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BEFORE THE SECRETARY OF AGRICULTURE

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P R O C E E D I N G S

8:30 a.m.

1
2
3 THE COURT: Okay. Good morning, everybody.
4 We're on the record right now.

5 And today's November 19th. It's 8:30 in the
6 morning in Seattle. It's the sixth day of our hearing, and
7 at this point, I believe Mr. Yale was going to call --
8 start calling his witnesses; is that correct, Mr. Yale?

9 MR. YALE: Pardon?

10 THE COURT: You're going to call witnesses right

11 --

12 MR. YALE: Yes. We're ready to call --

13 THE COURT: Well, let's have our first witness
14 then.

15 MR. YALE: This is Mr. Benjamin F. Yale on behalf
16 of Smith Dairy, Edaleen Dairy, and Mallory's Dairy, and we
17 call as our first witness Mr. David Beene.

18 MR. BERDE: Could you spell it?

19 MR. YALE: B-e-e-n-e.

20 THE COURT: I'll have -- when I swear them in, I
21 always have them state their name, Mr. Berde, and spell it
22 for us, so we'll get a little ritual here.

23 Please raise your right hand.

24 DAVID BEENE, WITNESS, SWORN

25 THE COURT: And could you please state and spell

1 your name for the record?

2 THE WITNESS: My name is David Beene, spelled B-
3 e-e-n-e.

4 THE COURT: Go ahead, Mr. Yale.

5 EXAMINATION

6 BY MR. YALE:

7 Q. Yeah, Mr. Beene, where do you reside?

8 A. San Antonio, Texas at the present time.

9 Q. And are you presently employed or --

10 A. I am not.

11 Q. Retired?

12 A. I'm retired.

13 Q. Let's give, if you would, to the participants
14 here and to the department a brief biography since your
15 secondary education. Where did you receive any education
16 after school -- high school?

17 A. I attended Baylor University for four years,
18 graduated with a bachelor of business administration.

19 Q. Okay. And what employment did you have after
20 your graduation from Baylor?

21 A. I worked for Sears Roebuck for three years. Then
22 I went to my home town where I grew up, Comanche, Texas,
23 became the Vice-President of Operations of a large
24 retailing firm that sold everything from dry goods to
25 funeral homes to lumber yards, very broad product makes.

1 And then I went to San Antonio as CEO of a large
2 firm that sold building materials. From there I went to a
3 firm called Gore's, Inc. (phon.), prior to their purchase
4 to Pure Milk Company (phon.). I worked for them until I
5 got ready to retire.

6 Went back to San Antonio, and a gentleman owned
7 some -- owned a dairy and a processing plant south of San
8 Antonio asked me to come and be the CEO of that company.
9 And then I retired in '99.

10 Q. Now, Gore's, Inc., what is Gore's, Inc.?

11 A. Gore's, Inc. is a integrated, agricultural
12 operation. When I went there they had large feed mill, had
13 a dairy farm with several different barns, and they have
14 some -- a retail store at that time, retail agricultural
15 products.

16 Q. And then they -- while you were there, they
17 acquired some additional parts to their operation?

18 A. We acquired the Pure Milk Company. It's actually
19 -- the proper name is Pure Milk and Ice Cream Company in
20 Waco, Texas, 100 miles east of the town where we operated,
21 which was Comanche. We also acquired some more feed mill
22 enterprises in New Mexico.

23 Q. Now, are you aware of what the predominant issue
24 is at the hearing today?

25 A. Yes, sir.

1 Q. And what is that issue.

2 A. As I see it, it's to put a cap on
3 producer/handler activity or sales.

4 Q. Do you have an opinion as to whether or not it is
5 necessary to impose -- the secretary to impose a cap on
6 producer/handlers?

7 A. Yes, sir, I do have an opinion.

8 Q. And what is that opinion?

9 A. That opinion is that it's not needed.

10 Q. And do you have a summary of the -- what your
11 testimony is going to be to the secretary today?

12 A. Yes, I do. I have a short summary. Would you
13 like me to read that --

14 Q. Yes, if you could read it.

15 A. "Limitations imposed on how much milk a
16 producer/distributor could buy and where a
17 producer/distributor can sell its milk, coupled with market
18 forces imposes a market created limitation on a
19 producer/distributor."

20 Q. Let's talk -- let's go back to this situation
21 that you mentioned before. What is your relationship to
22 Gore's?

23 A. I had been on the board of directors at Gore's
24 for a number of years, I don't remember how many, when they
25 asked me to come back there. My wife's family actually

1 owned the vast controlling interest in that endeavor, and
2 they felt like I had some management expertise that would
3 help in the growth of the company.

4 Q. And was it predominantly owned by family members?

5 A. Yes, there was a few shares of stock out to some
6 key employees, but outside of that, for all practical
7 purposes, it was a family company.

8 Q. And the key employment positions or the main
9 officers and directors, were those family members?

10 A. Yes.

11 Q. And that included the operation of a dairy farm?

12 A. Yes.

13 Q. And how big was that dairy farm?

14 A. As most dairy farms do, it varied in size. Our
15 peak was close to 5,000 cows.

16 Q. And you said you made a decision to purchase the
17 Pure Milk Company. What was the purpose and the intent of
18 acquiring the Pure Milk and Ice Cream Company?

19 A. Well, outside of temporary insanity, it was that
20 we -- the folks that had built this company prior to my
21 coming to work with them had done an outstanding job of
22 building a very good cattle herd and an extremely good herd
23 health program. They were deeply involved in the embryo
24 transfer program which gave them genetics for some
25 extremely good milk cows, and as I said, the herd health

1 program.

2 Couple those two things together, they were
3 talking about how -- what could they do to maximize the
4 outstanding herd health and the genetics that were in the
5 cows, and came up with the belief that the thing to do in a
6 case like that was try to market that product,
7 differentiate it to the consuming public, and see if they
8 could make it as a producer/distributor.

9 Q. And was the Pure Milk and Ice Cream Company an
10 existing company?

11 A. Yes. Excuse me, I did leave one thing out. They
12 hoped to make money out of it. I mean, obviously there was
13 a motive to improve their class one sales, but yes, Pure
14 Milk was a operating company

15 Q. And who are some of the prior owners of the Pure
16 Milk and Ice Cream Company?

17 A. My understanding is that that actually started as
18 a Borden plant back in the '30s, and it was producing, I
19 believe, the canned milk, the condensed milk. After that,
20 it was -- I'm unclear of who owned it for a number of years
21 in there. There was a Mr. -- oh, a gentleman out of
22 Dallas, I'm sorry, that controlled interest in it, and I
23 can't remember his name at this time, when we bought it.

24 Q. Now, by acquiring the operation of Pure Milk, did
25 that change the status of Pure Milk under the -- at that

1 time, the Texas milk marketing order?

2 A. Yes, it did.

3 Q. And what did that make the Pure Milk Company?

4 A. A producer/distributor.

5 Q. All right. And how many years did you operate
6 the Pure Milk Company as a producer/distributor?

7 A. I can't give exact dates, but it was from some
8 time in 1987 until a date near the end of 1995.

9 Q. Okay. And you were involved in those operations
10 that entire time?

11 A. I was the chief executive officer, yes, of
12 Gore's, Inc..

13 Q. Now, as the CEO of Gore's, Inc. and your -- were
14 you involved in any of the day-to-day operations of the
15 plant and in sales?

16 A. Yes.

17 Q. And were you intimately involved in the decisions
18 that were being made in that -- in operating that business
19 on a day-to-day basis.

20 A. Yes. Operational side of it, other people did
21 most of it. I was not an expert in that at that time, but
22 the financial side and management decisions, yes.

23 Q. When -- describe the Pure Milk Company, if you
24 would, please, to the secretary. I mean, how big was it?
25 I mean, what was its volume of sales --

1 A. Our volume --

2 Q. In milk -- in terms of milk.

3 A. Our volume in milk reached 800,000 gallons a
4 month and held that for a substantial period of time, a
5 year, a little over a year. It was much lower than that
6 when we purchased the plant. It's located, as I said, in
7 Waco and distributed through its own routes. Waco, Temple,
8 Austin, a little in San Antonio, big school business in
9 several different locations, got some military business for
10 a while, and was a -- it was one of the standard old milk
11 companies. Did some serious distribution in one discount
12 retailer.

13 Q. Now, what was the product mix that you made at
14 that plant?

15 A. Product mix was fluid milk in the form of
16 gallons, half gallons, quarts, half pints, pints. We did
17 five gallon bag and box for a while. We did -- that's
18 about all that we did -- well, we made eggnog during the
19 season, buttermilk. Then we had other products that we
20 could and did purvey that were not whole milk, such as we
21 made the ice cream mix that goes to places like Dairy
22 Queens.

23 Q. Now, did your operation as a PD draw any kind of
24 regulatory action?

25 A. Oh, my goodness. Yes, sir.

1 Q. And can you describe what happened?

2 A. We had a hearing much like this, and it was a
3 short time after I joined the company. It was
4 disconcerting, but it was a large hearing in, I believe,
5 Fort Worth, Texas.

6 Q. And what was the nature of the regulatory -- what
7 was being sought to be done there?

8 A. Well, as I remember, it was very similar to this.
9 The sky was going to fall in if we were allowed to be a
10 producer/distributor, and there -- it was going to wreck
11 the market, it was unfair advantage that we had, and that's
12 about it. Very, very similar --

13 Q. All right.

14 A. -- to what I've heard here.

15 Q. And what was the result of that regulatory
16 hearing?

17 A. We were allowed to become a producer/distributor.

18 Q. And in the years that you were a
19 producer/distributor in Texas, did the sky fall in, in that
20 market?

21 A. Well, no, sir, unless it was fall -- fell in on
22 us.

23 Q. And were you involved in any other regulatory
24 situation involving being a PD?

25 A. Well, one I -- one comes to mind. When we were

1 selling a very, very large grocery chain and the milk
2 administrator charged us back with some, I think it was
3 \$315,000 of money because it was felt by the market
4 administrator that we were selling to another distributor,
5 or another processor of milk since this company did process
6 their milk, and our milk was going through their warehouse.
7 not the milk plant, but their warehouse.

8 Q. Was this a significant customer of yours?

9 A. Yes, sir. At that time, it was the largest,
10 single customer we had.

11 Q. And the result of that regulatory action from a
12 regulatory standpoint was what, ultimately?

13 A. Well, I started to say we won the case. We won,
14 and we lost. We lost -- we won with the court side of the
15 case, but in the process, there was so much -- trying to
16 think of words. If you'll excuse me. There was so much
17 activity that involved our customer having to answer
18 questions that they quit using us in the capacity that we
19 were being used.

20 Q. So the fact that you were a PD and the scrutiny
21 that it gave your customer, you being a PD, had the impact
22 of denying you a significant market for your milk?

23 A. Well, for that milk, yes, sir. And that's my
24 opinion, and its based on, you know, what was said to us at
25 the time by our customer. We did not lose that account as

1 a customer, but we lost what we were -- private labeling
2 for them.

3 Q. Now, I want to take your attention over to the
4 competitive situation that you experienced as a -- in that
5 Texas market. First off, let's talk about the cost
6 structure and the cost to produce milk. Do you recall
7 approximately what your -- you considered your standard
8 costs in processing milk were?

9 A. Yes, sir. In our market, we computed standard
10 costs by figuring what we considered all of the production
11 expenses from the time the milk came in the door, or into
12 the silo, until it went out with -- and it included the
13 management of plant. It did not include the sales force or
14 the container. And when we got there, it was something
15 over 30 cents a gallon. I think it was 33, but I couldn't
16 swear to that.

17 Q. And what did you get it down to?

18 A. Well, we got it -- I think, as I remember, the
19 best month that we had, we were around 17 cents.

20 Q. Now, did you develop some intelligence as to what
21 you believe the costs were of other plants that you were
22 competing with in the market were?

23 A. Yes, sir.

24 Q. And what was your understanding that their costs
25 were in competition to you?

1 A. We tried to sell some larger, major grocery
2 chains in the area, and we -- in order to do that, we had
3 to lay out all our costs to them and project what the costs
4 would be if we received the volume that we were hunting,
5 and each time they would point to the standard cost and say
6 it's way too high, just way too high. You've got to bring
7 it down.

8 Q. And how low did you bring it down, in number, to
9 bid the business?

10 A. We brought it down to around 13 cents -- 13 and a
11 half cents in one case.

12 Q. And was that low enough to match what was being
13 done in the market?

14 A. No, sir, it was not.

15 Q. did you make a determination of the size that you
16 felt you needed to be in order to make this a sufficiently
17 profitable operation, reflecting a return on investment?

18 A. Yes, sir, we did.

19 Q. And what was that size?

20 A. It was, in our market, 1,200,000 gallons per
21 month.

22 Q. And were you able as a PD to reach that size?

23 A. No, sir.

24 Q. Now, I want to take your -- bring your attention
25 to the -- continue with this discussion on the size of the

1 market. The types of competitors that you dealt with, did
2 they have -- what -- did they have any advantages over you?

3 A. I don't feel like they had any unfair advantages
4 over us, but they had a number of advantages and there were
5 advantages we were striving to achieve ourselves, primary
6 the benefit of the lower production costs because of the
7 volume going through their plants. They could, not all of
8 them, but many of them, I'm -- I want to say most of them,
9 but I'm not sure it was most of them, ran their plants
10 seven days a week, 24 hours a day. We ran ours five days a
11 week, and about 17/18 hours a day, and you know, more power
12 to them. They beat us.

13 Q. How -- what were the size of the plants you
14 competed with?

15 A. I --

16 Q. You don't remember?

17 A. Well, I don't know. I know we had one very large
18 retail chain that owned their own plant, and gee, there's,
19 had to be, who knows, 20 million gallons. I, you know, I
20 -- it's -- that's not a figure I would try to substantiate,
21 because I can't.

22 Q. Moving -- I want to talk about the situation of
23 operating the -- your operation there as a
24 producer/handler. Did the fact that you were -- or, what
25 limitations did the producer/handler regulations put on you

1 as -- operating as a plant?

2 A. Well, we could not buy and bring into our plant
3 virtually any fluid milk. If I remember correctly, the
4 gallonage was like -- something like 2,100 gallons a month,
5 and we couldn't -- and I'm not sure but what that may have
6 been 2,100 pounds. It was so small that it, you know, we
7 just couldn't buy outside of class one product. And on the
8 other side was the limitation of -- that was imposed by the
9 nature of us being a producer/distributor, and that was the
10 need for milk at certain times of the year when the cows
11 were not at their peak production, and the loss of business
12 at a time of the year when the cows may have been at their
13 peak production.

14 Q. Well, let's talk a bit about this idea that you
15 were limited on how much you purchased, and let's talk
16 about the practical impact on a producer/handler that
17 cannot purchase milk from anyone else. Can you describe on
18 a day-to-day operation of a plant the situations that arose
19 as a result of being not able to purchase milk from anybody
20 other than using the milk from your own farm?

21 A. Well, Mr. Yale, when school started, our cows
22 didn't know it, and it was really, really difficult because
23 in that part of the country, very, very hot August, and
24 that's when school's starting. And it was so hot that our
25 production would nearly always be down. And so you'd find

1 yourself at the plant many, many times with a full work
2 force waiting on milk to get there from the dairy because
3 we're milking 24 hours a day. There were times when we
4 simply couldn't get the milk there when it needed to be
5 produced or processed, excuse me.

6 Q. And were there any other situations where the
7 inability to purchase milk hampered your ability to grow
8 sales?

9 A. Yes, sir. I suppose one of the most telling
10 examples of that would be when we tried to pick up a
11 custard -- excuse me, a customer with any real size to
12 them, we'd have to tell them that they -- if we weren't
13 going to -- if we were not going to have to build another
14 barn to bring in the cows, then we at least needed a month
15 to bring in the cows. But if we were going to have to
16 build another barn, you're looking at four to six months.
17 And it's hard to sell that blue sky to somebody that you're
18 going to do it, but it won't be there for a while.

19 Q. Do you have an estimate what the average cost was
20 to add production to your --

21 A. As near as we thought we could figure it,
22 counting the cost the cow, and the land, and the building,
23 about \$3,000 a cow.

24 Q. And what was your average production per cow
25 under that scenario?

1 A. Again, it varied. Our temperatures vary a lot in
2 Texas, and we'd have a low -- hopefully the low would be
3 around 70 pounds, and it'd get up to 78 pounds, sometimes
4 80 pounds.

5 Q. And the -- in this situation if you made that
6 investment, was there the ability in that market to obtain
7 long-term, contractual agreements with the buyers to hold
8 on and furnish your milk for a long term period?

9 A. Oh, no, sir. No, sir. Schools, of course, you
10 could get a contract for nine months. Prisons, which we
11 seem to have a lot out in Texas, and maybe not enough, we
12 -- you could get them for a year. Some government
13 contracts were annual.

14 Q. Now -- so if you made this investment as a
15 producer/handler to have that milk, there was no assurance
16 that the sales would be there, right? Is that what you're
17 saying?

18 A. Yes, sir, that's specifically why we sold our
19 plant.

20 Q. Well, let's talk about that for a moment. Did
21 there ever come a time where you did make an expansion of
22 the herd to supply a particular market?

23 A. Yes, sir.

24 Q. And what was the result of that expansion? Did
25 you get the sale?

1 A. Yes, sir, --

2 Q. And how long did you have that sale?

3 A. I really don't remember, but it wasn't months.
4 It was probably in the neighborhood of two years.

5 Q. And what happened?

6 A. Well, it was a major discount retailer, and one
7 day we got a call that said we've given the business to
8 someone else. We were putting gallon -- 80 gallons on
9 bossy carts (phon.) for this customer, and they decided
10 that their -- the best way to market milk was have two
11 gallon containers instead of one gallon containers. So we
12 not only lost the sale, we had some \$400,000 worth of bossy
13 carts to try to get rid of.

14 A. So what did you do with the milk that you had
15 that wasn't going into bottled milk? Well, first of all,
16 what percentage was that of your market at that point, or
17 your sale?

18 A. Best of my recollection, it was conservatively 22
19 percent.

20 Q. And what was -- what did that do to your
21 operations of your producer/handler?

22 A. We had to find somebody that would take what, for
23 us, was a large, large amount of our production.

24 Q. And did you -- were you able to get a class price
25 for that production?

1 A. We got -- as I remember it, it was a little bit
2 under class three, and we had to provide the freight.

3 Q. So it netted out approximately -- do you remember
4 approximately how much?

5 A. Well, we weren't coming out whole on it. No, I
6 can't remember the exact number. I just -- I want to say
7 it was \$1 a hundredweight below class three, and we paid
8 the freight.

9 Q. And the result -- the end result of the loss of
10 that sale was what?

11 A. We sold our plant.

12 Q. And who did you sell it to?

13 A. The Oak Farms.

14 Q. Now, in this situation with the sale of, or this
15 -- is there anything, as you look back that the risk of
16 operating that plant as a PD that you could've, in any way,
17 have reduced that risk of fluctuation of sales, or is the
18 market such that that's just the way it --

19 A. I can't think of anything. We even bred the cows
20 so that they'd come fresh, you know, when we needed, or
21 anticipated the need for the milk. And so no, I don't know
22 of anything. There may have been something.

23 Q. What about -- well, I'll withdraw that question.

24 Now, the time came, I think you testified
25 earlier, that you retired, that they closed the plant, you

1 retired, and then you went back in employment and operated
2 another dairy operation?

3 A. Yes, sir.

4 Q. And what was the name of that?

5 A. Promised Land Dairy.

6 Q. And was it a producer/handler?

7 A. Yes, sir.

8 Q. And what did it -- what was its nature of its
9 market, just briefly?

10 A. It was a very muchly (sic) a niche market that
11 consisted of whole foods and health food stores, and we
12 were in some major grocery chains, very small space. Their
13 drawing card was it was jersey milk, and it was in glass
14 bottles.

15 Q. And did the operation of that as a PD under the
16 regulations have an impact?

17 A. Did the regulations --

18 Q. Being a PD to maintain PD status, did that impact
19 the operation of that operation?

20 A. Yes, sir, the same as it did in the other one.
21 It was obviously on a much smaller scale.

22 Q. Yeah. And did they -- you've not left that
23 company and retired, right?

24 A. Oh, yes, sir, in '99.

25 Q. Do you know whether or not they remained as a

1 producer/handler?

2 A. They are not.

3 Q. Now, what is the -- are you still involved with
4 Gore's, Inc.?

5 A. I'm still on their board of directors.

6 Q. And what is the status of Gore's, Inc. today in
7 terms of the types of operations it has?

8 A. Well, I'd have to step back a little bit. Even
9 while I was there, after we had sold the milk plant, we saw
10 what we felt like were greater opportunities in another
11 area. This last -- it's either this last month or the
12 first of this month, Gore's sold their cows and leased
13 their barns.

14 Q. So as -- at this point, you're -- it's no longer
15 a dairy farm?

16 A. That's correct.

17 Q. Now, if you were a dairyman today, and you had
18 the size, would you consider being a producer/distributor
19 as an attractive opportunity for a large -- by the way, let
20 me back up a second. The size of your farm in comparison
21 to other dairy farms at that time in Texas, how did it
22 rank?

23 A. We were one of the largest at that time. That
24 would not be the case today.

25 Q. But if you were a dairyman today, as being a PD,

1 would you see that as an attractive option knowing what you
2 know?

3 A. Well, not with any limitations on how big we
4 could get.

5 Q. And why is that?

6 A. The economy of scale was so important in our
7 experience, that the producer/handler benefit was a good
8 one, except for it being so difficult to balance your
9 supply, and even then the advantage of running seven days a
10 week, 24 hours a day, and of course, involving -- that's
11 the clean-ups now, they're not producing milk every second
12 of the day. But you just need a lot more volume than we
13 could get. So yes, under certain circumstances and in
14 certain markets, I would sure consider it, but not that
15 one.

16 Q. And during that period of time, the regulated
17 handlers were able to compete with you?

18 A. Yes, sir.

19 Q. And in that environment, was there situations
20 where you gained sales from your competitors?

21 A. Yes, sir.

22 Q. And did you lose sales to competitors?

23 A. Yes, sir.

24 MR. YALE: Your Honor, I don't have any more
25 questions.

1 THE COURT: Okay. Thank you, Mr. Yale.

2 Should I have cross-examination first, or should
3 -- or would -- Mr. Ricciardi, do you want to ask a few
4 questions first?

5 MR. RICCIARDI: I'm going to, at this point,
6 reserve my questions.

7 THE COURT: Okay. Yeah. Let's try to just sort
8 of like I did yesterday, backwards and we'll have the cross
9 be -- proponents ask some questions now. Don't forget to
10 identify yourself when you're speaking.

11 EXAMINATION

12 BY MR. BERDE:

13 Q. Mr. Beene, my name is Sydney Berde. I represent
14 the United Dairymen of Arizona.

15 I want to ask you a few questions about the
16 operation of Gore and Pure Milk. Where was Pure Milk
17 located?

18 A. Waco, Texas.

19 Q. Waco?

20 A. Yes, sir.

21 Q. And Pure Milk was a regulated handler under the
22 order that regulated that area, was it not?

23 A. Yes, sir.

24 Q. And how large an operation was Pure Milk?

25 A. You're talking about when we bought it?

1 Q. Yes.

2 A. I don't remember. I know it was much less than
3 800,000 gallons.

4 Q. And Pure Milk competed in the marketplace with
5 whom?

6 A. Oh, the same people that we competed with, --

7 Q. Can you identify some of them.

8 A. Oh, yes, good competitors. Great competitors.
9 Of course, we competed with HEB who owned their own milk
10 plants. We competed with Oak Farms, Bordens, just a little
11 bit with your plant -- with the Dean plant, rather, out in
12 Lubbock. We're on the fringe of their territory. And
13 basically that's the ones I can remember.

14 Q. Pure Milk's raw milk supply was AMPI, was it not?

15 A. I believe that's correct.

16 Q. And AMPI is -- was a cooperative supplying raw
17 milk to handlers in that marketing area, was it not?

18 A. Yes, sir.

19 Q. So that the milk that Pure Milk processed and
20 distributed, AMPI benefitted by the receiving -- the use,
21 or the market area -- the order, benefitted by receiving
22 the use value of that milk?

23 A. Yes, sir.

24 Q. And that affected, of course, the blend price for
25 all of the producers in that order, did it not?

1 A. Yes, sir.

2 Q. Now, at that time, Gore was a substantial
3 producer, was it not?

4 A. Yes, sir.

5 Q. Or Mr. Gore was. And Mr. Gore had a number of
6 farms, did he not?

7 A. We had four barns, three farms or -- yeah.

8 Q. And Gore was a member of AMPI, wasn't he?

9 A. That's correct.

10 Q. And AMPI marketed the Gore's milk production?

11 A. Yes, sir.

12 Q. And Gore, in turn, received the blend price or
13 the share of the market's use value of the milk that was
14 marketed in that marketing area, --

15 A. Yes, sir.

16 Q. -- didn't he?

17 Do you recall the year in which Gore decided to
18 purchase the Pure Milk operation?

19 A. I think I do.

20 Q. What year was that?

21 A. I believe that was 1987.

22 Q. And when Gore purchased Pure Milk operation, how
23 long did Pure Milk remain a regulated handler?

24 A. We remained a regulated handler until our
25 contract with AMPI ran out, and I can't tell you how many

1 months that was.

2 Q. You terminated your membership in AMPI; --

3 A. Yes.

4 Q. -- is that correct?

5 A. Yes, sir.

6 Q. And you then marketed all of your production or
7 whatever Pure Milk could use of your production, as a
8 producer/handler?

9 A. Yes, sir.

10 Q. Where else --

11 A. Excuse me. I'm sorry.

12 Q. Yes.

13 A. Most of the time.

14 Q. Most of -- where else did you dispose of your raw
15 milk?

16 A. We sold some raw milk to a processor in -- new
17 Wichita Falls.

18 Q. What kind of a processor, fluid milk handler?

19 A. Yes, sir.

20 Q. And where else did you dispose of your milk?

21 A. Oh, we disposed of our cream to Bluebell. I
22 can't remember -- after we lost the volume with the big
23 discount retailer, I can't remember where we disposed of
24 it. I just remember how difficult it was, and how much it
25 cost us.

1 Q. Well, when you disposed of your milk to those
2 outlets, you recall what price you received from the fluid
3 handler?

4 A. Never more than class three.

5 Q. Class three?

6 A. Yes, sir.

7 Q. And you disposed of your cream to an ice cream
8 maker?

9 A. Yes, sir.

10 Q. Now, when Gore through Pure Milk became a
11 producer/handler, the market order was denied the use value
12 of that distribution, wasn't it?

13 A. Yes, sir.

14 Q. So that depressed the blend price to whatever
15 extent was withdrawn from class one sales in that market?

16 A. Yes, sir, that was covered in the market order
17 hearing, and it was like one percent. It was very small.
18 I'm not sure exactly what it was.

19 Q. When Gore acquired Pure Milk, did you continue to
20 compete in the market with the same regulated handlers that
21 Pure Milk had competed with?

22 A. Yes, sir.

23 Q. And can you identify who those -- whether there
24 was a change or whether the handlers remained the same?

25 A. I'm sorry. Could you ask me that question again,

1 please?

2 Q. Were they the same handlers with whom Pure Milk
3 had previously competed?

4 A. Yes, sir.

5 Q. And when I use the term "compete," you understand
6 I mean you took business from them, they took business from
7 you; that correct?

8 A. Yes, sir.

9 Q. When you made offers to buyers of your processed
10 milk, how did you go about setting the offering price?

11 A. Could you be more specific?

12 Q. Well, how did you decide you're going to -- what
13 -- how did you decide the price you're going to put on a
14 gallon of milk?

15 A. Same way we did when we were a pool plant. The
16 price that was in the marketplace at that time provided one
17 gauge for us as to how high we could go or how low we had
18 to go, if we knew the price that customer was buying for
19 when we were trying to get his business. And, of course,
20 then we computed our cost of operation of the plant and the
21 transportation costs. The milk was sold to us -- no,
22 excuse me. Milk was transferred to us as a -- as if it
23 were class one, if we were selling to a class one customer.

24 Q. You started increasing your gallon offering price
25 by the -- your raw milk cost, didn't you, and built it up

1 from there?

2 A. No, sir, not necessarily.

3 Q. What then?

4 A. We built our costs up from there, but in pricing
5 the product, we had to look at who we were selling to, what
6 type of business they had, how distant they were from our
7 plant, how much volume they could provide to us, just a
8 number of other factors other than what it cost us to
9 produce a gallon of milk at our farm.

10 Q. Did you maintain cost accounting records in which
11 you established a transfer price for the raw milk to your
12 processing operation?

13 A. Yes, sir.

14 Q. And what was that transfer price that you used?

15 A. Transfer price for accounting purposes was the
16 price at which the product was being used, the current
17 price in the market at which the product was being used.

18 Q. Well, I don't know if I understand that answer.
19 When I speak of a transfer price, I'm referring to the raw
20 milk that you had to price in some fashion entering your
21 processing operations. What was the transfer price of the
22 raw milk that you used?

23 A. I'm sorry, I'm trying to answer your question.
24 We transferred it to the plant at whatever category it was
25 being used in, the same way it was before.

1 Q. Well, what -- when you say the category, you mean
2 if it's going to go into class one use --

3 A. Yes, sir.

4 Q. -- you use -- did you use the class one use of
5 the market?

6 A. Yes, sir.

7 Q. The class one use of the market was the process
8 value of that milk, not the raw milk value, was it?

9 A. I'm sorry. We used the price in the marketplace
10 --

11 Q. You mean the blend price --

12 A. Yes, sir.

13 Q. The blend price of the market?

14 A. Yes, sir.

15 Q. Okay. And that was your transfer price.

16 A. Yes, sir.

17 Q. Okay. Now, you indicated that you sold out
18 ultimately to Oak Farms?

19 A. Yes, sir.

20 Q. Oak Farms was a competitor of yours?

21 A. Yes, sir.

22 Q. And could you tell us what motivated the decision
23 to sell out to Oak Farms?

24 A. More than one thing. The biggest single one may
25 have been the lost sales, and therefore the excess milk

1 that we had. And when I say it may have been, I mean it
2 may have been the most important factor, and I think it
3 was, trying to recall the specific instance.

4 Another was, as I indicated, that we saw what we
5 felt were some more attractive ways to invest our money.

6 Q. You mean, you have more attractive investment
7 opportunities for the value of the land, for example?

8 A. No, sir, we were pretty large in the feed
9 business, and we decided we wanted to expand that feed
10 business --

11 Q. How long did you remain in the business of
12 producing milk after you sold out the plant to Oak Farms?

13 A. We sold that plant in 1990 -- I believe right at
14 the end of 1995. The Gores went out the dairy business
15 either last month or early this month. Do believe it was
16 last month.

17 Q. And Gore's no longer in the business of producing
18 milk; is that it?

19 A. That's correct.

20 Q. Now, did you practice adjustment of a breeding
21 cycle in order to level out production?

22 A. Yes.

23 Q. And to the extent that you were able -- well, can
24 you describe to what extent you were able to level out
25 production by adjusting the breeding cycles?

1 A. No, sir, I really can't. I couldn't get specific
2 with the number of pounds that we were able to transfer
3 from one season to another, it wasn't enough. That's all I
4 can remember.

5 Q. But it did help you to take care of the
6 production shifts from the flush to the short season,
7 didn't it?

8 A. It had some impact. It wasn't enough as I
9 testified earlier. We had numerous times the plant was
10 sitting there -- we couldn't let the work force go home
11 because milk was on the way, but it wasn't there.

12 Q. Now, you mentioned that you packaged milk for the
13 school business, half pints?

14 A. Yes, sir.

15 Q. Who did you compete with in the distribution of
16 milk, or who did you compete with in the bidding of
17 contracts for school milk?

18 A. Oak Farms, Bordens. Oh, there were others based
19 on where we were bidding. We competed with Gandy's
20 (phon.). That's all that come to mind right now, but there
21 were many more.

22 Q. And were you a successful bidder?

23 A. Sometimes we were, and sometimes we were not.

24 Q. And what other distribution channels did you
25 market your milk in. Institutions for example?

1 BY MR. BESHORE:

2 Q. Marvin Beshore for Dairy Farmers of America.

3 Mr. Beene, have you ever testified in a legal
4 proceeding before?

5 A. Yes, sir.

6 Q. In federal order hearings?

7 A. No, sir.

8 Q. What, civil court litigation of some nature?

9 A. Yes, sir.

10 Q. Have you ever offered your opinions on -- with
11 respect to the milk regulations or operating milk plants in
12 any legal proceeding before?

13 A. No, sir.

14 Q. Prior to Gore's becoming a PD, it operated a
15 dairy farm, I think you've testified, correct?

16 A. Yes, sir.

17 Q. 5,000 cows, if I remember that right?

18 A. What I said was, we had nearly 5,000 cows at our
19 absolute peak.

20 Q. As Gore's, not Pure Milk now, but as Gore's.

21 A. Well, they were all the same company. When we
22 went to the bank, there wasn't any distinction.

23 Q. Okay. Prior to acquiring Pure Milk and Ice Cream
24 Company, Gore's had a dairy farm; is that --

25 A. Yes, sir.

1 Q. And you were a member of AMPI, I think, and sold
2 your milk -- marketed it through AMPI; is that right?

3 A. Yes, sir.

4 Q. Okay. How many cows were in the operation?

5 A. I don't know. I wasn't -- I can't remember, but
6 it was significantly less than the 5,000 cows. Probably
7 would've been in the high 3,000s.

8 Q. Okay. Was the dairy farm profitable?

9 A. Yes, sir.

10 Q. And you received the blend price from the market

11 --

12 A. Yes.

13 Q. -- from AMPI?

14 A. Oh, yes, sir.

15 Q. Blend or more or less, depending on how the
16 coop's operations worked out, I guess?

17 A. Yes.

18 Q. Okay. Now, when Gore acquired Pure Milk and Ice
19 Cream Company, you added how many cows from their
20 operations to your total milk production capacity?

21 A. Pure Milk did not have any cows.

22 Q. Oh, it was just a plant?

23 A. Yes, sir.

24 Q. Did they make ice cream as well, they followed
25 their name?

1 A. They used to. No, they did not when we bought
2 them.

3 Q. Okay. So you never made ice cream as --

4 A. No, sir, we made the mix that goes in the soft
5 serve machines. That's all.

6 Q. Okay.

7 A. Like Dairy Queen has, for example.

8 Q. Okay. You -- it's more profitable to market your
9 excess cream to Bluebell, which made ice cream than to make
10 it yourself, I take it?

11 A. Well, you know, that was certainly what previous
12 management and ownership had decided.

13 Q. And you continued that pattern?

14 A. Yes, sir.

15 Q. Now, in operating the Pure Milk and Ice Cream
16 Company as a producer/handler, I'm interested again in --
17 Mr. Berde asked you some questions about this, I think, but
18 I'm not sure I understood it completely. When you -- the
19 first think you looked at in pricing your products -- well,
20 first of all, I guess, when you bought the company, they
21 had established customers, correct?

22 A. Yes, sir.

23 Q. Okay. And they were supplying those customers
24 with milk that they purchased from probably AMPI, I
25 suppose; is that -- or other coops in the marketplace?

1 A. They were purchasing from a coop, and I assume it
2 was AMPI

3 Q. Okay.

4 A. I don't remember.

5 Q. So they were buying milk. They were a pool
6 handler. They were buying, paying classified prices?

7 A. Yes, sir.

8 Q. Okay. And they were -- they had customers in the
9 marketplace that they were selling their fluid products to,
10 correct?

11 A. Yes, sir.

12 Q. Okay. Now, you acquired -- when you acquired the
13 dairy, you acquired the business, the customer
14 relationships, correct?

15 A. Yes, sir.

16 Q. And they had established prices that they were
17 marketing their fluid products at?

18 A. That's right.

19 Q. Okay. Now, the thing that changed was, you
20 didn't acquire milk from AMPI or from pooled sources any
21 more, but you acquired milk from your own farm, correct?

22 A. After a period of time, yes, that's correct.

23 Q. Okay. When you became a PD. And then you no
24 longer had to pay the classified prices to the market
25 administrator, --

1 A. That's correct.

2 Q. -- to the market pool, correct?

3 And I think you said that there were benefits to
4 being a PD, and that was a major benefit, was it not?

5 A. I don't think I said it was a major benefit. It
6 was --

7 Q. Well, I'm asking you --

8 A. -- definitely a benefit.

9 Q. Okay. And the benefit was, on the class one
10 price in Texas at that time was, you know, what, \$1.75 a
11 hundredweight, \$2 a hundredweight difference between class
12 one and blend price?

13 A. I honestly don't remember.

14 Q. Okay. Well, it was in that range, wasn't it?

15 A. I'm sorry, I can't remember.

16 Q. Okay. When was the last time you looked at any
17 of the records of these operations before preparing and
18 coming to testify today?

19 A. Years.

20 Q. Okay. And all your memory's been from that --
21 all your testimony about their operations is based on your
22 memory without any refreshing of any recollection of the
23 records for years?

24 A. Yes, sir.

25 Q. Okay.

1 A. I did talk to their accountant to verify -- their
2 current accountant, who was the accountant to verify what I
3 have said this morning.

4 Q. Okay. Who --

5 A. I did not ask him what, you know, what the
6 differential was in --

7 Q. Okay.

8 A. -- at the time we took over the plant.

9 Q. Who did you mean by "their accountant?" Whose
10 accountant?

11 A. Gore's.

12 Q. Okay. Now, as I understand it, you had a
13 profitable dairy at Gore's, making money receiving the
14 blend price, and now you became -- when you acquired Pure
15 Milk and Ice Cream Company, you became a PD. You acquired
16 a pool handler, which had -- was it a profitable one, by
17 the way, Pure Milk and Ice Cream Company when you bought
18 it?

19 A. Yes, sir.

20 Q. Okay. Now you have a profitable pool handled
21 supplied by a profitable dairy farm, and you integrate the
22 operations and operate them as a producer/distributor,
23 correct?

24 A. Yes, sir.

25 Q. Okay. the cost of operating your plant, you

1 said, was -- you got as low as 13 cents --

2 A. No, sir, I believe I said 17 cents.

3 Q. 17 cents. Okay. What was the 13 cent number
4 that you mentioned, or was that inadvertent?

5 A. Probably.

6 Q. Okay. So --

7 A. I know that -- I may have responded to a
8 question, what would it have taken, and -- but I never knew
9 that for sure.

10 Q. Okay.

11 A. Oh, excuse me. I just remembered where I came up
12 with that. It was a number that we thought we could get to
13 with this added distribution and added input into the
14 plant. That's where the 13 cent -- and so when we
15 discussed that as a part of our price, we were told it
16 wasn't low enough.

17 Q. What volume of sales did Pure Milk and Ice Cream
18 Company have when you acquired it?

19 A. I don't remember. Significantly less than what
20 we built it to.

21 Q. Okay. So you increased the volume of Pure Milk

22 --

23 A. Yes, sir.

24 Q. -- and Ice Cream Company.

25 I take it then that when it was operating, before

1 you acquired it when it was operating at lower volumes than
2 you got it to, that its cost per unit were higher than they
3 were when you were operating it?

4 A. I believe I testified to that a little earlier.
5 My memory is, their standard cost was around 33 cents. I
6 can't remember the mills.

7 Q. Okay. And they had a profitable business at that
8 time?

9 A. We certainly thought so.

10 Q. When you -- the product that you package, fluid
11 milk products at Gore, some of them were in the store
12 labels, I think you said. Package for some chains, and you
13 did it in the store labels?

14 A. Yes, sir.

15 Q. Okay. You didn't supply all of their needs for
16 that particular label in all of their stores, did you?

17 A. No, sir.

18 Q. And did that chain have its own bottling
19 operation that was a pool plant, and it -- where it bottled
20 the rest of its fluid milk products?

21 A. Question's going to have to be answered yes and
22 no. We had one of each.

23 Q. Okay. One did -- one had its own bottling plant,
24 which was a pool plant, correct?

25 A. Yes, sir.

1 Q. Okay. And it bottled all the -- much of its
2 needs for fluid milk product, and you supplied some of the
3 rest in the same label?

4 A. Yes, sir, less than one tenth of one percent, but
5 we did supply some.

6 Q. Okay. Did you basically supply them everything
7 that you could with your production capacity in that label?

8 A. No, sir.

9 Q. Okay. I take it that since your plant was short
10 of milk at times, that you were basically as a
11 producer/distributor putting all of your raw milk
12 production through the plant; you were using all the milk
13 that you produced for your fluid milk products?

14 A. For a very limited period of time, that's
15 correct, but the cows didn't know when Christmas came and
16 schools were out either. So at that time the same cows
17 were producing way more milk than we had sold.

18 Q. Okay. When you were CEO of -- were you CEO of
19 Promised Land Dairy?

20 A. Yes, sir.

21 Q. Okay. For what period of time?

22 A. Early '96 to mid-'99.

23 Q. Okay. Okay. As CEO of Promised Land, did you
24 seek to retain the best dairy plant cost accounting
25 services that you could find?

1 could interpret some of the numbers you gave us here.
2 First of all, do I recall that you said you competed in
3 Waco to Austin area principally? Is that --

4 A. Certainly, we had a large base of sales in that
5 area. Probably -- I don't know what percent.

6 Q. And down to San Antonio?

7 A. Yes, sir.

8 Q. Over to Houston?

9 A. Over towards Houston. I don't believe sold any
10 milk in Houston.

11 Q. And up as far as Dallas?

12 A. Yes, sir.

13 Q. Okay. So within that region, Greater Dallas,
14 Greater Houston, Greater San Antonio, do you know roughly
15 how many people were there?

16 A. Oh, my goodness, no.

17 Q. No?

18 A. No, I don't have any idea how many people were in
19 that --

20 Q. The reason I'm asking, and I'm trying to get a
21 sense of your market. I can represent to you that there
22 might be, you know, no more -- less than 15 million people
23 in Washington, Oregon and Idaho combined. I'm trying -- my
24 impression is that that region of Texas would be maybe
25 twice as large in terms of population base and --

1 A. Well, yes, sir. San Antonio -- and understand we
2 had a very small operation in San Antonio that certainly
3 did not distribute to all of San Antonio, but it was in
4 that market, and San Antonio's a million people. It was
5 less than that then, but it was 900,000 at that time. I'm
6 sure the Dallas/Fort Worth area's over a million.

7 Q. Well, obviously it was substantially over a
8 million. Yeah. Well, what I've tried to do is get a sense
9 of the market. So bear with me if you don't know, but --
10 how many people are there.

11 A. I don't know.

12 Q. How many plants would we find if we were to look
13 at the list of distributing plants or producer/handler
14 plants in that market, well say, during the '90s when you
15 were in that market; how many --

16 A. I don't remember.

17 Q. Talking about more than ten, less than ten?

18 A. I was told not to guess by you, so I won't guess.

19 Q. Okay. That's fine.

20 A. I don't know.

21 Q. I'm interested in the sizes of the plants that
22 you must have competed with, and I -- my impression is that
23 the Texas market has relatively few plants and a whole lot
24 more people, say, compared to our market, and that's what I
25 was just trying to get at. If you don't know, you don't

1 know.

2 So let's revisit some of what I heard you testify
3 to. I believe you said that at peek, your Pure Milk volume
4 would've been in the neighborhood of 800,000 gallons per
5 month; did I get that right?

6 A. Yes.

7 Q. And if I just roughly multiply that by eight
8 pounds per gallon, I get about six and a half million
9 pounds a month; is that right?

10 A. Yes, sir.

11 Q. You said you had 5,000 cows?

12 A. I said at the peek, we had around 5,000 cows.

13 Q. At that peek period. Would those have included
14 just milking cows, or are you talking about all cows and
15 maybe heifers?

16 A. No, not heifers, but milk cows.

17 Q. Dry cows.

18 A. Some dry cows, yes, sir.

19 Q. So not all 5,000 were milking, right?

20 A. That's correct.

21 Q. The reason I ask is if I multiplied 5,000 cows
22 times 80 pounds a cow, which is what you said was your
23 maximum, I'd get as much as 12 million pounds a month of
24 potential volume. So can you give me a sense of what the
25 typical volume was of production on your farm?

1 A. No, sir. It varied greatly.

2 Q. At the peek.

3 A. But we had several peeks and valleys during one
4 year. The spring was our top production. Summer went
5 down. Winter, depending on the severity of it, went down
6 even more sometimes.

7 Q. Well then, maybe I could ask the question a
8 different way. Did you produce more milk than you were
9 able to process at the plant as -- at times of peek
10 production -- at times of peek milk production on the dairy
11 farm?

12 A. Our experience was then and remains today that
13 producer/distributor must produce more milk than the plant
14 can hold because it --

15 Q. Okay. You testified earlier there were some
16 balancing costs. Is that what you're referring to then is
17 that having to cover that difference between farm
18 production and plant --

19 A. Yes, sir. If you're trying to produce exactly
20 where the plant is, you're in a big, big world of hurt.

21 Q. You testified that you thought you needed to be a
22 1.2 million pounds; did I get that right?

23 A. No, sir.

24 Q. 1.2 million gallons?

25 A. No, sir. I said a million 200,000 gallons.

1 Q. You needed to get to be at 1.2 million gallons
2 per month to be as efficient as you would like to be?

3 A. That what our calculations showed. Yes, sir.

4 Q. And that would be roughly 50 percent larger than
5 you were?

6 A. Correct.

7 Q. Or --

8 A. At the top.

9 Q. -- ballpark at 10 million pound a month plant;
10 would that be ballpark?

11 A. I'm sorry. Say that again.

12 Q. Yeah. Well, often our statistics are in pound --
13 millions of pounds per month. I'm trying to equate your
14 gallon figure to roughly a ten million pound a month plant.

15 A. I suppose. I don't have my calculator with me,
16 and I sure don't trust my math --

17 Q. Okay. I beg -- I represent to you that if you
18 needed to be at 1.2 million gallons, that you would be
19 processing roughly ten million pounds per month. You said
20 that you had competitors in the marketplace, and if my
21 notes are correctly as -- with volumes that you thought
22 might be as high as 20 million gallons per month.

23 A. No, sir, I threw that figure out to illustrate
24 how little I did know about it. I don't know what our
25 competitors gallonage was. I know they had bigger capacity

1 plants than we did, and some of them ran seven days a week,
2 excluding clean-up time.

3 Q. Sure. Do you have a sense of how many plants in
4 the Houston/San Antonio/Dallas/Waco region processed less
5 than ten million gallons per month or --

6 A. I have no idea.

7 Q. -- 1.2 million -- excuse me, less than ten
8 million pounds per month, or less than 1.2 million gallons?

9 A. No, sir, I don't have any idea.

10 Q. I want you to assume for a moment that -- well,
11 actually I guess I don't have to assume it. You go back to
12 the point where you first acquired Pure Milk. I believe
13 you testified that for some time you were buying milk from,
14 I believe, AMPI or at least some cooperative down there.

15 Q. Yes, sir, I believe it was AMPI.

16 A. Did they have an over-order premium at that point
17 in addition to the class one price?

18 A. I do not -- goodness, that was years ago. I
19 don't remember.

20 Q. Fine. Okay. I'm confused about the 13 cent
21 number that you had testified to and Mr. Beshore asked you
22 about further, the 13 cents per gallon that you thought, or
23 you were told wasn't going to be low enough for you to get
24 certain business; do you recall that?

25 A. As standard costs. Yes, sir.

1 Q. 13 cent standard cost would not have been low
2 enough for you to get the business?

3 A. Was not low enough.

4 Q. Do I understand you to say then that as you
5 approached the customer in question at that time, you
6 proposed a pricing arrangement that was based on a cost per
7 gallon of 13 cents, or are you saying that you were
8 actually going to process for them at 13 cents? Did they
9 see the 13 cent number, or did they see a total price per
10 gallon?

11 A. Both.

12 Q. Does that 13 cents include packaging costs?

13 A. No, sir.

14 Q. Okay. So were they looking for a contract which
15 would have in it a breakdown of the costs between milk
16 packaging and operating costs?

17 A. Yes, sir, and freight.

18 Q. And freight. Sure. Delivery costs.

19 And how did they value the raw milk costs in such
20 a contract proposal, or how did you?

21 A. At the price in the market at that time. At your
22 market order price for raw milk going into fluid milk.

23 Q. Okay. So do I understand correctly that this
24 would be a mover contract based on the federal order price?
25 Is -- that terminology we use in this region would be a

1 mover contract that would be adjusted, based on the federal
2 order price and adjusted as things like packaging and raw
3 milk costs change.

4 A. In that particular instance, I don't remember
5 whether we priced it that way or not. We well may have.

6 Q. At the time of this approach to that customer,
7 were you bidding for business against other bidders, or
8 against an incumbent supplier?

9 A. It might be more accurate to say we were quoting
10 against them. There was not a formal bid that I remember
11 taking place at that time. It was on our initiative, and
12 we were trying to get some business.

13 Q. Okay. Understood. Is the -- was the then
14 current supplier a pooled plant, a regulated -- fully
15 regulated plant?

16 A. To the best of my knowledge, it was, yes.

17 Q. So you were showing the potential customer a cost
18 structure based on a milk price that, I assume from what
19 you said earlier, was the federal order milk price, plus a
20 processing cost of 13 cents, plus other costs of both
21 delivery and packaging?

22 A. Yes, sir.

23 Q. Earlier you said, I believe, that the standard
24 cost of Pure Milk when you acquired it was in the range of
25 33 cents.

1 A. Yes, sir.

2 Q. Did that number include packaging?

3 A. Best of my knowledge, it did not. I'm not
4 positive.

5 Q. May have?

6 A. It -- no, sir, it shouldn't have, because we just
7 didn't include it in our standard cost, but I wasn't the
8 one that did the computation on it.

9 Q. Why wouldn't you include packaging as part of
10 your cost structure?

11 A. It is part of the cost structure, not part of
12 what we call standard cost, trying to measure the
13 efficiency of our plant and our people.

14 Q. You began, I think, your testimony by standing the
15 opinion that market forces would put some limitation on a
16 producer/handler operation thrust of your testimony, --

17 A. Yes, sir.

18 Q. -- if I recall it correctly.

19 And then -- and as you and I have been
20 discussing, you felt you needed to be at ten million pounds
21 a month to compete effectively in that Houston/Dallas/San
22 Antonio market in the 1990s; is that --

23 A. Yes, sir.

24 Q. If there were a regulated plant less than ten
25 million pounds in that market at that time, do you feel it

1 could've competed successfully? That is to say, paid the
2 full blend price, assuming the full -- let me repeat the
3 question. If at that time there had been a plant in that
4 region that was fully regulated, and therefore was paying
5 full class prices, do you feel that they could've competed
6 effectively at that time, in your opinion?

7 A. It depends on what kind of plant it was, how
8 modern it was, whether they had a fully automated plant, an
9 awful lot of things. I can't answer your question.

10 Q. Did you benchmark you 13 cent operating cost --
11 standard cost number against other plants in that region in
12 any way?

13 A. Would you define "benchmark?"

14 Q. Did you do a comparison of you costs against your
15 competitors' costs?

16 A. We do not absolutely know our competitors' costs.

17 Q. Understand that. Did you feel your costs
18 structure was -- in processing, the 13 cent number, do you
19 feel that was lower or higher?

20 A. Higher than our competitors.

21 Q. Expressed an opinion about that ability to
22 compete. Let me ask you to express a similar opinion or
23 little bit different circumstances than you actually were
24 operating under. I'm recalling specifically the testimony
25 regarding a customer who, as I think you put it, dropped

1 you guys rather than -- as a supplier rather than go
2 through the hassle of hearings, audits, and whatever
3 associated with your company's producer/handler status.
4 Does that accurately recall your testimony?

5 A. Yes, sir. Probably.

6 Q. What would've been the situation with respect to
7 your ability to compete for that business had there been no
8 federal order at all? I'm asking you to consider
9 everything when you express an opinion.

10 A. I think that's a set of circumstances I can't
11 even -- there are so many other things that would happen
12 without any federal order. I don't know how many milk
13 producers there would be. I don't know how many plants
14 there would be. I'm sorry, but that -- with no federal
15 order, it's a world I don't think I encountered.

16 Q. You've described how the federal order audit
17 (phon.) process was a disadvantage to you.

18 A. I'm sorry. I'm not trying to be difficult.
19 Would you say that again?

20 Q. I'm beginning a question --

21 THE COURT: I don't think he had a question yet,
22 so.

23 BY MR. MARSHALL

24 Q. I'm beginning the question, yeah. You've
25 described how the federal order audit process disadvantaged

1 you in dealing with that customer.

2 A. Yes, sir.

3 Q. And you've also acknowledge in prior questioning
4 some advantage under the federal order system because you
5 were not charging yourself the blend price -- excuse me.
6 You were not charging yourself the class price on your
7 plant operation while receiving only the blend price on
8 your farm operation. Was the federal order system a net
9 benefit or a net disadvantage for you, between the one
10 advantage and the one disadvantage, or any other
11 disadvantages or advantages?

12 A. I'm really from the country. You're going to
13 have to do that again. I didn't understand what you're
14 trying to get me to say or where the question is.

15 Q. Well, let's it --

16 A. Are you asking me overall?

17 Q. Yes. Uh-huh.

18 A. Overall was the federal order an advantage to us
19 or a disadvantage to us?

20 Q. That's my question, yes. Or I -- we can break it
21 down and do a step at a time, but if you can answer that,
22 go ahead.

23 A. I don't know. I'm trying to imagine the world
24 without the federal order, and that's -- you know, to us we
25 -- the cost of milk was what it took for us to produce it.

1 Q. There'd been no federal order system, would not
2 the large plant, larger than yours plants have also been
3 able to acquire milk at roughly the cost of production on
4 dairy farms in Texas?

5 A. Yes, sir.

6 Q. You wouldn't have had any cost advantage to them
7 in terms of raw milk into your plant, would you?

8 A. No, sir. It's just that that's not near all the
9 costs going to it.

10 Q. Right. Well, I'm just trying to get a sense of
11 whether the advantages of the federal order system -- the
12 federal order system -- well, we can take it a step at a
13 time then. Would you imagine that the prices that you were
14 paying when you were a regulated plant, including any
15 service charges that you had to the cooperative, were
16 greater than what your cost of production was on your farm?

17 A. You're asking my opinion?

18 Q. Yes, I am. And based on your experience as the
19 person -- one of the people in the management of your
20 company who saw the financial records when you moved from
21 regulated status when you were buying milk from the coop
22 and paying any services charge that may have -- or premiums
23 that may have existed, did you have a lower cost when you
24 went to your own farm production?

25 A. Yes, sir.

1 Q. And did you ever attempt to quantify any
2 disadvantages of the federal order system in dollar terms?

3 A. While we were a producer/distributor or?

4 Q. Yes, I'm sorry. When you were -- after you
5 became a producer/handler, did you quantify the
6 disadvantages associated with being a producer/handler
7 under the federal order system and living within the
8 federal order restrictions?

9 A. I don't think so.

10 Q. Well, then that's an answer, and I appreciate
11 your acknowledging that you didn't do that, so that's all
12 --

13 A. I'm just trying to be sure that what I didn't do.

14 Q. If you didn't, you didn't, and that's just fine.
15 I just wanted to know if you had the ability to quantify
16 the pros and the cons. It sounds like you had not done
17 that kind of analysis.

18 A. Well, on specific instance, we might have, but it
19 varied with the month, it varied with the customer. But
20 it's a situation where once you become a
21 producer/distributor, another situation you face is, boy,
22 you have bet the farm, and in you're in that deal. So --

23 Q. You mean, you've invested in the farm?

24 A. No, I mean you've put all of what you have on the
25 line. Both the plant and the farm are dedicated to trying

1 to get out there and get enough business, --

2 Q. Sure.

3 A. -- make more.

4 Q. And you could've, at any time, have given up
5 producer/handler status?

6 A. Well, we did.

7 Q. You could've drawn --

8 A. Yes, sir.

9 Q. You could've drawn the blend price from the pool.
10 You could've paid the pool price, but then have the -- have
11 had the ability to not worry about buying milk from outside
12 sources and some of the other disadvantages you've
13 discussed, right?

14 A. That's correct.

15 Q. And you elected not to do that, I assume, because
16 it was not to your advantage to operate in that fashion?

17 A. For a variety of reasons. That's right, until
18 we'd lost a significant share of our business.

19 Q. Okay. So can I -- would it be fair to say then
20 that there was more -- once there -- I was asking you
21 earlier questions about what would be pros and cons of the
22 federal order system. Now I'm going to change the topic
23 ever so slightly. There was a federal order system. Let's
24 now assume that to have been the case, and is it fair for
25 us to conclude that you're testifying that there was more

1 advantage to being a producer/handler than to being a
2 pooled producer and a regulated handler at that time?

3 A. And are you restricting that to the price, to the
4 --

5 Q. No, I'm asking as a business man whether you
6 evaluated the option of giving up your producer/handler
7 status, which would've meant being a pooled producer, and
8 would've meant paying same prices as other regulated
9 handlers. Did you evaluate that option and compare it with
10 the advantages of being a producer/handler?

11 A. Yes, sir, we did.

12 Q. And you elected to remain a producer/handler?

13 A. Yes, sir, we did.

14 Q. Okay. Because it was more advantageous?

15 A. Yes, sir.

16 Q. That's all I wanted. One other question -- one
17 other line of questioning, and that is, could you give us
18 an estimate roughly what the percentage of the milk you
19 were using -- correction. What percentage of the milk you
20 were producing on the farm actually was used in class one
21 type uses, that is to say, bottled milk?

22 A. No, I can't. I can remember it varied a lot.

23 Q. Sure. It sounds like in August it was like 100
24 percent.

25 A. It got close, you know, we had the class two

1 product of that soft mix ice cream.

2 Q. Yeah, you had to serve that customer with class
3 two.

4 A. So it never reached 100 percent. I don't see how
5 a producer/distributor could and stay in business, but
6 there were times when it was much higher, and times when it
7 was not.

8 Q. Was the soft serve business a significant
9 percentage of the --

10 A. No, sir.

11 Q. So your -- what I'll call your class two uses
12 might have been what, five percent, ten percent?

13 A. I just could not guess at a percent, but I will
14 submit that they were small.

15 Q. What percentage of your milk then would you have
16 had to dispose of to other plants, say, during the course
17 of a year -- calendar year or fiscal year?

18 A. I can't recall those figures.

19 Q. Had you ever read a calculation as to the
20 percentage of your milk that was used in what would've been
21 class one uses or class two uses or class three uses?

22 A. Every month, but I'm sorry, I don't remember what
23 they were.

24 Q. Understand. It's been a long time, and --

25 A. Yes, sir.

1 Q. -- if you don't remember, that's perfectly
2 understandable. There's a lot about the '90s I don't
3 remember either.

4 So but you did a calculation each month of the
5 percentage using one, two, and three?

6 A. Yes, sir.

7 Q. And then did you compare that against what would
8 have been your cost of milk as a plant if you had been
9 paying the regulated class price?

10 A. Yes, sir.

11 Q. And did that help you then understand the
12 profitability of your processing plant by comparing --

13 A. Yes, sir, it did.

14 Q. So you were comparing against the alternative of
15 regulation versus --

16 A. Yes, sir.

17 MR. MARSHALL: -- producer/handler status.

18 Excellent. Thank you so much for your help.

19 THE COURT: Anything else from the proponents'
20 side?

21 (No response)

22 THE COURT: Okay. Mr. -- oh, go ahead, Mr.
23 English.

24 EXAMINATION

25 BY MR. ENGLISH:

1 Q. Sir, you mentioned -- Charles English for Dean
2 Foods and Shamrock Farms.

3 You mentioned one of the concerns, the balancing
4 costs, correct?

5 A. Yes, sir.

6 Q. Did you for Pure Milk or for Promised Land have
7 the ability to dispose of any surplus milk into a marketing
8 area other than a federal marketing area, and receive any
9 kind -- any form of a blend price?

10 A. Not that I remember. Now, what -- excuse me.
11 Did we have an opportunity, was that your question?

12 Q. Did you have that -- have and use that
13 opportunity?

14 A. I don't remember using it. There may have been a
15 time when someone asked us to bid some excess milk to
16 Mexico, but we never carried any down there.

17 Q. Okay. But Mexico would not have provided a
18 effectively -- a blend price. You would've gotten a price
19 that whatever Mexico would pay, correct?

20 A. Yes, sir, that's correct.

21 MR. ENGLISH: Thank you. I'm done with the
22 questions.

23 THE COURT: Any questions from the front row
24 here, Mr. Deskins and Mr.?

25 EXAMINATION

1 BY MR. TOSI:

2 Q. Hi. Good morning. Thank you for appearing.

3 Gino Tosi with the USDA.

4 What was the appeal of the decision to become a
5 PD in the first place versus a -- remaining either as a
6 producer or as a handler that may be regulated.

7 A. Several, but one that we felt was extremely
8 important was, we believed we could differentiate our milk
9 from other milk so that it wouldn't be as much as a generic
10 product, and we hoped to benefit from that economically,
11 and we hoped that we could provide to the customer a
12 overall better product simply because it wasn't co-mingled.

13 Q. Okay. Was it considered to be a significant --
14 would a significant consideration in choosing to be a
15 producer/handler, was the fact that you wouldn't have to
16 pay the difference between class one and the blend price
17 into the federal order pool?

18 A. Yes, sir, that was a significant part of our
19 decision. Sure.

20 Q. And as you look back on that experience that you
21 had, would it be accurate to say that, or to characterize
22 your testimony as that even with that -- if you want to
23 look at that as a cost savings, that it's a cost that a
24 producer/handler is not paying that a regulated handler
25 pays, that it was sufficient or not sufficient to offset

1 all the other limitations that come with being a
2 producer/handler?

3 A. There's another that is yes and no answers. At
4 some -- better than 50 percent of the time, it was, and
5 then there was a period of time when it became not feasible
6 for us to own the plant, we sold the plant.

7 Q. Okay. Would it also then be accurate to say that
8 to the extent that you're not making this payment to the
9 Producer Settlement Fund that it had a role in whether or
10 not you were able to successfully gain business with your
11 other regulated competitors?

12 A. I don't know. We would've been paying more for
13 our milk. Our quoted price would've had to have been
14 higher, if that's the question you're asking.

15 Q. Let me ask the question again. Maybe I didn't
16 ask it correctly.

17 To the extent that you're not making a payment to
18 the Producer Settlement Fund, was that advantage over a
19 regulated handler enough to cause you to be able to
20 increase your market share or your ability to compete with
21 other regulated handlers?

22 A. It improved our ability to compete with regulated
23 handlers. It's just one of the many factors that you have
24 to take into consideration, but it did help us compete.
25 Yes, sir.

1 Q. And that issue aside, what I think I hear you
2 saying in your -- in the sum total of your testimony is
3 that there's many, many other factors other than that price
4 advantage that are important?

5 A. Yes, sir. We got beat because the people did it
6 better than we did. Some of these folks do an outstanding
7 job, and I say more power to them. That provides to the
8 consumer a real value and a product that's needed.

9 Q. And then some of the questions that you've been
10 asked sort of suggests are asking you about your opinion of
11 the value of the federal order as in your capacity as a
12 producer/handler in the past, and when you're trying to
13 decide what your milk cost is, did you view the federal
14 order as the end of either to set sort of a benchmark for
15 you as to what milk value was?

16 A. If I understand your question properly, I'm going
17 to try to answer it this way. I think the industry needs a
18 federal order very much because it does a lot more than
19 price milk. Okay. It's very important. If you're asking
20 me again, if the federal order price helped us compete, it
21 helped us compete because we did not have to pay into the
22 pool, but that was one of many factors.

23 MR. TOSI: Okay. That's all I have. Thank you
24 very much. I appreciate it.

25 THE COURT: Mr. Ricciardi, do you have any

1 questions of this witness?

2 MR. RICCIARDI: I do, Judge. Would you like me
3 to ask them now?

4 THE COURT: Well, maybe we -- it's after 10:00
5 o'clock. Let's take a 15 minute break. And before -- when
6 we come back, I'm going to ask Mr. Yale and Mr. Ricciardi
7 just to give me a list of their witnesses for claim (phon.)
8 purposes. Okay.

9 (Off the record and reconvened.)

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

11 I just met briefly with Mr. Yale and Mr.
12 Ricciardi to get a list of their anticipated witnesses for
13 the remainder of this proceeding, and I'm just going to
14 read that list off for people's interest. Obviously it's
15 still flexible. I may change things around, but after Mr.
16 Beene testifies, I have Alexis Koester, Rob Heerspink
17 (phon.), Don Morrison, Pete Ellis, Ron Knutson, one of the
18 Brandsmas, Duane or Ed, Flannigan, both of the Hennigahs,
19 Tom Swanson, a Costco rep. and Joe Albright. That's my
20 list of witnesses as -- that's the latest list of witnesses
21 that I have for the opponents.

22 And just a reminder, once again, if there's
23 anyone else, particularly from the Seattle area, I don't --
24 wherever we resume the hearing, it's probably not going to
25 be here. So anyone from this area who wants to testify has

1 to get it -- has to let me know and be done with it before
2 about 11:30 on Friday morning.

3 With that, I think I had Mr. Ricciardi was about
4 to get a chance to ask some questions of Mr. Beene.

5 EXAMINATION

6 BY MR. RICCIARDI:

7 Q. Al Ricciardi on behalf of Sarah Farms.

8 Good morning, Mr. Beene.

9 A. Good morning, sir.

10 Q. How are you?

11 A. I'm not sure. Thank you.

12 Q. I'm sure that as the clock ticks down, you're
13 getting better.

14 Your testimony today that you have given from the
15 start of this morning was from your personal knowledge, as
16 I understand it?

17 A. Yes, sir, to the best of my memory and
18 recollection, I have tried to answer their questions from
19 personal knowledge.

20 Q. You were there, you lived it, you remember the
21 best that you can?

22 A. I remember the best that I can, yes.

23 Q. I understand. Were you around when Gore went
24 through this process of trying to be limited as a
25 producer/handler --

1 A. Yes, sir.

2 Q. -- '88/'89?

3 A. Yes, sir.

4 Q. As I understand it, there's a hearing like this,

5 --

6 A. Yes, sir.

7 Q. -- and as I also understand it, there was a
8 proposed, I think, \$4 million cap in that situation?

9 A. There was one, and I don't remember what it was.

10 Q. And there was a claim at that point back in
11 '88/'89 that there's some kind of disorderly marketing with
12 regard to Gore and its area, correct?

13 A. That was there concern. Yes, sir.

14 Q. After '88 and '89, and after '93 or whenever the
15 decision was, were you still competing against the
16 regulated handlers in the area

17 A. Yes, sir.

18 Q. Was there competition with both regulated
19 handlers and other producer/handlers in the area?

20 A. I don't remember any other producer/handlers in
21 the area.

22 Q. Regulated handlers so existed?

23 A. Oh, yes, sir.

24 Q. And the sky didn't fall in on the regulated
25 handlers?

1 A. No, sir.

2 Q. You were asked some questions, and I think was
3 Mr. Beshore, and one of your responses was, and I'm going
4 to quote it as close as I can, "When we went to the bank,
5 they considered us to be one business or one entity."

6 A. Yes, sir.

7 Q. And in terms of operating as a producer/handler,
8 you considered yourself to be one business and one entity,
9 correct?

10 A. Yes, sir, we were. We either made it all as one,
11 or we failed all as one.

12 Q. And when there was milk from the dairy that went
13 to the processing plant, you didn't consider that you were
14 selling milk to the processing plant, did you?

15 A. No, sir, we were delivering milk.

16 Q. You also indicated, and I'll quote this, "that as
17 a producer/handler," and I think this may have been in
18 response to Mr. Marshall's questions, you "bet the farm."
19 Did I get that right?

20 A. I'm sorry?

21 Q. You "bet the farm" as a producer/handler?

22 A. Yes, sir, that's sort -- I shouldn't let my Texas
23 persuasion enter into this, I suppose, but that's sort of
24 what was said at the hearing. It was -- you've put so many
25 resources together, and they just don't fail separately

1 because they're all part of -- if one tire blows out on
2 your car, the car pretty well stops, and that's, I guess,
3 what I was trying to get to.

4 Q. Okay. Everything that Gore had was on the line,
5 as you said, in terms of being able to operate its business
6 when it was a producer/handler, correct?

7 A. Yes, sir.

8 Q. I mean, it had to get its own customers, correct?

9 A. Yes, sir.

10 Q. Had to balance its needs on a month-by-month and
11 a yearly basis in terms of its output and the customer
12 requirements, correct?

13 A. Yes, sir, except I'd amend what you said to say
14 that there were many, many, many times when that was a day-
15 to-day balancing situation.

16 Q. Fair enough.

17 I think it was Mr. Marshall that asked you a
18 question -- well, wait a minute. Gore had the option as to
19 whether to be a regulated handler or producer/handler; do
20 you remember that question?

21 A. Yes, sir.

22 Q. But it had the option without any kind of
23 artificial cap or limitation, correct?

24 A. That's correct.

25 Q. So the option was to be a producer/handler and be

1 subject to whatever requirements or regulations or to be a
2 regulated handler, but not have some artificial cap put on
3 it, correct?

4 A. Yes, sir.

5 Q. And I think this is a question that Mr. Tosi
6 might have asked you. He was inquiring on a topic about
7 one of the -- some of the factors that Gore went through in
8 making a decision as to be a producer/handler. And I think
9 that one of the things you said that, as a marketing
10 decision, you wanted to have a single source of your milk
11 to be able to market; is that -- am I recalling --

12 A. Yes, sir.

13 Q. -- your testimony correct?

14 A. Yes, sir. We use that in our advertising.

15 Q. What's the importance of having a single source
16 to a customer?

17 A. It seemed to appeal to a lot of customers in that
18 from all the way from the feed the cows ate, literally
19 because we had our own feed mills, all the way to appearing
20 on the shelf in a store, we not only maintained control of
21 it, but we're responsible for it and had to answer for it.
22 And there was nobody to lay anything off on, and on
23 occasion, if you got a -- some milk and you left it out in
24 your car while you did shopping somewhere else, and it
25 spoiled, they knew who to bring it to, and we made it good

1 for them. But if something else happened, we were also
2 responsible for it. Nobody else to lay the blame on.

3 Q. And is that true with regard to the entire
4 operations as a producer/handler that you had personal
5 responsibility, no one to lay the blame on, and you took
6 all of the risk involved in being a producer/handler,
7 correct?

8 A. Yes, sir, we took that into consideration, too,
9 before we came on -- became one, and realized we were going
10 to have to be big boys about it, and take care of things.

11 Q. In terms of advertising as a single source, was
12 that a benefit to the ultimate consumer, at least as
13 reported back to you, that they like the fact that they
14 knew this milk was coming from your farms and your dairies?

15 A. Yes, sir.

16 Q. After Gore became a PD, you competed with
17 regulated handlers, correct?

18 A. Yes, sir.

19 Q. You lost business of regulated handlers, correct?

20 A. Yes, sir.

21 Q. You gained some business from regulated handlers,
22 correct?

23 A. Yes, sir.

24 Q. Lastly, there's a question about what could you
25 have done with your excess milk, and I think you indicated

1 that there was a potential place for excess milk in Mexico.

2 A. No, I think I remember us being called on one
3 occasion by somebody that thought he could sell excess milk
4 in Mexico. It never did materialize into anything.

5 Q. And so you never did that?

6 A. No, sir.

7 MR. RICCIARDI: I don't have anything further.

8 Thanks.

9 THE COURT: Mr. Yale, do you have any redirect?

10 MR. YALE: Yes, Judge, a little bit of redirect.

11 MR. COURT: Mr. -- wait, you have a question,
12 too, Mr. Marshall?

13 MR. MARSHALL: Yeah, --

14 MR. YALE: Oh, I just want to be, you know, --

15 THE COURT: Do you want to be the last one --

16 MR. YALE: Let him go, and then he can follow up.

17 THE COURT: Okay. Go ahead, Mr. Marshall. Get
18 another chance.

19 MR. MARSHALL: Thank you, Your Honor.

20 EXAMINATION

21 BY MR. MARSHALL:

22 Q. Again, Doug Marshall with Northwest Dairy
23 Association, Mr. Beene.

24 Just want to follow up on two lines of cross-
25 examination from others. Just now in talking with Mr.

1 Ricciardi, you described your desire to be -- the strategy,
2 the business strategy for your company would be a single
3 source supplier/marketer for advertising purposes, and I
4 could understand that. I don't question that desire. I do
5 want to, though, ask if there's anything about that that
6 required you to be a producer/handler rather than to be
7 pooled and to be a -- to be -- let me rephrase the
8 question.

9 You could still have been a single source
10 processing plant and still have been a pooled producer and
11 a pooled plant, could you not?

12 A. No, sir, not the way we approached it. That
13 approach being that we fed the cows. We bought the cows.
14 We put the genetics into the cows. We milked the cows and
15 transported the milk. Then we processed the milk. So it
16 was the chain of custody, I guess, that we advertised with,
17 and it seemed to appeal to the consumer.

18 Q. I do understand that. I'm not questioning that
19 at all.

20 I'm referring to basically how the regulations
21 were. When you had bought Pure Milk initially, it was a
22 pooled plant?

23 A. Yes, sir.

24 Q. You were part of the pool?

25 A. Yes, sir.

1 Q. If -- and you had to go to the market
2 administrator and say, we wish to have our status
3 determined as fulfilling the requirements of a
4 producer/handler under this relevant, federal order, did
5 you not --

6 A. Yes, sir. That's correct.

7 Q. And you didn't have to do that, did you?

8 A. No, sir.

9 Q. You could've remained a pooled producer?

10 A. Yes, sir.

11 Q. And you could've remained a regulated plant?

12 A. Yes, sir.

13 Q. Now, at that point then it seems to me, and I'm
14 just -- my question is, was it the fact that you chose to
15 be a single source plant, or the fact that you were a
16 producer/handler that caused you to incur the costs of
17 balancing and so forth that you've described?

18 A. Oh, it was because we chose to be a
19 producer/handler.

20 Q. Now, wait a minute. How would it have worked
21 differently had you been -- had you remained a pooled plant
22 and a pooled producer?

23 A. The -- we could not at that point, and I sure may
24 be misunderstanding your question, but let me try. At that
25 point we could not have said, could not have claimed care,

1 custody, and control throughout the chain of custody of the
2 milk. And we were trying to convince the consumer that
3 because of that, we could guarantee a "better product."

4 Q. Well, you didn't have to buy from anyone else
5 just because you were a pooled producer and a regulated
6 plant, did you? You could still have bought normally from
7 your own dairy farm?

8 A. Yes, sir, but --

9 Q. And --

10 A. -- I think I said at the outset that one our
11 goals was to make more money, or to make money, and the
12 producer/handler phase of that contributed to that. It
13 just --

14 Q. How so?

15 A. -- wasn't all of it.

16 Q. How so? How did the producer/handler phase
17 contribute?

18 A. Because the costs of our milk was what it cost us
19 to produce it, which most of the time, most of the time,
20 not all the time, was a benefit.

21 Q. And when you chose to make that decision to
22 become a producer/handler, to take advantage of that
23 benefit, what was your thought about how you would use that
24 savings in raw milk costs to your plant?

25 A. To --

1 Q. Were you going to use that to expand the market,
2 to improve your facility, or to -- how would you intend to
3 use that?

4 A. Differentiating between the time that we were
5 making that decision as a theory, we hoped to be able to
6 expand our plant, get bigger, buy more cows. As it turned
7 out, after all of the ups and the downs, it didn't work.

8 Q. And when you attempted to expand your market, and
9 when you quoted prices to new customers in order to expand
10 your market, did you contemplate a price of milk at your
11 production cost on the farm, or did you contemplate a price
12 of milk equal to the class one price?

13 A. We used the class one price in our -- in building
14 our models.

15 Q. Well, I'm confused here because if you used the
16 class one price, you weren't getting any advantage out of
17 becoming a producer/handler, were you?

18 A. No, sir, we were not at that -- not on the
19 surface of that quote, but certainly we knew what the
20 producer/handler advantage was. We did that to see how
21 efficient we could get in our processing plant. We put
22 into the calculation milk at that price for a number of
23 factors -- well, really two. One, that is where our
24 competitor would be coming from.

25 Q. Yes. Understood.

1 A. So if we're going to compete in that world, then
2 let's start with the same priced milk he has. And number
3 two, you don't tend to price yourself out of business that
4 way.

5 Q. All right. So how were you going to expand your
6 market without a change in your cost structure?

7 A. Well, we were -- a lot of what we were counting
8 on was the efficiencies that are associated with larger
9 production or large --

10 Q. You could've done that -- excuse me. I didn't
11 realize you weren't finished. Please continue.

12 A. With larger output from the processing plant
13 which, to a point, until your barns are absolutely full,
14 would also be true at the dairy farm. And as I tried to
15 testify before, while we didn't put it into our calculation
16 of a price, we knew what the producer/handler benefit was,
17 and we relied -- we were going to rely on it to some
18 degree, varying degrees, because sometimes there wasn't
19 much.

20 Q. Well, you agree with me, would you not, that you
21 could've remained a pooled plant, regulated plant and
22 expanded your volume and utilized efficiencies related to
23 scale in expanding your volume?

24 A. Yes, sir.

25 Q. Without having to become a producer/handler?

1 A. Yes, sir.

2 Q. But you elected not to do that because you needed
3 the advantage of being a producer/handler, right?

4 A. That was certainly one of the reasons. It's not
5 the only one.

6 Q. So what were you intending to do with that
7 advantage then if not to price milk below the class one
8 price? What were your intentions?

9 A. Whoa. I'd as soon slap a wildcat as to go pick a
10 fight with some of those people. We needed to make money.
11 We knew our plant costs were not what theirs were.

12 Q. All right. So you're telling me you didn't
13 compete on price?

14 A. We competed on price all the time. It's just
15 that, as I stated earlier, in the long run, we couldn't --
16 we could not get our figures down to where their figures
17 were. So yes, sir, we competed on price.

18 Q. So when you say you couldn't get your figures
19 down to where theirs were, you mean you couldn't get your
20 figures down to where you felt you needed to be if you
21 assumed the class one price for your bottled milk?

22 A. When we lost a significant portion of our
23 business, we could not compete using the producer/handler
24 "advantage," and the volume we had built up in our plant.
25 The two combined were not enough for us to --

1 Q. Are you -- I think you're telling me, I'm going
2 to ask you, are you telling me that the advantage of a
3 producer/handler plant did not fall to your bottom line
4 enough to make you profitable?

5 A. That's correct.

6 Q. Thanks so much.

7 A. I appreciate your patience. I really do.

8 THE COURT: Mr. Yale, do you want to --

9 MR. YALE: No, I think Mr. Tosi had a few
10 questions.

11 THE COURT: Oh, go ahead.

12 MR. TOSI: Just a couple of more questions here

13 --

14 THE COURT: (Indiscernible)

15 EXAMINATION

16 BY MR. TOSI:

17 Q. Mr. Beene, I'm Gino Tosi from USDA.

18 A. Yes, sir.

19 Q. Just following up here a little bit. I guess it
20 adds to maybe what some of the questions Mr. Marshall was
21 asking you.

22 In the context of what you just said then, that
23 to the extent that you had -- if you could imagine for a
24 moment that your market share was larger than what it was,
25 if you were, say, ten percent of the market, and you had

1 achieved a certain plant efficiency, that you were hoping
2 to use as producer/handler advantage to impart to achieve
3 that, would you have been able to see a point at which,
4 given that your plant efficiency achieved a level that you
5 would -- were hoping to achieve, and that that in
6 combination with your impact in the market, or what percent
7 of the market that you represented, that the only thing
8 left then in your capacity as a producer/handler would be
9 this price advantage that you had over fully regulated,
10 class one handlers?

11 A. I'm sure you've asked a good question. I'm
12 having trouble -- is there any way you can simplify that
13 for me?

14 Q. Well, let me see if I can simplify it.

15 If you had achieved the desired plant efficiency,
16 --

17 A. Yes, sir.

18 Q. -- and maybe to put it in a homespun way, that
19 you were pretty much convince you're pretty much on a plan
20 efficiency that you're facing with your competitors who
21 were --

22 A. Yes.

23 Q. -- fully regulated, then it would seem logical,
24 and correct me if my logic's wrong, that then what you're
25 left with once you've achieved those things is, is that as

1 a producer/handler, this advantage that you now have over
2 your regulated competitors is that price difference, this
3 obligation that you don't pay into the pool, that leaves
4 you with a price advantage. And that coupled with, if you
5 also have a significant market share.

6 A. Yes, sir. The way you've phrased it, I'd have to
7 answer your question yes, that I can see it happening that
8 way. However, I think the indisputable fact that it didn't
9 work shows the pressure of the marketplace on the
10 producer/handler, plus it's a lot easier to make that model
11 than it is to make the model work.

12 Q. Right.

13 A. And we think we were doing a good job of our
14 calculations, but we'd also experienced some problems that
15 no one could've expected, and it -- that combination of
16 those things, we feel like that caught us, and our
17 competitors probably experienced the same thing. So I'm
18 not trying to say that we ought to have an advantage. We
19 shouldn't outside of the fact that we had to be responsible
20 all the way from the feed the cow ate to what went on the
21 shelf at somebody's store. And that's a great big
22 responsibility.

23 Q. And to the extent that someone, a
24 producer/handler is able to achieve all the most desirable
25 things, does there come a point in your opinion where, with

1 all the price advantages in terms of regulation that's
2 afforded to a producer/handler, and to the extent that
3 they're able to successfully exploit that advantage in the
4 enumerable ways that you would have to remain as a
5 producer/handler, to achieve all these quality differences,
6 --

7 A. Efficiencies.

8 Q. -- and all that -- efficiencies and all, that
9 there comes a point then where an entity that is very
10 successful in doing that places himself in par then with
11 folks that are fully regulated?

12 A. Okay. I think I understand --

13 Q. In other words, does there come a point where
14 these advantages should be no longer be afforded?

15 A. I would say -- you know, I wasn't in this
16 business, directly involved in it until '87, but I was on
17 the board during that period of time for about some 15
18 years before that. During that entire period of time, I've
19 never seen that occasion arise. In theory, I think it
20 sounds good. You'd like to think you could get there, but
21 I've never known a producer/handler that did.

22 So I think that's -- if you go back to the
23 statement I made about the market having a direct tendency
24 to control the producer/distributor, it just seems to me
25 that experience bears that out. That's an opinion.

1 MR. TOSI: That's all I had. Thank you very
2 much.

3 THE COURT: You have more questions?

4 MR. MARSHALL: Yes, Your Honor, I'd like to
5 follow up on one of these last comments here.

6 THE COURT: Go ahead.

7 MR. MARSHALL: With respect to --

8 THE COURT: Say who you are.

9 EXAMINATION

10 BY MR. MARSHALL:

11 Q. This is Doug Marshall with Northwest Dairy
12 Association.

13 With respect to the costs that I think you were
14 describing, in answer to Mr. Tosi's question, because you
15 had, as you put it, the responsibility and burden of
16 putting everything that went from the feed to the shelf,
17 what were those additional costs that you had because of
18 that? What you -- did you suffer some higher feed costs,
19 do you think, as a result of that decision to sole source
20 your feed?

21 A. No, sir, not necessarily. Our feed costs, we --
22 I could not tell you how much those costs were there very
23 dramatically, but an example would be that we had cows on
24 the dairy farm that we took to the sick pen if any sign of
25 mastitis showed up. We could not --

1 Q. Okay. So you affected how you managed the farm?

2 A. We could not count on blending our milk in with
3 someone else's.

4 Q. All right. So because you chose not to use
5 additional sources of milk, you had a disadvantage in both
6 the unexpected impact on your herd, and the inability to
7 buy other sources when you were short of milk?

8 A. Yes, sir.

9 Q. That was because of your decision to be
10 controlling your source?

11 A. Yes, sir.

12 Q. Then as a plant, you also had the responsibility
13 to find a way to market all of what you were --

14 A. Yes, sir.

15 Q. -- producing on the farm. So because you had
16 made a decision to buy from only one source, you had
17 additional costs there, including balancing costs, right?

18 A. Well, I don't think I'd say we bought from a
19 source. I think I would say that because we chose to be a
20 producer/distributor that yes, sir, we incurred some costs.

21 Q. Your balancing costs that you incurred -- I think
22 that's all I need to ask. Thank you so much.

23 A. Yes, sir. I'd simply add, you know, every month
24 was different, you know. Some months looked a lot better
25 than others.

1 THE COURT: There's no question before you, but
2 go ahead. Come on, Mr. Yale.

3 EXAMINATION

4 BY MR. YALE:

5 Q. Well, I forgot to ask one of the more important
6 questions. As a Buckeye, what happened to Baylor and
7 Oklahoma last week?

8 A. I thought you were going to be easy on me. We
9 did better than the Aggies. And we don't discuss
10 basketball.

11 Q. I just want to follow up on two things. In
12 pricing your milk -- I want to make sure this is clear.
13 You relied upon the class one price and your standard costs
14 and the packaging cost to price that milk, right?

15 A. Yes, sir, if it was a class one product. Yes.

16 Q. Right. And you said 13 cents was the target, but
17 I think the testimony also was, was that -- ended up that
18 was not going to be low enough?

19 A. That's what we were told.

20 Q. And that 13 cents was based on 1.2 million
21 gallons, reaching that; was that what --

22 A. I don't think we quite got to the 1.2 with that
23 one, Mr. Yale. I may have said something that -- I did say
24 that 1.2 was where we thought we could make a decent return
25 on our investment. I think we were just a little under

1 that with that particular quote, like 1.1 million, but we
2 would -- our anticipation was that from the barns to the
3 plant, we would have the capacity to do that.

4 Q. Now, you mentioned in the -- this thing. I think
5 there was a question like, you know, about the advantage
6 and disadvantage, and you said some of the time it was
7 advantageous to be a PD, and sometimes it was disadvantage
8 -- there was a disadvantage. And, you know, in the total
9 scheme of things, from 1987 when -- or, '88 when you became
10 a PD until 1995, I guess it was, when you sold --

11 A. Yes.

12 Q. -- the plant, what was the impact of being a PD?

13 A. Well, it was certainly, more months than not, it
14 was better for us to be a PD until we had that large
15 surplus of milk that we couldn't market anywhere. So I
16 guess in the big picture, you know, we won the battle and
17 lost the war. It didn't work.

18 Q. So in large part, that was -- being a PD and
19 dealing with the customer was a large percentage of your
20 sales, right?

21 A. Yes, sir.

22 Q. And because that was a large percentage of your
23 sales, to lose that, it was more difficult to replace that
24 size of a sale?

25 A. Yes, sir. It was. We always had what we thought

1 was one company back there that would be a fail-safe for
2 us, and we quoted them that quote I've been talking about.
3 It didn't work, and so your -- you've got all of that
4 excess milk, and you're going to get a buck less than class
5 three after you transport it. And that won't work either.

6 Q. Now, you understand what I mean by the term
7 "leverage?"

8 A. Yes, sir.

9 Q. And what is leverage?

10 A. Talking about our financial leverage --

11 Q. Right.

12 A. -- at the bank.

13 Q. Right.

14 A. What we owe, and you know, our bank was seeing
15 the same reports every month, and it was --

16 Q. Well, I believe in general the concept leverage,
17 what does it do? When you talk about your leverage, you
18 get to use leverage, how does it work?

19 A. I'm sorry, I --

20 Q. I'm -- let me just talk -- I mean, leverage is a
21 concept, means that you can take -- use the leverage, take
22 what you have and with some other things, do more with that
23 (indiscernible) --

24 A. Sure.

25 Q. -- right?

1 A. Yes, sir.

2 Q. And how does leverage work? Does it work the
3 same way in both directions? I mean if you're leveraged,
4 and you're making a profit, does it leverage your profits
5 and make them bigger or?

6 A. To leverage our profits?

7 Q. Yeah, I --

8 A. You take the profits and put them into more
9 assets?

10 Q. No, let's -- I'm going to withdraw the question.
11 I've got -- we're --

12 A. I'm sorry.

13 Q. That's okay. Based on these questions and the
14 concept that you reached a point where it worked for you,
15 and it didn't work. Would you suggest to the department
16 that in analyzing a PD issue, is that they need to take --
17 they need to recognize that a PD always is exposed to a
18 risk associated with that PD, even though they may not have
19 seen it at this point?

20 A. Yes, sir.

21 Q. And that if you are a PD and the risk of loss of
22 sales occurred, does that put you in a different situation
23 than if you are a regulated 7A plant that's paying minimum
24 prices?

25 A. About 180 degrees. Yes, sir, because you can't

1 call up and cancel the milk.

2 Q. Right. So although the cost has not occurred,
3 because of that loss of the sale and that excess supply,
4 that doesn't mean the risk is never there, right?

5 A. Risk is there every, single day.

6 Q. All right. Now, and the same thing, you talked
7 about this risk that if, you know, if a consumer picked up
8 a gallon of milk at a grocery store in Waco that said "Pure
9 Milk" on it and took it home and had a complaint about it,
10 that if it turned out to be a problem at the farm, as a
11 producer/handler, you were responsible for that, right?

12 A. Yes, sir.

13 Q. All right. And -- but if you were purchasing
14 this from a coop, would you be responsible for that?

15 A. Not necessarily. No, sir.

16 Q. You'd be able to shift that risk to the coop,
17 right?

18 A. Should be able to, yes, sir.

19 Q. Right. And -- but can you measure the value of
20 that? I mean, that really doesn't show up in a dollar and
21 (indiscernible) --

22 A. No.

23 Q. -- right?

24 A. No, sir.

25 Q. But it's there, right?

1 A. It's there. If you're going to claim the
2 advantages, then you got to take the risk of the
3 disadvantages.

4 Q. All right. I want to wrap up with this. There
5 was this -- I think it was by Mr. Marshall that said
6 something about that you could still buy the feed, grow the
7 feed, do the genetics with the cow, feed the cows, market
8 the cows -- or, not market, milk the cows, put the milk on
9 trucks, your trucks, haul -- use that milk, haul those
10 trucks down to your plant in Waco, bottle that milk, and
11 still have all the advantages of having that efficiency, so
12 to speak, from the farm to the consumer that you talked
13 about, but still pay money into the pool. Did you
14 understand that question? Did he make that question
15 something to that effect?

16 A. That's what I thought he was saying.

17 Q. All right.

18 A. Why would you pay money into the pool?

19 Q. Well, that was my question. Why -- what would
20 that -- why would you want to do that?

21 A. I think -- I took the direction of his question,
22 but he couldn't -- we achieved some of the same
23 efficiencies at the plant by getting this additional
24 volume. And, you know, the answer to that would be maybe,
25 because you just lost your calling card, which is, we

1 control it all. The issue of something foreign being put
2 into the feed or something that makes the cows give more
3 milk or anything, all those circumstances are under your
4 control. And if you choose to do those things, that's your
5 risk. If you choose not to do them, that's also a risk.

6 Q. But if you choose to do those things and you take
7 that risk, you shouldn't share the benefits from that risk
8 with others; is that your position?

9 A. Yes, sir. That's right.

10 MR. YALE: I have no other questions.

11 THE COURT: Thank you. You may step -- oh,
12 almost. I almost got --

13 MR. BESHORE: I'm sorry. Just --

14 THE WITNESS: Nice try.

15 EXAMINATION

16 BY MR. BESHORE:

17 Q. Just one question, Mr. Beene.

18 A. Yes.

19 Q. Marvin Beshore for Dairy Farmers of America.

20 A. Yes, sir.

21 Q. Did you testify, if I understood you correctly,
22 in response to Mr. Yale's last series of questions, that if
23 you're buying milk from a coop, and you process it and sell
24 it through a store, and a consumer finds a bad -- has a bad
25 experience with the product, that you're going to blame

1 that on the coop?

2 A. No, what I tried to say was you ought to be able
3 to do that, meaning that you can prove that you handled it
4 properly in your plant with all the charts and records that
5 you keep in the plant. Meaning that you at least have
6 somebody else to turn to, where the producer/handler
7 doesn't. If you got milk that was -- had nastatis count
8 (phon.), if you got milk that was below the regs. and the
9 bacterial count, you can pretty well turn that back to the
10 coop, get them to replace it, maybe replace your whole silo
11 full of milk.

12 Q. Well, if you're buying milk from a coop, before
13 you process it, don't you test it?

14 A. Yes, sir, you do.

15 Q. Test it for bacteria count, got specifications in
16 your contract. You're not going to buy it if it's got too
17 high a bacteria count, right?

18 A. You hope you don't.

19 Q. Well, what do you mean you hope you don't. You
20 test it, and you either buy it or you don't.

21 A. Yes, sir, that's right.

22 Q. Okay.

23 A. And if your tests turn up right, you're okay.

24 Q. So you're going to blame it on the coop if the
25 test -- if you tested it wrong?

1 A. I think it's a moot point. We didn't have a coop
2 to blame.

3 Q. Well, but that -- you were telling Mr. Yale, if I
4 understood you correctly -- maybe I didn't. Tell me I'm
5 wrong, we can stop. That if you're buying milk from a coop
6 and you process it and package it, and a consumer has a bad
7 experience with it, that you got the coop to blame.

8 A. Well, I see your point, and maybe I need to
9 retract my answer there.

10 Q. Okay.

11 A. They're not necessarily to blame.

12 Q. Okay.

13 A. No, I see where you're coming from, and I
14 apologize to you.

15 MR. MARSHALL: Okay. Thank you.

16 MR. BERDE: Let's talk about the reality --

17 THE COURT: Identify yourself.

18 EXAMINATION

19 BY MR. BERDE:

20 Q. Sydney Berde.

21 Let's talk about the reality of the marketplace.

22 A. Yes, sir.

23 Q. And what happens when Mrs. Jones buys a gallon of
24 milk from Safeway, Kroger, any retail outlet you want to
25 mention. She takes the milk home, milk is bad. She takes

1 it back to the store from which she bought it and said,
2 this milk is bad, and I bought it here. The next thing
3 that happens, isn't it a fact, the store gives her another
4 gallon of milk, and that's the end of the story?

5 A. Unless --

6 Q. That -- isn't that the reality of today's
7 marketplace?

8 A. Well, it's not the end of the story as far as the
9 person that supplied the milk to the store.

10 Q. But --

11 A. And that goes back to chain of custody.

12 Q. Well, though, they may go back to it, but that in
13 terms of the marketplace, that's how it works, isn't it?

14 A. Normally it would be. I should've stopped my
15 example with the receipt at the plant. If we shipped a bad
16 load of milk to our plant, we had nobody else to blame.
17 But if -- and co-mingled it with a silo. Now, it's not
18 supposed to be done.

19 Q. Well, if the retailer who purchases that milk
20 from a supplier, Oak Farms, for example, --

21 A. Okay.

22 Q. -- has that experience time after time with Oak
23 Farms, that retailer's going to change his supply source,
24 isn't he?

25 A. Absolutely is.

1 Q. And that's the end of that story --

2 A. Yes.

3 Q. -- in terms that a relationship between the
4 supplier of that milk and the retailer?

5 A. Yes, sir.

6 MR. BERDE: Thank you.

7 MR. YALE: I need to clarify this, Your Honor.
8 Benjamin F. Yale.

9 THE COURT: Go ahead.

10 EXAMINATION

11 BY MR. YALE:

12 Q. Let's talk about from the farm to the plant.

13 A. Yes, sir.

14 Q. All right. A load of milk arrives at the plant,
15 and you test it.

16 A. Yes, sir.

17 Q. And it's a bad load of milk, --

18 A. Yes, sir.

19 Q. -- and you're a PD.

20 A. Uh-huh.

21 Q. What's the result?

22 A. Well, you go dump the milk to the hogs.

23 Q. Right, and what about your supply to meet your
24 customers' needs?

25 A. You don't have it.

1 Q. Okay. 7A plant, you're paying into the pool.
2 Load of milk comes from the coop. You test it, and you
3 reject it. What happens?

4 A. You get another load.

5 Q. All right. Is that a financial advantage to a 7A
6 plant over a PD?

7 A. Yes, sir.

8 Q. All right. And the other part of it is, is that
9 there are circumstances that you -- regardless of what the
10 legalities are or whatever is, is that as a PD you are
11 responsible for it irregardless (sic), or regardless in
12 that the not having a coop there to replace the bad milk or
13 compensate you for damages done for bad milk, was a
14 detriment of being a PD over being a 7A plant?

15 A. Yes, sir.

16 Q. And is that a significant factor in deciding to
17 be a PD, or should it be?

18 A. It was in our case because we -- as I said, we
19 thought we could convince the public that they would be
20 better off buying our product.

21 Q. All right. That was my next point. That once
22 you're able to achieve that by taking that responsibility,
23 you went to the public and said, we take that
24 responsibility; --

25 A. Yes.

1 Q. -- that's right?

2 A. Yes.

3 Q. Could you have taken that kind of responsibility
4 if you weren't responsible all the way back to the plant --
5 all the way back to the farm?

6 A. Not and be truthful, no, sir.

7 MR. YALE: All right. Thank you. I have
8 nothing.

9 THE COURT: Do we have any more questions?

10 EXAMINATION

11 BY MR. MARSHALL:

12 Q. Doug Marshall, NDA. In that very last line of
13 questions, sir, responsibility back to the plant. That was
14 because of your strategic decision to be a single source,
15 and therefore to market to the public as a single source
16 supplier, correct? Because you could've bought some loads
17 of replacement milk as a producer/handler and still not
18 have lost your exemption, small number of loads in the bag
19 milk example, could you not?

20 A. We could not have bought a load. 2,100 gallons,
21 I don't think will fill up a tanker truck. It's like 4,500
22 gallons, but we -- in our order at that time.

23 Q. Well, if the -- perhaps, I want you to assume for
24 the sake of argument that you're into the Pacific Northwest
25 order today, --

1 A. Oh, okay.

2 Q. -- which allows up to 150,000 pounds of outside
3 purchases. You could've replaced a bad load of your own
4 milk with a load, say, from us in a situation such as you
5 described to Mr. Yale and still not have voided your
6 producer/handler exemption unless you bought 150,000 pounds
7 total, --

8 A. That's correct.

9 Q. -- and our trailer loads are about 70,000, so you
10 could've bought two loads from us. But you wouldn't have
11 done that, would you, as long as you had marketed to a
12 single source strategy?

13 A. I suppose not.

14 Q. So was the problem the producer/handler
15 regulation or your single source strategy?

16 A. The producer/handler regulation comes into play
17 in that we're telling our customer it all comes from -- has
18 all been controlled by us from the point it was milk until
19 it go virtually to their table.

20 Q. But you've said the producer/handler doesn't say
21 you have to provide all of your own milk. The
22 producer/handler regulations you can provide all of your
23 own milk except two additional loads, if you need to, from
24 in the case of the Pacific Northwest order, --

25 A. Yes.

1 Q. -- from people like me.

2 A. And --

3 Q. That's a marketing strategy to be single source,
4 is it not?

5 A. If that was Mr. Yale's question, then you're
6 right. I understood his question to be, could we have
7 claimed to have had care, custody, and control all the way
8 through the chain?

9 Q. And the answer's no?

10 A. And the answer is no.

11 Q. Okay. But that's -- has to do with the claim you
12 make as a single source processing plant, not because of
13 the producer/handler regulations, correct, because the
14 producer/handler regulations wouldn't allow you to buy
15 additional milk. It'd only because of your marketing
16 strategy that you're limiting your source of supply?

17 A. But you still couldn't tell the customer.

18 Q. That's true.

19 A. Okay. So --

20 Q. You couldn't tell the customer anything false
21 under other rules, but the federal order doesn't regulate

22 --

23 A. Oh, that's right. That's right.

24 Q. The Federal Food and Drug Act --

25 A. I see your distinction, but you -- that's right.

1 MR. UNIDENTIFIED: -- let him finish his answer
2 and then we're going to milk this cow completely dry?

3 THE COURT: Is there anything else in this line,
4 Mr. Marshall? Do you have -- I mean, it sounds like you
5 have your answer.

6 BY MR. MARSHALL:

7 Q. Did I get an answer, that you agree that it's a
8 different set of regulatory problems such as the Federal
9 Food and Drug Act that is prohibiting you from making false
10 claims, as opposed to anything with in the producer/handler
11 --

12 MR. UNIDENTIFIED: Well, Judge, I'm going to
13 object to that. The answer he got is on the record.
14 (Indiscernible)

15 MR. MARSHALL: Well, because I didn't hear the
16 answer because, by the way, he was interrupted --

17 THE COURT: If he can give a one word answer,
18 then we can be done with this witness, I hope, for the
19 witness' sake as well.

20 THE WITNESS: Yes.

21 MR. MARSHALL: Thank you.

22 THE COURT: You may step down.

23 THE WITNESS: Bless you. I do appreciate your
24 patience. I've tried to answer your questions honestly,
25 and you've been very patient with me.

1 THE COURT: You may call your next witness, Mr.
2 Yale.

3 MS. REED: Christine Reed (phon.), Your Honor, --

4 THE COURT: Okay.

5 MS. REED: -- on behalf of Pacific Northwest
6 Producer/Handlers, and we call Alexis Koester of Smith
7 Brothers Farms.

8 Your Honor, Alexis has prepared testimony that
9 we're distributing, and that I would like to have marked
10 also.

11 THE COURT: Okay. Let's see. This will be --
12 I'm going to mark this as Exhibit No. 39, and I'll swear
13 you in first. Would you please raise your right hand.
14 (Exhibit No. 39 was marked.)

15 ALEXIS KOESTER, WITNESS, SWORN

16 THE COURT: Okay. And can you please state and
17 then spell your name?

18 THE WITNESS: My name is Alexis Koester, A-l-e-x-
19 i-s, K-o-e-s-t-e-r.

20 THE COURT: Go ahead.

21 MS. REED: Thanks, Alexis. Please go ahead, and
22 read your testimony.

23 THE WITNESS: "I am the president of Smith
24 Brothers Farms. Smith Brothers is a family owned, small
25 business based in Kent, Washington. Kent is located

1 halfway between Seattle and Tacoma, and our milk and dairy
2 products are distributed almost exclusively within the
3 Puget Sound region.

4 "We currently produce more than three million
5 pounds of milk per month, and our business would suffer if
6 Proposal 1 or Proposal 2 were to be adopted. In addition,
7 we currently ship surplus milk to a processor in Alaska,
8 and the adoption of either proposal, even without a
9 production cap, would adversely affect our ability to
10 balance our milk supply.

11 "I am testifying in oppositions to Proposals 1
12 and 2 in their entirety.

13 "Since 1960 we have operated as a
14 producer/handler in Order 124 without creating disrupting
15 marketing conditions, and there is no evidence that
16 disrupting marketing conditions are now occurring. We have
17 carefully operated our business under guidelines that the
18 department has left virtually unchanged, and Congress has
19 consistently protected.

20 "We do not purchase milk from any source. All
21 the milk we process comes from our own herd.

22 "Benjamin Smith, my grandfather, established
23 Smith Brothers in 1920. We have been serving our customers
24 for four generations, and the Smith family always has been
25 intricately involved in the operation of the business.

1 Currently six members of the Smith family make their living
2 by working in the operation of the dairy. Four of the five
3 voting stockholders are women.

4 "In addition to my family members who are
5 involved with the dairy, we employ 110 people in our
6 production and processing operations, whose families depend
7 on our continued existence. We also contract with
8 approximately 60 independent distributors who service our
9 customers through home delivery of our dairy products.
10 Approximately one third of our employees are Hispanic.
11 Their livelihood also depends on our continued existence.

12 "Over the years, dramatic changes in the dairy
13 industry have been seen. We have been able to survive by
14 providing niche services to our customers in areas that are
15 unserved or under-served by other distributors in the
16 marketed area.

17 "Our markets are those which have largely been
18 abandoned by regulated processors. Our largest market, for
19 example, is home delivery of milk products. While the once
20 familiar milkman has all but vanished from the American
21 landscape, we still sell approximately 70 percent of our
22 products through home route distribution through
23 independent distributors. In 1980, home deliveries
24 accounted for only 33 percent of our sales, but we have
25 been able to increase our presence in this niche market,

1 while others have all but abandoned it.

2 "Over 30,000 Seattle area families depend on
3 Smith Brothers to supply their dairy products directly to
4 their homes. We fully expect that home delivery will
5 continue to be our primary outlet into the future, but our
6 future, even in that market is dependent upon our ability
7 to grow as may be necessary to meet the demands of our
8 unique market.

9 "Our product list includes fluid milk,
10 buttermilk, chocolate milk, eggnog, whipped cream, half and
11 half, and sour creme. We also serve our customers by
12 providing delivery of staple food items such as coffees,
13 eggs and juices. In addition to our home delivery routes,
14 we also serve coffee shops, restaurants, schools, and small
15 businesses by providing many of the same products for their
16 unique needs.

17 "Unlike the milk bottled and sold by the
18 proponents of this rule change, we do not sell our product
19 through large retail outlets or chains. We have chosen to
20 compete in a different arena.

21 "In addition to serving unique customers, we have
22 been able to compete by differentiating our products. One
23 quality of our milk is that Smith Brothers guarantees it to
24 be BST-free, which is a feature that many of our customers
25 find important. By controlling the quality of our bottled

1 milk starting with raw milk production, we can deliver
2 great tasting products more consistently. This is another
3 feature of Smith Brothers Farm's milk that our customers
4 appreciate.

5 "We operate as a producer/handler in full
6 compliance with the current federal regulations, and we
7 have built our operation to ensure our continued compliance
8 with the rules. Over the years, we have been presented
9 with numerous challenges to our status as a
10 producer/handler.

11 "Most recently the USDA received comments from
12 the industry during the course of federal order reform that
13 suggested the curtailment or elimination of the
14 producer/handler exemption. The secretary properly
15 concluded that it has been a long-standing policy to exempt
16 from full regulation many of those entities that operate as
17 both a producer and handler. A primary basis for exempting
18 producer/handlers from the pricing and pooling provisions
19 of a milk order is that these entities are customarily
20 small businesses that operate in a self-sufficient manner.
21 Also during the history of producer/handler exemption from
22 full regulation, there has been no demonstration that such
23 entities have an advantage as either producers or handlers
24 so long as they are responsible for balancing their fluid
25 milk needs and cannot transfer balancing costs, including

1 the cost of disposing of reserve milk supplies to the other
2 participants, 64 Federal Regulation 16135, April 2nd, 1999.

3 "The secretary also discussed the small changes
4 that were made to producer/handler regulations for the sole
5 purpose of standardizing the consolidated orders.
6 Importantly, the secretary noted that no changes have been
7 made that would intentionally regulate a producer/handler
8 that is currently exempt from regulation under current
9 operating procedures, i.d. (phon.) the secretary also took
10 note of Congress' unwavering support of the
11 producer/handler exemption.

12 "Smith Brothers is now faced with another
13 challenge to our continued existence. Despite not
14 significant change in marketing conditions since order
15 reform and without any evidence of disorderly marketing
16 having been presented at this hearing, the proponents again
17 seek to shut our doors. All the talk about equal
18 treatment, fairness among producers, and unfair competition
19 is simply not born out by the facts. In reality, this
20 hearing is an attempt by the largest players in the dairy
21 industry to reallocate Smith Brothers Farms to the low end
22 of the marketplace.

23 "The adoption of the cap on producer/handler
24 production, even one that would exempt our farm today,
25 would limit our future growth at a time when farm sizes are

1 increasing, cooperatives are consolidating, and independent
2 processors are vanishing.

3 "Elvin Hollon's testimony reveals the goal of the
4 proponents. It is to freeze producer/handlers out of any
5 real chance to compete with DFA and Dean Foods for
6 warehouse and superstores sales, the fastest growing
7 segment of dairy sales. This is anti-competitive and would
8 only vest more power in a small number of entities that
9 already exert far too much control in this industry.

10 "The proposals, if adopted, would force Smith
11 Brothers Farms to change the way we operate our business,
12 and we would incur increased cost. Depending on market
13 conditions, our ability to continue our operation may be
14 threatened.

15 "The loss of nearly \$1 million per year is
16 particularly troubling to Smith Brothers Farms by natural
17 well-being because of the debt load that we are currently
18 carrying. This was a result of a new farm which we built
19 two years ago, and which is based 150 miles from our plant.
20 I want to stress that the decision to build a new farm was
21 not the result of herd expansion. Our herd size did not
22 increase with the move. That move was necessitated by
23 environmental and population concerns because of our
24 proximity to the Seattle area. In addition to our capital
25 costs, we face increased transportation costs with this

1 move.

2 "The impact of the various proposals would force
3 Smith Brothers to incur additional costs in the form of
4 class one settlement fund contribution, despite the fact
5 that we purchase no milk. Even if the AMAA were to permit
6 such action, the proponents' own testimony established no
7 basis for this dramatic change in policy.

8 "In the proponents' testimony, they have
9 submitted a table showing the number of producer handlers
10 in Oregon and Washington, which shows route distribution
11 for the years 1975, '80, '85, '90, '95, and 2000. See
12 Exhibit 7, Table 4. This exhibit plainly demonstrates that
13 the number of producer/handlers declined during that period
14 from 73 to 11. Although route distribution has climbed
15 over the full 25 year period, route distribution by
16 producer/handlers has fallen by nearly six percent since
17 the year 2000. See Exhibit 20.

18 "The reduction in the number of producer/handler
19 reflects the consolidation in the industry, but also
20 reflects the reality that being a producer/handler involves
21 a substantial amount of risk that the typical dairy farmer
22 does not bear.

23 "The unfair advantage claimed by the proponents
24 is a fallacy. The proponents have repeatedly testified
25 about the allegedly unfair and unjustifiable advantage

1 enjoyed by producer/handlers and have suggested that we can
2 out-price competitors at will. This is false and is not
3 supported by the facts.

4 "Common sense and simple economics tell us that
5 if there are large and easy profits to be made by operating
6 as a producer/handler, there will be a rush to seize that
7 opportunity. That has not happened. If being a
8 producer/handler was the fast track to wealth that the
9 proponents claim, then why aren't there more of us?

10 "Changes in marketing conditions since 2000 have
11 not been favorable to producer/handlers. Table 11 of the
12 market administrator's statistical information for Order
13 124 class one in area sales establishes that the percentage
14 of those sales attributable to producer/handlers has
15 actually decreased. Using that data, we calculate a simple
16 ratio of class one sales by producer/handlers in Order 124
17 to all class one sales in the order. In 2000
18 producer/handler sales accounted for 10.43 percent of class
19 one sales in the order. For all of 2002, the percentage
20 had decreased to 10.08 percent, and the first six months of
21 2003, the percentage is only 9.8 percent. See Exhibit 7.

22 "Further analysis of the same market
23 administrator's data indicates a decline in the presence of
24 producer/handlers as class one suppliers to the
25 marketplace. Our Table 3 compares for each of the first

1 six months of this year the year-over-year change to
2 producer/handler class one route distribution. Between
3 2001 and 2002, there was an average decrease of four
4 percent, and the first six months of 2003 were at only
5 94.35 percent of the sales for 2000. See Exhibit 20.

6 "For the reasons cited by the secretary, in order
7 of her last decision on this topic, the department should
8 not adopt these proposals. Payment into the producer
9 settlement fund by producer/handlers is not authorized by
10 statute, and even if it were, it contradicts Congress'
11 often repeated intent that the producer/handler exemption
12 be preserved and would also constitute a change in the
13 long-standing policy of the department.

14 "The proponents seek to close our business
15 despite the fact that Smith Brothers does bear all of its
16 balancing costs, is entirely self-sufficient and is a small
17 business as a dairy products manufacturer that employees
18 less than 500 employees. Any growth of our production in
19 recent years has been due to increased efficiencies, not
20 additions to our herd. In fact, we are milking about the
21 same number of cows today that we were milking 20 years
22 ago.

23 "Smith Brothers Farms is not engaged in unabated
24 growth as has been suggested. Accordingly, we have not
25 added substantial amounts of milk to the Pacific Northwest

1 order. The proponents suggest that our operations threaten
2 their ability to market milk in the order, and that Smith
3 Brothers Farms is somehow a threat to their business.
4 These claims are made despite the fact all of our --
5 despite the fact all of the proponents and most, if not
6 all, of the others testifying in support of the regulations
7 are significantly larger than our operation. In fact, with
8 the possible exception of other producer/handlers, our
9 processing facility is smaller than most of those within
10 Order 124.

11 "The businesses that compete with Smith Brothers
12 Farms for the small percentage of our sales outside of home
13 delivery are all able to compete effectively against us.
14 Testimony was given about sales we lost to a Vitamilk
15 distributor. The loss of this sale was not due to undue
16 greed on the part of Smith Brothers Farms. Aside from the
17 fact that we do not control the bids entered by our
18 distributors, I can recount numerous sales contracts that
19 we did not win. In many cases, we find that we are outbid
20 by contracts for some of the competitors here today. We do
21 not have an unfair price advantage over regulated handlers.
22 If we did, we would never lose a sale on price, but we do
23 lose sales based on price.

24 "Instead of leveling the playing field as the
25 proponents suggest, the adoption of these proposals would

1 place us at a distinctive price disadvantage. Based upon
2 the letters submitted to the department, we believe that
3 the real purpose of this hearing it to prevent or dissuade
4 a new large Oregon dairy farm from becoming a
5 producer/handler and competing with Dean Foods and DFA for
6 that part of the market now serviced by predominantly large
7 players.

8 "The proponents of the changes, all large
9 cooperatives or the large handlers they serve, have heard
10 rumors about this farm, and they are fearful about losing
11 revenue to the Boardman Dairy should he obtain PD status.
12 Of course, this is pure speculation at this time. By
13 eliminating producer/handler status as a viable option, the
14 proponents would succeed in that effort and Smith Brothers
15 Farms would be a casualty of their protectionless actions.

16 "However, the current marketing conditions do not
17 support a change in the order. The imposition of a cap,
18 even one high enough to exempt Smith Brothers Farms would
19 restrict our future growth whatever that may be. Meanwhile
20 other farmers, other cooperatives, and other handlers
21 retain the ability to expand without restriction.
22 Furthermore, the imposition of any cap base on what
23 marketing conditions might occur in the future is
24 unjustified and speculative.

25 "Of course, a cap that is lower than our current

1 production would force us to examine whether to continue as
2 a producer, whether to continue as a handler, or whether it
3 would be feasible to continue operations at all. Quite
4 simply, this proposal would dramatically injure or
5 terminate our business, all because the proponents fear the
6 unknown affects of a possible new competitor.

7 "As the secretary has noted in previous
8 decisions, there is no demonstration or evidence that Smith
9 Brothers Farms or any other producer/handler hold an unfair
10 advantage as a producer or a processor. In fact, the
11 evidence established that in exchange for partial
12 regulation, we bear costs usually born by other market
13 participants.

14 "The proponents also testified that
15 producer/handlers do not play by the same rule as other
16 market participants. That is untrue. We all play by the
17 same rules. All producers and processors are subject to
18 the same marketing orders. If we purchase milk, we would
19 pay into the pool and draw from it, just as do other
20 processors and producers who buy and sell raw milk.
21 Similarly, there are no barriers that prevent a handler
22 from buying a dairy herd or that prevent a dairy farmer
23 from opening a bottling facility.

24 "Producer/handler status place limits on the
25 types of customers that we can effectively serve. First,

1 we can only serve those customers who require less milk
2 than we produce. Unlike a pool handler, we cannot simply
3 purchase more milk to fill the larger growing needs of a
4 customer. We cannot serve customers whose demand for milk
5 is irregular.

6 "Our profitability depends on our ability to
7 effectively control our surpluses and its disposition.
8 When a customer has needs that exceed our farm capacity or
9 would upset our ability to balance, we are faced with a
10 choice of losing our producer/handler status or a customer.
11 Our limited ability to service large accounts demonstrates
12 yet another reason why we are not direct competitors of the
13 Krogers, Safeways, and Dean Foods of the world. This
14 proposal would, however, effectively bar us from ever
15 servicing these processors.

16 "The proponents have suggested that payments from
17 producer/handlers into the producer settlement fund are
18 necessary because Smith Brothers and other like situated
19 producer/handlers enjoy an unfair advantage because we can
20 acquire our milk -- our class one milk for the blend price.
21 This is not accurate. Smith Brothers does not, as
22 suggested, enjoy an advantage equal to the difference
23 between class one price and the blend price. Our milk is
24 acquired at whatever our costs of production is. Our cost
25 of production often exceeds the Order 124 blend price, and

1 in times of weak prices, it exceeds the class one price.
2 Likewise, a producer/handler has its own blend of uses
3 because none of our -- not all of our milk is used in class
4 one products.

5 "This blend which Mr. Hollon identified in his
6 testimony must also take into account the unique and
7 significant balancing costs of producer/handlers. We sell
8 surplus milk for less than class price. Typically we are
9 paid the class three price, less \$1.50 per hundredweight.
10 In addition to the cost of balancing, producer/handlers
11 have expenses in transportation that other producers do not
12 bear.

13 "Producer/handlers bear huge amounts of risk in
14 the event there are problems at their processing facility.
15 A stoppage in production can mean the loss of raw milk that
16 cannot be replaced by a purchase from another farm.
17 Likewise, problems on the farm, such as herd health issues
18 are not only a loss to a producer, they can mean the loss
19 of milk to the plant that cannot be replaced. The result
20 can be lost customers.

21 "Managing the timing of deliveries to the plant
22 is also critical, or we must incur additional cleaning
23 costs and difficult scheduling. These demands, in addition
24 to increasing our operating costs effectively self-regulate
25 the size of producer/handlers. At the farm level, we are

1 required to carefully maintain the level of our herd.
2 Fluctuations pose the risk of causing large pool plant
3 purchases which would require us to lose our status, or
4 alternately have large surpluses, which must be disposed
5 of, often at substantial loss.

6 "These balancing demands are unique to
7 producer/handlers and have required us to find novel ways
8 to remain competitive. One of our solutions has been to
9 ship milk to Matanooska Maid in Alaska. Their expenses
10 associated with that which other producers do not
11 experience that are not accounted for either by the
12 proponents' incomplete suggestions (phon.). Despite these
13 costs, we are proud that we have found another under-
14 service market that both balances our supply and provides a
15 wholesome supply of milk to Alaska.

16 "In summary, there was no disruption in the
17 marketplace found during order reform. There have been no
18 changes in the marketing conditions and the marketing areas
19 since order reform. There are no facts supporting the
20 change or disruptive marketing. The proposal should not be
21 adopted."

22 MS. REED: Thank you, Alexis. The witness is
23 available for examination.

24 EXAMINATION

25 BY MR. BESHORE:

1 Q. Marvin Beshore for Dairy Farmers of America.

2 Good morning, Ms. Koester.

3 A. Good morning.

4 Q. Tell me more about Smith Brothers Farms. How
5 many cows do you milk?

6 A. We have about 32/3,300 cows, some of which are
7 dry and.

8 Q. Okay. And that's about the same number you had
9 -- you've had over the last 20 years, --

10 A. Yes.

11 Q. -- I think you testified.

12 A. Yes.

13 Q. What's your average production per cow today?

14 A. That's proprietary information.

15 Q. Proprietary?

16 A. Uh-huh.

17 Q. Okay. What was it 20 years ago?

18 A. I don't know.

19 Q. Okay. The -- how many employees are involved on
20 the farm production side of your business?

21 A. I believe it's about 45 or 50.

22 Q. 45 or 50?

23 A. Uh-huh.

24 Q. Okay. By the way, is your average production per
25 cow more or less than the state average; do you know that?

1 A. I don't know. Don't know that.

2 Q. 45 or 50 employees at the farm. How many of
3 those are family members?

4 A. Currently there are no family members working on
5 the production side of the farm.

6 Q. The 45 or 50 members on the production side, how
7 many of those are managerial employees, supervisory? Well,
8 do you have any?

9 A. Yes.

10 Q. Okay. And --

11 A. I don't know the exact number.

12 Q. What are the -- you know, the job categories,
13 what jobs, what managerial jobs you have at the farm level?

14 A. Well, we have a farm manager --

15 Q. Okay.

16 A. -- who manages the overall farm. And then we
17 have herdsmen, and then I believe that there's some
18 assistants under the farm manager. They're assistant
19 managers, and then the herdsmen under that.

20 Q. Do you employ a nutritionist?

21 A. Yes. He's not an employee.

22 Q. Not an employee?

23 A. No.

24 Q. Okay. How many farm locations do you have?

25 A. We have one.

1 Q. And that's the new one?

2 A. Yes.

3 Q. Okay.

4 A. I'm sorry, we have a few cows in Kent that we --
5 when we moved our cows to Eastern Washington, we kept a few
6 cows, under 100 in count.

7 Q. Okay. Is that the show string?

8 A. Somewhat.

9 Q. Okay. By the way, is that a facility which is
10 open for display to the public, if you -- you know, if you
11 want to buy Smith Brothers milk, you can come see our farm
12 and our cows?

13 A. Not at the present time.

14 Q. Okay. So you've got a 3,000 cow dairy at the new
15 location. How many acres did you buy there?

16 A. I believe it was about 250.

17 Q. Okay. And you moved them there from Kent because
18 sounds like you're getting squeezed by suburbia.

19 A. We also had another farm in Snohomish, so we
20 consolidated the two. We were getting squeezed both
21 places.

22 Q. Okay. Did you sell the land at those locations?

23 A. We sold the land in Snohomish.

24 Q. And in --

25 A. In Kent we did not. We -- that's where our

1 processing plant and our distribution center is.

2 Q. Okay. Was there land in Kent used for milk
3 production?

4 A. Yes.

5 Q. There was?

6 A. Yes.

7 Q. Okay. What's that land used for now?

8 A. It's just sitting there vacant because we are so-
9 in farm (phon.) and we can't really do anything else with
10 it.

11 Q. Okay. How -- the farm in Snohomish, how large
12 was it that you sold?

13 A. 500 acres.

14 Q. Okay. Was that also being encroached upon by
15 development?

16 A. Yes.

17 Q. Okay. Did you sell it for development?

18 A. No, it's also so-in farming (phon.).

19 Q. Okay. The -- your home delivery business. Let
20 me ask you about that. Do you -- is any of that done by
21 employees?

22 A. No, we have independent distributors because back
23 in the 1970s, we made an agreement with the union that we
24 could turn our retail business over to them. The employees
25 that were working for us could become independent

1 distributors because it -- we just couldn't continue it
2 with union paid employees. So they are all one man shows
3 where they each have their own route and their own set of
4 customers.

5 Q. Okay. Do you know what their prices are to their
6 home customers for a gallon of Smith Brothers milk?

7 A. I don't know their exact prices because they can
8 vary depending on the area.

9 Q. Okay.

10 A. And we don't do a lot of gallons of milk like
11 it's been talked here. We do mostly half gallons.

12 Q. Okay.

13 A. That's what we sell. And I know they have to be
14 competitive with the grocery store, so my guess is that
15 they're selling about that price that they can get at the
16 grocery store.

17 Q. You're -- you think that your independent
18 distributors are providing home delivery of milk for the
19 same price that Kroger or Safeway is offering it out of the
20 -- off the grocery shelf to the consumer who goes and
21 purchases it and takes it home?

22 A. I believe it's competitive with the half gallon
23 prices in --

24 Q. The half gallon prices. Excuse me.

25 A. Half gallon price, not the gallon at all.

1 Q. Okay. What do your distributors get for their
2 labor and delivering the milk?

3 A. The difference between what we charge them and
4 what they sell it for.

5 Q. Okay. What do you charge them this month?

6 A. Well, my -- our competitors are here in the room,
7 and I can't really tell you what we charge them.

8 Q. Okay. But you're certain that their sales price,
9 home delivered to their customers, is -- by competitive I
10 assume you mean roughly equal to the out-of-store price for
11 half gallons at Kroger or Safeway stores?

12 A. No, I'm not positive about that.

13 Q. Okay. You don't really know; is that your
14 answer?

15 A. I really don't know.

16 Q. Did I read that, what, 70 percent of your
17 products of your class one sales are home delivery?

18 A. Yes.

19 Q. Okay. What is your class one sales volume,
20 approximately, on a monthly basis?

21 A. Well, it varies from month to month, and a lot of
22 it has to do with schools --

23 Q. What's the range?

24 A. I'd say it's probably at the highest five
25 million, and at the lowest it could be four.

1 Q. Four to five million? Okay.

2 How many school -- schools do you service?

3 A. We service about ten school districts, and the
4 one thing that has been unique with us in that area is, we
5 have company drivers that actually deliver that milk to the
6 schools. We -- it's not like the distributors of most of
7 the other dairies where they sell it to them and they do
8 it. Our actual company drivers go directly to the schools
9 with the milk.

10 Q. So your school milk is provided directly by your
11 company and not through distributors?

12 A. Yes.

13 Q. And you bid on those school milk projects
14 directly by your company then?

15 A. Yes.

16 Q. Okay. You bid flat prices for your milk to the
17 school districts?

18 A. If that's what they ask for. We -- whatever they
19 ask for. Some of them ask for flat, some of them ask for
20 escalated (phon.), and we do both.

21 Q. Do you know -- now, you say the family's not
22 involved on the production side. It is involved on the
23 processing side of the business, I assume?

24 A. Yes.

25 Q. Okay. And what is the processing capacity of

1 your plant? How much milk could you process if it was
2 running at full capacity, fluid milk products?

3 A. Oh, probably not much more than six million
4 without running around the clock, which we almost are
5 anyway without, you know, with clean-up time and that. So
6 probably six million.

7 Q. Seven days a week you're running?

8 A. No, six.

9 Q. Six. What variety of containers do you package?

10 A. We have some gallons, majority half gallons,
11 quarters, pints, and half pints.

12 Q. Okay. Why is it you don't sell gallons on home
13 delivery?

14 A. We're not very efficient in our gallon. We
15 aren't set up for gallons. It's just not something that we
16 ever tried to get into. We've just stuck with the half
17 gallons, and we just never got into the gallon business.
18 So our machine is very inefficient.

19 Q. Okay. Now, do you know -- well, let me ask you
20 about your Alaska sales. Your sales to -- how long have
21 you been selling to Alaska?

22 A. I'm not sure.

23 Q. Okay. That's bulk milk that's sold to Alaska?

24 A. Yes.

25 Q. Okay. And you treat the milk before it's -- it's

1 pre-pasteurized or heat-treated before it's shipped up
2 there?

3 A. Yes.

4 Q. In your plant?

5 A. Yes.

6 Q. Okay. What price do you get for that milk?

7 A. That's confidential.

8 Q. Okay. Get more than the class three price for
9 that class one milk you're sending to Alaska?

10 A. I would hope so.

11 Q. Well, you know --

12 A. I don't know their -- I don't know the exact
13 price.

14 Q. Well, you're president, right?

15 A. Yes.

16 Q. You don't know how much you're --

17 A. But it's a blended price of something, and I
18 don't -- I'm not the one that gives them that price. Our
19 controller does that, so I don't know the exact price.

20 Q. Well, I take it from your testimony it's a better
21 sale than the sale of surplus milk to Northwest Dairy
22 Association.

23 A. It is better than that, yes.

24 Q. Okay. But you don't know the relationship to the
25 class one price and the market for that milk which you have

1 processed and heat-treated to Alaska?

2 A. Not off the top of my head, I don't.

3 Q. Are you charging for the processing service that
4 you do on the milk before you ship it --

5 A. It's figured into the price, yes.

6 Q. There's a distributor who's going to testify
7 tomorrow, Mr. Ellis. Is he one of your distributors?

8 A. Yes.

9 Q. Okay. Is he one of your home delivery
10 distributors?

11 A. Yes.

12 Q. So he might know more about what price he charges
13 to your home delivery customers than you do?

14 A. He would know what he charges.

15 Q. Right. Okay. Are there any other dairies in
16 Washington that do home delivery of milk?

17 A. I believe that Wilcox may have some distributors
18 that do home delivery that they inherited from Vitamilk. I
19 don't know -- Dairy Gold might, too. I don't know.

20 Q. Now, you have -- you've made the statement a
21 couple of times in your testimony. By the way, did you
22 write your testimony?

23 A. I did it with the help of my attorney.

24 Q. Are you an attorney?

25 A. No.

1 Q. Had you -- did you locate the language from the
2 Federal Register that you quoted on page five of your
3 testimony?

4 A. I was shown it. They located it for me.

5 Q. Okay. Do you know -- have you ever read the
6 Agricultural Marketing Agreement Act?

7 A. In its entirety, no. Parts of it.

8 Q. Okay. You've stated a couple of different
9 locations that you play by the same rules as all other
10 market participants. Do you recall that?

11 A. Uh-huh.

12 Q. Okay. Well, you don't -- in terms of regulated
13 distributing plants, you don't account to the market
14 administrator at the class prices for your products,
15 correct -- for you utilization, correct?

16 A. We show them. They get a full report of where
17 our utilization is.

18 Q. But you do not pay class -- an account to the
19 producer settlement fund for the minimum class values --

20 A. No.

21 Q. -- for your usage?

22 A. No, our cost is what our cost is.

23 Q. Okay. Do you know what your cost is?

24 A. It varies.

25 Q. Okay. Do you know what it is -- can you tell me

1 what it is -- what it has been for any particular period of
2 time?

3 A. Well, it depends on what cost -- if we're had
4 (phon.) everything into it, and I don't think I'd want to
5 say that in front of my competitors.

6 Q. Well, first of all, do you know -- well, when you
7 say, you know, you -- when you just said, you know, your
8 cost is what your cost is. What costs are you talking
9 about?

10 A. When we do our income statement, whatever it
11 costs us to produce the milk, what it costs to transport
12 it, what it costs in the plant to process it and the
13 packaging, and then what it costs to deliver it and get it
14 on the trucks, that's what our cost is. And then what we
15 sell the milk for in finished product is what our selling
16 price is, and the difference is either a profit or a loss.

17 Q. Has Smith Brothers been profitable?

18 A. Sometimes.

19 Q. Are -- how many family members are employed in
20 the business as employees -- salaried as employees?

21 A. There are five that are employees, and one is a
22 distributor.

23 Q. Okay. Do you produce any products other than
24 fluid milk products, any class two products? Do you make
25 ice cream?

1 A. No.

2 Q. Cottage cheese?

3 A. No.

4 Q. Cream products of any --

5 A. We do sour cream, half and half, and whipping
6 cream.

7 Q. Okay. Do you sell -- do you have excess cream to
8 sell?

9 A. Sometimes we do, sometimes we don't.

10 Q. Okay. So there are times when your own sales of
11 product, including the whipping creams, utilize all of the
12 butter fat produced by your cattle?

13 A. Yes.

14 Q. Okay.

15 A. Majority of the time.

16 Q. Most of the time it does?

17 A. Yes.

18 Q. So what -- approximately what portion of your --
19 oh, by the way, are your milk products standardized for
20 test? Your fluid milk products, your -- when you sell
21 whole milk, what's the butter fat test at?

22 A. Oh, they are standardized.

23 Q. Okay.

24 A. Whatever the standard is, the 3.5 or whatever the
25 allowance. It always is in that.

1 Q. Do you sell low fat also?

2 A. Yes, yes.

3 Q. And skim?

4 A. Yes.

5 Q. Okay. But most of the time you utilize all your
6 butter fat --

7 A. Yes.

8 Q. -- produced?

9 A. Yes.

10 Q. Does that mean that when you're selling off
11 surplus milk, it's skim milk for the most part?

12 A. No, I'm sorry. If we're selling surplus milk,
13 it's whole milk. You know, it's the full butter fat, but
14 we don't have a lot of surplus, just cream going out.

15 Q. Okay. Okay. Now, are you involved in
16 determining the prices which you establish for either
17 direct customers or distributors, you personally?

18 A. Yes.

19 Q. Okay. What -- and how do you establish those
20 prices?

21 A. Well, we look at the market forces. We look at
22 the cost of our milk, cost of processing, at our overhead
23 costs, and we have to compete in the market, and so we take
24 all that into consideration when we decide on our pricing.

25 Q. When you talk about market forces, what do you

1 mean by that?

2 A. Well, we have to compete with Safeway and Wilcox
3 and Dairy Gold. So we have to look at that, has to be
4 consideration when we're doing our pricing.

5 Q. Okay. And those -- when you compete with them,
6 you're talking about looking at the prices which they
7 charge to the customers that you are mutually attempting to
8 serve, correct?

9 A. Yes.

10 Q. Okay. You have, I think, made the assertion, if
11 I heard it right -- at page ten of your testimony, you've
12 said that "the proposals would place you at a distinct
13 price disadvantage." And what do you mean by that?

14 A. Well, if we had to take over a million dollars a
15 year out of our bottom line into -- and pay it into the
16 pool -- we're already paying for our own milk and the
17 transportation and everything else. I believe our costs
18 would be more than a regular plant.

19 Q. Okay. Do you understand that the proposals, if
20 adopted, would cost you about a million dollars a year?

21 A. Yes. Or more

22 Q. Okay. What --

23 A. Or more.

24 Q. Or more. Okay. Now, what are the gross sales
25 annually of Smith Brothers?

1 A. That is proprietary information.

2 Q. You understand, do you not, that your competitors
3 that you've just identified, Wilcox Farms, for instance, is
4 already equalizing -- paying into the pool with the market
5 administrator in the same manner that Proposals 1 and 3
6 would require you to do?

7 A. Yes, but they don't have the costs of producing
8 the milk and getting it to their plant on top of that.

9 Q. Well, they have to purchase it from somewhere,
10 don't they?

11 A. They do, but if we're not selling milk or buying
12 milk, our costs would be more if we had to do both, I
13 believe.

14 Q. Okay. So you're not able -- do you mean by that,
15 that you are not able to produce milk in your own farms for
16 the prices which Wilcox, for instance, or Safeway or
17 Kroger, pays from their suppliers?

18 A. I believe that if we had to produce the milk, get
19 it to our plant, and still pay that amount, that we would
20 be at a disadvantage.

21 Q. In other words, it costs you more to produce your
22 own milk and deliver it to your plant than it does Wilcox,
23 Safeway or Kroger to buy milk from other producers and have
24 it delivered to their plant?

25 A. When you look at the balancing costs and the

1 other costs that we have to do that, I believe that we're
2 on the even playing field.

3 Q. Okay. Now, do you understand that if Proposals 1
4 and 3 were adopted, and you continue to have more than
5 three million pounds of class one sales, that with respect
6 to your surplus milk, non-class one utilizations, you would
7 draw the blend price out of the pool?

8 A. Yes.

9 Q. Okay. And when you say it would cost you a
10 million dollars, have you factored that draw into your
11 calculations?

12 A. Yes.

13 Q. Okay. What -- maybe I asked you this, but let me
14 ask it again. What class one utilization do you experience
15 on a regular basis, on a monthly, yearly?

16 A. It's a little higher than the order, but I don't
17 know -- I don't have the --

18 Q. More than 30 percent?

19 A. I don't have the figure of exactly what our class
20 one utilization is.

21 Q. Well, can you give us any idea?

22 A. No.

23 Q. You're not willing to?

24 A. I don't know the answer.

25 Q. And you don't know. But the million dollars,

1 let's be sure about this now, because this --

2 A. And that was an estimate. I mean, that was -- it
3 would be at least that much.

4 Q. Well, is that a reasoned estimate. I mean, oh,
5 at least a million. You're sure it would cost you a
6 million?

7 A. At our present level.

8 Q. Okay. And that's netting out the benefit you'd
9 get from any draw from the pool for your non-class one use?

10 A. Yes.

11 Q. Okay. And you're -- as president of the company,
12 it's your sworn testimony that that's what the net
13 financial impact would be on you, recognizing that there's
14 data here from which we could determine, based on
15 utilization, approximately, you know, volumes that you
16 would need to have and utilizations for that net financial
17 impact?

18 A. My controller gave me that information by his
19 figuring out our -- I didn't do it myself.

20 Q. Okay. Did your controller read the proposal, do
21 you know?

22 A. Yes.

23 Q. Okay. And has he ever had to -- have you ever --
24 have there ever been any months when Smith Brothers was
25 regulated because you went over the 150,000 pound purchase

1 from the pool or anything like that?

2 A. No, there was years ago where we may have been
3 pooled, but it's been before I was president, and so I
4 don't know the details. But not since that 150,000 pounds
5 was put in.

6 Q. Okay. So your controller, has he ever been
7 employed by a regulated handler and had to make those kind
8 of calculations, to your knowledge?

9 A. He hasn't been employed by another handler, but I
10 believe that he has the ability to know -- understand the
11 regulations.

12 Q. You're confident that the million dollars is a
13 minimum, firm, good number for the impact on your
14 operations?

15 A. I am.

16 Q. Okay. You make the comment on page 13 that
17 managing the timing of deliveries to your plant is critical
18 and we must incur additional cleaning costs and difficult
19 scheduling. You've got complete control over that, do you
20 not?

21 A. Not necessarily. Our tankers have to come over
22 the mountains and when it snows, they have to be able to
23 get over here, and get back and get the milk before the
24 tanks over there are full, or there's no place for it to
25 go. So we have control as long as the truck doesn't break

1 down or they close the pass, or those type of things. Or
2 something happens to the milk, --

3 Q. Okay.

4 A. -- have a bad load or something, and --

5 Q. Okay. So when you locate -- when you recently
6 bought a farm and located it at your present location, it's
7 on the other side of some mountains that are sometimes
8 difficult to transverse transportation wise, I take it?
9 Yes?

10 A. Yes.

11 Q. Okay. And that's what you're referring to. The
12 problem with getting across the mountains is the delivery
13 challenge you have that you're referring to?

14 A. Yes, that and a break down on one of our trucks.

15 MR. BESHORE: Okay. Thank you. I have no other
16 questions at this time.

17 EXAMINATION

18 BY MR. BERDE:

19 Q. Ms. Koester, my name is Sydney Berde. I
20 represent United Dairymen of Arizona.

21 Ms. Koester, are you one of the owners of the
22 Smith Brothers operation?

23 A. I am.

24 Q. And can you identify the other owners?

25 A. I have two sisters that are owners. I have three

1 children that are owners, my husband is an owner, two
2 brother-in-laws, and a niece, and five nephews.

3 Q. And they all constitute owners of the enterprise?

4 A. Yes.

5 Q. And I think you testified that none of them are
6 involved in the production end of the business that is on
7 the dairy farm?

8 A. That's correct.

9 Q. How far is the dairy farm from your plant?

10 A. 150 miles.

11 Q. When Smith Brothers operation started in 1920, it
12 certainly was not a three million a month operation, was
13 it?

14 A. No.

15 Q. And how long has your operation produced, let us
16 say, a million pounds a month?

17 A. I don't know that exactly because we had cows up
18 until a certain point, and the valley used to flood. So we
19 had to get rid of our cows for a while. And then when they
20 put a dam in, we got our cows back, so --

21 Q. Now, --

22 A. -- I would say since 1960.

23 Q. You think you achieved a million pounds per month
24 production in 1960?

25 A. I believe some time in the '60s.

1 Q. When Smith Brothers started in 1920, how did it
2 market its milk?

3 A. I believe that my grandfather was selling to
4 homes, was delivering to neighbors and started home
5 delivery routes.

6 Q. You mean as raw milk?

7 A. I don't know when the processing plant was built.
8 Long before --

9 Q. You have no idea --

10 A. No, it was long before my time. I just don't
11 know.

12 Q. No idea when the -- when you first decided to
13 process the raw milk and market it as packaged milk?

14 A. I don't. It was always packaged, but it was
15 probably raw at the beginning. I don't know when they put
16 the processing plant --

17 Q. Did he -- did your grandfather or his descendants
18 ever deliver raw milk to another processing plant?

19 A. I don't know.

20 Q. Do you think that the processing end of the
21 operation started within the last 30 years?

22 A. Oh, no, it -- I know that it was there in the --
23 because of old pictures, I know it was there in the '40s,
24 probably in the '40s --

25 Q. In the '40s?

1 A. So I guess the processing plant probably started
2 in the '30s.

3 Q. And did it start as a home delivery operation?

4 A. Yes.

5 Q. And at that time, who were the family members
6 involved in the business?

7 A. When it first started, it was my grandfather and
8 his brother.

9 Q. And his brother?

10 A. Yes.

11 Q. And by 1940, who were the family members in the
12 operation?

13 A. My grandfather and my dad and my uncle.

14 Q. And how about in 1960?

15 A. The same.

16 Q. Same. And when did they all leave the farming
17 end of the operation?

18 A. Probably when my grandfather died. He had the
19 most -- that was his -- he had more knowledge in that than
20 his two sons did.

21 Q. And so they left the operation of the farm and
22 concentrated on bottling milk; is that it?

23 A. Well, my father was alive, he oversaw it
24 somewhat, but he didn't actually work out there. He was
25 more involved in the processing and in the marketing.

1 Q. By the way, who owns the processing plant?

2 A. The same family members that I just told you.

3 They -- we all own the whole operation.

4 Q. And you also own -- the dairy farms is in the
5 same ownership as the processing plant?

6 A. Yes.

7 Q. It's not a separate tax payer?'

8 A. No.

9 Q. You just file one tax return?

10 A. That's correct.

11 Q. You indicated that about four or five of your
12 family members now are involved in the processing end of
13 the business?

14 A. Well, not necessarily the processing. The
15 administration and the distribution.

16 Q. But all involved in the -- what might be called
17 the marketing of processed dairy products part of the
18 business?

19 A. Yes.

20 Q. Okay. And none of them involved in the operation
21 of the dairy farm?

22 A. Not as far as running it.

23 Q. Who do you rely on to run the dairy farm?

24 A. We have a manager over there, a farm manager, and

25 --

1 Q. Not -- has no ownership in it?

2 A. He does not. And our controller who oversees him
3 and reports to me.

4 Q. And you indicated you had an estimated or
5 approximate time when you reached a million. When did you
6 reach two million?

7 A. I don't know.

8 Q. 1970?

9 A. I really don't know.

10 Q. What's the -- during the past -- during 2002,
11 what was your total, or what was your average, monthly
12 production?

13 A. By gallons of milk, are you talking about?

14 Q. By pounds, --

15 A. By pounds --

16 Q. -- hundredweight. Pounds -- let's say pounds per
17 month.

18 A. I'd say that's confidential. Confidential.

19 Q. But you've indicated it's over three and a half
20 million.

21 A. Yes.

22 Q. And is three and a half million constitute the
23 amount of milk that you process and market as processed
24 milk, or is that your production? You -- let's withdraw
25 that question.

1 You certainly produce more milk than the three
2 and a half million that you distribute as processed
3 product, don't you?

4 A. I don't think I said we distributed three and a
5 half million, that that was our total --

6 Q. Well, you --

7 A. I might have said we did at least that or more.

8 Q. Well, you indicated that if the regulatory
9 proposals that are in the proposal stage were adopted,
10 you'd be regulated.

11 A. Yes, so we're over three million.

12 Q. So you're over three million?

13 A. Yes.

14 Q. So that means you produce a substantial amount in
15 excess of three million?

16 A. Yes.

17 Q. And would you estimate that that -- and -- that
18 that monthly production averages about four/four and a half
19 million?

20 A. More than that.

21 Q. More than that?

22 A. Yes.

23 Q. Okay. Now, you stated that you do some school
24 bid business, don't you?

25 A. Yes.

1 Q. And in some cases, it's a flat price?

2 A. Some are flat, and some are escalating.

3 Q. Some are flat, some escalated. Who do you bid
4 against?

5 A. We bid against distributors for other dairies.

6 Q. And those other distributors are associated with
7 regulated handlers?

8 A. Not always.

9 Q. Some of them?

10 A. Some of them.

11 Q. Do you know what regulated handlers supply the
12 milk that the distributors bid for school business?

13 A. When the distributors go in there, do I know who
14 they're getting their milk from?

15 Q. Yes.

16 A. I can guess, but I don't know that for sure.

17 Q. But you know that they deal with regulated
18 handlers?

19 A. Yes, unless they're dealing with another
20 producer/handler.

21 Q. Unless they're dealing with another --

22 A. Producer/handler. There could be some of those.

23 Q. If it's not a producer/handler, then it's got to
24 be a regulated handler; --

25 A. Correct.

1 Q. -- is that correct?

2 A. Yes.

3 Q. And you know that the price -- class one -- this
4 is a class one product, isn't it?

5 A. Yes.

6 Q. And you know the class one price varies from
7 month to month?

8 A. Yes.

9 Q. And that would make it extremely difficult, if
10 not, virtually impossible, for a distributor who deals with
11 a regulated handler to bid a flat price?

12 A. Well, historically the schools used to always ask
13 for flat prices. They didn't -- it's only been in the last
14 few years that I'm aware of that they would accept anything
15 else because they didn't understand it. And they -- and
16 the -- they were doing it then.

17 Q. Yeah. And the reason they changed is because the
18 flat price they realized that was bid and accepted was so
19 far higher than necessary in order to cover the possibility
20 of a variation, that they decided it made more sense to bid
21 on a escalator base; isn't that correct?

22 A. I don't know what made them change their --

23 Q. But in any case, they did change to escalation,
24 did they not?

25 A. Some.

1 Q. Yeah. Now, your -- you would agree, would you
2 not, that a bidder whose milk emanates from a regulated
3 source could not bid on a flat price basis?

4 A. No, I don't agree on that.

5 Q. You don't agree with that? At least if he did
6 bid, he'd have to submit a bid that was high enough to
7 cover any risk that the class one price might increase
8 during the term of the contract?

9 A. Yes.

10 Q. Okay. But you don't have that problem, do you,
11 because you could set your own price and let it be fixed
12 for a period of time?

13 A. We could, but our costs could go up to be more
14 than that.

15 Q. Your costs? Which costs do you mean?

16 A. Our labor costs, our distribution, our
17 processing, our feed costs.

18 Q. But your raw milk costs would not increase?

19 A. Well, our feed costs increase. Our raw milk
20 costs increase.

21 Q. Okay. But --

22 A. We don't know ahead of time what our feed costs
23 are going to be necessarily.

24 Q. But you would not be faced with the same
25 variation of class one price that the regulated handlers

1 would be?

2 A. We would be faced with different ones.

3 Q. Different. And have you been successful in
4 getting the school bids through your distributors?

5 A. We do our school bids through -- we don't do it
6 through the distributors. Oh, you mean, do we get them
7 against the distributors that we were up against?

8 Q. Yes.

9 A. Some cases they get them, and some cases we get
10 them.

11 Q. When you bid directly as a handler for school
12 bid, do you invariably bid against other distributors, or
13 some of the bidders directly regulated handlers?

14 A. In the last few years, I would say most of it's
15 distributors, although we did bid against Vitamilk, and
16 they took a school district away from us.

17 Q. Uh-huh.

18 A. So it goes both ways.

19 Q. Do you market any of your product through
20 supermarket chains?

21 A. No, we do not.

22 Q. Do you deliberately avoid that channel of
23 distribution?

24 A. Yes.

25 Q. And why do you do that?

1 A. Because we feel that our niche market is the home
2 delivery, and that we don't have the same efficiencies that
3 the larger 7A plants do, and that we couldn't compete in
4 that market. And we try not to put all of our milk into
5 one source. We like to have it in different sources out so
6 if we lose a customer, we don't have all this excess milk.

7 Q. You do institutional business?

8 A. We do some.

9 Q. What kind of institutions do you sell to?

10 A. We -- federal detention center, hospitals.

11 That's all I can think of right now.

12 Q. Do you bid against -- is that a bid business?

13 A. The federal detention center is.

14 Q. And do you bid against regulated handlers for
15 that business?

16 A. We bid against regulated handlers and
17 distributors.

18 Q. And you're successful in obtaining that business?

19 A. Sometimes we are, and sometimes we're not. We
20 lost it this year.

21 Q. Yeah. You indicated that 70 percent of your
22 total distribution is home delivery?

23 A. Yes.

24 Q. And can you give me a description of the
25 remaining 30 percent?

1 A. We have school districts, and we do coffee shops
2 and restaurants, and made a few convenience stores, just
3 small ones that just wanted to have milk in there. A few
4 gas stations, that type of thing. And then we sell some to
5 some other distributors that sell to wholesale accounts.

6 Q. And who are your competitors for that business?

7 A. Wilcox, WestFarm, Faith Dairy (phon.), Edaleen
8 Dairy (phon.). That's all I can think of right now.

9 Q. Now, going back to the family involvement in the
10 business for a minute. You said there were four -- five --

11 A. No, there are five of us that are employees.

12 Q. Okay. Okay. Five. And what do they do in the
13 operation?

14 A. One is a distribution manager. Two are office
15 workers, and one manages our properties and different other
16 aspects of the business, like if we have rentals and things
17 like that.

18 Q. Is the ownership equally distributed?

19 A. The ones that have the voting stock have a little
20 more ownership than the ones that don't. So it's equal
21 amount the non-voting, and so the ones that have the
22 voting, the five of us that have the voting have a little
23 bit more than the others.

24 Q. And when was that structure established?

25 A. When my father passed away in 1996.

1 Q. I take it that the business has been profitable.

2 A. Yes.

3 Q. You talked about a million dollar bottom line
4 that might be shifted or lost or transferred to the order
5 if you were regulated?

6 A. Yes.

7 Q. And if that happened, you'd still be viable,
8 would you not?

9 A. No, not necessarily.

10 Q. Be a disadvantage, is that what you said? I
11 think you characterized it as a disadvantage.

12 A. If we had to produce our own milk and have all
13 the costs of that, plus pay into the pool, yes, it would be
14 a disadvantage.

15 MR. BERDE: Thank you.

16 MR. UNIDENTIFIED: Your Honor, it's 12:15. How
17 much longer do we expect to go?

18 THE COURT: A lot of that depends on you. I'm
19 happy to break for lunch now if that's --

20 MR. UNIDENTIFIED: I'm not asking to,
21 necessarily. I just wanted (indiscernible)

22 THE COURT: It's as good a time as any. I just
23 lose track of the time. Let's just take an hour today.
24 Okay? Is that okay? Come back at 1:15?

25 Okay. We're off the record.

1 (Off the record at 12:15 p.m. and reconvened at 1:15 p.m.)

2 THE COURT: Okay. We're back on the record, and
3 who would like to question Ms. Koester next? Is that you
4 -- is -- Mr. Marshall was nodding in the affirmative.

5 MR. MARSHALL: Thank you, Your Honor.

6 EXAMINATION

7 BY MR. MARSHALL:

8 Q. Good afternoon, Ms. Koester.

9 Part of your testimony --

10 THE COURT: I just need you to -- even though I
11 said "Mr. Marshall," easier if you'd identified yourself.

12 BY MR. MARSHALL:

13 Q. Thank you. Doug Marshall, Northwest Dairy
14 Association.

15 You had some -- portion of your testimony
16 addressed to your status, the status of your entity as a
17 small business. First of all, your testimony identifies
18 that entity as Smith Brothers Farms. Is that the full,
19 legal name of the entity?

20 A. It's Smith Brothers Farms, Incorporated.

21 Q. Okay. And I have read that Smith Brothers, and
22 this maybe go back to when your father was alive, had a
23 tractor implement business. Is that still the case?

24 A. No.

25 Q. Does Smith Brothers Farms, Inc. own or operate

1 any other businesses besides the dairy business described
2 in your testimony?

3 A. We have a business that we have that's just a
4 subsidiary of it that we call Smith Real Estate
5 Development, and we own a couple of buildings in it, and
6 that's all. It's just -- it's part of Smith Brothers
7 Farms, but --

8 Q. When you described your entity as a small
9 business, did you mean to represent Smith Brothers Farms,
10 Inc. as coming within the statutory concept of a small
11 business of which the secretary is in the hearing notices
12 indicated has desired to take note?

13 A. Yes.

14 Q. And you did that analysis, did you include any
15 aspects of that subsidiary?

16 A. Yes.

17 Q. In, I think, earlier questioning, you identified
18 that really none of the other owners besides yourself is
19 involved, at least day-to-day, in the management of the
20 business. Did I understand that correctly?

21 A. No, there are four others that are employees that
22 are owners.

23 Q. Oh, they are employees --

24 A. Yes.

25 Q. -- that are involved --

1 A. Yes.

2 Q. I'm sorry. I did misunderstand.

3 A. And then there's one distributor that is an
4 owner, too.

5 Q. Now, is that distributorship part of Smith
6 Brothers Farms, Inc.?

7 A. He's one of the independent distributors of home
8 delivery.

9 Q. So he's independent of Smith Brothers Farms,
10 Inc.?

11 A. Yes, he buys his milk from us.

12 Q. You testified in opposition to Proposal No. 2, I
13 believe. That's the proposal regarding similar labels. I
14 understand that you oppose that proposal -- understand
15 correctly that you propose -- oppose that proposal?

16 A. Yes.

17 Q. I don't see in your testimony why you're opposed
18 to it. Can you tell us why?

19 A. And where -- what page was that on, do you know?

20 Q. Towards the beginning. Let's see if I can help
21 find it. Yes, the very first paragraph, bottom sentence.
22 Am I right, the Proposal 2 is --

23 MS. UNIDENTIFIED: Yes.

24 THE WITNESS: At the time, I knew I was against
25 it. I can't.

1 BY MR. MARSHALL:

2 Q. Ms. Koester, your attorney has kindly given me a
3 copy of the hearing notice, and I will show it to you, if I
4 may.

5 A. Okay.

6 (Pause)

7 THE WITNESS: Okay. It says that we couldn't --
8 a producer/handler couldn't supply a wholesale customer who
9 is already buying milk from a fully regulated plant,
10 correct?

11 BY MR. MARSHALL:

12 Q. My understanding of the proposal is that it mean
13 that you couldn't sell a product to such a customer in a
14 label similar to labels supplied to them by other sources.

15 A. Right.

16 Q. Is that your understanding?

17 A. Yes, that's what I thought. Well, we do have a
18 couple of distributors that buy milk from WestFarm and
19 Wilcox and Safeway, and they might buy some from us and
20 some from one of those. So that would make their ability,
21 not be able to buy it from us.

22 Q. If it were the case that all that would do would
23 mean that they -- that you could not package milk in the
24 WestFarm foods labels or in the labels of somebody else,
25 from, like Wilcox, but -- that if it would mean that you

1 could continue to sell to them under your own label, would
2 you still oppose Proposal No. 2?

3 A. So what you're saying is if they were buying some
4 product that they had their own label in, they were buying
5 some from another farm and some from us under that label,
6 would I still oppose it?

7 Q. No, I think I got it -- I think we got it
8 backwards. So let's -- glad you asked. Let's get it
9 straight.

10 I want you to assume that Proposal No. 2 would
11 apply to a situation where any customer is buying product
12 from you under a certain label and other products from
13 somebody else under the same or a similar label. For
14 example, suppose both you and we were supplying Safeway and
15 licensed to use the Lucern (phon.) label.

16 Q. Well, I feel that wouldn't truly be fair to the
17 distributors either if maybe they, for whatever reason,
18 they wanted to buy some from us and some from somebody
19 else, that -- and like I said, we don't sell to grocery
20 stores, so -- at this time, but what if a grocery store
21 want -- of course, what if a grocery store wanted to have
22 some milk that was from WestFarm and some from Smith
23 Brothers, and their own label, for whatever reason. I
24 don't see why that would -- why the secretary would want to
25 regulate that. Doesn't make sense to me. So to me it

1 seems like it shouldn't limit the customer --

2 Q. Other --

3 A. -- from who they could buy from.

4 Q. Are you finished now?

5 A. Yes, I am.

6 Q. Sorry. I apologize.

7 Other than the fact that you don't think it makes
8 sense, do you see any way in which Proposal No. 2 would
9 negatively impact Smith Brothers?

10 A. At the present time, I can't think of how it
11 would negatively impact, but I -- it would limit what we
12 could do in the future if something came up where we could
13 do that.

14 Q. Would it limit you from co-packing a product
15 under somebody else's label that somebody else might ask
16 you to do in order to maintain a designation or a claim of
17 their milk as being not produced with the aid of artificial
18 hormones or some similar kind of claim?

19 A. I don't know because that label wouldn't be
20 similar than if they were putting it up under a label that
21 didn't have that. Wouldn't that make it the label not
22 similar?

23 Q. You know, that's a very good question. I don't
24 know the answer to that. I was assuming you might have,
25 for example, the same package that we have as one of our

1 labels with a little, small insignia saying something to
2 that effect. I would think that would be a similar label.

3 Is that a concern to you? Would that kind of
4 restriction be a concern to you?

5 A. It could be because it would restrict how we
6 could do business if an opportunity came up.

7 Q. Do you believe you're doing anything like that
8 today?

9 A. I don't know if -- we're not putting anything up
10 in the same package that somebody else is doing for a
11 customer, that I know of.

12 Q. Okay. Fair enough.

13 Let's turn to your marketing strategies, which I
14 think you described, and my -- I would agree with you as a
15 niche strategy. Would you agree that the Puget Sound
16 market is a highly competitive market?

17 A. Yes.

18 Q. For fluid milk products, --

19 A. Yes.

20 Q. -- I should clarify.

21 And you mentioned that one of your niches is what
22 you described as BST free. Let's describe that. Is BST a
23 hormone that occurs naturally in cows and cows' milk?

24 A. Yes.

25 Q. How can you represent that your milk is BST free?

1 A. What we represent is that we do not give any
2 added BST to our cows, and that's what our label says.

3 Q. Okay. And you're referring, I think, to a
4 product sometimes known by the trade name of "Pozolac"
5 (phon.)?

6 A. Yes.

7 Q. Do you recall the testimony of Paul Arbuthnot in
8 the Phoenix phase of this hearing?

9 A. Yes.

10 Q. And you're familiar with Sunshine Dairy, of which
11 --

12 A. Yes.

13 Q. -- he used to be the manager?

14 A. Yes.

15 Q. Are you aware that some of their products are
16 distributed with a label on the carton, something to the
17 similar effect that -- of your claim, that they are not
18 produced with artificial hormones?

19 A. I'm not familiar with Sunshine Dairy enough to
20 know what their label says.

21 Q. Are you aware that Sunshine does private label
22 packaging for Trader Joe's with a similar characterization
23 of its being produced without the aid of Pozolac?

24 A. No, I didn't know who put up Trader Joe's milk.

25 Q. Are you aware that Vitamilk was making such a

1 claim?

2 A. Yes.

3 Q. Would you agree that it's not necessary to be a
4 producer/handler in order to use that market niche?

5 A. I believe that it -- to a lot of consumers it is
6 important for them to know that you control the milk from
7 the cow to their home. And we have a lot of customers that
8 that's a very important thing to them.

9 Q. Okay. Great. Well, that's a good answer. So
10 let's talk a bit about that.

11 Would you agree with me that Vitamilk, though,
12 was marketing milk is not produced with the aid of
13 Pozolact, however their claim was stated, but was not
14 making the claim that you can legitimately make about
15 control of the milk supply from farm to the customer?
16 Vitamilk was making part of the claim, no BST artificially
17 added.

18 A. Uh-huh.

19 Q. No hormones added. I think they were
20 mischaracterizing it as. They were making that part of a
21 claim, but you can make the larger claim that not only are
22 you not doing that, but you have control of the milk supply
23 from farm to the shelf?

24 A. Yes.

25 Q. All right. So in the case of Vitamilk, they also

1 had a designation of free farmed certification, I think it
2 was testified to in the Phoenix phase of the hearing. Have
3 you -- you recall that from that hearing --

4 A. Yes.

5 Q. -- testimony?

6 It's possible for regulated handlers such as
7 vitamilk then to establish a similar market niche to yours,
8 is it not, other than, I agree, the control of milk from
9 farm to -- through the plant?

10 A. Yes, they did that.

11 Q. So let's focus for a moment on the unique claim
12 that you can make, and the others cannot, about control of
13 the milk from farm to the customer. What additional costs
14 does that impose upon Smith Brothers as an operation?

15 A. Well, the fact that we don't give them that
16 hormone, our milk production is probably lower because of
17 that, so --

18 Q. Additional costs in terms of cost of production
19 --

20 A. Yes.

21 Q. -- on the farm?

22 A. Uh-huh. When you don't get as much milk, your
23 costs are going to be higher per pound of milk. And so if
24 we're not -- don't use that, then our cost would be higher.

25 Q. Right. But if I were a regulated handler like

1 Vitamilk and also chose -- or like Sunshine, and I can
2 represent to you that Sunshine is making those claims as
3 well. If I were a regulated handler such as those two who
4 wanted to use the rBST-type claim or the Pozolact claim,
5 they could do that, and we've established that. And they
6 may involve higher costs for them or their milk supply as
7 well, right?

8 A. I don't know.

9 Q. Involves the higher cost of production on your
10 farm not to use it, right?

11 A. Right, but whether or not they pay that farmer
12 more for their milk, I don't have that information.

13 Q. Well, it would be fair to conclude, would it not,
14 that either they did or the farms who agreed not to use
15 BST, absorbed that cost advantage that Pozolac
16 hypothetically can offer?

17 A. Yes.

18 Q. And it's not necessary to be a producer/handler
19 in order to do that, so I guess I'd like to focus just for
20 a moment on the unique advantage that you have in marketing
21 by being able to claim -- claim is a legal term. I'm
22 sorry. To be able to advertise that you have control from
23 farm to the plant, which others cannot say. That's a
24 market niche by itself, is it not?

25 A. Yes.

1 Q. Are there costs associated with that control
2 issue that you wouldn't have if you were, for example,
3 willing to buy milk from other sources?

4 A. Well, if we never buy the 150,000 pounds per
5 month because of that, where sometimes that would be an
6 advantage to us to be able to do that. We don't have
7 enough milk.

8 Q. So you elected not to utilize the 150,000 pound
9 opportunity because you want to make the assurance to your
10 customers that you control all of the raw milk --

11 A. True.

12 Q. -- going into your plant?

13 A. Yes.

14 Q. So that's a marketing strategy then that isn't
15 required by the terms of producer/handler qualification,
16 correct?

17 A. I'm sorry.

18 Q. You could buy outside milk with -- as a
19 producer/handler --

20 A. Well, only a small portion --

21 Q. -- if you couldn't -- yes. I'm sorry.

22 A. Small portion.

23 Q. Let me finish the question, and then you can give
24 the same answer probably.

25 It's not necessary to -- a producer/handler who

1 doesn't wish to make a claim in advertising that they
2 control all the milk can buy from outside, right?

3 A. Yes.

4 Q. And the fact that you use -- choose to do so is a
5 penalty that you choose to elect in hopes that that'll pay
6 off in your marketing strategy, correct?

7 A. Yes.

8 Q. Are there any costs beyond any that you've
9 identified so far? Are there any costs associated with
10 I'll call "sole sourcing" or "exclusive use of your own
11 farm production?"

12 A. The balancing costs.

13 Q. Okay. We'll get to that at some -- let's talk to
14 Alaska.

15 A. You testified about sales to Matanooska Maid,
16 which is -- I believe earlier testimony's indicated a dairy
17 in Anchorage, correct?

18 A. Yes.

19 Q. And this is essentially raw milk sale rather than
20 a packaged milk sale, correct?

21 A. Yes, it's just pasteurized -- heat-treated.

22 Q. And as you describe on page one of your
23 testimony, that is a -- one of the ways you balance your
24 fluctuating milk supplies, right?

25 A. Yes.

1 Q. I believe on page 13 of your testimony, you
2 described it as a novel approach to balancing. How is it
3 novel?

4 A. Well, I think it's an opportunity that Matanooska
5 Maid has probably sought out to find producer/handlers that
6 they could buy from, and I'm not really sure exactly what I
7 meant by novel on that. It was -- it just was a different
8 way to get -- to sell to somebody to our surplus that
9 really wanted our product.

10 Q. Do you have an understanding from Matanooska Maid
11 as to why they might have sought out producer/handlers to
12 provide milk that they need for bottling in their plant in
13 Anchorage?

14 A. No, I do not.

15 Q. If you were a regulated handler, would you have
16 to account to the pool based on their ultimate uses at the
17 full federal order class prices?

18 A. I don't know.

19 Q. I can represent to you that you would.

20 A. Okay.

21 Q. And I'll ask you to assume that a regulated
22 handler such as our plant or our cooperative would have to
23 account to the pool based on the class of use as determined
24 by the market administrator at the plant in Anchorage,
25 which would mean then that we as a supplier have had to

1 charge Matanooska Maid enough to cover our full federal
2 order class prices, or represent that to you and ask you to
3 assume it.

4 Is there any reason why in what you do, you are
5 different -- in selling to Matanooska Maid, is there any
6 reason why what you're doing there is different than what
7 we do that would justify your not having to charge them
8 full class of use based for bulk milk sales based on class
9 of use?

10 A. Well, the only reason I can think of is we're
11 closer to the Tacoma docks where they pick it up. So the
12 transportation costs would be less.

13 Q. Yes, I can agree with you that there may be a
14 slightly different cost of getting the product to Tacoma,
15 but I'd like to focus for a minute on the distinction that
16 I asked you to assume a minute ago, which is that today if
17 Matanooska Maid buys from a company or a cooperative like
18 ours, their milk would be accounted to the pool at the full
19 class price, which means that we, in turn, have to charge
20 them a price to cover that full class price, --

21 A. Yes.

22 Q. -- whereas you would not.

23 A. Yes.

24 Q. And I'm asking if there's any reason, any theory,
25 any rationale that you can provide to the secretary why

1 when you sell bulk milk to a bottling plant in Anchorage,
2 you would not have to account to the pool, and we would.

3 A. Is it because they are not under the federal
4 order up there?

5 Q. Well, that is why it happens in a way, but I'm
6 not asking a quiz here of you. I am asking you to focus on
7 the policy question of whether Smith Brothers Farms feels
8 it is justifiable in the policy set by the Secretary of
9 Agriculture to require a company like ours to account to
10 the pool with a full class prices on a sale to a plant that
11 is, yes, outside the federal order marketing area, but not
12 require Smith Brothers Farms to do the same. Is there any
13 policy reasons you could offer the secretary for continuing
14 that difference in treatment on those bulk milk sales?

15 A. Not that I can think of at the moment.

16 Q. Well, you're welcome to add to that later, either
17 here or in brief, I'm sure, --

18 A. Okay.

19 Q. -- with the help of your attorney, you can up
20 with a good one.

21 When you make those sales, do you consider that
22 to be a profitable sale?

23 A. In -- we don't actually say how -- what -- you
24 know, what part of our -- he'll look at the whole thing all
25 together where we have to sell some at different prices in

1 order to -- it's the whole bottom line that we look at. We
2 have to sell our milk to somebody, and if we have surplus,
3 we sell it to them. We can't supply them all the time. So
4 we don't look at it as an individual thing. Sometimes it
5 could be profitable; sometimes it might not be as
6 profitable, but is better than the alternatives.

7 Q. Are there costs to your processing enterprise
8 then associated with serving that customer that you cannot
9 recover from that customer?

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

11 Q. Is there a cost to you in using Matanooska Maid
12 to balance your milk supply?

13 A. Yes.

14 Q. What would that be?

15 A. Well, depending on what the price of milk is at
16 the time, how much our --

17 Q. A minute ago, I --

18 A. Sorry. And how much our production was. So
19 depending on the price we received, and how much it cost us
20 to get it there, and that could be -- go either way.

21 Q. Right. Well, I'm not trying to confuse you here,
22 and this is something that I'm ready to talk about, and you
23 are hearing these questions for the first time. So let's
24 make sure you understand what I'm asking you because it's
25 important.

1 A minute ago I think you said you did not
2 consider yourself to be losing money on those sales to
3 Matanooska Maid, right?

4 A. We don't look at it as a separate sale,
5 individually. It's part of the cost of our doing business;
6 it's in the balancing.

7 Q. Is the sale to Matanooska Maid sufficient to
8 cover the costs of your farm production plus the cost of
9 handling it at your Kent facility plus the costs of
10 delivering it to wherever they take ownership? Are you
11 able to recover all those costs from Matanooska Maid?

12 A. I don't know.

13 Q. So you don't know whether it's a loss, do you?

14 A. No. As an individual sale, I don't know if it is
15 a loss.

16 Q. So would it be fair to describe it then as a
17 balancing cost if it's not at a loss?

18 A. I don't know.

19 Q. Fair enough. And by the way, you mentioned
20 earlier you could not supply all their needs. What do they
21 do when you cannot supply all their needs?

22 A. I don't know who they buy for -- buy from at all
23 times.

24 Q. You indicated earlier, I think, that they do
25 solicit milk from producer/handlers. There are others than

1 yourself, right?

2 A. I believe they do.

3 Q. And at times do -- are you aware that they've --
4 will at times purchase milk from our organization, NDA or
5 WestFarm Foods?

6 A. Yes.

7 Q. All right. So when you cannot supply all their
8 needs, then they turn to us, correct?

9 A. I don't know if you're the only other option or
10 not, but I know they do buy from WestFarm, but I don't know
11 who else they buy from.

12 Q. Would it be fair to say that when they can --
13 when Smith Brothers Farms cannot supply all their meets --
14 needs, they turn either to other producer/handlers or to
15 regulated handlers to supply their needs?

16 A. Yes.

17 Q. In that respect then, are they not using the pool
18 to balance their needs?

19 A. I can't speak for them.

20 Q. Logically, though, is it not true that if you're
21 using them to balance your milk supply, and they buy from
22 others when you cannot supply them, that in effect your
23 milk supply is being balanced by those of us that supply
24 them when you cannot?

25 A. I don't know if we're their first choice, or if

1 they call us and just want it at certain times, because
2 there are times we have it to sell to them that they don't
3 want it. So I don't know who their first choice is.

4 Q. If you did not have it available and if other
5 producer/handlers did not have it available, would they not
6 be purchasing from regulated handlers who are taking their
7 needs from pool producers?

8 A. Yes.

9 Q. In that sense then, isn't Matanooska Maid using
10 the pool to balance its needs that are in excess of what
11 its own producers or you can supply?

12 A. On the surface that sounds true.

13 Q. I'm not trying to trick you here. If you don't
14 understand the question, please ask.

15 Well, then, just to kind of make sure I'm not
16 going be -- be mischaracterizing your testimony, let me
17 note that on page nine you describe yourself as entirely
18 self-sufficient. You have explained to me how you use them
19 to balance your needs and how they in turn pass that
20 balancing back to the pool. Do you still agree that you
21 are entirely self-sufficient, because I'm going -- tell you
22 that I'm going to argue in brief that you're not? So you
23 -- would you like to rebut my potential argument now?

24 A. We have surplus milk that we sell at certain
25 times of the year that, if you could characterize it as not

1 being self-sufficient, if that's what you would
2 characterize it, and then that is true, because we do have
3 surplus milk.

4 Q. Fair enough. You mentioned something about \$1.50
5 charge at times to balance. That would be sales to our
6 organization, would it not?

7 A. Yes.

8 Q. And that would be the \$1.50 that -- below class
9 price that we charge for your use of our plants, correct?

10 A. Yes.

11 Q. Can you -- would you agree with me that the
12 amount of your excess needs that you sell to our plants is
13 a fraction of your -- of the milk you don't bottle -- small
14 fraction, I should say?

15 A. It is a small fraction, except in the summertime
16 when we -- I don't have as many sales, we do a much bigger
17 proportion.

18 Q. Would you care to -- since one of the issues
19 raised by your counsel in this hearing, and then their
20 question relates to the costs of balancing, would you care
21 to estimate what proportion of your total milk supply is
22 sold to anybody who's charging you below class price for
23 the service of taking that milk or balancing it?

24 A. What percentage of our -- I wouldn't know that
25 without sitting down, figuring it out. So I couldn't guess

1 at it at this point.

2 Q. Well, maybe we can develop some of that here.
3 And regrettably, I feel an obligation not to use knowledge
4 that I have from our purchases from you, unless you release
5 me from testifying about that. So we're going to have to
6 go about this in a little more difficult way, but maybe we
7 can get to the same point without violating any
8 confidential information that you have.

9 Before we do that, though, let me ask you some
10 other questions. What other balancing costs do you have
11 because you're a producer/handler, other than what we've
12 just been discussing with your sales to Matanooska Maid?
13 And I think you mentioned also in your testimony some
14 things like being able to service only certain kinds of
15 customers. What other balancing costs might you have?

16 A. Well, there's been some businesses where
17 distributors have asked if we could supply them, and
18 because of the quantity we couldn't do it on an ongoing
19 basis, because at some point we may not have enough milk to
20 do it. So we have to try to balance our sales with our
21 production, and there is always a cost in that there always
22 are some lost sales or there -- you have the problem of
23 having too much milk, and then you've got to sell it at a
24 lower price. So it's hard to quantify exactly how much in
25 dollars that it, but all of that is definitely added to the

1 bottom line, or subtracted from the bottom line, I should
2 say.

3 Q. Okay. A moment ago you just said you -- said
4 your extra, then you would have to sell the lower price.
5 Can you quantify that in any way for the secretary so that
6 they could -- secretary and the department can understand
7 the impact of that on you?

8 A. No, I'm just talking about what we would sell it
9 for surplus, that that would be the lower price as to
10 WestFarm Foods, but I can't quantify how many dollars that
11 costs us to do that.

12 Q. Are there any other costs besides those that
13 might be a balancing cost that you incur because you are a
14 producer/handler that you would not incur if you didn't
15 have the restrictions that are part of the qualification of
16 a producer/handler in -- under the order? What other costs
17 of balancing do you have?

18 A. I guess sometimes if our milk doesn't get here
19 from our farm, we would have to stop production or stop
20 bottling the milk, and then have to clean up and keep our
21 people on overtime, and sometimes that can be a problem if
22 we're a little short of milk and waiting for the milk to
23 get from our farms. We have that extra costs where if were
24 probably a regulated plant, the milk would always come in
25 on a regular basis, and you wouldn't have to worry about

1 not having a much -- enough milk that day.

2 Or if something happened to a load, or we broke
3 down, or whatever, that -- we probably wouldn't have that
4 problem if we -- if the milk was coming in from somebody
5 else.

6 Q. I believe you mentioned something about the fact
7 that your farm is in Eastern Washington, for the benefit of
8 those reading this transcript. It's true, is it not, that
9 there's a mountain pass between your farm and those of us
10 that are here today in the Seattle area and, of course,
11 your plant at Kent's in the Seattle area, right?

12 A. Yes.

13 Q. So you mentioned snow in the winter, and
14 sometimes that impacts the ability of your loads to get
15 over the mountains, right?

16 A. Yes.

17 Q. Okay. And you also referred to transportation --
18 costs associated with transportation break-downs, loads not
19 arriving on time. How would that be different than a
20 regulated handler?

21 A. I don't know because I don't know that they have
22 ever had that problem getting it over there. So I don't
23 know.

24 Q. I can represent to you that sometimes the snow
25 stops our tankers as well. Probably have a bunch of

1 tankers up there on the pass with a union meeting, right?

2 A. Yeah.

3 Q. You testified that you would have a million
4 dollar a year change in your cost structure if you were to
5 be regulated under this or any other proposal, correct?

6 A. Yes, at least a million.

7 Q. The cost that you've identified to me, somewhat
8 generally, would those costs add up to a million dollars a
9 year?

10 A. Those costs wouldn't go away if we just still
11 used all of our own milk, and if we were paying into the
12 pool, we'd be paying into this milk and not getting
13 anything for it that I can see.

14 Q. I understand. You're choosing to be your own and
15 only source of milk, and some of the costs you've described
16 are because of that?

17 A. Yes.

18 Q. I agree with you and understand that point. I'm
19 asking, though, whether the costs that are associated with
20 your being a producer/handler, that you've also identified
21 separately, offset that million dollar a year difference in
22 cost that you've testified you would have?

23 A. I don't know the answer to that.

24 Q. Okay. Fair enough. Let's shift gears then.

25 (Clears his throat)

1 BY MR. MARSHALL:

2 Q. Excuse me.

3 To talk about your plant a little bit. I think
4 in your testimony under questioning from Mr. Beshore before
5 lunch, you indicated that a number of four to five million
6 pounds, and I wasn't clear. Was that route dispositions or
7 in class one sales, or was that all milk?

8 A. That was all milk going through the plant.

9 Q. Through the plant.

10 A. Bottled in one way or another.

11 Q. Including the milk -- but -- and so it would not
12 include then any milk that was sent to Matanooska Maid?

13 A. No.

14 Q. That milk does go through the plant, though, does
15 it not?

16 A. Yes, but this would be packaged.

17 Q. You said, I think, to him also that plant
18 capacity today is about six million pounds?

19 A. And I'm guessing on that.

20 Q. Okay. Fair enough. You also mentioned an old
21 gallon filler. What would your capacity be if you were to
22 simply take that old gallon filler out and -- move the
23 inefficient (phon.) one out and lease a modern gallon
24 filler? Are there any idea what your plant capacity would
25 be if you made that change?

1 A. No, I don't. I know that we would have to do
2 more than just buy the machine because right now when we
3 run our gallon filler, we can't run any other machine. So
4 there would be a lot more updating to the plant we would
5 have to do than just buy -- than leasing a machine. Would
6 entail a lot more.

7 Q. Or you would have to run the plant longer hours?

8 A. Yes, and there -- yes.

9 Q. On page nine you described your plant operation
10 as smaller than most regulated plants in Order 124. Did I
11 get that correctly?

12 A. Yes.

13 Q. And I believe you were here when Mr. Van Dam
14 testified and listed plants in his estimates of plant
15 volumes. Do you have any disagreement with his list of
16 plants and plant volumes?

17 A. They weren't what I expected. I know that ours
18 wasn't correct, so I presume that some of the other ones
19 possibly could not be correct, too, and I've always felt
20 that we were smaller than the other dairies in our area,
21 other than the other producer/handlers. I'm thinking of
22 Safeway, WestFarm and Wilcox. And I guess that's what I
23 look at in our area, is the --

24 Q. All right. How about, for example, Valley of the
25 Rogue Dairy down in Southern Oregon?

1 A. I don't know anything about them.

2 Q. Eberhard Dairy in Bend, Oregon?

3 A. I'm not familiar with any of dairies in Oregon.

4 Q. That would include then WestFarm Foods in Medford

5 or --

6 A. That's true.

7 Q. -- or Sunshine?

8 A. That's true. I do not know.

9 Q. Your seven million pound figure, I think, was the
10 -- correction. In Mr. Van Dam's list, I believe, had Smith
11 at seven million. Would that approximate your on-farm
12 production?

13 A. No.

14 Q. You produce less than seven million on your farm?

15 A. Yes.

16 Q. On page six of your testimony, you indicated at
17 one point there that if you were to become regulated, "it
18 would change the way we operate our business." Did you
19 describe the changes that you would make in the way you
20 operate your business?

21 A. I don't know what we would do. We would
22 definitely have to change it because we couldn't do
23 business like we are now. So that would have to be
24 decided. We would either not bottle milk or not milk our
25 own cows or -- it would just have to be completely changed,

1 but I don't know which way we would go.

2 Q. Well, let's talk about milking your own cows. Do
3 you believe that your cost of milk production would be
4 higher than -- today than it would be if you were buying
5 milk from what I'll call pooled sources?

6 A. That changes from month to month. I believe that
7 sometimes our costs are higher, and sometimes our costs are
8 lower at the farm level.

9 Q. Well, let's look at that. I believe you
10 testified, excuse me, that at times your cost exceeds the
11 class one price; is that right?

12 A. Yes.

13 Q. And I represent to you that the lowest class one
14 price this year is \$11.54. With that, would your cost of
15 production have exceeded that \$11.54 price last April?

16 A. Yes.

17 Q. Were you here when Dr. Terry Smith testified?

18 A. Yes.

19 Q. On page four of his testimony, he had a graph,
20 and I'm going to ask if you have a comment on it. I'd be
21 glad to show it to you, showing the average cost of dairy
22 operations, average production costs per hundredweight for
23 dairy operations with 500 cows or more being \$10.46, and 89
24 percent of them producing at \$12.50 per hundredweight or
25 less. May I show this to you?

1 A. I do remember that. It doesn't fit our operation
2 at all.

3 Q. You have a 3,200 cow operation, right?

4 A. Yes, --

5 Q. And so you're --

6 A. -- and we've never been able to produce milk at
7 the prices he's got on there.

8 Q. Okay. Fair enough. In your testimony, you
9 speculated about motivations pertaining to Boardman Farms
10 -- excuse me, to the farm or farms located at Boardman,
11 Oregon, and I think it might be useful just to explain for
12 the record what you're referring to there. Is it true that
13 there are two -- I guess, three farms who ship to a cheese
14 plant at Boardman, Oregon that are located near Boardman,
15 Oregon?

16 A. Yes.

17 Q. And that's what you're referring to as concern --

18 A. Yes.

19 Q. -- that one of those farms, or more than one
20 might become a producer/handler?

21 A. Yes.

22 Q. Do you know if Smith Brothers are represented,
23 has Smith Brothers ever discussed with any of those three -
24 -

25 A. I have not. I'm not aware of anybody else that

1 has.

2 Q. Have you looked at how they operate their farm?

3 A. I have not.

4 Q. With respect to your farm, you testified that the
5 -- you did not build a new farm as a result of herd
6 expansion, and you testified that you've not expanded your
7 herd beyond what it was before you had that farm, but do
8 you have any plans to expand the herd in the future?

9 A. Not at this time.

10 Q. Do I recall -- do I understand correctly that you
11 purchased that farm from an organization that had used it
12 as a feed lot operation for beef?

13 A. No, we produce it -- we purchased it from a
14 farmer over there where we put our new dairy. We have a
15 feed lot next door that we've owned since the '80s --

16 Q. Oh, the feed lot is next door?

17 A. Yes, we've owned it since the '80s.

18 Q. I see. Okay. Well, what is your -- thank you
19 for that clarification.

20 What is your -- with respect to your dairy farm
21 operation, you have a permit, do you not, from the state of
22 Washington to operate that farm?

23 A. Yes.

24 Q. What number of cows are you -- what is the
25 maximum number of cows you're currently permitted for?

1 A. I don't know. I presume it's probably 32/3,400
2 about what we have, but I don't know that to be the fact on
3 the permit.

4 Q. So is your testimony that you presume that you
5 are not able to grow beyond your current amounts -- under
6 current permits, I should say?

7 A. No.

8 Q. Could you clarify that so I understand what you
9 --

10 A. I just -- we haven't had any plans to grow our
11 herd. I'm not saying that we're not permitted to grow it
12 any more than that. I don't know what that would entail if
13 we wanted to have more cows over there, but we don't have
14 any plans to add cows at this time.

15 Q. Who's Earl Davenport?

16 A. Our controller.

17 Q. Is he based in -- at the farm, or is he based at
18 Kent?

19 A. He's based in Kent.

20 Q. Would he be the person who identified to you that
21 the potential cost of regulation would be a million dollars
22 a year?

23 A. Yes.

24 Q. Do you recall an article about Smith Brothers
25 Farm that appeared in the Columbia Basin Herald last May?

1 A. I'm not familiar with the exact article, no.

2 Q. I represent to you that Mr. Davenport was quoted
3 in that article as saying that 20,000 gallons of raw milk
4 per day moved from the farm to your plant. Do you have any
5 reason to dispute that figure?

6 A. No.

7 Q. Now, would you agree with me that a gallon of
8 milk weighs roughly 8.6 pounds?

9 A. Yes.

10 Q. I'm going to represent to you that 28,000 gallons
11 times 8.6 is --

12 A. I'm sorry, did you say 28,000 is what he said?

13 Q. 2-8, 28, yes.

14 A. Okay. I'm sorry. I thought you said 20. The 28
15 is -- was not accurate, at least it's not at this time.

16 Q. I'm going to represent to you that if it was
17 accurate last May, 28,000 gallons times 8.6 pounds times 30
18 for a 30 day month, would be 7.2 million pounds per month
19 of production. Do you have any reason to dispute that that
20 would've been roughly what your production was last April
21 or May when this article was written?

22 A. I don't believe it was that high, just my own
23 personal -- I don't remember it being that high per day,
24 but maybe at one peak it was, but that isn't our normal
25 average.

1 Q. And I'll represent to you that I'm about two
2 quote that article, which -- believe me, I've had myself
3 misquoted in the press, so this may not be Mr. Davenport's
4 fault. But I just want to -- this will probably find its
5 way as an exhibit, so I want to let you comment on whether
6 it's accurate or not.

7 "The company has its own truck fleet that hauls
8 28,000 gallons of raw milk per day from the Royal Slope" --
9 by the way, the Royal Slope is where your farm is, right?
10 That's a geographic --

11 A. Yes.

12 Q. -- area in Eastern Washington?

13 A. Yes.

14 Q. "Hauls 28,000 gallons of raw milk per day from
15 the Royal Slope to Western Washington where it's processed
16 into consumer-ready milk, sour cream, buttermilk, eggnog,
17 and chocolate milk, sold mostly to schools." It then goes
18 on to say, however, the most -- that 65 percent goes to
19 home delivery. So would you say that that was inaccurate
20 that 28,000 gallons of raw milk were moving to be processed
21 into consumer-ready milk, sour cream, buttermilk, eggnog,
22 and chocolate milk?

23 A. I don't believe that we have 28,000 a day going
24 into packages. I think he probably was generalizing is my
25 guess, but I can't say that for sure. I'm not sure what he

1 meant by that.

2 Q. I'm going to represent to you that Mr. Davenport
3 was quoted as saying, "We are exceeding our expectations
4 about milk production without adding any animals, milk
5 production," and then this is no longer a quote, "milk
6 production with the current herd level is projected to
7 increase 20 percent over the next 12 months." Do you
8 recall projections about your milk supply on the farm
9 increasing 20 percent between last May or April and next
10 spring?

11 A. I never heard those projections it would go up 20
12 percent. That would be nice. I don't think it's possible.

13 Q. Well, I'm going to represent to you that if that
14 were the case, you would have 20 percent more than 7.2
15 million pounds, which would be a whole bunch.

16 A. Yes. I don't know if that -- if Mr. Davenport
17 was misquoted, or he was just throwing numbers around. I
18 don't know. I guess I didn't -- if I saw that article, I
19 didn't question him about it.

20 Q. Okay. Well, did you notice that he was quoted as
21 saying that he expected production per cow would increase
22 20 percent from 75 pounds a day to 90?

23 A. No, I didn't, but I think I'm going to ask him
24 about that now.

25 Q. Do those numbers sound about right? Are you

1 achieving 90 pounds a cow yet?

2 A. No, we're not. Long ways from it.

3 Q. That would be pretty good, though, wouldn't it?

4 A. Yes, it would.

5 Q. Well, is Mr. Davenport the person that gave you
6 the million dollar figure? I think you said it was, wasn't
7 he?

8 A. Yes.

9 Q. And then I just did the math, and I'll represent
10 to you that under Mr. Van Dam's analyses testified to
11 earlier, the difference between the blend price, the
12 regulated price for 2000 to October of '03 was \$1.79, and I
13 think his exhibit showed the year-to-date for 2003. It's
14 \$1.77 difference. I represent to you that I computed that
15 \$1.77 would indicate that his million dollar figure would
16 represent close to five million pounds, so that's
17 consistent with your earlier testimony about roughly five
18 million pounds of milk in -- five million pounds per month
19 going into class one uses. That sounds like it might be
20 where it came from to me.

21 My question of you is, that if that five million
22 pound figure then is your quantity of milk into the bottle,
23 and if you're producing anywhere close to the 7.2 million
24 pounds he indicated, you'd have considerable amount of milk
25 going to other locations, including, for example,

1 Matanooska Maid or surplus to us or anyone else.

2 Can you tell me, does that difference between
3 whatever your production is and the five million pound
4 level, does it go to any place other than Matanooska Maid
5 or to one of our WestFarm Foods plants?

6 MR. UNIDENTIFIED: Yes, Your Honor, I want to
7 object. He is -- these numbers are becoming very
8 confusing, and he's taking numbers that he's creating and
9 there's no testimony. She hasn't agreed to the seven
10 million or any of these numbers, and now he's wanting to
11 know what happened between the five that she hasn't agreed
12 to and the seven that she hasn't agreed to, and it's a
13 deceptive thing. If he has the evidence, let him testify
14 what his math is. He's creating math on the boards,
15 submitting that it's testimony. It's not a question, but
16 he's confusing numbers, and I think that we've got to get
17 on to something that she can talk about, not something that
18 he can talk about.

19 MR. MARSHALL: May I respond?

20 THE COURT: You may.

21 MR. MARSHALL: I've indicated that at some point
22 we'll have to introduce this into evidence, and we will
23 comment on it therefore as an exhibit in our brief. and
24 while Ms. Koester and we are on opposite sides, she is one
25 of the nicest people in our business, and I wanted to give

1 her the chance to address the issues we would be raising,
2 by suggesting to her that there's quite a variation, and
3 that that would impact the analysis suggested earlier by
4 Mr. Yale, trying to compute the burden bearing balancing
5 costs, which, of course, would be quite different if you've
6 got, for example, only five eighths of your milk going into
7 the bottle versus 90 percent.

8 THE COURT: Well, she's already testified as to
9 what her numbers were and what they mean to her, and says
10 that she has no knowledge of the numbers that you're using
11 for some of these calculations. So presenting these
12 numbers to her and asking her her opinion of these
13 calculations, I'm not sure that it's really adding
14 anything.

15 I think you'll have a chance to introduce the
16 document that you're referring to into the --

17 MR. MARSHALL: Okay.

18 THE COURT: -- exhibit --

19 MR. MARSHALL: Fair enough. And you can be --

20 THE COURT: -- and yeah, I think you've certainly
21 given her fair notice and the opponents fair notice that
22 that's what you're going to do, so --

23 BY MR. MARSHALL:

24 Q. Right, I withdraw the question and promise that I
25 will ask you at the end, unless I forget, if there's

1 anything else you want to add. So you can be thinking
2 about that if you wish.

3 Is there any reason to believe, though,
4 regardless of what the numbers may be, that you could not
5 today utilize a considerable amount of milk that you
6 produce to expand your bottling volume? Let me repeat --
7 let me rephrase that question. Is there any reason not to
8 believe that you have sufficient farm production to
9 significantly expand your bottling volume?

10 A. What do you mean by significantly? I --

11 Q. Oh, say from five million to seven. I mean, I
12 don't know. That you would likely exceed a five million
13 pound class one sale.

14 A. We don't have a home for those class one sales at
15 this time.

16 Q. Is there any limitation in terms of your farm
17 that would cause you to not to increase your production --
18 your processing into class one uses by, say, 20 percent?

19 A. First we'd have to get the cows up by 20 percent,
20 and that's not that easy to do. I'm not sure how we would
21 obtain that.

22 Q. Fair enough. Turning again to the other issues
23 relating to costs. On page 11 of your testimony, you note
24 that we, Smith Brothers, "We bear costs usually born by
25 other market participants." Could you identify what costs

1 you bear that are usually born by other market
2 participants? What are you referring to? On page 11, that
3 was.

4 A. I'm sorry, I don't see exactly --

5 Q. Okay. Look at the first new paragraph on page 11
6 Quite simply it begins, the last sentence ends, "that the
7 evidence establishes that in exchange for partial
8 regulation, we bear costs usually born by other market
9 participants." And I just want to clarify what you're
10 referring to.

11 A. I'm talking about the costs of producing the milk
12 and hauling it to our plant, and the balancing, and the
13 marketing of our product, and the distribution, just the
14 whole thing that we do that a handler doesn't do or a
15 producer does not do. We take care of all -- we have all
16 of those costs.

17 Q. Is it your belief that neither handlers nor
18 producers bear the costs of moving milk from farms of
19 pooled producers to regulated plants?

20 A. I believe somebody does bear that, but I don't
21 know that any one organization bears all of it as we do.

22 Q. I'm going to represent to you that producers in
23 Central Washington on the Royal Slope who ship their milk
24 to our cooperative are assessed a hauling cost in the
25 general range of --

1 MR. UNIDENTIFIED: Objection, Your Honor, he can
2 have his people testify to that statement.

3 THE COURT: Well, he's making a representation
4 for the purpose of a question. It's --

5 MR. MARSHALL: Yes.

6 THE COURT: -- that's the same as a hypothetical
7 or an assumption. He can -- that's not -- he's not -- that
8 factor's not in evidence. It's an assumption for a
9 question, --

10 MR. MARSHALL: That's right.

11 THE COURT: -- and he can ask it.

12 BY MR. MARSHALL:

13 Q. And I want again to represent to you that our
14 producers in your neighborhood would have a hauling charge
15 in the general range of 50 cents a hundredweight. Would
16 that approximate -- would 50 cents a hundredweight
17 approximate what your costs of hauling are to move milk
18 from the Royal Slope to Kent?

19 A. I don't recall that number at the present time
20 exactly what it is.

21 Q. So you don't know whether that is a cost that's
22 not born by -- usually born by other market participants,
23 do you?

24 A. What I meant by the statement was that we bear
25 the costs of both the producer and the processor.

1 Q. Of both a regulated pooled producer and a
2 regulated pool plant?

3 A. Yes.

4 Q. So there's no difference between your scenario
5 when you bear those costs and the alternative of
6 regulation, is there?

7 A. Well, I believe that we do have added costs with
8 our balancing and with trying to match our sales with
9 production.

10 Q. Okay. In just those two?

11 A. Yes.

12 Q. On top of page nine, you suggest that if you had
13 a cost advantage, you would never lose a sale. I assume
14 you mean you'd never lose a sale to a regulated plant,
15 based on price. But you do lose sales based on price. Are
16 you aware that sometimes it's necessary for plants in a
17 competitive market to meet the competition, even if it is a
18 sale below their cost?

19 A. Yes.

20 Q. Now, later in that paragraph you refer to having
21 a distinct price advantage. Did you mean a cost advantage?

22 A. I'm sorry, what page was that on?

23 Q. The -- I'm sorry, I misquoted you. On the top of
24 page ten, "Adoption of these proposals would place us,
25 Smith Brothers, at a distinct price disadvantage." Did you

1 mean a cost disadvantage, or did you mean --

2 A. Is this bottom of nine and top of ten?

3 Q. Yes, that paragraph.

4 A. I said, "We do not have an unfair price
5 advantage."

6 Q. Right, and then you go on in the last sentence of
7 that paragraph, "The adoption of these proposals would
8 place us at a distinct price disadvantage." Did you mean a
9 cost disadvantage?

10 A. Well, it would be the price of our milk, what we
11 had -- what I meant was the price we'd pay getting it into
12 our plant would be a price disadvantage. So I guess it
13 would be the same as a cost, but it was the price we'd have
14 to pay for our milk, which right now is our cost, but if we
15 were --

16 Q. I follow you. Okay.

17 A. Okay.

18 Q. Understood. Thank you.

19 Okay. I -- this is my last question. I accept
20 that I did promise that I would ask you if there's anything
21 that you thought of about the testimony that you've given
22 in response to my questions that you'd like to amplify.

23 A. Not that I can think of at the moment.

24 MR. MARSHALL: Okay. Thanks very, very much.

25 MR. BERDE: I think that was a wise answer. As

1 you probably know by now that every question and answer
2 prompts another question. That's the nature of these
3 proceedings.

4 I apologize if I'm prompted to do it.

5 Sydney Berde.

6 MR. UNIDENTIFIED: Well trained.

7 EXAMINATION

8 BY MR. BERDE:

9 Q. You indicated in your prior testimony that one of
10 your owners is a distributor; is that right?

11 A. Yes.

12 Q. And is that distribution business a separate
13 business that he owns?

14 A. He's self-employed. The --

15 Q. He's self-employed?

16 A. The distributors are self-employed, individuals
17 that buy their milk from us, and then they sell it to their
18 individual homed customers.

19 Q. I understand, but is -- but he owns, as a
20 separate business, and receive the benefits of the revenues
21 of that business as an individual, does he not?

22 A. He doesn't actually own it, but it's his
23 customers that -- he doesn't own the route. We actually
24 lease it to him, but he receives the benefits of the
25 difference in the price that we charge him and what he

1 charges his customers, less his gasoline, his truck
2 expense, and all the expense of doing business. He --

3 Q. Okay.

4 A. That's his job. That's what he does for a
5 living.

6 Q. What does he realize in terms of his own income
7 from the operation of that distribution business?

8 A. I don't know what his income is for -- total
9 income for the year. I have no idea.

10 Q. Well, for openers, it's the difference between --
11 it's the margin between what you transfer that packaged
12 product for and whatever he gets from the ultimate buyer,
13 is it not?

14 A. Yes, less all of his expenses for gasoline and
15 truck and all of that.

16 Q. Okay. Does he pay those?

17 A. Yes.

18 Q. Okay. When he files a tax return at the end of a
19 year, does he file it as the operator of a fluid milk
20 distribution business?

21 A. Yes.

22 MR. UNIDENTIFIED: How in the world is this
23 witness supposed to know --

24 THE COURT: She -- well, she doesn't know, and
25 she can say she doesn't know. But she said yes, so I

1 assume she must know, --

2 MR. UNIDENTIFIED: Well, you know, --

3 THE COURT: -- you know.

4 MR. UNIDENTIFIED: -- maybe she gets tired of
5 trying --

6 THE COURT: I don't know.

7 THE WITNESS: And I'm assuming he files his tax
8 return.

9 MR. BERDE: Well, yeah, but does he --

10 THE COURT: I've heard her say that she doesn't
11 know. Any question that anyone asks you, if you don't know
12 the answer, --

13 MR. BERDE: Yeah.

14 THE COURT: -- you say you don't know, but --

15 MR. BERDE: Now, --

16 THE COURT: -- once you say yes, we assume that
17 you know what his tax return says.

18 BY MR. BERDE:

19 Q. So he pays his own costs of the operation of that
20 business, right?

21 A. Yes.

22 Q. And he retains whatever net margin is left after
23 paying all those costs from the revenues derived from the
24 sale of the product; is that correct?

25 A. Yes.

1 Q. Okay. Now, if he comes to you and said, look,
2 I've got to have some help on the cost of this batch of
3 product because I got a piece of business that I can get,
4 but I can't get it unless you give me some help, how --
5 what do you do -- how do you respond to that?

6 A. Well, he hasn't ever asked me that.

7 Q. Okay. Now, do you transfer the product to him at
8 the same cost for the same product as you transfer a
9 similar product to your other distributors?

10 A. Absolutely.

11 Q. So all of the distributors pay your processing
12 plant the same price for the same product; is that it?

13 A. All of our home delivery distributors, yes.

14 Q. Oh, is he a only a home delivery?

15 A. Yes.

16 Q. Okay. But some of your distributors sell to
17 institutions, don't they?

18 A. They could. I don't have their customer base. I
19 don't know exactly what their -- who their customers are in
20 all cases.

21 Q. I understood from your prior testimony that some
22 of your business is institutional business.

23 A. Yes, but we have institutional business at our
24 house accounts that we serve with our employees.

25 Q. Directly, you mean?

1 A. Yes. Yes.

2 Q. Not through your distributive handler -- not
3 through your distributors' business?

4 A. Some of them could, but we do also, ourselves.
5 What I was referring to before, I was talking about us
6 serving the institutions.

7 Q. Okay. Now, so I'll ask you a question about,
8 what happens again if one of your distributors comes to you
9 and says, I can get some more business, but I need some
10 help? How do you respond to that kind of request?

11 MR. UNIDENTIFIED: Your Honor, it's been asked,
12 she's answered it. Can we move on to something else?

13 THE COURT: Well, it was asked, but with respect
14 to one particular person. So he's asking her now
15 generally, which is not the exact, same --

16 MR. UNIDENTIFIED: (Indiscernible)

17 THE COURT: I don't -- if it's the same answer,
18 then we'll find that out.

19 MR. UNIDENTIFIED: And at some point, Judge, can
20 we get some relevance so we can move on --

21 THE COURT: I don't know what people are going to
22 ask, you know. I just don't know.

23 MR. UNIDENTIFIED: (Indiscernible) responsibility
24 in that area.

25 MR. BERDE: I find it exceedingly odd to hear a

1 question about relevancy from counsel who is just posed
2 that problem.

3 THE COURT: I'll just let you have --

4 MR. UNIDENTIFIED: And (indiscernible)

5 THE COURT: Okay. Was the question fully asked?
6 I can't remember now any more. You asked her a question,
7 right?

8 MR. BERDE: I asked, yeah.

9 THE COURT: Okay. Do you remember the question?
10 (No verbal response)

11 THE COURT: Okay. Why don't you try to answer it
12 then?

13 THE WITNESS: I haven't been asked that question,
14 so I can't give you an answer.

15 BY MR. BERDE:

16 Q. Now I want to talk about your own distribution to
17 institutional business. If you have an opportunity to get
18 some increased institutional business, would you sell
19 directly and you have a problem with competition, how do
20 you respond to that kind of a problem?

21 A. We don't serve that customer that time.

22 Q. Uh-huh.

23 A. Sometimes we have the business, sometimes we
24 don't.

25 Q. Uh-huh.

1 A. Every time we bid we take the risk of losing it,
2 so our response is, we just don't have that customer at
3 that time.

4 Q. Okay. Have you ever done any private label
5 business?

6 A. We've done a little.

7 Q. And for what kind of outlet?

8 A. That's proprietary information.

9 Q. Have you ever done -- and this may be a
10 repetition of what you've testified to before, but if it
11 is, I apologize.

12 Have you ever done any private labeled business
13 for an outlet for which another handler has done a private
14 label in the same package?

15 A. I'm sorry, would you ask that again?

16 Q. Have you ever done private label packaging for an
17 outlet where another handler has also supplied that same
18 outlet with the same private label?

19 A. Not that I'm aware of.

20 Q. Do you sell any packaged products to distributing
21 plants outside the marketing area?

22 A. I'm sorry, packaged products outside the
23 marketing area?

24 Q. Yes.

25 A. No.

1 Q. Are there any periods during the flush (phon.)
2 when your production goes up that you attempt to dispose of
3 product by discounting from your regular price?

4 A. Not that I can recall.

5 Q. You're not in business, of course, to sell at a
6 loss, are you?

7 A. To sell where?

8 Q. To sell at a loss. I mean, you're in business to
9 make a profit in every packaged sale?

10 A. Yes, but as Mr. Marshall said, sometimes you have
11 to sell things at a loss, part of it, where you're not
12 covering all your costs.

13 Q. But when he asked your questions about your sale
14 to Alaska, I don't think we got an answer as to whether
15 that was a profitable transaction.

16 A. I don't know that off the top of my head.

17 Q. Well, that was the reason for my question.
18 You're not in the business to sell at a loss, are you, and
19 if you got that business, can we presume that it was
20 profitable?

21 A. Yes.

22 Q. Over the period of a year, what is the small
23 fraction -- quoting your description, what is the small
24 fraction of your total production that you find necessary
25 to dispose of? You mean, small fraction, you mean about

1 two to three percent?

2 A. I'm sorry, which page was that testimony on?

3 Q. It wasn't in the testimony. It wasn't in your
4 prepared testimony, it was in your response to some
5 questions. You indicated that you -- during -- that some
6 times of the year you are required to dispose of some
7 surplus, and you described that disposition as a small
8 fraction, using your words, of your total production, and
9 I'm asking you what you mean by a small fraction. Is it
10 about two to three percent?

11 A. It varies. It varies from month to month, and I
12 don't know what it would be on an overall year -- I don't
13 know that number.

14 Q. But -- well, I'll ask it then with respect to
15 month-to-month. Month-to-month, is it about two to three
16 percent?

17 A. No, right now we don't have any surplus.

18 Q. No surplus now?

19 A. No.

20 Q. When would the surplus begin?

21 A. I don't really know, but it could happen at
22 Christmas time when schools are out for holiday. Could
23 happen then. I don't perceive it happening before then.

24 Q. Yeah. How long would it last, over the period of
25 the Christmas holidays?

1 A. Probably.

2 Q. And at that point, would it be about two to three
3 percent?

4 A. I don't know.

5 Q. And then it would subside in succeeding months,
6 no surplus; is that right?

7 A. If our production stays the same and our sales
8 stay the same, and we haven't lost any sales or gained any.

9 Q. All right. Now, taking all that into
10 consideration over the period of a year, can you give me an
11 estimate of what that would bottom out to, about -- would
12 it be about two to three percent over the 12 month period?

13 A. I don't know.

14 MR. BERDE: Thank you very much.

15 EXAMINATION

16 BY MR. BESHORE:

17 Q. Marvin Beshore for Dairy Farmers of America.

18 Ms. Koester, just a couple of questions about the
19 farm operation -- the new farm operation out on the Royal
20 Slope, you call it. Why was it located there? I take it
21 that's a favorable production area in the state; is that
22 correct?

23 A. We had a feed lot right next door, and it was in
24 Eastern Washington which is not as populated as Western
25 Washington. So it just made sense for us to have our

1 facilities side by side there.

2 Q. Isn't that also a favorable part of the state of
3 Washington for the production of milk?

4 A. More so than Western.

5 Q. Okay. And is it -- while it's not, as far as you
6 know, it's not presently permitted for more cows, is the
7 facility sized to handle more cows?

8 A. We don't have barns for more, and we don't have a
9 milking parlor for more. We would have to build all that
10 if we, indeed, wanted to.

11 Q. Do you have land for more facilities?

12 A. We do.

13 Q. How many more could you accommodate?

14 A. We probably have land to double the size.

15 Q. Okay. Now, there have been a couple of areas
16 where you have stated with certainty that information in
17 the record or presented to you in a question was not
18 accurate. For instance, you responded to Mr. Marshall that
19 the 28 million pounds per -- was it 28 million pounds, that
20 the --

21 MR. UNIDENTIFIED: (Indiscernible) gallon --

22 BY MR. BESHORE:

23 Q. 28,000 gallon figure quoted in the newspaper
24 article was not accurate?

25 A. No, I don't believe it is.

1 Q. Okay. What is the accurate figure, if you know
2 that's not accurate, are you prepared to provide for the
3 secretary, information that's in the record about what the
4 accurate figure is for production --

5 MR. UNIDENTIFIED: Per day.

6 BY MR. BESHORE:

7 Q. -- per day at your farm?

8 A. I believe that's proprietary information.

9 Q. Well, is 25 million accurate -- 25,000, I'm
10 sorry, gallons.

11 A. It's closer than 28.

12 Q. Okay. Closer than 28. Okay. How about 22?

13 A. No.

14 Q. That's not accurate?

15 A. No.

16 Q. Okay. Is it closer than 25?

17 A. No.

18 Q. It's not closer than 25?

19 A. No.

20 Q. Is it between the two?

21 A. No, it varies day to day. I hate to give a
22 figure here exactly.

23 Q. Because you don't know, or because you just don't
24 want to provide the information?

25 A. I don't know exactly because it varies day to

1 day.

2 Q. Okay. Is there -- can you give us a monthly
3 average per day, or a yearly average per day?

4 MR. UNIDENTIFIED: Objection, Your Honor, she
5 said that's proprietary information.

6 THE COURT: Right, and I'm going to just ask her
7 that again. I mean, is it proprietary, or is it a number
8 that you would give if you knew what the number was?

9 THE WITNESS: Well, it varies, because --

10 THE COURT: Well, I'm saying -- but, no, no,
11 that's not my question.

12 THE WITNESS: Okay.

13 THE COURT: My question -- a minute ago you said
14 it was proprietary, and then you fell for the guessing
15 games of Mr. Beshore, and --

16 MR. BESHORE: I didn't start the guessing game,
17 Your Honor.

18 THE COURT: I know, but okay.

19 MR. BESHORE: She testified with certainty what
20 it is not.

21 THE COURT: Right. Okay. Okay. So the question
22 is, you know, it's sort of like having your cake and eating
23 it, too. Is it -- it's either proprietary, or it's not
24 proprietary. So it's up to you to decide what you want to
25 do.

1 THE WITNESS: I believe it is close to 25,000 per
2 day.

3 BY MR. BESHORE:

4 Q. Okay. Now, with respect to your costs, do you
5 know your cost of production per hundredweight at your
6 farm?

7 A. No, not at the present time. It varies month to
8 month, too, and I -- and that is proprietary, but I don't
9 know it, even --

10 Q. Okay. It's proprietary, --

11 A. Yes.

12 Q. -- but you can testify with certainty that the
13 United States Department of Agricultural statistics
14 reflected in the publication reproduced by Dr. Smith is not
15 accurate; is that your position here?

16 A. It was not accurate for our farm.

17 Q. Okay. But you will not provide information with
18 respect to what the accurate figures are for your farm,
19 correct?

20 A. Yes, I will not.

21 Q. What type of containers do you supply your fluid
22 milk products in, cardboard?

23 A. Yes and a few plastic gallons.

24 Q. Okay. Are all the half gallon and smaller,
25 cardboard containers?

1 A. Yes.

2 Q. Do you purchase your feed for the cattle or grow
3 feed for the cattle?

4 A. We purchase it.

5 Q. 100 percent?

6 A. We might do a little bit of alfalfa, but very
7 little, just very small.

8 Q. Is the -- the feed lot is beef cattle, I assume?

9 A. No, we raise our replacement heifers there.

10 Q. Okay. So when you talk about a feed lot, that's
11 your own dairy replacement operation. And the dairy
12 replacements were there even when the milking dairy was in
13 Kent?

14 A. Yes.

15 Q. Okay. Do you engage in -- since you purchase all
16 your grain, do you hedge those prices?

17 A. No.

18 Q. Ride with the markets?

19 A. Yes.

20 MR. BESHORE: Okay. Thank you.

21 THE COURT: Okay. Ms. Deskins?

22 EXAMINATION

23 BY MR. ROWER:

24 Q. Jack Rower, USDA.

25 Ma'am, I just wanted to ask very quickly, it's

1 been an observation of ours that with a few notable
2 exceptions, the largest, most successful producer/handlers
3 are located in states that bordered on regulated areas. Do
4 you ascribe that to a balancing advantage, perhaps?

5 A. Well, we're not -- we don't really border
6 unregulated.

7 Q. Well, Alaska. No, Alaska -- obviously we don't
8 border Alaska, but you're nearest of any of the other
9 states to Alaska.

10 A. Okay. And so what was your question again?

11 Q. Would you ascribe the number of large, successful
12 producer/handlers to their location with respect to
13 unregulated areas within the federal system?

14 A. I don't know.

15 MR. ROWER: Thank you.

16 EXAMINATION

17 BY MS. DESKINS:

18 Q. I have a couple of questions for you.

19 On page three --

20 THE COURT: Please identify yourself.

21 BY MS. DESKINS:

22 Q. Oh, I'm Sharlene Deskins with Office of General
23 Counsel, USDA.

24 On page three, you talk about servicing a niche
25 area customers. Do you compete with other

1 producer/handlers to service that niche?

2 A. Not in the home delivery business.

3 Q. If the proposals were changed to exempt
4 producer/handlers that service a niche area, would you be
5 in favor of that?

6 A. Well, it would help us if it didn't limit us just
7 to the niche area. If we couldn't do anything else, it
8 would help us, but my true belief is that I don't believe
9 producer/handlers should be in the pool whether they have
10 that niche market or if they serve other types business.

11 Q. Okay. On page -- this question relates to your
12 testimony from page eight, and I was just wondering if you
13 were suggesting with that testimony that there are economic
14 conditions that would limit the size of a producer/handler?

15 A. On the second paragraph there?

16 Q. I believe so, yes.

17 A. Where it says there's a decline?

18 Q. Yes.

19 A. And I'm sorry, what was your question again?

20 Q. My question is, I was wondering if you were
21 suggesting that there are economic conditions that will
22 limit the size of a producer/handler?

23 A. Yes.

24 Q. Okay. Can you tell us what those economic
25 conditions are?

1 A. Well, I believe that raising your own cows and
2 producing your own milk is an economic condition, and
3 depending on what the climate is for selling your milk in
4 the area that you are, if you can get a fair price or a
5 price that you can make money on would make a difference.
6 There's the investment and the risk of having the dairy
7 cows and the farm and the plant and the trucks for
8 distribution. There's a lot of risk there, that you're
9 putting everything on the line to the bank for all of your
10 -- you have a lot more at risk because you have a larger
11 operation for different aspects of it.

12 Q. Okay. Since you do think that economic
13 conditions would limit the size of producer/handlers, do
14 you have any idea of how big a producer/handler would get
15 for the economic conditions starting to limit their size?

16 A. I don't.

17 Q. And this also relates to page eight. I was
18 wondering -- you might have already answered it, but let me
19 just ask you this. How would a cap of three million pounds
20 be contrary to the Congressional purposes for having a
21 producer/handler?

22 A. Because in the past they haven't limited their
23 size of any sort. They've just made them have an
24 exemption. I feel that limiting their size would be
25 against what the policy has always been.

1 Q. Okay. Another question I have is, do you only
2 compete with other handlers on the basis of price for a
3 customer, or are there other things such as quality that
4 you compete with them on?

5 A. There are a lot of issues, and quality has been
6 something that we have really prided ourselves in, the fact
7 that our customers, especially the home delivery ones, say
8 their children will only drink our milk, and they say it
9 different. And there seems to be a demand for that, and as
10 far as service, there is a big discrepancy in there, and we
11 have to compete in that, and we have to be able to service
12 the accounts. We have gotten calls from customers that
13 have gotten service from distributors that don't give the
14 same quality of service that we do as far as putting the
15 product away and doing that sort of thing. So we have to
16 compete very strictly in that, in the service area, and in
17 the quality.

18 Q. Okay. Also as it relates to your testimony, I
19 believe this is from page nine. Can you tell us how the
20 producer/handler status limits the customers that you can
21 have?

22 A. Well, it would -- if we had a large customer that
23 would want to grow, or their business would grow, it could
24 limit our ability to serve them. I'll give you an example.
25 We used to serve a distributor that sold to Starbucks

1 Coffee, and we were the sole supplier to them. Starbucks
2 got too big where we couldn't supply the distributor with
3 all the milk for Starbucks. We lost that business because
4 they got too big. So if a customer grows too much, then we
5 wouldn't have the milk to do it, unless we chose to invest
6 more in cows and all that.

7 Q. And also if the secretary should find that
8 evidence does support limiting the size of
9 producer/handler, do you think that such a limit should be
10 based on what percentage the producer/handler has of the
11 market or on any other factors?

12 A. I'm sorry. Ask that again.

13 Q. Okay. If the secretary should decide that it is
14 appropriate to limit the size of the producer/handler, do
15 you think such a limit should be based on the percentage
16 that the producer handler has of the market, or any other
17 factors?

18 A. I feel it should be based on maybe the ones that
19 are already producer/handlers and give them some
20 opportunity to grow, because for so many years we've been
21 under this cloud of them trying to do away with our status,
22 and it's very difficult to keep operating and always
23 thinking they could do away with us, and wondering if we're
24 making the right decision to keep putting more money into
25 your business. And I believe that they should leave some

1 room for growth and shouldn't limit the ones that are
2 already in operation.

3 MS. DESKINS: Okay. Thank you.

4 THE COURT: Mr. Ricciardi, do you have any
5 questions of this witness?

6 MR. RICCIARDI: I don't, Your Honor.

7 THE COURT: Ms. Reed, do you have any more -- any
8 redirect or any other questions?

9 MS. REED: Could we -- could I have just a
10 moment? Could we take a break now and (indiscernible) I
11 don't believe that we do, but she's been on the stand for a
12 while now.

13 THE COURT: Hours and hours. Okay. Let's --
14 I'll tell you what. Let's take our -- let's take a 15
15 minute break, and when we come back, I want to have an off-
16 the-record discussion as to where we have -- where and when
17 we have our next session. Not tomorrow, I mean, but when
18 this week's over, because this is not going to be over when
19 this week is over (indiscernible).

20 Go off the record.

21 (Off the record and reconvened.)

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

23 Two announcements. One about tomorrow. I don't
24 know if people were -- have -- we apparently are not in
25 this room tomorrow. We're apparently in the grand

1 ballroom, which is just across that little patio, whatever
2 it is around the corner here. It's directly opposite us,
3 so I think we're there tomorrow, and then we're back here
4 again on Friday.

5 We just had an off-the-record discussion looking
6 at calendars and all, because this is -- this hearing
7 obviously isn't going to finish this week. And I just
8 blocked out the -- from -- there's a four day week in
9 January. It's the week of Martin Luther King Day, which is
10 January 19th. So the January 20th through 23rd, we're
11 going to continue this hearing in Washington, D.C., in the
12 Washington, D.C. metropolitan area, not a guarantee that
13 we'll be in D.C. We might be in Alexandria or somewhere
14 within a reasonable distance, depending on if we can find a
15 room.

16 I'll plan it for four full days. So we'll plan
17 to go, like, 8:30 to whatever, 5:00 or 5:30 or 6:00 or
18 whatever, Tuesday through Friday that week.

19 We're also in the -- in the event that we can't
20 finish that week, we're at least for now, just reserving
21 the week of February 17th through 20th. February 16th is
22 Presidents Day, I believe, so that's also a federal
23 holiday. So it'll be another four day week, and that would
24 also probably be in D.C. unless there's a really good
25 reason to have it elsewhere.

1 So that's where we stand now in terms of
2 continuing the hearing. And in terms of continuing the
3 hearing today, I've been advised that Ms. Reed did not have
4 any redirect of the witness, and therefore the witness is
5 excused, and it's time to hear who the next witness is
6 going to be.

7 MR. UNIDENTIFIED: Your Honor, we would call
8 Daniel Morrison.

9 THE COURT: Okay.

10 MR. UNIDENTIFIED: His statement is in the back
11 of the room.

12 THE COURT: Oh, I never did ask, she had Exhibit
13 39 -- Mr. Miltner -- Mr. Yale, Exhibit 39 she had marked
14 for identification.

15 MR. YALE: We'd move that to be admitted, Your
16 Honor.

17 THE COURT: Okay. And I'm going to admit Exhibit
18 39 into evidence.

19 (Exhibit No. 39 was received.)

20 THE COURT: Do you have a copy for me, by any
21 chance?

22 MR. UNIDENTIFIED: -- have one, Your Honor.

23 THE COURT: Will you please raise your right
24 hand?

25 DANIEL R. MORRISON, WITNESS, SWORN

1 THE COURT: Okay. Could you please state your
2 name for the record, and then spell it?

3 THE WITNESS: My name is Daniel R. Morrison, D-a-
4 n-i-e-l, R., M-o-r-r-i-s-o-n.

5 EXAMINATION

6 BY MR. MILTNER:

7 Q. Mr. Morrison, thank you for coming today. My
8 name is Ryan Miltner, and I represent Smith Brothers Farms,
9 Mallory's Dairy and Edaleen Dairy.

10 Mr. Morrison, were you retained on behalf of
11 those dairies to participate in this hearing?

12 A. Yes, I was.

13 Q. And as part of that agreement, have you done some
14 analysis of prior testimony in the hearing?

15 A. Yes, I have.

16 Q. Okay. Before we get into that analysis and your
17 report, what you've prepared, I have -- you also represent,
18 or have prepared this on behalf of Sarah Farms; is that
19 correct?

20 A. That is correct.

21 Q. Thank you. I'd like to go over your background a
22 little bit before we get into your report. Could you just
23 provide for the record a description of your education and
24 professional background?

25 A. Yes. Yes, I'd like to do that. I'm a CPA. I

1 have a BS in accounting and an MBA, and I've worked as an
2 accountant and in various financial roles over the last 20
3 plus years, starting in Big Four Public Accounting, moving
4 through industry, and for the last ten years, I've been
5 associated with the dairy industry, nine with Dean Foods
6 mostly as the CFO of their dairy operations, but also as
7 corporate controller. And then over the last year, I've
8 started up a business that I call the Aperio Group (phon.),
9 which consults with retails with regard to dairy costs.

10 Q. Can you describe for the record what types of
11 duties you would be responsible for in your various roles
12 with the Dean Foods Company?

13 A. In the Dean Foods role, was pretty broad. I
14 reported to the president of the dairy division, and I was
15 responsible for all aspects of accounting, financial
16 reporting, very involved in acquisitions, cost accounting,
17 strategic planning, kind of you name it, I did a lot.

18 Q. But your primary focus or one of your primary
19 focuses was in the area of cost accounting?

20 A. Cost accounting was an important piece of it,
21 yes.

22 Q. Was that done at the plant level?

23 A. Yes, it was.

24 Q. And then you left the Dean Foods Company, and you
25 started the Aperio Group?

1 A. That's correct.

2 Q. What does -- what's your role with the Aperio
3 Group?

4 A. I'm one of the -- I'm a partner with the Aperio
5 Group and one of three founders. So essentially, all
6 aspects of developing this business. We've not gone to
7 market yet, but what the Aperio Group's going to be about
8 is kind of demystifying, I guess you could say, dairy
9 costs, all aspects of dairy costs for retailers, to help
10 them negotiate dairy supply contracts.

11 Q. Is there any other information you'd like to
12 provide on your background either --

13 A. I think that's a fair representation.

14 Q. Okay. You were not in attendance for the initial
15 portion of this hearing in Phoenix, were you?

16 A. No, I wasn't.

17 Q. Okay. Are you aware that there was a gentleman
18 who testified at that hearing by the name of Carl Herbine?

19 A. Yes.

20 Q. Have you had a chance to review Mr. Herbine's
21 testimony?

22 A. Yes, I have. I've reviewed Mr. Herbine's
23 testimony and his financial schedules.

24 Q. And how did you obtain that information?

25 A. I received that from my clients.

1 Q. Okay. Through our office?

2 A. Through your office, yes.

3 Q. After you had a chance to review Mr. Herbine's
4 testimony and his accompanying exhibits, you reviewed
5 those, and you prepared your report which you're prepared
6 to present today?

7 A. That is correct.

8 Q. And would you like to go ahead?

9 Additionally, did you have a chance to review the
10 testimony of Roger Cryan?

11 A. I reviewed piece of that, yes.

12 Q. Okay. But primarily it was Mr. Herbine's --

13 A. Mr. Herbine's, correct.

14 MR. MILTNER: Mr. Berde suggested we would --
15 we've prepared written testimony with four attached tables,
16 which we would like to mark for identification, Your Honor.

17 THE COURT: Okay. That will be Exhibit No. 40.
18 (Exhibit No. 40 was marked.)

19 THE COURT: I've marked it as one exhibit. You
20 don't want to piecemeal --

21 MR. MILTNER: No, one exhibit is fine.

22 BY MR. MILTNER:

23 Q. Mr. Morrison, will you go ahead and read your
24 testimony for the record, please?

25 A. Yes, I will.

1 "My name is Daniel R. Morrison. I'm a partner of
2 the Aperio Group, LLC, whose offices are located in Downers
3 Grove, Illinois.

4 "The Aperio Group is a consulting business
5 specializing in dairy cost management systems for large
6 grocery retailers. Aperio's proprietary efficient
7 processor cost technology provides clients with critical
8 information from which to negotiate a dairy supply
9 contract. Prior to forming the Aperio Group this year, I
10 was employed by Dean Foods Company at their corporate
11 headquarters in Franklin Park, Illinois for nine years. My
12 position at Dean Foods included Vice-President of Finance
13 and Administration of the Dean Foods Dairy Group and Vice-
14 President and Corporate Controller of Dean Foods Company.

15 Q. Dan?

16 A. Yes.

17 Q. Slow down just a little bit so we --

18 A. Okay.

19 Q. -- can get that --

20 A. I'm sorry.

21 Q. -- recording down.

22 A. It's just a lot to read.

23 "At Dean Foods, as a member of the senior
24 management team, my responsibilities included accounting,
25 financial reporting, acquisitions, cost accounting, and

1 strategic planning. Prior to Dean Foods, I held senior
2 level positions in industry and Big Four Public Accounting.
3 I'm a CPA and hold a BS in accounting from Illinois State
4 University and an MBA from Northwestern University.

5 "I've been engaged by Smith Brother Farms,
6 Edaleen Dairy, Mallory's Dairy, and Sarah Farms to provide
7 financial information regarding efficient dairy processing
8 plant size and cost.

9 "My analysis of the testimony previously
10 presented at this hearing suggests that Carl Herbine's
11 testimony that producer/handlers processing more than three
12 million pounds of milk per month can effectively compete as
13 processors against larger processing facilities is
14 inaccurate. Additionally, the analysis done by Mr. Herbine
15 on warehouse store sales reached a conclusion unsupported
16 by market realities.

17 "My expertise is in the area of dairy plant
18 costs, not in federal milk marketing orders. My testimony
19 is intended only to address the methods, data, and
20 conclusions of Carl Herbine.

21 "The competitive landscape. All three players in
22 the fluid milk supply chain, dairy farmers, dairy
23 processors, and retailers have been consolidating at a
24 rapid pace over the last ten years. This consolidation is
25 driven by the same issues that face all industries, the

1 need to continuously reduce operating costs and the need to
2 expand geographic coverage to better service the customer.

3 "Cost reduction in the fluid milk processing
4 industry -- cost reductions in the fluid milk processing
5 industry are largely achieved through a scale. Operating
6 scale does matter in fluid milk processing plants.

7 "Larger production plants do delivery
8 substantially lower processing costs, and national
9 retailers, with their continued consolidation and demand,
10 are demanding more from their suppliers, and they're
11 getting it. Considering this, I find it curious that the
12 issue at this hearing is the alleged disruption PHs are
13 causing in the fluid milk marketplace. Larger fluid
14 processors today have enormous advantages over PHs in terms
15 of scale, geographic coverage, and product breadth.

16 "The large national and regional fluid processors
17 offer customized dairy programs to their customers with
18 incentives and efficiencies a PH could never offer. For
19 instance, the multiple plant networks many fluid processors
20 have allows them to provide regional and/or national
21 service to keep customers. This is a substantial benefit
22 to the retailers, allowing them to streamline the number of
23 dairy suppliers they deal with, and accordingly, reduce the
24 cost of their purchasing operations.

25 "The multiple plant networks also provide many

1 other benefits to the retailers, included the added
2 insurance of production back-up in the event of a single
3 plant supply disruption and access to additional production
4 capacity during periods of unusually high sales volume,
5 such as promotional periods or seasonal surges and volume.
6 These are hugh issues to retailers and play an important
7 part in their supply decision-making process.

8 "The large processes also offers scale based
9 services that smaller processors find more challenging to
10 offer, including technology driven programs such as
11 automated order entry, scan pay and EDI invoicing and
12 payment systems. These systems not only drastically reduce
13 the cost of doing business for the retailer, but also lock
14 in customers by raising the cost and complexity of changing
15 suppliers.

16 "All of these issues add up to large fluid
17 processors having substantial non-plant cost advantages
18 over PHs today. If fluid processors do have a threat
19 today, perhaps it lies in the area of captive dairies.
20 Many of the largest national chains, such as Kroger and
21 Safeway operate their own dairies and for good reason.
22 Milk is the largest, private label category in the grocery
23 store, and retailers have been able to successfully develop
24 their own brands in the milk category.

25 "Captive plants typically have substantial cost

1 advantages to full line fluid plants, and consequently can
2 be a strong, economic alternative to independent suppliers
3 for a retailer. Captive plants can be scaled precisely to
4 the retailer's volume requirements and thereby achieve the
5 full benefit of production leverage, which independents
6 seldom achieve due to the breadth of their product line and
7 the fluctuating volume.

8 "Plant volume and costs. Testimony has been
9 given at this hearing on the plant volume and cost per
10 gallon by Mr. Herbine. This testimony was used to draw
11 conclusions about plant scale needed to achieve competitive
12 costs for fluid milk processors. No rational economist or
13 cost accountant would argue against the fact that as volume
14 at a plant increases to approach the theoretical capacities
15 of the plant, economics of scale are achieved in the unit
16 costs of processing milk decreases according. That is, I
17 agree with Mr. Herbine to the extent the processing costs
18 are inversely related to plant volumes.

19 "However, in my professional judgment and
20 opinion, Mr. Herbine's conclusions in these areas to not at
21 all reflect the reality of today's fluid milk marketplace.
22 For example, Mr. Herbine states, "At the two million pound
23 per month size, a producer/handler can be fully competitive
24 with regulated pool plants on a cost of processing and
25 packaging basis." At this point, the competitive

1 interaction between these handlers and the marketplace will
2 be determined by the respective cost of raw milk.

3 First of all, to suggest that at only three
4 million pounds a month, a PH can be fully competitive with
5 a regulated pool plant in his assumption -- is an
6 assumption not founded in the facts of today's marketplace
7 and is not even close to reality. One only needs to look
8 at the standard productive capacity of fluid milk filling
9 equipment today to realize how off base this conclusion is.

10 "For example, standard gallon bottle fillers
11 purchased today are rated at line speed of up to 100
12 gallons a minute. The following example illustrates the
13 theoretical capacity -- productive capacity of a single
14 gallon line, assuming a run rate of 80 gallons a minute in
15 a 100 hours of weekly processing time, both reasonable
16 industry benchmarks. Gallons per minute, 80; gallons per
17 hour, 4,800; gallons per week at 100 hours of processing
18 time, 480,000 gallons, which converts to pounds at 4.1
19 million pounds per week, which calculates to over 16
20 million pounds on a monthly basis.

21 "In this illustration, a single gallon line alone
22 could process over 16 million pounds a month. When you add
23 in half gallons and other products a plant would likely
24 produce, you quickly see that the minimum volume of 20
25 million pounds per month are necessary to effectively

1 utilize the productive capacity of a plant, and thereby
2 have competitive costs.

3 "To suggest that a fluid processor could somehow
4 run a dairy plant and what amounts to ten percents of its
5 theoretical capacity and achieve a competitive cost is not
6 reasonable. This fact was confirmed years ago in the
7 February 1997 Cornell study of fluid milk plant
8 productivity. Cornell selected 35 respected dairies --
9 dairy processing plants from throughout the United States.
10 The plants were a mix of independent, coop, and captive
11 fluid processing plants.

12 "All aspects of fluid milk processing costs were
13 surveyed and a detail report was issued. From a plant
14 volume standpoint, the average plant in the study was
15 running at 75 percent of capacity and averaging 27 million
16 pounds a month. Indeed, the smallest plant in the study
17 was processing 12 million pounds a month, and the largest
18 was in excess of 50 million pounds per month. To suggest
19 that a PH could somehow be cost competitive with this set
20 of processors while only running three million pounds a
21 month is simply not realistic.

22 "The Cornell study was also informative with
23 regard to plant costs. In the survey plant costs ranged
24 from a low of 12 cents a gallon to a high of 28 cents a
25 gallon. Fully one third of the plants had costs below 18

1 cents a gallon and 65 percent of the plants fell within the
2 15 to 25 cent range. The information provided in the
3 Cornell study and my experience and professional judgment
4 continues to be reflective of what productive processors
5 can achieve today, gallon processing costs in the 15 to 25
6 cent range.

7 "The plant costs used in the Herbine testimony
8 range from 34 cents to 88 cents a gallon, and are not
9 reflective of anything that could be remotely considered a
10 competitive cost.

11 "If a producer/handler are bottling milk at that
12 type of cost in the marketplace, not only would they be
13 competitively disadvantaged relative to the market, but
14 long term viability of the plant would be questioned. In
15 my professional opinion and experience, a plant that
16 inefficient, if operated by a large, regulated handler
17 would be shut down or folded into a larger, efficient plant
18 that could handle the capacity.

19 "If we except a distinct probability that the
20 cost data upon which Mr. Herbine based his analysis is
21 over-inflated, then the conclusions that are drawn from the
22 data must also be called into question. The determination
23 that the economies of scale occurring at the processing
24 level off at three million pounds is not born out by
25 reality.

1 "As a result, the conclusions drawn in the
2 Herbine analysis suggesting the producer/handlers were
3 selling below cost or selling at a level that regulated
4 handlers could not match is simply incorrect. Using the
5 exact model offered by Mr. Herbine, I input recent
6 warehouse prices observed in the Portland and Seattle
7 market and compared. This analysis is comparable to Mr.
8 Herbine's Exhibit 25, Table E.

9 "As did Mr. Herbine, I backed out a profit for
10 the warehouse store and removed the processing cost
11 identified by Mr. Herbine. This yielded a raw milk cost
12 which was converted to a per hundredweight cost. The per
13 hundredweight cost was compared to the appropriate class
14 one in order uniform price, which was calculated by the
15 market administrator's office and supplied by Mr. Yale's
16 office to me.

17 "These tables which utilize the methodology and
18 cost data of Mr. Herbine reveal that the same alleged
19 servicing of warehouse stores at below the class one price.
20 However, these observations were based in milk supplied by
21 regulated handlers. No producer/handler supplied any of
22 the milk utilized in this price survey. In fact, none of
23 the dairies offering this testimony supplied warehouse
24 stores in Order 124.

25 "The information supplied to me by my clients

1 indicated that this milk is supplied by regulated handlers,
2 not producer/handlers. Since the regulated handler is
3 supplying milk in a manner similar to the Arizona
4 producer/handler, the only conclusion that can be drawn are
5 that either, (1) the warehouse store is selling milk as a
6 loss leader (phon.); or (2) Mr. Herbine's underlying data
7 and methodology is suspect.

8 "What this does demonstrate affirmatively is that
9 the regulated handlers in the Pacific Northwest can
10 effectively compete for the business provided by warehouse
11 stores, despite the presence of three large
12 producer/handlers in the marketplace. As a corollary, it
13 at least implies that the status as a producer/handler in
14 the corresponding class one exemption is not the
15 determinative reason for -- that Sarah Farms may have
16 earned the business on any warehouse stores in Order 131,
17 as suggested by Mr. Herbine.

18 "Conclusion. The scale of processing plants in
19 the fluid milk business continues to grow, and smaller,
20 less efficient plants continue to be sold, shut down or
21 folded into larger, more efficient plants. Captive
22 operations with a limited number of skews (normally just
23 gallons and half gallons with one or two labels) set the
24 cross curve (phon.) from which other processors must
25 compete.

1 "Considering this, in order to be a long-term
2 player in the fluid processing business, plants must run
3 efficiently and process sufficient volumes to achieve a
4 competitive cost. Establishing a maximum monthly
5 processing limit of three million pounds for
6 producer/handlers would simply put them out of business by
7 relegating them to operating plants that cannot capitalize
8 on the economies of scale required to reduce per-unit costs
9 to competitive levels."

10 Q. Thank you. I'd like to follow up with some
11 questions, and we are going to go through the four tables
12 that are attached to your statement.

13 But first I wanted to deal with a couple of
14 preliminary items. You indicated in your opening and your
15 background that you had -- were employed by Dean Foods
16 Company, and that you no longer are employed by that
17 company, correct?

18 A. That is correct.

19 Q. Do you have any non-compete or confidentiality
20 agreements that would prevent you from offering your
21 testimony here today?

22 A. I do not.

23 Q. And is any of the testimony that you have given,
24 any of the information contained in your report based on
25 proprietary information of Dean Foods Company?

1 A. No, it's not. It's based on my experience in the
2 industry as well as the Cornell study.

3 Q. Okay. Before we go through the four tables that
4 you had prepared and attached, let's talk about Carl
5 Herbine's testimony. You stated that you had a chance to
6 review his statement, the tables he attached as well as the
7 transcript of his testimony from Phoenix?

8 A. Yes, that's correct.

9 Q. Did you observe any problems in the raw data that
10 Mr. Herbine used to compile that testimony and those
11 exhibits?

12 A. Well, specifically in looking at the information
13 and focusing directly on the plant costs, as my testimony's
14 provided, yes, I found the plant costs to be
15 extraordinarily high.

16 Q. In your professional opinion, what could've led
17 to costs being inflated?

18 A. You know, there are a lot of things, and as many
19 plants as there are in the industry, you could probably
20 find a plant with, you know, with any cross, but it really
21 depends on a few, I think, key factors. One would be the
22 mix going through the plants. How much is weighted towards
23 gallons versus half gallon through quart, pint, and perhaps
24 even cultured UHG items could skew that substantially. And
25 then what goes into the cost pool that's described as

1 processing costs as well, you know, whether it's a clean
2 cut and doesn't include other things.

3 Often times you see surveys that have a very poor
4 quality of data with packaging costs, ingredients costs,
5 SG&A costs varied in a plant cost. So those are -- and I'm
6 not suggesting that's the case. Those are things that can
7 lead to inaccurate data in inflative costs.

8 Q. Can you elaborate on -- you talked about the cost
9 pool and a clean cut. Can you just describe that? I mean,
10 I'm -- personally I'm not familiar with the -- with clean
11 cut. How would -- what would be a better way to break
12 those costs out, rather than put them in a single cost
13 pool?

14 A. I mean, I'm -- I think most plants probably do
15 it, you know, in somewhat of a unique, you know, unique
16 way, but I mean, typically you could define plant costs
17 from raw receiving through load out of the cooler.

18 Q. Do you recall reading the testimony and seeing
19 how Mr. Herbine selected the plant data that he used in
20 compiling his testimony?

21 A. My recollection that it was just a random
22 selection.

23 Q. Is it possible that it wasn't a random selection,
24 that it maybe was hand selected by Mr. Herbine?

25 A. It certainly could've been, but --

1 Q. Okay.

2 A. -- I don't have knowledge --

3 Q. Okay.

4 A. -- with regard to that.

5 Q. You also reviewed the tables that Mr. Herbine had
6 attached to his written statement.

7 A. Yes.

8 Q. In looking at the methodology that Mr. Herbine
9 used to put together that -- those spreadsheets, was there
10 anything in the methodology he used that you found unique
11 or problematic, something that could've led to skewed
12 results?

13 A. With regard to the -- I don't have his testimony
14 in front of me, but are you talking with regard to the
15 schedules used to draw the conclusions --

16 Q. Yes.

17 A. -- on the pricing? I mean, generally my comments
18 would be, you know, specific to the various categories of
19 cost that were included.

20 Q. Okay. I'm going to provide you with a copy of
21 Exhibit 25 so you have it in front of you, and then we can
22 walk through --

23 A. Okay.

24 Q. -- those spreadsheets that you had prepared.

25 A. Thanks.

1 Q. Now, you do have -- I have handed you Mr.
2 Herbine's exhibits, which I believe have been marked and
3 admitted as Exhibit No. 25. If you could turn to Exhibit
4 E, which is headed, "Comparative Analysis of Return to
5 Producer/Handlers and Regulated Distributing Plants
6 Supplying a Warehouse Store." Do you have that --

7 A. Yes, I do.

8 Q. -- in front of you?

9 A. Yes.

10 Q. Okay. And if you could look side by side with
11 that, the first spreadsheet that was attached to your
12 written statement, which --

13 A. Yes.

14 Q. -- has a lower case "A" in the bottom?

15 A. Okay.

16 Q. Are these two spreadsheets, analyses similar in
17 the calculations and methodology with which they were
18 prepared?

19 A. Yes, they are.

20 Q. So assuming whatever false or positive qualities
21 which may have been in Mr. Herbine's testimony, those were
22 accepted by you and utilized the same methodology in
23 preparing your spreadsheets?

24 A. That is correct, that both the calculations and
25 the categories titled, "Dairy supplier costs," were the

1 same.

2 Q. Okay. And as I understand what Mr. Herbine did
3 and what you did in preparing your spreadsheets was to take
4 the shelf price of a two gallon, two percent package of
5 milk sold at a warehouse store in various markets at
6 various times, and then analyzed that as compared to the
7 class one cost and the uniform price in that market order?

8 A. Yes, that is correct.

9 Q. If we want to just look at your spreadsheet A,
10 can you read me the first -- the top line, the very top
11 line on there?

12 A. "September 2000, 12 million pound plant,
13 Seattle."

14 Q. And that would I assume would indicate that these
15 are based on September 2000 previous --

16 A. Yes, that is correct. That's based upon
17 September 2000 retail pricing.

18 Q. In the Seattle market?

19 A. In the Seattle market.

20 Q. And does the 12 million pound plant indication
21 indicate that you used the costs that Mr. Herbine indicated
22 were associated with a 12 million pound plant?

23 A. Yes, I did.

24 Q. And I believe that is Exhibit I in Mr. Herbine's
25 statement. At the top it's labeled, "Warehouse Store by

1 Pool Distributing Plant 'D'." And those were the costs
2 that went into the area where it says "Dairy supplier
3 costs" on your spreadsheet?

4 A. That's -- Plant D is the costs that are included
5 in my schedule A.

6 Q. Okay. And maybe my notes are wrong. I wrote
7 down at the bottom, --

8 A. Yes.

9 Q. -- I think we had hand-labeled these --

10 A. It's -- in the Herbine testimony, if you go to
11 the D in the earlier schedules, it is for a monthly volume
12 of class one poundage, 12 million pounds.

13 Q. Okay. I think we're talking about the same one
14 then.

15 A. Yeah, so all the costs on my schedule reflect the
16 same costs that are on Carl Herbine's D schedule.

17 Q. Okay. The next line on your Exhibit A says,
18 "Average Retail Out-of-Store Prices," and it lists \$4.29.

19 A. Yes.

20 Q. How was that figure obtained?

21 A. That figure was given to me by my clients as
22 representing the retail price during September out of a
23 club store for two percent milk, two pack.

24 Q. And then how were the numbers on the next two
25 lines calculated?

1 A. The store mark up is simply a cost based mark up
2 from the price paid by the dairy supplier -- excuse me,
3 paid to the dairy supplier by the retailer.

4 Q. And in the following line, which you've labeled
5 "Price Paid to Dairy Supplier," is that a simple
6 subtraction of the mark up from --

7 A. Yes, it is.

8 Q. -- the retail price?

9 A. Yes, it is. It's simply retail less mark up,
10 which represents the processor's sale price.

11 Q. Okay. And then the dairy supplier costs, were
12 those then subtracted from the result on the line, "Price
13 paid to dairy supplier?"

14 A. That's correct.

15 Q. And then that resulted in the value of raw milk,
16 which you've calculated?

17 A. Yes, exactly. Deducting these costs, which are
18 the costs that -- in the Herbine study for this particular
19 product, gets you down to a value of raw milk on a two
20 gallon basis.

21 Q. How did you calculate a one gallon value?

22 A. Divided by two.

23 Q. That's why you're a CPA, isn't it?

24 A. That's right.

25 Q. How did you then calculate the conversion to

1 hundredweight?

2 A. The conversion to hundredweight is multiplying by
3 11. -- well, it's 100 divided by 8.6. I think that's 11.2,
4 isn't it?

5 Q. 11.6?

6 A. 11.6? Okay. I'll take your word for it.

7 Q. Okay. Can you check that? Do you have a
8 calculator?

9 A. No, I don't.

10 Q. Okay.

11 A. Thank you, sir. An accountant without a
12 calculate. Sorry about that.

13 Q. That's okay.

14 A. 11.6.

15 Q. Okay. I believe you said in your testimony that
16 the following line, class one cost was obtained from market
17 administrator's data?

18 A. That's correct.

19 Q. As was the uniform price?

20 A. Yes, that's correct. From the MA website.

21 Q. What do the following two lines represent,
22 "Compare to class one" and "Compare to uniform price?"

23 A. What the compare to class one is, is essentially
24 just a comparison of the hundredweight conversion to the
25 class one price. So the 15.81 divided by the 12.83, and in

1 the eight percent column, what you see here is a shortfall
2 of \$2.97 a hundredweight, which is huge, which is almost 30
3 cents a gallon. And then going over to the following
4 column, same math, obviously less mark up assumed. So
5 lower delta -- lower change, but again, a huge difference
6 of \$1.76.

7 So it's really -- you know, from this that the
8 conclusion was drawn that the understanding that this is a
9 regulated handler, that, you know, there's -- it's
10 extremely unlikely that they would be selling at these kind
11 of losses.

12 Q. And that's where you came to the conclusion that
13 either they were incurring those types of losses, or that
14 Mr. Herbine's analysis didn't reflect the situation in the
15 marketplace?

16 A. Yes, that's correct.

17 Q. And then if you could turn on your exhibit to
18 what is labeled "B" in the bottom.

19 A. Okay.

20 Q. And based on what you had described in the
21 previous analysis of chart A, this represents the October
22 2002 market in Seattle?

23 A. Yes, that's correct.

24 Q. And when you look down at the bottom line, what
25 does that show?

1 A. Comparable results in terms of a large shortfall
2 between the computed hundredweight cost and the class one
3 cost.

4 Q. And if you then look at the following page,
5 Exhibit C.

6 A. And again, the trend just continues, and the only
7 difference in all of these would be the retail price, you
8 know, that we're using and obviously, you know, month to
9 month the class and the uniform price changes. But again,
10 both in Portland for the month of September and the month
11 of October, the shortfall, the regulated handler relative
12 to the class one price was enormous.

13 MR. MILTNER: Your Honor, could we have ten
14 minutes before --

15 THE COURT: Ten minutes.

16 MR. UNIDENTIFIED 1: We need to verify something,
17 Your Honor. If I could have about five minutes
18 (indiscernible) just something I want to verify before we
19 (indiscernible)

20 THE COURT: Okay. Let's come back at 4:00
21 o'clock. It's six minutes before 4:00.
22 (Pause)

23 THE COURT: What?

24 MR. UNIDENTIFIED 2: I think --

25 MR. UNIDENTIFIED 3: On direct examination of the

1 witness?

2 THE COURT: He asked, you know, I mean.

3 MR. UNIDENTIFIED 3: The time to consult with
4 counsel about his testimony?

5 MR. UNIDENTIFIED 1: No, we're not going to talk
6 to counsel. I want to talk to co-counsel. We have a
7 question that we want to resolve before (indiscernible) and
8 it'll save a tremendous amount of time if we could solve
9 it.

10 THE COURT: I'm going to allow it. You know,
11 people ask people -- a few minutes. I'd give them a few
12 minutes. I'm trying to be a reasonable judge. So we'll
13 take about five minutes.

14 (Off the record at 3:55 p.m. and reconvened at 4:00 p.m.)

15 THE COURT: We're now on the record.

16 MR. ENGLISH: Thank you. Your Honor, Charles
17 English for Dean Foods and Shamrock Foods.

18 The representation was made before we went off
19 the record that there would only be a consultation between
20 co-counsel. On that ground, the counsel on this side of
21 the room, proponents, did not further object.

22 After the consultation of co-counsel, there was
23 at least a brief conversation. I don't know what was said,
24 maybe it was just hello, but there was a consultation with
25 the witness, and obviously we're going to have to ask about

1 that. But moreover that, breached what I thought was the
2 agreement of this break.

3 THE COURT: You want to say something to that,
4 Mr. Yale?

5 MR. YALE: Yes, I do, Your Honor. First of all,
6 I want to apologize. We, in processing this paperwork, we
7 had submitted a table, that the wrong table got exhibit,
8 and then it didn't get caught until in the midst of this
9 direct, I saw that. And rather than take up a lot of time
10 with all these people trying to catch what was clearly an
11 error, it was our objective to correct that at the earliest
12 possible moment so that the testimony and the cross-
13 examination can deal with things that are more important.
14 Okay.

15 Now, did I talk to the witness? The answer is
16 yes. I told him that there was an error in the class one
17 price that we had on that table. I didn't tell him what it
18 was, and that we were going to present that to him and ask
19 him if that changes his results or what he has to do with
20 by giving him that correct amount (phon.).

21 MR. UNIDENTIFIED: Well, whose table is it, Your
22 Honor?

23 THE COURT: Okay. Just -- that's what we'll find
24 out. You'll have a chance to -- if he's -- you'll have a
25 chance to examine the witness on whatever Mr. Yale or Mr.

1 Miltner asks.

2 MR. YALE: You know, Your Honor, it's one of
3 those things that unfortunately, sometimes in the process
4 of this, mistakes are made, and it's an exciting moment in
5 the life of an attorney to catch a witness in a mistake,
6 and you can eat them alive.

7 And this is a situation where, unfortunately, I
8 think I've taken some meals away from a few people, but all
9 we're trying to do is to make sure that there's a correct
10 thing. And we had submitted in our office, and it was our
11 error, that we had prepared one table, corrected it, but
12 the wrong table persisted throughout.

13 And it is simple math, it is common math known.
14 These guys caught it in a matter of two or three minutes.
15 I'm sure, maybe 60 seconds with the brilliance of some of
16 the counsel, and with the numbers that are available
17 commonly from the market administrator, it's not rocket
18 science, and we just, before we got any further, wanted to
19 get that corrected.

20 If they want to deal with that in terms of
21 credibility and all that, have at it.

22 THE COURT: Well, they can do whatever they want
23 -- I mean, they can ask questions on cross-examination.

24 MR. YALE: Right. So that's all we're doing.

25 THE COURT: Okay. Are you going to resume

1 direct, or is Mr. --

2 MR. YALE: No, he is. I just wanted to take care
3 of their objection. Go ahead.

4 BY MR. MILTNER:

5 Q. Mr. Morrison, I apologize to you for that delay.

6 A. That's quite all right.

7 Q. Earlier in your testimony you stated that the
8 class one and uniform prices that you included in your
9 analysis were provided to you, based on market
10 administrator's data from our office; is that correct?

11 A. That's correct.

12 Q. If it were -- if your Table A were changed, such
13 that the class one cost, which is currently listed at
14 \$15.81, were changed to \$14.62, how would that affect the
15 number presented on the line labeled, "Compare to class
16 one?"

17 A. Going down \$1.19 in terms of the class one, so
18 you'd go down a \$1.19 against the 2.97 at the bottom, which
19 would put you at 1.88, if my math is correct.

20 Q. How would that change the number in the following
21 column?

22 A. Would change it considerably. The new number
23 would be 31 cents.

24 Q. Is that a negative 31 cents?

25 A. Yes.

1 Q. Is that a negative \$1.88?

2 A. Yes. Yes, that's correct.

3 Q. And similarly on Table B, if the number that we
4 had provided to you at \$16.37 were changed to \$14.52, how
5 would that change the numbers in the row "Compare to class
6 one?" The change again is to \$14.52.

7 A. Go down -- excuse me, would go down \$1.85, so the
8 3.53 minus 1.85 would change it to a negative \$1.78. And
9 then the 2.32 minus 1.85 would change it to a negative 47.

10 Q. If on Table C the class one costs were again
11 changed from \$15.81 to \$14.62, how would that change your
12 line labeled, "Compare to class one?"

13 A. You'd go down, excuse me, \$1.19 again. So that
14 would be 2.97 minus 1.19, so you'd be at a negative 1.78.
15 And then 1.76 minus 1.19 would be a negative 57.

16 Q. And on Table D, if "Compare to class one" were
17 changed from \$16.37 to \$14.52, how would that affect your
18 "Compare to class one?"

19 A. Again, down \$1.85. So you'd do 2.72 minus 1.85,
20 so you're down negative 87, and then 1.46 minus 1.85, and
21 that would be a positive 39.

22 Q. Given the changes made in these four tables that
23 we just went through following the recess, does that change
24 any of your observations about the plant cost data supplied
25 by Mr. Herbine?

1 A. Clearly there material reductions in terms of the
2 difference on the computed hundredweight cost to the class
3 one, that are probably better looked at, you know, on a
4 schedule by schedule basis. So, for instance, on A, at a
5 \$1.88 difference, by any measure that's a significant
6 variation on a, you know, per gallon basis. In that case,
7 you'd be maybe at 18 cents or something along that nature,
8 which is a huge loss. Would put the -- at the eight
9 percent margin, would put it somewhat close to a break
10 even.

11 And then if you move on to Schedule B, where I -- and
12 I think I wrote all these down there correctly. So please
13 correct me if I'm quoting bad data again. But with regard
14 to Schedule B, on the -- be negative 1.78 and a negative 47
15 as well. So again, you're in a loss position significantly
16 at the 14 percent mark up, much less significantly at the
17 eight percent mark up.

18 You know, \$1.78 order magnitude, if you take
19 \$1.78 and divide it by the 11.6, I mean, you know, you're
20 at a gallon loss of 15 cents, which is significant against,
21 you know, a price at little over \$2 retail; 47 get you more
22 into a marginally unprofitable scenario.

23 And I think those conclusions pretty much follow
24 throughout the schedules.

25 Q. Is it still your opinion that a plant processing

1 three million pounds of raw milk per month --

2 A. Yeah, this was simply mathematical exercise,
3 which drew some conclusions which has a lot of assumptions.
4 One being the margin which frankly unaware of exactly what
5 the retail margin is, but the costs were enormous enough on
6 the dairy supplier cost side, and just far beyond what my
7 experience tells me would be in the realm of reason for an
8 efficient processor. So yes, as my testimony stated very
9 clearly, I strongly believe that 15 to 25 cents a gallon is
10 where an efficient processor would be from a processing
11 standpoint, running efficient plant with high volumes and
12 high plant utilization. So looking at 40 cents a gallon is
13 far beyond that.

14 Q. And do you believe that a three million pound per
15 month plant could achieve those goals?

16 A. It's impossible. The -- let me back that off a
17 little bit, but when you look at the productive capacity of
18 assets that's available, to suggest that you could run a
19 plant, you know, a matter of hours daily and be productive,
20 I've never seen it done. I find it hard to believe that it
21 can be done.

22 Q. And that conclusion is independent of whatever
23 these sheets say? Either --

24 A. Oh, of course.

25 Q. -- correct form or in the form that we eventually

1 --

2 A. Of course.

3 Q. -- went through?

4 A. Of course.

5 Q. Again, I apologize for anything that -- any
6 chaney (phon.) errors that were made in the data we
7 supplied you and also for the delay in your testimony.

8 And I don't think we have anything else to
9 question you about at this time.

10 Thank you, Your Honor.

11 THE COURT: Two little points. One is, are you
12 going -- you want this in evidence, Exhibit 40?

13 MR. MILTNER: Yeah, we would move to have that --

14 THE COURT: And secondly, since you've --

15 MR. UNIDENTIFIED: We're going to move to --

16 THE COURT: I was going to say, do you want to --
17 I don't know what -- how much time it will take you to do
18 that, but I mean, you going to -- you want to submit
19 corrected tables?

20 MR. UNIDENTIFIED: Yes, we do.

21 THE COURT: I'm going to leave the original ones
22 in because they've been referred to in the record, and I'll
23 -- what I'll do is I'll leave Exhibit -- the Exhibit 40(a),
24 I'll leave that number open, Exhibit 40(a), and you can
25 tomorrow, submit corrected tables, I assume.

1 MR. UNIDENTIFIED: And Your Honor, at the same
2 time we'd like -- and I think it kind of carries over what
3 was already done, but take official notice of the
4 announcement (indiscernible) final for September 2003 and
5 October 2003 for the Pacific Northwest, Western, and
6 Arizona/Las Vegas orders as announced by the United States
7 Department of Agriculture.

8 MR. UNIDENTIFIED 1: Better yet, let's make them
9 exhibits.

10 THE COURT: Okay.

11 MR. UNIDENTIFIED 1: The next two numbers.

12 THE COURT: Okay. So that's -- that'll be
13 Exhibit -- Exhibits 41 and 42. Do we have -- we don't have
14 enough copies, I guess, right now for that, right?

15 We'll get that straightened out later on.

16 Okay. So --

17 MR. UNIDENTIFIED: 41 is September.

18 THE COURT: 41 is September 2003, and

19 MR. UNIDENTIFIED: 42 is October.

20 THE COURT: 42 is October.

21 (Exhibit Nos. 41 and 42 were marked.)

22 THE COURT: Okay. I'll just trust that we'll get
23 the copies straightened out some time later on today or
24 tomorrow morning or whatever. We'll get the copies made,
25 but okay. Those two documents, without objection, are

1 admitted into evidence as well.

2 (Exhibit Nos. 41 and 42 were received.)

3 THE COURT: Okay. You all done with the direct?
4 Are you ready to turn the witness over for cross-
5 examination?

6 MR. MILTNER: We are, Your Honor.

7 THE COURT: Okay. Does anyone have any questions
8 of the witness?

9 Go ahead, Mr. Beshore.

10 EXAMINATION

11 BY MR. BESHORE:

12 Q. Marvin Beshore for Dairy Farmers of America.

13 Mr. Morrison, I'd like to show you what has now
14 been marked as Exhibits 41 and 42, the official price
15 announcements of announcement of minimum class and
16 components prices for September and October in these
17 markets.

18 Now, let's turn to September first. The
19 September, Exhibit 41. Okay. And I'd like you to turn to
20 your Schedule A and the Exhibit 40.

21 A. Okay.

22 Q. Okay. Now, the number that was on Schedule A as
23 distributed and testified before correction, for the class
24 one cost in Federal Order 124, can you derive that anywhere
25 on Exhibit 41?

1 A. Your asking me if -- so I understand your
2 question, the 15.81?

3 Q. Yeah, that you used in Exhibit A or page A, Chart
4 A --

5 A. Right.

6 Q. -- of Exhibit 40.

7 A. Yes, it's -- well, it's right on the face of the
8 document.

9 Q. Okay. Is that where you got it?

10 A. I got the number from the Yale Law Firm.

11 Q. Okay.

12 A. We were -- I mean, I'll be honest with you
13 because we made an error. My focus has been on the plant
14 cost and on the processing cost, and we had -- we were kind
15 of hustling to do these schedules, and so this amount was
16 given to me, and I honestly presumed it to be correct.

17 Q. Okay.

18 A. I made an error.

19 Q. And you presented this as your testimony and your
20 calculations, correct?

21 A. Yes, I did.

22 Q. Okay. Now, the 15.81, can you read from Exhibit
23 41 and indicate how that's derived?

24 A. Excuse me, I --

25 Q. The 15.81 number --

1 A. Have -- no, I'm not a MA so I'm not sure of your
2 question --

3 Q. Well, right on the face of the document, --

4 A. Yeah.

5 Q. -- doesn't it show that it has two components?

6 A. Yeah, it shows a -- yes, it does.

7 Q. Okay. And those components, would you read them,
8 please?

9 A. Skim and butterfat? Excuse me?

10 Q. No, the -- doesn't it show as -- there's a 15.61
11 number and a 20 cent number?

12 A. No, that's a subtotal, sir. There's 14.21. It's
13 the skim price, and 1.31 is the butterfat.

14 Q. Okay. And that -- there's also a 20 cent number
15 on there, is there not, per hundredweight in the 15.81?

16 A. Yeah, yeah, the processor assessment. Yeah, but
17 the big pieces of this are the skim and the butterfat --

18 Q. Well, let's talk about -- but 15.81 includes the
19 20 cents, does it not?

20 A. Of course.

21 Q. Processor assess --

22 A. Yes, it does.

23 Q. Okay. Now, look at Table A -- Schedule A, your
24 Schedule A in 40. Okay. Did you include that 20 percent
25 elsewhere in that calculation as well?

1 A. Well, the 3.4?

2 Q. Yes.

3 A. Yes.

4 Q. Okay. And what's the 3.4?

5 A. The 3.4 is probably the 20 cents divided by the
6 11.6.

7 Q. Probably? It's your table. What is it?

8 A. That's -- that should be the milk assessment.

9 These -- I'll tell you what happened on this. The --

10 Q. Well, tell me whether the 20 cent has not -- you
11 haven't accounted for it twice?

12 A. Relative to 15.81, yes, it does appear that the
13 20 cents, which would amount to 2 mils a gallon was counted
14 twice.

15 Q. Okay. Now, the new number that you've replaced
16 15.81 with is -- oh, I'm sorry, that Mr. Miltner instructed
17 you to use for 15.81 is what?

18 A. Was 14.62.

19 Q. Okay. Now, would you calculate, Mr. Morrison,
20 explain to us how you derived the 14.62 from the market
21 administrator's price announcement --

22 A. Well, it was --

23 Q. -- Exhibit 41 -- no, no, I asked you a question.
24 Would you calculate for us, explain to us the basis for the
25 14.62 with respect to Exhibit 41?

1 A. The 14.62 and -- the 15.81 is the 3.5, so the
2 calculation on the 14.62 would adjust for butterfat at two
3 percent, is my understanding.

4 Q. Okay. How --

5 A. I'm not a -- in fact, if you look at my
6 testimony, I'm not a milk math expert.

7 Q. Are you a dairy class -- dairy plant cost
8 accounting expert, Mr. Morrison?

9 A. I believe I am, yes.

10 Q. Okay. And are you able to calculate the cost of
11 butterfat and skim milk, --

12 A. I don't --

13 Q. -- and the ingredients in the milk plant. Let me
14 answer my -- finish my question first, please.

15 A. Please do. I'm sorry.

16 Q. Yes. Are you able to adjust 3.5 milk prices to
17 other butterfat percentages?

18 A. Yes, I think I can probably --

19 Q. You are?

20 A. -- do that.

21 Q. Okay. I would like you -- do you have the
22 information on Exhibit 41 that shows you what the value of
23 class one butterfat is per pound?

24 A. I don't want to do the dairy math. I -- my
25 answer is no.

1 Q. You're not prepared to do the dairy math --

2 A. I don't -- I would like it to be understood that
3 I understand a mistake was made here, and I was hasty in
4 attaching this, but I'm not going to let you destroy my
5 credibility by doing -- having to do butterfat calculations
6 in front of this crowd.

7 Q. Okay. Would you --

8 A. I'm not going to do that.

9 Q. Thank you. You're not able to do that then?

10 A. I did not say I'm not able to do that. I said
11 I'm not going to do that.

12 Q. You refuse to do that, to show your ability to do
13 that? Is that --

14 A. Yes, I do.

15 Q. Okay. Now, with that statement made, are you
16 prepared under oath to state that what \$14.62 represents,
17 the new number that you're adopting as your testimony for
18 analysis on Exhibit -- Page A, Chart A of Exhibit 40?

19 A. I have not calculated that number.

20 Q. What does it represent?

21 A. My understanding it was -- would represent the
22 hundredweight for two percent milk.

23 Q. And if it does not, what would --

24 A. Then these schedules would be inaccurate.

25 Q. And I assume --

1 A. I would like to say -- if I made an error once, I
2 don't want to repeat it here. So in terms of trying to do
3 this again, it requires more --

4 Q. And if the schedule is inaccurate, your
5 conclusions drawn from it would also be inaccurate, would
6 they not, Mr. Morrison?

7 A. My conclusion with regard to plant costs and
8 volumes has not changed. I feel strongly about that. If
9 indeed this number changed in terms of the two percent
10 hundredweight calculation as we're comparing to the derived
11 amount, absolutely. That would be a change in the
12 conclusion. In other words, if the 1.88 changed, yes.

13 Q. Okay. And your conclusions then would be
14 inaccurate as presently stated; isn't that correct?

15 A. If the number changed.

16 Q. Now, if -- did you read Mr. Herbine's testimony?

17 A. Yes, I did.

18 Q. Okay. Did you look at his -- do you have his
19 exhibit available to you, 25?

20 A. I have his testimony. I don't have -- I don't
21 believe I have it marked as an exhibit, but if you could
22 tell me specifically what schedule you're looking at, I
23 could probably find it here.

24 Q. Well, how about Schedule E.

25 A. Yes.

1 Q. Okay. Now, Schedule E, you didn't use that in
2 your charts A, B, C, or D, did you?

3 A. No, I did not.

4 Q. Did you read Mr. Herbine's testimony about what
5 schedule Exhibit E was, Schedule E on his Exhibit 25?

6 A. I read Mr. Herbine's testimony, yes, but I
7 focused more on looking at the aggregate cost data as
8 opposed to these calculations again, because I have been,
9 you know, hired to speak with regard to volume and plant
10 costs.

11 Q. Okay.

12 A. So my focus, to answer your question, was really
13 looking at the costs at the specific volume levels that
14 Carl testified to.

15 Q. Okay. Well, let's look at Exhibit E, and the
16 title of that is "Comparative Analysis of Return to
17 Producer/Handlers at Regulated Distributing Plants
18 Supplying a Warehouse Store," correct?

19 A. That's correct.

20 Q. And did you read his testimony that the cost that
21 he used were very specific to the costs for supplying
22 warehouse stores?

23 A. Yes, I did.

24 Q. Okay. That's what Exhibit E is. It's not a
25 fully loaded cost for any plant at any volume. It's the

1 cost supply a warehouse store; isn't that correct?

2 A. That's what the title says, yes.

3 Q. Okay. Well, isn't that what he testified to?

4 A. I didn't hear him testify. I read his testimony
5 and read his reports, so --

6 Q. And isn't that what you read?

7 A. What I read was a summary of costs in volume that
8 range from, on a per gallon basis, 33 cents to upwards of
9 80.

10 Q. Okay. Well, let's assume with me for a moment,
11 that in the testimony of this proceeding, which is been
12 transcribed and filed of record. Mr. Herbine described in
13 detail that the cost on Exhibit E are customer specific
14 costs relating to servicing a warehouse store.

15 A. Uh-huh.

16 Q. Okay. Now, first of all, those costs are quite
17 different than any you've used in A, B, C, and D on your
18 Exhibit 40, are they not?

19 A. I'll have to compare them; 43 for plant on two
20 gallon.

21 Q. Correct. Versus 79 on yours.

22 A. And then the packaging, obviously, is much
23 higher. Yeah, there's some variations between the two
24 schedules.

25 Q. So the total cost that he showed for supplying a

1 warehouse store was \$1.1372 -- 1.1372, correct?

2 A. That's correct.

3 Q. And you were using 1.552, quite a little bit of
4 difference, isn't there, Mr. Morrison?

5 A. That would be a significant difference, yes.

6 Q. And if you used the correct set of costs of Mr.
7 Herbine's for supplying a warehouse store at \$1.1372 and
8 put them on your Exhibits A through D, the bottom lines
9 would be a bit different --

10 A. I would need to understand, yeah, the difference
11 between those two, because honestly when I read the
12 testimony, it didn't follow that the 43 cents was --
13 particularly packaging and the other things changing, so it
14 didn't follow that that was the cost he was suggesting for
15 a gallon -- excuse me, for two gallons.

16 Q. It did not?

17 A. No, it did not.

18 Q. How much time did you spend with his testimony,
19 Mr. Morrison?

20 A. I read through the testimony.

21 Q. Once?

22 A. No, multiple times.

23 Q. Okay.

24 A. So --

25 Q. Now, assume with me that when you -- well, maybe

1 you can -- maybe this is the kind of math that you can do
2 and are prepared to do on examination. If you substitute a
3 \$1.1372 into Chart A on Exhibit 40 for the \$1.552 total
4 cost, can you tell us how that changes the bottom line?

5 A. It would change the -- yeah, you have 40 cents --
6 a 40 cent reduction in total cost.

7 Q. 40 cents per --

8 A. Per two gallon.

9 Q. Per two gallon, --

10 A. Yeah.

11 Q. -- 20 cents per gallon.

12 A. Right.

13 Q. How much per hundredweight?

14 A. Divide by 11.6.

15 Q. Divided by?

16 A. Or, excuse me, multiplied. Yeah, so it would be
17 a material change.

18 Q. And how much?

19 A. It would put it -- it would put this schedule --
20 if -- it would put it into a profitable position.

21 Q. Ah-ha. Now the sales in Seattle and Portland are
22 profitable, correct?

23 A. If you had --

24 Q. The regulated handlers' sales --

25 A. If you had a reduction of 40 cents on supply

1 costs or 20 cents a gallon, and you're comparing to
2 hundredweight. So you'd be 20 times the 11.6. Excuse me.

3 (Pause)

4 THE WITNESS: Yes, it would change the schedules
5 considerably.

6 BY MR. BESHORE:

7 Q. And --

8 A. I mean, going from an 80 cent plant cost to a 43
9 cent plant cost, obviously, would be significant.

10 Q. And it would now make the sales profitable,
11 correct?

12 A. Yes.

13 Q. Okay. And that would change your analysis and
14 your conclusions, would it not?

15 A. It would materially change -- the 43 cents or
16 21.5 on a plant cost basis would be in the range of cost
17 that I testified to as being fair costs.

18 Q. Mr. Herbine's costs are fair costs, Mr. Morrison?
19 Is that what you just said?

20 A. I would say that a 20 cent plant processing cost
21 would put it in the range of a fair processing cost.

22 MR. BESHORE: I have no further questions at this
23 time, Your Honor.

24 THE COURT: Thank you, Mr. Beshore.

25 Any more questions from the proponents' side?

1 MR. ENGLISH: Based upon the examination --

2 THE COURT: I just need you to --

3 MR. ENGLISH: I'm sorry. Charles English for
4 Dean Foods and Shamrock Foods.

5 THE COURT: Thank you.

6 EXAMINATION

7 BY MR. ENGLISH:

8 Q. 41.38 cents on Table A, the total of your plant
9 and packaging number's higher than Mr. Herbine's numbers;
10 is that correct?

11 A. I'm sorry, could you say that again, please?

12 Q. Can you tell me how much higher your plant and
13 packaging costs are on your Table A than actually appear on
14 Exhibit E of what is Exhibit 25?

15 A. Our schedule has 39.6, and the Herbine schedule
16 is 34.8.

17 Q. And that is 4.8 cents inflated on Table A over
18 Exhibit A for packaging costs?

19 A. Yeah, that's correct.

20 Q. And for plant costs, how inflated is your Table A
21 over Exhibit E?

22 A. Essentially the 80 cents minus the 43 or 37 cents
23 on a two gallon basis.

24 Q. So we're looking at something over 41 cent
25 difference, correct, on a two gallon basis?

1 A. Yes, combining the packaging in the plant.

2 Q. And the percentage of your inflation -- inflated
3 numbers of Table A over Exhibit E of 41 cents over 1.13 is
4 what percent?

5 A. I'm sorry, say that again, please.

6 Q. What percentage of \$1.13 is the 41 cent that you
7 have inflated on Table A over Exhibit E, the numbers?

8 A. Please, one more time.

9 Q. What is the percentage of \$1.13 at your inflated
10 number, 41 cents, constitutes?

11 A. Whatever that percentage would be, which is
12 probably 35 percent.

13 Q. And now you agree that the cost listed on Mr.
14 Herbine's Exhibit E are a fair representation of actual
15 costs, correct?

16 A. No, I didn't say that. I would --

17 Q. You said that to --

18 A. I would say with regard to plant costs on this
19 schedule, which would -- which was a schedule that
20 obviously we didn't use. At 43 cents for a two gallon,
21 which would be 21.5 cents on a gallon basis, with regard to
22 plant processing costs, I would view that as fair. With --
23 I'm not --

24 Q. You reached --

25 A. I'm not commenting or testifying with regard to

1 package and distribution --

2 Q. All right. So you're just doing plant costs and
3 you now agree that's fair?

4 A. Say that again. I'm sorry, you said that
5 quickly.

6 Q. You're only testifying as to plant costs, you're
7 saying?

8 A. Yes.

9 Q. And you're now --

10 A. Plant costs and plant volumes relative to achieve
11 certain costs.

12 Q. So can we now agree -- let me strike that.

13 You did not actually run this analysis for Order
14 131, did you?

15 A. What do you mean by run this analysis?

16 Q. The analysis that is contained in Tables A, B, C,
17 and D was run for Seattle and Portland, correct?

18 A. That's correct.

19 Q. And that's Order 124, correct?

20 A. Correct.

21 Q. And you didn't run any analysis for the Arizona
22 market, correct?

23 A. That is correct.

24 Q. You drew a conclusion that because -- for
25 adjustment for your inflated numbers, the Portland/Seattle

1 numbers were somehow inflated, that the Arizona numbers
2 were inflated, correct?

3 A. That is correct.

4 Q. Your testimony discussed at some length the
5 difference between cost between large plants and smaller
6 plants, correct?

7 A. Yes, it does.

8 Q. Your testimony does not, however, show the
9 difference in cost between a fully regulated plant and a
10 producer/handler plant of the same size, does it?

11 A. The difference in cost between -- what do you
12 mean by the difference in cost between those two? I'm not
13 sure the basis of your question.

14 Q. Well, does your testimony show the difference in
15 cost for a fully regulated, 7A distributing plant and a
16 producer/handler plant of the same size?

17 A. No. What my testimony really is, is regard to
18 the -- it -- I would say this, that from a processing
19 standpoint, and I'm not here to testify on the farming side
20 of the PD equation, but from a processing standpoint, I
21 would view the two as the same. In other words, if you run
22 X volume under a certain productive capacity in a certain
23 plant set up, whether you're a PD processor or regulated
24 handler, I wouldn't view the cost to -- the cost that you
25 would achieve to be different.

1 Q. But if the cost of the raw product are different,
2 that could be very significant to a handler, could it not?

3 A. I'm not here to talk about the difference in raw
4 costs between the two.

5 Q. And you made no such comparison in your
6 testimony, correct?

7 A. With regard to?

8 Q. With regard to --

9 A. Raw costs?

10 Q. Full cost for an operation, including the cost of
11 raw milk.

12 A. That is correct. That's correct. I focused just
13 specifically with regard -- I testified and wrote my report
14 specifically with regard to the plant processing side of
15 the equation.

16 Q. Are there fully regulated plants on either Orders
17 124 or 131 that are smaller than the plants that are your
18 clients?

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

20 Q. Are there plants -- fully regulated plants on
21 Order 124 that are in the range of three million pounds?

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

23 Q. On page two of your testimony, you refer to the
24 advantages enjoyed by captive milk plants that are
25 integrated with grocery stores. Do you recall that

1 testimony?

2 A. Yes, I do.

3 Q. Isn't it possible that a similar advantage is
4 available to a producer/handler who integrates milk
5 production with fluid milk processing?

6 A. I don't understand why that would be.

7 MR. BESHORE: Then I have no further questions,
8 sir.

9 EXAMINATION

10 BY MR. MARSHALL:

11 Q. Mr. Morrison, my name is Doug Marshall. I'm with
12 Northwest Dairy Association here in Seattle. We've never
13 met. Welcome to Seattle.

14 A. Thank you.

15 Q. You ever been to Seattle before?

16 A. Long time ago.

17 Q. Little bit different than Illinois, isn't it?

18 A. Yes, it is. Windy and rainy, though.

19 Q. When were you retained by your clients to
20 represent them in this -- in connection with this matter?

21 A. In terms of the date?

22 Q. Or how long -- how many days ago?

23 A. I'm -- I don't know the exact date, but I would
24 say three weeks ago.

25 Q. Over the course of the last three weeks, have you

1 studied the Pacific Northwest federal order market in any
2 respect?

3 A. Other than reading the testimony that I've
4 testified to, no.

5 Q. There's a table -- excuse me, there's an exhibit
6 introduced by the market administrator that describes a lot
7 of things about the order. Have you looked at that? About
8 this order area, excuse me.

9 THE COURT: Can you just identify that exhibit by
10 number, just to -- oh, sorry.

11 MR. MARSHALL: It's either 5 or 6 or 7. 7 is the
12 Pacific Northwest.

13 MR. UNIDENTIFIED: The gray one, yeah.

14 BY MR. MARSHALL:

15 Q. I refer to Exhibit 5, but it looks like this.
16 Have you looked at this exhibit in preparation for your
17 testimony --

18 A. Could you show it to me, please? I'm not sure
19 what you're talking about exactly.

20 Q. Happy to.

21 A. No, I have not.

22 Q. Let's talk a little bit about your work with Dean
23 Foods. By the way, you have an MBA from Northwestern.
24 That's a pretty good business school, isn't it? One of the
25 top ones in the country? You had a career position that

1 indicates here with Dean Foods in strategic planning. So
2 you have some background in business strategies; is that
3 right?

4 A. That's correct.

5 Q. Including academics --

6 A. That's correct. I wouldn't characterize it as
7 responsible, completely for strategic planning, but as far
8 as the management team, everyone participated in the
9 strategic plan, which I did as well.

10 Q. Page five of your testimony, middle of the page,
11 you conclude a paragraph by suggesting that only two
12 conclusions can be drawn from your preceding testimony.
13 One is that the warehouse store might be using milk as a
14 loss leader (phon.). Second is that Mr. Herbine's
15 methodology might be suspect.

16 Is there anything about business strategies that
17 would suggest that a warehouse store might sell milk as a
18 loss leader, irrational on your view?

19 A. Well, certainly retailers will have strategies to
20 get more people coming through the front door. So that's
21 the whole concept of a loss leader.

22 Q. How is a processing plant any different than
23 that?

24 A. With regard to establishing sale price?

25 Q. Yes.

1 A. I think it would be more challenging for a
2 processing plant.

3 Q. Why so?

4 A. Well, the mix you have in a processing plant is
5 just different than a retailer.

6 Q. And come back to product mix in a minute. In
7 your opinion, would it be irrational for a processing plant
8 to sell milk below cost in order to maintain volume?

9 A. Depends how deep below cost you're referring to.

10 Q. Does it depend at all on the difference between
11 fixed costs and variable costs?

12 A. It can.

13 Q. Did you -- at the University of Washington, the
14 undergraduate course in economics was -- sequence was 101
15 and 102, and in one of those two, there was a textbook
16 which indicated that it was logical to sell milk or any
17 other product below your total cost as long as you're
18 recovering your variable costs. Would you agree that that
19 can be a rational strategy?

20 A. Not over the long term, no.

21 Q. And why not?

22 A. Because you're selling below cost.

23 Q. But you are covering all your variable costs and
24 your fixed costs are sum (phon.) costs, and that's what I
25 learned in Econ. 101. Agree or disagree with that

1 principle?

2 A. With what principle?

3 Q. That you stay in business as long as you're
4 covering your fixed costs.

5 A. That you stay in business as long as you're
6 recovering your fixed costs? It's too --

7 Q. Excuse me, as long as you're recovering your
8 variable costs.

9 A. It's too vague of a statement for -- from which
10 -- for me to comment on. I'm not really here as an
11 economist.

12 Q. Well, at the risk of asking a question about
13 economics then, when you were with Dean -- assuming this
14 was the old Dean Foods Company, not the current Dean Foods
15 company?

16 A. Correct.

17 Q. Was it ever considered that you would lower costs
18 -- correction, lower price below your total cost in order
19 to retain volume under the threat of losing that volume to
20 a competitor? Did you ever do that, Dean Foods?

21 A. I don't wish to testify about Dean specifically.

22 Q. Let's not talk about Dean then, would it be
23 rational for a company, whether it's Dean's company or
24 mine, to cut costs below -- cut price below total costs in
25 order to maintain business and keep it away from a

1 competitive --

2 A. I would say it depends on a lot of factors that
3 we would be here all day to discuss. So the hypothetical
4 is almost, in my opinion, is unanswerable.

5 Q. I just asked you, do you stand by your assertion
6 that the -- on page five, "the only conclusion that can be
7 drawn is that the warehouse store is selling milk as a loss
8 leader rather than -- or that Mr. Herbine's methodology is
9 suspect, rather than that there might be a conscious and
10 rational business reason for the processor to be selling
11 milk below cost?" Do you stand by that statement?

12 A. It's possible.

13 Q. What's possible?

14 A. That the processor could be selling below cost.

15 Q. And would that be in all cases irrational in your
16 judgment?

17 A. Depending on the competitive situations. You
18 know, a lot of things could happen. So again, I couldn't
19 comment specifically unless I knew more.

20 Q. Agree that that does depend on those things, and
21 you would need to know more.

22 I ask you to go back then to page four and
23 towards the bottom of the page, the next to the last
24 paragraph, you conclude by saying, "In my professional
25 opinion and experience."

1 Do you see that?

2 "In my professional opinion and experience, a
3 plant that inefficient, if operated by a large, regulated
4 handler would be shut down or folded into a larger
5 efficient plant that could handle the capacity." Do you
6 recall that?

7 A. Yes, I do.

8 Q. What other considerations might go into that
9 decision of folding Plant A into Plant B?

10 A. Specifically in this case I'm talking just to
11 leverage down on costs.

12 Q. Plant costs?

13 A. Yes.

14 Q. What other costs do you have to deal with as a
15 dairy processor?

16 A. Well, it'd be all the costs that exist in the
17 income statement.

18 Q. So I refer you to the Tables A, B, C, and D, that
19 somebody prepared for you, and refer to the line called
20 "Distribution." Is that one of the significant cost
21 factors?

22 A. It can be if you distribute, yes.

23 Q. Would one of the decisions to be made as to
24 whether or not, in your professional opinion and
25 experience, a plant that inefficient should be or would be

1 shut down, folded into a larger efficient plant. Would one
2 of the considerations be how far it is between the two
3 plants?

4 A. Of course.

5 Q. You didn't mention that in your testimony. Would
6 you like to amplify on that consideration at this point?

7 A. I would just to say that if you're at that cost
8 range from a plant production standpoint, you know, unless
9 you -- it's just geographically impossible, it would make
10 economic sense to do it.

11 Q. Well, --

12 A. You can't --

13 Q. Anything's possible geographically as long as you
14 want to pay the transportation --

15 A. Well, --

16 Q. -- or distribution expense, right?

17 A. Well, yeah. Yeah. I mean, I don't think they're
18 going to cross the Rockies and do it, but if you're at 34
19 to 88 --

20 Q. How about crossing the state of Oregon?

21 A. If you're at 34 -- I will say, if you're at 34 to
22 88 cents and within that range, and that is a very wide
23 range, you're at a plant that can't compete from a cost
24 standpoint.

25 Q. If there are competitors nearby, you mean?

1 A. If you're in a competitive marketplace, sure. If
2 you're the only processor in that marketplace, then you
3 will attract other processors at those prices -- at those
4 costs.

5 Q. From what distance?

6 A. I can't answer that.

7 Q. In your professional opinion and experience, what
8 does it cost to move a trailer load of milk on a per gallon
9 basis, trailer load of prepackaged milk, let's say 100
10 miles or 200 miles or 300 miles?

11 A. Again, I'm not here to comment on distribution
12 costs, so.

13 Q. But they're -- they do matter. You did testify
14 to that, and you didn't consider them in your --

15 A. If -- they matter, you know, again, depending on
16 the size of them and the distribution that the particular
17 operation is undertaking, so.

18 Q. Your exhibit has a distribution cost of, as we
19 say, roughly 30 cents. What kind of a distribution radius
20 would you expect there?

21 A. Can't answer that.

22 Q. Well, I'm going to give you a hypothetical
23 situation. Let's suppose you are a owner of
24 producer/handler plant right near the Canadian border,
25 approximately 100 miles from Seattle, and I want to ask you

1 to suggest whether a producer/handler in that situation
2 could somehow be cost competitive with larger processors in
3 the Seattle area if they had substantially more volume.

4 A. Could you rephrase the question. I --

5 Q. You bet.

6 A. I'm not sure exactly what you're asking.

7 Q. -- I'll take it a step at a time.

8 Producer/handler plant near the Canadian border,
9 100 miles distant from the two Seattle area regulated
10 bottlers. That's the hypothetical.

11 A. Uh-huh.

12 Q. Is it reasonable to suggest that that
13 producer/handler can be competitive with large plants in
14 Seattle given the transportation costs involved?

15 A. It's not that simple. You have one cost variable
16 in that complex question, so I can't balance that question
17 on distribution alone.

18 Q. Are you aware that people asking the secretary to
19 balance those kinds of cost considerations?

20 A. Yes, but my testimony again is not delivery
21 based.

22 Q. Oh, really. So it may not be correct so suggest
23 that a producer/handler could not be cost competitive under
24 those circumstances?

25 A. I --

1 Q. It's just what you've testified.

2 A. I don't understand where you're going with it.

3 I'm sorry, --

4 Q. Page four.

5 A. -- I'm not tracking --

6 Q. Page four, your comment, "To suggest that a
7 producer/handler could somehow be cost competitive with a
8 large processor, my comment, in Seattle, while running only
9 three million pounds a month is not realistic."

10 A. It's not realistic from a plant cost standpoint.
11 That's correct.

12 Q. But he's got 100 miles' distance. Is that enough
13 to insulate him from that kind of competition?

14 A. My point here is simply, at that level of volume,
15 I don't know what the costs would be, but it would be so
16 substantial that you wouldn't be competitive as a
17 processor, and I believe it would overwhelm all the other
18 costs. So regardless of your efficiency up and down, your
19 costs -- if you're running the three million pounds would
20 be an extreme challenge.

21 Q. Do you have any idea how many plants in the
22 Pacific Northwest market are operating in the three to
23 five/seven million pound a month range?

24 A. I do not know.

25 Q. Would it be fair to conclude from your testimony

1 that all of those plants are not running efficiently?

2 A. I think it would be -- yes, I think it would be
3 challenging, from my experience, to see a three million
4 pound plant running at a cost competitive to those plants,
5 for instance, that we've seen in the Cornell study which
6 average 27 million pounds.

7 Q. How many 27 million pound plants do you think
8 there are in the Pacific Northwest federal order market?

9 A. Do not know.

10 Q. You don't know much about this market, do you?

11 Let me ask you this. Within a 100 -- 300 mile
12 radius of Chicago, where you are familiar with, I assume,
13 how many people are there?

14 A. Within 300 miles of Chicago, I really don't know.
15 I'm not going to guess those types of numbers.

16 Q. Would you be willing to wager a guess as to
17 whether it's more or less than the distance between --

18 A. The distance or the people?

19 Q. -- within the 300 mile radius of Portland?

20 A. No, I wouldn't.

21 Q. How many plants in the Pacific Northwest market
22 could be operated in the range of size of the Cornell study
23 that you referred to? How much market is there for how
24 many plants?

25 A. I can't answer that.

1 Q. Okay. Well, what would it take in terms of
2 gallons or millions of pounds a month to be efficient in
3 your view?

4 A. I can't put a specific poundage. However,
5 clearly looking at what the Cornell study looked at, those
6 types of volumes would be required to be efficient on a
7 larger scale plant.

8 Q. And what are those volumes that you refer to?

9 A. The average, 27 million pounds.

10 Q. Okay. I want to represent to you that in that
11 table -- in fact, let's ask you to look, and I think it's
12 -- see page 11? Would you -- taking a look at the pounds
13 of class one in that left-hand column, for the total
14 market, not counting producer/handlers, that it's roughly
15 180 million pounds a month?

16 A. Yes, that's what the schedule says.

17 Q. How many 27 million pound plants could this
18 market accommodate then?

19 A. It would probably be around six.

20 Q. Only six efficient plants could handle the entire
21 marketplace; is that your testimony?

22 A. My testimony that there are plants of varying
23 sizes and plants of varying efficiencies, but there are
24 certain dynamics that need to be achieved to compete with
25 the large pool processors, and to do that, I do believe you

1 need to be in the significant processing from a poundage
2 standpoint of the range that I just quoted.

3 Q. Mr. Morrison, how does that square with the fact
4 that in this market area, there are over 25 plants? Might
5 it have anything to do with transportation costs and the
6 insulation that provides to a plant?

7 A. Again, I'm not here to comment on transportation
8 costs.

9 Q. Are you here to tell us then that transportation
10 costs do not matter?

11 A. Not here to do that.

12 Q. How do you -- how does the fact that --

13 A. I'm -- if you discretely look at a plant and look
14 at the productive capacity of the assets that go into that
15 plant to run the volume, you can draw some good conclusions
16 in terms of what volume is needed to be competitive, and
17 that's what I've done.

18 Q. Well, the standard of being competitive is to
19 have volume in that rough 27 million pound range, right?

20 A. The standard to be competitive is to optimize the
21 productive capacity that you have, and if you're in a
22 competitive market where you have processors in scale to
23 achieve these kind of volumes, you better get there, or
24 it's going to be tough to be a real player.

25 Q. And your clients better get there, or it's going

1 to be tough for them to be a real player, right?

2 A. I think to limit their volume to a small fraction
3 of what some of those players are processing would extinct
4 them, yes. I don't know how you get from, you know, at the
5 low end of the 27 and be competitive. Let me rephrase
6 that. I don't -- competing against the Cornell-type
7 business with a three million cap would be impossible, in
8 my opinion.

9 Q. All right. Well, let's suppose you had nine
10 producer/handlers with 27 million pounds each. That would
11 take up the entire market, would it not?

12 A. No. You're still talking about the same market?

13 Q. Yeah.

14 A. And you had nine producer/handlers with three
15 million pounds each?

16 Q. No, 27 million pounds each.

17 A. With 27 million pounds each?

18 Q. Might --

19 A. Your math is correct.

20 Q. Might exceed the market, right? Now, one, two,
21 three, four, five, six, seven, eight, nine. I represent to
22 you that the table on page eight of your Exhibit 5 shows
23 that there are nine producer/handlers. Was it your
24 testimony that the federal order should allow each of those
25 nine plants to become efficient and grow to the 27 million

1 pound range?

2 A. I'm not commenting on that with regard to what
3 you should grow to or not. I'm commenting on the volume
4 range that's necessary to be competitive with larger,
5 regulated handlers, --

6 Q. Okay. And --

7 A. -- and I think to do that, you need to have the
8 substantial volume that the plants provide, that the
9 footprint provides.

10 Q. Okay. Let's go to that very question then. I
11 think Mr. English touched on it earlier. If you assume
12 that the regulated handlers are all at 27 million pounds or
13 thereabouts, what volume does a producer/handler plant have
14 to be at to be competitive?

15 A. I don't know that number.

16 Q. Well, you know that Mr. Herbine was trying to
17 determine that number, don't you, because you read his
18 testimony, right?

19 A. Yes.

20 Q. And you --

21 A. I know it's no where near three million pounds.

22 Q. Well, you didn't duplicate his analysis then, did
23 you, to determine at what level it would be?

24 A. Did not. Really wasn't necessary in terms of --

25 Q. Dated --

1 A. -- if you look at a three million pound cap and
2 suggest that you're going to run a plant that's efficient
3 by today's standards for a few hours and send everyone home
4 with an eight hour payday, you're simply not going to
5 achieve costs that are anywhere close to competing with the
6 big fluid processor, and that's reality, so.

7 Q. I suppose you didn't send --

8 A. Now, where that line is -- could I finish,
9 please?

10 Q. Sure, I'm sorry --

11 A. Where that line is between 3 million and 50
12 million, I don't know, but it's a lot closer to the 50 than
13 it the 3.

14 Q. What if you didn't -- what if the
15 producer/handler didn't send their employees home after
16 working less than eight hours and give them an eight hour
17 paycheck? What if, instead, they put them to work out in
18 the barn?

19 A. You're still running a plant three hours a day.
20 I don't think you want to do that.

21 Q. But you know the three million pound number's the
22 wrong number. Do you have a right number to suggest based
23 on your economic and/or other analysis?

24 A. I don't have a number, but I mean, my testimony
25 spoke to the productive capacity of what a Dean or any

1 large fluid processor on simply a gallon line could
2 achieve. And of course, you're probably not going to just
3 run a gallon line, you're going to run a half gallon and
4 other products, so -- and to be efficient, you know, you're
5 going to have to run those substantial hours.

6 In my example, I used 100 hours. There are
7 plants obviously running a lot more than 100 hours. There
8 are plants running less, but you know, you would need to
9 be, you know, again, and I feel like I'm saying this for
10 the umpteenth time, but you would need to be in that range
11 or running your plant at those levels for those number of
12 hours to, you know, average down the huge fixed cost in the
13 plant that you have to have a reasonable shot at competing
14 at large business.

15 Q. Transportation costs aside?

16 A. Transportation costs, again, aren't what I'm
17 testifying to.

18 Q. I'm asking you if you're testifying that you need
19 --

20 A. I mean, it's -- the math works. So if your
21 delivery costs -- you know, your delivery cost obviously is
22 part of the factor and can be a significant part of the
23 factor. I'm just simply not testifying to it.

24 Q. Understood. Thank you very much.

25 Now, one last thing. You said a 100 hour plants,

1 that was kind of a standard, the Dean -- the old Dean Foods
2 -

3 A. No, that's -- again, that's not -- that's -- my
4 industry experience and looking at the Cornell study which
5 has a lot of good data and knowing, you know, the
6 footprints of some of the plants that were in that study
7 has led me to that conclusion.

8 Q. I would --

9 A. I mean, essentially if you do the math, you have
10 the 168 hours, if I did it correctly, a week, and these
11 plants can run a substantial number of hours each day.

12 Q. I represent that I was told by a Dean Foods
13 person something once, and I'm going to ask you if you
14 agree with it. The most efficient plants are those that
15 run about 100 hours a week minimum and that are old plants
16 that are largely depreciated but have modern equipment.
17 Would you agree with that statement?

18 A. The 100 hours plus, you know, certainly is a key
19 factor to achieving costs. The new equipment, obviously,
20 that you mentioned is important, too, because you need the
21 productivity that's available on, you know, the gallon
22 lines that you purchase today. Fully depreciated, it's
23 just simply a -- it's not a real relevant factor in my
24 mind, but.

25 MR. MARSHALL: Okay. Thanks for your help.

1 THE COURT: Before we continue, I just want to
2 ask, are you going to call any more witnesses today, Mr.
3 Yale, or is it --

4 MR. YALE: The time is such, I think the answer
5 is no.

6 THE COURT: Then why don't we take -- can we take
7 a ten minute break and then we'll -- just because I think
8 he's going to be up a while longer, and we might as well
9 take a break. This will be our last witness, and then
10 we'll resume with Mr. Berde.

11 Okay. Off the record.

12 (Off the record and reconvened.)

13 THE COURT: Okay. We're back on the record, and
14 Mr. Berde, it's your turn to ask some questions.

15 EXAMINATION

16 BY MR. BERDE:

17 Q. Good afternoon.

18 A. Good afternoon.

19 Q. Sydney Berde for United Dairymen.

20 Mr. Morrison, when did you go to work for Dean
21 Foods?

22 A. In March of 1993, if I remember correctly.

23 Q. Was that your first job out of college?

24 A. No, no.

25 Q. What did you do before that?

1 A. I worked in various -- out of college, I worked
2 in Big Four Accounting, and then I went into industry as,
3 well, controller and audit-type positions. And then
4 actually graduated in '79, so I've been working
5 professionally for 24 years now.

6 Q. So Dean Foods was your first experience with
7 anything that had to do with the dairy industry; is that
8 correct?

9 A. Yes, that's correct.

10 Q. And when you went to work for Dean Foods, what
11 was your first job?

12 A. Dairy Group Controller.

13 Q. Dairy what?

14 A. Dairy Group Controller was the title of the job.

15 Q. That was at Franklin Park, Illinois, right?

16 A. Yes, that's correct.

17 Q. At the corporate headquarters?

18 A. Right.

19 Q. What else goes on at Franklin Park?

20 A. Well, today I don't know, but you're talking in
21 terms of when I was there?

22 Q. Yes.

23 A. All the corporate management functions are there,
24 so what you'd traditionally see in a corporation would be
25 there.

1 Q. Now, Dean Foods operated a number of regulated
2 processing plants in the general area of Franklin Park, did
3 it not?

4 A. In Northern Illinois, yes.

5 Q. Yeah, at Shemmong (phon.) and Huntley?

6 A. Yes.

7 Q. Those are two processing plants -- regulated
8 plants, right?

9 A. Yes.

10 Q. And when you first went to work for Dean, what
11 did they have you do as your first job?

12 A. I'm not sure.

13 Q. Well, --

14 A. I mean, but I was financially responsible for the
15 dairy group from day one, so I mean, you know, it was more
16 or less get out and learn the business, --

17 Q. I see.

18 A. -- I suspect.

19 Q. And did you spend just about all of your time
20 right there at the Franklin Park office?

21 A. No.

22 Q. What else did you do?

23 A. Traveled.

24 Q. Traveled. You visited plants?

25 A. Yes.

1 Q. I see. What plants did you visit?

2 A. I don't recall. I mean, most of the processing
3 plants I have visited.

4 Q. You never managed a dairy farm, did you?

5 A. No.

6 Q. And your responsibilities never included staying
7 at a plant and observing its operations, did it?

8 A. I would do that, yes.

9 Q. You would do that. And they wanted you to move
10 from plant to plant?

11 A. I would visit several plants over the course of a
12 year, yes.

13 Q. What size plants were part of your
14 responsibility?

15 A. I don't want to comment specifically on Dean
16 Foods' operations, so I -- and it's been a while, so --

17 Q. Well, --

18 A. -- I'd prefer not to comment on that. Dean was
19 part of the Cornell study, so if you look at the Cornell
20 study, you get an idea of the size of plants.

21 Q. Well, we don't have Cornell available for cross-
22 examination, so I've got to get my answers out of you.

23 And can you tell me what plants of Dean that you
24 visited during the course of your employment with Dean?

25 A. I don't want to answer that. I would say that I

1 left Dean in early 2002, and I would say that there were
2 less than ten percent of the plants that I had not visited.
3 So I've visited virtually all of them.

4 Q. And for what purpose?

5 A. I was responsible for them financially.

6 Q. These were substantially -- substantial sized
7 plants, weren't they in the area of 3 million/40 million a
8 month?

9 A. I don't want to comment on that specifically, but
10 yes, I mean, you know.

11 Q. Well, you just did.

12 A. I know. Dean operates large-scale plants, yes.

13 Q. Yeah. Any plants below 20/25 million?

14 A. 20/25 million in sales, or are you talking pounds
15 per month?

16 Q. 25 million a month.

17 A. In poundage?

18 Q. Yeah.

19 A. Don't recall.

20 Q. What was the smallest plant that you visited?

21 A. I don't recall specifically.

22 Q. Certainly never a three million pound plant; is
23 that correct?

24 A. Three million pound a month?

25 Q. Yeah, --

1 A. No.

2 Q. -- three million a month.

3 A. No.

4 Q. No. Or five million a month?

5 A. Doubtful.

6 Q. Or ten million a month?

7 A. Again, I'm just -- you know, the scale was larger
8 there.

9 Q. Now, --

10 A. There could've been some on the -- on, you know
11 -- in the range you're getting in now, I'm sure there were
12 some that --

13 Q. Uh-huh.

14 A. -- fell into that at some point during my career.

15 Q. Your testimony describes your responsibilities as
16 accounting, financial reporting, acquisitions, cost
17 accounting, and strategic planning. Of that array of
18 activities, I want to focus on cost accounting. Describe
19 for me what that involved.

20 A. Product costing essentially.

21 Q. What's that?

22 A. Product costing at the plant level.

23 Q. Product costing --

24 A. Product costing, yes, gallons, half gallons,
25 quarts, pints. Going through the attachment of cost to the

1 individual products for purposes of understanding their
2 profitability.

3 Q. Okay. I see. And would you do that on an
4 individual plant basis, or --

5 A. I wouldn't personally do it.

6 Q. What's that?

7 A. I didn't personally do it, but we had plant
8 accountants that did that, yes.

9 Q. I see. Well, what was your responsibility with
10 respect to what your plant accountants did?

11 A. Direction in terms of methodology and
12 consistency.

13 Q. Did you get involved at all in, for example, the
14 cost of receiving milk at a plant?

15 A. I was aware of the, you know, pieces to the
16 puzzle with regard to cost/bill (phon.), yes.

17 Q. You mean --

18 A. And raw receiving is, in some plants, would be a
19 cost pool.

20 Q. You mean the aggregate fragments of the
21 processing -- receiving, processing, packaging, et cetera?

22 A. Yes.

23 Q. Yeah. But in terms of actual management, that
24 was not part of your responsibilities?

25 A. It was very much my responsibility.

1 Q. Management of the plant, I'm talking about.

2 A. No, no. Management of the plant, no. I'm sorry,
3 I thought you meant with regard to overseeing cost
4 accounting. Plant management was not my responsibility.

5 Q. So it's fair to say --

6 A. They wouldn't put an accountant in charge of a
7 plant.

8 Q. I'm sorry. Is it fair to say that much of your
9 testimony here with respect to the theoretical cost of
10 operation of a plant at various levels is what you derived
11 from the Cornell study?

12 A. Yes.

13 Q. And that's the -- mainly the basis of your
14 testimony?

15 A. It's the Cornell study, and it's just the
16 experience in the industry that allows me to look at that
17 make sense of it, yes.

18 MR. BERDE: Thank you.

19 THE COURT: Go ahead, Mr. Beshore.

20 EXAMINATION

21 BY MR. BESHORE:

22 Q. Now, Mr. Morrison, Marvin Beshore, Dairy Farmers
23 of America.

24 Mr. Morrison, with respect to the Cornell study,
25 which you just indicated you relied upon substantially,

1 there are a proliffery (phon.) (sic) of costs which were
2 not included in this Cornell figures that you relied upon;
3 isn't that true and correct?

4 A. Explain what you mean.

5 Q. There were costs -- plant costs that are not
6 included in the figures that you've used from the Cornell
7 study, correct?

8 A. Which -- again, which costs are you suggesting
9 aren't in there? I -- you need to be more specific.

10 Q. Well, didn't the Cornell study say what costs it
11 did not include?

12 A. The Cornell study was comprehensive with regard
13 to plant cost, --

14 Q. Well, let me read --

15 A. -- in my opinion.

16 Q. Okay. Let me call your attention -- do you have
17 the Cornell study available, by the way?

18 A. I don't have it on me, no.

19 Q. Okay. On page 35, overview of results, plants
20 costs per gallon (phon.). It says, "we did not" in bold,
21 include, and under a series of costs, do you remember?
22 Remember that?

23 A. If you could continue, I'm sure it'll jog my
24 memory.

25 Q. Okay. The cost of labor for blow molding, not

1 included, correct?

2 A. Yeah, that's correct.

3 Q. Okay. Cost of packaging materials, not included.
4 You're aware of that?

5 A. Yes.

6 Q. Cost of ingredients not included. They go --

7 A. Yeah, those aren't plant costs that you're --

8 Q. Okay. How about --

9 A. -- suggesting. So that's not a surprise.

10 Q. Depreciation expenses on equipment and
11 structures, not included.

12 A. Depreciation in the plant was included.

13 Q. Was not included?

14 A. Was included.

15 Q. In what?

16 A. Your -- did you read the entire --

17 Q. No, I'm reading you --

18 A. -- Cornell study, because there's several pieces
19 to the puzzle, and one of the common ways to look at
20 plants, because depreciation can be very different on a per
21 gallon base, depending on whether it's a new plant or an
22 old plant. So the study was conducted with and with out
23 depreciation.

24 Q. Well, this says --

25 A. So you may -- it wouldn't be -- it wouldn't --

1 you would never do a study and not include depreciation.

2 Q. Well, this -- I'm just reading you verbatim. "We
3 did not include depreciation expenses on equipment and
4 structures."

5 A. Yeah. Well, you'd have to read the whole study
6 to understand how they did it. You're reading a piece of a
7 large study, so you're drawing an inappropriate conclusion.

8 Q. Well, --

9 A. It was done with and without depreciation, and
10 that's a really good way to look at it because old
11 plant/new plant, you can draw some conclusions with regard
12 to cost.

13 Q. Okay. Cost of distribution?

14 A. That's not a plant cost.

15 Q. Okay. General and administrative expenses?

16 A. That's not a plant cost.

17 Q. Selling expenses? Not a plant cost?

18 A. Not a plant cost, yes.

19 Q. Okay. Are they costs that are nevertheless,
20 incurred by facilities in make sales?

21 A. Depends on the facility.

22 Q. Some don't have selling expenses, correct?

23 A. That's correct.

24 Q. Okay. The -- are you familiar with the
25 information that Mr. Hollon presented with respect to

1 plants and the federal order system, plant sizes?

2 A. No, I'm not.

3 Q. Okay. Well, let me represent to you that he's
4 surveyed the -- all of the -- obtained information from all
5 of the market administrators in the federal order system.
6 And the information showed there were 278 fully regulated
7 plants in the system. And the smallest one third grouping
8 had average volumes. That's 90 plants give or take.
9 Average volume of 3.7 million pounds.

10 A. Per?

11 Q. Plant per month.

12 A. Per month?

13 Q. Yes.

14 A. Of all regulated plants, the bottom third --

15 Q. Correct.

16 A. -- is processing four million pounds a month?

17 Q. Correct. Okay. Now, is it your --

18 A. They better get moving then, would be my thought.

19 Q. Okay. How about the middle third that process an
20 average of 11.4 million?

21 A. That's the survey period of this? Is this
22 current data?

23 Q. May 2003.

24 A. May 2003. That's current.

25 Q. Okay. The middle third, 11.4 million per month

1 average. Same comment to them, they'd better get moving?

2 A. They're headed in the right direction.

3 Q. Did you read Mr. Cryan's testimony -- Dr. Cryan's
4 testimony?

5 A. I didn't read it comprehensively, no.

6 Q. Did you read the other studies that he cited and
7 relied upon with respect to plant processing costs?

8 A. What were those studies?

9 Q. One was from the University of Maine.

10 A. Is that the '02 study?

11 Q. There may have been two. One was --

12 A. There are. They updated. Yes. I'm quite
13 familiar with that study.

14 Q. Okay.

15 A. I didn't read it through his testimony. I'm just
16 aware of it, and it's --

17 Q. Okay. You've not --

18 A. It's good data.

19 Q. Pardon?

20 A. It's meaningful data.

21 MR. BESHORE: Okay. Thank you. That's all.

22 THE COURT: Ms. Deskins do you or your colleagues
23 have any questions of this witness?

24 MS. DESKINS: No, we don't.

25 THE COURT: Mr. Miltner? I didn't give Mr.

1 Ricciardi a chance, did I? Go ahead.

2 EXAMINATION

3 BY MR. MILTNER:

4 Q. Mr. Morrison, I just have a couple of questions
5 regarding Mr. Herbine's exhibits. If you could turn to the
6 very last page of his exhibits, which I believe is Exhibit
7 K, titled "Warehouse Store by Pool Distributing Plant - F."

8 A. Okay. Yes, the -- okay. I think I have the one
9 that you're speaking of.

10 Q. Okay. Should be the last page.

11 A. Okay.

12 Q. And do you recall that Mr. Herbine represented
13 that this was representing a 30 million pound per month
14 plant?

15 A. Yes, that's correct, 30 million pounds monthly
16 volume.

17 Q. A 30 million pound per month plant that had a
18 cost -- plant cost for two gallons of milk of 67 cents.
19 Would that be competitive?

20 A. No, in my opinion, it would not. That would be a
21 high volume plant that -- you know, again, depending on the
22 mix of product, but what's being suggested here in the
23 Herbine testimony is this is a cost for a gallon. So this
24 is a cost for the most efficient product that is run
25 through a plant, and this would not be competitive at all.

1 Q. And just to clarify. Even if that's a two gallon
2 price, is that competitive?

3 A. Well, I'm dividing by two, so I mean, if you're
4 at 33 and a half cents on a per gallon basis, on a high
5 volume plant, you have trouble with your gallon line.

6 Q. Do you have any opinion as to the propriety --
7 the competitiveness of the 34.8 cent packaging cost for two
8 gallons?

9 A. I'd rather not comment on that.

10 Q. That's fine. If I could turn to the previous
11 page, Exhibit J, same title, except it ends with a "-E."

12 A. Okay.

13 Q. If you recall, Mr. Herbine represented that that
14 was for an 18 million pound per month plant. If such a
15 plant had a plant cost of 70 cents per two gallons, 35
16 cents a gallon, would that be a competitive plant?

17 A. No, it would not. At that level of volume,
18 you're getting to the point where you should be running
19 your lines -- you have at least the volume to be running
20 them efficiently -- pretty efficiently, and at 35 cents a
21 gallon, you know, again, doing the 15 to 25 cents that I've
22 testified to is a fair, competitive cost. This would be
23 well in excess of that, almost double.

24 Q. Following all the cross-examination from the
25 proponents and their counsel, has your opinion regarding

1 the ability of a three million pound per month plant to
2 compete in the marketplace changed?

3 A. No, it hasn't.

4 Q. Is there anything else you'd like to add before
5 we release you from the stand?

6 A. No, I have nothing else to add.

7 THE COURT: Let me just ask Mr. Ricciardi if he
8 -- I didn't give him a chance. Did you have any questions
9 of this witness?

10 MR. RICCIARDI: I don't.

11 THE COURT: Okay. Anyone else?

12 MR. UNIDENTIFIED: We don't have anything
13 further, Your Honor.

14 THE COURT: Okay. You may step down.

15 This witness didn't last as long as I
16 anticipated, I thought, to me (phon.), and so I'm -- what
17 I'm wondering is -- I'm, like, full of energy, and I'm
18 perfectly willing -- if you have one of your local
19 witnesses or someone.

20 MR. UNIDENTIFIED: (Indiscernible) maybe I can
21 have --

22 THE COURT: Let's get a consensus. I don't care.

23 MS. DESKINS: Judge Hillson? I think maybe the
24 hotel wants us out of here by a certain time. I think --

25 THE COURT: What time is that?

1 MS. DESKINS: -- they spoke to the court
2 reporter.

3 THE COURT: Did they give you a time?

4 Let's -- off the record.

5 (Off the record and reconvened.)

6 THE COURT: Okay. Let's get back on the record.

7 Mr. Yale, if you'll call your next witness.

8 MR. YALE: Sure, Your Honor. We have Mr. Rob
9 Heerspink.

10 THE COURT: Okay. And I'll swear you in first.
11 Would you please raise your right hand?

12 ROB HEERSPINK, WITNESS, SWORN

13 THE COURT: Okay. If you would state and then
14 spell your name, please.

15 THE WITNESS: Rob Heerspink. R-o-b, H-e-e-r-s-p-
16 i-n-k.

17 EXAMINATION

18 BY MR. YALE:

19 Q. And what is your business address, Mr. Heerspink?

20 A. 9409 Depot Road, D-e-p-o-t, Road, Lynden,
21 Washington, L-y-n-d-e-n.

22 Q. And what are you -- how are you employed at this
23 time?

24 A. I'm employed at Edaleen Dairy and also I'm a co-
25 owner of the company.

1 Q. And who are the other owners of Edaleen Dairy?

2 A. Ed and Aileen Brandsma, Duane and Susan Brandsma,
3 myself and my wife Cheryl, Mitch and Karen Moorlag.

4 Q. And are all of you related in some way or
5 another?

6 A. Yes, Ed and Aileen are mom and dad. Duane,
7 Cheryl, Karen are all brothers and sisters, and then the
8 in-laws.

9 Q. And do you have any children?

10 A. Yes, I do.

11 Q. And what are the ages of your children?

12 A. 12, 10, and 8.

13 Q. And what do you do for -- at Edaleen Dairy?

14 A. I manage the production facility. I manage the
15 dairy farm portion, and my responsibilities are to get the
16 milk into the tank for (indiscernible)

17 Q. After high school, did you have any further
18 education?

19 A. I attended two years at the community college.

20 Q. Okay. And how long have you been employed or at
21 Edaleen Dairy?

22 A. Since 1988.

23 Q. Now, in your -- you said, head of the farm.
24 Describe what that means, what you do.

25 A. I oversee all the day-to-day operations of the

1 dairy, responsibility of all the cattle's health, the feed,
2 the production, the quality to make sure that there is a
3 steady supply of milk for the processing plant.

4 Q. And how many employees do you have underneath you
5 at?

6 A. Approximately 35.

7 Q. All right. And in terms of ethnic background, is
8 there a diversity there?

9 A. I would say about a third are white caucasian,
10 and two thirds would be a minority backgrounds.

11 Q. And those are full time employees of that
12 business?

13 A. Correct.

14 Q. Now, what is your experience on a dairy farm?
15 How many years have you been with dairying?

16 A. I grew up on a dairy farm. When I was a teenager
17 through the college years, I was -- I worked for three
18 other, different dairies, and then when I got married to
19 Cheryl, then came to work for Ed.

20 Q. Now, when you say grow up on the dairy farm, does
21 that mean that you just lived there and were not part of
22 the thing, or did you actually have chores and tasks
23 associated --

24 A. You know, we had chores.

25 Q. And what were some of the chores you had as an

1 individual, as a kid?

2 A. Cleaning stalls, feeding calves, helping out with
3 the irrigation, the -- just the day-to-day pitch in help --
4 help your parents when you could.

5 Q. Now, when it comes to your position today, you
6 know, operating this dairy farm, did those experiences as a
7 young child or adolescent on that farm have any --
8 contribute at all to your knowledge or assistance in that?

9 A. Oh, absolutely. When I approach fellow employees
10 and see certain circumstances arise, the background and
11 experience comes into play, how to approach these jobs and
12 how to work with these people for -- to get it done in an
13 efficient manner.

14 Q. All right. And what about knowledge of the
15 animals?

16 A. That would apply also to that. Seeing the --
17 being out as a kid with the vet. calls (phon.) and being
18 involved with the other dairies and their management
19 styles, and then working my way up through the present
20 company, that you accumulate a lot of background experience
21 that way.

22 Q. Now, the farm that you operate, what is the range
23 of its daily average production per cow?

24 A. I would definitely classify it higher than the
25 average that was presented by Mr. Smith.

1 Q. And is getting that high -- higher than average
2 production, is that a fairly easy thing to do as a
3 herdsman?

4 A. No. No, it's definitely a challenge. Obviously
5 with previous testimony it would show that you're already
6 in the upper half of the echelon, and then to pursue that
7 is a continuing -- a difficult challenge.

8 Q. Right. And what are -- are there a few factors
9 -- how many factors are involved in the daily production of
10 an animal?

11 A. There's a multitude of factors into that. You're
12 -- the environmental, the weather, the condition of their
13 housing, the feed that you're able to grow yourself and/or
14 purchase, the ability to source nutritionists and
15 consultants to help balance those feeds, the age of your
16 herd, your access to genetics. There's a -- an extensive
17 list that all contributes to that.

18 Q. Are all of those in your control?

19 A. Yes. I -- well, the weather's not in my control,
20 and there's absolutely variables that I have no control.

21 Q. Okay. And in the -- this operation, to do this,
22 I mean, if you spent time developing skills to establish
23 nutrition and stuff for your animals?

24 A. Absolutely, in -- being able to -- I source
25 information in textbooks, going to conferences, hiring

1 consultants, using a multitude of information sources, the
2 extension agents from the universities. You collaborate
3 the information, and you sort through them, and find what's
4 the most applicable for our dairy.

5 Q. Now, you were here yesterday, were you not, when
6 Dr. Terry Smith testified?

7 A. Yes, I was.

8 Q. All right. And did you hear all of his
9 testimony?

10 A. Yes, I did.

11 Q. And you heard his testimony regarding components
12 and changing components?

13 A. Yes, I did.

14 Q. And based upon your experience as a headman with
15 a higher than average production per cow, do you have an
16 opinion as to what he said, whether it be applicable to an
17 operation such as yours?

18 A. In the presentation that he did it, it would not
19 be as cost advantage as he would've speculated it to be.
20 The two options to -- that he referred to as far as being
21 able to move the butterfat components, he referred to
22 feeding them more cheaply. And in my experience and
23 pursuing some contacts in the meantime, I checked that --
24 the -- going to cheaper feed route enough to change the
25 diet to where that butterfat would get suppressed, you're

1 risking the health of the animal.

2 He also referred to the Canadian industry having to
3 look into doing this, which I -- which is a normal practice
4 up there because of the quota system. I -- in our -- being
5 our proximity to the Canadian border, I have quite a few
6 relatives and contacts up there. So in talking to those
7 dairymen, they have suggested that there is technology out
8 there today that allows feed additives to the rations that
9 would suppress the butterfat, like Dr. Smith suggested, but
10 in reality, it actually increases your feed cost to do it in
11 a health manner.

12 Q. And they offset the higher feed costs because they
13 get a higher value in response to their quota system and --

14 A. Absolutely.

15 Q. And you don't operate under a similar economic
16 system, right?

17 A. No, I do not.

18 Q. All right. But in terms of Edaleen Dairy, the
19 product mix at Edaleen Dairy has, does it include any demand
20 for the cream, other than the class one?

21 A. Minimal. There is -- we do do some ice cream
22 sales.

23 Q. All right. Do you handle a lot of excess cream?

24 A. Sometimes we do, yes.

25 Q. Now, this idea of turning on components and

1 adjusting those, can that be done easily on a day-to-day or
2 week-to-week or month-to-month basis?

3 A. In talking to the industry people of Canada, they
4 suggested in a month-to-month situation it could be possible,
5 and a day-to-day or week-to-week, no.

6 Q. And the demands for -- in the fluctuation of the
7 milk and the demand for milk by Edaleen Dairy, does it only
8 fluctuate on a month-to-month basis?

9 A. No, it definitely fluctuates week-to-week, day-by-
10 day.

11 Q. So it's your opinion that in an operation, the
12 testimony yesterday from Dr. Smith would not be of any value
13 to you in operating the herd for Edaleen Dairy to adjust its
14 supply to meet its demand?

15 A. Not economically, which I -- he portrayed as being
16 an opportunity for us handler/producers.

17 Q. Now, did you ever operate a farm that was not a
18 producer/handler or work on a farm that wasn't a
19 producer/handler?

20 A. I worked on farms that were not handler/producers.

21 Q. Okay. Now, is there a difference at the farm -- at
22 that animal level and the feed and everything, between those
23 that were in the -- that were not a producer/handler and
24 those that were?

25 A. The -- there is different management styles among

1 the four different farms that I've been on, yes.

2 Q. All right. And is any of those managed --
3 differences in management style reflect the fact that Edaleen
4 is a producer/handler, and the others were not?

5 A. No.

6 Q. Now, did there come a time when there was a
7 prospective customer for Edaleen Dairy that required
8 significant, additional milk supply?

9 A. Yes, there was.

10 Q. And approximately how much additional milk was
11 going to be required?

12 A. I'm -- I know we've been talking in pounds, but I
13 know it was about 400 cows.

14 Q. About 400 cows?

15 A. Yes.

16 Q. All right. Now, when that time came, was that a
17 situation where you learned that you needed that amount of
18 milk, that tomorrow you had the 400 cows, and you had the
19 production?

20 A. Repeat your question.

21 Q. It wasn't very well stated.

22 I mean, what's the time lag? If you need an
23 additional 400 cows, how long would it take -- how long did
24 it take you from the time that that decision was made until
25 you were able to have that production?

1 A. Approximately one year.

2 Q. Okay. And what all did that entail?

3 A. Initially was the discussion among the owners,
4 whether that is something we wanted to pursue. Second of
5 all, when we decided as a family to pursue that, then we did
6 the cost analysis and solicited financing. Once that was in
7 place, then we, of course, had to go into construction. Once
8 construction was complete, then we went into the purchase and
9 freshening (phon.) of animals. And by that time it was all
10 of a year.

11 Q. And then once you got the animals and they were
12 freshening, did the volume of milk come on instantly?

13 A. Actually it took another three to four months
14 before that to come full circle, once construction was
15 complete.

16 Q. Have you been involved in other expansions of dairy
17 herd?

18 A. Yes.

19 Q. And is that time frame a reasonable one, an --

20 A. I would think so in our area, yeah.

21 Q. Now, when you made this adjustment, this additional
22 investment, did you have a specific customer in mind?

23 A. Yes, we did.

24 Q. And what was that customer?

25 A. Starbucks.

1 Q. And they were willing to wait 15 months for the
2 milk, or a year?

3 A. In that particular situation, they were. Well, yes
4 and no. That company was a rapidly growing company at that
5 time, and they at that time knew that they were bringing on
6 lots of stores coming on in that year. So their corporation
7 was able to project the oncoming stores and what their
8 typical stores did and projected that much additional milk
9 supply. So there was a push by them, and of course, there
10 was some supply issues and -- in the interim to get that
11 done. But there was pre-planning done by both companies.

12 Q. Now, has there been other times in the history of
13 Edaleen Dairy? By the way, is the family unit -- I mean, are
14 you -- and you are on the farm, but are you involved in
15 hearing discussions of other business plans of the firm as a
16 whole?

17 A. Yes, we meet weekly, and then we also meet monthly
18 to review the financials.

19 Q. Okay. Have you had other situations you're aware
20 of where Edaleen was asked to sell additional volumes of milk
21 that you didn't have?

22 A. Yes.

23 Q. And were those buyers willing to wait for you to
24 add the herd?

25 A. No.

1 Q. So you had to -- being as a PD since it was only
2 your milk, you had to forego those business opportunities?

3 A. That is correct.

4 Q. Is that -- was that -- has that happened more than
5 once?

6 A. Yes, it has.

7 Q. Now, you indicated that you got the wind, and you
8 put in this additional 400 cows, barns, and the like. First
9 of all, let me take another thing. At this point, based upon
10 the location of your farm and the volume that's coming off of
11 that farm, would you be able to today, add another 400 cows?

12 A. No, I would not.

13 Q. And why is that?

14 A. At this time, there -- the facilities are full.
15 The milking parlor is running at capacity, and also with
16 environmentally, I am at what my dairy permit would allow me.

17 Q. So that to add additional cattle at this time to
18 increase sales would require a greater investment and greater
19 effort than what this last one did?

20 A. That is correct.

21 Q. Now, you indicated you worked with them. They gave
22 you some time. You grew with them, and approximately 15
23 months, you had these 400 cows up to production. How long
24 did you continue to market -- did Edaleen sell milk to
25 Starbucks?

1 A. The expansion we just talked about was the biggest
2 jump. The following years, there were smaller, more
3 incremental expansions. In the year 2000, we were --
4 actually '99, we were ramped up (phon.) at that -- what at
5 that time was our max production -- maximum sales, let me
6 correct that. Maximum sales to Starbucks. The following
7 year is when we lost that account.

8 Q. And how did you -- what was the circumstances
9 surrounding losing that account?

10 A. The two main reasons that we were told the fact
11 that we were unable to meet the price that they were being
12 offered, and secondly, the inability for us to service the
13 western market, up and down the I-5 corridor.

14 Q. So are you saying that somebody was offering this
15 milk to them at a cheaper price than you?

16 A. That is correct.

17 Q. Do you know how much cheaper?

18 A. No, I do not.

19 Q. And the other part was, was that you didn't have
20 sufficient volume?

21 A. That is correct.

22 Q. All right. Do you happen to know who got that
23 account?

24 A. Safeway.

25 Q. All right. And do they still have that today, to

1 your knowledge?

2 A. Yes.

3 Q. Now, let's talk a moment. One of things and one of
4 the disappointments I have, by the way, with this seminar is
5 that we don't have the good Starbucks coffee here, but you
6 know, there's a lot of lattes and cappuccinos and stuff,
7 right, in the Northwest?

8 A. Yes, there is.

9 Q. And do you, through Edaleen, or, I mean, are some
10 of the sales made to companies that do, in fact, have a
11 coffee shop type thing with cappucinos and lattes and the
12 like?

13 A. Do we have --

14 Q. Yes.

15 A. -- some of those today to --

16 Q. Right.

17 A. -- different stores other --

18 Q. Sure.

19 A. -- than Starbucks? Yes, we do.

20 Q. And have you ever gotten any feedback from them or
21 your distributors regarding your product and the --

22 A. Yes. We have had positive feedback in the fact
23 that we are typically -- an espresso stand is a small store
24 either on a city corner or in a kiosk in a mall, and they
25 have the inability to have large volumes of storage. They

1 can't take a semi-load direct. And the fact that we were
2 willing to service those smallers with frequent stops, that
3 is the service portion. The other portion is, is they
4 commented on the quality, the ability to get the milk to foam
5 faster than a -- than some other products that they've
6 compared to.

7 Q. Did you get the same response in terms of the
8 quality of the product from Starbucks?

9 A. Yes, we did. That was the original pursuit of
10 keeping us as a client.

11 Q. And they recognize that they maybe lose that, but
12 because of the price, they made the change?

13 A. That is correct.

14 Q. Now, what percentage of your market, or of the
15 sales by Edaleen did that loss of Starbucks represent at that
16 point?

17 A. At that point, it was approximately 25 percent.

18 Q. Now, as a PD, without that 25 percent, what were
19 you going to do with that milk?

20 A. When we lost the account?

21 Q. Yes.

22 A. We had to pursue other avenues to purchase and/or
23 sell it at surplus.

24 Q. And let me ask this, this next question. Was this
25 a situation where you had to suddenly lose that volume, or

1 did they give you any kind of fair warning?

2 A. They staged us out.

3 Q. So you have some opportunity to find replacements?

4 A. That is correct.

5 Q. Now, have you had other situations where customers
6 have terminated their relationship with Edaleen Dairy?

7 A. Yes, we have.

8 Q. And is it ordinarily one in which they give you any
9 kind of long-term notice?

10 A. No.

11 Q. What is the typical amount of notice of the --

12 A. Anywhere from the next Monday till a month. I
13 mean, it's the next Monday. They're -- they've found another
14 source of milk.

15 Q. Now, when that happens, what do you have to do with
16 that milk? Do you tell the cows to stop milking or --

17 A. No. No. At that point, it becomes surplus.

18 Q. And how do you deal with that surplus?

19 A. Pursue either additional customers or end up
20 selling it to a regulated handler.

21 Q. Now, do you ever, from time to time, sell this to
22 NDA?

23 A. Yes, we do.

24 Q. And at what price do they -- are they always
25 willing to purchase it?

1 A. No.

2 THE COURT: Excuse me a second. Could -- Mr.
3 English, could you just whisper a little quieter over there?
4 I just -- it's distracting.

5 MR. ENGLISH: Sorry.

6 THE COURT: Thank you. Go ahead, Mr. Yale. I just
7 --

8 MR. YALE: Well, it was bothering me, but I -- I'm
9 becoming numb, so.

10 THE COURT: Just continue.

11 MR. UNIDENTIFIED: If you'd (indiscernible.)

12 BY MR. YALE:

13 Q. Mr. Heerspink, we were talking about this idea of
14 the surplus, and you were selling it to NDA, or you offered
15 it. There's times they didn't buy it?

16 A. That is correct.

17 Q. And there never come a time when you had to dump
18 the milk?

19 A. Not recently, but we have in the past.

20 Q. And as a result, receive no value; is that right?

21 A. That is correct.

22 Q. Now, as a farmer who grew up on a dairy farm and
23 producing milk, what's it like to turn that product into the
24 field or --

25 A. It's difficult to do. You spend -- as a producer,

1 you spend your working time, trying to find efficiencies and
2 take care of the animals to produce that product. And always
3 recognizing that it is a perishable product. It is hard to
4 see it to go for no value.

5 Q. So as -- one of the situations is a -- you'd say
6 with Edaleen as a producer/handler, at any moment you take
7 the risk the customer's going to call, and you don't have a
8 sale, right?

9 A. That is correct.

10 Q. And then you're going to have an opportunity where
11 you may be able to sell it, or you may not, right?

12 A. That is correct.

13 Q. Now, some of this milk you said -- is there time to
14 time NDA does purchase it?

15 A. Yes, there is.

16 Q. And do they exact any terms from you for doing
17 that?

18 A. They typically pay us class three minus a two --
19 \$1.50 charge.

20 Q. Now, let's -- I want to go to another subject. One
21 of the things that was also talked about yesterday by Dr.
22 Smith was costs of production.

23 A. That is correct.

24 Q. Now, you saw some numbers that he had?

25 A. Yes, I did.

1 Q. Did those represent the cost that you would see for
2 a farm of your size in the region that you produce milk?

3 A. In the summaries I've seen from accounting
4 services, like Moore, Stephens and Torbet (phon.) puts out a
5 regional study that did not correlate. They showed that cost
6 of production is higher in our area.

7 Q. Is this Torbet the same company that he indicated
8 that he was associated with from time to time, or do you
9 know?

10 A. I do not know.

11 Q. But you indicated that it was higher than what he
12 was indicating?

13 A. Yes.

14 Q. All right. And during the last couple years -- I
15 mean, do you follow, like, what the blend prices and what
16 your neighbors are receiving --

17 A. Yes, I --

18 Q. All right. And during the last couple years, has
19 there been periods of time when your cost of productions were
20 greater than those blend prices?

21 A. Yes, it has. Yes, there has been some.

22 Q. Significantly higher, or just a little bit?

23 A. Significantly.

24 Q. Now, I -- we -- I want to kind of, I guess,
25 apologize. I want to go back. We talked about this

1 balancing. So I understand it, is that Starbucks was an
2 unusual deal for you in terms of allowing you to ramp up in
3 sales, and they also were able to work with you to ramp down
4 after you made an investment for them; is that correct?

5 A. That is correct.

6 Q. And that is the exception?

7 A. Absolutely. The only time it's -- we've ever
8 experienced it.

9 Q. Now, in terms of the quality of the milk on your
10 farm, there was some testimony today. Did you hear the
11 testimony of David Beene.

12 A. Yes, I did.

13 Q. And he talked about the quality and how they were
14 responsible from grass to glass, do you recall?

15 A. Correct.

16 Q. Yeah. Do you feel the same way?

17 A. Absolutely.

18 Q. And has that created any changes in the way you
19 operate your farm with that in mind, as opposed to the farms
20 that you were on that were not part of a producer/handler?

21 A. I would like to think we put more emphasis than the
22 farms that I did work on, on double-checks. On the farms I
23 worked on, definitely paid attention to quality and tried to
24 produce a sure -- a good product, but we will -- we have
25 implemented -- it's doubles and sometimes triple checks, like

1 in the case of antibiotics, just to make sure that there is
2 no hot loads. And we also have tried to do in all case
3 possible, for cooling and other items that contribute to
4 quality, to the best that we can do.

5 Q. Let's talk about -- what is the issue with
6 antibiotics? Will you explain that?

7 A. If a load of milk were to receive an antibiotics
8 into it, that it is not a safe milk -- a safe milk for the
9 public. So then it becomes milk that is of no use.

10 Q. And how to antibiotics get in the milk?

11 A. The -- any animal that has been treated for -- with
12 penicillin then would produce antibiotic milk with -- milk
13 with antibiotic residues.

14 Q. All right. And the standard's very low that you
15 cannot -- I mean, it's a zero --

16 A. It's very sensitive, yes.

17 Q. Right.

18 A. Yeah.

19 Q. And how much -- if you have one cow that's treated,
20 how much milk can that impact?

21 A. From my understanding, thousands of gallons.

22 Q. So to -- if at Edaleen Dairy you had a situation
23 where you had a -- antibiotic had gotten into the milk, what
24 would be the response to the supply to that -- to the plant?

25 A. It would not receive that load, and it would be

1 shorted that day's production that has been contaminated.

2 Q. Now, what steps then have you taken to ensure -- I
3 mean, that would not be a good thing, right?

4 A. Correct.

5 Q. So what steps have you taken at Edaleen's farm that
6 -- to do to avoid that?

7 A. We have put all antibiotics under lock and key,
8 that -- and made protocols where only certain individuals
9 have access to those locked drugs, built a separate milking
10 facility for all treated animals, have the gates padlocked
11 into those pens so that there would not be any opportunity
12 for people to open those gates and allow those animals into
13 the mainstream production. And also there is another two
14 sets of gates that, per se, the person did not lock the lock,
15 and the cow banged the gate open. It would have to do an
16 additional gates to get into the milking herd.

17 Q. Because one of the problem, cows are a very social
18 animal?

19 A. Absolutely.

20 Q. And if you remove a cow from her friends, she wants
21 back --

22 A. She wants back. Yeah.

23 Q. She wants back?

24 A. Yeah.

25 Q. Even when you tell her she's sick?

1 A. Yeah, well, she hasn't made her mind up always.

2 Q. So what about the milking of those cows? What do
3 you do?

4 A. We have a separate milking facility that there is
5 no provisions in that facility to capture the milk. It is
6 piped straight into the drain and into the waste drain.

7 Q. Now, is that an extra cost to set that type of a
8 set-up as compared to other management techniques for
9 antibiotics?

10 A. Yes, there was additional costs.

11 Q. And did you make those additional costs and take
12 these additional protocols in part because of the
13 responsibility that you have to the plant and its risk?

14 A. Yes, we did.

15 Q. Okay. Is that the type of situation that's
16 ordinarily done by other farmers in your market?

17 A. There are dairymen that have taken those types of
18 precautions. The extreme probably is not the normal in the
19 industry, but it is -- I can't sit here and say that nobody
20 else is taking those precautions.

21 Q. But your protocol in dumping the milk right there
22 at that milking facility, --

23 A. Uh-huh.

24 Q. -- separate milk -- that is not ordinarily done?

25 A. No.

1 Q. It can be, but it's -- not -- it's not ordinarily
2 done?

3 A. Correct.

4 Q. And one of the decisions you did that for is
5 because the fact you are a producer/handler?

6 A. That is correct.

7 Q. Ever had situations in operating your herd where
8 you said there are some things that are out of your control
9 in terms of feeding or the production of cattle, right, in
10 the --

11 A. Correct.

12 Q. And if you ever had a situation in those things
13 where things happen you couldn't understand and it was
14 reducing the volume?

15 A. Yes.

16 Q. Has that had -- have you gotten any phone calls
17 from the plant, being upset about that?

18 A. Yes.

19 Q. Has there been significant drops as a result of
20 that?

21 A. There has been in my terms with Edaleen.

22 Q. And I'm not going to talk about what happens to --

23 A. No, please.

24 Q. And, of course, it was your fault, right?

25 A. Oh, yeah.

1 Q. But in terms of -- at the plant, where changes had
2 to be done with the customers and some of the deliveries in
3 response to that?

4 A. Yes, there was.

5 Q. And did some of those come with some extra costs?

6 A. Absolutely. And cost of customers even, in some
7 situations. I mean, we have experienced where on Saturdays
8 where the -- we'll have customers in the store waiting for
9 the milk to get processed so that we could bring it to them
10 for their purchases, double deliveries for routes, just
11 trying to keep these customers happy and understanding that
12 we had a situation at the dairy, and try to -- all means, try
13 to keep them as customers. They're valuable to us, but
14 there's definitely additional costs into doing that.

15 Q. Now, you've indicated you've had some growth on the
16 farm, and right now you're stymied. You'd have to make a
17 major investment to do another growth, but do you have a view
18 as to whether continued growth of that farm is going to be
19 necessary for its viability?

20 A. In the '90s during those growths, there was the
21 three additional families that bought into the dairy. There
22 is a fourth member that is not a member of the dairy right
23 now that has the opportunity to buy into that dairy.
24 Depending on economics and customer base, yeah, I think there
25 would possibly be a situation where growth would be, become

1 appropriate, but there is nothing in the 12-month thing that
2 has -- that we do see to expand.

3 Q. So putting a cap or a limit even at your current
4 level production would have an impact on your ability to
5 absorb other family members into your operation?

6 A. Yes, it would.

7 Q. What about the growth and the size of the customers
8 you deal with? Are you seeing anything there?

9 A. Yes, as the previous testimonies, you know, the
10 industry's always changing. The box stores now are the
11 biggest growing portion of the retail industry, and as the
12 class one purchases change, you know, the customers change
13 also. And there will be, I would assume, situations coming
14 that we will have to adapt to that also.

15 Q. And what about the efficiencies at the farm, do you
16 think that that has now plateaued, and that there will be no
17 -- your competitors will not longer ever seek efficiencies in
18 their production?

19 A. Put that question again --

20 Q. Well, it was not a very well stated --

21 A. Okay.

22 Q. -- question, was it? I'll withdraw. We'll start
23 it again.

24 A. I went two directions (indiscernible)

25 Q. Is there a trend in the management of farms to

1 continue to exact what they sometimes refer, greater
2 efficiencies at the farm?

3 A. Yes.

4 Q. And what is the primary technique used to reduce,
5 or to increase the efficiency at a farm?

6 A. Maximize your capital investment.

7 Q. And how do you do that?

8 A. Run your facilities at their maximum capacity.

9 Q. And then at some point if that facility at maximum
10 capacity isn't efficient enough, you have to expand it?

11 A. That would be correct. That would be one option.

12 Q. And is that not really the trend in all dairy farms
13 that are surviving and moving on as --

14 A. Yes.

15 Q. -- as an expansion?

16 A. Yes.

17 Q. And do you see the idea that at some point -- I
18 mean, do you see yourself plateauing at your production for a
19 long term as it stands now?

20 A. Environmentally, yeah.

21 Q. But at some point you may have to look at another

22 --

23 A. Yes.

24 Q. -- options, right?

25 A. Absolutely.

1 Q. And one final issue just to try to get on point. I
2 don't want to know the specific volume that you have at the
3 farm, because of it's confidentiality, but if the amount of
4 three million pounds were used as a cap, --

5 A. Yes.

6 Q. -- for class one sales, --

7 A. Yes.

8 Q. -- would that affect Edaleen Dairy?

9 A. Yes, it would.

10 Q. And that would make you unregulated, or it'd make
11 you fully regulated, subject to the minimum prices?

12 A. That is correct.

13 MR. YALE: I have no other questions, Your Honor.

14 THE COURT: Thank you, Mr. Yale.

15 Who would like to -- go ahead, Mr. Beshore.

16 EXAMINATION

17 BY MR. BESHORE:

18 Q. Marvin Beshore for Dairy Farmers of America.

19 Is it Heerspink?

20 A. Yeah.

21 Q. Am I close?

22 A. Yeah, you got it.

23 Q. Mr. Heerspink, a number of us here grew up on dairy
24 farms. I'm sure mine back in Pennsylvania was smaller than
25 the one you grew up in this region. How -- what size was the

1 farm where you were raised here?

2 A. 100 cows.

3 Q. 100 cows. We were even under that.

4 Were you -- of course, it wasn't a
5 producer/handler, you were a coop member there?

6 A. That is correct.

7 Q. Okay. Were you involved in 4-H as you grew up?

8 A. Yes, I was.

9 Q. Show your cows --

10 A. Yes, I did.

11 Q. Okay. And other pedigrees?

12 A. Yes, I did.

13 Q. Do their sires?

14 A. Yeah.

15 Q. Pick the sires?

16 A. No. That's dad's job.

17 Q. Okay. That's your job now though.

18 A. Yes, it is.

19 Q. Okay. when you're producing on a -- you know, for
20 the pool, it's a member of coop, one of the things you want
21 to do -- well, you cage paid incrementally for more butterfat
22 than milk, correct?

23 A. That is correct.

24 Q. Okay. So, you know, you're looking for, to
25 increase that paycheck, you want to hire a butterfat test as

1 well as hire milk production generally, correct?

2 A. Okay. And you can select sires for that? Some
3 sires are high test and some are lower tests?

4 A. Yes, you can do that in addition to breeds also.

5 Q. In addition to breeds. Okay. By the way, what
6 breed was the farm where you grew up?

7 A. Holstein.

8 Q. Okay. What breed --]

9 A. Holstein that.

10 Q. All Holstein.

11 Q. Okay. Well that's -- we got something in common
12 anyway.

13 A. Okay.

14 Q. The -- so within holstein breed, genetics and the
15 sires, there's a range of butterfat level that you know
16 predictably you will get from those genetics?

17 A. Incrementally, yeah.

18 Q. Incrementally?

19 A. Yeah.

20 Q. Right. Now -- and of course when you're producing
21 for the pool, more butterfat, more money, correct?

22 A. Yes.

23 Q. Okay. But when you're producing for your supply at
24 a -- for fluid milk supply as you've testified to Mr. Yale,

25 --

1 A. Uh-huh.

2 Q. -- butterfat's excess a lot of times because the
3 fluid milk supply -- fluid milk drinks want less fat, not
4 more?

5 A. There is situations where butterfat is of excess,
6 yes.

7 Q. Okay. Well, in general -- what's the average you
8 produce whole fat -- I mean, whole milk, I assume --

9 A. That is correct.

10 Q. And two percent?

11 A. That is correct.

12 Q. Skim milk?

13 A. Yes.

14 Q. Okay. But the average production in a butterfat
15 for all cows in the market, according to the market
16 administrator is 3.57 percent.

17 A. Okay.

18 Q. Okay. What's your average butterfat at your farm?

19 A. 3.5.

20 Q. 3.5. Now, what's your average fluid milk -- the
21 average test of the fluid milk products that you sell?

22 A. Whatever the standards are for those product lines
23 that we're selling.

24 Q. Okay. But now -- but I'm talking about average,
25 all of them together.

1 A. I would not know that.

2 Q. Okay. So you're -- now, let me make sure I
3 understand. You're responsible for providing the raw product
4 to your plant?

5 A. That is correct.

6 Q. Okay. Because you're the farm manager.

7 A. That is correct.

8 Q. And you don't know what the butterfat requirements
9 are at your plant for the products it sells on average?

10 A. I can't honestly say I know what the exact ranges
11 are for a two percent milk. I mean, two percent, I -- for me
12 is two percent, but whether the USDA allows it to be 1.8 to
13 2.2, I don't know about that --

14 Q. Oh, okay. Maybe I didn't say my question right.

15 A. Okay.

16 Q. Okay. My question is, do you know what the
17 average, you know, the blended butterfat level of all the
18 fluid milk products at Edaleen Dairy --

19 A. I do not know that.

20 Q. Okay. So your plant has never told you that, you
21 know, if all things were right, what we need is an average
22 two percent butterfat --

23 A. No, they have not told me that.

24 Q. Okay. Is producing excess butterfat a profitable
25 -- or an excess cream, is that a profitable line for Edaleen

1 Dairy? Selling the excess cream, I should say. Is that a
2 profitable line?

3 A. I do not know that either.

4 Q. You don't whether it's a good sale or --

5 A. No, I don't. No.

6 Q. If it's not a good sale --

7 A. Well, let me restate that. Any sale is going to be
8 better than putting it down the drain.

9 Q. Got you.

10 A. Okay.

11 Q. But it's probably not as good as putting in the
12 bottle?

13 A. That -- I don't know that either. I mean, --

14 Q. You're not sure?

15 A. Drain versus bottle?

16 Q. No, no, no, no.

17 A. Okay.

18 Q. Selling the excess cream. By the way, do you know
19 where you sell your excess cream?

20 A. No, I do not.

21 Q. Okay. So you don't know whether you get as much
22 revenue per unit for that sale of excess cream as you do if
23 you run it through your plant and put it in your package
24 fluid milk --

25 A. No, --

1 Q. -- products and sell it?

2 A. -- I do not know that.

3 Q. Okay. Do you -- you've got a 3.5 average at the
4 herd there. If your mix of fluid sales is market average,
5 and in the market, it averages about two percent. Let's --

6 A. Okay.

7 Q. That's what the market administrators show.

8 A. I can take your word for it.

9 Q. Okay. Do you think you're about market average
10 sales at two percent/one percent scale?

11 A. I would not know that.

12 Q. Have you, in your breeding strategies, at Edaleen,
13 have you bred for cattle genetically that would produce a
14 lower level of butterfat?

15 A. No, I have not pursued that.

16 Q. Okay. If you assume with me that sales of excess
17 cream are not profitable, better than pouring it down the
18 drain, --

19 A. Okay.

20 Q. -- but not as good --

21 A. Uh-huh.

22 Q. -- as putting the volume in your fluid milk
23 products, --

24 A. That is correct.

25 Q. -- it would be a good strategy to have less excess

1 cream produced at your farm, wouldn't it?

2 A. I lost you. Go again, just --

3 Q. If the extra --

4 A. We put too many things in order there.

5 Q. If the additional butterfat --

6 A. Yeah.

7 Q. -- has a value that's less than what you need for
8 your products, for your fluid milk products at the plant, --

9 A. Okay.

10 Q. Okay.

11 A. Now, we're assuming that I'm getting additional
12 milk with less butterfat, is --

13 Q. I'm assuming you've got less aggregate butterfat --
14 less total pounds of butterfat produced.

15 A. Okay.

16 Q. Now, let me say it. I'm assuming that you're
17 producing -- that you'll have too much butterfat, too many
18 pounds of butterfat --

19 A. Right.

20 Q. -- in the farm milk, in the raw milk --

21 A. Okay.

22 Q. -- for what you need in your finished product.

23 A. Okay.

24 Q. Okay.

25 A. So we got 3.5 going into two percent?

1 Q. Right.

2 A. Okay.

3 Q. Okay. And I'm assuming that selling off that
4 cream, that extra butterfat, --

5 A. Uh-huh.

6 Q. -- is not as profitable as putting the rest of it
7 in a bottle.

8 A. I would not know that.

9 Q. You don't know that?

10 A. No.

11 Q. But if you assume it's not as profitable, okay,
12 that you get less per pound for that cream, for that
13 butterfat sold as excess cream, less per pound than when its
14 sold in your class one products. Okay?

15 A. Okay.

16 Q. You assume that's less valuable. A strategy might
17 be to have less of it produced by your cows. Fair enough?

18 A. That's not -- let's make sure I'm understanding
19 your question. I've got -- let's just do one gallon. Okay?
20 I got a gallon of 3.5 milk, and the customer wants a gallon
21 of two percent milk, right?

22 Q. Right.

23 A. Okay.

24 Q. Right.

25 A. There is going to be a portion of that butterfat

1 removed.

2 Q. Right.

3 A. Okay. Now you're trying to ask whether selling
4 that gallon of two percent milk --

5 Q. Whether you get more per pound for the butterfat in
6 the two percent than you do in what's sold off.

7 A. And like I told you earlier, I don't know that.

8 Q. Okay. Okay. That's fair.

9 How many cows do you milk?

10 A. That would be proprietary.

11 Q. Okay. You testified that the average -- your
12 average production was greater than the average production
13 information that Dr. Smith used, correct?

14 A. That is correct.

15 Q. And you're referring there to the 20,000 pounds per
16 cow average he used?

17 A. That is correct.

18 Q. Okay. So your average production is more than
19 20,000 per cow --

20 A. Yes, it is.

21 Q. Okay. Is it more than 25,000 per cow per year?

22 A. It is more than the average that was stated in Mr.
23 Smith's testimony.

24 Q. It's more than 20,000?

25 A. Yes.

1 Q. Okay. Is it more than 21,000?

2 A. Proprietary.

3 Q. You have 35 employees at the farm. You said about
4 two thirds of them are minorities. By the way, that's not
5 unique to your --

6 A. No, that would not be.

7 Q. Okay. It's throughout the area. In larger farms,
8 it's very common for there to be Hispanic or other minority
9 employees on farms?

10 A. That's correct.

11 Q. Pool farms and producer/handlers?

12 A. That is correct.

13 Q. Okay. Now, the information that you provided Mr.
14 Yale with respect to accounts, you know, losses of accounts,
15 gains of accounts and what not, --

16 A. Uh-huh.

17 Q. -- that's not part of your responsibilities in the
18 business, but you gathered that information from other
19 persons, I take it?

20 A. It is not my direct responsibility to be talking to
21 these accountants, but I am sharing the responsibility being
22 a part owner --

23 Q. Okay.

24 A. -- of losing these accounts, yes.

25 Q. Do you share in any of the responsibility of

1 establishing prices for your fluid milk products?

2 A. No, I do not.

3 Q. Okay. Do you know how those prices are set when
4 you're selling to Starbucks or anybody else?

5 A. Somewhat.

6 Q. Okay. How's that done?

7 A. We look at a multitude of factors, what it cost us
8 from getting that gallon to the dock, and then locating the
9 particular customer to where he is, and -- relative to our
10 processing place, and look at the industry as who we're
11 competing against and where the federal milk market orders
12 prices are historically been and where the trends may be
13 going, and try to adjust our price to accordingly.

14 Q. Okay. What federal milk order prices do you look
15 at?

16 A. The class one louvre (phon.).

17 Q. You indicated that your cost of production -- do
18 you know the cost of production per hundredweight at your
19 farm?

20 A. Yes, I do.

21 Q. Okay. What is it?

22 A. Proprietary.

23 Q. Okay. It's -- you indicated you didn't agree with
24 the -- the USDA -- by the way, the data that Dr. Smith
25 depicted and testified about was -- you understand that was

1 US -- United States Department of Agriculture data?

2 A. Yes, I do.

3 Q. Okay. Your -- is it your testimony that your costs
4 are greater than the costs in some of that data?

5 A. Yes.

6 Q. Okay. Do you -- which -- you're in the 500 plus
7 cow category, I assume?

8 A. Yes, I am.

9 Q. Okay. Now, the graph showed a range of costs --

10 A. Uh-huh.

11 Q. -- for the 500 plus cow category, and they showed
12 -- there were actually two lines on the graphs. Did you
13 notice that?

14 A. Yes, but I have not looked at it today, so --

15 Q. Okay. Well, I just wondered --

16 A. -- detail with me. I'm --

17 Q. Since the graph showed a range of costs --

18 A. Okay.

19 Q. -- okay, which costs were you higher than, all of
20 them?

21 A. I think there was a bar in there that identified
22 it, 10 -- approximately a 10.50 cost per hundredweight
23 average.

24 Q. Okay.

25 A. That's the dollar I'm -- figure I'm referring to.

1 Q. Okay. You were greater than 10.50?

2 A. That is correct.

3 Q. Per hundredweight. Okay.

4 Would you assume that your costs of production at
5 your farm are similar to the costs at other farms of your
6 size in the state of Washington?

7 A. I've never been privy to that information.

8 Q. You don't know?

9 A. I'm -- no.

10 Q. Okay. Well, is there any reason to think that they
11 would be substantially greater than the cost of any other
12 farms of similar size?

13 A. Just in the fact that that's the lowest number I've
14 seen for a median cost of production in cumulative reports
15 that I've seen in the private sector.

16 Q. Okay. You referred to some reports from an
17 accounting firm?

18 A. And I certainly could've misquoted that. I get a
19 mailing from --

20 Q. Okay.

21 A. -- an accounting company, and that has clients in
22 the Pacific Northwest, and that's the one I was referring to,
23 and I don't have access to know what the official title of
24 that document is.

25 Q. Okay. Is that the 10.50 number you're referring

1 to? What was the 10.50 number in that --

2 A. Is -- no, no, --

3 Q. Okay.

4 A. -- I'm saying the number that I recall from there
5 was higher than the 10.50.

6 Q. Okay. What about your -- is your own number higher
7 than the 10.50?

8 A. Yes, it is.

9 Q. Okay. Is your own number approximately what you
10 saw in the number in this accounting newsletter?

11 A. That's proprietary.

12 Q. What was the number that you saw in the accounting
13 newsletter?

14 A. The number I'm recalling was in the 11.70 range.

15 Q. Okay. What period of time was that?

16 A. In the 2000s. Whether it was 2001, 2002, I.

17 Q. Okay. And you understood that to be a number that
18 reflected the costs of an -- on a number of dairies in this,
19 what, Pacific Northwest?

20 A. That is correct.

21 Q. Okay. Were they dairies of similar size to yours?

22 A. I do not recall.

23 Q. Okay. Now, you've talked about -- Mr. Yale asked
24 you questions about how you handle milk that's -- or, cows --
25 how you handle cows and their milk production when they're

1 treated --

2 A. With antibiotics, yeah.

3 Q. -- with antibiotics. Okay. And you segregate
4 them.

5 A. Uh-huh.

6 Q. By the way, something was made of your not using
7 that milk or making sure it was disposed of immediately.
8 That milk is not usable -- when the cows have been treated
9 with antibiotics, it's not usable for commercial use, period;
10 is that correct?

11 A. That is correct.

12 Q. Whether it's your farm or any other farmer's farm
13 in the United States of America, correct?

14 A. That's correct, yeah.

15 Q. Okay. So that, you know, the fact that you pour it
16 down the drain, --

17 A. Uh-huh.

18 Q. -- that's what everybody does or feeds it to
19 calves, I suppose.

20 A. Okay. They are. I was going to say, there is a
21 lot of dairies that would feed that to calves.

22 Q. Okay. But you don't use it for calf feed?

23 A. We have made the decision that we don't want -- do
24 not want it stored in any capacity anyway to risk any chance
25 of it ever getting cross-contaminated.

1 Q. Okay. So --

2 A. That's the point I was trying to make in that.

3 Q. Okay.

4 A. Yeah.

5 Q. You could use it for calf feed, but you decided
6 that might be risky --

7 A. That is correct.

8 Q. -- because why? Why -- what's the risk in that?
9 One of your employees might pour it in the milk tank instead
10 of --

11 A. Yeah, if it's in a five gallon bucket and some guy
12 walks off to the other production facility and happens to
13 spill it, I mean, there's a -- I mean, a bird could fly away
14 with it. I just don't want that chance.

15 Q. Okay. That's fair. Now, the risk that you have in
16 terms of antibiotic contamination of a -- of bulk tank,
17 you've eliminated that risk by sequestering the cows --

18 A. We've reduced our risk, yes.

19 Q. Reduced the risk. Okay. Do you somehow understand
20 that if another farmer -- if a farmer who's not a
21 producer/handler --

22 A. Uh-huh.

23 Q. -- infects, you know, markets -- attempts to market
24 antibiotic-contaminated milk that that farmer's not
25 responsible for that milk --

1 A. I -- now, I don't have any factual data to see
2 contracts, but from what I understand, the industry would
3 make that farm responsible either financially or in --

4 Q. He might lose --

5 A. -- financially and physically, --

6 Q. Yeah.

7 A. -- return the back -- milk back to his farm.

8 Q. He's going to have to dispose of that tanker load
9 of milk instead of just --

10 A. That is correct. Right.

11 Q. -- bulk tank, and he's going to --

12 A. The point that we were leading to is that we do not
13 have the ability to order up another tanker load --

14 Q. Okay.

15 A. -- off our dairy to provide the plant for that day.

16 Q. Okay. Now, so you make sure you don't have that
17 problem?

18 A. We try to reduce that risk.

19 Q. Well, have your employees ever contaminated the
20 tank with milk, even though the cows were sequestered and
21 segregated when they're treated?

22 A. It has not happened recently, no.

23 Q. Today can you tell us what portion of your -- the
24 production at Edaleen Dairies is not sold as fluid milk
25 products?

1 A. You asked me what our class one utilization is?

2 Q. That's a much better way of --

3 A. Uh-huh.

4 Q. -- stating it, yes.

5 A. I don't know that exact figure.

6 Q. Okay. Do you know the approximate figure?

7 A. It would be higher than the market order, it's
8 average.

9 Q. Okay. And the market order average, do you know
10 what that is?

11 A. It's in the low 30 percents.

12 Q. Okay. So it's better than 30 percent?

13 A. That's correct.

14 Q. Okay. It's better than 50 percent?

15 A. That -- yes, it would be.

16 Q. Better than 70 percent?

17 A. That's -- you're getting proprietary.

18 Q. What's -- well, why -- what's the sensitivity to
19 that, can you tell me?

20 A. Because there's competition in the room, and --

21 Q. And, so what?

22 A. If they were to know what my product --

23 MR. UNIDENTIFIED: Objection, Your Honor.

24 MR. YALE: Objection. He does not have to explain
25 why it's proprietary. He says it's proprietary --

1 THE COURT: He can answer the question if he wants
2 to. He asked a question. He doesn't have --

3 MR. YALE: I think the line of --

4 MR. BESHORE: I think that's fair. I mean, I'm not
5 -- I think it's fair, Ben. If it's -- the class one
6 utilization is --

7 THE COURT: If he wants to say why he thinks it's
8 proprietary then he's entitled to explain it. He's entitled
9 to ask the question.

10 MR. UNIDENTIFIED: Or he can say that that's
11 proprietary.

12 THE COURT: Well, he could, but he didn't. He
13 decided to answer the question, so you may finish your
14 answering the question if you want to.

15 THE WITNESS: I don't feel that that's information
16 that is absolutely necessary to these proceedings. That
17 would give my competitors information I don't feel is
18 necessary.

19 Q. Okay. But the extent to which you -- you have made
20 a point, you and the others that are represented by Mr. Yale,
21 Mr. Ricciardi, you made a point of the difficulty or costs
22 associated with marketing the non-class one utilization.

23 A. That is correct.

24 Q. Okay. Wouldn't it be important for the secretary
25 to know what proportion of your volume that might be?

1 A. Well, how about we reverse the situation, and I'll
2 answer that I do not have 100 percent cost going to
3 utilization?

4 Q. Okay. And what proportion do you have?

5 MR. UNIDENTIFIED: Your Honor, he's already said
6 that it's proprietary. I think --

7 THE COURT: Okay. He's saying --

8 MR. BESHORE: Proprietary.

9 THE COURT: Okay. That's the answer that we have.
10 I can't order him to answer --

11 Q. I understand, and I don't -- I certainly respect
12 the proprietary nature. I don't frankly understand what's
13 sensitive about that percentage, but I'll leave it at that.

14 MR. UNIDENTIFIED: Your Honor, may I
15 (indiscernible) the hour, you know, is getting late. I mean,
16 we've been here for an hour and a half, two hours. I mean,
17 is this a situation with the change that we could begin
18 tomorrow morning with this witness?

19 THE COURT: I have no objection to calling it a
20 night at this point. We've gone until a quarter of 7:00.

21 MR. UNIDENTIFIED: Right. (Indiscernible) for another
22 four days, I mean, it's scheduled. I mean, it's --

23 THE COURT: I know. I just want to make sure we
24 get done in those 4 days. I don't want to have another --

25 MR. UNIDENTIFIED: I understand (indiscernible) the

1 problem is, I think we're -- and maybe I'm even kind of
2 certain of it, this exhaustion and these things. I mean
3 (indiscernible) unproductive, and I think this would be --

4 THE COURT: Well, plus they're bugging us to leave
5 the room at the hotel, too, so I'll call it a day, but I
6 would like to go to about this time tomorrow night as well,
7 7:00 o'clock or so.

8 MR. UNIDENTIFIED: We're going to cooperate --

9 THE COURT: So we'll start at 8:30 tomorrow.

10 MS. DESKINS: And Judge? Judge Hillson, can you
11 remind people we're not going to be in this room, we'll be
12 across the hall.

13 THE COURT: Yeah, sure. I think you just did.

14 MS. DESKINS: Okay. We'll be in another room
15 across from here.

16 (Whereupon, the proceedings were recessed at 7:00 p.m.)

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