

A. Yes, sir.

Q. Wilcox Dairy is a joint venture with DFA, correct?

A. That's my understanding.

Q. Okay. And Wilcox Dairy has a current fixed term agreement with Cosco to supply milk to Cosco in the

northwest, right?
A. I don't know.
Q. You don't have any information as to that?
A. I do not.
Q. Perhaps Mr. Wilcox does.
When you worked for the market administrator's office prior to joining the NDA, were you required to determine whether or not a producer/handler met the requirements to be a PD?
A. That was not part of my --
Q. That wasn't your responsibility?
A. That wasn't, no.
Q. Okay. Sometimes when customers are trying to get a better price, they might exaggerate the truth with regard to the price they had been offered by other potential suppliers of milk, correct?
A. Yes.
Q. So they may say that they were going to get a price from someone, whether a regulated handler or producer/handler, and you don't know whether or not they actually got that particular price that particular month, correct?
A. Right.
Q. As I understand it, there have been -- there are some losses of customers of which you complain in your

testimony, correct?

A. Yes.

Q. Okay. Customers can be lost for a variety of reasons. For example, if you were to supply leakers to the customer, the customer might not want to do business any longer with you because there's a product issue, correct?

A. Okay.

Q. Is that a yes?

A. Yes.

Q. Okay. And there might be some other service issues in terms of the type of service you were providing or not providing to a customer, for which they might decide either to do business or not to do business with you, correct?

A. There could be a lot of factors.

Q. Price might be one of them, all of these other issues might be another?

A. Yes.

Q. And quite frankly, unless you go ahead and get a lie detector test from a customer, you're not going to know exactly why they decided not to use you any more. It may be price, it may be other things, correct?

A. It could be a number of things.

Q. Now, as I understand it, NDA has not subsidized any of its customer plants with below order pricing as of this date, correct?

A. Correct.

Q. And in 1999, they didn't do that either, that is, subsidize customer plants with below order pricing, correct?

A. Correct.

Q. And in 2000 you didn't do that?

A. Correct.

Q. Or in 2001, correct?

A. Correct.

Q. And 2002, correct?

A. Correct.

Q. And up till today when we're sitting here at this hearing, that has not happened, correct?

A. Correct.

Q. I think you were asked this question, and let me see if I can get some clarification on it. The Medford plant for which you attached a graph to Exhibit 37, that is how old, 25 years old, 30 years old, 10 years old?

A. It's old. I mean, I'm not sure when it was -- we acquired it in a merger with Mayflower Farms in 1981.

Q. And it had existed for how long when you acquired it?

A. That I'm not --

Q. Okay. So it's at least existing since 1981 and probably another ten years beyond that?

A. At least before that. I don't -- I'm not sure.

Q. Now, you'd agree with me that the age of a bottling or processing plant as it gets older, it has the potential for increasing costs because of the fact that you have break downs, and you have to end up repairing them, correct?

A. Correct.

Q. And the better idea, of course, is if you have the ability to do it, the capital to do it, is to build a new processing or bottling plant, right?

A. Or just update the equipment.

Q. Okay. You told, I think, in response to Mr. Miltner's question, that this Medford plant basically produces gallons and half gallons, correct?

A. Yes.

Q. How many skews (phon.)?

A. That I don't know. I don't know.

Q. Do you know why the decision was made at Medford to produce basically gallons and half gallons?

A. No.

Q. Isn't it true that the more that you reduce the number of skews, or products that you are bottling, the more efficient that the plant can be?

A. The plant will be efficient based on the volume of milk that you can run through it.

Q. That's one thing, but also the type of product that you're sending out the door, too, can also increase the efficiencies, right?

A. Yes.

Q. Okay. So if you are only doing one product or one skew, or two skews, then the potential for increasing the efficiencies, and therefore decreasing the cost to that plant is there, correct?

A. You would have some efficiencies.

Q. And efficiencies ultimately go to the bottom line for a processor, right?

A. Yes.

Q. So you can then make a decision whether or not, once you get those efficiencies, to keep that in terms of profit, or to go ahead and distribute it effectively by giving a lower cost to the customer, correct?

A. The idea with this chart was to sort of see the impact of, you know, volume running through the plant, how it does lower the per gallon cost. That was the intent of the --

Q. I wasn't --

A. -- study on the chart.

Q. I wasn't asking you about the chart. My question was in general. The fact is that once you increase the efficiencies and it goes to the bottom line, a decision can be reached, keep it as profit or pass it on as a lower cost to the customer, correct?

A. Yes.

Q. This particular chart, this was prepared for purposes of this hearing, correct?

A. Yes.

Q. This is not a document that you keep in the normal course of your business, --

A. No,

Q. -- correct? And --

A. -- not that I --

Q. I didn't hear you.

A. Not that I keep.

Q. Okay. That anybody keeps?

A. I don't know what they.

Q. And you say for confidentiality reasons, you're not giving us other details like the overhead covered or capital costs so that we can test the information on hour chart, correct?

A. Correct.

Q. And by the way, just so I am clear, you do not have any information at all with regard to Sarah Farms, correct?

A. Correct.

Q. You do not have any information at all that you are trying to present with regard to Order No. 131, correct?
A. Yes.
Q. Does NDA have its own stores to market its milk?
A. No.
Q. Why not?
A. We were -- we're a, you know, producer coop. We pick up the milk, we process the milk, and sell to distributors.
Q. So you made a decision as a business plan that you weren't going to, for example, expend the capital to go and produce retail outlets that you can sell your milk to?
A. That decision was made, yes.
Q. Okay. Safeway, on the other hand, has its own retail outlets to sell its milk, correct?
A. Yes.
Q. And producer/handlers have not only the dairy, but they also have a production plant to process their milk, correct?
A. Correct.
Q. And the producer/handler made a decision whether or not to expend the capital to have its own dairies and have its processing plant, correct?
A. Correct.

Q. Do you believe that Safeway has an unfair advantage over your coop because it has retail locations?
A. They have an advantage.
Q. They have an advantage over you because they already have their own captured customers that have to buy its milk?
A. Correct.
Q. Whereas your coop doesn't?
A. We sell to distributors.
Q. And, in fact, you don't know whether Safeway sells its milk to its own customers for a different price than it may to outside customers, assuming it has those?
A. I do not know that.
Q. Okay. A couple of other things. Exhibit 38, do you have that in front of you?
A. Yes, sir.
Q. Okay. In the middle part of the second paragraph where it talks about the management report of July's dairy producer newsletter.
Do you see that?
A. Yes.
Q. NDA is simply moving more milk more miles. "This costs money, and we can no longer afford to subsidize haul rates as we have done in the past." I read that correctly?
A. Yes.

Q. NDA, if it, in fact, is transporting milk over more miles, has more costs associated with the transportation, correct?

A. Yes.

Q. Okay. And what it's doing in this letter is passing on that additional cost to its members, correct?

A. Yes.

Q. Now, if a producer/handler had additional costs such as in transportation from the dairy to the processing plant, it can't pass on those costs to members because it doesn't have any. It absorbs those costs itself, correct?

A. Or passes it along in their price to the products.

Q. They may, in fact, pass it along, and then as we talked about before, in the price of its product, but otherwise, they have to deal with that particular cost, correct?

A. It's a cost, yes.

Q. Yeah. And they'd have to deal with their own balancing costs and other costs associated with the production of milk, correct?

A. Yes.

Q. I mean, they deal with it as producer/handlers literally from cradle to grave in terms of the production of that gallon of milk, correct?

A. Correct.
Q. Nothing further.
Sorry, I do have a couple of questions.
A. So close.
Q. You were -- you could almost taste it.
How many class one sales --
MR. UNIDENTIFIED: How much.

EXAMINATION

BY MR. RICCIARDI:
Q. How much -- sorry, I can't read any more.
How much in class one sales has NDA or WestFarm Foods lost within the last ten years?
A. Last ten years?
Q. Yes, to producer/handlers.
A. Well, I can, you know, tell you here in the last couple of years when we've lost the 940 or the eight million pounds to the -- that Mallory's, you know, is now supplying in Oregon. We've lost some sales of gallons and half gallons that we were historically supplying to distributors, but how much we've lost in the last, you know, ten years, you know, I don't have that number at hand.
Q. Five years?
A. I can -- alls I have is basically right here that's in the testimony.

Q. All right. How many sales -- class one sales -- how much, excuse me, in class one sales has NDA or WestFarm Foods lost to regulated handlers?

A. I don't have that number.

Q. But you have lost sales to regulated handlers, correct?

A. The customers will, you know, move from handler to handler. It's also why you lose some through consolidations.

Q. You lose some through consolidation. You lose a customer, you gain a customer. That's the -- that is the nature of the milk business, correct?

A. Yes.

MR. RICCIARDI: Now I think nothing further.

THE COURT: Did you have questions, Mr. Yale?

MR. YALE: Just ones that Mr. McBride was told that he was going to answer.

THE WITNESS: Yes, no, maybe, proprietary and 60 percent.

EXAMINATION

BY MR. YALE:

Q. Let me get the questions, but it is (indiscernible)

I wanted you to think you were off the hook.

Benjamin F. Yale (indiscernible)

THE COURT: -- identify yourself.

BY MR. YALE:

Q. Yeah. Benjamin F. Yale on behalf of Smith Brothers, Etteline and Mallory's.

The -- there was a question raised, and Ryan -- Mr. Miltner has taken care of a few of them, but I want to talk a minute because of your knowledge of the sales. First off, have you done any analysis of the trends of the types of customers in the Northwest marketing area?

A. I have not.

Q. Do you have any sense of whether there's a movement to the larger discount, big box type sales as opposed to the traditional grocery stores?

A. You've seen consolidations within the industry. You've also seen the increased, you know, warehouse stores.

Q. Does WestFarm sell to any of the -- I don't need the specific ones, but let me give a group, the Coscos, the Sams', the Wal-Marts. Are those customers of WestFarm?

A. We may have, you know, some products in there. I don't think we're, you know, big in any of those three. I mean, I don't think it's the fluid products.

Q. As I was reading through your testimony, I got this sense that you still rely an awful lot on jobbers?

A. On -- yes.

Q. And the role of the -- what's the role of the jobber in this market?

A. Well, we will, you know, we will supply them with product which they can go out and sell, they -- you know, to the ultimate customer.

Q. Now, is this a situation where the person acts as a salesperson, and you deliver it on a WestFarm truck, or do they pick it up in their own trucks and deliver it?

A. I think it's probably a combination of both.

Q. Okay. Are you familiar with the retail marketing of milk in the rest of the country?

A. No.

Q. So you don't know whether that's a normal or an unusual practice in today's retail market system?

A. I do not.

Q. Now, you mention in page two this thing, "Interestingly they sometimes offer multi-month fixed price contracts, which is something Congressional policy does not allow regulated bottling plants to do with producers." I want to explore that subject, because I think this is -- I found this sentence a little confusing based on my understanding of what the law was. Okay.

A. Okay.

Q. Now, first off, from a standpoint of a milk plant, WestFarm as a plant, you have the right to sell milk to any customer you want any price you want, right?

A. We sell milk to a --

Q. Packaged milk. As WestFarm as a plant, can sell in retail or wholesale to anybody it wanted, any price that you would deem prudent for your business, right? There's no minimum prices on the packaged milk?

A. We have -- you're saying the product -- the finished product that we sell to customers --

Q. Right. Put it in a gallon, you got a gallon, and --

A. Right.

Q. -- you want to sell it. There's no minimum price that you have to sell that for, right, from a legal standpoint, a regulatory --

A. No, we could give it away.

Q. Right. Or sell it for whatever price you can get, right, but it's not set by what the government -- or, there's no government price on regulated milk -- or on packaged milk, right?

A. The federal orders basically deal with the, you know, the cost of the milk.

Q. Right, the raw milk?

A. Right, they do not deal with retail prices.

Q. Okay. So there is nothing to prohibit WestFarm from selling packaged milk to any customer at a flat price for more than one month, right?

A. With this portion of the testimony, it's referring to, was the ability to go out and forward contract, you know, prices to a customer for a -- an extended period of time like we can do in other classes of product. I mean, that's what we're referring to --

Q. Well, I understand. We're going to get -- I appreciate that, because that's where I want to come to, but I want to -- there's something I want to flush on it. I want to make sure that I understand that right now there's nothing that keeps you regulatorily from selling it -- packaged milk for multi-months at a fixed price?

A. Okay.

Q. Am I right on that?

A. Well, I mean, --

Q. Now, in -- are you familiar with the school business in Washington State?

A. Not really. I don't -- we do not supply, you know, I don't even know if we any school business currently.

Q. Do you have half pint bottling capacity at your plants?

A. We do have that in our Seattle plant.

Q. And where does that get sold to?

A. I'm not sure what the, you know. I mean, there are some that, you know, half pints that are sold, you know, sold in the stores.

Q. So you don't know what the long-time tradition was in the Washington market for schools and negotiating prices, right?

A. I do not.

Q. So if the -- prior to the last couple of years that the testimony establishes from other sources, that schools routinely wanted flat pricing for the full year from regulated 7A plants and producer/handlers alike, you have no reason to disbelieve that, right?

A. If others can show it, that's what it is. Sure.

Q. Okay. Now, you've been in the dairy industry how many years in one form or -- one position or another?

A. Long time.

Q. Let's not match years, but I mean, it's been a while, right? So you've seen a lot of ups and downs in the prices, right?

A. Yes.

Q. All right. So one of the dangers in -- coming back to this forward contracting, one of the dangers in flat pricing from a plant standpoint is that you have no way necessarily when you've asked some questions, but to offset your risk on the raw product side, right, because you don't know what those prices are going to be for six months or twelve months out, right?

A. Correct.

Q. Okay. And when a producer/handler enters into such a relationship, they don't know that either, do they? They don't know what the costs are for the next twelve months.

A. They may have an idea what the cost of production is.

Q. Okay. But -- because that's really what their cost is for their milk, right?

A. That would be, you know, a big portion of it.

Q. Right. So -- but they don't know -- so when they -- when you say in here that it could get as much as 45 cents, could be from a standpoint, not that they ever intended to sell it for 45 cents less. They had not estimate, they did not believe the price would ever get that high in class one. They just -- it just happened; isn't that possible?

A. The possibility is that, you know, the class one prices are very volatile and will fluctuate quite a bit in a short period of time, and if they hold their prices and the class one price is, you know, is increasing, that, you know, that difference could get to that level.

Q. Now, coming back to this forward contracting, does WestFarm forward contract on its other classes of milk with its producers; does it offer that?

A. We offer a forward contracting program with the producers.

Q. All right. And you have a -- the pool of milk that's more than just class one, right, that your -- WestFarm, or that Dairy Gold sells or NDA sells to not just NDA -- or to WestFarm, but to other plants?

A. Yes.

Q. So you could internally use the sale of that fixed price of that class three and four to protect as a price risk the forward contracting of your class one milk, right?

A. We can use that to protect the forward contracting of the -- that we have for the producer program.

Q. And one of the problems is with the higher of, it's pretty difficult to really protect a class one anyhow, right?

A. It can. It can. That makes it more challenging.

Q. Now, I want to just to clarify some questions here. You talk about associated grocers. In these sales, and I kind of want to get this so we're looking at apples and apples type of deal, or at least Mackintoshes. What's the best Washington apple up here? I know you guys got a -- what's --

A. They're all good.

Q. They're all good. Okay.
So Washington apples and Washington apples. For example you say that you'd lost approximately one million gallons per year to Mallory's. I mean, one million, that's a big number, right?
A. Yes.
Q. But in terms of a weekly, how many loads of milk is that per week?
MR. UNIDENTIFIED: Objection, Mr. McBride (indiscernible) loads or truck loads (indiscernible)
MR. YALE: I didn't say that -- Your Honor, I didn't say that. I'm --
THE COURT: He can answer the question if he knows the answer.
THE WITNESS: I don't know. I deal in hundredweights, and I don't know how much --
BY MR. YALE:
Q. Did you see the testimony of Elvin Hollon that said there's 4,500 -- approximately 4,500 gallons of milk per trailer load?
A. I saw his testimony.
Q. But you don't remember seeing that?
A. You know, I don't remember what the exact number was. I mean, that certainly --
Q. And that that was approximately divided by 50,000

(phon.). I mean, isn't this really down to about two trailer loads of milk a week?

A. I don't know if that's what it works out to, it's.

Q. Or the one down here where it talked about -- or maybe as much as four, but the one down here, the one load, or the 250,000 gallons per year, which was lost to a Shop N Cart is basically, you know, a load of milk a week.

A. Okay.

Q. I mean, even if you divide it by a tanker load, 50,000 gallons, that's pretty standard, right, 50,000, isn't that kind of a benchmark number that's used to determine size -- the number of loads of milk is by 50,000?

A. You know, that's --

Q. Huh?

A. Well, we have 70,000 pound.

Q. You got to make the math difficult, don't you?

A. I do.

Q. Okay. So it's even fewer truck loads?

A. Well, --

Q. So it's about a truck load a week of milk, right?

A. If that's what it works out to. I mean, that's.

Q. Is that a lot of volume, though, when you think of it in terms of the total plan?

A. You know, the issue here is not necessarily the number of loads or the cost of, you know, service charges or anything else. I mean, you know, there's just -- it's lack of uniform pricing, you know, that can lead to the disorderly marketing because, you know, we're competing for class one sales.

Q. Right.

A. You know, and I've got to have the class one sales so that I can qualify, you know, the milk to be able to pool it. I mean, and that's, I mean, all these other costs and services and everything, that's fine, but you know, we're coming down to basically, you know, it's just the lack of uniform pricing, and the fact that these producer/handlers -- I mean, yeah, they're good business men. They're doing a good job. We -- but, you know, they're becoming more aggressive, and they're taking those sales away, which is making it more difficult to be able to pool, or it could make it more difficult to pool all the milk.

Q. Right, but in the exhibits that -- and I identified some with Mr. Van Dam that talks about total class one sales of producer/handlers indicates that those have stabilized and gone down the last couple of years in total.

A. Okay.

Q. So although you have some sales here, you don't talk about the sales that you lost, or your distributors gained from Etteline or Mallory's or Smith Farms, do you?

A. Well, you know, we -- there's been a lot of movements within the industry. I mean, yeah, except customers are, you know, they're going to come, and they're going to go, but you know, they -- the issue is that we have lost milk to other, you know, to the producer/distributors, which is taking, you know, our ability to be able to, you know, could cause us, you know, to be able to pool all of the milk, you know, from that base.

Q. But isn't it true, Mr. McBride, that the total universe or the volume of milk that is represented by the type of business that distributors and jobbers and the smaller chains and stores have, that that amount of volume of milk in the Northwest has been declining as a percentage of the total class one sales in the market?

A. Total class one sales or total sales?

Q. Total class one sales in the market.

A. Our class one sales have basically been relatively flat.

Q. Right. Right, as a percentage, that the percentage representative by the volume of milk that is sold through these traditional chains that you're mentioning in this thing, the jobbers, the distributors, the small chains, the schools, that percentage of the market as a -- of the total class one has been declining, has it not?

A. Yes.

Q. All right. And that has been the traditional area where the producer/handlers have been, right, in that market?

A. Well, I'm not sure if serving the schools has been a traditional, you know, market for the producer/handlers or not. They've been -- you know, I think -- like I said earlier, their traditional market, I think's been, you know, the smaller stores, you know, in a -- basically a smaller location, you know, around where they're processing facilities are.

Q. And these are the types of stores that Elvin Hollon testified that represented the bottom 25 percent or the bottom quartile (phon.) of class one outlets in the market, right, --

A. Okay.

Q. -- national market?

A. Okay.

MR. UNIDENTIFIED: Your Honor, just want to object because that is not what Mr. Hollon testified to at all.

THE COURT: He can answer the question, and you can clarify it later on. I mean, I --

MR. UNIDENTIFIED: Well, it was Mr. Yale's statement, not Mr. McBride's. That's why I --

THE COURT: Well, I don't remember what Mr. Hollon testified to --

MR. UNIDENTIFIED: It's stating something not of record or incorrectly characterizing the record in a question --

THE COURT: Why don't you state the question without mentioning Mr. Hollon, just to make that clear?

MR. YALE: We'll just move on with that. I mean, I -- we'll do an indirect, because it's in his record. It's in his testimony, but.

BY MR. YALE:

Q. But again, back to the smaller -- isn't really what's going on here, Mr. McBride, is that the universe in which WestFarm finds itself, having to have sales is growing smaller because it's not competing effectively with the larger things, such as Wilcox is with the Coscos and the Big Box and the Safeways and the Krogers? And it's now competing against the PDs and the other smaller regulated handlers because that's all that's left?

A. Well, with -- like I said earlier, with market consolidation with the warehouse stores, I mean, there -- you're seeing more and more of those sales go there, and

there's -- you know, there are fewer customers out there.
Q. And the effect of adoption of your proposal is basically for the secretary to say, this universe of stores belongs to the Westfarm, but the PDs are not allowed to be there?
A. I don't think so. I mean, again, the, you know, the reason for this hearing is lack of uniform pricing that's out there that the regulated plants have to pay and that the, you know, producer/handlers are, you know, are exempt from, and you know, they have becoming (sic) a bigger and bigger portion, you know, of the market.
Q. And I -- and that market -- and I think you identified on page five of your statement that that left Vitamilk, like Westfarm, with a gradually increasing dependence on individual stores, smaller chains, and independent distributors, right?
A. Correct.
Q. Okay. Now, bottom of page five, you have a -- or near the bottom, you have this statement that says, "While competition from producer/handler has not currently led in an NDA to subsidize any of our customer plants with below-order pricing." So at this point, that's not going on, right?
A. Correct.
Q. All right. But as a cooperative, you have the

ability -- I think there was some testimony, or somewhat doing it because of this crisis that you're dealing with right now with -- at Westfarm, have the ability to reblend from your producers -- your entire producer base to subsidize any of your plants, whether they're bottling or cheese plants, right?

A. Being a coop, we have the ability.

Q. And you have then that ability to use that large base of volume of milk, and that ability to reblend, to modify or to subsidize and sell prices to customers at below class one prices, right? Under current regulations, you have that authority, right?

A. The authority may be there.

Q. But you're not doing that now?

A. No, sir.

Q. And I just want to make sure. You've done those study of an operation of a producer/handler from the production of the milk through the sales in terms of their efficiencies and their costs and operational aspects or anything, right? That's not part of your testimony?

A. No.

Q. Okay. And you have no expertise in that, right?

A. No.

Q. As Westfarm, have you run into any competitive problems with someone like Safeway that has multi-state and multi-order plants that you compete against in your market, with some of your customers, do you know?

A. That I do not know.

Q. Your plants, what's the -- how many employees do you have in your plants, your operation, your plant operations? Do you have more than 500?

A. Yes, we do.

Q. Significantly more than 500?

A. Well, given today's labor situation, I'm not sure.

Q. Fewer today than maybe you had a few times, but I wasn't trying to go there. I was just --

A. We have more than 500.

Q. Okay. And that's at the plant level, right? That -- of course, you don't have any farms, so that's.

I want to come back now. For -- first page, "Confidentiality, Westfarm prefers not to release such details as the degree of overhead and covered capital costs," right?

A. Yes.

Q. Now -- and I respect the issue of the confidentiality, but if plant operations have become an issue in this case, I mean, you've had Carl Herbine testify in terms of plant costs, theoretically, based on a national database, and the implication, and I understand that NDA is relying upon Mr. Herbine's testimony to argue that the producer/handlers have some cost advantage, basically, based on the size of their plants, right?

A. The testimony -- what I've done, I think, what Mr. Herbine did was -- shows that plants at higher, you know, volumes will have a lower per gallon cost.

Q. All right. And I think nobody --

A. And that's all that this -- that I was trying to show there.

Q. -- that's all you wanted to say, but you're not going to argue whether his plant costs are too higher or too lower, right?

A. No. I mean, he came at that from a, you know, a different approach. He had a fully loaded situation. I'm just doing bare bones, just labor and overhead on our -- on this analysis.

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

THE COURT: Any questions from the (indiscernible)

Go ahead. Don't forget to identify yourself.

EXAMINATION

BY MR. ROWER:

Q. Jack Rower, USDA.

Mr. McBride, is there currently an over-order premium in Order 124?

A. We have a small service charge, over-order premium.

Q. Could you tell me what it is?

A. It varies.

Q. Okay.

A. Basically it'll go from, you know, 45, you know, 40 cents down to 30 cents.

MR. ROWER: Thank you. That's all.

THE COURT: Anyone else over there? Okay.

Mr. Berde, go right ahead.

EXAMINATION

BY MR. BERDE:

Q. Sydney Berde.

Dan, are you order of any authority that would permit a cooperative operating under federal order system to sell milk to handlers at below order prices as was suggested by -- in Mr. Yale's question?

A. I'm not aware of any authority.

Q. Directing your attention to Exhibit 38, which describes certain deductions from October pool -- the October blend that you were questioned about.

A. Yes.

Q. Your cooperative receives the blend price from the order, does it not?

A. Correct.

Q. And that blend price, according to testimony previously offered and received in this proceeding, indicated that by reason of the presence of producer/handlers in the market, the blend part price (phon.) was reduced by somewhere around 2.8 to 4 cents per hundredweight. Do you recall that?

A. Yes.

Q. And if that blend price had not been reduced, it would've been increased by the amount of that reduction, wouldn't it, by that 2.8 to 4 cents per hundredweight?

A. It -- yes.

Q. So then that -- the net affect of reducing the producer's pay price by reason of the deductions that are described in your letter is that that net result would've been higher by 2.8 to 4 cents per hundredweight after the deductions, wouldn't it?

A. If the producer/handler milk was part of the uniform pricing of the orders, you know, the blend price would've increased by, you know -- to the, you know -- the price to the producers would've been increased by 2.8 to 4 cents, yes.

Q. And accordingly their price would've been increased by that amount after the deductions?

A. Correct.

MR. BERDE: Thank you.

THE COURT: Any further questions from the proponents' side now?

Go ahead, Mr. Beshore.

EXAMINATION

BY MR. BESHORE:

Q. Marvin Beshore for Dairy Farmers of America.

Just a question in an area or two, Dan.

Your graph, the last page of Exhibit 37, am I correct that what you have done -- what you did in terms of data collection and what you've depicted on the graph is, you took a uniform set of costs over a ten year period, calculated them -- uniform set of plant costs, calculated it on a per gallon basis and came out with an annual number and plotted that on the graph?

A. Yes.

Q. Okay. And your disclaimers with respect to overhead, capital costs, or whatever was just to indicate what you did not include, correct?

A. Correct.

Q. Okay. But you did include was uniform every year, and that's what's depicted on the graph?

A. Yes.

Q. And I think you described in your testimony that it was consistent with Mr. Herbine's testimony to the extent that the slope of the curve was generally the same and the trend at two to three million pounds was even steeper in your case than in Mr. Herbine's testimony?

A. Yes.

Q. Sales to Alaska. Can farm milk move directly from state of Washington to the processing plant in Alaska?

A. Directly from the farm?

Q. Yes.

A. I don't think so, I mean, it's --

Q. Okay. Does the milk have to be processed and treated prior to --

A. When we --

Q. -- shipment to the plant in Alaska?

A. When we send the milk to Alaska, we will heat treat the milk, load it on a barge, and send it up there.

Q. Okay. And that treatment has to occur in a plant, correct?

A. Yes.

Q. Okay. So the treatment, I assume, is to maintain the sanitary qualities of the milk during the trip on the barge to the plant in Alaska, correct?

A. Yes.

Q. Now -- so every -- if it -- if milk for the plant in Alaska must come from -- and I guess it comes from Washington, because there aren't a lot of cows in Alaska that -- source the milk for the plant up there?

A. Not that I'm aware of.

Q. Okay. Now -- so if that milk's coming from plants in Washington, it's got to be plant processed -- it's got to come from plants in Washington. All the plants in Washington are regulated by the Pacific Northwest order, but for the producer/handlers, I assume, correct?

A. Yes.

Q. And so that's going to be pool milk unless it comes from a plant that is exempt from pool for some reason or another, correct?

A. Yes.

Q. And it's going to be plant milk in any case?

A. Yes.

MR. BESHORE: Thank you.

THE COURT: Any more question from the proponents?

(No response)

THE COURT: Mr. Marshall, I'm assuming you wanted Exhibit 37 in evidence since you asked to have it marked for identification; would that be a fair guess on my part?

MR. MARSHALL: Yes, Your Honor. We'd like Exhibit 37 received into evidence, please?

THE COURT: Okay. Exhibit 37 is admitted into evidence, and I think Mr. Yale -- or, did you have any more questions, Mr. Marshall? I'll -- Mr. Yale --

MR. MARSHALL: I will have some redirect, yes, but I also note the hour is such that it might be time for an afternoon break.

THE COURT: Oh, no, we're not even close. Mr. Yale, did you have any --

MR. YALE: Just follows up with two that were --

THE COURT: Okay.

EXAMINATION

BY MR. YALE:

Q. Thank you. Mr. McBride, my name is Benjamin F. Yale on Behalf Etteline, Mallory's and Smith Brothers Farms.

I want to first of all talk about this Alaska situation. There's nothing to prohibit anybody from just finding some plant that qualifies for grade A status to pasteurize or heat treat the milk and put it on a barge, and if that -- all the milk that went through that plant went to Alaska, it would not be a pool plant under the federal order, right?

A. The milk if it went through a pool plant --

Q. No, not a pool plant. You made a separate building, separate plant that all it did was heat treat this milk and ship it to Alaska.

A. If that milk was supplied then by producers that are -- you know, that are pooled on the federal order, then that would then be pool milk because it's going to go up there, and the ultimate utilization is going to be class one.

Q. Even if it's a non-pool plant that it's delivered to and --

A. If it's -- if it puts milk into a bottling -- it goes up to bottling, it's a pool plant if it's producer milk. Otherwise, you know, in this order you have to count for all of a producer's milk or none of it. So, I mean, it's --

Q. But if you don't pool the milk -- the producer's milk, you can ship it there because it's not going into this marketing area, right?

A. Technically, I guess.

Q. I mean, the ability is, is that you can supply milk from Washington without being subject to the federal order, whether you're a PD or not? So supply milk to Alaska from the state of Washington, whether you're a PD or not?

MR. BESHORE? If you have a plant that doesn't exist?

THE COURT: Don't do that, Mr. Beshore. If you want to make an -- if you want to modify a question, you got to come up and identify yourself, object to whatever, but --

THE WITNESS: Under your scenario with a non-pool class one plant, which, you know, I guess hypothetical you can say it exists, because the milk going up there will be used in class one.

BY MR. YALE:

Q. But there's no milk distribution in the Washington state or the Pacific Northwest from that plant.

A. It's still the ultimate destination or utilization of the product that will determine the class of the milk.

Q. Mr. Berde asked you this. As I understand it, I think the concept was that 2.8 to 4 cents would be added on, I think, you know, the implication was it would offset some of the five cents that your producers have had to suffer as a part of this emergency situation. Is that what your understanding was, that if you -- they wouldn't have quite the lower -- as low in that check as they have right now?

A. Yes.

Q. Okay. It -- the five cents that you're reblending as a result of some specific situations with Westfarm, it's not a situation dealing with the PDs, right?

A. Five cents that we're reblending has to do with the federal orders. It has to do with the make costs that, you know, that are outdated --

Q. For --

A. -- you know, we went -- when, you know, we had the hearing back in what, May of 2000, and I mean, that's the cost.

Q. The current ones?

A. I mean, right now -- yeah. The current May costs (phon.) which have not been updated, you know, in -- since the time of the hearing when they used the '99 information, which, you know, at that -- you know, since then the energy costs have doubled, and that is not reflected in the cost -- in the current May cost, and that's what's caused us to put in the five cent assessment.

MR. YALE: All right. That answers the question. Thank you.

THE COURT: One -- oh, go ahead, Mr. Ricciardi.

EXAMINATION

BY MR. RICCIARDI:

Q. Al Ricciardi for Sarah Farms.

Is the Northwest Dairy Association charging to its members any costs associated with its involvement in this hearing? Either in preparation for it or in cost associated with being at the hearing?

A. If -- I lost you. Are we charging --

Q. Yes.

A. -- our producers with the cost of this -- well, at least, you know, my salary, which may not be much, is going to be, you know, part of the cost of doing business, which is part of the nine and a half cents that they do pay to the association to --

Q. Okay. But it's absorbed in the current costs. It's not a separate cost item that you're charging, correct?

A. That is correct.

Q. And I'll see what I can do about getting you a raise.

A. Okay.

MR. RICCIARDI: Thank you.

THE COURT: Did you want to do your redirect, or do you need that break now? I just -- why don't we do the redirect, get him off the stand, and then I'll give you guys --

MR. UNIDENTIFIED: My bladder would like a break if you're going to take on.

THE COURT: Okay. In that case, then -- okay. We'll take a ten minute -- we'll take a break now until a quarter of 4:00.

(Off the record and reconvened.)

THE COURT: Okay. On the record.

You've got some redirect, Mr. Marshall, right?

MR. MARSHALL: Yes. Doug Marshall, Northwest

Dairy Association. Thank you, Your Honor.

EXAMINATION

BY MR. MARSHALL:

Q. Mr. McBride, you were asked some questions about pasteurization technique and the shorthand of HTST type pasteurization. Is there another type of pasteurization as well?

A. There's, you know, the ultra-pasteurized, UP.

Q. Which has longer shelf life because of its ultra-pasteurization?

A. Yes.

Q. Does WestFarm Food operate an ultra-pasteurized facility?

A. Yes, our plant in Portland is ultra-pasteurize.

Q. You were asked, I think, by Mr. Ricciardi why only gallons and half gallons were processed at Medford, Oregon. What happens to the products served -- what is the source of the other products other than gallons and half gallons that go to the customers served by the Medford plant?

A. Those are UP products, and they will come out of our Portland facility.

Q. And why would you use UP products or ultra-pasteurized products on those items and not for gallons and half gallons?

A. Because they will have a longer shelf life and there's not, you know, the gallons and half gallons are going to, you know, basically move fairly fast.

Q. You were asked by Mr. Ricciardi about sales of -- sales to schools, or sales of school milk out of our WestFarm Foods plants systems, and we -- you indicated you weren't sure about that. Are you sure whether or not within the last five years we've had substantial amount of sales to schools?

A. We've had -- we have had sales to schools. I don't know if we have sales right now or how much school milk sales we have.

Q. You didn't prepare for that --

A. No.

Q. -- testimony.

What was the point of your raising the issue of school milk sales in your testimony?

A. Basically just to, you know, go -- that producers/handlers have the ability and are competing head to head with us, you know, at all the different, you know, with -- at all levels.

Q. On page five of your prepared statement, do you have that in front of you?

A. Yes, sir.

Q. The one, two, three, four, fifth paragraph describes your intent of the testimony, and you've seen a lot of cross-examination about things -- everything from leakers to service and the other -- and the many reasons that a customer might change suppliers.

I'd ask you to reread that statement about the intent of the foregoing testimony out loud, and then answer the question, is anything changed -- anything in those cross-examination questions changed your belief?

MR. RICCIARDI: Your Honor, the testimony is the testimony. It's already in the record. I don't know why --

THE COURT: Oh, he can ask him that question.

MR. MARSHALL: Ask if you have changed his mind by talking about leakers and so forth, Mr. Ricciardi.

MR. RICCIARDI: That's --

THE COURT: That's okay. Let him answer the question.

MR. RICCIARDI: Don't have to debate with me, just go ahead and ask the question.

THE WITNESS: Okay. So reread the entire paragraph?

BY MR. MARSHALL:

Q. Just the sentence that describes your intent.

A. Okay.

"The intent of the foregoing testimony has been to demonstrate my belief that the larger producer/handlers in the Pacific Northwest competes successfully against regulated plants, including ours and formerly Vitamilk's."

Q. Do you believe that to be true, even though there are these other facts --

A. Yes.

Q. -- that can affect competition?

A. Yes.

Q. On page two of your testimony, you refer to forward contracting programs with producers. I repoint out the, I guess, it would be the paragraph towards the middle that begins, "During the past five years or so." But the sentence that Mr. Yale was asking you about at some length is the last sentence in that paragraph, which talks about fixed price contracts to bottled milk customers and forwarding contracting programs with producers. Were you referring to a federal statute there that has, at least until it expires, limited forward contracting programs with producers by proprietary class one facilities?

A. Yes.

Q. And does the inability of a bottling plant to offer such programs limit its ability to hedge fixed price contracts in the marketplace?

A. Yes.

Q. Finally, turn -- please turn to Exhibit 38 and the section with respect to -- towards the bottom of the first page with respect to the five cent make allowance adjustment that was brought up for some reason by Mr. Miltner. He's implied in his questions there's a burden to NDA producers, and perhaps there is relative to the pool producers generally. Mr. McBride, if the energy costs that you described in your testimony and is -- that are described in this letter have been factored into the thinking that the federal order system used in developing the current make allowances, would the current class three and four make allowances be greater than they are today, to reflect those higher energy costs?

MR. UNIDENTIFIED: Objection, Your Honor, there's no foundation for his testimony to ask him what the federal government (indiscernible)

MR. MARSHALL: There's a federal order theory that applies to formulas, and I think he's an expert enough in federal orders to have an opinion.

MR. UNIDENTIFIED: Well, I don't think he is.

THE COURT: Well, what's the point of your question?

MR. MARSHALL: Your Honor, I think it relates to the question of whether producers are being assessed a penalty as suggested in questions by the opponents.

THE COURT: You can answer it if you know the answer to the question.

THE WITNESS: Well, had they stayed with their theory of the, you know, the make cost with the new -- with the current energy costs, the make cost would be higher, which would mean a lower class three and four prices.

BY MR. MARSHALL:

Q. So the blend price is higher than it would be if the current make -- if the make allowances that had been adjusted reflect current energy prices?

A. Yes.

Q. And then this nickel takes back some of that increase, does it not?

A. A portion of it, yes.

Q. If -- in your opinion, if producers were to leave NDA or if the opponents were to argue that producers should be allowed to leave NDA to address that nickel being shifted back to the amount of the blend price, would that be, in your opinion, evidence of disorderly marketing conditions?

A. Yes.

MR. MARSHALL: I have no further questions.

THE COURT: Anything else

(No response)

THE COURT: You may step down.

Who's calling the next witness?

MR. ENGLISH: Charles English for Dean Foods calls Mr. Paul Christ. The testimony has been out of the back (phon.).

THE COURT: Mr. English?

MR. ENGLISH: Yes.

THE COURT: Why don't you hand him a clean glass?

MR. ENGLISH: I can do that.

THE COURT: Assuming he's going to want to drink some water --

MR. CHRIST: Probably.

THE COURT: -- and wants to have his own glass.

Would you please raise your right hand?

PAUL G. CHRIST

having been first duly sworn, was examined and testified as follows:

THE COURT: Okay. Could you please state your name and spell it for the record?

THE WITNESS: My name is Paul G. Christ, last name spelled C-h-r-i-s-t.

THE COURT: Go ahead, Mr. English.

EXAMINATION

BY MR. ENGLISH:

Q. Mr. Christ, let's first go through your CV for a few moments. Not everybody in the room may have been familiar with -- you've worked in the dairy industry for a

number of years, correct?
A. Yes, my first job out of college and my last before retiring, and all the time in between was in the dairy industry.
Q. And in addition to college, you also have a masters in agricultural economics?
A. Yes, I have a masters from Southern Illinois University.
Q. And you're also a professor today, teaching agricultural economics?
A. At the present time, I'm an Ag-El (phon.) professor at the University of St. Thomas in St. Paul. I teach in the Masters of International Management program and the Executive MBA program.
Q. And at one time you worked in -- with federal marketing orders?
A. Yes. Early in my career, I worked in the Detroit federal milk marketing market administrator's office and the Kansas City federal milk market administrator's office, as well as in the Washington, D.C. office of the dairy programs.
Q. And approximately for how long did you work for USDA total?
A. I worked a total of 14 years, two of which were interrupted by the military service.

Q. And in addition to your time at USDA and military service, you've also then been with a company called Land of Lakes?

A. Yes, I joined Land of Lakes in 1974, and retired a little more than 26 years later in the 2000.

Q. And you're appearing today on behalf of Dean Foods?

A. Yes, I am. I've been hired by Dean Foods to assist you, Mr. English, in making a case in support of Proposals No. One and No. Three, but I am an advocate for Dean Foods Company.

Q. Now, maybe try to handle a couple of thing in advance. You're not here for Land O' Lakes?

A. No, I am not. Lane O' Lakes is aware of my interest in this subject, and -- but I'm not representing Land O' Lakes in any way.

Q. And how familiar are you with Dean Foods' operations?

A. Dean Foods has been a player in the dairy industry for a long time, and they were active in the Chicago market, but I know very little detail about their internal operations, their scope of operations, the names and locations of plants. I know very little of that.

Q. And given your 40 some years of work in the dairy industry -- let me back up, for Land O' Lakes, were you involved in any way with milk procurement?

A. Yes, there was a period in which I supervised the milk procurement activities of Land O' Lakes, and I've always been closely associated with milk procurement activities, even though I did not directly supervise it.

Q. And you're testified in a number of federal order hearings regarding --

A. Yes, I've been to many, many hearings. My responsibility at Land O' Lakes from the beginning was to engage in any federal milk order matters that arose of interest to Land O' Lakes for the full 26 years.

MR. ENGLISH: Your Honor, under the circumstances, I would ask that Mr. Christ be recognized as an expert in the application that -- of federal milk marketing orders --

THE COURT: Okay. You are --

MR. ENGLISH: -- (indiscernible) give opinions.

BY MR. ENGLISH:

Q. Now, under -- with your experience of federal orders, what orders are open for consideration at this proceeding?

A. In this proceedings, there are just two orders, Federal Orders No. 124 and No. 131.

Q. Okay. And what evidence in -- should the secretary be considering with respect to these proceedings?

A. I believe by rule, he's required to consider evidence relating to marketing conditions in these two federal order areas, and none other.

Q. So leaving aside some of the hyperbolae for a moment, let's turn -- did you bring Exhibits 5 and 6 with you?

A. Yes, I did.

Q. And I realize that you don't know a lot about Dean Foods' operations, but in examining Exhibits 5 and 6 for these two orders that are open, and for the marketing conditions and evidence, what, if anything, can you conclude with respect to these markets and Dean Foods?

A. Well, one other question that's arisen in earlier testimony and cross-examination is, how big a player is Dean Foods in these two markets? It's my belief that Dean Foods is a marginal player in these two markets. They do not have a regulated distributing plant in either of them.

In the statistical information, for example, in Exhibit 5 on page 37, it's showing class one sales in the marketing area from a variety of types of plants. Dean Foods is not a pool plant, so it's not in the first column. Dean Foods is not a producer/handler, so it's not in the second column, and so any activity that Dean Foods had would be included in the third column, class one in-area sales by other plants.

These other plants included plants fully regulated under other federal orders and plants partially regulated, distributing plants and exempt plants. I counted 21 partially regulated, distributing plants and exempt plants. I have no idea how many plants are included in this number that are fully regulated under other orders.

The composite for 2002 of sales by these plants was 14.8 million pounds of class one sales. The total market class one sales were 2,175,000. That means all these plants, the 21 identified in the exhibit, plus any other order plants represented less than -- around two thirds of one percent of the total class one. So Dean Foods would be included in that two thirds of one percent, but I have no estimate of how much of it is Dean Foods.

Q. Turning to Exhibit 6 and Order 131. Did you do any analysis similar?

A. I did similar analysis on Exhibit 6, page 27, showing the year 2002, the source of in-area class one sales for the market. The largest number, of course, was in-area sales by pool plants. Dean Foods did not operate a pool plant in the Arizona/Las Vegas market. There is no -- there are no data reported for producer/handlers because it is restricted.

For all other plants, in this case including fully regulated plants under other federal orders, partially regulated distributing plants, exempt plants, and for all of 2002, producer/handler plants. In this case, I counted 23 plants that did not include plants fully regulated by other order -- by other orders. And there's a number of plants that would've been regulated by other orders that would be included in this 368 -- 369 million pounds of in-area sales.

All of these plants combined represent 28.9 percent of the total class one in-area sales in the year 2000. Again, Dean Foods would be --

Q. 2002?

A. Excuse me?

Q. 2002, you said 2000.

A. In 2002. Again, Dean Foods would be included in that number. However, it's possible to make some presumptions about the data. In March of 2001, producers/handlers were included in the statistics relative to these other plants, and the number of class one sales by this group of plants more than doubled between February and March. So we could conclude at that time that there was somewhere in the neighborhood of 15 million pounds of producer/handler milk.

If we look at December of 2002, all of these plants combined represented a little more than 31 million pounds of class one milk. If producer/handlers represented

15, then the other 15 million would be represented by all of the other plants, including some of Dean -- maybe one or more Dean's plants. So somewhere around -- may participate in this residual 15 percent, but clearly they're not all of the 15 percent, and they could easily be a very small share of it.

Q. Thank you, sir. Now, you have a prepared statement. Before I ask you to read it for the record, I'd ask, who prepared the statement?

A. I prepared this statement. I was asked during the Phoenix session to prepare my own data, views, and arguments relative to the issue of producer/handlers in these two markets.

Q. And this is based upon your 40 years' of experience in federal market?

A. Yes. Yes.

Q. And other than some minor edits of grammar and other nature, what, if anything, did Dean Foods add to that?

A. Well, I did not review this with any of the management staff of Dean Foods. I did have it read by the two other individuals who are here representing Dean Foods, and a few grammatic (sic)(phon.) and punctuation and spelling corrections were offered, and that's about it. The rest of it is my testimony.

Q. Thank you, sir. Would you then please deliver your testimony and opinions about these markets and producer/handlers?

A. Okay. "My name is Paul G. Christ. I reside at 245 Indian Trail South, Afton, Minnesota 55001.

"I appear here as a dairy consultant with 40 years' of experience in working with federal milk marketing orders, both as an employee of the dairy programs of the Agricultural Marketing Service and as a Vice-President of Land O' Lakes, Incorporated. During this time, I have been exposed to nearly all issues related to federal milk orders and participate in the development of many of the current provisions of milk orders. My testimony here is intended to support Proposals No. 1 and No. 3 that would place certain limits and the size and flexibility of producer/handlers in Federal Orders No. 124 and No. 131.

"It is my view that exemption from the pricing and pooling provisions of the federal milk order should be a rare and highly restricted privilege. The foundation for this view is my belief that the basic purposes of a federal milk order are to, (a) assure an adequate supply of milk for fluid uses, and (b) enhance the returns to milk producers. There is also an implicit objective that these first two purposes should be accomplished in an efficient manner.

"Federal milk orders achieve their objectives by doing four things: (a) classify milk according to how it is used; (b) setting different prices for each class of milk. This is a form of price discrimination; (c) pooling the proceeds from all uses of milk to all producers, and (d), verifying the accuracy of reports of milk receipts and utilization.

"The critical features of these activities that ensure the effectiveness and equity of federal milks orders is that they be applied universally and uniformly. Without universality and uniformity, some participants in the market will enjoy competitive advantages over other participants that arise from regulatory laxity rather than from business acumen.

"Historically, there have only been a few types of firms that have been exempted from the pooling and pricing provisions of milk orders. These included, (a) institutional milk processing plants such as those operated by governmental institutions and universities, (b) small plants for which the administrative costs of regulation exceed the regulatory benefit, (c) plants located in Clark County, Nevada, and (d) producer/handlers. Only plants in Clark County, Nevada have a legal right to be exempted from regulation. The exemption of the other three types of plants has been permitted for administrative convenience or to achieve a modest, social objective.

"The idea that a typical dairy farmer should be able to enjoy a regulatory advantage in processing his own milk has a measure of social appeal. And the key word here is 'typical.' The expectation was, and I hope continues to be, that such an exemption would have a negligible effect on the other producers and handlers in the market who are fully subjected to the regulatory program.

"An exempt plant, and in particular, a producer/handler plant enjoys a significant and competitive advantage over other producers and other handlers in the market. As a producer, the exempt producer/handler can receive more than the blend price for his milk depending on his internal transfer price between his plant and his milk production activity. As a handler, the exempt producer/handler may pay less than the class one price for his milk supply, again, depending on his internal transfer price between his plant and his milk production facility.

"Of course, if the producer/handler views his milk production activities and his milk processing and marketing activities as a single, integrated enterprise, his profitability depends on all of his costs and all of his revenues. Nevertheless, the combination of these two activities and the presence of regulatory exemption gives the producer/handler a significant, competitive advantage over his rival producers and handlers. This advantage is the difference between the local class one price and the local blend price.

"A producer who participates in the federal milk order pool receives the blend price for the milk he sells. A handler who is regulated, pays the class one price for the milk he buys and uses in class one products. In 2002, the difference between these two prices amounted to $1.84 in the Arizona/Las Vegas order. That $1.84 gap is eliminated for a producer/handler who is exempt from regulation, and that amount of money is available to the producer/handler to create a competitive advantage for his business. As a result, a producer/handler represents a severe, competitive problem for rival handlers and rival producers.

"There are other sources of competitive advantage that the producer/handler may or may not be able to exploit. These might include efficiency in milk production, efficiency in milk processing and distribution, effective marketing, high quality, and better service. However, these sources of competitive advantage are equally available to the producer/handler and to his rival producers and handlers. They are not a consequence of regulatory privilege.

"A competitive advantage arising from exemption from the pooling and pricing provisions of a milk order is a consequence of regulatory privilege, and is not a consequence of the skill, luck, or effort employed by the producer/handler. Other pool participants effectively subsidize the operation of a producer/handler. To the extent that he experiences a raw milk cost for his fluid milk products that is less than the class one price, the producer/handler can use its financial advantage to offer lower prices and better service than his rival, regulated handlers can. As a result, his rivals must reduce their selling price or increase their service costs to maintain their business. This means reduced profits or increased losses to those rival firms.

"To the extent that a producer/handler as a producer experiences a raw milk selling price higher than the local blend price, his profits in milk production will be larger than those of his rival producers, and he can use these profits to acquire more and better resources than his rivals can.

"In the long run, given equal skill, luck, and effort, the producer/handler wins the competitive struggle with both his handler rivals and his producer rivals. All of this arises out of a regulator artifact and not out of the merit of the producer/handler business enterprise. In effect, the producer/handler is able to extract significantly more from a particular market environment than can his rivals because he is exempt from the minimum pricing and pooling regulations of the order. The more he extracts means that the other firms extract less. This shows up most vividly in the reduced resale prices and profits for packaged fluid milk in the reduced amount of producer milk classified as class one in the market, and in the reduced blend price that accrues to other producers.

"I stated earlier that the exemption of a processing firm from the pooling and pricing provisions of an order -- of a milk order would be tolerable if it had a negligible effect on the other firms in the market, including producers and handlers who are fully regulated. This raises the question of what is negligible and what is not? I would assert that anything more than one cent per hundredweight reduction in local blend price is not trivial. Dairy farmers, both individually and collectively are very sensitive to differences in pay prices, even differences as small as one cent.

"In the Arizona/Las Vegas market, a shift of about 950,000 pounds of class one sales per month between a fully regulated handler and a producer/handler would change the blend price by about one cent per hundredweight. So an argument can be made that any and all producer/handlers with class one sales of more than 950,000 pounds per month has more than a negligible effect on the market.

"Early in this hearing Carl D. Herbine, CPA, stated that a price difference of one half cent per gallon was significant to his fluid milk processing clients. The $1.84 per hundredweight potential cost advantage of a producer/handler in the Arizona/Las Vegas market is 31 times the one half cent per gallon level of significance. It is not negligible.

"The question arises as to why there are not more or bigger producer/handlers if they enjoy such great advantages. In fact, there is a shift that favors producer/handlers in the Arizona/Las Vegas order. They have not increased the number, but they have increased in size and importance.

"The same question can be asked more generally as to why more resources do not move more rapidly into the more profitable activities in the general economy. The answer is that resources are sticky and cannot be quickly or easily shifted among alternative uses. Also, as more resources move into an apparently profitable activity, the profitability of that activity goes down, and the resource shift turns out to be a mistake.

"In addition, there is a high risk of regulatory change. The corner (phon.) witness stated earlier that because of its size, his firm expected that if it sought producer/handler status for one of its plants, there would be an immediate legislative or regulatory change, and the plant would become fully regulated. The same risk does not seem to apply to existing producer/handlers who choose to expand their size and importance.

"For what size of producer/handler is exemption tolerable? There is no definitive answer, but it is imperative to choose a fixed number. Fixed numerical standards are common and have been find -- found to be necessary in all forms of regulation, including the tax code and environmental standards. Federal milk orders are no different in that an objective measure is needed to judge whether an individual or firm is, or is not, in compliance with the order.

"I offered one measure above, that the exemption of producer/handlers collectively could be based on the volume of class one sales that would cause a one cent per hundredweight change in the blend price. In the Arizona/Las Vegas order, that would be about 950,000 pounds per month.

"Another measure could be the average size of milk producers in the market. This measure would conform to the idea of a typical dairy farmer integrating into processing. In the Arizona/Las Vegas market, the average producer sells about 2,400,000 pounds of milk per month, so a size limit for exempting producer/handlers could be set at about that level.

"How relevant is the cost of milk production for a producer/handler? Obviously, it is important to him as it affects his profits, but it is not important whether his costs are more or less than other producers in the market. The cost of milk production varies greatly from one producer to another as a result of differences in management and resources employed.

"The decision of whether to continue in milk production is based in the short run on whether all variable costs are paid. In the long run, the decision to produce milk depends on whether all costs of production are paid. As a result, when milk prices go up and down, most producers continue to produce milk because variable costs are being paid.

"For the market as a whole, the cost of production must be at or below the blend price. Otherwise, milk production would fall, and there would not be an adequate supply of milk for class one use. For the Arizona/Las Vegas market as a whole, milk production has been expanding, so the cost of production must be below the prevailing, average blend price.

"If a producer/handler cannot survive paying the class one price for his fluid milk supply and receiving the blend price for his milk production, that means that he is less efficient in milk processing and distribution and/or in milk production than his rivals, and should be discouraged from continuing in the business. If he continues in business, there is a loss of economic efficiency because other producers and regulated handlers are willing and able to provide the same goods and services at lower costs. Society benefits as a result.

"Balancing is an important cost for the fluid milk market. Significant reserve of milk are needed to ensure that sufficient milk is available for class one use at all times. Each plant needs an operating reserve that covers unavoidable class two, class three and class four uses, such as shrinkage and a disposition of cream arising out of standardizing class one milk. In addition, a reserve is needed to cover seasonal variations in class one sales and milk production.

"In an average market, the minimum average of these two kinds of reserves is about 15 percent. The actual size of the reserve in a particular market depends on how much milk is pooled and how many class one sales are regulated. In 2002, the class one utilization of producer milk in the Arizona/Las Vegas market was 31.85 percent, meaning that 68.15 percent of pooled milk was reserve.

"Reserve milk must be disposed of in lower valued uses. This is one of the reasons for classified pricing and pooling in federal milk orders. The processing and -- the process of pooling ensures that all producers share in the lower value of reserve milk. Producer/handlers do not share the cost of disposing of the market-wide reserve, but they do incur the cost of disposing of their own reserve. However, their reserve is likely to be much smaller than the market-wide reserve, and they may have opportunities to get higher prices than can be obtained for the market-wide reserve.

"A producer/handler has a high degree of control over both the volume and variation in monthly milk production. For example, if he operates both a farm associated with a producer/handler enterprise and another pool farm, he can shift columns back and forth to tailor his producer/handler milk supply to his class one needs. A pooled producer can control his own milk production, but he cannot control the volume or monthly variation of other producers in the market-wide pool. Therefore, a producer/handler is like to experience an even smaller reserve than the minimum average of 15 percent mentioned above.

"Also, a producer/handler may be able to sell his reserve milk in a non-pool class one market while a regulated handler cannot. So the producer/handler may be able to get higher returns for whatever reserve milk he has than can a regulated handler. Whatever costs a producer/handler does incur in balancing his milk supply against his class one sales are no different in kind than the cost incurred by pool participants, but they are likely to be much smaller in degree.

"That concludes my testimony."

Q. Mr. Christ, again, with 40 years of experience with the government and also in the dairy industry in private industry, have you formed an opinion as to the definition of disorderly marketing?

A. This is been a subject of long-standing debate, but I have developed two definitions. One is that if the -- disorderly market exists when the regulatory terms of trade are different among competitors in the same market. Second, I would argue that disorderly market arises -- marketing arises when there are several ways to achieve a regulatory objective, and we choose not to use the most efficient. If we incur higher costs in achieving our regulatory aims than necessary, that is disorderly marketing as well.

Q. Do either of those definitions apply as you have attended these proceedings in Phoenix and here to Order 124 and Order 131?

A. Well, I would clearly apply the first definition where the regulatory terms of trade are not equal among competitors in the same market, and that is the case between a regulated handler and a producer/handler on the one hand and a pool participant producer and a producer/handler on the other hand.

MR. ENGLISH: Thank you. The witness is available for cross-examination.

THE COURT: Did you want this document marked at all, or just want me to --

MR. ENGLISH: I don't need it marked.

THE COURT: Okay. That's fine.

MR. ENGLISH: The witness is available for examination.

THE COURT: Thank you. And who would like to go first?

MR. YALE: I guess it's me.

EXAMINATION

BY MR. YALE:

Q. Good afternoon or evening, Paul, how are you?

A. Good afternoon. I'm fine. Thank you, sir.

Q. My body still says its evening. Benjamin F. Yale on behalf of Smith Brothers Farms, Etteline, and Mallory Dairies.

You went to some great pains early on in Q & A with Mr. English regarding Dean Foods' involvement in these two orders. If it's such a little -- it's so much, so little involvement, why even waste the resources of Dean Foods to be here?

A. Dean Foods, I believe, is a participant, even on the small scale in these markets. I do not know the precise scale. Nevertheless, they are a participant, and the plants from which milk is distributed in these areas is likely to be regulated under either federal order or the California marketing system.

Q. Isn't it true that Dean Foods has an interest in doing this on a nation-wide basis and not just this one?

A. That is likely to be true, but I -- we're not discussions conditions and markets, other than the two noticed in the hearing here.

Q. Now, in a general description of the testimony provided, you had some specific numbers dealing with 131 and some references to 131. I do not see the same references to the Pacific Northwest. Is there a reason for that?

A. No substantive reason. I put these numbers together during the Phoenix phase of this hearing, and I just used the document from Order 131. The same calculations could easily be done for Federal Order 124. I doubt if they would differ much in degree. I think the same story would be told.

Q. You provided a definition of disorderly marketing, two of them.

A. Uh-huh.

Q. And my first question is, is that have you seen the secretary specifically use either of those as the basis for decisions?

A. I don't recall reading these two definitions.

Q. Do you believe the secretary should look at the existence of disorderly marketing conditions as they were in the '30s in making this decision, or should they look at different types of disorderly definitions today?

A. I don't know what disorderly marketing conditions, how I would define them with respect to the 1930s. I gave you a definition that I would apply to current marketing conditions, and I would advise the secretary to use the definition as it applies to current marketing conditions.

Q. Now, isn't one of the -- with the proposals of setting caps and stuff on PDs, I mean, isn't one of the issues the fact that in a market that has producers, processors, and buyers that it is difficult to obtain a one size fits all regulatory things that treats all of them in the same way? That is, is that if whatever regulation you come up with is that some, based on their size of their relationship to other participants, are going to obtain an advantage?

A. I would argue there exists -- there will exist in each order some sort of equilibrium, and if the equilibrium does not destroy -- the regulatory equilibrium does not destroy participants in the order, that that's acceptable. But any time there's a change in federal milk order regulation, there is a change in the terms of trade, and some people will likely lose, and other people will likely gain, but we go through this process repeatedly to try to improve the balance and equity and to find a stable equilibrium in federal milk orders.

Q. In fact, that's one of the benefits or one of the reasons the federal orders that survived is that ability to adapt to change, right?

A. Yes, that's correct.

Q. But another reason that it has been able to survive is that it's always tried to keep in touch with actual market -- free market reality as much as its regulatory. It has not operated totally independent of a free market, right?

A. The federal milk order system has not, primarily because of the hearing process. The data and evidence that the secretary has available to him is developed at hearings like this from people who are active participants in the market.

Q. Now, you indicate that whatever result of a regulatory hearing, there are winners and there's losers. Does the degree --

A. From a change, yes.

Q. Huh -- as a result of a regulatory change. Thank you. One could argue that the hearings create winners and losers, too, but we won't go there.

The issue of a regulatory change, creating winners and losers, what types -- or, let me back up. Isn't it true, though, that in determining to make that change, the secretary has to consider the degree to which there are winners and loser, or to the degree that a certain person is a loser -- I mean, how much they're going to lose as compared to the overall change. Isn't that part of the consideration?

A. Well, he has a responsibility to pursue orderly marketing, and if the existing regulatory system does not provide orderly marketing, for example, a difference in regulatory terms of trade among market participants, then I think he has an obligation to make a change.

Q. Does he have to make the change -- isn't it true, though, that in doing that, that he needs to do -- inflict the least loss on any one individual to reach that orderly marketing?

A. I don't think he has that responsibility because before he'll make a change, he will have made a finding that some people who are affected by the regulation are experiencing a significant disadvantage because of the regulation. I'm not sure that he has an obligation to minimize the impact on anybody. I think he has an obligation to ensure that the terms of trade under the regulatory program are as uniform as he can make them.

Q. Now, let's talk about the terms of trade and its regulatory (phon.), and let's look at a situation with a particular, hypothetical bottling plant.

There are a wide range of issues that address -- first of all, I think you would agree, would you not that the viability of a bottling plant can create, or at least has an impact on the orderly marketing of milk in that market, right?

A. Depends on -- I may or may not agree. Depends on whether the viability or lack of viability arises out of normal business behavior, competitive activities, or whether it arises out of regulatory differences.

Q. All right. Will you restate that answer again. I think I caught it, but I'm getting a little slow --

A. Okay.

Q. -- because it is evening for me.

A. The -- I think the secretary's responsibility is that the regulatory program by itself does not create viability or lack of viability among competing firms. Other things will create that, business behavior, business strategies, ability to acquire resources, the skill in operating a plant and marketing the product. All of these things affect the viability. I don't think these are matters of interest for the secretary.

Q. Okay. And some of that -- and part of that things that aren't of interest is that there may have been long-term decisions made by a plant that finally have accumulated to a problem. Maybe failure to maintain the plant, or failure to invest and make changes over time, failure to have an adequate sales force. All of those things could contribute, right?

A. Yes, they can, but the thing that the secretary needs to focus on are what does the regulatory program do in terms of either destroying a business or enhancing a business.

Q. So when we come -- so I -- the -- your point, I think as I understand it is, is that when the secretary looks at all this evidence, and we seem to have a lot of stuff in the record. How much of it, you know, is evidence, I guess, is her decision to make. But there's a lot of stuff in the record that she needs to discern whether a particular movement of milk from one handler to another is the result of a regulatory issue or the result of other issues intrinsic with that plant, such as its inefficiency, its location, its management, the quality of its product, its reputation in the market, right?

A. I think that would be useful to be able to make those distinctions, that I would argue that all else being equal, the secretary's interest is to make sure that the regulatory program has equal effects. And what happens in terms of individual business decision-making is not a matter of her concern outside of the regulatory effects.

Q. So you're saying then that if there's evidence in the record that suggests that there's movement of milk from one participant to another, is the result of competitive situations other than the regulatory, that she is to ignore those?

A. That's a very broad suggestion, and I can't think of every possibility that -- of a competitive environment that might exist. I'd say in general, I would agree with you that normal business behavior is outside the scope of her concern. What is within the scope of her concern is how the regulations will affect business behavior.

Q. All right. So let's take a situation where we have a plant that is located, or a plant that has the ability to deliver to the customer -- the wholesale customer in an efficient way.

A. Uh-huh.

Q. All right. And we have another plant of equal size that, for whatever reason, is not able to deliver it in the level of efficiency that the customer wants. Okay?

A. Okay. I understand the proposition.

Q. All right. Now, if that is existing, and the second plant is complaining about the situation, you're saying that the secretary should not get involved in interfering with that relationship between those two plants; is that correct?

A. I think that the plant that is disadvantaged in that situation might complain that the regulatory system creates the problem. The secretary may want to investigate that, but if the regulatory system is not creating the problem, I think it's outside of her scope of interest.

Q. Which comes back to my point, that that's really what's got to be done here with all this discussion of movement of milk and sales and stuff, is that the duty of the secretary is sort out whether that change is in response to the regulatory environment and the differences in the regulatory treatment, or the result of just ordinary competition between plants in an orderly market, right?

A. I think in general I would agree with you, but I -- it would be more helpful if I had a specific application. Then I could say I agree or disagree, but in general, I think the -- it's a sound principle.

Q. Now, taking that another step further, the -- it would be in the long-term creating in a disorderly market if the secretary were to interfere with ordinary competition within the marketing relationship by virtue of regulation alone, right?

A. I would answer no in that case, that the federal milk order system by -- almost by definition is an interference with regular, competitive activity, setting minimum prices, uniform prices, the whole range of thing is an interference with the free market, competitive environment. But I would say it is justified in terms of the regulatory objectives of assuring an adequate supply of her class one use and enhancing prices to producers. So okay, then we can go to my second definition of orderly marketing, is this accomplished in the most efficient manner?

Q. Now, let's -- but I want to come back to them. I'm going to follow up, go either with one of these, but I -- the follow up of this type of situation is, is that you would agree, would you not that in an orderly marketing, there will be the movement of supply contracts from one provider to another in the free trade of competition, right?

A. Yes, there will be give and take in the market based on a whole lot of competitive things. I would hope not because of the regulator --

Q. Right.

A. -- application.

Q. And, in fact, if you have a market in which there is no movement and competition and a trading back and forth of contracts and the like, indicates that there is disorderly marketing going on, right?

A. I would not conclude that either, that stable relationships -- a lot of stable relationships exist in the dairy industry where buyer and seller relationships may be in effect for a generation. And there are changes that occur, but many relationships are very, very long standing.

Q. But in a healthy one, there's got to be some movement. If there's absolutely no change in those relationships in a market indicates that there may be something going on other than a healthy market, right?

A. I guess I'm not competent to answer that because I've never observed such a market.

Q. Now, what about -- you understand the term "monopsony?"

A. Yes, I do.

Q. And what is a monopsony?

A. A monopsony is where there is a single buyer in a market.

THE COURT: If we could just spell that just so I think it's straight --

MR. YALE: I think it's m-o --

THE WITNESS: M-o-n-o-p-s-o-n-y.

BY MR. YALE:

Q. P-s-o-n-y.

A. A monopsony is a situation where there's a single buyer and many, many sellers of homogeneous product.

Q. And an -- what is an oligopsony, is the -- a few --

A. A small number of --

Q. -- buyers.

A. -- buyers.

Q. It's the other side of a monopoly, in a oligopoly.

A. You say those words fast, you'll get them mixed up.

Q. And at this point, I could get them mixed up slow or fast, but is the existence of a monopsony an indication of a disorderly market?

A. A -- an existence of a monopsony may characterize an inefficient market because the volume of transactions would be lower, and the prices -- purchase price is likely to be lower than in a competitive market on both sides.

But that is not a consequence of the regulatory program. That's a consequence of maybe failure to enforce antitrust laws, but it's not a failure of the federal milk order regulatory program.

Q. But it is possible, is it not, that the regulatory program can create a monopsony through its pooling and other restrictions on participation in the pool, right?

A. That I don't know. It would have to be a destructive regulatory system to drive everybody but one buyer out of the market. It would really have to -- there cannot be -- other circumstances that would lead to that, such as economies of scale, that might lead to that, but it would -- I think if the regulatory program drove competitors out of the market, that would be a serious matter, but I don't know of a case like that.

Q. But it's a consideration the secretary needs to make sure that regulations do not create that situation, right?

A. Yes. The regulations should not create a situation where one otherwise equal competitor is favored over another otherwise equal competitor.

Q. Would you agree, Mr. Christ, that the -- that another sign of an orderly market is the ability of new entrants to come into the market and compete?

A. I think the ability of new entrants depends on many things other than the regulatory program. I believe that the regular program should not exclude new entrants or discrimination against new entrants, and that is a situation where the regulatory program, in terms of trade, would not be the same. But new entrants will depend on efficiencies and technology, transportation economies, maybe new marketing relationships, those sorts of things.

Q. Now, let's kind of take this to another step. You talk about this regulatory equality, I guess, for want of a better term. But isn't it also a role in establishing these regulations that their connection with the market realities cannot be lost? I mean, they can't do it just artificially and without any consideration of what the market reality are?

A. I agree. They need -- the secretary needs to take into account normal, competitive behaviors, what normal economic incentives will exist in the market, and try to achieve the regulatory benefit with the least loss of efficiency.

Q. Now, let's take that -- you indicate some of the ways to obtain orderly marketing. Is -- you have the classification of milk, --

A. Uh-huh.

Q. -- and we're not going to talk about three and four, and whether that's --

A. No.

Q. -- appropriate thing. Some day I'd like to talk to you about that, but we don't have time for that today.

But you said the setting the different prices for each class of milk, or price discrimination, that's one of the hallmarks of the federal order program, right?

A. Yeah, and that achieves two results. The first result is that it assures an adequate supply of milk for fluid use because it's the highest value in the market. Therefore, it has first claim on the milk supply.

And the second thing it does is it makes it feasible to dispose of the reserve in that market at a lower price, and the third thing that it does is -- well, the pooling is the third thing that goes with that. But it is a almost an essential feature in federal milk orders. It achieves -- first assures an adequate supply of milk for fluid use. Second, it enhances prices to producers. Price discrimination is a classic technique for increasing revenues to sellers.

Q. Now, in setting these minimum classes, I mean, wouldn't you agree that the secretary has tried to correlate those to some free market values? I use the word "try." I'm not asking you whether they succeeded, but that's been kind of the effort with, like, the three and four?

A. I agree that they have achieved some coordination with free market activity, and especially in the variation over time, but not in the absolute levels. It's my belief that class one prices are higher than what exists in unregulated market, and class three and four prices are lower than they would exist in an unregulated market.

Q. You answered my question before I asked it. Thank you.

Now, I want to talk about the differences between a regulated 7A pool plant, one that pays minimum prices, and a producer/handler. Okay?

A. Okay.

Q. That's the topic we're going to talk about for a moment.

There is -- first of all, you would agree the producer/handlers are subject to regulation within the federal order?

A. Yes, they are subject to have to report. They have to permit an audit of their books and records. They have to -- there are a number of things on limitations on who they can sell to and --

Q. Right.

A. -- who they can buy from. But they are not subject to the minimum pricing regulation --

Q. Right.

A. -- of the order.

Q. Right. So conversely, for example, a producer/handler is limited to how much they can purchase from other producers?

A. Yes.

Q. A 7A handler has no such limitation, right?

A. That's correct.

Q. All right. Does that have value to a plant, the ability to have an unlimited -- roughly an unlimited supply of milk available?

A. Yes, I agree that this gives a 7A plant more flexibility in deciding where it gets its milk.

Q. And that also translates in the ability of that 7A in its marketing decisions in a much more flexibility to obtain customers much more rapidly, right, because it has the supply of milk available almost instantly?

A. The -- yeah, the 7A handler has more flexibility in at least trying to acquire additional milk supplies. They may or may not be able to attract somebody --

Q. Right.

A. -- to sell them the milk, but they don't have to develop the milk production themselves.

Q. But in Order 124 and 131 with the low class one utilization, the availability of milk for a class one handler should be there, right?

A. Well, there's an abundance of milk in both markets for class one use and class one being the higher valued use, they likely to get the milk.

Q. Now, at the same time a 7A handler has the opposite benefit, and that is the ability to right-size its milk production relatively quickly and push that onto the pool to over those losses, if it doesn't have the need for all that milk, right? Let me restate the question.

A. Please.

Q. We have -- you mentioned this idea that you have lower prices for three and four to clear the market, right? That's one of the hallmarks --

A. Yes.

Q. And then at the same time you pool those low prices with the higher prices so that individual producers don't take the blunt of that market clearing function within the order, right?

A. That's correct. The market -- the cost of disposing the reserve is shared across the market, yes.

Q. All right. And so it makes it less painful and --

A. For individuals.

Q. -- creates some efficiency.

And so a handler who has to make that balance who's a 7A handler can take and enjoy the benefit of this ability to pool or put onto the pool its cost of balancing and the federal order system designed to balance and absorb that cost and distribute to all the participants equally, right?

A. Yeah, the federal order system includes a mechanism for doing it. The bottler, whether he has a great deal of flexibility in his milk supply depends on his relationship with his suppliers. If he buys from a cooperative, he may have some sort of full supply agreement with him or something like that, where they take all the ebbs and flows, but he may have a fixed volume contract with them. So it depends on the arrangement he's negotiated with his individual suppliers, which may be individual producers, may be his own production, and may be a cooperative.

Q. But -- and in any event, the producers that supply his milk, how be it they are producers individually or cooperatively, those producers don't share the full cost of that balancing. It is shared with all the rest of the participants in the pool, right?

A. That's correct. In --

Q. And that's a --

A. -- a market-wide pool, yes.

Q. And that's a benefit to that 7A plant, is it not?

A. I'm not sure that the benefit accrues to the plant. It accrues to his suppliers because they have confident that there will be a market available, and one group of producers will not suffer with respect to another group of producers.

Q. But from the plant standpoint, it doesn't have the cost associated with having to provide for that individually?

A. Yes, I agree that there's less friction in the market. I would call it friction where arrangements have to be made by this party or that party. These arrangements tend to be established and function over a long period of time.

Q. Now, on the other side a producer/handler is limited in its supply to the amount of milk that it actually has on its farm, right?

A. Not completely, but very closely. It is able to buy some milk from other sources, but very -- it's much more limited than a 7A.

Q. Right. And at the same point as well, is that its excess is not the cost or the -- associated and the losses associated with its surplus are ordinarily not born by the rest of the pool, right?

A. Not the losses associated with the limited amount of reserve that the producer/handler has to dispose of, but if the producer/handler's able to dispose of the reserve on favorable terms, that also is not shared with the rest of the pool.

Q. Right, but it's a risk either way?

A. Yes.

Q. Right. And that's a function of the market at that time, not the function of the regulation?

A. Well, in most respects, yes, but in one respect, no. A producer/handler could dispose of milk into an unpooled class one outlet and in effect get the class one return, but a pool handler would not be able to do that.

Q. Another advantage that a 7A plant is that it has a, in a sense, a fixed cost for its class one milk, irrespective of what the actual cost to produce that milk is?

A. That is correct.

Q. And a producer/handler doesn't have that benefit. Their costs for that milk ultimately is really what it cost to produce it, right?

A. Yeah, and that depends on the accounting systems that they apply. If they use enterprise accounting, then the transfer price can be anywhere between the blend and the class one. However, if the -- if it's a whole enterprise accounting, then the cost is -- all the input costs associated with both milk production and milk processing and the revenues that accrue both through milk processing and selling cold dairy cows or whatever.

Q. But ultimately it's always a single entity -- enterprise, because the profit or loss is based -- and their long-term viability is on the whole operation, right? They may isolate where there's -- they're apt to control it, --

A. Yeah, yeah.

Q. -- but ultimately --

A. I think it would be useful for management information purposes to know how the two enterprises are doing, but you're correct, that the ultimate success of the operation depends on both parts of it.

Q. So we've identified, and there may be some others, but there are -- between a regulated 7A paying minimum prices and a producer/handler plant who is regulated, but not paying 7A plants, that there is a difference in the benefits that the order provides -- a 7A plant that does not provide a producer/handler, right?

A. I would agree that there's some marginal benefits, for example, in flexibility of milk supply and maybe ease of surplus disposal that may not be available to a producer/handler. But I view these as being very small and insignificant relative to not having to account to the pool at the minimum order prices.

Q. You don't think that there's not a dollar value, a 50 cent value --

A. Well, there's some value, but I've never made any attempt to calculate it.
Q. But hasn't the secretary used some of that in determining the value of class one?
A. That I don't know. That I don't know.
Q. You -- over on page -- well, item number seven in your outline, you talk about this movement of units to a producer/handler as opposed to a -- the regulated scheme of individual producers selling to a 7A --
A. The movement of what?
Q. The movement from the traditional 7A plants, that buy milk from producers at minimum prices, to a producer/handler, right? Isn't that talked about in seven, why there's not more bigger producer/handlers, there's a great advantage --
A. Oh, I see. You mean where they change the nature of their operation --
Q. Right.
A. -- to become eligible. Yes.
Q. You know, you've testified at length, and I think there's been a lot of testimony at this hearing that talks about, or at least suggests this huge advantage between a producer/handler --
A. Uh-huh.
Q. -- and another. And I think if the numbers were

believed, it really is. It could be 10 or 15 percent of the value of the milk, right?

A. Yes.

Q. Okay. And that's -- in dairy -- of your years of experience, that's a significant number, right?

A. Yes.

Q. All right. And you used to work with Land O' Lakes, I believe?

A. That's correct.

Q. And producers move from coop to coop, and that was in the upper Midwest, right?

A. Yes.

Q. And they moved from coop to coop for a nickel or a dime, didn't they?

A. Easily.

Q. All right.

A. Easily.

Q. So if there is, in fact, this kind of number out there, you really would expect, as an economist, to see a substantial movement into this direction, right?

A. You would expect the people who were in the best position to make the shift to do it first. For example, if I learned that opera singers were making a million dollars a year, it would take a while before I would become an opera singer, because I would need a lot of training and to develop my skills.

Q. You would have hope. I wouldn't have any.

A. But it -- the talent that a person possesses may not fit a producer/handler operation. The investment's already made may still have a long life to them, and I may have difficulty disposing of them, and I'm better off to continue to operate them rather than to reinvest into something else.

But it's -- it is difficult to shift resources from one type of business to another. Human resources, physical resources.

Q. But from a new entrant (phon.) standpoint, they don't share that burden of having --

A. Yes, when someone -- well, at least with the physical resources, they can -- if they're deciding to get into the business, this would be one of the options, but they also have the -- have to have the talent to apply to that activity as well.

Q. And I think there was -- and you would agree, would you not, the spread between the class one and the blend price contributes to the attractiveness of wanting to go to a PD, right?

A. Yes, the wider the spread, the more attractive it becomes to become a PD.

Q. Now, you go on to make this next statement that at some point, equilibrium -- I'm not -- kind of paraphrasing, --

A. Uh-huh.

Q. -- but at some point the advantage begins to decrease as more people come in, and there's kind of an arbitrage that goes on, and it balances out and equilibrium has been established, right?

A. Well, the process that I would anticipate would be, as more and bigger producer/handlers enter into a market, they will eventually destroy the firms who were fully subject to the regulation, and then they're left with an unregulated environment, which is producer/handlers. Then equilibrium would be established. I think that would represent disorderly marketing because the regulated firms do not enjoy the same beneficial terms of trade as the producer/handlers.

Q. Over on the end of paragraph nine, or section nine, you say that if plants supply milk at a lower cost, society benefits.

A. Well, that's the definition of economic efficiency, is to get either the same outputs of goods and services at a lower cost, or to get more goods and services for the same resources.

Q. I have just one final line I want to ask. Over on your last page, you make the statement, "A producer/handler has a high degree of control over both the volume and variation of monthly milk production. This idea of shifting cows back and forth, has there been any testimony that their shifting of cows back and forth?

A. I don't know. No, there's been no testimony. If I was a producer/handler, I would think about that, and not necessarily between my own farms. I could shift to my neighbor who's on the pool. I -- and I don't know the economics of that, whether it's economically feasible, but it seems like a strategy that could modify the milk supply.

Q. But isn't that a situation where the definition of being in their sole risk and control seems to be modified, and the secretary already has the authority to regulate that aspect?

A. I don't know that the secretary has exercised her authority if she does have it. I don't know of any limitations that have been placed on the sale of animals or the purchase of animals by a producer or a producer/handler.

Q. Do you have any evidence that that's going on now?

A. I don't have any direct knowledge of it. It just -- part of my life as a dairy economist is to try to figure out what you can do and be successful under the regulations.

Q. Sometimes that's my rule as a lawyer.
A. Yes.
MR. YALE: All right. Thank you very much.
THE COURT: You can go, Mr. Ricciardi, if you're ready.
MR. RICCIARDI: May I proceed, Judge, and --
THE COURT: If he's ready, and you're ready, then I guess we're ready.
MR. YALE: I'll get my glass off of there so he doesn't.

EXAMINATION

BY MR. RICCIARDI:
Q. Al Ricciardi for Sarah Farms.
Mr. Christ, you are here as an advocate for Dean Foods to make the case for Dean Foods, correct?
A. That's how I view my role, yes.
Q. Okay. Would you agree with me that rather than being a "marginal player," that Dean Foods, in fact, is the significant player, or one of the significant players in the dairy industry of the United States?
A. Dean Foods Company is a big fluid milk operator, but, you know, the only areas of the United States that are subject of interest here are Federal Orders 124 and Federal Orders No. 131, and I believe in these markets, they're not a major factor.

Q. In the United States and the dairy industry overall, they're a significant player, correct?
A. Oh, the dairy industry's very big when you count cheese and butter and powder and everything else, and milk production. They're a large, fluid milk operator and have been for many years.
Q. Land O' Lakes is a significant player in the overall dairy industry in this country, correct?
A. Yeah, significant is a relative term. Land O' Lakes had eight percent of the national milk supply.
Q. As is marginal, but we're dicing between those --
A. Uh-huh.
Q. -- standards.
DFA's also a significant player, correct?
A. Yes, I would agree so.
Q. Now, your definition -- one of your definitions, which I wrote down, of disorderly marketing, and by the way, that's your definition, correct?
A. That's correct. I didn't lift that from anybody.
Q. You said, nor -- and you didn't lift it from the secretary, because the secretary's never used it, correct?
A. She may have, but I don't remember that she has.
Q. Okay. Now, the definition, one of them, that you used was, and you'll correct me because I think I wrote it down correctly, but I may be wrong. Where the regulatory

terms of trade are not equal, is that one of your definitions?

A. That's correct.

Q. Okay. Now, you would agree with me that the regulatory terms based upon your testimony have not been equal concerning producer/handlers and regulated handlers for the last 40 years?

A. I would agree with that, and it's also true relative to producer/handlers and producers.

Q. And that would be -- that would have existed, this disorderly marketing existed, in your opinion, back in '99 and 2000, during the time of order reform, correct?

A. That's correct.

Q. So obviously, the secretary disagreed with at least your definition and your conclusion, correct?

A. I'm trying to remember if I -- I don't know that I was ever actively involved in a producer/handler dispute other than this. I believe that I did file a proposal to limit the size of producer/handlers in federal order reform, but I can't remember for certain whether it got beyond negotiating stage with other organizations or not.

But one issue related to that is, as exhibit in my testimony is that it's tolerable if it's insignificant if it has a negligible affect on the other participants in the market, and at least in the markets where I had an influence in Land O' Lakes, it was insignificant.

Q. And this, as I understand it from your last answer, this is sort of the first attempt, 131 and 124, and then what's going to happen is, there going to be an attempt to change all of the orders on a nation-wide basis, correct?

A. That may or may not be true. This is the first attempt that I've been involved in.

Q. Tell me the significant changes that have occurred in 131 and 124 since '99/2000.

A. Well, as has already been mentioned, one of the important changes is the smaller number and the much larger size of dairy farms. The smaller number and generally larger sizes of plant operations. Those things are occurring across the country, but in particular, in the West. I don't know of any -- looking at the market statistics for the last few years, the -- I believe that these exempt plants have grown influence in the Arizona/Las Vegas market, but they've stayed about the same in the last few years in importance in the Pacific Northwest.

Q. Tell me the increase in numbers in producer/handlers in the 124 area since '99/2000.

A. I would have to refer to the statistics provided by the market administrator. My suspicion is that there are fewer producer/handlers. When you look at the volumes of milk accounted by these non-pool plants, it's stayed about the same.

Q. Tell me the significance in the change in the number of producer/handlers in the 131 area since '99/2000. And if you have to review to the statistics, --

A. I would have to refer to the statistics on that. I remember the testimony in Phoenix. I think there may have been one more producer/handler a few years back.

Q. Using your opera singer example, the fact is that someone may have a talent to be good as a producer/handler, and another person may not, correct?

A. That's correct, yes.

Q. And there may be also luck involved. They may be at the right place at the right time, correct?

A. Correct.

Q. And there's also the question of effort. That is, things like the number of hours worked. For example, a producer/handler who works half a day may consider 12 to 15 hours to be half a day.

A. That's correct.

Q. And all --

A. All those could enhance success.

Q. And, in fact, those have nothing to do with the price of milk. They have to do with the three things that you just mentioned, talent, luck, and effort, correct?

A. Correct. And those sources of success are outside the scope of the regulatory program, and more power to whoever benefits from them.

Q. And they apply equally to every industry in this country, correct?

A. That's correct.

Q. And even if there is universality and uniformity, the fact is that one person, if he has talent and luck and effort, and the other person who doesn't, one may succeed, the other may not?

A. That's correct.

Q. By the way, there is no sale between the producer/handler and himself, correct?

MR. ENGLISH: Objection. Charles English for Dean Foods and Shamrock Foods. That calls for a legal conclusion and has been answered by the Third Circuit and Ideal Farms, and that is just not simply a state of the law. So don't say something that isn't (indiscernible)

MR. RICCIARDI: You know what? Why don't you make an objection and allow this witness to answer, and stop giving speaking information --

THE COURT: Go on, go on, go on --

MR. RICCIARDI: -- and stop telling him what to say.

MR. ENGLISH: I object to (indiscernible) calls for a legal conclusion. That's my objection. I have a right to.

MR. RICCIARDI: Yeah, well make your objection and stop telling him what to say.

MR. ENGLISH: I'm not telling him what to say.

MR. RICCIARDI: You did. You just gave it to him.

MR. ENGLISH: I gave my objection. I have a right to make my objection, sir.

MR. RICCIARDI: All right. Make your objection.

THE COURT: Come on, stop this. Stop this.

MR. ENGLISH: I object, Your Honor.

MR. RICCIARDI: Get away from me. I'm --

MR. ENGLISH: Your Honor, now I have a different objection.

THE COURT: Okay.

MR. RICCIARDI: Well, you just bumped me.

THE COURT: Okay. I'm calling a --

MR. ENGLISH: I didn't bump you.

THE COURT: I'm calling (indiscernible) recess right now. Off the record.

(Off the record and reconvened.)

THE COURT: Okay. Let's go back on the record. It's 20 minutes after 5:00. Everyone have a seat, please. We're going -- we're back on the record.

Just a couple -- two or three preliminary things. Okay? I'm not even going to address what just happened before I had to call this recess. We're going to go -- we're going to just skip that.

But one is, I've been told that the current witness, Mr. Christ, is going to be the last witness for the proponent. So we're going to -- and I've also been told that -- Mr. Yale at one time had told me that he wanted to have somebody testify today, and now he says no. And -- yes, Mr. Beshore?

MR. BESHORE: The only caveat, subject to Mr. Hollon possibly coming back to testify about the changes, possible additional language, fine tuning, that had been reserved previously.

THE COURT: Okay. Well, at this point I'm inclined to think that we probably shouldn't do that today.

MR. BESHORE: Not today. No, no.

THE COURT: No. We might have a few --

MR. UNIDENTIFIED: I thought you meant period.

THE COURT: No, no. Well, no, this is the end of the case in -- well, then impression I was given about -- given just talking in the hallways the last -- well, this is the end of the proponent's basic case in chief, that they may want to -- that does not have anything -- that there may be one or two rebuttal witnesses --

MR. UNIDENTIFIED: (Indiscernible) subject to Mr. Hollon --

THE COURT: Yeah, subject to whatever is called later on. So I'm going -- so -- and before I get back to resume the questioning, I also want to say that, you know, tomorrow -- so we're not going to go till 7:30 today, unless this part of the thing goes a lot longer than we hope. And so we'll start with a (indiscernible) normal time of 8:30 tomorrow.

What I would ask people to think about is, it's become right evident to me that once again, we're probably not going to finish this by 11:00 or 11:30 on Friday morning, and what I want you to think about -- well, I want you to have your calendars, those people who are sure they're going to want to be here. I also want you to think of appropriate location for the remainder of the hearing. I don't know how far we're going to get in the next two days. I don't know if the direct and cross have the witnesses for the opponents who's going to be fast, shorter or longer than we've had thus far. I have no way of knowing that myself.

So I just -- well, I just want to maybe tomorrow afternoon, we'll think about -- go over it for the first time maybe during the afternoon -- an afternoon break. We'll go off the record, and we'll try to figure out with calendars and get some ideas on location. I know originally I was talking about, like -- in Phoenix, I was mentioning finishing up in Alexandria. I'm not sure that that's -- well, it may work out the best for me. I don't know if that's the best for everybody.

MR. UNIDENTIFIED: That's a question that I was going to ask you. Are we frozen into the idea of having to go to Alexandria?

THE COURT: We're not frozen to anything. We're frozen -- I'm frozen into the idea that we're going to have to finish this hearing one of these days, and --

MR. UNIDENTIFIED: (Indiscernible) If we're not firmly committed (indiscernible) by the Department.

THE COURT: No, there's no commitments at all right now. That was an -- that was something that a person who should remain nameless and was, or is in this room, suggested to me back when we were in Phoenix, and it became clear that we weren't going to finish there.

MR. UNIDENTIFIED: (Indiscernible)

THE COURT: Well, anyway, I just want -- so I just want people to think, you know, talk to your -- the people you represent, figure out how many witnesses you're going to have left over, and the travel costs, and -- et cetera, and we'll take it -- we'll talk about it on Wednesday, try to make a decision maybe by -- before we close on Thursday on where we're going to go next.

Mr. Beshore?

MR. BESHORE: Rather than throwing in the towel immediately on the week's efforts, we were scheduled to go till 7:30 tonight. And just because the proponents are done, the opponents have 20 witnesses or whatever on the list, I don't see any reason why we can't start and --

THE COURT: Well, yeah, the only person -- you're the only person who I've talked -- who's talked to me whose said anything like that, Mr. Beshore. Everyone else is telling me, can we please stop after this witness, and I've heard it from both sides of the isle that that's what they'd like to do. So, you know, maybe we'll still end up going till after 6:00 tonight. We can plan on that doing that tomorrow, but I'm happy to go on, but it seems like you and I are the only ones who are happy to do that right now.

MR. UNIDENTIFIED: (Indiscernible)

THE COURT: Oh, okay. See, look at that. I think we're going to stop after this witness. I think it's a logical place to stop. We can go late tomorrow, I mean, unless you want to walk out in the rain, we might as well stay here, right? So let's do it that way.

Now, I'm going to let him ask -- answer your question if he, by some remote chance, remembers what it was, because I think that that was part of his direct testimony, even though that might have been resolved in some case. He spoke to that in his direct, and I'm going to allow him to answer it.

BY MR. RICCIARDI:

Q. Do you remember what the question was?

A. Let me see if I can recite it roughly --

THE COURT: Well, why don't we just have Mr. Ricciardi --

THE WITNESS: Okay.

THE COURT: -- re-ask the question.

MR. RICCIARDI: Well, first of all, Judge, while you haven't addressed it, I will address it, and certainly want to apologize to Mr. English. I want to apologize to the Court. These days are long, and tempers get short. And so I'll try to make sure that we don't have that issue again, and maintain my professionalism.

BY MR. RICCIARDI:

Q. Now, Mr. Christ -- and I beg your indulgence. My question, I think, was, and I didn't formulate it very well before. I'll try it now.

Isn't it true that when you have a producer/handler that there is no sale between the producer side and the handler side?

A. That's correct. There's no arms length transaction, and there may be, I guess, a hypothetical sale in the form of a transfer price so that the performance of each of the two sub-enterprises can be measured.

Q. Not a legal, but a hypothetical sale, correct?

A. Uh-huh. Uh-huh.

Q. Is that a yes?

A. Yes.

Q. Okay. Let me go through some of the portions of your testimony, and I have, for my convenience, marked the pages of your testimony one through six. Everybody's actually going to --

A. Mine are marked the same way now.

Q. Everybody's gone to school, so I see they're going through and doing what I asked. That's nice. Good.

Question is, the top of page two when you talk about certain exemptions, --

A. Yes.

Q. -- (a) through (d), you indicate -- you conclude that only the plants located in Clark County have a "legal right" to be exempted from regulation. You're trying to make a distinction between what is a legal right and administrative convenience; is that --

A. Yes, that's correct.

Q. -- what I understand?

Isn't it true that with regard to Clark County, that we're talking political expedience as opposed to legal rights?'

A. Well, as I understand it, there's been legislation adopted that exempts plant in Clark County from any farm or federal milk order regulation.

Q. And that would be the Dean Foods plant that's being built?

A. Dean Foods does not -- I don't know of any plant in Clark County.

Q. Did you know that there is one being built --

A. I heard testimony in Phoenix that there are plans related to a new plant, and I also heard testimony that they are supporting legislation to get rid of that exemption.

Q. Have you also heard recently that they are backing off on supporting that legislation?

A. No, I have no knowledge of that.

Q. Your opinion, as I understand it, and this is about the middle of page three, but it's not important that you refer to unless you need to, is essentially that if everything is equal, literally, that a producer/handler wins the competitive race over a regulated handler, correct?

A. And a pool participant producer. That's correct.

Q. Okay. And if that -- and based upon your testimony also, given your definition of disorderly marketing that's gone back 40 years or so, what you're telling me is that there should be a significant number of producer/handlers. In fact, those producer/handlers should outstrip the regulated handlers, correct?

A. I'm not sure about that. As I mentioned, it's difficult to move resources from one enterprise to another, and I believe it takes some specialized talent to be able to operate a producer enterprise -- a producer/handler enterprise, and not everybody has that talent.

Another thing that enhances the attractiveness of being a producer/handler is the increasing difference between the class one price and the blend price.

Q. Well, we've had -- you have increasing differences between class one and blend prices over the last 40 or 50 years, right?

A. No, the utilization of the -- in the federal milk order has dropped over my lifetime experience with the federal milk order program. That means that the differences have gotten larger.

Q. One of the other reasons why we don't have a significant number of producer/handlers is the significant risk factor to the producer/handler in being both the producer and the handler, correct?

A. Well, there's more a management risk, I think, in trying to operate two different types of enterprises. It takes maybe a little different kind of management skill --

Q. It also --

A. -- to do that. But there -- as I mentioned in the testimony, there's also the regulatory risk that this exemption may go away some day.

Q. Of course, I've heard that before. That exemptions go away or things get changed all of the time, right?

A. Yes, that's correct, and a lot of amendments have taken place in the federal milk order system.

Q. Of course, there has been no change in the federal order system with regard to the issue of the exemption of the producer/handler, correct?

A. Well, one of the reasons for that, I believe, that there has not been any significant change is that we've had a series of legislative directives with the farm bills, not to change the status, that legislative directive was not renewed in the 1996 farm bill.

Q. And there was no change in '99/2000 in order reform, correct?

A. No.

Q. And another reason why there are not as many producer/handlers is because there are significant capital has to be expended for both the dairy side and the production side, correct?

A. Well, it depends on the size of the enterprise, of course, but clearly it takes more capital to establish -- it probably takes no more capital to establish an integrated dairy farm and -- with a processing plant than what it would take to establish the same size dairy farm and the same size processing plant. It depends on the size of the activity.

Q. Well, and the concern that you've expressed is that producer/handlers are becoming larger. So to the extent that there is going to be a larger producer/handler, there would be more capital risk, correct?

A. I would expect that there's more capital investment given the larger size of the enterprise.

Q. If a producer/handler is only a producer/handler and does not have any type of a pooled farm, he or she does not have a higher degree of control over the volume and variation in monthly milk production over anybody else, correct?

A. I'm not sure that I would agree -- I don't agree with that, that the -- a dairy farmer in a market-wide pool will get the same price for his milk no matter how much he sells. He'll get the blend price.

A producer/handler as a producer will get a high price, presumably from the class one market, for the milk he puts into the bottle, and he probably will get a lower price for any additional milk. So he has a greater incentive not to increase milk production beyond his class one needs.

Q. In terms of the -- we're not going to talk about balancing and balancing costs. In terms of balancing and balancing costs, all of those issues fall directly on the shoulders of the producer/handler, correct?

A. The cost of balancing his own milk supply with his own class one needs falls on his shoulders, and they may be smaller, or they may be as high as the market-wide pool experience.

Q. And, in fact, if his production is higher than the required output, then he's got to feed the milk to his cows or dump it down the drain, correct?

A. He would sell it to the highest -- he would market it to the highest valued use, and that would occur if and only if he had no higher valued market opportunity.

Q. And if he had no opportunity at all with regard to the milk, then he'd have to get rid of it by dumping it down the drain, right?

A. But that's true of any dairy farmer. No dairy farmer's guaranteed a market in a federal milk marketing order. If he finds a market, a pool outlet for his milk, then he participates in the blend price, but he's not guaranteed a market.

Q. He's guaranteed a certain price?

A. If he finds a pool outlet for his milk, yes, he's guaranteed the blend price.

Q. You also indicated at the bottom of your testimony on what is page six as I've marked it, that a regulated handler can't sell any reserve milk in a non-pool class one market. Is that your testimony?

A. He can sell it in an un-pool class one market, but he has to account to the pool at the class one price, so --

Q. So, for example -- I apologize. Did --

A. No.

Q. -- I interrupt you?

A. No, that's fine.

Q. Okay. So, for example, if you wanted to sell milk into California and you produced milk in Arizona like Shamrock does, you could do that, right?

A. Yeah, if they processed package milk in Arizona, they can sell it in California. You know, there are other complications associated with that, but they will have to account to the Arizona/Las Vegas pool at the class one price.

Q. So they -- but they could sell the reserve milk into California, right?

A. They -- well, that would not be reserve, that would be class one use.

Q. Class one use. Okay.

A. Yeah, that would be class one use.

Q. Now, you don't have any specific information concerning the cost of operation for Sarah Farms, correct?

A. I do not.

Q. Okay. And you don't know, for example, what it cost them to produce their milk on the farm, or what it cost them to process their milk at the plant, correct?

A. I do not, and I do not know that about any other producer or any other handler in the market.

Q. Okay. Are you aware that -- and actually, let me preface this by asking you to turn to the top of page four of your testimony.

A. Okay.

Q. Your assertion there is that a penny per hundredweight reduction in the blend price is not trivial, and that's your opinion, right?

A. That's my opinion, but it's based on my experience of facing farmers face-to-face for 26 years at Land O' Lakes.

Q. Understand.

A. Uh-huh.

Q. But that's your opinion, --

A. Uh-huh.
Q. -- a penny is important --
A. Uh-huh.
Q. -- in milk pricing, --
A. Uh-huh.
Q. -- correct?
A. That's correct. It's an observable difference.
Q. So I would assume that 15 cents assessment would also be a significant amount. In fact, 15 times more, and therefore more than not trivial, significant?
A. I would argue the dairy farmers are attentive to any difference in price.
Q. Are you aware that there's a 15 cent assessment for the promotion of milk and milk products that is taken out of each producer's cost --
A. Yes, and the National Dairy Promotion Program assessment is 15 cents.
Q. And in 2001 and 2002, about a third of that went to the promotion of fluid products, and about two thirds to cheese, correct?
A. Okay. I don't know the allocation of the promotion dollars. You know, they're divided between regional promotion agencies and the National Dairy Board.
Q. Then let's talk hypothetically.
A. Uh-huh.

Q. If you assume that two thirds, in fact, went to the promotion of cheese, would you believe that that would potentially lead to the increase in the production of cheese products?

A. Okay. That's a complicated question to answer. Okay. If promotion for cheese is effective, I would expect that the demand for cheese to rise. The demand for cheese -- a rise in the demand for cheese can be manifested in two ways. One is through increased production, and the other is through higher prices.

I would think that if -- and the initial affect would be higher prices for cheese, which in turn would cause class one prices to rise through the federal order pricing mechanism. With higher prices for both class one and cheese, then you're likely to get more milk production and more cheese production. So through a series of linkages, yes, you're likely to get more cheese production.

Q. And if you were to get more cheese production, that might have the potential to lower the blend price for fluid milk, correct?

A. Not in -- I would argue, not necessarily. Depends on how much price increase was associated with the increase in demand for cheese. It could offset the affects of a bigger percentage of milk being used in cheese.

Q. But if, in fact, what you did was, you got increase use production of cheese and a decrease, therefore, in the production of milk on the fluid level, you would lower the blend price, and therefore create disorderly marketing, correct?

A. That would be correct, and I -- okay. I will first talk to your logic. If you increase a proportion of the milk supply that in class three and reduce the proportion as class one, all else being equal, you'd have a reduction in blend price. But you would not likely to get that shift unless you had some incentive for producers to increase milk production, and that would be the higher price resulting from the higher demand for cheese.

Now, the second part of that question I don't think I agree with at all. It doesn't match either of my definitions of disorderly marketing, the fact that the price went down. That's a normal market phenomena associated with changes in supply and demand.

Q. So a reduction in blend price is normal, not necessarily disorderly marketing, correct?

A. If it's associated with normal economic incentives.

Q. So even though there's -- in my hypothetical there's a reduction in the blend price, your testimony is that that is not necessarily disorderly marketing?

A. No.

Q. And even though there's 15 cents taken out of the hundredweight, which is certainly not trivial based upon your testimony, that is not anything that you would attribute to the potential for disorderly marketing, correct?

A. Okay. The 15 cents is not trivial, yes. Okay. The question is, does it result in higher prices or lower prices? The reason producers have affirmed and reaffirmed the National Dairy Promotion Program is that they believe that it does result in higher prices, and that would be favorable for producers. But it is not disorderly marketing from the standpoint that it has a different terms of trade for different participants in the market.

Q. Does a producer/handler pay the 15 cents per hundredweight?

A. I believe he does.

MR. RICCIARDI: Thanks.

THE COURT: Ms. Deskins, you or Mr. Rower have any questions?

MR. UNIDENTIFIED: (Indiscernible)

THE COURT: Just working my way around. Do you have any questions?

MS. DESKINS: I don't have any questions.

THE COURT: Okay. Go ahead, Mr. Berde. You had something? All right.

EXAMINATION

BY MR. BERDE:

Q. Sydney Berde.

Do you know of any circumstance, Mr. Christ, that would compel a producer/handler to dump milk down the drain because of his inability to dispose of whatever he has to dispose of as raw milk, and a revenue producing transaction?

A. My answer is, I don't know of it actually happening. I've heard of milk being dumped for other reasons, but not by producer/handlers, and a rational producer/handler would do that if and only if he had no other higher valued market for the milk.

Q. Do you know of any reason why in the Arizona/Las Vegas marketing area adjacent to California, and adjacent to manufacturing outlets, and class one outlets, why such an occurrence could happen?

A. I personally don't know of any situation like that.

MR. BERDE: Thank you.

THE COURT: Mr. Marshall?

MR. MARSHALL: Thank you, Your Honor. Doug Marshall, Northwest Dairy Association.

EXAMINATION

BY MR. MARSHALL:

Q. Paul, on the recent discussion with Mr. Ricciardi regarding the 15 cent promotion value?

A. Yes.

Q. The hypothetical he posed to you was that more class three might mean less milk used in class one.

A. I don't think it was less milk in class one, a smaller percentage of milk in class one. That's how I viewed the question.

Q. Is it not possible that the amount of milk in the pool might not change -- the amount of milk in class one might not change, the percentage of milk in class one might not change, but the amount of milk shifted from four to three would be the change?

A. That's possible. That's possible, depending on the relative values of milk in class three and class four.

Q. I'd like to go back to Mr. Yale's examination of you and a very interesting discussion about a whole number of items. I appreciate it very much a chance to witness it. It was most educational.

One part that I was confused on, and I wrote down the question that I think you were asked, the thrust of which was that a 7A handler -- I think you were asked, could a 7A handler put onto the pool the cost of the balancing, and you referred to some ebbs and flows, but it wasn't real clear to me what all you're referring to there.

I'd like to talk just a bit about balancing as we have with witnesses earlier in the hearing.

Balancing costs, the term "balancing" and "balancing costs" refers to what as you understand the term?

A. Okay. I think there are two aspects of the balancing situation. One is, disposing of milk, not neither for class one into lower valued use as class two, class three, and class four. And the cost of that is reflected in the difference between the class one price and the blend price to producers.

There's another aspect of balancing, and that is, the impact on plant utilization and manufacturing plants that absorb the class two, class three, and class four milk. Now, the first part is reflected -- the lower prices for the lower classes of milk is reflected in the blend price. The second part of balancing, the lower level of capacity utilization is associated with balancing is not reflected in federal milk order prices.

Q. And as you were discussing balancing with Mr. Yale, I think you agreed that the burden of the reserve supply in lower classes of use was shared in the pool, but, as I understand what you're saying now, then the discussion about did not include the cost of ebbs and flows in the volume of milk processed at balancing plants?

A. That's correct. To the degree that the supply of milk to a manufacturing plant is more variable than the milk supply in general, the plant experiences a lower level of capacity utilization than it would with no interaction with the fluid market.

Q. And in your experience, is that cost associated with fluctuations and capacity utilization issues typically recovered, if at all, through over-order charges, rather than through the federal order system?

A. If they're recovered at all, those costs would be recovered through over-order charges. My experience has been that there's a very poor correlation because over-order charges reflect much more than the cost of balancing. They reflect the relative market power as well as the availability of competing supplies of milk.

Q. In drawing a comparison between the balancing problem faced by a producer/handler with respect to ebbs and flows in his class one or bottled milk demands, and comparing his balancing costs with the balancing costs absorbed by the pool handlers as a group, including the manufacturing plants, would you agree that the costs of those fluctuations are not intended to be born by the federal order system?

A. I'm not sure I agree fully with you that we've had legislative change that permits the adoption of market-wide service payments in federal milk orders, which would or could reflect these -- this effect on capacity utilization. So far it has not been done.

Q. I appreciate that correction. You're quite right.

Absent those formal attempts to capture within the order -- an order a specific type of market-wide balancing cost, would you agree that the problem of handling fluctuating demands of a producer/handler plant and the problem of handling the fluctuating demands of class one plants of 7A handlers should be analyzed outside the federal order system until the system changes?

A. I have difficulty answering because I guess I don't have an opinion on, you know, whether it should be analyzed within or without the federal order system.

Q. Well, let me --

A. I guess maybe I don't understand the question.

Q. Yeah. Excuse me for interrupting there. Maybe I should break it down.

It's -- do you agree that the costs of balancing fluctuating supplies of milk to the market to the pool and the fluctuating demand of bottling plants through the seasons of the year is not currently intended to be part of the federal order pricing system?

A. Given the current status of federal milk order decisions, none have adopted balancing payments, so -- and clearly then, it's not the intend of the secretary to do that at this point.

Q. Right. So is there any reason as you would see federal order theory for such balancing costs to be considered in evaluating the appropriateness of regulating producer/handler plants above or below a three million pound limit based on their costs? It's outside the federal order system --

A. Yeah, I guess --

Q. -- 7A plant, is it not also --

A. Yeah, I'm trying to trace through whether there's any relevance that applies to producer/handlers, which is different in kind that the relevance that applies to regulated plants, and I don't see any on the surface, yes. I don't see any difference.

MR. MARSHALL: Great. Thank you very much, Mr. Christ.

THE COURT: Mr. Beshore?

EXAMINATION

BY MR. BESHORE:

Q. Marvin Beshore for Dairy Farmers of America.

Mr. Christ, you were asked a number of questions about the federal -- so called federal order reform rule changes which took place in 1999 or January 1, 2000; do you recall that, by Mr. Ricciardi, I think, and perhaps Mr. Yale?

Are you aware that in those decisions the secretary announced an explicit intention not to promulgate regulations which would change the regulatory status of any parties?

A. I don't remember seeing that explicit statement, but I would agree that that is -- that was the outcome.

Q. Okay. And, in fact, marketing areas were not changed so that they -- so that any new parties became regulated. You're aware of that?

A. I knew there was an attempt not to regulate any new parties.

Q. Okay. And pooling provisions were the so called lowest, common provision was adopted in many areas so that there wouldn't be changes in, you know, in regulatory exclusion of milk previously regulated, things of that sort?

A. Well, the pooling requirements were changed, but yes, maybe they did adopt the lowest, common denominator, but it had -- did have a significant impact on the ability to pool different markets.

Q. But in the permissive sense as opposed to the exclusive sense?

A. Yes.

Q. Okay. If the decisions -- if the secretary stated in those -- explicitly in those decisions that there was an intention not to change the regulatory status of handlers, in effect, any changes in the producer/handler regulations that would have regulated new producer/handlers were not even on the table, fair?

A. Well, same line of reasoning, that would be consistent reasoning. I was not very attentive to that particular feature of the decision, but the logic, it would be consistent.

Q. So if they weren't on the table, the fact that they weren't adopted doesn't have a lot of materiality?

A. And maybe that's why my interest in, you know, producer/handler proposal got lost somewhere. I don't know.

Q. Okay. Just one other question.

Does your -- the term "disorderly marketing," which you've defined, is that defined in any of the economic textbooks that you consult in your academic --

A. No, I think disorderly marketing is relative only in a regulatory environment. There are other -- I guess, you could argue that there are a lot of sources of inefficiency in non-regulated markets, related to monopoly or monopsony or oligopoly, those sorts of things. There are number of sources of inefficiency, but I think orderly marketing or disorderly marketing is a consequence of regulation.

Q. But isn't that -- as we use the term in this context, isn't it language that specifically in this statute, the agricultural --

A. Yes, the Secretary of Agricultural has an obligation to reduce or correct disorderly marketing conditions.

Q. Because those words are in the statute?

A. That's correct.

Q. That authorizes --

A. I read the statute not recently, but I recall those words.

MR. BESHORE: Thank you.

THE COURT: Mr. English, do you have any --

MR. ENGLISH: Yes, I have one or two questions.

THE COURT: Step on up.

EXAMINATION

BY MR. ENGLISH:

Q. You were asked a series of questions, I believe, by Mr. Yale having to do with 7A provisions versus the requirements of a producer/handler. Do you remember those questions?

A. Yes.

Q. If the -- as an economist, if the costs associated with being a producer/handler, that it to say, the lack of flexibility as opposed to a 7A, the costs of balancing, all of those issues that you discussed with Mr. Yale, if those costs exceeded the benefit of not paying the class one price to the pool, accounting for the pool, what is your opinion would happen?

A. Well, a rational decision maker would choose to become a regulated handler rather than a producer/handler, if the costs of being a producer/handler were greater than the benefits.

Q. And if notwithstanding that, the producer/handler chose to nonetheless remain a producer/handler, is that the kind of inefficiency that is disorderly marketing under your second definition?

A. I would not generalize quite that far because there's all the issues of some capital, past decisions, commitments, and those sorts of things. But in the long run, yeah, his inability to shift in the long run, I wouldn't call it disorderly marketing, but I would call it making less than optimal decisions.

MR. ENGLISH: Thank you, sir.

THE COURT: Anything else?

MR. UNIDENTIFIED: (Indiscernible)

THE COURT: You may step down.

THE WITNESS: Thank you.

THE COURT: And I got about three minutes to 6:00. An hour and a half earlier than the farmers, but I think it's a good time to call it a day. I'll see everyone at 8:30 tomorrow morning. We'll have the opponent's case.

Off the record.

(Whereupon, the proceedings were recessed at 5:57 p.m.)

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