Before the Secretary
United States Department of Agriculture
Washington, D.C.

Hops Produced in Washington, Oregon, Idaho and California; Hearing on Proposed Marketing Agreement and Order No. 991	Docket AO-F&V-991-A3; FV03-991-01

Post-Hearing Comments and Proposed Findings and Conclusions of the Hop Marketing Order Opposition Group

Introduction.

This proceeding for the development of an Order imposing producer allotments on the U.S. hops industry must be terminated on the basis of the testimony and exhibits presented at the hearing held in Portland, OR., October 15-17, 2003, and continued in Yakima, WA., October 20-24, 2003. Proponents have not demonstrated: that the industry, most recently deregulated in 1986, is beset by any form of disorderly marketing conditions, dysfunctional or failed markets, or extreme or unreasonable fluctuations in supplies and prices; or that re-regulation of the industry by imposing producer allotments will achieve the objectives of the AMAA. Indeed, a new Order would spell economic ruin for the U.S. industry by

obstructing and frustrating multi-year contracts, imposing inequitable burdens on innovative and efficient producers who would be forced by buy or lease allotments, and causing a reduction of long-run revenue and market share. The industry is evenly divided and utterly lacking the consensus necessary to implement and fairly administer an Order containing such a draconian supply control regime. Imposing excessive stability on a well-function unregulated market is contrary to the AMAA which forbids imposing supply controls on a market characterized by "reasonable" supply and price fluctuations. Common sense, empirical observations, and economic analysis demonstrate that the market for U.S. hops is relatively elastic (given the relatively low market share of U.S. hops with respect to total world production and the globalization of the market for alpha acid), meaning that any use of supply controls will reduce revenue and invite the further expansion of foreign production. It is axiomatic, and no doubt evident to high school economics students, that you can't cartelize a market unless you control substantially all production and entry. Several Order provisions, such as the definitions for handle, are simply too undefined and vague to be implemented on this record. Several provisions, for example, authorizing the sale or lease of allotment, and "bumps" for aroma hops, are unlawful in violation of the "uniform rule" and "equity" limitations in § 608c(6)(B).

Proponents are to commended for their efforts to deal constructively with the "problems" brought about by recent changes in the industry, and for presenting heartfelt and sincere testimony about the present state of the industry and the need for an Order. USDA must, with all respect, be condemned. The Order, if adopted as proposed will consign the industry to lower revenue, declining market share, and a tedious regulatory treadmill that cannot work. The industry will be mired in controversy for years given the severe inequities in the base allotments and in endless frustrating debates about implementing rules and regulations, desirable saleable and carryouts, etc. The present lack of consensus will be exacerbated and made permanent as growers who perceive themselves as winners and losers compete for control over industry decisionmaking. Secrecy, jealousy, the same type of greed that ultimately destroyed the old Order, and growing concerns over compliance and enforcement will exacerbate the uncertainty of losing control over one's economic destiny to the morass of collective decisionmaking. The industry will become increasingly obsessed with a myriad of efforts to "game" the system to the advantage of a particular firm or group, at the expense of energy and resources devoted to innovation and competition with foreign producers. The cooperation and cohesion, not to mention the "espri de corps" in this extremely close knit group of growers and families, will be replaced by years of often bitter

controversy and seemingly endless litigation given the very high stakes. USDA well knows that a very high degree of consensus is essential to operate a producer allotment program efficiently and fairly, utterly absent here with this evenly divided industry. With its vast legal and economic "expertise," USDA should have counseled the proponents at the outset that a producer allotment program cannot work and is doomed to fail given the present industry structure and dynamic global market. The mere pendency of this proceeding creates market uncertainty and may delay some industry participants from making decisions appropriate for their own unique economic circumstances.

I. The Industry Lacks the Consensus Essential to Fair and Effective Implementation of a Producer Allotment Program.

Proponents failed to demonstrate the industry consensus needed to justify promulgation of the Order, a required finding under the AMAA. The Order is supported by what is in reality a narrow segment of the industry, basically Yakima Chief and a few Washington growers. Outside of the Proponents Committee, there were no Idaho growers who testified in favor of the Order, no California growers who testified in favor of the Order; one Oregon grower who testified in favor; and only six Washington growers who testified in favor. On the opponents side, the entire state of Idaho testified in opposition to the Order; five Oregon

growers testified in opposition (including a representative speaking for the remainder of the Oregon growers), and seven Washington growers testified in opposition. More growers in each state testified in opposition to the Order than testified in favor of it.

Since the record demonstrates that approximately 50% of producers oppose the Order, this promulgation proceeding should be terminated at this time in order to save resources of the parties and USDA and to end the uncertainty surrounding the possible establishment of a state or federal program. Such regulatory uncertainty has possibly delayed producer decisions, e.g., to exit the industry and/or to make new investments.

USDA has cited the need for industry consensus as a necessary element of an effective marketing order, especially one that uses the rigid supply management tool of producer allotments. Indeed, the lack of consensus was cited by USDA as an additional reason to terminate the old Order, even without the suspended supply control provisions, if only to give the industry time to agree on some new regulatory tools:

> The provisions of the referendum order specified that approval by two-thirds of those voting, or by a majority of producers voting who represented two-thirds of the production volume voted, would be needed to confirm producer support for continuation. The referendum was held as announced. Eighty-three percent of all hop growers (by number and volume of production) participated in the

> referendum. Of those voting, 56 percent of the growers, representing 53 percent of the production volume during a specified representative period, favored continuance of the hop marketing order. Given the high level of grower participation, the results are a reliable indicator of grower sentiment, and clearly demonstrate that a significant portion of the producers do not favor continuation of the hop order. In the absence of substantial industry support, marketing order operations tend to be less effective. Experience in similar circumstances indicates that it often becomes difficult for marketing order committees to obtain the requisite majority of votes necessary to approve recommendations for implementing order authorities. Moreover, a committee may experience difficulty in obtaining compliance with order requirements from all handlers in such a circumstance. Such lack of effectiveness is recognized in the act in connection with the provisions for the adoption of new marketing orders and amendments to existing orders, which require that the Secretary determine that the issuance or amendment of an order is favored by two-thirds of the producers voting or by producers representing two-thirds of the volume of production. Given the demonstrated lack of producer support for the hop order and consistent with the intent of the Act, it is determined that it is no longer possible to achieve the objectives of the program.

51 Fed. Reg. 32779 (Sept. 16, 1986) (emphasis added). The 56% that favored continuation of the old Order (without supply controls) is greater than the level of support demonstrated on the record for the proposed new Order with its highly controversial supply controls.

II. There is No Justification to Repeat the Mistakes of the Past.

Reimposing an Order that contains essentially the same defects that led to the termination of the old Order cannot be justified. All of the innovations,

structural changes, and adjustments the industry has undergone since deregulation favor continued reliance on market forces rather than a return to the rigid rules and supply controls that failed in three previous Orders. USDA called for proposals to amend the old Order, focusing on eliminating barriers to entry:

> Considerable controversy has existed within the domestic hop industry for several years on matters relating to Marketing Order No. 991 for hops of domestic production, primarily in regard to entry of new producers and the ability of existing hop producers to expand their operations. The controversy has been of such magnitude and duration that an amendment of the order may be necessary. Accordingly, USDA now is soliciting amendatory proposals to be included in a notice of hearing, and especially proposals to eliminate entry barriers and to limit transfer of allotment base by producers.

49 Fed. Reg. 1380 (Jan. , 1984).

HAC conceded that it had badly mismanaged the process of developing its annual marketing policies and that the saleable percentage was being set, and regulatory requirements waived, without regard to actual market conditions, but instead solely to cater to conflicting demands within the industry for the "right" to sell hops:

> The HAC recommended waiving the bona fide effort requirement for the 1984-85 marketing year because it concluded that its implementation would result in additional and unneeded production. Currently, the hop market is inactive and an oversupply of hops exists, and enforcement of the bona fide effort requirement for the 1984-85 marketing year could further depress the market.
> All four producers in opposition to the marketing policy contained in the notice objected to establishing an allotment percentage of 115

percent and three wanted the allotment percentage to be 130 percent. The basis for their objection to this allotment percentage was: (1) That the HAC had promised producers in a meeting held in October 1980, that the allotment percentage would be held at 130 percent through the 1984-85 marketing year: (2) that setting the allotment percentage at 115 percent would increase the value of allotment base and especially leased base; and (3) that such action would encourage an increased transfer of allotment bases among producers. Another alternative recommendation made by the four producers was for the suspension of all volume regulations for the 1984-85 marketing year. The four producers also commented on other issues not related to marketing policy but rather the amendment of the order.

Notice was published in the Federal Register (49 FR 1380) January 11, 1984, inviting interested persons to submit proposals by March 12, 1984, to amend the order. That time was extended to April 10, 1984 (49 FR 9740). The actions contained in this final rule are independent of that action and should not be considered to establish any precedent for actions taken in subsequent marketing years. Any findings and conclusions on proposals to amend the hop marketing order will be based on the record compiled at public hearings in the formal rulemaking proceedings.

All of the objections to the proposed marketing policy are denied because marketing conditions have changed considerably since the HAC's marketing policy meeting in 1980. The hop market is depressed by an oversupply of hops, diminishing demand, and current inactivity. It would be inappropriate to establish a marketing policy (whether in the form of a 130 percent allotment percentage or suspension of volume regulation) that promotes a high level of production in view of current market conditions. The recommended salable quantity is still higher than actual market needs but it endeavors to accommodate producers who are contracted at high levels, while attempting to adjust production to market needs. Because of these current marketing conditions, the recommended allotment percentage should not have a significant effect on the value or transfer of allotment base.

49 Fed. Reg. 18813 (May 3, 1984). USDA announced an amendment hearing to

consider 31 proposals, from minor procedural changes to a complete deregulation of the hop industry. 49 Fed. Reg. 18862 (May 3, 1984).

The Secretary terminated the Order based upon the hearing record, finding that it obstructed and no longer tended to effectuate the policy of the AMAA. 7 U.S.C. § 608c(16)(A). The termination notice explained:

> The salable quantity recommended for the past several years has not accurately reflected market needs but rather has attempted to prevent the allotment percentages from cutting across the contracts producers have with dealers and to keep the price of leased base at reasonable levels. This has resulted in actions by producers that are outside of the order's purpose such as the leasing of allotment base to other producers, and has caused considerable controversy both within and outside the hop industry over certain provisions of the current program. Moreover, the order restricts entry so that producers who did not receive allotment base when the order was issued in 1966 had to either inherit, purchase, or lease allotment base in order to market hops.

50 Fed. Reg. 26977 (July 1, 1985). The decision foretold the slow decline in hop acreage and increasing yields as newer high-alpha varieties were deployed:

> Total hop acreage in the U.S. is expected to decline over the next several years as newer high alpha acid varieties replace some of the older varieties. Yields per acre in the U.S. have been trending upward from an average of approximately 1,600 pounds in the 1950's to 1,900 pounds in the 1980's. Most other hop producing countries have not increased yields, probably because irrigation is not used to the extent that it is in the U.S.
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> If this trend of changing to higher alpha varieties and increasing yields continues and beer production remains constant, the acreage required to provide the quantity of hops needed by brewers will decline, necessitating further adjustments by producers in

acreage planted to hops.

Id. The decision went on to explain that the substantial entry barriers imposed by the base system and the manner in which the Order was administered (waiver of "bona fide effort" requirement and failure to issue significant additional allotment) led to trafficking (lease and purchase) in allotment:

> Because of the "base" allotment system, there is a substantial barrier to entry by new producers. The current order provides for allotment bases which are the foundation for determining the market share allocated to each producer. The allotment bases in the current order are still based upon the quantity of hops producers sold during the years 1962-65.
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> The "bona fide" effort requirement in the order currently prescribes that the right of each producer to retain all or part of his order allotment base depends on his continuing to make a bona fide effort to produce his annual allotment, and failing to do so, his allotment base must be reduced by an amount equivalent to the unproduced portion. The "bona fide" effort requirement has failed in its goal of assuring that allotment holders are genuine producers. Although the order requires a bona fide effort to produce the full allotment, the *26978 requirement has been waived for the last several years.
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> Entry of new producers has been severely restricted because additional allotment base was not issued. When the order became effective in 1966, a total of 59,270,000 pounds of allotment base was issued to producers who had a sales history during the representative period 1962-65. Since that initial issuance, virtually no additional allotment base has been issued. Instead of issuing additional base, the increased demand has been met by adjusting allotment percentages and salable quantities. In 1980, for example, the need for additional hop marketing was met by increasing the annual allotment percentage to well over 100 percent of the total allotment base for 1981. The same action was also taken subsequent to 1981.
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> The order currently permits a producer to transfer all or part of

> an allotment base to another producer by notifying the HAC in writing of the transfer. Transfers of allotment base between producers have been relatively free of restrictions. As a result of the liberal transfer provisions, a secondary market has developed which focuses producer concern more on allotment base trading than on the production and marketing of hops. Since virtually no additional allotment base has been issued, available allotment base has become a scarce commodity commanding a high price. This activity in leasing and transferring allotment base, especially where new hop producers were concerned, has contributed to an overexpansion of hop production and hop producing facilities.

Id. at 26977-78. The decision explained that the conflict between one-year volume regulation under the Order and the "typical" 3-5 year contracts encouraged HAC to set saleable percentages to protect contracts but which contributed to an imbalance between supply and demand:

> There is a conflict between the order provision permitting only one-year volume regulation and contracting practices in the hop industry. The order provides that the HAC can recommend a volume regulation for only the following marketing year. However, the practice in the industry is for producers and handlers to contract for three to five years. This conflict has created serious problems for the industry and has resulted in the establishment of salable quantities in excess of market needs to allow producers to fulfill their contractual obligations. Since the Act was intended to eliminate such imbalances between supply and demand, the volume regulation recommendation provisions of the order have clearly failed.

Id. at 26978 (emphasis added). The decision concluded that the Order helped cause the supply-demand imbalance, the "poor" market for hops, and failed to correct these conditions:

> The purpose of marketing order programs normally is to provide a stable and orderly market environment which will tend to improve grower returns for the commodity involved. The hop marketing order now in effect has not achieved and maintained this market stability as evidenced by current market conditions. The market for hops is depressed. Prices in the spot and contract markets are at very low levels and frequently during the past few years have been below the average costs of production. Furthermore, there is little expectation that the prices producers receive for hops will improve over the next few years unless dramatic reductions in world hop production and supplies occur.
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> Brewers and handlers are overstocked with hops to the extent that they now hold about one and one-half year's brewing needs. This situation is further exacerbated by the lagging production and sales of beer which are not expected to show much improvement over the next few years. Contracting is practically non-existent. In fact in 1983, 1984, and 1985 many producers were offered incentives, such as extensions in their current contracts, and partial payment of their contracted prices not to deliver hops against those contracts. The only new contracts currently being negotiated are for specific varieties or with a few producers.
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> All of these market conditions developed while the marketing order was in full operation. However, the order did not function to correct the marketing conditions in a time of declining market demand. Furthermore, the order has not functioned so as to be responsive to changing market conditions and apparently was unable to adjust supply, even with its allotment provisions, to meet actual market needs. For these reasons, the order obstructs and has not effectuated the declared policy of the act.

Id.

Congress passed a special interest rider to an appropriations bill at the behest of "hops" Congressman Slade Gorton which had the effect of canceling the termination decision and reinstating the Order. The Secretary suspended the key

regulatory provisions of the Order for essentially the same reasons set forth in the July 11, 1985 termination decision:

> For the reasons set forth in the July 1, 1985, termination order, the Hop Marketing Order now in effect has not achieved the statutory purposes. The principal operative provisions of the order such as the base allotment system which determines the market share of hops allocated to each producer, the "bona fide" effort requirement, and the transfer provisions have clearly failed to achieve the marketing goals contemplated by the Act. Entry of new producers has been severely restricted, a secondary market has developed which focuses more on allotment base trading than on production and marketing, and there remains an imbalance between supply and demand. Therefore, since the order obstructs and does not tend to effectuate the declared policy of the Act, this suspension of the principal operative provisions is issued.

51 Fed. Reg. 4887 (Feb. 10, 1986). The Secretary simultaneously gave the 60-day notice to Congress of intent to terminate the entire Order, now required by an amendment to § 608c(16)(A) made by the Food Security Act of 1985. The industry was given yet another opportunity to achieve a consensus on Order provisions that addressed the fatal flaws cited in the termination decision:

> Subsequently, the Department afforded hop producers a 90-day period to develop and submit new order proposals if the producers agreed that a marketing order of some kind was desirable. The industry was advised that any such proposals had to address the deficiencies of the existing marketing order and conform with the act and USDA marketing order policy guidelines.

51 Fed. Reg. 27400 (July 31, 1986). The Secretary ultimately terminated the suspended volume control provisions "because they did not effectuate the declared

policy of the act" and ordered a continuance referendum August 11-23, 1986, to determine if the industry favored the Order without the volume control provisions:

> Simultaneously, for reasons set forth in both the July 1, 1985, and February 10, 1986, documents, USDA reaffirmed its conclusion that the Hop Marketing Order then in effect had not achieved the statutory purposes. Accordingly, the provisions of the order dealing with volume limitation, pooling, and transfers, and the related administrative rules and regulations were suspended in accordance with the act. USDA also notified the Congress that the Secretary intended to terminate the hop marketing order after the waiting period prescribed by the Food Security Act of 1985 had elapsed.
> The Hop Administrative Committee (HAC) polled industry members by questionnaire to determine whether they favored continuation of the order without the suspended volume control provisions. In that poll, a majority of the producers responding favored the continuation of such an order. Based on the poll results, the HAC submitted a resolution to the Department which in part proposed continuation of a marketing order and termination of the volume control provisions subject to an understanding that if in the future, industry members achieved agreement on revised volume controls consistent with the act and guidelines, a hearing would be held. Although by this order the Department continues the research and development, quality control and marketing information provisions, pending review of the results of the upcoming continuance referendum, this action should not be interpreted as a commitment to conduct a hearing in the future on a volume control proposal. Any such proposal will be judged on its own merits when submitted to the Department.
> For the reasons set forth in the July 1, 1985, termination order which were reaffirmed in the February 1986 suspension order, the suspended volume control provisions of the order, §§§§ 991.36 through 991.46, are terminated because those provisions do not tend to effectuate the declared policy of the act.

Id. The producer referendum failed to demonstrate the needed consensus, so the Order was terminated, again, effective October 31, 1986:

Because of the significant restructuring of the order which resulted from the termination of the provisions specified above, the August 1, 1986, order also announced a referendum to be held August 11-23, 1986, to ascertain whether growers favored continuance of the remaining order. The provisions of the referendum order specified that approval by two-thirds of those voting, or by a majority of producers voting who represented two-thirds of the production volume voted, would be needed to confirm producer support for continuation. The referendum was held as announced.
Eighty-three percent of all hop growers (by number and volume of production) participated in the referendum. Of those voting, 56 percent of the growers, representing 53 percent of the production volume during a specified representative period, favored continuance of the hop marketing order. Given the high level of grower participation, the results are a reliable indicator of grower sentiment, and clearly demonstrate that a significant portion of the producers do not favor continuation of the hop order. In the absence of substantial industry support, marketing order operations tend to be less effective. Experience in similar circumstances indicates that it often becomes difficult for marketing order committees to obtain the requisite majority of votes necessary to approve recommendations for implementing order authorities. Moreover, a committee may experience difficulty in obtaining compliance with order requirements from all handlers in such a circumstance. Such lack of effectiveness is recognized in the act in connection with the provisions for the adoption of new marketing orders and amendments to existing orders, which require that the Secretary determine that the issuance or amendment of an order is favored by two-thirds of the producers voting or by producers representing two-thirds of the volume of production. Given the demonstrated lack of producer support for the hop order and consistent with the intent of the Act, it is determined that it is no longer possible to achieve the objectives of the program.

51 Fed. Reg. 32779 (Sept. 16, 1986).

Proponents seek to impose an Order and reregulate the industry with

precisely the same features that justified termination of the old Order, i.e. a base allotment system, and "bona fide" effort requirement, and transfer provisions that impose entry barriers and encourage a focus on base trafficking rather than on production and marketing. Reimposing terminated regulations–without a heavy and specific justification showing that the rationale for termination no longer exists–is a textbook example of arbitrary and capricious agency action.

III. The Industry Has Functioned Well in a Deregulated Market Relying on Ordinary Market Forces.

The U.S. industry has operated in an orderly, if not enviable, fashion since termination of the old Order. The hop and brewing industries have experienced tremendous technological innovation since termination of the old Order. New technologies used by processors, brewers, and some growers has improved utilization, resulting in the need for fewer hops to satisfy existing demand. New technology and more efficient and higher-alpha varieties at the grower level have resulted in the need for fewer acres devoted to hops. A truly globalized market has developed for alpha acid. New producing areas, notably China, have the capacity for substantial additional output in coming years. Since the primary commodity of concern to brewers is alpha acid, improved methods of extraction and processing hops into forms that can be more readily stored have eroded price

differentials between production areas, leaving only transportation costs and customs duties.[1]

To some extent the industry is a "victim" of its own incredible success. The industry is going through an orderly phase of adjustment in response to clear trends in the market. The development of high-alpha varieties coupled with vertical integration into downstream products by the producer sector has reduced the demand for hop acreage.[2] During this same period, beer consumption has remained relatively flat, while a change in consumer preference for less bitter and "lite" beers has reduced the demand for hops.[3] While total acreage has declined, the production of alpha acid has increased, reflecting the worldwide transition to higher yielding and higher-alpha varieties.

Some growers have declined their production and some have exited the industry, presumably because they are less efficient and high-cost, but possibly for economic reasons unrelated to the hops market. New and expanding producers have invested substantial resources indicating their belief in the near and long-

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Ex. 31 (Sparks-USDA letter) at 1-2.

[2] World acreage in 1989 was 91,182 ha., peaking in 1992 at 95,535 ha., declining to 56,618 ha. by 2002. During this same period, US acreage has also declined, but to a lesser extent, from 14,060 ha. in 1989 to 11,851 ha. in 2002, while the US acreage share has increased slightly, from 15.4% to 20.9%. Hopsteiner Guidelines 2002, p. 9.

[3] For example, in 1995 the average alpha acid dose was 6.3 g. alpha/hl., falling to 5.2 g. alpha/hl. by 2002.

term health of the industry. Growers have used and adapted to a variety of mechanisms to manage risk and maintain the overall profitability of their farming operations, including horizontal diversification to other crops and vertical integration to greater post-harvest processing. There was a near universal consensus at the hearing that the hop market had been restored to a good sense of order and balance as a result of substantial adjustments in response to the above-noted industry changes.

IV. Proponents Have Not Demonstrated Any Need for the Order.

The proponents have the burden of demonstrating that the hop market is in some way disorderly, chaotic, or characterized by some sort of failure, sufficient to justify the extraordinary intervention in the market of reimposing supply controls in the form of rigid producer allotments. Congress limited the use of the tools set forth in § 608c(6) to the correction of dysfunctional markets:

> Through the exercise of the powers conferred upon the Secretary of Agriculture under this chapter, to establish and maintain such orderly marketing conditions . . . as will provide, in the interests of producers and consumers, an orderly flow of the supply thereof to market throughout its normal marketing season to avoid unreasonable fluctuations in supplies and prices.

Varying justifications were offered by proponents for the HMO. These included an alleged oversupply of hops, unreasonably low prices, and an alleged

need to amass market power. However, the proponents failed to establish the level of market disruption necessary to justify intervention by imposing rigid supply controls.

V. The HMO Will Disrupt Orderly Marketing Contrary to the Purpose of the AMAA.

Even if proponents had established sufficient market disruption to justify supply controls, they have not and cannot demonstrate that their "solution" will solve the supposed problem consistent with the purposes of the AMAA. The AMAA does not authorize regulation for the sake of regulation, or because an industry or dominant group within an industry wants regulation, or to provide a mechanism to set a common price in violation of the antitrust laws. Indeed, Congress specifically required the suspension and/or termination of any order or provision that "obstructs or does not tend to effectuate the declared policy" of the AMAA. 7 U.S.C. § 608c(16)(A)(i). Supply controls can't be used to protect inefficient producers, e.g. by entry barriers, subsidies, or income transfers, to increase the costs of production or marketing, or in a manner to retard innovation. Perhaps most important, supply controls must never be used in a manner to disrupt the "normal" or "reasonable" price fluctuations that occur in an agricultural industry in a manner that leads to long-run misallocation of resources. According

to USDA Guidelines, producer allotments may only be used to ameliorate "extreme" fluctuations in supplies and prices, but without imposing entry barriers:

> The Department's economic review evaluated the impact of the numerous programs permitted through the marketing order system. After extensive analysis, the report concluded that orders have the potential to effectively stabilize supplies and prices but some may impose inefficiency on the production and marketing system.
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> Recognizing the inherent instability in producing and marketing agricultural commodities in general, and these crops in particular, the Secretary intends to operate marketing order programs in a manner to reduce extreme fluctuations in supplies and prices. Reducing risks to both buyers and sellers provides producers and consumers a degree of protection against extreme losses arising from economic and natural causes. . . .
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> Producer Allotment Programs (celery, cranberries, spearmint and hops): The Department's recent economic review pointed out that producer allotment programs have the potential for limiting supply, causing underinvestment by industry, and reducing open competition by restricting entry of new producers.
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> While the allotment system is contrary to the general policy of this Administration, it does have a statutory basis. To balance policy goals with statutory requirements, the Secretary will carry out these programs in a manner that will eliminate barriers to entry.

Guidelines for Fruit, Vegetable, and Specialty Crop Marketing Orders (1982), Ex. 28 at Appx. A (emphasis added).

AMS Administrator Thymian announced specific policy decisions to implement the Guidelines for the hop industry at a meeting in Portland on March 19, 1982:

> First, it is suggested that allotment and base not be permitted to be

> transferred (sold, leased, traded, or given) to another individual (person, partnership, or corporation). Thus, when a produce ceases to produce hops for any reason, that producer base must revert to the Committee for redistribution. Secondly, an additional base quantity equal to five percent of the preceding year's base must also be made available for distribution each year. The base from both of these sources must be distributed to new industry entrants and to existing producers who wish to expand their operations, such distribution each year being 1/3 to existing producers and 2/3 to new producers. The committee shall develop and propose to the Department rules and provisions that offer such new base to both classes of growers on an equitable basis. An annual increase of base of this magnitude will result in a progressive reduction in the value of base and thus a gradual, but eventual, elimination of barriers to entry.

HAC Grower Bulletin 82-3 (March 23, 1982), Ex. 28 at Appx. B.

Thus, proponents must demonstrate that the proposed supply controls and accompanying regulatory mechanisms will be used solely[4] to "avoid unreasonable fluctuations in supplies and prices." 7 U.S.C. § 608c(2).

A. Definition of "Handle" and "Handler."

Several Order provisions were not well thought and were basically lifted from the mint Order. One of the most crucial elements of a new marketing order are the definitions of key regulatory terms, like handler and grower. These definitions determine who and what is regulated, who must file reports, and who

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[4] The AMAA also authorizes the use of supply controls to gradually correct producer prices to parity. 7 U.S.C. §§ 608c(1), 608c(2), 608c(5). However, proponents are not invoking this regulatory authority.

must fact potentially draconian compliance investigations and proceedings. The proponents repeatedly changed the definition of "handle" in § 991.08. fundamental changes indicate either that the program was not well thought out in advance or that the uncertainty in the definition could be used to "game" the regulatory system.

The problem with the original definition is that it did not adequately deal with handlers outside the production area, custom processing, or the status of foreign producers. Moreover, every brewer or user of hops would become a regulated handler, subject to reporting requirements and enforcement. definition was changed in Ex. 43, but under this definition, brewers would still be considered handlers, and many producers (who have vertically integrated processing operations) would be considered handlers. The definition was again changed in Ex. 53 to specifically exclude brewers and exempt "preparation for market" as a form of "handling." Even this definition is full of problems. For example, brewers are excluded, but not other end users such as herbalists and pharmaceutical manufacturers. The term "acquire" is vague, especially when compared to "sell" later in the definition, and "transfer" in the exceptions. For example, assume that a producer prepares hops for market by producing alpha acid stored in barrels. Assume that the producer decides to store his hops in a

warehouse in Germany. This would not be "handling" because acid, not hops, was transferred outside the production area. If the German warehouse were owned by a dealer and not the producer, and the definition of "acquire" required an actual sale (as opposed to consignment, for example), then there would still be no "handling." In both of these cases, however, the identity of the eventual handler, if any, would remain vague, and the acid would be far outside the compliance and enforcement jurisdiction of HAC.

The concerns over definition are far from trivial. Both proponents and opponents readily conceded that there was considerable cheating under the old Order. Such cheating would be much easier under the new Order, in part because of the value of even small quantities of fungible alpha acid, because of the inevitable brewer demand in the face of unpredictable events such as a drought or other crop loss, and in part because of retained resent over its demonstrably unfair provisions and demonstrated lack of consensus over the need for an Order in the first place.

B. The Proponents Failed to Present a Scenario Illuminating Order Operation.

The lack of an operational scenario and a "pro forma" presentation of the econometrics of Order operation is fatal to the proposal. Part of the proponents'

burden of proof in demonstrating that the Order will achieve the purposes of the AMAA is to show, typically with historical and recent data, how the Order would have operated had it been in place and how it is expected to operate during the next few seasons. It simply is not enough to present a naked framework, with little more than "trust us" on how supply controls would be used in practice. This obligation is especially important here because of the "greed" and enforcement problems which in part caused the termination of the old Order,[5] the lack of consensus, the immediate creating of winners and losers with resulting inequities, the severity of supply controls, and the concessions that the Order will fail, with a potential devastating economic impact, if not properly managed.

C. The Proponents Presented Unclear and Conflicting Objectives and Vague Justification.

Proponents offered several, sometimes conflicting or inconsistent, goals for operation of the HMO. This uncertainty, coupled with the absence of an econometric analysis and operating scenario, makes it impossible for USDA to judge whether the HMO is needed or will "work" to solve the "problem," and

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[5] See, e.g., Tr. 282:2-288:4 (Roy, conceding the old Order effectively broke down in 1980 because of greed and that HAC did not make decisions in the best interest of the industry); Tr. 325:5-327:10 (Roy, conceding that the saleable was set too high at the end of the old Order, that the reserve pool was not operated properly, and that HAC improperly responded to extreme pressure from greedy growers).

makes it impossible for the voters to fairly judge the merits of the proposal. None of the proponents were able to define key regulatory terms and concepts, such as an "unreasonable" fluctuation in supplies and prices (a necessary trigger to determine whether a problem exists and whether producer allotments likely to solve it), a formula for determining either supply or demand, or a price target (essential to any "balance" of supply with demand, and a goal, at least for some proponents).[6]

The proponents' "economic" justification for the Order is set forth in Ex. 26 (Folwell) and Ex. 15 (Need for Order in the U.S. Hop Industry). The relatively high cost of establishing a hop yard, p. 1, is no justification. First, the aim of the proponents is to reduce hop acreage and production, not to encourage an expansion in the industry. Second, there are new and expanding producers, indicating a healthy industry. Third, proponents presented no evidence that those desiring to enter the industry or expand their production are unable to secure the necessary investment or financing. The relatively high cost of entry, in fact, provides a natural economic disincentive to cyclical overproduction, certainly when compared to industries like kiwi (where short-term fads can lead to long-term overproduction cycles) and raisins (where massive over-production is fueled

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[6] See, e.g., Tr. 288:5-289:3 (Roy).

by bad Order decisions and excess raisins as salvage when not needed for wine).

The "slowly declining" percentage of contracts (cited as Problem One by the grower proponents, Ex. 15 at p. 2), does not justify the Order. Contracts were down a bit during the alleged "oversupply" years, but contracts are now trending back up, hitting a relatively high 90% in 2000. The ability to contract is a useful market tool, giving producers essential information about expanding and contracting, and more importantly, identifying the more efficient producers (one lower cost ones likely to get the contracts). Not all hops should or could be contracted, as an active spot market is necessary to fill unanticipated sort-run demand and small or large fluctuations in crop yields.

The proponents' economist next cites the decline in the number of producers and dealers.[7] Every agricultural sector has become more concentrated on both the supply and demand side. Indeed, similar concentration occurred during operation of the old Order, from 348 growers in 1966 to 211 by 1986.[8] The

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[7] The fact that nobody seems to really know how many producers there are argues against an Order. While they claim there are about 70, Ex. 26 at p. 1, the list compiled to determine who was a an eligible grower to vote in the referendum, Ex. 57, had approximately 100.

[8] Ex. 28 (Folwell) at p. 6, Table 2. There is no support for the proponents' blaming deregulation for a "traumatic 65 percent reduction in grower numbers in the 17 years since the last marketing order." Ex. 15 (Need for Order) at p. 1. The number of growers hit a low of 192 in 1979, increasing to 235 by 1986 as the industry experienced relaxed regulation following the 1980 German crop failure. Thus, under regulation the industry experienced a 45% reduction in the number of growers.

formation of a cooperative, Yakima Chief, was a purely voluntary act designed to confer substantial benefits on its members, and should not be counted as a "negative" for purposes of justifying an Order. There is no evidence at all that the supply side concentration has led to more or less variable acreage or more or less variable prices. Concentration, at least at the levels in the hop industry, is a normal market mechanism in response to changing needs of the market and individual producers and is not evidence of any disruption of orderly marketing conditions at which supply controls should be directed. Indeed, the concentration cited by proponents–alleged to be a problem–actually contributes to a more "orderly" market. Larger producers are arguably better able to make "good" decisions, protect their substantial investments, acquire important market information, and coordinate with others in the market. It is the "perfect competition" business model, with countless small buyers and sellers, that tends to depress returns.

Similarly, buyer concentration is no justification for the Order. Proponents presented no evidence that the buyers are colluding in a way that might be a violation of the antitrust laws, fixing unreasonably low prices, engaging in any unfair trade practices, or engaging in any other behavior that might arguably contribute to a disruption of orderly marketing. Here again, a relative degree of

concentration would be expected to have a stabilizing effect. The claim of "excess" or unreasonable concentration on the buyer side is contradicted by the own numbers. In 1986, there were 23.4 (211/9) producers per buyer, but now there are 25 (100/4). The claim, p. , that "[s]uch an imbalance in market power is not a desirable situation" is unsupported and without a nexus to the use of supply controls. The facts that brewers must have hops and that producers have no other significant commercial use for their hops besides beer have not changed.

Finally, Dr. Folwell asserts that the stabilizing effect of the old Order justifies a return to supply controls. But stability, in either supplies and prices, is not necessarily a desirable goal. Nor is even a legal purpose of supply controls, which speak only to the "disruption" of orderly markets and the avoidance of "unreasonable" fluctuations in supplies and prices. Thus, "reasonable" fluctuations in supplies and prices must be allowed. According to grower proponents, what is needed is not so much stability, but a substantial reduction in hop acreage.

Although supply controls are usually supported by growers because they believe, wrongly, that they will increase price and revenue, Dr. Folwell contends that although under the old Order HAC was unable to accurately match supply and

demand,[9] the use of supply controls was able to stabilize supplies and prices:

> Resulting from the optimism of the HAC in expanding its share of the world hop market, the level of carryouts have been 10.2% greater than anticipated or the projected level of carryouts by the HAC. Thus, on the average, a larger than needed supply of hops has been made available to the market by the HAC in recommending the saleable percentage to the U.S. Secretary of Agriculture. Thus, the behavior of the HAC has not been in a monopolistic vein in terms of restricting the quantity of hops marketed.
>
> Despite the fact that the HAC behavior has resulted in larger than desired supplies of hops on the market, the marketing order has been successful in terms of stabilizing hop prices and acreages.

Folwell, "The U.S. Hop Marketing Order: The Price of Success is Misunderstanding," at 3 (1982) (Ex. 28) (emphasis added). Folwell also observed:

> [T]he saleable quantities the HAC ultimately recommended have caused larger carryout stocks than the projected carryout stocks that the HAC suggested as desirable levels. Given the overstated saleable quantity recommendations and the resultant larger than desirable carryouts, one might suspect that the HAC has explicitly attempted to expand the size and market share of the U.S. production base. This philosophy has often been stated in the minutes of the HAC's marketing policy meeting.

Ex. 29 at p. 31

A careful reading of Dr. Folwell's research reveals that he has found little evidence of stabilization, concluding that the Order reduced variation only in acreage and in nominal prices, but not in real or nominal sales and real prices:

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[9] See also Ex. 29 (Folwell, et al.) at p. 25: "[T]he HAC's desired level of carryouts has not been achieved on the average, nor do desired carryouts represent accurate estimates of actual carryouts in marketing year t+1."

> [T]here is only weak statistical support for the contention that Federal Order operations have contributed to increased stability of real sales of hops. There is essentially no statistical support for the hypothesis that nominal sales variation has been reduced in the Federal Order period.
>
> Regarding variation in hop prices, there is no statistical evidence to support the contention that real price variation has been reduced in the Federal Order period. In fact, the calculated F-statistic might be used as weak statistical evidence in favor of an alternative hypothesis of a real-price variance increase in the Federal Order period. . . .
>
> There was insufficient statistical evidence to conclude that either real and nominal sales or real prices were more stable in the Federal Order period.

Ex. 29 at pp. 26, 31.

According to Dr. Folwell's observations, the supposedly greater price and acreage stability under supply controls may have actually come at a terrible price to the industry in terms of decreased long-run revenue:

> [T]he federal marketing order for hops has achieved its orderly marketing objectives in terms of price (income) and quantity (acreage) stability while supplying a larger than necessary quantity of hops to the market.

Ex. 28 (Folwell) at 4. Folwell is generally always careful to point out that the old Order was not able to increase short- or long-run revenue or profit, relying exclusively on the supposed "benefits" of stability:

> [T]he Sparks report repeats numerous times that the purpose for the hop marketing order with a producer allotment provision is to maximize total revenue to hop growers. Past history of the U.S. hop industry and its constituents strongly suggest that such a behavior

> pattern would not exist. . . . "The analysis revealed that on the average, the committee overestimated demand components and underestimated supply components. The HAC can best be described as overly optimistic in their decision process (projections), and placing on the market a larger quantity than needed if they had perfect knowledge and were able to predict all supply and demand components with complete accuracy. . . ."

Ex. 26 at 6, quoting Folwell, R. J., A. H. Harrington, P.K. Hennessy, and R.C. Mittelhammer (1982), "United States Hop Industry and the Volume Control Provisions of the United States Federal Hop Marketing Order," XT 0092, Agricultrual Research Center, Washington State University, Pullman.

Dr. Folwell's final conclusion in justification of the Order, with all respects, invokes a near Biblical sense of apocalypse:

> U.S. hop producers are in need of such a marketing tool [producer allotments] and the countervailing power it can create for the producer side of the market. If the U.S. hop producers are not allowed to use such a marketing tool, the industry will continue to shrink in size and will someday become extinct.

Ex. 28 at 7.

Problem Two according to the grower proponents, Ex. 15 at p. 3, is the "lack of a structure to manage the quantity of hops produced or sold." This is simply circular and provides no justification: the lack of supply controls cannot by itself justify reimposing supply controls. The "evidence" includes continued production in the face of low prices based on "hope," the strong dollar (Problem

Three), a supposed inability to obtain bank financing, and the lack of "once fairly common" German crop failures. The alleged over-production has been reduced during recent seasons as growers reduce production or exit the industry in response to ordinary market signals and their own unique situation (cost, alternatives, etc.). The Order can and will have no effect on exchange rates or German crop failures. As the dollar has softened, U.S. exports have increased. The industry has recently experienced above-expected returns because of the severe drought in Europe. The proponents have provided no explanation of how the Order would be managed to account for or anticipate any exogenous events such as a crop failure. Indeed, by restricting supply below "free market" levels, the Order would likely deprive growers of substantial revenue from such crop failures. HAC's regulatory response to the 1980 German crop failure (as opposed to a free market response) contributed to a boomerang effect in overproduction, massive entry barriers, and years of bitter controversy in the industry as to who should be allowed to benefit from the sudden spike in demand, and for how long.

The proponents presented no evidence of any financing difficulties. On the contrary, the record reveals that proponents at Yakima Chief have been able to make substantial investments in equipment and facilities, that many growers are entering the industry or substantially expanding (while others are exiting and

declining), and that investment in newer higher-yielding and higher-alpha varieties is moving into production in an orderly manner.

Problem Four suggests some sort of market failure apparently based on an inability to obtain or utilize information, although proponents concede that "arguably growers today are more informed on market decisions than ever before." Indeed this is true. Growers have access to a wide variety of information from USDA and HGA statistical reports, cost of production surveys, the developers of new varieties, reports and contacts by dealers and brewers, formal conventions and countless informal meetings and discussions in this tightly knit industry, and visits to other production areas. Spot and contract prices provide perhaps the most vital information, coupled with the unique economic situation of each grower, helping growers decide whether to plant, harvest, expand or contract.

Implicit yet unstated is the assumption that HAC would be "better" at using all of this vast data to achieve some vague and often conflicting goal (orderly marketing, price increases, reduction of oversupply, etc.). Herein lies the fatal flaw in the justification. Proponents have completely failed to show that collective decisions produce a "better" result than the net result of unhindered individual decisions. Proponents make no claim to a lack of needed information, market failure based upon inadequate or incomplete information, misleading

information, or secret deals. It is undisputed that the net result of individual decisionmaking is gradually leading to the supposed desirable results of reducing acreage and oversupply. It is also undisputed that since deregulation, the industry has gone through an extraordinary period of innovation and investment in new technology.

The proponents' economist, Dr. Folwell, conceded that HAC under the old Order was unable to match supply with demand, leading to larger than desired carryouts. His analyses also showed that only acreage and nominal prices were more stable under regulation, while sales and real prices were at least as variable. HAC is completely unable to deal with essential information, the unique economic circumstances of individual producers. This problem is dramatically illustrated by the record which demonstrates that some producers are rapidly expanding while others are rapidly contracting, each in response to the same public market information PLUS information they have about their own circumstances (risk tolerance, alternative uses of resources, diversification and integration, cost of production, varietal mix, etc.). Imposing a "one size fits all" solution not only deprives the market of the collective benefits derived from the use by individual firms of all their unique information, but worse, punishes efficient expanding producers and unjustly rewards declining/exiting producers, totally without regard

to their individual economic conditions.

The proponents, Ex. 15 at p. 4, sets forth four objectives, all revolving around matching supply with demand. Foremost, HAC is supposed to "accurately" estimate demand and match supply to this "need." However, as explained above, Folwell explained that HAC was unable to achieve this "matching" in the past, typically providing greater than desired carryouts. It is impossible to estimate demand, much less match supply to this supposed demand, without regard to price. In order to raise prices, which many proponents testified are too low, even below the cost of production, HAC will be tempted in the beginning to significantly reduce supply. Such a decision will begin a devastating downward trend for the U.S. industry, transferring short-run sales, and more important, long-run incentives to increase production to new (e.g., China) and expanding foreign producing regions. Moreover, since HAC has no information regarding each producer's unique economic circumstances, any demand estimate by HAC will overstate the demand "seen" by high-cost producers and understate the demand "seen" by lower-cost producers. HAC cannot meet this objective in a manner either beneficial to individual producers or the industry as a whole.

Proponents do not suggest that the U.S. industry is somehow unable at present to meet demand, their contention is the opposite, that the industry is over-

produced. They offered no reason to doubt the ability of the continued free market to meet present and expanded demand.

Management of any reserve pool is potentially quite problematic. Hops can be processed and stored much more readily than under the old Order, hence will be a much greater temptation to transform any perceived "oversupply" into a reserve pool This will tend to depress prices because buyers will correctly perceive that the "industry" has one additional and potentially very large "grower," the reserve pool, and they will have no incentive to bid up the price with so much alpha acid in storage.

Finally, proponents offered no evidence tending to show that the "needs of the market" are not "consistently met" with a deregulated industry. Indeed, brewers, dealers, new and expanding producers, and many producers of aroma hops all testified in opposition to the Order, presumably happy with an unregulated market. Much of the proponent testimony came from declining, high-cost, or non-diverse producers as well as many members of the Yakima Chief cooperative (who might believe themselves in a unique position to benefit from the Order).

Proponents have not demonstrated the harm from or the need to "stabilize" the "reactionary planting cycle" that has allegedly existed since deregulation

variation in prices between $1.60 and $1.83 over a ten-year period is just not unreasonable, much less extreme. The proponents have not shown that the variance in alpha acid production is unreasonable, especially since it is affected not only be acreage decisions but also by decisions concerning variety and independent variables, e.g. weather, affecting yield. While the old Order, basing allotments on acreage, may have produced some forced stability in acreage, the new Order will be virtually incapable of stabilizing alpha acid production because there are so many factors besides planting decisions that affect yield.

As noted above, the AMAA only allows supply controls to deal with "unreasonable" (interpreted as "extreme" under the Guidelines) supply and price fluctuations, i.e. ones that impair financing. There is no evidence that the observed fluctuations are anything but ordinary and desirable, or that they in any way have impaired financing. Indeed, there are both new and expanding producers suggesting a very healthy deregulated market.[10] While the reasons for declining and exiting producers are not fully known, those doing so because they are higher-cost are again responding appropriately to market signals and it would

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[10] Proponents note that between 1983 and 2001 growers removed 20,671 acres and planted 19,161, not counting acreage on which varieties were changed. Ex. 15 at p. 7. Simultaneous entry and exit is compelling evidence of a healthy industry, not a dysfunctional market, since the "replacement" acreage would represent investment by more efficient and/or lower-costs producers, benefitting not only them but the industry as a whole.

be inefficient to protect their continuation in the industry with supply controls Forced stability, without proof of harm from "extreme" variations in the free market and proof of substantial benefits from re-reregulation, is simply not a justification for supply controls under the AMAA.

Proponents complain about low prices, below the average cost of production, and seek to use supply controls to "stabilize" them, most likely meaning limit supply to increase prices. As explainer above, the old Order was unable to stabilize real prices or sales. Any effort to increase prices would self-defeating as there was unanimous agreement that, at least for alpha acid, there was a single unified world market with price determined not by U.S. production but by total world supply

Regarding proponents' "assumptions and limitations," Ex. 15, p. 8:

> 1. The old Order was unable to stabilize either real prices or sales. No evidence was presented that merchant and user prices were other than fair and reasonable under deregulation.
>
> 2. No evidence was presented that growers are presently unable to produce for the "anticipated world demand." No evidence was presented that the unregulated market was sufficiently unstable or dysfunctional to justify re-regulation. To the extent the Order was used to raise prices, the U.S. would lost sales to foreign producers who would quickly act on the incentive to expand their production. It is simply impossible to benefit the U.S. industry by imposing supply controls in the face of a dynamic and expanding world market.
>
> 3. There is no evidence that the unregulated market is unable to

satisfy annual world demand. HAC was unable under the old Order to accurately match supply with demand. There is no evidence, and economic theory teaches otherwise, that a collective decision about demand would be any "better" than the net impact of decisions by individual firms relying not only on public information but on information about their own unique economic circumstances.

4. Perhaps the most preposterous of the assumptions, it is utterly impossible for HAC to "influence the amount of hops produced each year by controlling the annual saleable available on the world market." Since the U.S. industry is only approximately a third of world production and there is significant and growing bilateral trade among hop producing regions, HAC's setting a saleable limiting only the U.S. share of world production will only have an insignificant effect on total world production (especially since the saleable is announced by HAC so early that foreign producers have more than adequate time to respond with increased production).

5. Existing inventories, presumably meaning carryouts and stored acid, are flowing to the deregulated market according to its needs. Significantly, proponents offered no evidence waste or salvage disposal. By imposing arbitrary limits on saleable (in an environment of variable alpha and acreage yields), the Order would likely quickly accumulate a significant reserve, which would tend to further depress prices.

6. There is no evidence that growers are "unable" in a deregulated market to plant to meet world market needs, or as above, that re-imposed supply controls would improve matters. Growers have accurately responded to market signals to reduce acreage as varietal and alpha acid yields have increased.

7. As noted above, Dr. Folwell's analysis demonstrated that the old Order was unable to stabilize real prices or sales and there is no reason to suspect that the new Order would be better able to achieve this objective. Even if it could be operated to stabilize prices, proponents have not demonstrated that such stability is desirable to either the industry as a whole or to individual producers. Some, i.e.

> reasonable, variability provides needed signals for investment and production adjustments. Moreover, the price fluctuations that might be associated with greater output in an unregulated market allow the industry a much better profit potential in the event of minor or major production failures in other regions. Growers have different tolerances for price and production variability, which should be respected, and have different

D. The Demand for U.S. Hops is Elastic.

As noted above, proponents are quite uncertain about the operational goals of the HMO. However, essential to the effective and beneficial operation of supply controls, especially producer allotments, is the assumption that demand is inelastic, meaning that a small change in the supply will produce a dramatic change in price. This premise of inelastic supply means that restricting the domestic supply (compared to the supply that would be produced in the absence of producer allotments) will lead to higher prices and greater revenue for the industry. Conversely, if supply were elastic, any restriction might increase price, but overall revenue would be reduced. Hence, the success of the proposed HMO in the ability of the supply controls to increase revenue depends on the inelasticity of the demand for hops. If demand is elastic, the imposition of supply controls spells economic disaster and ruin for the industry. If elasticity is approximately 1 over the range of relevant prices, meaning that a reduction in the quantity supplied does not produce a significant increase in revenue, supply controls should still not

be used due to intra-industry inequities, the damage to overall industry competitiveness, and the encouragement of substitution.

Dr. Jakanowski of Sparks explained why the U.S. hops industry does not fit the textbook model of an agricultural ingredient amenable to supply controls:

> Generally, products of highly specialized uses for which there are few (if any) substitutes tend to have inelastic demand. Hence, marketing order proponents point to the use of hops almost entirely as an ingredient in beer, and lack of substitutes for this use, as evidence that demand is inelastic. But, in fact, the situation is much more complicated. While overall brewer demand for hops likely is quite inelastic–since it is a necessary [ingredient] for which there are no real substitutes–brewer demand for U.S. hops produced in a given growing season could likely be quite elastic. This follows from the fact that in most cases there are very close substitutes for U.S. hops produced in the current growing season: hops produced overseas, and hops produced in a previous season that remain in storage. Of course, neither one of these might be a "perfect substitute" for fresh, domestic hops, but each is becoming a better substitute as improved processing techniques allow for longer storage with minimal loss of quality, and as expanding global trade makes imports more competitive in U.S. markets. Therefore, it is quite reasonable to expect that over time the demand for domestic hops has become less inelastic than it once was.

Ex. 31 (Sparks-USDA letter) at 2.

Dr. Jakanowski went on to explain how supply controls would hurt the overall competitiveness of the industry by, e.g., restricting innovation and investment:

> It is also important to note that revenue maximization does not necessarily imply profit maximization. Economic theory states that

> individual firms maximize profit by producing output at a level where marginal cost of production equals marginal revenue. But for the hop industry as [a] whole (and for many individual producers in particular) the cost of alpha acid production has declined over time as varieties have improved and scale has increased. Hence, the marginal cost curve for alpha acid production (and the industry supply curve) has shifted lower, allowing at least some producers to continue to earn a profit even though marginal revenue (i.e. the price of alpha acid) might be lower than what was once required to cover costs. Thus, even if restricted alpha acid production led to an increase in price sufficient to improve overall industry revenue, the lost production from low cost suppliers could increase the average cost of production for the industry as a whole, upsetting the profit maximizing balance that typically governs output decisions. Plus, the value of previous fixed investment in higher-yielding hop varieties is dramatically reduced when output is restricted, potentially threatening the financial viability of some firms–especially those that recently incurred substantial debt to expand production and efficiency. And, this type of quantity restriction clearly decreases future incentives to invest in higher yielding varieties that over the long run could decrease costs (and improve profits) for the entire industry.

Id. at 3.

In an effort to estimate the elasticity of demand, Dr. Jakanowski constructed an econometric model that used historical (1977-2001) data and regression analysis to estimate the inflation-adjusted price of alpha[11] as a function of the

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[11] The price response to changes in the quantity produced, or price flexibility, is the inverse of demand elasticity, i.e. the change in the quantity produced in response to changing prices. In many agricultural markets, including hops, short-run supply is generally fixed based on each season's level of production, so the relevant question is not how quantity produced changes with price, but rather, the market clearing price given the available supply. Price is a function of the available supply, production plus storage, and the relevant relationship to estimate is not the price elasticity, but the price flexibility, i.e. the percentage change in price associated with a 1% change in quantity. Therefore, if demand is inelastic, te price flexibility coefficient will be greater than 1, i.e. the decrease (increase) in price resulting from a 1% increase (decrease)

current season alpha harvest, alpha stocks available Sept. , and beer production (to account for long-run changes in demand). His analysis produced the surprising result that decreasing the quantity produced using an HMO supply control did, as expected, lead to an increase in price, but not enough of an increase to offset the loss in revenue from the reduced quantity:

> The proponents of a marketing order intend to restrict the production of alpha acid in order to increase its price in the market, and thereby improve industry revenues. However, the simple model estimated above suggests that this strategy is not likely to result in the desired outcome. Based on the parameter estimate for alpha production in any given year, a 1% decrease in production would likely lead to only a 0.73% increase in the domestic price of alpha acid, i.e., the price of alpha acid is relatively inflexible to changes in quantity produced over the past 25 years. This implies that while the price of hops will likely rise in response to restricted quantities in the domestic market, total industry revenues are likely to decrease directly as a result. Hence, the [supply control] mechanism would be self-defeating.

Id. at 4-5 (emphasis added). Dr. Jakanowski used a specific example to illustrate the prediction from his model that the imposition of supply controls would decrease rather than increase industry revenue:

> For example, for the year 2001 (the most recent year data is available), the Hop Growers of America report that 7.6 million pounds of alpha acid was produced domestically. Based on an implied alpha acid price of $16.27/lb. (based on a season average hop price of $1.85), total industry revenues in 2001 were approximately $123.6 million. The estimates in Table 1 suggest that, for example, a 10% reduction in the quantity of alpha acid produced in a subsequent

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in supply would be greater than 1%. See Ex. 31 (Sparks-USDA letter) at 3.

year would result in a rise in price equal to 7.3%. Hence, the 10% reduction in alpha production would mean 6.84 million pounds harvested, coupled with a 7.3% increase in price to $17.45, resulting in total revenues of $119.4 million–a revenue decrease of about $4 million as a result of the supply restriction.

Id. at 5.

Dr. Jakanowski next explained that even his estimates understated the true risks of imposing supply controls due to recent changes in the industry:

> As is always the case with econometric models, it is problematic to predict results "outside the range" of the data. Over most of the time period examined (with the exception of the period until 1986), the historic data reflects the result of a market operating with little constraint or outside interference. Imposing a marketing order would certainly create a "shock" to the system, the results of which cannot be estimated directly since a similar situation has never before occurred. While there have been marketing orders imposed in the past, the basic market and industry structural conditions have changed over time, and never has a marketing order been based directly on alpha acid controls. Thus, predicting the effect of this marketing order–over either the short or long term–is subject to considerable uncertainty. Therefore for gauging the likely impact of a marketing order, basic economic theory is perhaps even more important than empirical models.
>
> Given the basic characteristics of the hop market today–especially the increased ability to store the product and the greater reliance on world markets–it is not surprising that the market price for domestic alpha acid appears by out estimates to be relatively inflexible (i.e. demand is more elastic than might be assumed). And, since domestic buyers will be aware of the intention of a marketing order to restrict supply, it would be rational for them to increase purchases of imported hops, and possibly even carry larger stocks (perhaps in the form of imports) to avoid the necessity of purchasing higher priced hops in a restricted market in the future. At the same time, foreign suppliers, which are

> also currently facing low prices, would view the increased demand for their hops by U.S. buyers as a signal to increase production–an option unavailable to domestic producers.

Id. at 5-6.

Finally, Dr. Jakanowski explained why the imposition of supply controls would have an especially severe impact on both exports and imports:

> The adverse effect of supply restrictions in the U.S. on exports and imports cannot be overstated. Without a coordinated effort to restrict supply worldwide, ho growers outside the jurisdiction of the marketing order will be the primary beneficiaries of market controls in the U.S. Not only would hop imports be expected to increase as a result of higher domestic prices and restricted local supply, but exports would be less competitive–and less available–as well. . . . It is not surprising that increases in U.S. production are closely correlated with growth in exports, while imports move in the opposite direction. Restricting domestic supply through fiat can only serve to sacrifice a positive and growing trade balance, since supporting domestic prices above world levels makes imports more attractive [to U.S. buyers], and exports less competitive.

Id. at 6-7 (emphasis added).

Dr. Folwell's attempted criticism, Ex. 26 at pp. 4-6, of Dr. Jakanowski's evidence of a relatively elastic hops market misses the mark. Dr. Folwell substituted binary variables for beer production allegedly to represent four historical periods during which demand for hops has shifted. He fails to explain, however, why beer production is not the best indicator of hops demand and why the demand curve inexplicably shifted during these four historical periods.

Folwell concedes an obvious but critical point by claiming that the availability of substitutes, in this case foreign hops, means that the reciprocal of price flexibility understates demand elasticity.[12] His observation leads to the conclusion that Dr. Jakanowski's elasticity estimate of 1.37 may, if anything, be conservative. Dr. Folwell goes to great lengths to dispute evidence presented in a memo from Sparks to USDA that suggests the demand for hops is elastic. However, the off-hand dismissal of the Sparks model is an excessive reaction to minor concerns, and is not justified on statistical or economic grounds. Furthermore, Folwell's proposed model suffers from statistical and economic shortcomings of its own, which add uncertainty to the strength of his results and illustrate the need to consider all evidence in its full context.

Dr. Folwell asserts that the Sparks model suffers from serious statistical problems, including insignificant explanatory variables and autocorrelation. Trained economists would agree that neither of these problems fundamentally affect the economic relationships estimated by the model, and they certainly do not warrant outright dismissal of the model results. Autocorrelation is a common

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[12] "[T]he Sparks report fails to acknowledge that the price flexibility coefficient only sets a lower limit of the price elasticity of demand (Tomek and Robinson, pp. 49-50). As indicated by Tomek and Robinson, if there are no cross effects or substitutes for a product then the reciprocal of the price flexibility is less than the demand elasticity. In the case of U.S. hops or alpha acid there exists a near perfect substitute in the form of the same product(s) from Germany and other hop producing countries." Ex. 26 at p. 4.

problem encountered with time-series data, resulting generally in a downward bias in estimated standard errors, and therefore overconfidence in parameter estimates. However, parameter estimates remain unbiased and consistent, so even accepting the possibility that statistical confidence should be adjusted downward in the Sparks model, the parameter estimates nevertheless provide evidence of an elastic price response.

Regarding insignificant explanatory variables, any researcher would agree that this is not a statistical problem in need of a solution. Beer production was included in the model to account for various changes in demand over time that could affect the price of hops. This is reasonable based on simple economic theory. The fact that the variable is not significant does not mean that it should not be included. In fact, if economic theory supports its inclusion in the model (which we believe it does), omitting beer production would bias the parameter estimates of the remaining variables, rendering them useless. This is a well-known result from textbook econometrics. On the other hand, if beer production in fact does not affect the price of hops, including it in the model (as an irrelevant variable) has no impact on other parameter estimates. So, it is far better to include possibly irrelevant variables in the model than to exclude potentially important ones.

Folwell finally criticizes the Sparks model for not acknowledging that flexibility estimates provide only a lower limit of the price elasticity of demand. He correctly notes that if significant substitutes and cross effects exist, the reciprocal of the flexibility is less than the elasticity. Surprisingly, he then points out that in the case of US hops, there exists a near perfect substitute in the form of products from Germany and other hop producing countries. This only supports our point. The Sparks memo suggests the elasticity for hops is elastic at about .37 (the reciprocal of 0.73). With significant substitutes, the reciprocal of the flexibility is *less than* the elasticity, suggesting in fact that the Sparks estimate of 1.37 is a lower bound, with the true elasticity somewhat higher (more elastic). Throughout the testimony the opposition witnesses tried to make the point that the near perfect substitutes for US hops from Germany and elsewhere make demand more elastic and therefore make supply controls less effective. Dr. Folwell's acknowledgment of these near perfect substitutes and the more elastic demand as a result supports the opposition's claims.

Dr. Folwell uses the criticisms identified above to suggest an alternative functional form that he believes to be superior. However, his own model suffers many deficiencies that add uncertainty to his results. Unlike the model presented by Sparks, Folwell inexplicably makes no effort to account for the effect on price

of industry stocks. Economic theory suggests this is a grave omission, since inventories available for sale certainly affect price as well as production decisions and current season production. He also uses a set of dummy variables to account for apparent "shifts in supply and demand," but the economic relevance of these variables is questionable and he provides no explanation of the factors possibly driving these shifts. Furthermore, based on criteria for which he criticized the Sparks model, his third dummy variable (D3) is not significant and should not be included in the model. Interestingly, when that variable (D3) is omitted (leaving all others the same), the elasticity estimate jumps to –0.98, nearly unitary, and with a 95% confidence interval that extends to –1.5, quite elastic indeed.

All of these issues point to the underlying difficulty in estimating complex economic relationships with a high degree of certainty. Hence, the statistical results should be viewed in the context of industry observations, market characteristics and economic theory. From this there is strong reason to believe that the demand for US hops is not inelastic, and that supply controls would be detrimental to the industry. The statistical results do not refute this view, but provide even more evidence in support.

E. Entry Barriers and Unwarranted Income Transfers.

Proponents conceded that new and/or expanding producers would have to pay to acquire base from existing producers.[13] Unless base is leased, creating in effect a system akin to feudal tenure, a rash of base transaction would occur during program startup.[14] These wealth transfers amount to an unjustified subsidy by new/expanding/efficient producers to "reward" those producers who have reduced their production, exited the industry, etc. Producers who reduce their hops acreage may have done so for a variety of reasons, beginning with their being less efficient or higher cost than their competitors. Other reasons include decisions to use higher-yield or higher-alpha varieties, or diversification into other commodities. It is totally irrational and arbitrary to reward producers with excess base with a subsidy and punish new and expanding producers with a tax that amounts to a wealth transfer having nothing whatsoever to do with promoting orderly marketing. Worse, forcing new and expanding producers to purchase allotment punishes precisely the group of most efficient and innovative producers, making the U.S. industry as a whole and these producers in particular less competitive. Technological innovation and productivity improvements are essential to the future health and well-being of the U.S. industry in an increasingly globalized

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[13] See, e.g., Tr 95:1-97.5 (Carpenter)

See, e.g., Tr. 1614:17-1617:20 (Roy, conceding inequities at Order startup).

market; hence, there is no conceivable reason to penalizing new/expanding producers by imposing a tradeable rights system in allotment.

Here again the proponents offered inconsistent testimony about operation of the HMO. Carpenter, for example, stated that it was the intent that there would be so much base available at the beginning that it would have no value:

> We have designed the order so that there should be plenty of base available on the front end. . . . What we tried to do is to take a big tent approach and tried to please as many as possible, recognizing we could not please everybody in terms of establishing what the base period would be. . . . In fact, subsequent to submitting our proposal, we added the 2002 year to that as well. We do not want base to have a value to speak of on the front end and that is one of the reasons why we went to the now six-year period so that there would be plenty of base available for those growers that needed it at hopefully a very low value. . . . I don't think we want to have -- certainly we don't want to have base to have a value at any point, ...

Tr. 95:13-96:11 (Carpenter).[15]

Not only would the entry barriers and wealth transfers harm new/expanding producers specifically, conferring unwarranted and unjust benefits on declining producers, they also harm industry competitiveness and efficiency as a whole by punishing–increasing costs–for producers likely to be the most innovative. Dr. Jakanowski explained:

The empirical discussion above [demonstrating that supply controls

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[15] See, e.g., Tr. 1614:7-1614:20 (Roy, citing mint Order startup base readily available for $0).

> would reduce industry revenue, encourage imports, and discourage exports] does not even consider the impact on industry-wide costs and efficiency–especially as it relates to the need for some producers (likely the most efficient ones) to incur substantial additional costs in the form of allotment purchases only to maintain their current productive level of output. This adds an additional dead-weight loss to the industry, sacrificing efficiency over the long term and decreasing competitiveness relative to foreign producers.

Ex. 31 (Sparks-USDA latter) at 7.

VI. The Program Contains Inadequate Safeguards.

A. Definition of Producer.

The hearing revealed that there was considerable "gaming" in order to create growers for the purpose of earning base and voting in any potential referendum. Some of the proponents had bails produced on their ranches marked with grower numbers who were not producers during the current season or with new grower numbers obtained from the states. They were initially not very forthcoming about these efforts, but eventually attempted to come to grips at least with the problem of which "growers" were eligible to vote in any referendum. Proponents and opponents were eventually able to achieve a consensus on growers eligible to vote. See Ex. 57.

Section 991.06 should be changed to expressly state that a producer must have produced hops commercially during the current season to qualify as a

producer for purposes of receiving base, voting in referenda. It should not be enough that they have infrastructure or that they "could" produce hops. Given the "gaming" disclosed at the hearing, the section must make clear that the hops must actually be produced by the producer, and that, for example, assignment of bails produced on other land would not qualify. The section should also expressly state that the creation of grower entities with the primary intent to manipulate base or proliferate voting rights is an unfair method of competition within the meaning of § 608c(7)(A).

B. Definition of Handle.

As explained above, the constantly changing definition of "handle" in § 991.08 is still hopelessly unworkable. This problem isn't due so much by a lack of desire on proponents' part to "fix" problems they did not envision and once called to their attention, but to the fact that there is probably no definition that is workable and free from the potential for "gaming" and manipulation, given the complex structural relationships in the industry and the huge financial incentives to "cheat" in proportion to the severity and/or unfairness of the supply controls. This problem also infects related concepts, such as the use of "purchase" in § 991.52.

C. Independence of Committee Members.

Section 991.15 should be amended to expressly state a requirement for membership that each member and their respective alternates must have a different primary marketing affiliation. The existence of Yakima Chief, a major and potentially growing cooperative, presents the serious risk that HAC decisions could become dominated by members, officers, affiliates, etc., of a single entity. This requirement of bona fide independence is especially important during the formative years of the Order, when rules and procedures are developed, when the potential for favoritism may be at its greatest. Section 991.16 should be amended to require continued bona fide independence throughout the term of office.

D. Public Member.

Section 991.18(d) should be amended to expressly state that the public member must have no prior or current affiliation with the hop industry. The intent of requiring committees to include public members was to have some modest check and balance on the primary underlying assumptions of an Order, in this case that perennial supply controls allegedly serves the public interest. Inviting an academic economist to serve as public member, for example, really adds no independent voice. To the extent that input from such economists and others

knowledgeable about hop marketing, such as dealers, is necessary and desirable, it can be easily obtained by special invitation to meetings, or in the case of professional studies, by contract. However, the efficacy of a truly "public" member's vote requires genuine independence from the industry.

E. Approval by the Secretary.

Sections 991.22(b) and 991.923(n), and every other provision requiring rules and regulations or implementing procedures should be changed to expressly state that HAC only has the power to recommend rules to the Secretary. Any legally binding rule, requirement, or procedure must have the independent approval of USDA following the substantive and procedural safeguards of the Administrative Procedure Act. The misuse of maturity color chips, variances, etc., is a good example of rogue committee decisionmaking without oversight and APA compliance that led to manifest unfairness and favoritism and spawned years of controversy and litigation.

F. Alpha Acid Factor.

Section 991.52(c) should be clarified to provide uniform and trustworthy procedures for determining these factors, including as noted above the

requirement that all rules and procedures relating thereto be recommended to USDA and approved in accordance with the APA. What if, for example, different laboratory tests produce different factors? When are the tests to be performed? What if the factor changes from season to season or is different for different producers or growing regions, for example in response to weather or soil conditions?

G. Allotment Base.

This provision is by far the most controversial aspect of the Order, apart from the need for supply controls. The AMAA[16] imposes severe restrictions on producer allotments. The annual allotment of each producer must be (1) calculated under a uniform rule (2) based upon representative prior years' sales and/or current quantities available for sale, provided that (3) the total saleable shall be apportioned equitably among producers.

Several conclusions flow from these limitations. First, there is no provision

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[16] 7 U.S.C. § 608c(6)(B): "Allotting, or providing methods for allotting, the amount of such commodity or product, or any grade, size, or quality thereof, which each handler may purchase from or handle on behalf of any and all producers thereof, during any specified period or periods, under a uniform rule based upon the amounts sold by such producers in such prior period as the Secretary determines to be representative, or upon the current quantities available for sale by such producers, or both, to the end that the total quantity thereof to be purchased, or handled during any specified period or periods shall be apportioned equitably among producers."

for the sale, lease, or transfer of base, i.e. prior years' production. A producer's annual allotment can only be a function of his prior years' "amounts sold by such producer" and his "current quantities available for sale." Obviously there is no authority to increase a producer's current allotment by the prior years' production or sales by other producers. Accordingly, provisions dealing with an inflexible initial base and transfers, i.e. § 991.58(b), must be deleted from the Order.

Second, a "uniform rule" must be used in calculating allotment. Since the commodity subject to supply controls is alpha acid, the 10% "bump" proposed for aroma hops in 991.53(c)(2) is not uniform and unlawful.

Third, again since alpha acid is the regulated commodity, any alpha acid stored by or available to a producer from any prior year's production must be included "current quantities available for sale." Thus, any "reserve pool" as proposed in the Order would have to be comprised of alpha acid handled during a previous season and maintained by handlers, unavailable to producers. Further, since the current allotment is a function of prior sales, alpha acid stored by a producer from prior a prior year's production could not be counted as part of the 'representative period," but as part of the amount available for current sales.

The prior period included in the calculation must be "representative." Since allotment can't be traded or leased, the concept of a base is virtually meaningless.

However, this still leaves open the question of how many prior years should be included in the calculation. The "representative period" must be interpreted in light of the objective of the Order which is match current supply and demand, and with the final requirement noted above that the annual saleable be "apportioned equitably" among producers. The reason to include some prior years' sales is that current production is subject to some uncertainty beyond the control of the producer, i.e. weather. Testimony indicated that hops, like all agricultural commodities, are subject to yearly fluctuations. The inclusion of two, and at most three, prior seasons in the "representative period" is reasonable in light of these uncontrollable yearly fluctuations.

Aside from the fact that creating an initial tradeable base is unlawful under the AMAA, the proponents desire to include six seasons (1997-2003) in the "representative period" is utterly unreasonable. The purpose of the "representative period" is to account for uncontrollable yearly yield fluctuations, not to freeze the industry structure arbitrarily determined to be its "halcyon days." The record demonstrates that individual producers have made substantial changes in their production since 1997, e.g., expanding and contracting acreage, changed varieties, etc.

Assuming, *arguendo*, that base can be traded as a matter of law, the

representative period must not exceed the three most recent seasons for which data is available for the reasons set forth in the previous section. Moreover, creating winners and losers based on an arbitrary historical period prior to significant structural adjustment is clearly inequitable within the limitations of § 608c(6)(B) as granting tradeable rights based on essential ancient history bears no relation to the purpose of matching supply and demand.

Creating so much "vapor" base seems solely for the purpose of facilitating wealth transfers and implementing the "exit strategy" or buyout desired by some proponents. As pointed about above, aside from being arbitrary and unfair, and unrelated to orderly marketing, imposing additional costs on new and expanding producers is a direct tax on innovation and efficiency, contrary not only to the interests of the industry's "best" performers but also to the overall health and future of the industry.

H. Adjustments to Base.

Section 991.53(d) should be eliminated. Its purpose is vague and unspecified and it isn't even clear whether adjustments would be available to all producers under a uniform rule. The potential for such adjustments simply increases uncertainty and invites further "gaming."

I. Additional Base.

Section 991.53(e), and other appropriate sections, should be amended to conform to the USDA Guidelines which require the elimination of entry barriers in producer allotment programs. The 0.5% for new producers is too low to create economically viable new producers especially if there are multiple applicants. Similarly, the 0.5% for existing producers is inadequate to supply the needs of the highly efficient innovative expanding producers. In any event, the provision is likely merely a sham because of its limitation to years of increasing saleable.

J. Bona Fide Effort Requirement.

Section 991.53(f) is fatally flawed, if only because it leaves implementation and "development" entirely to the discretion of HAC. As noted above, tradeable allotments are unlawful. If there were authority for such allotments, the bona fide effort requirement must be strictly enforced and leases prohibited in order to avoid creating a system of feudal tenure (akin to peanut allotments) in the hops industry. Paying nonproducers for the right to produce and sell hops contributes nothing to "orderly marketing" and imposes an unwarranted tax on the most innovative and efficient producers.

K. Contracts Exception.

Section 991.54(c) contains in effect an automatic grant of additional allotment to fill 2003 forward year contracts which might be above the allotment computed under the Order. As written, this additional "pre-existing contracts" allotment is unlawful as a violation of § 608c(6)(B) "uniform rule" and "equity" requirements. There should be a general exception for multi-year forward year contracts as these are the very essence of orderly marketing. This could be implemented by limiting the Order to regulation of the "spot" market as forward contracts would not be includable within "current quantities available for sale" in § 608c(6)(B).

L. Transparency.

Supply controls, especially these proposed in the Order, and their administration, can be extremely controversial and subject to considerable "gaming." This is especially true in this Order because of the checkered history of Orders and enforcement and the lack of consensus on the need for and terms of regulation. Accordingly, it is essential that all regulatory features of the Order be completely transparent and in full view of the entire industry. This is particularly

important at the inception of the Order because of the conceded inequities of the procedures for allocating initial base. Such full disclosure and transparency must include, without limitation, names and location of production of all producers, computation of initial bases, all base transfers including date, terms, and compensation, recipients of "new" base, applications for initial allotment, hardship applications and decisions, compliance with the bona fide effort requirement, the location and current quantity of reserve pools, alpha acid factors and the exact method of their determination, enforcement/compliance audits and investigations and their results, and the names and locations of handlers.

The proposed HMO contains a variety of deadlines by which actions are supposed to be taken. Producers and handlers rely on these deadlines to make decisions the can impose or avoid real costs. However, HAC can waive or alter these deadlines, with little effective oversight by USDA, in a manner than can benefit those who "knew" the changes would likely be made and burden those who relied on strict compliance with the Order's procedures and deadlines. This risk further increases the costs and uncertainty of regulation. See, e.g., 45 Fed. Reg. 79006 (Nov. 28, 1980) (delaying deadline for designating reserve); 45 Fed. Reg. 71760 (Oct. 30, 1980) (increasing saleable from 115 to 127%); 46 Fed. Reg. 60177 (Dec. 9, 1981) (increasing saleable from 130 to 132.5% to allow all 1981

crop to be marketed; delaying date for designation of reserve); 48 Fed. Reg. 31866 (July 12, 1983) and 48 Fed. Reg. 48219 (Oct. 18, 1983) (waiver of bona fide effort requirement because market "inactive" and in a condition of "oversupply;" 1983 saleable had been set at 130%); 49 Fed. Reg. 11185 (March 26, 1984) and 49 Fed. Reg. 18813 (May 3, 1984) (extend date to transfer base; waiver of bona fide effort requirement; hop market "inactive" and in "oversupply;" saleable set at 115%); 50 Fed. Reg. 27814 (July 8, 1985) (waiver of bona fide effort and extension of deadline for allotment transfers; saleable at 97%).

VII. Representative Period for Referendum.

The AMAA provides that producer support for the proposed HMO be determined by a referendum among those who produced hops during a representative period. This period should be the most recent harvest. See 51 Fed. Reg. 27400 (July 31, 1986) (voters in continuation referendum had to produce hops between August 31, 1985 and July 31, 1986).

"Producers" who merely have a producer number issued by a state, or who have hops reported as "produced" on their behalf by another producer, cannot quality to vote in the referendum.

Conclusions of Law.

. The record fails to demonstrate a problem that can be addressed by the regulatory tools authorized under the AMAA, i.e. the market for hops is not dysfunctional or disorderly, nor are there "unreasonable" fluctuations in supplies and prices within the meaning of § 602(4).

2. The record fails to demonstrate that producer allotments will achieve the objectives of the AMAA, i.e. avoiding (in the interest of both producers and consumers) "unreasonable" fluctuations in supplies and prices within the meaning of § 602(4) and the obligation of the Secretary under § 608c(4) to make evidence-based findings.

3. The record fails to demonstrate the necessary producer/handler consensus required for approval of the Order under §§ 608c(8), (9), and required by USDA policy for the efficient and effective administration of a supply control marketing order.

4. The entry barriers in the Order are contrary to USDA Guidelines which called for their elimination in producer allotment programs.

5. The Order is contrary to USDA Guidelines which limit the use of producer allotments to markets characterized by "extreme" fluctuations in supplies and prices.

6. The annual allotment of each producer must be (1) calculated under a uniform rule (2) based upon representative prior years' sales and/or current quantities available for sale, provided that (3) the total saleable shall be apportioned equitably among producers, as required by § 608c(6)(B).

7. Since allotment can only be a function of prior years' sales and the quantity of alpha acid currently available for sale, provisions for the sale, transfer, and lease of allotment are unlawful.

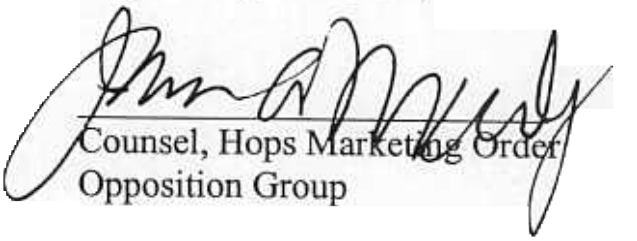
8. The "representative period" for determining allotment must be no longer than the three most recent seasons for which data is available.

9. The 10% "bump" in the alpha acid factor for aroma hops is unlawful as a violation of the "uniform rule" limitation in § 608c(6)(B).

10. Basing allotment on historical production unrelated to factors beyond a producer's control is unlawful as a violation of the limitation in § 608c(6)(B) that the saleable be "apportioned equitably" among producers.

11. All legally enforceable requirements, rules, and regulations of any sort can only be recommended by HAC to the USDA and must be approved in compliance with the procedural and substantive requirements of the Administrative Procedures Act.

Respectfully submitted,



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