UNITED STATES DEPARTMENT OF AGRICULTURE

BEFORE THE SECRETARY OF AGRICULTURE

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In re: [AO]

) Docket No. 15-0071

) Milk in California

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BEFORE U.S. ADMINISTRATIVE LAW JUDGE

JILL S. CLIFTON

Tuesday, November 10, 2015

9:01 a.m.

Piccadilly Inn Airport
5115 East McKinley Avenue
Clovis, California 93727

TRANSCRIPT OF PROCEEDINGS

VOLUME 34

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JUDGE CLIFTON: We're back on record on November 10, 2015. It's a Tuesday. It is approximately 9:01 in the morning. We are in Fresno, California, and this is Day 34 of the milk hearing.

My name is Jill Clifton. I'm the United States Administrative Law Judge who is assigned to take in the evidence at this case, I would -- or in this case I should say. I would like to have my fellow United States Department of Agriculture employees come forward at this time and enter their appearances for the day. I would like them, for them to be followed by teams of proponents and opponents and other participants. Also, if you are here to testify today, I would like you to come at the end of all the others to state and spell your name as the others will do.

MR. RICHMOND: Good morning, my name is William Richmond, R-I-C-H-M-O-N-D, I'm with USDA Agricultural Marketing Service, Dairy Programs in Washington, DC.

MR. CARMAN: Good morning, Clifford Carman, C-A-R-M-A-N, Assistant to the Deputy Administrator, Dairy Programs, Agricultural Marketing Service, USDA.

MS. FRISIUS: Good morning, Meredith Frisius, F-R-I-S-I-U-S, here with USDA Dairy Program.

MS. BECKER: Good morning, Lauren Becker, B-E-C-K-E-R, I'm an Attorney in the Office of the General Counsel for USDA.

MS. MAY: Good morning, Laurel May with USDA, AMS Dairy Program. I'm a rule maker in the Order Formulation and Enforcement Division.

MR. HILL: Good morning, I'm Brian Hill with the Office of the General Counsel, Marketing Regulatory and Food Safety Programs Division.


MS. OLIVER THOMPSON: Good morning, Megan Oliver Thompson, Megan is M-E-G-A-N, I'm an Attorney with the law firm Hanson Bridgett, H-A-N-S-O-N, B-R-I-D-G-E-T-T, also Counsel for the Proponents of Proposal Number 1.

MR. SCHAAD: Good morning, my name is Dennis Schad, S-C-H-A-D, I work for Land O'Lakes.

MR. ERBA: Eric Erba, California Dairies, E-R-I-C, E-R-B-A.


MR. GARBANI: Good morning, Pete Garbani, spelled G-A-R-B-A-N-I, and I'm with Land O'Lakes.

MR. ENGLISH: Good morning, your Honor, Chip English,
E-N-G-L-I-S-H, with the law firm of Davis, Wright, Tremaine, my office in Washington, DC. And thank you very much, Mr. Sumner, for reminding me, I was going to say here on behalf of the Dairy Institute of California supporters of Proposal Number 6, just to see if everybody was listening, but Proposal Number 2, thank you.


MR. BLAUFUSS: Good morning, Rob Blaufuss, B-L-A-U-F-U-S-S, with the Dean Foods Company.

MS. TAYLOR: Good morning, Sue Taylor with Leprino Foods.

MS. HANCOCK: Nicole Hancock with Stoel Rives, representing the California Producer Handlers Association and Ponderosa Dairy.


JUDGE CLIFTON: I'm sorry, I have got to get the spelling again. I know I have gotten it once or twice, but --

MR. SHEHADEY: On the last name? She - had - EY.
JUDGE CLIFTON: She - had - E-Y.

MR. SHEHADEY: There you go. Good?

JUDGE CLIFTON: Give me the letters, please.

MR. SHEHADEY: S-H-E, she -- had -- H-A-D -- E-Y.

JUDGE CLIFTON: I get it. Thank you.


MR. GONSALEZ: Good morning, Anthony Gonzalves, Professional Legislator, Representative for the California Producer-Handlers, G-O-N-S-A-L-V -- as in Victor -- E-S.

Thank you.

MR. DeGROOT: Good morning, Amos DeGroot, Rockview Farms, Ponderosa Dairy.

JUDGE CLIFTON: That's spelled the same as Ted spells it?

MR. DeGROOT: Yes.

JUDGE CLIFTON: Thank you.


MS. LOPES: Good morning, Linda Lopes, L-O-P-E-S, dairy person.

MS. REED: Good morning, Kristine Reed, I'm an Attorney with the Miltner Law Firm, and I represent Select Milk Producers.


JUDGE CLIFTON: Is there anyone else who would like to be identified at this time? No one. I would like now to invite preliminary matters, announcements, and the like.

MS. MAY: Good morning, Laurel May with USDA AMS Dairy Program, also feeling victorious because I was finally able to get into the VPN -- it's monumental.

As you know, everybody is welcome to testify at this hearing, if they would like to. And to do so, you merely need to let me or somebody else on the USDA staff know that you would like to do that and we'll get you into the line up. Anybody who would like to may also question any of the witnesses during cross-examination, and to do that you would just notify the Judge and approach the podium and you can do that.

We are broadcasting this session of the hearing via live audio feed and you can access that at www.ams.usda.gov/live.

The court reporter is taking transcripts and making those available to you online approximately two weeks after the end of each hearing week. You can access those at the AMS
Dairy website. We do have some extra copies of exhibits on
that table back there behind Mr. Vandenheuvel, and so you are
welcome to help yourself to those if you would like.

Yesterday, at the end of the day we had Mr. Blaufuss on
the stand, I believe, and he's looking forward to returning,
but I think that according to what I have heard, we might be
hearing from a couple of women producers, Lisa Lopes and
Antoinette Duarte, who are here from Turlock and Elk Grove,
respectively. So I will turn the time over to somebody else to
tell us what's happening.

One more thing, just as a reminder, after this week's
sessions here at the Piccadilly, we will be moving over to the
Falls Event Center, which is at 4105 West Figarden Drive, and I
can give you more precise directions to that if you want.

JUDGE CLIFTON: Thank you, Ms. May. Mr. English?
MR. ENGLISH: Good morning, Chip English.

Yes, your Honor, Ms. May is correct that, of course
obviously Mr. Blaufuss was on the stand when we finished
yesterday, I think we all know that. And we certainly are
prepared to return him to the stand when the time permits. We
have had, I can say, extensive discussions after the hearing
yesterday, over the evening, early this morning, and I believe
we have reached sort of the following sort of concept; the two
dairy persons who just identified themselves would testify
first, and we are happy to do that. We believe, and I thank
Ms. Hancock for sharing the testimony of Mr. Gonsalves last night, we believe based upon what we have read, and at least what I think, subject to how I have been wrong throughout this hearing, how long the cross-examination would likely go, that it should be -- emphasize the word should be -- safe to then turn to him, and we are prepared to accommodate the professional lobby person on that with respect to his testimony, with the hope and expectation that he can be done by 1:00 p.m. when that's when he needs to leave. With that, we would then turn back to Mr. Blaufuss to complete Part 4, fortification. And then depending on exactly how things work with what's ready at that moment, what we will be ready today with Rob Blaufuss, Part 6, transportation, and Sue Taylor, Part 3, price impacts.

I have a couple of housekeeping things to do after that, and other than I think you raised an issue before the hearing, your Honor, that would complete our testimony and the overly optimistic part of me says we can finish that today. After much laughter -- I think more realistically, we should be able to finish that, I would think, before noon tomorrow. So I think, again, subject to all the vagaries of these things being different than you think they are going to be, while I'm taking some risk, and if I'm wrong, this is going to be on me, that I think we can accommodate Mr. Gonsalves today, as requested by Ms. Hancock, and we are prepared to do that with the hope and
expectation -- by the way, I understand from Mr. Beshore there are four dairy farmers tomorrow, but my understanding is they would be in the afternoon, so hopefully we would finish with what we have got.

So we're willing, I hope it's not a big risk. I think we have all had the opportunity now to have Mr. Blaufuss' testimony over night so hopefully that would compact a little bit of the examination. Ms. Taylor has a short statement and four tables. I'm not going to predict how long cross-examination is going to go on that. Mr. Blaufuss has a short statement on transportation credits. So we are cautiously optimistic that we could be done by noon tomorrow.

JUDGE CLIFTON: Would anyone else like to be heard with preliminary matters? I have a couple.

I thought of some additional questions that I would like Dr. Schiek to respond to. I would actually like every Economist who has not yet testified on quota, to keep in mind what I'm thinking and help me with this struggle.

I would like to have a practical suggestion for USDA to consider. Nobody knows what USDA is going to do, but in the event it determines that a Federal Milk Marketing Order is in order, that it would be a good thing, USDA has to deal with quota. USDA has control over very little about how quota is priced, how it's issued, and so on. There could be changes that might occur through California entities, so this is what I
want everyone to think about. Suppose that the USDA determined
that the idea of sunsetting quota is a good one, a step toward
uniform prices, but that it should not be abrupt and that it
should allow the value of quota to be realized. So suppose
that the USDA determined that the way it would deal with quota
is that the receipts would have a percentage that is devoted to
quota holders, and that that percentage would diminish over
time, very gradually, until no more percentage was paid over to
the quota holders. If some system like that were to be
evaluated, what would the starting percentage be? What is the
current percentage that is paid to quota holders? And if the
USDA determined that some percentage would be paid over to
quota holders, that would just be a mathematical calculation of
what the receipts are, that percentage goes to quota holders.
Now, it does come from the top of the pool and I know there's
some objection to that. But it's one pool at least. And
anyone doing business with the California pool would have,
would be on notice there's quota that has to be dealt with and
then they can choose whether or not to have business
transactions that involve the California pool. And if the
percentage diminishes gradually over time in a way that's
designed to recognize the value of the quota and not rob
anybody of his quota value, you could eventually work toward
uniform prices.

So I have no idea if this could be figured out, but if
it could be, we certainly need the help of all the Economists
to figure it out. Mr. Beshore?

MR. BESHORE: Marvin Beshore. If I might, and I don't want
to go into a long discussion, it's -- but just to make it known
and clear on the record -- it's the position of the
cooperatives that the quota rights under state law are vested
property rights which must be recognized pursuant to the
Federal Statute authorizing this hearing. And therefore, they
are not subject to erosion or dissipation by Federal
Regulation. I'll leave it at that, but I want that noted.

JUDGE CLIFTON: Thank you. Mr. English?

MR. ENGLISH: First, your Honor, thank you, and we
certainly will do so, but clearly not today. And, in fact, it
may be later and allow things to move forward.

I just want to make sure I had all of it, because at
least when you said procedurally to me before going on the
record that you might want to recall Dr. Schiek, I thought you
suggested that there were a couple questions you wanted to ask.
Is this the whole -- does this encompass it or is there more?

JUDGE CLIFTON: No. No, well, I guess my overall concern
is, how does USDA deal with the fact that it does not control
what California is going to do with respect to quota? It
doesn't control changes with regard to how quote is paid, it
doesn't control whether quota is issued, it doesn't control
anything about quota. So how does, number one, how does a
Federal Order deal with figuring out what part of receipts would be paid over to quota holders, so that's the first thing.

And then the second thing is, how to work toward uniform pricing. And then the third thing is, how to compensate quota holders for the full value of their holding.

If, for example, there were some sort of a formula and California decided to go on and retire quota and appropriated the money to do it, or that would be -- that would be an impact that wouldn't change anything under the Federal Order because the Federal Order would pay a certain percentage over to the quota holders, and if there are no more quote holders, there would be no more percentage. So I don't know how it can work, I just think if there's to be a Federal Milk Marketing Order in California, this is probably the biggest problem.

MR. ENGLISH: And thank you, your Honor, and obviously we heard you yesterday with some of your questions. Let me respond very briefly, I don't want to get into a legal debate and upset our apple cart with timing, but obviously, I fundamentally disagree with Mr. Beshore on what the statute means and requires. And, you know, we certainly believe that, yes, there's the Farm Bill language, but because it was not written with language such as notwithstanding any of the provision of law, because it was not written to physically amend Section 608c(5)(b), the Secretary, in our view, needs to read all of those and make them consistent, and one cannot
overrule the other. That is our thesis from yesterday.

So, yes, especially I wrote down number two, the Secretary needs to look at this issue, which is why we tried to provide at least one piece yesterday. So I thank you for that, I don't want to, again, get into an extended legal debate today, but I wanted to make sure -- and I just wanted also to say I think that there is something that gets lost in this proceeding, and that is that the quota money isn't just extra dollars lying around. That's money that is coming out of other dairy farmers. And one of the questions is, who are those dairy farmers going to be, and how long should that continue?

So I'm ready to go with dairy farmers.

JUDGE CLIFTON: Thank you. Ms. Hancock?

MS. HANCOCK: I just want to make sure that in the discussion of value and quota that what's also not lost in this is the treatment, the historical treatment for exempt quota as well and the values that are assigned to that. And I'm not saying that I agree with kind of an extended buy out, but to the extent that that is an option that's being considered, I think it is important to consider the exempt quota as well, as well as the treatment for the out-of-state producers and the impact it would have on them in changing the system.

JUDGE CLIFTON: Thank you. And I hope you will have the true solution. I'm looking forward to it. No pressure, right? No pressure.
I have said it before, I'll say it again, I am so grateful for the experience and the wisdom and the help that we are getting from every participant in this proceeding. It's very much appreciated.

All right. Let's see, let me ask, let me ask the two dairy producers who will testify first, to come to the podium together. Have you discussed, and as each of you responds to this you can speak into the microphone and say who you are before you tell me your answer. Have you discussed which one of you will go first?

MS. LOPES: Yes, I will. Linda Lopes.

JUDGE CLIFTON: Linda Lopes will go first. All right. And do you have any document that you want to have made an exhibit?

MS. LOPES: Yes, I have my testimony.

JUDGE CLIFTON: All right. And do you have copies of it to distribute?

MS. LOPES: Yes, they have, it's been taken care of.

JUDGE CLIFTON: All right. And people are holding up their copies. So let's see, who still needs them. I would like a copy, and I would like to make sure Ms. Frisius has her four.

All right. And Ms. Duarte, will you be involved at all in Ms. Lopes' testimony? Will you be asking her any questions from the podium, for example?

MS. DUARTE: No, I won't. I have testimony from my heart and my mind. I have not prepared anything to pass out.
JUDGE CLIFTON: All right. Very good. Then I would invite you to be seated until Ms. Lopes has completed her testimony and then we'll call you.

Ms. Lopes, you may be seated in the witness stand, which is this big table to my right. Please raise your hand if you would still like a copy of the testimony of Linda Lopes, California dairy producer? It appears they have all been distributed. Ms. Frisius, will this Exhibit be 149?

MS. FRISIUS: Yes.

JUDGE CLIFTON: Yes. Exhibit 149, (Thereafter, Exhibit 149, was marked for identification.)

JUDGE CLIFTON: I'm marking my copy. Ms. Lopes, I'll swear you in in a seated position. If you will raise your right hand, please.

Do you solemnly swear or affirm under penalty of perjury that the evidence you will present will be the truth?

MS. LOPES: I do.

JUDGE CLIFTON: Thank you. Please again, state and spell your name.

MS. LOPES: Linda Lopes, L-O-P-E-S.

JUDGE CLIFTON: Thank you. You may proceed.

MS. LOPES: My name is Linda Lopes and I'm a dairy producer from Turlock, California, where my husband and I own and operate a 500 cow dairy operation for 48 years. We ship our
milk to California Dairies, Inc. I currently serve as
President the California Dairy Women, am a member of the
California Dairy Campaign, California Farmers Union,
Progressive Ag Organization, the National Family Farm
Coalition, and California Milk Advisory Board.

I greatly appreciate the opportunity to testify here
today in strong support of the Federal Order proposal put forth
by California Dairies, Inc., Dairy Farmers of America, Inc.,
and Land O'Lakes. An important aspect of the proposal is to
maintain our state quota system. I realize the proposal will
not solve all the problems of the California dairy producer,
but it is a start.

I do not claim to be an expert on milk pricing, but I
am in charge of the financial business of the dairy operation.
This job has been very difficult. I have become an expert in
balancing a checkbook and knowledgeable in the business's
income and expenses. I know that we're not covering our cost
of production. Our dairy has been on the CDFA cost study for
over 20 years and I know the majority of the dairies have been
losing money.

In the past 15 years, I have testified many times at
the California Department of Food and Agriculture in order to
correct this bad situation, only to be granted pennies or
nothing. I had high hopes when Karen Ross was appointed
Secretary of Ag. I thought she would be a change. She wasn't.
She has been the biggest disappointment for California dairy women. She has done nothing of significance for California dairymen.

The California dairy business at this moment is disintegrating before our eyes. I hear from many distressed dairy wives who say they cannot take this constant pressure much longer. Thousands of cows have been sold for beef. We have lost many dairies, many dairymen, some committing suicide. The dairy industry in California has split many families. My husband and I have worked side-by-side to maintain our operation, along with our son, our only child. When our son returned from Cal Poly he was excited to be back on the dairy. When he married in 1998, we made him a partner. He became the manager, as we cut back on some of the physical work. He had a difficult time handling the stress of the business, the work and not covering the cost of production during the bad years. There have been more bad years than good years. On July 3, 2013, he left the business without notice. We had to give him a settlement for his partnership. Since he left, my husband and I had to step up. We've taken over his jobs. We have not seen our grandchildren since Christmas. They loved the dairy. This has been the most difficult thing I've ever had to endure. He resents us for being in the dairy business, which led him into the business. If the Federal Order had been in place, we would have been paid at least a dollar more per hundredweight
and things might have been different today for our family.

I realize this hearing is not for the purpose of pricing milk -- no, I realize this hearing is not for the purpose of pricing milk, however, we have to have a more stable pricing system if we want the younger generation to continue the dairy industry.

Today, many dairymen are changing to trees. Trees are a lot less work and a lot more money. I think the Federal Order will be the first step as it puts the California dairy farmers in line with other producers throughout the federal system. The cost of production must be part of the equation. The Margin Protection Program does nothing for us in California.

In conclusion, it has been far too long that dairy producers in California have been at this disadvantage. We need to be on a level playing field. I urge you to adopt the Cooperatives' Federal Order proposal. I thank the United States Department of Agriculture for the opportunity to present this testimony today. Thank you.

JUDGE CLIFTON: Thank you, Ms. Lopes. How long have you and your husband been operating the 500 cow dairy operation?

48 years, you say?

MS. LOPES: Yes.

JUDGE CLIFTON: Has it been located on the same ground that entire time?
MS. LOPES: No, we originally started in Merced, and then we bought in Turlock in 1981, so we have been there for 34 years.

JUDGE CLIFTON: And I'm sure that when you included your son in the partnership, you expected that to be a benefit to him. When was that?

MS. LOPES: That was in 1998 when he got married, we made him a partner.

JUDGE CLIFTON: And were there good years for a time?

MS. LOPES: You mean as a business having good years or good years?

JUDGE CLIFTON: Yes. Yes, financially for the business.

MS. LOPES: Yes, but we have had a lot less good ones than bad ones.

JUDGE CLIFTON: Has that been true ever since 1998?

MS. LOPES: Oh, that's been ever since the beginning, I believe. But at the beginning, as long as you worked hard, you could get through it. But today that is not true. Today it is so far off, like today, say the cost of production is $19.00 and we're getting 15, so that's a big difference to make up. And two people in their 60's can't do all the work, you have hired help that you have to pay.

JUDGE CLIFTON: There's one word in your statement that I think we may want to change on the record copy. It's on Page 2, and it's in the top paragraph, which is just a partial
paragraph. And when you say fourth line up from the bottom of that paragraph, "this has been the most difficult thing I have ever had to endure." We just need to respell thing, is that right? Do you see it? I'm looking at it.

MS. LOPES: Yes, I have "think". I'm sorry.

JUDGE CLIFTON: No problem. We can fix it now. All right.

So Ms. Frisius, do you see where I am?

MS. FRISIUS: Yes.

JUDGE CLIFTON: Thank you. So we're just changing the word "think" to "thing". And is there anything else you would like to add before I invite questions from all the people here?

MS. LOPES: No, I just think we really need this at this time to finally get some stability in the industry here in California. It's been needed for quite some time.

JUDGE CLIFTON: Now, when you say civility --

MS. LOPES: Stability.

JUDGE CLIFTON: Thank you. Thank you. Stability.

MS. LOPES: It could be civility too, as far as that goes.

JUDGE CLIFTON: Who would like to ask the first questions of Ms. Lopes? Mr. Beshore.

CROSS-EXAMINATION

BY MR. BESHORE:

Q. Marvin Beshore. Thank you for coming and testifying today, Ms. Lopes. I have just one question. You have heard, you were here in the room when there was some discussion this
morning about quota, the quota program, and you, of course, had
prepared your comments here today before -- before coming, and
made the statement, "an important aspect of the proposal is to
maintain our state quota system." So I would just like you to
elaborate on that. Tell us why that was part of your statement
and how it's -- how it's important to you.

A. Well, we have a lot -- there's value to our quota. We
have a lot of money invested in our quota depending upon how
much quota you have, and to just take it away I don't think
that would be fair. So there would have to be some way to --
to, I don't know what would be the right way to do it, you
know. But doesn't some other states in the Federal Order
system also have quota? Isn't there another state that has
quota?

Q. Actually --

A. Is it Ohio or someplace?

Q. No, there are not.

A. There are not? Somebody always says there is someone
that does.

Q. No.

A. That's what my husband always tells me.

Q. Virginia has a system called the Base System, which
sometimes is thought to be somewhat similar, but it is
actually, it is actually quite different. So on your, so,
what, do you own quota?
A. Yes.

Q. Okay. And what portion of your production roughly is covered by quota?

A. It's not a large. I think maybe like 30 percent. Yeah. Some people have a lot more. But, you know, there's a value to that quota on your financial statement when you look at it. But I know that when quota started, we weren't supposed to do, to have a value, but it's become a value and people have spent a lot of money buying quota, and there should be some way to compensate for that.

Q. And it is a value on your --

A. Yes, definitely.

Q. -- on your balance sheet?

A. Yes.

Q. So when you go to the bank --

A. Yes.

Q. -- that's part of your financial statement?

A. Yes, yes, and I would hate to lose it. Yes.

Q. Thank you very much. That's all I have.

JUDGE CLIFTON: Who next has questions for Ms. Lopes?

Mr. Richmond? And Ms. Lopes, be sure to wait until he is finished talking before you respond.

MS. LOPES: Thank you.

CROSS-EXAMINATION

BY MR. RICHMOND:
Q. Bill Richmond, USDA. Thank you very much for coming here this morning. We appreciate your testimony. We just wanted to thank you, especially, we know you have put a lot of effort into this process so far with your work with California Dairy Women and the California Dairy Campaign, and it's really been a big help to us in the Department in better understanding the California dairy industry. So thank you.

A. Thank you.

JUDGE CLIFTON: Are there other questions for Ms. Lopes?

Ms. Lopes, what else would you like us to know before you leave?

MS. LOPES: Well, the dairy business is a good business, and I think we need to do this to help to get it more stable so the younger generation will want to be in the dairy business. You know, the average age for people in the dairy business is pretty high, and if we want it to continue and have a product for our consumer, we have to do something to keep the younger generation wanting to continue with this business.

JUDGE CLIFTON: Thank you so much.

MR. BESHORE: Your Honor, has the exhibit been marked and received?

JUDGE CLIFTON: It's been marked, but not yet received, Mr. Beshore, thank you. Does anyone have any other questions for Ms. Lopes before you determine whether you have any objection to Exhibit 149? No one. Are there any objections to
the admission into evidence of Exhibit 149? There are none.

Exhibit 149 is admitted into evidence.

(Thereafter, Exhibit 149, was received into evidence.)

JUDGE CLIFTON: Ms. Duarte, you may now come forward. Now, I think you will need to pull your chair closer to the table so that your mouth will be at the right distance from this microphone. I'll swear you in in a seated position. If you would raise your right hand, please.

Do you solemnly swear or affirm under penalty of perjury that the evidence you will present will be the truth?

MS. DUARTE: I do.

JUDGE CLIFTON: Thank you. Please state and spell your name.


JUDGE CLIFTON: I am pronouncing it wrong.

MS. DUARTE: It is the Portuguese.

JUDGE CLIFTON: Thank you. We want to know about you and your involvement in the industry, in addition to your message for us. So you may proceed in any way you like.

MS. DUARTE: Thank you. I would apologize for not preparing anything, but this is, I was asked to come down weeks ago, and to put something on paper, I was having a difficult time. I attended and presented testimony in Sacramento, and it
just seemed like you get tired of putting things on paper. And sometimes coming from your mind and your heart is better.

My husband and my son and I own and operate a dairy in Elk Grove, California, where, at one time we had 28 dairies and today we have 6. My son did not go to college, he went to a JC, and because of an injury back in, I would say 18 years ago that my husband got, my son did not pursue his college career, and he stayed home, and he has been with us ever since then.

Five years ago my husband suffered a stroke. And all the responsibility of the dairy fell on my son's hands on the morning of May 22nd, 2010. And he is with us struggling, working hard, doesn't have anytime to spend with his children. He's got three kids, two boys and a girl. And I look at the dairy industry and I see there is no future for my grandchildren. In fact, I have sat down with them and I basically told them, "If you guys decide you want to think about coming to the dairy, I'm going to smack your hands with a ruler." Because it's a lot of hard work, a lot of stress. The rewards are you work as a family, but the negative is every month you are eating away your equity.

We do have approximately 56 percent of our milk is quota. Our quota value is 56 percent. We belong to, we ship our milk to DFA. And I am the Vice President of California Dairy Women, which we began our organization in 1996. And like I mentioned, I've been to Sacramento many times and presented
testimony.

In our area, the reason why we have lost a lot of dairies is the volatility. There's quite a few young dairymen who could not stay in business any longer. They did not see a light at the end of the tunnel. The equity was being eaten away. And then when you have investors coming in and offering large amounts of money for acreage to turn those nice dairies into walnut trees. In our area it's either walnut trees or grapes. And in the past four years there has been three large dairies that have gone into walnut trees and one dairy behind me who is being sold, I believe it's this Thursday, and one of them, part of the parcel will be into walnut trees.

I believe it is time for a change that California goes into the Federal Order. We have suffered enough volatility. It is time to change hands on how our milk is being priced. I realize that there is a lot of opposition, but in order for us to have a healthy dairy industry on the farm side, if there's no changes, we're not going to have a local milk, such as I stated, in Elk Grove, from 28 dairies down to 6. It is very sad. It is a very sad situation.

I have had, my road where I live on is very, very busy now because Elk Grove is growing, and I have had people who stop by don't realize how far we are from Elk Grove, that they have run out of gas, because they go down and visit the local correctional center. And many of them have stated where did
all the dairies go?

We, at one time, had many children come out and tour our dairy, and because of the responsibility that we have incurred in the last five years due to my husband's health, we had to stop it because it took a lot of time. But I'm seeing that the people that lost because we stopped was the children. Because they don't have the advantage of coming out to the dairies and seeing where their milk comes from. And so if we do lose more and more dairies, that is going to be a major impact for the local supply of our milk, and then, of course, the economy of our community, and also the children who will not be able to see where the cows are at.

I support the Proposal Number 1 from the DFA and CDI, and I'm hoping that the Department will see fit that we, in order to have a stable industry on the dairy producer side, that we can have the opportunity to go into the Federal Order.

JUDGE CLIFTON: I don't know where Elk Grove is. Could you describe for me what county you are in?

MS. DUARTE: We're in Sacramento County, approximately 15 miles from Sacramento. My husband and my son, my, actually, my husband and I started the dairy 43 years ago. I am a third generation dairy farmer. My son, like I said, has taken over the responsibility, and at one time I thought maybe my children would be a great business for them. But if this continues, we might not be in business for my children. My oldest grandson
is 11. He's out there driving tractor, pulling calves, very hands-on, so it's nothing where he shies away from work. But like I say, I keep instilling in him, get an education and go find something else to do, because we might not be in business if this continues this way. Equity is being eaten. And we just renewed our loans, our hay loan and our lines, and speaking to our banker, they are very concerned with the loss of dairies that are going out every week. These are not small operations. We're milking 560 cows, and when you see dairies that are going out every week and advertising, sending out to other dairymen, 5, 6, 7, 1000, 1200 cows, it is a signal that things need to be, the pricing system needs to be changed in order for us to have a healthy dairy segment for the producers.

JUDGE CLIFTON: When you say you're a third generation dairy producer, where were the original location -- where was the original location and has that changed over time?

MS. DUARTE: My grandfather started his dairy in Stockton, and then went back to Azures and took my father and my two uncles. And then at the age of 19, my dad remembered how California was a land of opportunity, so he came here at the age of 19. And then my uncle, his brother, followed five months later. They milked cows for, I believe it was almost two years, and then got married and then they started a dairy as a partnership. And then in 1973, my dad bought some property, and along with my brothers, they went and they moved
half of the cows to Escalon, which is in the Stanislaus County area. And then when my dad passed away 10 years ago, my brothers decided, four 4 years ago, to sell the dairy.

And it was a wonderful dairy. It was one of the largest, I should say it was one of the most efficient, because it was president first round barn that milked eight cows at the time in 1973. It was an idea that came from New Zealand. And the dairy is still there. The people that bought the land, also, it's going to go into almond trees.

But my husband and I did start our own dairy. Actually, went into debt before we even got married. At that time, the banks allowed the husband and wife not being married to sign on the dotted line. So we love our area, we love the industry, but the volatility, as I stated, my husband suffered a stroke and it was the effects of the stress. He was very involved with the dairy industry as far as he was a Board Member of Western United for many years. And at that time, him and another gentleman who have also passed, and his sons have carried on the legacy of their dairy, stressed that going into the Federal Order. And here we are years later and we're still talking about it.

JUDGE CLIFTON: When you say equity is being eaten, do you have any numbers for the USDA to consider about the equity being eaten and the business that you are involved in? For example, do you know how much of your equity is lost each year?
Do you know how much your dairy operation is losing? Do you have any kind of numbers like that that would be of assistance?

MS. DUARTE: To give out personal information, I have no problem on that. I'm roughly about $24,000 short each month. I finished our year-end, we are incorporated, became incorporated 2006 because our son is in the dairy business, and we have two other children who are not. So to protect his hard work and dedication, we incorporated. And our year ended October 31st. And of course, by the beginning of October I already know basically, what our standings are. And I don't need $24 milk, I don't need $20 milk. I just want whatever it cost me to produce that milk. We have five employees, and everything has gone up. Each month you look at the bill and there's an added surcharge for this, and an added surcharge for that. And that extra dollar that we would be getting by being in the Federal Order, it would help with all the extra charges that we are getting.

We have become so efficient -- we have been told, "you need to be efficient in order to stay in the business." We have become efficient. We have no other way to tighten the belt. And yet, we're losing dairies, we're losing equity, and I'm only in here because my son wants it. And in the past two years I keep telling him, "Justin, we need to get out." He goes, "Mom, one more year." How could I put a For Sale sign and sell my cows if my son is there working from 4:30 in the
morning until sometimes 8:00 at night. And he does all the
breeding, he does the relieving, the feeding. Not the milking,
we have good relief milkers for that. But to oversee
everything. And I don't have the heart to put a big For Sale
sign because he just pleads, one more year, one more year. So
I told him, I said, "If we do not go into the Federal Order,
Justin, there is no future, so you better start preparing that
we will put this dairy up for sale and join the rest of the
community and put trees in."

JUDGE CLIFTON: What is the name of the incorporated
business?

MS. DUARTE: Duarte Family Dairy, Inc. And hopefully, like
I mentioned, I told my grandsons, please get an education and
go in, if you like the dairy industry, there's other aspects of
the industry that you can become involved in and be in business
with, but not on the farm. But I see my grandson out there
with his dad, and he's literally out there working very hard,
and I'm so proud of him, and I would like to carry on the
legacy to have the fifth generation involved in the dairy
industry on the ranch.

JUDGE CLIFTON: Do you have anything else you would like to
add before I invite questions?

MS. DUARTE: No. I want to thank you for the opportunity
and I do support the Proposal Number 1, as I stated.

JUDGE CLIFTON: Who would ask the first questions of
Ms. Duarte? Mr. Beshore?

CROSS-EXAMINATION

BY MR. BESHORE:

Q. Marvin Beshore. Thank you, Ms. Duarte. Just one question. Can you tell us a little bit and provide, you know, for this record, information about how you acquired the quota on your farm, or how you came to have that quota holding?

A. We purchased it. We purchased every pound of it in increments, as we could. And we have gotten information, like I said, dairies going out of business, and people are buying quota. There is one of the brokers that told me every time some quota is available he's got people buying it, so there is a value to it. And there, hopefully there is, you know, for it to stay in with the value, if we do want to move on to the Federal Order.

Q. Okay. So neither your business, you and your husband's operation, nor your family, actually had any quota issued to you at the time the law was passed in --

A. Very few pounds. Just a couple pounds here and there and that was it. But no -- no 95 percent of it was purchased.

Q. Okay. Very good. Thank you very much. Thanks for coming.

A. Thank you.

JUDGE CLIFTON: Who else has requests for Ms. Duarte?

Mr. Richmond?
Mr. Richmond: Bill Richmond. Thanks a lot, Ms. Duarte, we appreciate it. It's been very helpful.

Judge Clifton: Are there other questions for Ms. Duarte? I thank you so very much. I thank both of you for coming and sharing your heartache, as well as the factual data that the USDA has to have. Thank you.

Ms. Duarte: May I add something?

Judge Clifton: Yes.

Ms. Duarte: My brother, when they sold the ranch, he got the opportunity to work for a local auction yard in Escalon, which is Stanislaus County, just a few miles away from the original dairy where my dad and my brothers and my mom had. And he, him and I have contact almost everyday. And he has shared with me that lately, in the past two months, about a month and a half I should say, that the faces of the dairymen going in to take the cows that are no longer productive to beef, and he said it's very, very sad to see the concern, the stress, the unknown, the uncertainty, the future that lies ahead of the dairy producers. And taking the cows that are no longer producing, hoping that that's going to pay a bill, fill that void between the cost and the income that we're receiving. And when we get our milk check and we see out there what we are getting paid per hundredweight, and it's around $16, it doesn't pay the bills. It does not pay. And that causes a lot of stress amongst the families, husbands and wives, the bankers.
and the dairymen, the dairymen and their suppliers, and it
trickles down on and on and on.

Thank you for this opportunity.

JUDGE CLIFTON: You are most welcome. And thank you.

I think we're ready now for Mr. Gonsalves' testimony.

If you would come forward at this time and take the witness
stand. And I would invite the distribution of any exhibit that
would be introduced through his testimony.

All right. I think there are two documents that are
being distributed, one is the Testimony of Anthony Gonsalves,
and the other is the Exhibits to the testimony. Please raise
your hand if you do not yet have a copy of each. All right.

Let us mark the exhibits first, and then I'll swear in
Mr. Gonsalves. Ms. Frisius, I believe the testimony of
Anthony Gonsalves would be Exhibit 150; is that correct?

MS. FRISIUS: Correct.

JUDGE CLIFTON: Exhibit 150.

(Thereafter, Exhibit 150, was
marked for identification.)

JUDGE CLIFTON: And the exhibits to the testimony of
Anthony Gonsalves would be 151. Exhibit 151.

(Thereafter, Exhibit 151, was
marked for identification.)

JUDGE CLIFTON: I will swear you in in a seated position.

Would you raise your right hand, please?
Do you solemnly swear or affirm under penalty of perjury that the evidence you will present will be the truth?

MR. GONSAKES: Yes.

JUDGE CLIFTON: Thank you. And Mr. Vu, if you will identify yourself and then you may proceed.

DIRECT EXAMINATION

BY MR. VU:

Q. Thank you, your Honor. Bao Vu.

Good afternoon, Mr. Gonsalves.

JUDGE CLIFTON: Oh, no, it's not.

BY MR. VU:

Q. It's morning. Good morning, Mr. Gonsalves. How are you doing?

A. Doing good, thank you.

Q. Thank you so much for being here today, and a special thank you to the parties, the Judge and the USDA for accommodating our schedule. So I'm going to have you just read your statement, and I may interrupt you from time to time to flesh some things out, but I don't anticipate doing so too frequently. So for now, I'll have you just get started, and please keep in mind to read the headings and to read slowly for the court reporter's benefit. Thank you.

MR. ENGLISH: Your Honor?

JUDGE CLIFTON: Yes, Mr. English?

MR. ENGLISH: I'm not going into interrupt the testimony.
What I would like to do, though, is just note that I want to reserve our rights to raise admissibility objections only until after he's read it, and just don't need to discuss it now we can let him go.

JUDGE CLIFTON: Good. Thank you. Yes, you may reserve that right. All right. Then, Mr. Gonsalves, when you give your testimony to us, I want the headings to be included in what you state.

MR. GONSALVES:

INTRODUCTION

Good morning -- not afternoon -- and thank you for allowing me to share my testimony with you today. My name is Anthony Gonsalves and I am President of Joe A. Gonsalves & Son, a lobbying firm, specializing in the representation of clients before the California State legislature. My dad, Joe A. Gonsalves, started the firm in 1975.

I am here to testify in support of the California Producer Handlers Association, Proposal 3, seeking to recognize existing quota value in California, including the value of "regular" and "exempt" quota presently held by a class of producers commonly referred to as "Producer-Handlers" or "Producer-Distributors". While these terms are interchangeable in California, I will call them "exempt quota holders" for the purpose of this testimony, in order to differentiate them from the producer-handler definition used in the federal orders and
as proposed by both the Cooperatives and the Dairy Institute. I have witnessed behind-the-scenes, the legislative efforts involving the Gonsalves Milk Pooling Act and related dairy and quota issues for the past 38 years. The legislative history I will be testifying about today, highlights that a class of quota called exempt quota held by the remaining four exempt quota holders has been an integral part of the California quota system since the conception in 1967.

Q. I'm going to interrupt you real quick, Mr. Gonsalves, I see in your testimony that you state that you --

JUDGE CLIFTON: That -- follow the example of the witness Mr. Vu, and pace your voice accordingly.

BY MR. VU:

Q. Oh, sorry. Thank you.

Mr. Gonsalves, I see in your testimony that you state you have been involved in the Gonsalves Milk Pooling Act and related dairy and quota issues for the past 38 years. Can you give us some of your education and work history following high school?

A. Well, I started out working as a Manager at Thrifty Drug Store, and worked my way up through the ladder, and decided I was more interested in politics so I took a job with the State Senate for a year before starting with my father in 1977. But I think my training started back in 1963 walking precincts for my father when he was running for the State
And I can tell you, he felt so emotionally involved in passing the Gonsalves Milk Pooling Act. I remember when he came home from Sacramento and he literally broke down in his office in tears when the Governor signed that bill.

Q. Perfect. You can continue.

A.

JOE A. GONSALVES

My dad, Joe A. Gonsalves, was a true exemplification of the fulfillment of the American dream. From the humblest beginnings in the farming region of the Imperial Valley, he and his immigrant parents settled in Artesia where they began the first of several dairy farms. He ultimately operated his own successful dairy farm. Then, he was elected in 1958 to serve as a City Council member for the new City of Dairy Valley (now the City of Cerritos). He then served for two terms as Mayor, until 1962, when he was elected to the California State Assembly. When he left to start his career in State office, his dad told him, "Joe, do something for the dairy farmers." And indeed, from 1963 to 1966 that is exactly what he tried to do, though with little success. Finally, in 1967, he introduced AB, Assembly Bill AB 910, the Gonsalves Milk Pooling Act. Which, after a series of amendments, became law on November 8th, 1967.

AB 910 -- THE GONSALVES MILK POOLING ACT
I. Background

Prior to the enactment of AB 910, California dairy farmers were often at the mercy of the processors. Too frequently, dairy farmers would be given little notice of changes in the amount of milk the processors would be willing to accept, leaving such farmers with no place to send their milk product, and placing them in a weak bargaining position to dispose of their perishable product. A number of milk pooling bills were introduced in the 1960's prior to AB 910, including another bill by my dad. These ultimately proved to be unsuccessful. However, because the dairy industry could not reach agreement upon how to achieve a Pooling Plan that it would be acceptable to all sectors of the industry.

Furthermore, before the introduction of AB 910, the Dairy Institute, which of course sought to protect the interests of the processors, had an "iron grip" on the Dairy and Livestock Committee. These factors often served as impediments to successful pooling legislation.

To overcome the obstacles to such enactment of pooling legislation, my dad decided to enlist the help of his friend, Assembly Speaker Jesse Unruh, who ultimately changed the dynamics of the Assembly Dairy and Livestock Committee by merging it with the Assembly Agriculture Committee. The increased membership of the newly merged committee resulted in a decrease of the Dairy Institute's influence. This allowed my
dad to push AB 910 through this first committee in which his
prior pooling bill previously stalled.

My dad worked tirelessly for each vote and closely
shepherded AB 910 through the entire legislative process,
including keeping in constant contact with the Governor and his
administration to avoid the possibility of gubernatorial veto.
For those of you who do not know, the Governor of California in
1967 was our former President Ronald Regan. On Thursday,
July 27th, 1967, at 11:40 a.m., the Governor signed AB 910 (the
Gonsalves Milk Pooling Act). It became law on November 8th,
1967. I have a photograph of my dad and Governor Regan the day
he signed AB 910 into law. That's part of the packet.

In light of the spirited debate and numerous
compromises that resulted in an amendment, in amendments to
AB 910, the bill represented a compromise in unity among all
facets of the California dairy industry. Specifically, because
a simple revenue pooling system as used under the Federal Milk
Marketing Order system would have imposed losses on farmers who
held covenant Class 1 contracts, the Gonsalves Milk Pooling Act
established the alternative "quota system". Under California's
quota system, farmers who had history of Class 1 contracts were
assigned enough quota to ensure them the highest price for that
portion of their milk that had previously been under contract.
Other farmers who did not previously have Class 1 contracts,
were assigned the rights to new quota that was created as
Class 1 sales expanded, thereby opening up, thereby opening the Class 1 market to those who may not otherwise have been able to obtain Class 1 contracts (and Class 1 prices for their milk).

A further balance was stricken to pass AB 910, the issuance of "exempt quota". To a class of producers who were producing raw milk that they processed themselves into a Class 1 finished product, rather than receiving regular quota, these producers were issued exempt quota as part of the quota system. Exempt quota holders were vertically integrated farmers with simultaneous ownership of both production and processing facilities. Because of this, they were not subject to the same pressures of regular farmers who were often at the mercy of milk processors. Thus, much like the compromise that resulted in allocation of regular quota, the exempt quota was issued to recognize the lack of financial assistance offered to them by pooling their milk. The exempt quota was issued as certificates of ownership to the producer entity, the handlers and the handler side, while it still had to report fully to the pool, received the deduction or credit for the volumes of exempt quota owned by the producer.

JUDGE CLIFTON: Now, you have written that a little differently, so I may need you to explain that. Would you read that last sentence again, the one you just read?

MR. GONSAVES: The exempt quota was issued as certificates of ownership to the producer entity, and the handler side,
while it still had to report fully to the pool, received the
deduction or credit for the volumes of exempt quota owned by
its own processor.

JUDGE CLIFTON: So --

MR. GONSALEZ: Producer, I mean.

JUDGE CLIFTON: Yeah, its own producer. So the handler had
to report the producer's exempt quota volume but got a credit
back? Is that right? Do I understand it?

MR. GONSALEZ: Yes.

JUDGE CLIFTON: Okay. Thank you. You may resume.

MR. GONSALEZ: Thank you. In addition to the provisions
for regular and exempt quota, the Gonsalves Milk Pooling Act
required the Director to come up with a formula for pooling,
for a Pooling Plan, and submit it in a referendum to all
eligible market milk producers for their approval or
disapproval. The Gonsalves Milk Pooling Act was quite specific
in certain permissive and restrictive provisions that the
Pooling Plan must contain. After extensive research,
revisions, and testing, the committee and the Department
prepared a draft of the proposed Pooling Plan, which went to a
public hearing held in several locations throughout the state
of California starting in February 1968.

Testimony at these hearings indicated the proposed Pool
Plan needed adjustments and the hearing, the hearings were
continued until May 1968 when amendment was presented. As a
result of this hearing, the final proposed Pooling Plan was submitted to producers for a vote on September 10th, 1968. The votes were counted on November 8th, 1968. Producers gave an overwhelming approval to the Pooling Plan far surpassing the required percentage for approval.

II. Exempt Quota Provisions

As I stated earlier, when the Gonsalves Milk Pooling Act was implemented, the quota system was established to include both regular and exempt quota. In July 1969, there were 49 exempt quota holders. For milk falling within exempt quota, the exempt quota holders paid their farm business units the Class 1 price.

The original Gonsalves Milk Pooling Act stated, however, that in the future, any Class 1 sales exempt quota holders were able to acquire, must have quota for those Class 1 sales, and instead of receiving the Class 1 price for that milk, the exempt quota holders would have to share those new Class 1 sales with the pool. That meant that although they sold Class 1 milk, they would receive a blend price for that milk. This was part of the sacrifice that the exempt quota holders had to make in conceding to the Gonsalves Milk Pooling Act, and part of the compensation that they gave up in order to receive their exempt quota. If they had not voted for the Pooling Act, they could have continued to grow their Class 1 market and continued to reap the benefits and higher payments...
for their increased Class 1 sales. By accepting the volume of
exempt quota assigned to them, they gave up the opportunity for
higher, for the higher sales.

It is very clear that from the beginning the
legislative intent was that the California producer holding
exempt quota in 1967 would participate in the quota system by
receiving exempt quota assignments in proportion to their
historic production.

I have included as exhibits various documents
supporting the legislative history. I believe it is clear in
these documents that the legislative intent was that exempt
quota holders be considered part of the quota system and the
foundation of AB 910.

BY MR. VU:

Q. I'm going to interrupt you really briefly,
Mr. Gonsalves.

And so as I look through the exhibits, the way I
understand they are organized, and you can correct me if I'm
wrong, is that the first exhibit, generally, is the enacted
legislation and then the exhibits following the enacted
legislation are the legislative history leading up to that; is
that correct?

A. That's correct.

Q. Who compiled all these exhibits that are in
Exhibit 151?
A. Well, my office and I compiled all the exhibits from the files my father kept from 1966 on, on Milk Pooling.

Q. And so it sounds to me like these are files that are maintained by your firm; is that correct?

A. That is correct.

Q. And how did your firm come to obtain these documents?

A. Well, the documents are all public record. The different ones from Legislative Council and the Senate Ag Committee actually came from the Policy Committees and from the attorneys for the legislature.

Q. Perfect. And in the interest of time, subject to Mr. English's admissibility objection, of course, I'm going to just highlight a few of the exhibits as we move forward that may be helpful to the USDA. So looking now at Exhibit 151, which is your exhibit packet; is that correct?

A. Correct.

Q. Exhibit A-1 is the Gonsalves Milk Pooling Act as it was enacted; is that correct?

A. That's correct.

Q. And then turning to Exhibit A-4, which is a series of photographs, can you explain to me what those photographs are of and why you include them here?

A. Well, for the historical theme I think it's very important to realize the history of the Gonsalves Milk Pooling Act. And these were pictures that were taken the day that the
Q. And then looking forward to the next section that
starts off with 1977 Amendments. I just want to be clear for
the record, you didn't become involved with the firm officially
until 1977, correct?
A. That's correct.
Q. So in with regard to these 1977 amendments, were you
involved in what you are about to testify to?
A. Yes.
Q. And being involved in these 1977 amendments, did you
have to go back and learn the history the legislative history
of the original Gonsalves Milk Pooling Act and how it came to
fruition?
A. If you had the opportunity to share in Thanksgiving
dinners and Christmas dinners, you were getting history on the
Gonsalves Milk Pooling Act on a regular basis.
Q. Perfect. You may proceed.
A. 1977 AMENDMENT TO GONSALVES MILK POOLING ACT.
In 1977, AB 1110 was introduced by a Assembly Member
Barry Keene on behalf of the producers. AB 1110, as
introduced, had a requirement forcing exempt quota holders to
share all their Class 1 sales with the pool, essentially doing
away with the exempt quota. After much debate and negotiation,
that proposal was removed. In its place was a provision
allowing exempt quota holders to buy additional exempt quota,
reaffirming the commitment to preserve the exempt quota as part of the quota system.

Specifically, in Assembly Ways and Means Committee, AB 1110 was amended to provide for the exempt quota holders to increase their amount of exempt quota. In this committee, this amendment was adopted over the sponsors and the authors objections. The exempt quota allowed under this amendment, was part of an overall amendment to the quota system, and the exempt quota acquired under this amendment, was part of the California quota system.

During the discussions about the proposed amendment there was some opposition from the dairy industry to allowing exempt quota holders to buy more exempt quota. Director Richard Rominger, from the Department of Food and Agriculture, wrote a letter calling for a meeting to help mediate the dairy industry's differences. If they came to an agreement, AB 1110 would be able to move forward in the legislative process.

After the meeting at the Department of Food and Agriculture and after all parties involved in those discussions reached a compromise position, the dairy industry agreed to support AB 1110, which included the containment, included the continued allowance of exempt quota. As you will see in Exhibit B-5, my dad composed a letter showing they had all come to a consensus and AB 1110 was signed into law three months after the Rominger meeting. As with the initial enactment of
the Gonsalves Milk Pooling Act, the quota system discussions, negotiations, and amendments, always included the exempt quota.

I have included as exhibits, various documents demonstrating the legislature's intent with the respect of the 1977 amendments.

Q. I'm going to interrupt you again, Mr. Gonsalves, and I'll let you grab a sip of water, too. So is it your understanding that the effect of these 1977 amendments were to, among other things, allow for then present exempt quota holders to obtain more exempt quota?

A. That's correct.

Q. And then turning to Exhibit B-1, which is, of course, in marked Exhibit packet 151, B-1 is, excuse me, B-1 is AB 1110 as enacted; is that correct?

A. That's correct, that's the chapter version.

Q. And then continuing to highlight only some of the more interesting exhibits, I'm going to move forward to B-3. Can you describe what this letter is?

A. B-3 is the letter from the Director of the California Department of Food and Agriculture, Mr. Rominger, requesting the dairy industry come to a meeting to try and resolve the issues an AB 1110.

Q. And then turning to the second page of the letter, it looks like it is actually in enclosure attachment to the letter. Joe Gonsalves is a person who received an invitation
in accordance with this letter, does that look correct to you?

A. I'm going to have to find it.

JUDGE CLIFTON: Just the next page after the letter, B-3.

MR. GONSALVES: Yes, it is.

BY MR. VU:

Q. And that meeting was ultimately held on July 14th, 1977, correct?

A. Correct.

Q. Then turning to Exhibit B-5, can you please describe that to me?

A. This is a memo written by my father that was distributed to the members of the Senate Finance Committee, which is the Fiscal Committee of the State Senate, and he is letting the members know that they had their meeting and everyone in the dairy industry were in support of the bill, and that he did not want to have any additional amendments to taken to the bill.

Q. So it's fair to state that a meeting was held on July 14th, 1977, correct?

A. Correct.

Q. And then as a result of that meeting, there is a memo from your father stating that the dairy industry had reached a compromise with regard to AB 1110, correct?

A. Correct.

Q. And the ultimate affect of AB 1110 was to allow those
presently, then presently holding exempt quota to obtain more
quota, correct?

A. Correct.

Q. And AB 1110 was ultimately enacted with that provision?
A. It was signed into law, yes.

Q. Perfect. I'll let you continue reading your testimony.

A. 1993 Amendment to the Gonsalves Milk Pooling Act

In 1993, Senator Dan McCorquodale introduced
Senate Bill SB 688. SB 688 revised the milk pooling statutes
to produce a fixed deferential of $1.70 between quota and
overbase. AB 688 also increased the ability of producers
holding exempt quota to capture the Class 1 price on more of
their production through additional exempt quota purchases.

My dad and I became involved in SB 688 when it was
heard in a subcommittee of the Senate appropriations hearing
bills that were on the suspense file. My dad presented an
amendment, and it was accepted by the proponents and entered as
an author's amendment by Senator McQorquodale. SB 688 then
went to the Agriculture Committee and through the rest of the
legislative process with our complete support.

This bill was overwhelmingly supported by all the
legislative policy and physical committees, as well as both
floors prior to the Governor's signature. AB 688 became law in
1993 because all the dairy industry gave its support and was
satisfied that AB 1285 would be introduced the following year.
In 1994, Assembly Member Sal Cannella introduced AB 1285 to address the sunset clause contained in SB 688 (which was to expire January 1, 1995). That sunset clause, however, did not affect the additional exempt quota allowed to producer-handlers.

I have included as exhibits to my testimony, legislative documentation concerning AB 688 and 1285. I believe my exhibits clearly show the legislature's intent on including the exempt quota amendments. Through substantive amendments, negotiations, compromises, and debates, the quota system that included both regular and exempt quota, were yet again approved by the industry.

Q. I'm going to interrupt you one more time, Mr. Gonsalves. With regard to exempt quota, what was your understanding of the effect that SB 688 had?

A. That legislation allowed the producer-handlers, producer-distributors, to buy exempt quota with no cap. It was an ongoing provision.

Q. And then you have included, it seems, some legislative history about AB 1285. Can you explain what effect, if any, AB 1285 had on the exempt quota provisions, then existing?

A. We have two legislative counsel's opinions, both on the McCorquodale Bill and the Cannella Bill, that state clearly that the exemption for the producer-handlers was not sunsetting, it was ongoing. But the legislative history on
1285 was very clear that in the McCorquodale Bill it had this language, but it also stated in there the ongoing exemption for the producer-handlers.

We even have a letter from the Republican leader of the senate asking for Governor Wilson at the time, to sign the Cannella Bill so that the deal that was made between the two pieces of legislation would continue, including the producer-handlers exemption.

Q. And the legislative history surrounding SB 688 and AB 1285 are included in your exhibit packet, and are generally Exhibits C and D in their sub exhibits, is that accurate to say?

A. That's correct.

Q. Okay. You can keep on going. Thank you.

A. Attempt to Eliminate Exempt Quota Failed

In 1995, Senator Dave Kelley introduced SB 105. This bill was introduced on behalf of a co-op, otherwise known as "California Milk Producers." They were attempting to reverse what was already agreed upon previously in the SB 688 and AB 1285 package. AB 105, as introduced, would have based the amount of exempt quota held by producers based upon 1978 figures. This bill was soundly defeated on the Senate floor on May 1st, 1995, with a vote of Ayes 10, Noes 20. In order for it to pass, SB 105 needed 21 Aye votes; it came up 11 short and was at a standstill. It was the legislative intent to preserve
exempt quota as part of the quota system.

Shortly after the Senate floor vote, and at the request of exempt quota holders, a meeting was called with the dairy industry. In an effort to have unity in the dairy industry, the exempt quota holders offered a compromise to cap their ability to purchase exempt quota and roll back the purchase date to March 1st, 1995. After this date, the exempt quota volumes were frozen and producers could no longer acquire or purchase any further exempt quota. Any quota acquired after that date was acquired as regular quota. The exempt quota would naturally sunset or expire with the tables of consanguinity when the generational limitations were met. Since that date, the quota system has continued to operate with regular quota and exempt quota, as well as the other pooling calculations for base and overbase production payments.

I have included as exhibits the legislative history on SB 105.

CONCLUSION

Throughout the legislative history of the Gonsalves Milk Pooling Act, the quota system has had many aspects beyond the regular quota held by any producer. The entirety of the quota system in California included both regular quota and exempt quota. Out-of-state milk was not subject to the pool in exchange for not receiving the benefits of a quota system. Together, all of these aspects make up the quota system since 6832
its inception in 1967.

When the USDA considers the quota system in California and the investments made by all quota holders, I respectfully request the investments of exempt quota holders be included in the Federal Milk Marketing Act for California, and the overall aspects of the quota system be preserved in its entirety.

Thank you.

I'm available to answer any questions concerning the Gonsalves Milk Pooling Act and/or the exempt quota that is outlined in California Food and Agriculture Code.

Q. Thank you, Mr. Gonsalves. And I have some questions for you.

So the 1995 amendments to the Gonsalves Milk Pooling Act that you describe in essentially the last section of your testimony, the legislative history supporting that amendment is an Exhibit E to your exhibit packet; is that correct?

A. I'm getting there. Okay. What was the question, I'm sorry?

Q. So the legislative history surrounding the 1995 amendments are in Exhibit E; is that correct?

A. That's correct.

Q. And you also state with regard to the 1995 amendments, that they limited the purchase of the exempt quota to March 1, 1995; is that correct?

A. That's correct.
Q. And you also state in your testimony that after that
date, exempt quota volumes were frozen and producers could no
longer obtain additional exempt quota; is that correct?
A. That's correct.

Q. And is that your understanding of the system between
1995 and the present? In other words, since 1995 and to the
present, exempt quota could not additionally be obtained,
correct?
A. That's correct.

Q. Mr. Gonsalves, what's your understanding of the Federal
Milk Marketing Order system?
A. I have been asked from time to time, because I have so
many friends in Congress and United States Senate, why don't I
lobby in Washington? And my patent answer for that is, "I
don't lobby foreign governments." I have no idea how the
Federal Order works.

Q. Have you ever read a Federal Milk Marketing Order?
A. No, I have not, no offense.

JUDGE CLIFTON: I think that's my favorite line from this
entire hearing.

MR. VU: I think that's it for my direct, for now, I'll
step aside.

JUDGE CLIFTON: Thank you, Mr. Vu. Ms. Hancock?
MR. VU: Oh, no, I will not step aside yet. Your Honor,
I'd offer Exhibit 150.
JUDGE CLIFTON: Does anyone wish to ask questions just on 150? We'll just start with 150, before we get to the exhibits.
So just 150, does anyone wish to ask Mr. Gonsalves questions about anything before you determine whether you have any objections to the admission of Exhibit 150? No one. Is there any objection to the admission into evidence of Exhibit 150?
Mr. English?

MR. ENGLISH: Your Honor, I said I would reserve my rights under of admissibility. And while I may know where this may be going, nonetheless, I rise to object on three grounds of various sections.

Certainly, before he joined the firm in 1975, and while he might have been visiting legislative offices, his testimony about things that happened before '75 are, and appear to be hearsay, and it's even double hearsay when -- may appear to be harmless, but nonetheless it is double hearsay when he puts in, when he left to start his career in the State office, "His dad told him, Joe, do something for the dairy farmers." So he's got what the grandfather told the father, which is double hearsay.

And there's other hearsay throughout this. For instance, the statements about before '75 when the committee was reconstituted about the so-called influence the Dairy Institute had.

I would also say that legislative history is not
something that is to be testified about, although a lot of
people have done it, and, in this proceeding, but legislative
history is a term of art. And frankly, he's attached a lot of
it, although some of the things he's attached are individual
statements of individuals, but there is legislative history in
the attachments. But to the extent that he says, this is
legislative history, or this is the intent, or this is what was
meant, that is objectionable on the grounds it's legal opinion
or is an attempt to offer his statements as legislative history
as opposed to what the actual legislative history is.

So we object to that extent. And again, I know how the
ruling is going to go, but we need to note the objection.

JUDGE CLIFTON: Yes. I value very much that objection
because I think it is a useful caution, nevertheless, it's
overruled, and it would not keep this document from becoming
part of the evidence.

Does anyone else have any objection to the admission
into evidence of Exhibit 150? No one. I do admit into
evidence, over objection, Exhibit 150. 150.

(Thereafter, Exhibit 150, was
received into evidence.)

JUDGE CLIFTON: Now, with regard to Exhibit 151.

Mr. English, the same objection you just made will apply here
and you are welcome to add to it if you wish. Is there anyone
that wishes to question Mr. Gonsalves before determining

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whether you have any objection to the admission into evidence of Exhibit 151? No one. Is there any objection, in addition to what Mr. English has already stated, which will be applied also with regard to Exhibit 151, any additional objection by anyone? I see none. Exhibit 151 is admitted into evidence, over objection.

(Thereafter, Exhibit 151, was received into evidence.)

MR. VU: I will now step aside.

JUDGE CLIFTON: Thank you, Mr. Vu. So people are saying it is time for a break before cross. Yes, it certainly is. It's already 10:45. Please be back ready to go at 11:00.

(Whereupon, a break was taken.)

JUDGE CLIFTON: We're back on record at 11:06. Who would like to ask the first questions of Mr. Gonsalves?

MR. GONSALVES: Your Honor?

JUDGE CLIFTON: Mr. Gonsalves?

MR. GONSALVES: On the objection of hearsay, I would like to respond to that, if I may.

JUDGE CLIFTON: I'm sorry, what, Mr. Vu?

MR. VU: That's okay.

JUDGE CLIFTON: Go ahead, Mr. Gonsalves.

MR. GONSALVES: On the question of hearsay on the Dairy Institute's iron grip on the committee back during Milk Pooling, and also on what my grandfather said to my
father, my father wrote a book called A Capitol Life. And that book is in the State library and the State Legislative Library, and those were quotes taken out of his own biography. Thank you.

JUDGE CLIFTON: Thank you. A Capitol Life, how is that Capitol spelled? How did he spell it?

MR. GONSAEVES: With an O.

JUDGE CLIFTON: With an O. Okay. Thank you. Mr. English, you may proceed.

MR. ENGLISH: I do want to respond briefly. As we've heard a lot in the news recently, what's written in a book isn't necessarily true. My hearsay objection stands.

JUDGE CLIFTON: Understood. Understood. And hearsay is admissible in USDA proceedings. Of course, the trier of fact needs to determine how reliable hearsay is. Mr. English?

MR. ENGLISH: Thank you.

CROSS-EXAMINATION

BY MR. ENGLISH:

Q. Mr. Gonsalves, I understand that you don't have a lot of experience with Federal Milk Orders, but you agree you're testifying in a Federal Milk Marketing Order hearing today, correct?

A. Correct.

Q. Okay. Have you read the proposal as submitted by the California Producer Handlers Association, which is
Proposal Number 3?

A. Yes.

Q. Okay. Have you read -- so that, it's my understanding that there's actually going to be specific language offered at some point in time to, well, I guess I should say, is there specific language, do you know the specific language to be offered to implement what is in the Hearing Notice Exhibit 147235?

A. Yes, I understand.

Q. Have you seen that language?

A. No, I have not.

Q. So you don't know whether it deviates in anyway from the language that appears on page 47235, do you?

A. I do not.

Q. Okay. You, yourself, raised the issue of consanguinity. And first, for the record, that's not a term that everybody uses everyday. What exactly do you understand that term to mean?

A. The producer-handlers in the statute has a definition what a producer-handler is. They can not sell their business and the people that buy the business then has the exempt quota, it has to be bloodlines and moving down the bloodline.

Q. So consanguinity --

A. Family members.

Q. -- consanguinity would be the degrees in which you
stand in place with the person who owns the right today; is that right?

A. Correct.

Q. Okay. And there are limits at some point to what can happen with that; is that correct?

A. That's my understanding.

Q. Okay. And again, understanding that you don't have a lot of that information on Federal Orders, do you know what the term individual handler pool is?

A. No, I do not.

Q. Okay. Do you understand that to the extent that producer-distributors in California hold exempt quota, they are not obligated to pay the California pool on that volume?

A. Correct.

Q. Okay. And that is what you are asking to be continued in a Federal Order, correct?

A. If the Federal Order is going to recognize the quota system, in the California quota system you have both the normal quota and the exempt quota, and they should recognize both.

Q. Well, my question was, do you understand that if it goes into a Federal Order, as your group is proposing, that effectively that volume that is subject to exempt quota of Class 1 sales, would not be shared with the other order producers?

A. That's correct.
Q. Okay. Now, you used, you did use the term producer-handlers and distinguished exempt quota holders from producer-handlers. Do you understand that under the producer-handler definition in Federal Orders, that, first, there is a limit that they have no more than 3 million pounds of total Class 1 sales?

A. That is my understanding.

Q. Okay. Do you also understand that except for a very modest amount of milk, 150,000 pounds, they cannot purchase any other volumes of milk from other sources?

A. I understand that, but I also understand this is a different Federal Order for California.

Q. I am asking you questions as to how you understand it works, sir.

A. Yes.

JUDGE CLIFTON: Now, I guess hearing the exchange between the two of you, were you asking him, Mr. English, how it works in all the existing Federal Milk Marketing Orders?

MR. ENGLISH: Yes, your Honor, but I was also using his own term of producer-handlers, which he was distinguishing from exempt quota holders. So it would, and in fact, as I understand it, theirs is a separate provision that wouldn't alter the fact that there would still be a producer-handler definition which would work under the Federal Orders. So in fact, it would be under both, it's just they are actually
asking for a different provision.

JUDGE CLIFTON: Okay. Ms. Hancock, let me hear from you then I'm going to ask Mr. English to ask his question again.

MS. HANCOCK: Your Honor, we have made clear as this witness has testified, he's here to talk about the legislative history. He's already said he does haven't any experience or knowledge about Federal Orders. We will have a witness that will put in our language. We will also have our producer-handlers that will testify about how it works for them and what they are proposing. But I think trying to trap him into some language or some admissions about how it would work in a Federal Order system, when he's already said he doesn't have any experience or knowledge about that, is outside the bounds of his testimony, and it's not reflective of the positions he's here to talk about.

JUDGE CLIFTON: Thank you, Ms. Hancock. Anyone who testifies here has two opportunities. The first is to share what they know and the second is to learn something new.

I have no objection to any questioner of a witness making the witness aware of certain things and asking their opinion about it, but I'm not sure, Mr. English, the way you asked your question, I'm not sure that it -- I would like to you start again.

MR. ENGLISH: I will certainly rephrase it and go back, but your Honor, I'm presented with two problems not of my making.
First, the witness said, "I'm hear today to testify in support of," I'm sorry, "I'm here to testify in support of California Producer Handlers Association Proposal 3." So that's what he's here to testify about. He didn't say, "I'm here to give you legislative history." If he said, "I was here to give you legislative history," and hadn't said, "I'm here to support Proposal 3," then Ms. Hancock might be right. But she didn't do that.

Number two, I am faced with the problem that I don't have the actual language of Proposal 3 in front of me. So that's not my fault, and it's a result of a drive-by witness which we have agreed to allow to come in early.

JUDGE CLIFTON: A drive-by witness?

MR. ENGLISH: Well, I can't say parachute because he drove.

MS. HANCOCK: I guess first off, I'm not entirely sure how we have kind of taken what feels like a little bit more of a hostile approach.

This would have been our first witness whether we went now or whether we went tomorrow, it is just that Mr. English has been telling us that we would be putting our case on since Friday of last week, and so we asked him, we also told him that if it didn't work out we would be happy to accommodate all of his requests. So he's not at all disadvantaged by the fact that Mr. Gonsalves has been our first witness. Our position hasn't changed. Unfortunately, we can only put on one witness
at a time, and so you have to eek out the information. We certainly haven't had the benefits of all of Mr. English's testimony, but that doesn't mean that one witness then becomes the voice for the entirety of the case.

As his witnesses have done, they have limited what they were testifying to. Mr. Blaufuss said specifically he would not be talking about quota, that would come with the later witness. In this case, this witness is here to talk about legislative history that supports our proposal, but he's not here to be the entirety of our case.

JUDGE CLIFTON: So do you want -- do you want to hear from this witness that he's not here to talk about quota and he's not here to talk about exempt quota? You don't want to hear that from this witness?

MS. HANCOCK: I didn't say that. I'm not sure what --

JUDGE CLIFTON: Okay. All right. Thank you. Mr. English, you may resume.

BY MR. ENGLISH:

Q. Thank you, your Honor.

So I believe where I was trying to go is that thinking about the existing provision in Federal Orders and the provision that would be in this Federal Order separate and apart from whatever language we have yet to see on Proposal 3, do you understand that producer-handlers, in addition to not being permitted to sell more than 3 million pounds of Class 1
milk to include not to lose their exemption, that they cannot purchase more than 150,000 pounds from outside their operations?

JUDGE CLIFTON: And in, in that phrase, Mr. English, you are using producer-handlers in the existing Federal Milk Marketing Orders; is that correct?

MR. ENGLISH: Yes and no, your Honor. And here -- okay. Let me ask it another different way.

JUDGE CLIFTON: Okay.

BY MR. ENGLISH:

Q. On page 1 of your testimony, Mr. Gonsalves -- this is where I got there, your Honor, from his own testimony. On Page 1 you have emphasized that because of some interchangeable terms, producer-handlers or producer-distributors, you were trying to clarify and speak about entities that you called exempt quota holders, correct?

A. I was referring to how producer-handlers and producer-distributors had been recognized in the California legislature in analyses and in statute.

Q. Okay. But for purposes of this testimony, because you understand that there's this other thing under producer, under Federal Orders, and as proposed in the California Federal Order in Proposals 1 and 2, called producer-handlers, isn't that why you, for clarity, tried to use the term exempt quota holders?

A. I think, Mr. English, I tried to make it fairly clear
the last time when I made a cute statement about "I don't lobby foreign governments," that I'm not an expert on the Federal Order, and it would be very difficult for me to be answering questions on that.

If you would like to ask me questions about California legislative history and the statutes, I think I could be of some benefit to you there.

Q. Okay. Well, let me -- I had actually gotten a clear answer from you, that you said you did understand that under the Federal Orders producer-handlers could not sell more than 3 million pounds of Class 1. You already answered that question; is that correct?

A. That is correct. I understand that is --

Q. Thank you.

JUDGE CLIFTON: However, Mr. English, Mr. Gonsalves added that, under consideration here is a Federal Milk Marketing Order that has not yet been promulgated, and that he's holding out the possibility that it might having some different in it.

MR. ENGLISH: And I understand that, your Honor, I'm trying to draw some distinctions, if I can.

JUDGE CLIFTON: Okay. Go ahead and do what you are going to do next.

MR. ENGLISH: Okay.

BY MR. ENGLISH:

Q. You represent a group of people who have a treatment
under the California system for something called exempt quota, correct?

A. Correct.

Q. Okay. Now, do your clients purchase, do any one or more, can you tell us whether any one or more of them purchase more than 150,000 pounds of milk from sources other than their own farms?

A. I don't know the answer to that.

Q. Okay. Fine. Do you understand that today, and in Proposals 1 and 2 as written for this California Federal Milk Order, there is no provision for a treatment of something like exempt quota?

A. That is my understanding.

Q. And if Proposal 3, as written in the Federal Register, if the language that we see, that we haven't seen yet, allows for the removal of the degree of family consanguinity, does that also mean that the exempt quota that exists today in California would be allowed for free trans -- basically transfer to other persons?

A. Not having seen the language --

MS. HANCOCK: Hold on one second.

JUDGE CLIFTON: Ms. Hancock?

MS. HANCOCK: Nicole Hancock. And I'll represent for the record, we put this in our proposal, in our amended proposal, we are not asking for any kind of modification to the tables of

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consanguinity. We understand, at the time that I wrote the initial proposal, I didn't have a full understanding of how the Federal Milk Marketing proposals would work in conjunction with the state statute. Once I had a chance to dive in deeper on that, I understand that it wouldn't, it wouldn't supersede that, and so the state limitations on the consanguinity requirements would remain in place. So we're not at all going to be proposing in this matter any kind of amendment or modification to the Tables of Consanguinity.

JUDGE CLIFTON: Okay. So Ms. Hancock, don't leave. So if I'm looking at language in the Federal Register on Exhibit 1, page 47235, that says, "CPA also proposes to remove the degrees of family consanguinity as it pertains to the ownership of exempt quota, to allow for the continuation of exempt quota transfers within a family." Should I consider that stricken?

MS. HANCOCK: If that's the appropriate mechanism, stricken or withdrawn, whatever the mechanism is to take that off the table for purposes of this hearing.

JUDGE CLIFTON: Okay.

MS. HANCOCK: And I had footnoted that into our amendment, and I probably should have made it clear before now, but it's not something that we are pursuing in this hearing.

JUDGE CLIFTON: Okay. That's helpful. Thank you very much.

MR. ENGLISH: Thank you, this is Chip English, thank you,
Ms. Hancock, that is very helpful.

BY MR. ENGLISH:

Q. Now, notwithstanding that, and with your vast experience in California legislature, there is certainly nothing that would prevent the legislature from changing those provisions in the future, correct?

A. That's correct.

Q. Okay. Now, you reference in your testimony the history of how exempt quota started and how there were some expansions. Isn't it the case that since 1995 there have been some efforts by the California Producer Handlers to further expand their ability to grow exempt quota?

A. There was one bill that was amended to include a provision to allow for the expansion for the producer-handlers. The bill was amended in Senate Appropriations Committee and passed that committee. The bill then went to the floor of the Senate and the bill passed the floor of the Senate to the Assembly. The author of the bill decided that he wanted to change course and amended the bill before it was ever heard in a policy committee in the Assembly, so there was no vote taken on the producer-handler in the Assembly exemption.

Q. So for clarity in the record, when was that?

A. What year?

Q. Yes, what year?

A. I don't have that with me.
Q. Okay. And going back to the question I just asked about consanguinity. In your experience with the California legislature, is there anything to prevent the California legislature in the future from amending the provision to allow exempt quota to be larger?

A. I would say that there, it is possible, but difficult.

Q. But nothing prevents your clients, after Federal Order is adopted, if one's adopted, from going to the California legislature to make that request, right?

A. That's correct.

Q. You referenced 49 exempt producer-handler, sorry, exempt quota holders back in 1967, and then I guess it got down to 6 by 1993; is that correct?

A. I don't know if that's correct.

Q. All right. In the interim, between 1967 and 1978, up through 1978, exempt quota holders were free to buy additional quota and exempt quota to grow their exempt quota?

A. I don't know the answer to that.

Q. Didn't you --

A. Oh, you mean in the amendment in 1978?

Q. Yes.

A. Yes, they were allowed to buy additional exempt quota, I'm sorry.

Q. Okay. And do you though whether they bought any of that quota from some of those 49 businesses who are not in
business today?

A. I do not know the answer to that.

Q. Going to page 3 of your testimony.

A. Okay.

Q. And on the bottom paragraph you used the term "covenant Class 1 contracts". And I may have missed something in this 34 days of hearing, but I don't think I have heard a definition of covenant Class 1 contracts. Do you know what that definition was?

A. That was a term my father used.

Q. But I got to be careful about asking about that.

JUDGE CLIFTON: Go ahead.

MR. GONSALVES: He used to tell the story about the representative from the creamery coming to the dairy farm before Milk Pooling, and having to have a case of his favorite case of booze or stock with his trunk full of meat to be able to keep his Class 1 contracts, and I think that's why he referred to that.

MR. ENGLISH: Your Honor, I object to my previous question.

BY MR. ENGLISH:

Q. I guess what I'm really getting at there, you have the sentence, "Specifically because of simple revenue pooling system as used in the Federal Milk Marketing Order system, would impose losses on farmers who held covenant Class I contracts, the Gonsalves Milk Pooling Act established the
alternative quota system."

And I understand, again, that you have limited
knowledge or no knowledge about Federal Milk Orders, but to the
extent when a Federal Order went into effect, if what it did
was establish a system of pooling of revenues that didn't exist
before that, wouldn't that have also taken from Federal Order
producers who had the privilege of selling to Class 1 plants,
those revenues to share with other producers?

A. Prior to the Milk Pooling Act?

Q. I'm drawing a distinct, yes, I'm drawing a parallel
between price to the Milk Pooling Act, how is that different
from prior to a Federal Order, if you accept with me the
proposition that a Federal Order adoption meant that producers
who sold to Class 1 plants and had the privilege of a higher
price, then had that money shared with the other order
producers.

A. Prior to Milk Pooling, the dairy farmer was at the
mercy of the creamery. They may have had Class 1 contracts,
and 30 days later they did not. They were going to get paid a
different amount. So the quota system was put in place so that
they would have a guarantee for their milk that they produced,
whether it was Class 1 or Class 4, or whatever the class was,
they would have, they would know what they were going to
receive each month from the creamery.

Q. So if the record in this hearing and the history of
Federal Orders were to demonstrate that identical situation existed in Federal Orders and that nonetheless pooling and pricing came along, how is what California did different in spirit than what the Federal Orders did?

A. I think the difference is the dairy farmers had quota, and that quota had a value, and that quota could be sold. And they had a guarantee that their milk would be shipped and taken by the creameries.

Q. And didn't Federal Order producers who had whatever revenue stream before a Federal Order, didn't the Federal Order effectively impose losses on those producers when the Federal Order came in and established no quota for them?

A. I do not know.

Q. Fine. On page 4, on the carry over paragraph, eight lines down, well, seven lines down, you say, "exempt quota holders were vertically integrated farmers with simultaneous ownership of both production and processing facilities."

Do you see that sentence?

A. Yes.

Q. Does that mean in that sentence that all the production they had went to the processing facility?

A. I believe that is the case. When the Gonsalves Milk Pooling Act was enacted, again, my father exempted them because they had their own dairy farms, they had their own processing plant, and they went out and got their own sales. They did not
need protection from themselves and they did not need to share in the pool for their own products.

Q. And turning the question on its head. Did the processing facilities buy only the from the production of the farms?
A. Back in 1968?
Q. Yes.
A. I believe because of the definition at that time there may or may not have been some dairy farmers that were selling their milk to these processors, but that milk would not be included in the exempt quota.
Q. And so going back to my question a few moment ago, do you know whether that has changed, whether today the processing facilities are buying other milk that's not subject to the exempt quota?
A. I believe that several of the producer-handlers are buying milk from other dairy farmers and they are treated the same in the quota system.
Q. That is to say for that milk they have to share, they actually have to pay the pool and share that money with the --
A. That's correct.
Q. -- producers. We're going to turn for a couple minutes, I'm going to flip back and forth, we're going to turn for a couple minutes to Exhibit 151. And you included as the last part of C-5, page, a page, well, I guess it is an entire
document, so it's, you included from the unfinished business, pages 1 through 4.

A. Mr. English, what am I looking for?
Q. You are looking for C-5.
A. C-5.

Q. Can you tell us what C-5 is, please?
A. Unfinished business is the Senate floor analysis essentially. It is done by the Senate Rules Committee, as you can see the Office of Senate floor Analysis.

Q. Okay. So this basically has an analysis of the legislation and then it has a list --
A. And what it means by unfinished business, it means that it has gone through the entire legislative process. It is back for concurrence only. And if passed, it goes before the Governor for his approval.

Q. Were you involved in this particular piece of legislation?
A. Yes.

Q. And were you involved when this unfinished business document was published?
A. Yes.

Q. Okay. At the very end of the report there's a discussion about arguments and opposition, and referencing Consumers's Union. We have had a lot of testimony in this proceeding and we haven't heard from Consumers, but do you
recall in your active involvement, the Consumers Union objected?

A. That's correct.

Q. Okay. And looking at the very last two sentences, was part of their objection that the quota system imposed additional costs on consumers?

A. Because of the $1.70 differential --

Q. Yes.

A. -- price, they were concerned that it was going to cost the consumers more money.

Q. Thank you.

A. And the bill had a sunset, and that's why the Cannella Bill had to be introduced, because the Department and the Governor wanted to see what the results were going to be, and so they did a short sunset on this bill. And finding that there wasn't a big spike in cost to the consumers, the Cannella Bill was passed and we moved the sunset.

Q. Now, turning to E-6.

A. E?

Q. As in English. I believe it is a two-page document.

A. That's correct.

Q. And this was your firm's opposition to Senate Bill 105?

A. Correct.

Q. Okay. And do you recall this document?

A. I do.
Q. Okay. So let me turn to the second page. And first of all, did Senate Bill 105 pass?
A. Senate Bill 105, which this document is referring to, in opposition to the members of the Senate floor received only 10 aye votes.

Q. But my question was did it pass? Did it pass?
A. Well, the bill passed after the language was removed that harmed the Producer Handlers Association.

Q. Okay. Thank you. So let's look at Exhibit 1 for a moment, because the language I think you just said, that got removed would have altered the current law, correct?
A. Correct.

Q. So does that mean that example 1 stayed the current law when the bill was ultimately passed without the piece of legislation that you said harmed the Producer Handlers Association?
A. The bill was introduced to roll back the exemption on quota for the producer-handlers. That portion of the bill was defeated on the floor of the Senate. After a meeting with the dairy producers, there was a compromise to put in a date that allowed the additional quota that the producer-handlers had already purchased from the McCorquodale Bill and the Cannella Bill to stand. And that was an agreement, and that agreement then, was put into the Kelley Bill, and that's when the Kelley Bill passed.
Q. All right. I'm sorry I'm struggling through this. I'm trying to understand, did the legislation that year, in the end, alter your little Example 1 chart?

A. In the Example 1 chart, that is current law that we were pointing out and how that affected them, and if the bill was to pass, it would have altered that --

Q. So --

A. -- from their -- from their purchase of the additional exempt quota that they purchased.

Q. Okay.

A. Example 3 shows what the bill was going to do.

Q. Yeah, and I'm not interested in what the bill was trying to do.

A. Well, you asked if it passed, so I was trying to give you an example how it passed and how it did not pass. To say a bill was introduced and did that bill pass and amendments follow --

Q. I am, sir, I'm trying to get at what change, if any, since you said Example 1 was current law, correct?

A. That's correct.

Q. Okay. After the legislation was passed, when it was all done, the next year, what, if anything, changed in Example 1?

A. The only thing that changed was they were not allowed to purchase additional exempt quota.
Q. Okay. But nonetheless, the chart as you show it, to the extent they had exempt quota, had not changed; is that correct?

A. That's correct.

Q. All right. Now, in your chart you show the PD, I assume that means producer-distributor, correct?

A. Correct.

Q. Pays, and there's an example of a Class 1 of $13.64. And you're showing an arrow from the plant pays to the state, and then you are showing an arrow from the state to the producer-distributor farm. Correct? That's what you show?

A. That's what it shows.

Q. Okay. Did the money actually flow from the producer-distributor plant to the state, and from the state to the producer-distributor farm, or was it an accounting mechanism that where the state wasn't involved in the actual flow of funds?

A. It is a generally an accounting mechanism.

Q. So it might have been the kind of thing we do when we are trying to show people in this complex world how it works, but it wasn't that the actual money flowed, correct?

A. That's correct.

Q. Thank you. Now, to the extent you say the producer-distributor farm receives the $13.64, that is not audited by CDFA, correct?
A. I don't know.

Q. Okay. So on page 5 of your testimony now, back to Exhibit 150 --

JUDGE CLIFTON: May I interject, Mr. English? For the court reporter typing the transcript, you have had three spellings that I would like for you to highlight for us, beginning after Mr. English took you to Exhibit E-6.

MR. GONSALVES: Okay.

JUDGE CLIFTON: So the first one was McCorquodale.

MR. GONSALVES: Yes.

JUDGE CLIFTON: And so would you just spell that from your letter?

MR. GONSALVES: M-C, C-O-R-Q-U-O-D-A-L-E.

JUDGE CLIFTON: And then the next one was Cannella, if you would spell that.

MR. GONSALVES: C-A-N-N-E-L-L-A.

JUDGE CLIFTON: And then the next one was Kelley.

MR. GONSALVES: K-E-L-L-E-Y.

JUDGE CLIFTON: And then you also referred, I believe, to Cannella when you were talking earlier with Mr. English about C-5, and you were talking about the concern about more cost to consumers, and there was a sunset provision, and it was taken away when the price to consumers did not increase. What bill was it that took away the sunset provision?

MR. GONSALVES: The first bill that passed was
Senator McCorquodale's Bill, SB 688. That bill had a provision with a sunset clause. Following the McCorquodale Bill was AB 1285, Cannella, which made some adjustments to that bill, but also removed the sunset clause.

JUDGE CLIFTON: Thank you. All right. Mr. English, back to where you were going.

MR. ENGLISH: Thank you. And thank you for doing that, your Honor.

BY MR. ENGLISH:

Q. So now I'm back on Exhibit 150, page 5 for a few minutes.

A. Okay.

Q. And under item 2, exempt quota provisions, in that paragraph, the third sentence, which is the last sentence, you say, "For milk falling within exempt quota, the exempt quota holders pay their farm business units the Class 1 price."

That's what you say, correct?

A. Correct.

Q. Okay. If that, if you don't know whether that is audited, how do you know that statement to be true?

A. I don't know for sure whether or not the state audits them on a regular basis.

Q. Do you know whether the state audits them at all for that particular issue?

A. No.
Q. Okay. So turning a little lower in that page you are
talking about, and I think we have talked a little bit about
the changes and how exempt quota holders, as you say, would
have to share new Class 1 sales with the pool, and that, as you
say, that meant that although they sold Class 1 milk, they
would receive a blend price for that milk. Your next sentence
is, "that was part of the sacrifice that exempt quotas had to
make in conceding to the Gonsalves Milk Pooling Act." So what
exactly is the sacrifice that they had to make?

A. Well, in instead of receiving the Class 1 price for
their fluid milk, they would get a blend price.

Q. Okay. And do you understand that to the extent Federal
Orders, when they came in and there were producers who were
getting a Class 1 price had to share that with the pool, that
that also happened to Federal Order producers, they had to
share that blend price?

A. I don't know that.

Q. Now, your last sentence on that page is, "by accepting
the volume of exempt quota assigned to them, they gave up the
opportunity for the higher sales." Is that --

A. That's correct.

Q. Okay. So does that mean that as a result of that, they
didn't grow?

A. I would say as a result of that, we only have four
left.
Q. Okay. And do you know whether those, if any of those four have grown since that time?
A. I believe they all have.
Q. Okay.
A. But they have also had two pieces of legislation that allowed them to buy more exempt quota.
Q. Well, let me turn, then, to your last, very last page of Exhibit 151, which is Exhibit A, E-8, and it is a one-page document. And first, in looking through your testimony and the relationship to that, it looks like from page 11 of page 150, in the footnote that is listed as producer-distributor outline, dated 1995. So was this a document that your firm produced as part of its talking points or discussion points for discussing legislation?
A. I believe this was produced by the legislature.
Q. Oh, this is the legislature that produced this?
A. I believe this was part of another document, actually.
Q. I mean --
A. That the front page must have --
Q. If you look at the last paragraph, it looks more argumentative to me than something the legislature would produce, because it says, "Why should the PD's have to share their hard working Class 1 sales?" I mean, that sounds to me like something your firm might have used to argue why a provision should or shouldn't be adopted.
JUDGE CLIFTON: Let me interrupt for just a minute. Is it possible that Mr. Gonsalves is right, that this is page 2 of a two-page document? Down at the bottom it shows total page 2.

MR. VU: We will have to double check that.

JUDGE CLIFTON: Very good. If it turns out that there was another page that would help identify the source of it, we'll add it. Okay. Go ahead.

BY MR. ENGLISH:

Q. Looking at this, do you recognize this document, sir?

A. I do recognize the document, and I believe there is a cover page to this. And I don't, I don't have it in the documentation, it may have got lost.

Q. Well, you have produced this document from your records, correct?

A. Correct.

Q. Okay. And when you see the statement at the bottom, this raises a good question, "why should the PD's have to share their hard working Class 1 sales," isn't that the kind of statement you would have made in terms of arguing in favor of your clients?

A. That is a discuss point that has been in the California legislature since the inception of the Gonsalves Milk Pooling Act and has been often written, not just by our firm, but also by legislative analysts and others.

Q. Okay. So you believe this could be a legislative
analyst issue?

A. It could be a follow up on a Senate Ag Committee
document or it could be legislative analyst, but that is an
argument that's been before the California legislature on when
they milk their own cows, they have their on processing plant,
and they go out and get their own sales, why do they have to
share in that?

Q. Okay. So let's go up a little bit. The second
paragraph there's the statement, "in 1978, the PD's only
represented 3.96 percent of the total Class 1 sales in
California." Do you see that?

A. Yes.

Q. Does that resonate with you as having been correct at
the time?

A. Yes.

Q. The next statement is, "to date, they even represent
less than 3.64 percent." Is that correct?

A. That's correct.

Q. Does that resonate with you?

A. Yes.

Q. Okay.

A. And those were figures that were given by the
Department of Food and Ag.

Q. Sure. And then it's followed with what one might call
a rhetorical question, but nonetheless, it says, "How much of
an impact could they have with this small percentage?"

Do you see that?

A. That's correct.

Q. Okay. Do you know what percentage the producer-distributors have of the Class 1 market today?

A. I do not.

Q. Okay. Do you know that there's testimony in this hearing that it is 24 percent?

A. I do not.

MS. HANCOCK: Your Honor, I would object, that misrepresents --

JUDGE CLIFTON: Come to the microphone, please, Ms. Hancock, and start again.

MS. HANCOCK: I object on the grounds I think it misrepresents what the comparison is today.

JUDGE CLIFTON: All right. Thank you. Your objection is noted.

MR. ENGLISH: I would note that Mr. Blaufuss testified that he did a calculation that it was 24 percent of the total Class 1 sales.

MR. GONSALES: And these calculations came from the California Milk Pooling Branch.

BY MR. ENGLISH:

Q. Well, and Mr. Blaufuss' came from the compilation of the CDFA as well, sir. So let me ask you this, having studied
California, do you also know that the overall sales of Class 1
have gone down in California, especially in the last decade?

A. I do not know that.

Q. Okay. I have no further questions for this witness.

JUDGE CLIFTON: Who next would ask questions of
Mr. Gonsalves? Mr. Beshore?

CROSS-EXAMINATION

BY MR. BESHORE:

Q. Marvin Beshore. I have just one question,
Mr. Gonsalves. On page 11 of Exhibit 150, your testimony, in
the conclusion there's a sentence, the first paragraph of the
conclusion, "out-of-state milk was not subject to the pool in
exchange for not receiving the benefits of the quota system."
I don't recall, and help me because maybe I missed it, any
prior observations in your recitation of the legislative
history, discussion of out-of-state milk, or I don't recall
seeing any references to that in Exhibit 151. Are there, can
you point me to some?

A. I don't believe there is any reference to out-of-state
milk there. I believe it was a federal court case.

Q. Okay. I just wondered why --

A. It wasn't part of legislative history.

Q. I just wondered then, why that observation, or what is
the basis for that statement in your conclusion?

A. Well, the basis in my conclusion is that the quota
system in California, although it's been somewhat flawed sometimes, has worked very well. And if we're going to go to a Federal Order, those who have purchased quota, those who have exempt quota, and those because of the federal ruling, ought to be considered.

Q. Okay. I'm just -- I'm just limiting my focus here to the out-of-state. I'm just wondering why the observation to, about out-of-state milk was included in your, the conclusion of your testimony here, when I didn't see it anywhere in the anything that came before it.

A. I did not bring legislation that I believe failed passage that was trying to limit out-of-state milk coming into California.

Q. Okay. Did Ms. Hancock's law firm, Stoel Rives, represents out-of-state producers, are you also here on behalf of out-of-state producers?

A. I'm here on behalf the California producer-handlers.

Q. And that group only?

A. Yes.

Q. Okay. Thank you very much.

A. Thank you.

JUDGE CLIFTON: Who next has questions for Mr. Gonsalves?

MR. RICHMOND: Bill Richmond, USDA. We don't have any questions, Mr. Gonsalves. We just want to express our gratitude for the legislative history. It really helps our
understanding of the program, so thank you for that.

MR. GONSALVES: Thank you very much.

JUDGE CLIFTON: Mr. Gonsalves, is there anything you would like to add now so we will have a full understanding?

MR. GONSALVES: Well, my father cared deeply about the dairy industry, being a former farmer, his father a farmer, his brothers were farmers, they went through tough times in the '40's, '50's, and '60's, and he truly wanted to set up a program so that dairy farmers would have the opportunity to invest money and have security and get a decent payment back so they could stay in business. And so when you take in your consideration of all the testimony, I hope you take into consideration the quota system. Thank you.

JUDGE CLIFTON: Mr. Gonsalves, we're honored that you came, and I thank you. And I'm very glad that we were able to have you testify while you were here this trip so that you did not have to stop again. And Mr. English, I'm very grateful for that, thank you.

MR. GONSALVES: Thank you again, Mr. English.

MR. ENGLISH: Your Honor, at about 5:00 a.m. this morning I said that I had fond hopes of getting one of my witnesses back on at noon, and I expressed concern that it might not happen, and so I thank Ms. Hancock, it is now 11:58, and I call Mr. Blaufuss back to the stand to discuss Exhibits 147 and 148. Which means, remember that little optimistic forecast I had
this morning, I'm feeling some optimism.

JUDGE CLIFTON: Mr. Blaufuss, you remain sworn. I would like you again to state and spell your name.

MR. BLAUFUSS: Rob Blaufuss, B-L-A-U-F-U-S-S.

JUDGE CLIFTON: Thank you. Mr. English, you may proceed.

MR. ENGLISH: Thank you, your Honor. Chip English.

CONTINUED DIRECT EXAMINATION

BY MR. ENGLISH:

Q. So we were sort of rushing last night to fill seven minutes, so I want to backtrack a little bit now.

So looking at Exhibit 147, which is your testimony. On the bottom of page 1, through a combination of production errors and either too many or a few eyes on this, you reference a fluid milk standards, FDA standard minimum level at the very bottom left hand, of 8.7 percent.

Do you see that?

A. I do.

Q. So is the -- as opposed to what, as someone phrased to me yesterday, what God had the cow produce, what is the FDA standard of identity for milk?

A. 8.25.

Q. 8.25 percent, correct?

A. Correct.

Q. Okay. Nonetheless, the statement at the end where you say "the California base fluid milk standards are set at 8.7
percent," that's correct?

   A. That's correct, that's a California standard flow.

   Q. And as it turns out, because milk from the cow
   actually, especially in California, would it average at least
   8.7 percent?
   
   A. Yeah, it would be north of that, yes.

   Q. Okay. So you don't have to standardize or that is to
   say, fortify whole milk in California, correct?
   
   A. Correct. Typically the standards are high enough where
   you don't fortify whole or skimmed milk.

   Q. So the correction that we put on the bottom of
   Page 1, and I guess, your Honor, we would like Exhibit 1 to
   modify, I'm sorry, Exhibit 147, not Exhibit 1, we're not trying
   to modify Exhibit 1, please -- Exhibit 147, page 1, the
   reference at the bottom line to the FDA standard of identity of
   8.7 percent we would ask to be modified to be 8.25 percent.

   JUDGE CLIFTON: Ms. Frisius, are you there? The first, the
   first content on the very last line of page 1. All right. So
   we're striking 8.7 percent and inserting 8.25 percent.

   BY MR. ENGLISH:

   Q. Okay. Now, does that change affect in any way your
   calculations and tables in Exhibit 148?
   
   A. No.

   Q. Okay. On page 2, I believe when you read the
   testimony, and I agreed with it, the bottom paragraph, the very
first line you read, "at the onset of the initial discussion around the possibility of a California Federal Order hearing. We would insert the word "a" between "of" and "California", your Honor, and that's how he read it.

JUDGE CLIFTON: Ms. Frisius, are you there?

MR. ENGLISH: Page 2, the bottom paragraph, the line that says, "at the onset of the initial discussion around the possibility of," that's first line.

JUDGE CLIFTON: All right. Done.

MR. ENGLISH: And then I think he inserted 148 a couple of times, and I think she actually did that as we went long on pages 3 and 4.

MS. FRISIUS: Yes.

MR. ENGLISH: And on 5 there's a, there is also 148. And, your Honor, I'm a little hazy in my recollection, it may be that we actually fixed it on page 5, but the paragraph up from the bottom that says, "the per gallon cost difference" the next line said, "three factor Class 1 pricing system compared to the two factor pricing formula," we struck the word "a" inserted the word "factor", and I can't remember now, whether we did that yesterday or not, Ms. Frisius.

JUDGE CLIFTON: Yeah, but then we made it different. So the way it ended for the record copy, it reads, and we're on page 5, the last full paragraph, second line, the way the record copy now reads, and I'm going to ask Ms. Frisius to
confirm this, but it reads, "compared to a two factor pricing formula." Is that correct, Ms. Frisius?

MS. FRISIUS: Correct.

JUDGE CLIFTON: And that was what Mr. Blaufuss asked for.

MR. ENGLISH: Thank you for correcting my incorrect correction.

JUDGE CLIFTON: Well, I had corrected it wrongly originally, so.

MR. ENGLISH: Well, I apparently wasn't following along to the next part.

And then a couple lines down where there's a blank after table, he read "as Table 2 of Exhibit 148," and she's nodding her head she has that.

JUDGE CLIFTON: Yeah, Ms. Frisius has that. Yes.

MR. ENGLISH: So that's all I had on Exhibit 147, your Honor, do you have anything else that we didn't get through yesterday?

JUDGE CLIFTON: Yes, I think we also did this.

Ms. Frisius, with regard to page 6, the first full paragraph, the fifth line down, I believe we inserted the word "time" before "jettisoning". Yes. So we did that, Mr. English, and that's all.

MR. ENGLISH: Great.

BY MR. ENGLISH:

Q. All right. So now turning to Exhibit 148, before I you
additional questions, did you have, Mr. Blaufuss, with respect to an Excel spreadsheet sort of issue, a correction for, a correction for Tables 3, 5, and 7, for the two factor formula?

A. Yes. So there's a label change we need to make. Basically what happened was my Excel spreadsheet didn't match up with the columns as shown here, so where Columns I, actually this would be Column I.

Q. Okay. So let's start on page 3, let's be as clear as we can be. We're on page 3 of Table 3, and Column I with the yellow Pearson Square, 2 percent below that, right? You have Pearson Square 2 percent in yellow?

A. Correct.

Q. And Column I and Column J are above that, so you are going to speak to Column I, correct?

A. Correct.

Q. So what is the change in the label of Column I?

A. So that equation should be 100*F-G/F-.335. So instead of the G it should say F, and instead of the H it should say G.

Q. Okay.

JUDGE CLIFTON: Do you have room, Ms. Frisius, just to strike the first G and make it an F, and strike the first H and make it a G?

MS. FRISIUS: Yes.

JUDGE CLIFTON: Then do you have room to strike the second G and make it an F?
MS. FRISIUS: Uh-huh.

JUDGE CLIFTON: Yes.

MS. FRISIUS: Yes.

JUDGE CLIFTON: Good.

BY MR. ENGLISH:

Q. Okay. So that same change, Mr. Blaufuss, would need to be made for Table 3, page 3 and page 4, correct?

A. Correct.

JUDGE CLIFTON: Table 3?

MR. ENGLISH: We were just on Table 3, page 3, but that table has two pages, your Honor, so on the next page, page 4, the identical change would need to be made changing the G to F, the H to G, and the G to F.

JUDGE CLIFTON: All right. Good. So we only do it twice.

MR. ENGLISH: Well, so far.

JUDGE CLIFTON: So far.

MR. ENGLISH: That's Table 3.

JUDGE CLIFTON: Okay.

MR. ENGLISH: Then we need to go to Table 5.

JUDGE CLIFTON: Now, let's not go there yet. Ms. Frisius, let me know when you are ready to move. You're ready?

MS. FRISIUS: Yes.

JUDGE CLIFTON: Okay. Good. Mr. English?

MR. ENGLISH: Page 22 is Table 5, and this is the two factor formula, and so this is the identical, is this the
identical change, Mr. Blaufuss?

MR. BLAUFUSS: That's correct.

MR. ENGLISH: So again, the G to F?

JUDGE CLIFTON: Wait, wait, now, I'm on page 22.

MR. ENGLISH: 22, Table 5,

JUDGE CLIFTON: Okay.

MR. ENGLISH: The difference, your Honor, is merely the level of the skim. Correct, Mr. Blaufuss?

MR. BLAUFUSS: That's correct.

MR. ENGLISH: So -- so basically, it's just the very same label change.

JUDGE CLIFTON: Okay. And Ms. Frisius, what's easier for you, just to copy it from what you have already done or to have us read it to you again?

MS. FRISIUS: It's fine, I will just do it from what I have already done.

JUDGE CLIFTON: All right. She says it's fine, she'll just do it from what she's already done.

MR. ENGLISH: And so for Ms. Frisius' purposes, it is pages 22 and 23 for Table 5, and one more time when we get to Table 7.

JUDGE CLIFTON: All right. So, Ms. Frisius, please alert us when you are ready.

MS. FRISIUS: Okay.

JUDGE CLIFTON: She's fast. Mr. English?
MR. ENGLISH: Faster than I can get to Table 7.

Table 7 is pages 41 and 42, and again, this is for the two factor formula only, Mr. Blaufuss; is that correct?

MR. BLAUFUSS: That is correct.

BY MR. ENGLISH:

Q. And it's just for the label under Column I; is that correct?

A. That is correct.

Q. And the G goes to F, and the H goes to G, and the G goes to F, correct?

A. Correct.

Q. You got 'em?

MS. FRISIUS: Yeah.

MR. ENGLISH: Great.

JUDGE CLIFTON: And we only do that twice, pages 41 and 42; is that correct?

MR. ENGLISH: Yes, your Honor.

JUDGE CLIFTON: All right.

BY MR. ENGLISH:

Q. Now, the most important question about those labels, does that change the results?

A. No. When I noticed it, I caught it on the three factor but didn't on the two. Obviously when I saw the label issue I had a little bit of anxiety if it was the formula, but it turns out it was just the column labels, the formulas are accurate.
Q. Okay. All right. So now let's sort of revisit, as you said yesterday, you put the cliff notes at the beginning, correct?

A. That's correct.

Q. So let's talk about Table 1. So what, walk us through Table 1 and we'll walk through one or two of the numbers for the lines. What exactly is Table 1 showing us?

A. So this Table 1 is the data table that was provided to me by USDA, and these are just the factors used to basically come to a skim equivalent value for both the fortification value and the increased volume due to fortification, which would be priced at Class I.

Q. And you say from USDA, did you work with a particular Market Administrator's office?

A. Yeah, it would be the Pacific Northwest.

Q. Okay. And so what does, what does the first line, just walk us through it. I understand that you got it from Pacific Northwest, the record won't know what that means. Why don't you just walk you us through the headings and the very first line.

A. So the first column is the percent total solids in the mixture, and that's just to represent the condensed skim percentage, which is basically what's going to dictate what factors you are going to use. So in this case I chose 33 and a half, which generally reflective of condensed skim, and that's
going to, that dictated what I used for, if you go to the last two columns, the volume factor and the Class IV fortification factor.

Q. So -- so you used, for your calculation purposes, going down about 30 percent of the way, you used the line over 33.5 but not over 34.5?

A. I used over 32 and a half but not over 33.5.

Q. All right. And again, USDA generated, Order 124 generated this for you?

A. I think it's a standard document that they have. I don't think the individual Order generated it, I think it is just a standing document that the Federal Order system abides by.

JUDGE CLIFTON: Do you, Mr. Blaufuss, for the purpose of this testimony, consider condensed and concentrated as the same thing?

MR. BLAUFUSS: That is my understanding.

JUDGE CLIFTON: Okay. All right. Mr. English?

BY MR. ENGLISH:

Q. Okay. Thank you. So the chart gives you more information than you needed; is that right?

A. Correct.

Q. What you needed was the volume factor and the Class IV fortification factor; is that correct?

A. That's correct.
Q. Okay. So you needed the volume factor of .0904, and you needed the Class IV fortification factor of 2.709?

A. That's correct.

Q. Okay. And where did you take those numbers next?

A. Well, they are going to show up, those individual numbers, so the .904 and the 2.709 will show up in the individual data tables as the factors to be used in order to figure out how many pounds of skim equivalent I need to fortify the fluid milk.

Q. So for instance, if we go to page 5, which is the third page of Table 3, you have an analysis called Costing at Actual California Skim Test 2 Price Formula, correct?

A. Correct.

Q. And you just used the numbers that appear in Columns R and S of that page, correct?

A. That's correct.

Q. Okay. And so throughout this document, for the back up for the various tables, that will be the Columns R and S -- or wherever the -- if it's different, that will be the columns for that column -- the numbers.

A. Yeah, I don't know the column labels, but anytime I have a volume factor or fortification factor, those will be consistent regardless if I'm talking two factor or three factor or any level of skim.

Q. Okay. So you tell me if this is the chart you want to
use or a different one as the example. Which one do you want
to use as, well, for walking it through?

A. Well, let's just do the actual since it is there.

Q. Okay. So we'll do actual for January 2010, does that
work for you?

A. That's fair.

Q. Okay. So we have got the 0.904 and the 2.709 in
Columns R and S, and those come from Table 1, 32 and a half,
over 32 and a half but less than --

THE COURT REPORTER: Mr. English, can you do numbers a
little slower, please?

MR. ENGLISH: No.

THE COURT REPORTER: Thank you. Appreciate that.

MR. ENGLISH: All right.

JUDGE CLIFTON: And just so people know where this is,
right now we're looking at Exhibit 148, page 5.

MR. ENGLISH: And page 1.

BY MR. ENGLISH:

Q. So just to be clear, we are using in what's Columns R
and S on page 5, the identical information coming from page 1
for volume factor and Class IV fortification factor for over
32.5 but not over 33.5. Correct, Mr. Blaufuss?

A. That's correct.

Q. Okay. So where does Column T come from, or should we
go look somewhere else first?
A. Well, it kind of depends on how much in the weeds you want to get in the numbers.

Q. I think we should do one line for the numbers so the record has January, let's do January 2010, and run the numbers so that anybody can either double check us or understand where they came from.

A. Okay.

Q. So rather than my trying to go through it, why don't you tell me how January 2010 works?

A. All right. Well, I'll just start from the beginning, then, on Table 3, on page 3. So obviously column A is just the month. Column B and C, since I'm using the actual in this case, are reflective of CDFA data for the actual market milk for both skim and fat for producer milk. So for January of 2010, the skim percent was 8.86 percent and the fat percent was 3.76 percent.

Q. Okay.

A. And so the next step was to calculate the percent SNF, which is the solids nonfat in a hundredweight of farm milk, and all I did there was 1 minus C, so it is essentially the percent of skim with the fat taken out, so that came to .9624.

Column E is just the percent SNF. So in this case, Column E on January 2010 is 0886, which is just 8.86 percent.

Q. Okay.

A. Column F was trying to figure out what the skim SNF
test of the market milk is. And what we're doing there is just
dividing column E by column D. And with respect to Columns G
and H, it's essentially trying to figure out what percent skim
do you need to hit once you put fat back in that you are going
to get to representing a 10 percent and 11 percent per the
California solids to meet the fortification standards of the
State of California.

Q. So what you mean is that once you have reduced the
butterfat in order to get it down to 2 percent, by definition
you now have less milk, correct?
A. Correct.

Q. And in addition, you need to fortify to a higher
standard than the cow would have given you anyway, correct?
A. Correct.

Q. So that is why you have that different percentage,
correct?
A. That's correct.

Q. Okay. And G is for 2 percent and H is for 1 percent,
correct?
A. That's correct.

Q. Okay. So what did you do next?
A. So the next step was to use a Pearson Square to figure
out, okay, I need this amount of skim, how am I going to divvy
that up between a condensed and just the regular market milk.
And so what the Pearson Square did here was basically tell me
in Columns I and J, how many pounds of condensed I need and how many pounds of milk did I use to get to the level. And I did it the same, so Columns I and J is using Pearson Square for 2 percent, and K and L is the Pearson Square for 1 percent, assuming, of course, the condensed skim is 33 and a half percent solids nonfat.

JUDGE CLIFTON: Now, this Pearson Square, P-E-A-R-S-O-N, Square, is that a formula that's widely used for this kind of calculation?

MR. BLAUFUSS: Well, I use it for this, I use it for other things, too. You are talking about if you got farm milk coming in, how many pounds cream generation you can use it for, and there's different things that it's used for in the dairy industry.

JUDGE CLIFTON: Okay.

MR. ENGLISH: Are you the only one who uses it?

MR. BLAUFUSS: No. I know I use it, I know the MA staff who we kind of walked through this with, that's what he also suggested using, so I believe it's widely used in the industry.

BY MR. ENGLISH:

Q. All right. So just to be clear, the abbreviation in a number of these columns, such as Column I and Column K and column M, COND, would that be condensed?

A. That's correct.

Q. Okay. So what did you do next?
A. So once I moved past the Pearson Square percentage, really what I'm doing in Columns M and N and O and P, is then standardizing that product to a 2 percent or 1 percent. So in the case of Column M, I'm talking Column I times 1 minus .02, so it's, in this case since I'm looking at 2 percent, .02 represents the fat level. So that's saying I have 98 percent skim in that product. So it is multiplying Columns I and Columns J by .98 to make sure that I'm not, I'm using 98 pounds of skim and I'm using 2 pounds of fat. Whereas in Columns I, J, K, and L is assuming a hundred pounds, so I need to standardize that down to reflect that there's fat in that product ultimately when it goes to the consumer.

Q. And you do that similarly for the 1 percent, but using .01 rather than .02, correct?

A. Correct. So the Columns M and N for 2 percent will add up to 98 pounds, and then for O and P on a 1 percent, the skim will add up to 99.

Q. All right. So we have gotten through Column P, and I had already jumped ahead, so now on page 5, Column Q is the month again, and we have already discussed Columns R and S, correct?

A. That's correct.

Q. So that brings us to Column T.

A. Yes. So columns T, U, V, and W, is just calculating the skim equivalent based on the factors that we just walked
through in Columns R and S, and the amount of condensed in milk
that I'll be using to fortify the product. So for Columns T,
or for Column T, you multiply the volume factor found in Column
R, times the condensed pounds in the product found in Column M.

Q. Which were the standardized pounds, correct?
A. Correct.
Q. Okay.
A. And then for the fortification factor I'll be taking
Column S times Column M.
Q. And that's for the two percent, so you would do
essentially the same calculation using the applicable columns
for 0 for 1 percent, correct?
A. That's correct.
Q. Okay. Otherwise the calculation's identical to what
you just discussed, correct?
A. Correct.
Q. All right. So what are columns, what is Column X?
A. Column X is the Class I skim milk price which includes
a $2.10 hundredweight differential. So all the analysis that I
did, whether I am talking a two factor or three factor, assumes
a 2.10 base differential, so that's already been included in
the numbers.
Q. And Column Y?
A. Is the Class IV skim cost, which will be used to
calculate the fortification value. So basically, you know, if
you want to maybe skip a step ahead to kind of give a broad overview.

Q. Sure.

A. Anytime that we're talking the volume factor, you are going to multiply that by the Class I value, and the fortification is going to be multiplied by the Class IV value. Kind of as I walked through in my testimony, you know, the bulk of the cost is going to be cost to the Class IV because most of it is allocated to fortification, but since you are fortifying a product you end up with a higher amount of Class I volume and that gets allocated on the volume basis.

Q. Okay. The displacement? Is that the displacement?

A. That's correct.

Q. Okay. All right. So now, that was page 6. We would next turn to page 8; is that correct?

A. That's correct.

Q. Okay. And Column Z is the month again, correct?

A. Correct.

Q. All right. So now, we've finished the Alphabet so we go to double A, correct?

A. We do. So the value of fortification is what we're trying to figure out in Columns AA, AB, AC, and AD. So just walking through the 2 percent value of fortification calculation, taking the Column X, which is the per hundredweight Class I skim milk price, times Column T, which is

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the pounds of volume skim equivalent divided by a hundred. So since I'm using a hundredweight price, I need to get the pounds into a hundredweight level as well so that I'm not overinflating the value. The fortification value, so the next column over in AB, I'm taking Column Y, which is the Class IV skim cost, times Column U, which is the fortification skim equivalent pounds divided by a hundred.

Q. And so that's the 2 percent for AC and AD, Columns AC and Columns AD, you are doing basically the same calculation but for 1 percent; is that correct?

A. That's correct.

Q. Okay.

A. And both the Class I skim milk price and Class IV skim costs are exactly the same, so there's no change in the price.

Q. So since AE is another column of months, what happens in AF?

A. So AF is, I'm actually looking at this and trying to figure out what the value of milk is. So the previous calculation was saying here's the value of fortification, well, that's not the only cost, obviously we're paying for the milk as well. And so in this case I'm valuing the milk at actual solids contents as we walk through in the first two columns, and going through and basically multiplying Columns X, which is the Class I skim milk price, times Column N, which, if I can remember, basically I'm just going through and looking at the
value and calculating this is how many pounds of skim I'll have, this is how many pounds of fat, and then adding that up and saying this is the value of milk, which is what Columns AF, AG, and AH are doing.

Q. Okay. And that's for 2 percent, correct?
A. That's correct.

Q. And for 1 percent it is the identical kind of calculation in Columns AI, AJ, and AK, correct?
A. Correct.

Q. All right.
A. And again, this assumes a 2.10 differential zone.

Q. All right. So, first of all, that basically is how Table 3 works, correct?
A. Correct.

Q. And then that's for -- that's for actual California Skim Test 2 factor. When we go through the rest of the tables, so Table 4, is the actual California skim test at the III Class. So that's going to be a little different, so we need to go through that example as well?
A. I don't think we need to go through the first part because it's identical, the only, obviously, the part that's going to change is we're not pricing it on a skim and butterfat, you are pricing it on butterfat solids nonfat in a fluid carrier.

Q. So what you are saying is Table 4, pages 11, 12, 13, 13
the first half, are identical, but when we get to the second
half of 13, once we start moving into columns, especially
Columns X, Y, and Z, it is going to change, correct?
   A. Correct.
   Q. But up until that point in time, up through Column W,
you are doing it the same way as you have done it, correct?
   A. Correct.
   Q. All right. Okay. So why don't we not repeat steps A
through W, and turn to Columns X on page 13.
   A. Okay. So the Class I skim milk price is being
calculated as it was before. Obviously, where we're different
here is we're splitting that skim value into the solids nonfat
fluid carrier. So as I walk through in page 1, we did make
some revisions to our pricing formula. When we had initially
put in the hearing proposal, we had an SNF factor of 9 and a
fluid carrier factor of 91, which would, of course, ignore the
fact that you are at standard going to have a 3 and a half
percent fat level. So California has pretty good milk, but I
don't think they can run 102.5 percent solids level in pricing.

   So we adjusted the fluid carrier down to reflect the
fact that, yes, there's butterfat in milk. So instead of 91,
we adjusted that down to 87.5, which is the value used in
Column Z. And then Column Y, we made that SNF value stay at 9
percent. Typically, in the Federal Order structure we're
valuing SNF at 9 percent. California runs theirs a little bit
different in their Class I price formula, they assume an 8.7
percent solids nonfat. So it is a little bit different, but we
figure we're talking a Federal Order proposal, let's try to
incorporate as much we can into our proposal.

Q. All right. And then what is Column Z?
A. So Column Z is the fluid carrier cost. So we're taking
the Class I skim milk times .24 and dividing that by 87.5.

Q. And Column AA?
A. Is the skim milk cost for Class IV. And then for AB
we're calculating the Class IV SNF, which is just AA divided by
9, which AA is the Class IV skim cost.

Q. And again, you are using the 9 from Federal Orders,
correct?
A. Correct.

Q. Okay. So we go to page 15. I'm sorry, that's not 15,
page 16. Why don't you, I think this completes the three
factors, this page?
A. This is the value fortification.

Q. Right?
A. Correct.

Q. Okay.
A. It is in the value of fortification, I just kind of
walked through with MA staff. This is going to assume that
there's a 9 percent SNF level in the milk being used to produce
the condensed, so I was describing that's why I have the .09 in
Columns AD, AE, and AF, and also, AG, AH, and AI.

Q. So again, 1 percent would be done the same way as 2 percent, so let's do the 2 percent in AD, AE, and AF?
A. Okay.

Q. Or is that what you meant, you just did already?
A. No, I'm just making sure I have the right columns here. Put this together a while ago. All right.

So Column AD we're taking Column T, which is the volume of the skim equivalent of the fortifying agent, times Column Y, which is the Class I SNF price per pound times .09. Column AE we're taking Column T, which again is the volume fortification factor, times Column Z, which is the fluid carrier cost per pound, and multiplying that by a 1-.09, and I guess another point I should mention here, since I am taking 1-.09, that obviously equals 91. It is important to point out that this is the base number that is being multiplied again, has already been standardized down to reflect the fat's been taken out, so it is truly 91 percent, 9 percent of the true skim, so I'm not overvaluing that value of fortification.

And then Column AF is the fortification value, so Column U, which is the skim equivalent of the fortifying agent for the fortification, times AB, which is the Class IV SNF price per pound times .09.

Q. And then again, the same analysis for 1 percent, correct?
A. Correct.

Q. All right. We're almost there. We need to turn, I think, to page 19; is that correct?
A. Correct.

Q. So what is this? How does this table work?
A. So, again, I'm calculating here the value of milk using the actual skim SNF test of the incoming milk, so it is going to be reflective of the monthly skim level in the milk being produced on the farm, so I'm pricing that using the Class I SNF price that we walked through. The amount of fluid carrier in the milk, times the fluid carrier price, and so on so forth, the butterfat, and ultimately arriving at a per hundredweight price using the actual skim test and the formulas laid out that we walked through.

Q. And again, the same for 1 percent, correct?
A. Correct.

Q. So now that is the analysis for actual California skim test three factor formula, correct?
A. Correct.

Q. You then do the identical analysis for both three factor and two factor for the high and the low skim test, correct?
A. Correct.

Q. And that's what follows in the, in those tables that follow, Table 3, so let's just look very quickly, I'm sorry,
the Table 5 is the high, what appear to be the high skim test
for two factor formula, correct?

A. That's correct. So in this case I am assuming a high
skim to be 9.2 percent.

JUDGE CLIFTON: Okay. So we have gone to page 22 of the
exhibit.

MR. ENGLISH: Right. And that is basically the identical
two factor test, the two factor, like Table 3, but for 9.2
percent, your Honor. Okay? And otherwise, Table 5 is
calculating the same way as Table 3, Mr. Blaufuss?

MR. BLAUFUSS: Correct.

BY MR. ENGLISH:

Q. Okay. So then we get to Table 6 which starts on page
30, and now we have turned to the three factor formula for the
high California skim test, correct?

A. Correct.

Q. And that, except for the fact it is California, it's
9.2 percent California skim test, otherwise the calculation is
done identically as on Table 4, correct?

A. Correct.

Q. And then that takes us to Table 7 which starts on
Page 41, and now we're looking at the 8.8 percent or low
California skim test, correct?

A. Correct.

Q. And for the two factor formula, correct?
A. Correct.

Q. And so other than the fact that it's the low skim test, Table 7 is identical to Tables 3 and Table 5, correct?

A. Correct.

Q. And Table 8, starting on page 49, is the three factor formula for the 8.8 percent or low California skim test, correct?

A. Correct.

Q. And other than it being the low California skim test, Table 8 is identical to Tables 4 and Table 6, correct?

A. Correct.

Q. All right. So that would take us through Table 8, which ends on page 59. So do we go to Table 9 next or do we go back to Table 2, Mr. Blaufuss?

A. You know, it would almost probably be easier to go through Table 9, then we can kind of walk through line by line once we do that, to get to where I got a landed cost.

Q. All right. Let's do Table 9, which is on page 60 of this document.

A. All right. So Tables 9, 10, and 11 are the same obviously basic calculations, I'm just adjusting the skim level to be reflective of high, low, and actual. And I guess maybe answering the question before it gets asked, over this period that I looked at, the average of the five years the SNF level was 8.88 percent, so there wasn't much of a difference between
my low factor and my medium factor, and I guess my rationale for that is, I didn't want to put an SNF test at, call it 8.5 and say that was low, and have to come back and fortify my whole and my skim milk. So I tried to go as low as low as I could go without having to create other complications in my math.

Q. Okay. So walk us through Table 9 and then tell us what's different for Tables 10 and 11.

A. So for Table 9 this is the actual skim SNF test. So if you look at the percent skim in producer milk, which would be the third label from the bottom left of the table, that 8.88 reflects the actual test. The 96.3 represents the percent skim, so it's a hundred percent minus the fat, so 96.3 percent.

Q. So your actual butterfat was 3.7?

A. I believe for the month I looked at in this case, yes. And then the SNF test in the market milk, which was just the 8.88 divided by the 96.3.

Q. Okay.

A. And in order to figure out how many pounds of SNF I have and how much I need to add to get to a 10 percent or 11 percent milk, I standardized that SNF test of market milk to be reflective of a 2 percent or 1 percent. So the 2 percent milk skim label is just taking .98 times that 9.22, and again, for the 1 percent, taking 9.22 times .99.

Q. So that's what gives you the 9.04 percent for
2 percent, and the 9.13 percent for 1 percent?

A. Correct.

Q. Okay.

A. So I guess just starting at the top and working my way down with the chart. So the first line is the gallons in the California hundredweight of milk. And this data was, I believe, provided by Dr. Schiek a few years ago. I think he received it, information from CDFA staff at that time to kind of give a general reflection how much a gallon of milk weighs in the California system, which varies, compared to what the Federal Orders have its standard weights. So in the case of 2 percent it was assumed that a gallon weighs 8.67 pounds, and for 1 percent, a gallon weighs 8.71 pounds. So obviously just doing the math, tells you you are going to get 11.53 gallons for 2 percent, and for 1 percent you will get 11.48 for each hundredweight of milk.

Q. Okay.

A. The pounds of solids per gallon of standard milk, this assumes standard is whole milk, so 8.7 percent solids. So .7499 is the pounds of solids per gallon in standard milk, and then try to, my goal here was to figure out the pounds of solids per gallon need to fortify. That's just the pounds of solids I needed to add to the mix to get up to the 11 percent and 10 percent solids content. And that's also the factor used to calculate the base condensed allowance. So the allowances
on per pounds the solids used, so that's how I'm getting at the 
.0082 and the 0161.

Okay. And then basically for the total fortification 
allowance credit per hundredweight, it is just the gallons in a 
hundredweight times that base allowance.

Q. So how is Table 10 different from Table 9?
A. The only thing that's been adjusted in Table 10 from 
Table 9, is again, that third line column label up, percent 
skim and producer milk has been changed to reflect the high 
skim that 9.2 percent skim, which then flows through the model 
to figure out the pounds of skim I need to fortify.

Q. And Table 11 does the same thing but the low test, 
right?
A. Correct.

Q. Okay. And so the purpose of that was to be able to 
create your analysis to show what impact some of this would 
have on the desirability of purchasing different levels if you 
didn't have a fortification allowance?
A. Correct. So you're going to have two components of 
this, there is going to be a milk price and a fortification 
cost. So you are going to have varying levels of both 
depending on what the solids content is. So if you have a 
higher solids content you are going to have a higher cost in 
your milk and you should have a lower cost in your 
fortification, and vice versa if you have lost test.
Q. So if you didn't make a fortification allowance adjustment in a California Federal Order, but because of California's statutory program requiring fortification, you would, without such allowance, create first a non-uniform price for milk, correct?

A. Yeah, and I think I said that in my testimony. We view it as creating unequal raw product costing for handlers.

Q. Which could create incentives to alter your milk supply in order to fix that problem, correct?

A. Correct. I mean, if I'm looking at it, just looking at the differences in the two factor I think it was roughly, we'll call it 4 cents to make easy math, and so that's basically telling me I've got roughly 40 cents a hundredweight in savings from high test skim compared to low test in a raw product milk cost.

Q. I'm going to go back to Table 2 I think in a moment, but did I read it correct that if you do a three factor versus two factor, that the cost of milk to Class I handlers actually goes up?

A. That's what my numbers would indicate, yes.

Q. Okay. All right. So having described Table 9 and having talked yesterday about the cliff notes, how do we get to, how do we get to the cliff notes in Table 2?

A. All right. So I guess I'll start line by line. The same basic premise is going to hold whether or not we're
talking a two factor or three factor. I'll start just first
with the two factor and with the 9.2 percent SNF milk. So the
milk cost for all of these different two factor, three factor,
all the various skims are going to be pulled off the data table
that I provided subsequently. So that's where the milk cost
lines are coming from. The fortification costs and the
displacement costs per hundredweight are coming from the same
data sources, so the various columns that we walked through.
Which, obviously, you have your milk cost, your fortification
cost, and your displacement are going to equal up to being your
raw milk cost. So using the example of a reduced fat, two
factor, with fortification, the raw milk cost would be $17.36
per hundredweight, your fortification cost would be .84 cents
per hundredweight, and the displacement value would be .34
cents per hundredweight.

JUDGE CLIFTON: I'm sorry, you've got to show me exactly
where you are, I'm lost.

MR. BLAUFUSS: So the third column from the left in the
upper left table.

JUDGE CLIFTON: All right.

MR. ENGLISH: Called reduced, correct?

MR. BLAUFUSS: Reduced, correct.

JUDGE CLIFTON: Okay. So tell me again what you just told
me.

MR. BLAUFUSS: So the milk cost, assuming 9.2 percent
solids in the milk, would be $17.36 per hundredweight. The
cost to fortify that product to meet California standards would
be 84 cents per hundredweight. And the extra volume increase
that we created as a result of fortification, which would be
price to Class I, that's called displacement and that would be
34 cents per hundredweight. You add the $17.36 per
hundredweight with the 84 cents per hundredweight, and the 34
cents per hundredweight, and that lands you at your raw milk
cost of $18.54 per hundredweight.

With regards to shrink, I assumed a 1 percent shrink.
And shrink will be priced at the lowest class price, so in this
case, lowest price between Class III or Class IV. And my
pricing formulas are reflective of that, so it's always going
to pull the lowest class price. And I guess the other portion
I should mention is, because I'm sure someone will notice that
the shrink isn't consistent across, I also assume that the
fortification, so the condensed coming in, is also going to be
factored into the shrink calculation.

BY MR. ENGLISH:

Q. So the more fortification, the larger the shrink.

A. Correct.

Q. All right.

A. So the total milk cost is going to be the raw milk cost
plus the shrink factor, so using the reduced, the total milk
cost is $18.71 per hundredweight.
JUDGE CLIFTON: The door closed just as you said that, say again what the total milk cost is?

MR. BLAUFUSS: The total milk cost would be your raw milk cost, so in the case of reduced, it would be $18.54 per hundredweight, and then you would also add in your shrink cost, so in this case 18 cents per hundredweight, which lands you at the $18.71 per hundredweight. Obviously, if you are looking at the face of that, that should be $18.72. I would imagine having a rounding difference there.

BY MR. ENGLISH:

Q. What about the fortification allowance? Is that actually do you need to take, would that be what takes you down to $18.71?

A. No. Because I am coming in, I brought that in since that's a per gallon cost, I brought that in at the end. So you are, I'm essentially taking the total milk cost, figuring out the weight of a gallon, and getting the per gallon cost, and then factoring in that per gallon fortification.

Q. So the fortification gets calculated, even though it's above it, it gets calculated after the total milk cost?

A. Correct. I brought that in at the end and that's just how I ended up doing it. You will have the same number, just get there a different way.

Q. And as you said, the analysis for the other five, the three factor, and the two and three factor for the different
levels of skim, are all done the same way, correct?

A. Correct.

Q. Okay.

A. Except, of course, in the three factor you are going to be factoring in the fluid carrier SNF not just skim.

Q. Should we walk through that quickly just to make sure it's not lost or do you think it's covered?

A. I think we covered it when we covered the two and three tables.

JUDGE CLIFTON: So, Mr. Blaufuss, as I look at Table 2, I understand your intention was to help us with the fortification issue, but this seems like a wonderful spreadsheet to show the cost of milk.

MR. BLAUFUSS: Yes, I guess I'll make a caveat here, and I don't think we mentioned this. After we went to publication, obviously there was a lot of moving targets with make allowances changes and the FOB adjuster changes, the one thing that I will note is my make allowance for the SNF for Class II and Class IV. I used the original make allowance and I didn't update that portion to be reflective of the recent up changes in the last week or two that have been made.

The analysis still holds true in talking about relationships, because whether or not I'm talking two factor or three factor, it's the same make allowance throughout. I don't have an issue of saying, here's the relationship, but I'm not
going to sit here and say that didn't play a role in saying here's the actual milk cost. So I'm not portraying this to be here's the per gallon cost, I'm portraying to say here's the relationship among the different factors.

BY MR. ENGLISH:

Q. Based upon the make allowance that was being used ten days ago?

A. Correct. So my make allowance is .1678, I believe the one that Dr. Schiek updated was .1997. So all the FOB adjusters are the same and yet are reflective of where we are at now. Merely the only thing that I didn't get updated was the make allowance for SNF for Class IV and Class II.

MR. ENGLISH: Now you are lost?

JUDGE CLIFTON: You know when I came in here, I didn't know that a gallon of milk under the California Order would weigh something different from the gallon of milk under the Federal Milk Marketing Orders. This is hard.

MR. ENGLISH: Well, I was thinking we would have three or for minutes of cross-examination and he would be done before lunch, right?

MR. BLAUFUSS: Well, maybe to make it a little more clear when I am talking about make allowance issue, so when you are calculating a solids not fat price, it is the nonfat dry milk price, minus the make allowance, minus, in our case, the FOB adjuster, times .99, so the only thing in the formula that
would be different is just that make allowance factor. So commodity prices are the same, the FOB adjusters are the same, it is just I used too low of a make allowance.

MR. ENGLISH: I'm going to let Mr. Beshore ask a quick question, I think it is purely for clarification.

MR. BESHORE: I may show my complete ignorance here. Are you using like Proposal 2 prices throughout this?

MR. BLAUFUSS: Yes, except I'm using the, I believe hearing proposal, USDA, basically said there's no western price formulas, so I'm using the pure default price, which was the NDPSR values.

MR. BESHORE: For the whole time period from January 10 --

MR. BLAUFUSS: Correct.

MR. BESHORE: -- forward, you went back and re-calculated what they would all be assuming proposal -- okay. Wow. Okay.

MR. BLAUFUSS: Correct.

MR. ENGLISH: Why do you think these price impacts have taken awhile to get to the stand. I agree, "wow".

I have a proposal to make. I think I'm done with direct exam. What I would like to do is move admission of Exhibit 147 and 148 and then take lunch. I think I will not have additional direct after that, but I'm hoping that maybe taking lunch would allow people to, if not digest food, digest this data, unless it gives them something else, and might shorten or might not, cross-exam.
But I agree, your Honor, this is, I agree with both you
with your comment that this is really intense stuff, and I
agree with Mr. Beshore's technical legal term, "wow". So I
think I'm done with direct and I think I'm very impressed, and
so I would move admission of Exhibit 147 and 148.

MR. BESHORE: Can Mr. Hollon get a question in before we --

JUDGE CLIFTON: Yes, I think that would help us as we
evaluate over lunch. And Mr. Hollon, if you would identify
yourself when you start.

MR. HOLLON: Elvin Hollon, Dairy Farmers of America.

Rob, the equation that you changed, it was -- go to page 3.

MR. BLAUFUSS: Uh-huh.

MR. HOLLON: And the Column I, the 4.11 is the equation
above supposed to yield 4.11? So if I take 100 times F minus
G, and divide by G minus 3.35 --

JUDGE CLIFTON: Divide it by F.

MR. HOLLON: Okay. Divide it by F?

MR. BLAUFUSS: That's what my formula said.

MR. HOLLON: Well, just asking you, F minus G has got to be
a negative number, 9.2 minus 10, so how do I get a positive
number?

MR. BLAUFUSS: Because you are also taking your F, which is
9.02 minus a negative, so that should also be a negative, so
you have two negative numbers.

MR. HOLLON: Okay. So -- so when it says F minus .335,
it's supposed to say F plus .335 if I'm minus the minus?

MR. BLAUFUSS: I'll double check my formula, but I believe that's F minus C, F minus .335.

MR. HOLLON: Man, I hate these complicated spreadsheets.

MR. BLAUFUSS: You and me both.

MR. HOLLON: We both have good reason to do that. Does --

MR. ENGLISH: Wait a minute, isn't F -- F is a percentage, but .335 is not a percentage. So if you express F as a non-percentage, Mr. Blaufuss, it would be .0920, correct?

MR. BLAUFUSS: Correct.

MR. ENGLISH: And so you would be subtracting .335 from .092662, so that would give you a negative denominator, a negative numerator, which gives you a positive, correct? Divide them?

MR. BLAUFUSS: I believe that's what my formula has.

MR. HOLLON: Assuming the numbers are right. One other question?

MR. ENGLISH: Sure.

MR. HOLLON: Back on Table 2, the 1.6171 or any of those numbers, can you show me where 1.6171 shows up in one of the other tables or does it?

MR. BLAUFUSS: It doesn't. So that's basically doing the simple math, but it is the cost build up, and then just taking the here is a weights, which I provided for reduced fat and low fat in the vat, and just figure out how many gallons I'm
getting per that hundredweight.

MR. HOLLON: Okay. Thank you.

JUDGE CLIFTON: Does anyone -- anyone else want to clarify
before you go to lunch? Think about this? Ms. May?

MS. MAY: Laurel May with USDA. Just a couple of questions
about the notations on your testimony, page 1. At the end of
the first paragraph you say that you are going to make
adjustments to the Class I price calculations as found in
Section 1051.50(a)(d), which is, there is kind of no such
thing, so are those paragraphs (a) and (d) maybe?

MR. BLAUFUSS: Yes.

MS. MAY: Those are on page 47228 of the Federal Register.

MR. BLAUFUSS: Yes, that should be (a) and (d), not (a)(d).

MS. MAY: Okay. And then my other question --

JUDGE CLIFTON: Let's make that change now. Thank you very
much. So Ms. Frisius, with regard -- we should have done that
from the, we should have noticed that from the beginning, but I
mean, I sort of noticed it, but all right. So we're on page 1,
the third line down, we're going to insert the word "and" in
between the (a) and (d). Thank you.

MR. ENGLISH: In fact, your Honor, a correction to
Exhibit 1, page 47228, column 2. Thank you for catching that,
Ms. May.

MS. MAY: You're welcome. I have one more. In the
sentence under fortification credit revision on the same page,
"proponents are also going to revise the fortification credit
calculation found in Section 1051.60(6), I'm wondering if that
isn't supposed to be paragraph (a) and paragraph (a)5 and (a)6,
which would be on the Federal Register page 47231, starting in
the middle column. 60(6) is not a correct notation.

MR. ENGLISH: Maybe we'll consider that one at lunch,
because obviously you are right, there's no 60(6), so rather
than rushing that and giving you an answer which we then
re-correct why don't we -- unless you have another question.

MS. MAY: No, those were my two just about the exhibits
themselves.

MR. ENGLISH: All right.

JUDGE CLIFTON: Okay. Good. So we haven't admit these
yet.

MR. ENGLISH: Well, let's hold off then, in case there's
other little things like that.

MR. RICHMOND: Bill Richmond, USDA. The only other
question we had was, and you can think about this, too, for
Exhibit 148, if you wanted to provide the actual spreadsheets
for us, we can potentially post them online when we do post the
PDF's, so it may help. It would absolutely help us in
understanding the spreadsheets, it may help others. Completely
up to you.

MR. BLAUFUSS: Okay.

MR. ENGLISH: By that, do you mean the underlying
spreadsheets in raw form? In other words, in native form?

MR. RICHMOND: Yes.

MR. ENGLISH: Okay. We will certainly think about that. I think I know what the answer is going to be.

JUDGE CLIFTON: The "show your work" provision?

MR. RICHMOND: Yes, absolutely.

JUDGE CLIFTON: Are there other questions before we break for lunch? I'd just like to say, I'm pretty impressed, Mr. English, with the way you grasped that negative divided by the negative issue. Well done. All right. Let's see what time it is. I'm going to call it 1:10, it almost is, so please be back and ready to go at 2:25.

MR. ENGLISH: Thank you, your Honor.

(Whereupon, the lunch recess was taken.)

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TUESDAY, NOVEMBER 10, 2015 - - AFTERNOON SESSION

JUDGE CLIFTON: We're back on record at 2:26. Mr. English.

MR. ENGLISH: Thank you, your Honor. Before I go back and
ask about admission of 147 and 148, and also turn Mr. Blaufuss
over to further examination, it's been suggested by more than
one person that today's scintillating discussion of the forest
may have lost track of the trees. And since we are where some
of the greatest trees are in the world, I thought maybe I would
return briefly, and maybe went too fast yesterday and decide to
retrace to yesterday. So, in a nutshell, Mr. Blaufuss, so
what?

JUDGE CLIFTON: That's good. That's good. That was so
what, question mark, right?

MR. ENGLISH: And may I help you out?

MR. BLAUFUSS: I can get it. So really when the initial
discussion of a potential California Federal Order hearing
started, from an internal perspective we tried to see what
California standard milk does if you are using a standard
Federal Order formula compared to what's going on in
California. And so what we tried to do here was look at the
relationships and how the Federal Order pricing versus
California pricing works given that you have to fortify, and
what those relationships are for different handlers who have
different solids content in the milk coming into the plant.
And so it's trying to look at a relationship to say is it a
half a cent a gallon, a penny a gallon difference under two
factor, and that's really what I was trying to accomplish here.
So I wasn't try to say, you know, here's the blended per gallon
cost of the Proposal Number 2. I'm trying look at the
relationship of a two factor versus three factor using the
prices as laid out in Proposal 2.

JUDGE CLIFTON: Okay. Remind me what the two factors are
in a two factor analyses.

MR. BLAUFUSS: So a two factor is just butterfat and skim.
In a three factor we are talking butterfat, solids nonfat, and
fluid carrier.

JUDGE CLIFTON: Mr. English.

MR. ENGLISH: Thank you.

BY MR. ENGLISH:

Q. So again, and part of this may be that I was trying to
get ten minutes of testimony into 6 minutes and 10 seconds
yesterday. Going back to Table 2 and your cliff notes, and
looking at the bottom of page 5 and the top of page 6. First
of all, you have included a column for whole milk, correct?

A. Correct.

Q. But this analysis is completely irrelevant as to whole
milk because you don't fortify whole milk, correct?

A. Correct.

Q. And for simplification, in page 5 and 6, you have tried
to look at just reduced fat milk, correct?
A. Reduced fat and low fat.

Q. I'm sorry, yes. And so what you were trying to show, looking at page 5, is you say that "under the two price formula, the cost of reduced fat milk at high test, the high test skim is 1.6171," and yesterday you pointed that out, correct? As being where on Table 2?

A. It would be the third column from the left.

Q. Under top spot?

A. Top left on Table 2.

JUDGE CLIFTON: Wait a minute now, you lost me at fat milk.

MR. ENGLISH: At reduced fat milk.

JUDGE CLIFTON: You didn't say reduced fat milk, you said fat milk. Start again.

BY MR. ENGLISH:

Q. On page 5 you were initially comparing reduced fat milk at the high test skim, correct?

A. Correct.

Q. And that's what you were just pointing out in that column is $1.6171, correct?

A. That is correct.

Q. And you are comparing that to the two factor, same thing, reduced fat milk, which is the bottom box, same column, of 1.6565, correct?

A. That is correct.

Q. And that has a, just under 4 cent difference, correct?
A. Correct.

Q. 3.9 --

A. 94 cents per gallon.

Q. Yeah. And when you go to the three factor formula for those same types of milk, so third column, reduced fat, upper right versus bottom right. Upper right you have 1.6815, correct?

A. That is correct.

Q. Bottom right you have 1.6810, correct?

A. Yes.

Q. And that is a difference of .05 cents, correct?

A. Yes.

Q. Okay. And what conclusion do you draw from those differences?

A. That you have a much tighter difference depending, or regardless of what the skim content is under a three factor pricing formula.

Q. And why is a tighter difference important?

A. You are ensuring equal raw product costing for handlers in the Class I space, so that nobody has a competitive advantage based on their skim content of the milk coming in.

Q. And in addition, what impact would that have to the pool of using a three factor formula versus a two factor formula?

A. My data would show that the per gallon cost would be
higher in a three factor than a two factor.

Q. And so the pool, maybe not a huge number, but the
pool's going to be bigger?

A. Correct. There will be more Class I dollars.

Q. All right. Your Honor, I repeat my request to admit
Exhibits 147 and 148.

JUDGE CLIFTON: Let's go back to Ms. May's question on
Page 1.

MR. ENGLISH: I'm sorry, thank you very much.

BY MR. ENGLISH:

Q. So this is the question in the middle of the page, and
so, Mr. Blaufuss, your testimony has focused exclusively on
condensed, use of condensed, correct?

A. Correct.

Q. So this language we are proposing would be for
condensed which is 1051.60(a)(6), correct?

A. Correct.

Q. Okay. And there could be conforming changes to (a)(5),
but Dean Foods doesn't use nonfat dry milk, correct?

A. That's what my belief is. I don't believe we use any
nonfat dry milk to fortify.

Q. So at the moment, we don't have testimony on what that
language would be, but we may very well brief it from the
Dairy Institute of California, but the focus of this testimony
has been on (a)(6).
JUDGE CLIFTON: All right. So the proposal, Mr. English, is, to insert (a) in the second line just below the heading Fortification Credit Revision on page 1 of Exhibit 147?

MR. ENGLISH: Yes, between the 60 and the 6.

JUDGE CLIFTON: All right. Do you see that, Ms. Frisius? Thank you. Done.

MR. ENGLISH: And we, just as a statement for the record, we don't disagree that it a similar change could be made to (a)(5) we just refocused on (a)(6) today.

JUDGE CLIFTON: Is there anyone who wishes to question Mr. Blaufuss with regard to Exhibit 147 to determine whether you have any objections to it being admitted? No one. Are there any objections to the admission into evidence of Exhibit 147? There are none. Exhibit 147 is admitted into evidence.

(Thereafter, Exhibit 147, was received into evidence.)

JUDGE CLIFTON: Does anyone wish to question Mr. Blaufuss regarding Exhibit 148 before you determine whether you have any objections? No one. Are there any objections to the admission into evidence of Exhibit 148? There are none. Exhibit 148 is admitted into evidence.

(Thereafter, Exhibit 148, was received into evidence.)

MR. ENGLISH: Your Honor, the witness is available for
further examination.

JUDGE CLIFTON: Who will be the first to question Mr. Blaufuss on this issue? Mr. Beshore?

CROSS-EXAMINATION

BY MR. BESHORE:

Q. Marvin Beshore. Good afternoon, Mr. Blaufuss.

A. Good afternoon.

Q. I have just a couple of questions and they are sort of this level and not down on this level.

A. You don't want to get buried in the weeds today?

Q. Not in the weeds, at the moment. So taking off from some of the last questions with Mr. English. Is there really a problem that needs to be addressed by this? Are there, do you have any information on actual tests to distributing plants which show a sufficient variation that needs to be addressed with this complication to the Order language? I'm assuming that your calculations and analysis, you know, is correct. And you know, there may be questions about it from people that are more capable of getting into it than I am, but assuming it is correct, is there actually a problem out there that needs to be addressed by bringing a fluid carrier into an order where we don't have it in any other orders? So I'm wondering is it, you know, there may be a theoretical problem, but the Order has, you know, large plants, diverse milk supplies. I mean, is there really any difference that amounts to any difference in
the, you know, in the content of the milk coming into
distributing plants which, you know, which needs to be
addressed here?

A. Well, first off, I don't have the other Class I
bottlers' information to know what their solids content are.
The only thing I can say, you know, it hasn't been a problem in
California today because they do have the three factor pricing
formula. So I can't stick to it and say there's disorder and
it is causing inefficient movements of milk today, but the
three factors what we have in California today, and whether or
not it's needed or not, it was at one point, when they put in
the pricing system in California, it was thought to be valid.
And I still think given how we price milk in California today,
I think it is still valid.

Q. So it's -- you want to -- it is preventive if not
curative?

A. I think you could look at it that way. I don't have
any data that says if we have a two factor, automatically
inefficient movements of milk are going to occur. If I'm
looking at how you price milk, I don't -- I have a higher per
gallon cost, but you have more equal raw product costing among
handlers.

Q. Okay. But for the issue with, you know, that you have
addressed with the fluid carrier, I gather that the amount of
of the fortification credit which is presently in California,
which is the same in Proposal 1 and is as in Proposal 2, is
appropriate and satisfactory as far as you are concerned, the
Dairy Institute is concerned?
A. Well, I will say, just talking fortification credit
alone, we have made the modification. If I'm looking at what
we had in our Proposal 2 and looking in the last five years, we
actually would have had an average credit significantly above
0987. And actually, I think if I remember correctly, credit
came to about 20 cents on average. So actually when we made
this modification, we're reducing the potential credit in our
proposal to reflect current California and to eliminate any
kind of increase fortification credit that we may receive under
what was originally Proposal 2.
Q. Okay. But with the modification, you are satisfied
that that's a sufficient fortification credit?
A. Correct.
Q. Okay. Just a question about the generation of the
fluid carrier value. Where does the .24 come from?
A. As I understand, actually, I talked to Dr. Schiek about
this probably a week or two ago. I think there was a late
'90's hearing or we'll call it residual value was put in place,
so they had attached the .76 to the SNF value and the .24 to
the fluid carrier. And the exact rationale behind it I don't
know. I was just informed that that's kind of when that got
put in place, was the late '90's hearing.
Q. Okay. And so that's, you just carried it forward because it is in the CDFA formulas now?
A. Correct.

Q. Basically. On --

JUDGE CLIFTON: I just want to make sure I'm clear. So Mr. Blaufuss, you just said .76 to the solids not fat and .24 to the what?

MR. BLAUFUSS: .76 solids not fat, .24 to the fluid carrier. And actually, if you go, if we just want to have a visual of what the formula looks like, it is page --

JUDGE CLIFTON: Yes, please.

MR. BESHORE: Page 1 of your testimony.

MR. BLAUFUSS: Oh, yeah, that will do.

JUDGE CLIFTON: Okay. So --

MR. BESHORE: That's where I was looking at it anyway.

MR. BLAUFUSS: You can get there different ways, it's certainly easier.

JUDGE CLIFTON: Okay. So I'm looking at page 1 of Exhibit 147, and I definitely see the .24. Where do I find the .76? Oh, I'm not concerned with that here, am I?

MR. BLAUFUSS: No, that's the only revision we made. So in order to calculate the SNF value, and this is, I didn't have it here, but basically, not basically, you are taking the Class I skim times .76 and then you are dividing that by 9.

JUDGE CLIFTON: Okay.
MR. BLAUFUSS: And that's the SNF calculation.

JUDGE CLIFTON: Okay. Thank you. Mr. Beshore?

BY MR. BESHORE:

Q. Okay. In Exhibit 148, on the two series, which cost out at the high and the low solids content at 9.2 on the high side and 8.8 on the low side. I notice on both of those you just use, you use pool butterfat contents in each case. That is just the same, same butterfat as on the actual table. And I'm just wondering if that, I mean, when you have high test, high solids milk, you tend, you always have higher butterfat, I think. And when you have low solids, you tend to, it tends to go with lower butterfat. I wonder if that makes any difference in any of this.

A. I didn't view it causing any kind of major change. If I was going to adjust it, I think looking at the files that I had, I had enough variables that were moving around, that I didn't see what benefit it would be to move around the fat as well, and I didn't want to create any different, any differences based on the fat alone, because really in this case I'm more worried about what's going on in the skim.

Q. Right. I guess, again, I'll take your word for it. I guess that doesn't make any difference. It is just, I don't know, intuitively I wonder whether it makes any difference because you are working with either more or less pounds of skim in the milk to generate your formulas. And maybe it doesn't
make any difference. I'll leave it at that. I just noticed it
and was interested.

One other -- one other little thing I noticed on the
numbers here. If you just look at Table 3, I guess it carries
all the way through, your targets, this is in G and H, Columns
G and H, your targets I noticed are 10.2 and 11.1, I mean,
slightly, I guess above the minimum required level. Is there a
reason for that?

A. That was the direction the MA staff pointed me towards
and I think ultimately when you land a skim test you want to be
slightly above the minimum to make sure that you are meeting
that threshold. I would assume they are just adding a little
extra value there to create a little more over run so you are
not creating a 9.8 or 9.9 once you have the full product in.

Q. Okay. Now, you have said that you, that all of
Exhibit 148 was run based on the prices that would be generated
by Proposal 2's formulas. Am I right on that?

A. Yes. So if I'm talking based commodity values, I'm
using the default values because obviously there's no western
price survey for the different commodities that we have in
Proposal 2. So for both the advanced and the announced, it was
the actual NDPSR prices, announced per USDA AMS, and then I
actually went back in, so we're talking these classified
pricing formulas. I also used, you know, our pricing formulas
today and pulled them all the way back so there was no formula
changes between 2010 and 2014.

Q. And were you using the Proposal 2 proposed FOB adjuster in the fault of a western price?

A. Yes.

Q. Okay. And the Proposal 2 make allowances?

A. With the one difference is I didn't make the update on the nonfat dry milk make allowance. But it was the same for, it's not like I had announced in one make allowance and the advanced in another, they were consistent. And so that's why in my view I didn't view having to reprint all this, because I wasn't trying to come to a full line of cost, I was looking at the price differences. So my view, as long as those formulas weren't different, it didn't create major issues.

Q. And what about the whey value?

A. In this I just used the base NDPSR whey, dry whey.

Q. Do you -- do you show the class, resulting Class I prices here anywhere?

A. The Class I, the skim portion, you can find, so if I'm just looking at Table --

Q. Column X, I guess.

A. Yeah, Table 3, Column X will have the Class I skim milk, so that's a skim value, and that includes a 2.10 differential. And then if we go further back and look at the butterfat, that actually has the butterfat value as well with a 2.10 differential.
Q. That would be --

A. Columns AJ and DG.

Q. And AJ is butterfat per pound? Since it is one percent, would that 1.5809 in January 10 would be a pound of butterfat?

A. Correct. So really AJ would be where you would look to find the value, since you are multiplying by one.

JUDGE CLIFTON: To find the value of what?

MR. BLAUFUSS: A pound of butterfat. So if you look in Column AG, that's two pounds of butterfat, so it's going to be double the rates on a per pound basis.

MR. BESHORE: That's all the questions I have right now.

Thank you, Mr. Blaufuss.

JUDGE CLIFTON: Who next has questions for Mr. Blaufuss?

Mr. Schaefer?

CROSS-EXAMINATION

BY MR. SCHAEFER:

Q. Henry Schaefer with USDA.

Good afternoon, Mr. Blaufuss.

A. Good afternoon.

Q. I think I'll start with what may be the more complicated issue.

In your revisions to the Part 50(d) and part 50(a) on page 1, in the Class I price which is (a), you use a SNF price times 9. And as you mentioned, in all the Federal Order stuff
we do use 9 for nonfat solids, but in most cases, if not all
cases, that's referring to 9 pounds of nonfat in the skim. And
it would seem to me that when you are combining it with 35
here, that that should be adjusted for, that that nonfat solids
is actually in the skim, because you have got the 3 and a half
percent butterfat. And the same would apply for the fluid
carrier, because that's really making up the skim fraction,
which, when we normally convert, when Federal Orders we
convert, we're using 9 pounds of nonfat solids in the skim,
would that be correct?

A. You mean 9 percent?

Q. Or 9 percent, or 9 pounds in a hundred pounds of skim.

A. Yes, that's what I'm interpreting that.

Q. Okay. So would it be, am I interpreting that correctly
that the 9 pounds, the number 9 in that equation should
actually be something lower than that to reflect the fact that
you are using it to combine into a 35 price?

A. I think this is what's used as the base mover price, so
when I look at it, even what the Federal Order speak is, you
have a 9 percent SNF value, that's the assumed factor for price
setting, and if you have 8.8 you are going to get costed at
that. So if I look at how you announce it, this is how I would
announce it, and then you look at the plant to see what skim
and the fat ended up being in the allocation.

Q. But when we announce the price at 35, it's not, does
not have 9 percent nonfat solids in it, it actually has 8.685
percent in it because of 35 test.

  A. I see what you are saying. Yes. I did not make that
differentiation, put it that way. Basically, in this I'm
saying, I'm assuming 9 percent SNF, 3 and a half percent and
everything else is fluid.

  Q. Okay. So really what we would need to do to get to a
3.5 is change that to 8.685, and the fluid carrier would have
to be .87815 or 87, I'm sorry, 87.815.

  A. Which is essentially what California does today. So
they announce it at 3 and a half percent fat, an 8.7 percent
SNF, and a 878.

  Q. Very close to what they do, we're not that far apart
when it comes to the 35. They are a little different on their,
currently on their nonfat solids because they use an 87 as
their number. Okay.

  A. Yes.

  Q. I think in your discussion on, I can't remember whether
it was Mr. English or Mr. Beshore, there was, in the next
paragraph there where you are talking about your fortification
credit revisions, and I think they clarified it for me, but I
kind of want to be sure here. So what you are saying is you
are going to replace, in the case of the condensed, which is in
51, Section 1051.65, 60, and then (5), that you are going to
replace it with the italics that you have in there and a
similar thing for nonfat dry milk; is that correct?
   A. Yes.
   Q. So we're going to take out all the language that's in
there today and just replace it with that?
   A. That would be our intent.
   Q. Okay. And do we need the pursuant to the provisions of
the Pooling Plan in if it is going to be in the Federal Order?
   A. No, I don't believe you would. Basically pulled the
quote and I wanted to make sure I pulled the full quote, not
the partial quote, in case anybody went back and looked.
   Q. Okay. Looking at a little more on the pricing scenario
with three of the three factors of butterfat, nonfat solids,
and a fluid carrier. So you're suggesting from what you have
said so far, that we would have those three factors allocated
when we do our allocation so that we would know how much of
each one of those factors is in there; is that correct? In
Class I?
   A. Correct.
   Q. Similar to what we do today with other solids and
protein in Class III?
   A. Correct.
   Q. Okay. Kind of a question that came to me that I found
kind of interesting is, do you know if a plant ships, currently
that if a California plant ships milk, packaged milk
out-of-state, do they collect a credit on that if it's going
out with fortification?

A. I don't believe so, because I don't know they could regulate that, though I don't know that a hundred percent to be the case. I think the pool is going to be produced, processed and sold. That would be my belief. I don't -- I'm not a hundred percent positive on that.

Q. Okay. And then I guess the kind of a question that keeps coming to mind in our, a lot of our discussion here in the California hearing is, is it really necessary, and I think this also came up, maybe Mr. Beshore brought it up, is fortification really necessary in California when the rest of the Federal Orders or the other Federal Orders in the United States don't have any fortification credit, or, and they do fortify? And so I guess my question is, do you really feel it is necessary here when we don't have it anywhere else in the country on milk that's fortified?

A. In that question are you saying there's milk in the Federal Order system that is fortified today?

Q. Correct.

A. I guess I'm not generally aware that there is a lot of milk that's fortified in the Federal Order system, besides some protein plus potentially. I don't know what they would be fortified to, if we are talking the same 10 percent or 11 percent, or if it's a number south of there. I would view there could be some differences among those two different
beliefs.

Q. So if I guess if I summarize that, when California, with their relatively high fortification on 2 percent and 1 percent, that you feel it's necessary to have that credit in there?

A. Yes.

Q. I believe that's all the questions I have. Thank you, Mr. Blaufuss.

JUDGE CLIFTON: Mr. Blaufuss, were you able to give more thought to whether you could produce the spreadsheets that support your exhibits? And Mr. English?

MR. ENGLISH: Your Honor, the conundrum we find ourselves in, is we would love to do it, but, Mr. Blaufuss, do you have any idea how many hours you spent in creating those spreadsheets?

MR. BLAUFUSS: Quite a few.

MR. ENGLISH: More than a hundred?

MR. BLAUFUSS: Let's ballpark it there.

MR. ENGLISH: So your Honor, it is not proprietary in the traditional sense of being confidential, but if we share with USDA and they put up on their website, then all other Class I processors who may be competitors of Dean Foods are basically getting a gift of that spreadsheet. And you know, it would be nice if we could do it, but given the ex parte rules and the nature of things, we can't hand it over to USDA without them
putting it up. And we could not get, and I don't think we're going to get, permission from Dallas to basically take Mr. Blaufuss' valuable time and basically put it out there. It's just something that we can't do.

I can say that there was a spreadsheet initially that Mr. Mykrantz shared with Mr. Blaufuss, and if it happens USDA already has that, they can, I guess, make that available generally, and then people could obviously, already getting a starting point with this analysis, which is already out there, be able to re-create it. But to simply hand over the work product, over lunch we just could not find our way clear to do that because of what is the very valuable time that it is and what it would mean as a gift to others who are competitors of Dean Foods.

JUDGE CLIFTON: When Mr. Mykrantz testified, did he provide the spreadsheet that you are referring to as an exhibit?

MR. ENGLISH: No, I think what he did was before the hearing was noticed, and I can ask Mr. Blaufuss, how many years ago did you start on this project?

MR. BLAUFUSS: I was actually looking at the e-mail, and I thought I'd looked correctly, and I think I initially contacted him about two years ago.

JUDGE CLIFTON: Could Mr. Blaufuss provide as an exhibit the spreadsheet he got from Mr. Mykrantz?

MR. ENGLISH: I'll let Mr. Blaufuss answer that.
MR. BLAUFUSS: It is USDA material so, yes.

JUDGE CLIFTON: That would help. At least then we have got a format.

MR. BLAUFUSS: And there would actually be two, so he provided a snapshot for one month for both two factor and three factor.

JUDGE CLIFTON: And was that your template?

MR. BLAUFUSS: Yes.

JUDGE CLIFTON: I think that would help.

MR. ENGLISH: We will get that done in the next couple days, your Honor.

JUDGE CLIFTON: Okay. Great.

MR. ENGLISH: I hope that's an appropriate compromise.

Again, I hope people understand the struggle we had, given the investment that Dean Foods made in creating the document.

JUDGE CLIFTON: All right. Very good. Are there other questions for Mr. Blaufuss? Mr. Beshore?

MR. BESHORE: So I have one question then I may yield to Mr. Jablonski who, they speak in a different language.

CROSS-EXAMINATION

BY MR. BESHORE:

Q. What's your thought, Mr. Blaufuss, of whether the credit, the fortification credit, should be applicable if milk is fortified beyond the State of California requirements?

JUDGE CLIFTON: Can you be more specific? I mean, he's got
nothing to work with at all.

BY MR. BESHORE:

Q. Well, I think he might, but I will try to tie it down some more. The language on 47231, 1051.60(a)(6) talks about deducting for each pound of milk, nonfat solids this is unrevised, but just to get the point, and condensed skim milk used for fortifying Class I products to meet the State of California's fluid milk standards. And of course, you have discussed how for one percent, reduced fat and one percent you need to fortify. So my question is, in that fortification credit, which is in Proposal 1 as well as Proposal 2, costs producers money, cost the pool money.

My question is, if, for whatever reason, fortification is done beyond that required by the State of California, should the fortification credit apply?

A. I can honestly say I haven't thought about that exact scenario, but it's not our intent to create some scenario where you are giving people the ability to abuse the credit beyond just meeting the State standards. So, I mean, you are not going to be able to -- it's not my intent to say you can fortify milk up to 20 percent solids and draw the credit. That's not my intent. I can honestly say I haven't thought about that.

Q. Okay. I will yield to Mr. Jablonski.

MR. JABLONSKI: Gary Jablonski.
CROSS-EXAMINATION

BY MR. JABLONSKI:

Q. Under the three factor pricing system, if you have differences in incoming milk receipts, like 8892 from unfortified products, doesn't that reflect a difference in cost for unfortified products currently, since there's a solids not fat pricing system in place now?

A. I'm not sure I'm understanding the question. What I --

I'll answer it in how I think you are asking it, and I'm sure you will correct me if I'm wrong. When I'm going through the formulas, I'm actually pricing the milk at standards. So I'm assuming 92, left over is going to be fluid, so it's actually a price in the actual solids in the milk and the fluid in the milk, so there's going to be a differentiation in just the base skim value or the base milk value and the fortification. So if you have a higher solids, you are going to have a higher milk price, whereas you will have a lower fortification. And vice versa with the low test.

Q. If you don't fortify --

A. Correct.

Q. -- you say you are going to have a higher milk test, milk cost for the higher milk, incoming milk?

A. Correct.

Q. And that's happening now, right? I mean, if you get a higher test milk, it is going to cost you more for your milk
and whole milk?

A. Correct. Correct.

Q. And point of clarification. I believe on Table 3, Column G and H, you were asked about the 10.2041 --

JUDGE CLIFTON: Hold on just a minute, let us get to Table 3. All right. And where do you want us to look, Mr. Jablonski?

MR. JABLONSKI: G and H.

JUDGE CLIFTON: Okay.

BY MR. JABLONSKI:

Q. There's a question about the 10.2041 percent and the 1.1111 percent.

A. Uh-huh.

Q. As I understand it, you have 98 pounds of skim at those it tests, so when you add the butterfat to it you get a hundred pounds of milk, and that's when they equal 10.00 and 11.00 percent solids not fat in the finished product. That's trying to clarify why those numbers aren't 10.0 and 11.0 on those?

A. Yes, that's my belief. This is the formulas that Mr. Mykrantz provided, and that's my belief is you're kind of overshooting on the skim to pull it back down when fat ultimately gets added.

Q. Thank you.

A. Yep.

JUDGE CLIFTON: Are there other questions for Mr. Blaufuss
on this topic? Ms. May?

CROSS-EXAMINATION

BY MS. MAY:

Q. Laurel May with USDA.

On page 3 of your testimony, you, at the second line up there it says, "a 9.87 cents per pound credit is applied." Is that a maximum of 9 cents credit? It's not a fixed number, right?

A. It's the max, but it's my understanding the last couple of years in talking to our plan accountants and to CDFA staff is that 98.7 is the credit applied, so it's the maximum, but it is also the credit plants are receiving on fortification credit.

Q. Because the formula that you use always comes up to at least that?

A. It's, you know, what you read in the first page is the actual, so there's not like you are subtracting one number from another to get to that. You know, you may deduct for each pound of milk solids nonfat in such condensed market skim milk, a maximum charge of 9 and 87 hundredths cents, and you are basically given that.

Q. Okay. So I just wondered like where the concept of a maximum came from. And are you, is Proposal 2 suggesting the same maximum number with some kind of sliding scale something below that?
A. No. So, I mean, I don't know where the initial 0987 came in, I just know that's currently what's in California regulations. And that's a number, it's not a sliding scale. If I could talk what we would have in our initial is what was in the Federal Register, there was months, a few months where the fortification credit would go to zero, but it was also some months where when you do the math, it comes to being about 30 to 40 cents on the value. So we wanted to eliminate all that and just keep the 0987.

Q. So it can be 0987 but no more than that, regardless of how much it really cost?

A. Correct.

Q. Okay. And did I miss where you or somebody else said whether this credit would be available to out-of-state handlers who ship milk into California for distribution?

A. I think with a lot of these regulations, if they are pooling that volume of milk, they should be eligible for the credit. So if that milk was being pooled as Class I in the state of California, I think they are eligible to receive the benefits of being in the pool in that case.

Q. Okay. Finally, on page 6 you say that it's Dean Foods view that you should use the three factor formula for calculating a fortification credit. Is that just Dean Foods view or do you have any sense that it is the view of all the other proponents of Proposal 2?
A. While I am a member of the Dairy Institute of California, I am only here for Dean Foods. I can't speak to what our competitors' views are in the issue.

JUDGE CLIFTON: Mr. English, would you also like to respond?

MR. ENGLISH: Yes. This is an official position of the Dairy Institute of California as well.

MS. MAY: Great. Thank you. That's all my questions.

JUDGE CLIFTON: Who else has questions for Mr. Blaufuss on this topic? Mr. Blaufuss, is there anything you would like to add before I invite redirect?

MR. BLAUFUSS: Nope.

JUDGE CLIFTON: Is there any redirect?

MR. ENGLISH: No, your Honor.

JUDGE CLIFTON: All right. Mr. Blaufuss, thank you so much. I am very pleased that there were people in our audience who knew how to talk to you about these figures.

MR. ENGLISH: Your Honor, if Ms. Hancock is ready to go, otherwise we would do Mr. Blaufuss, Part 6. But I think for those who don't know from the Internet, we had a discussion before lunch, after we went off the record that we had some scheduling issues, and Ms. Hancock has kindly, I think got a witness ready to go. So I think Mr. Blaufuss will now come off the stand, and he'll be the next witness after this, subject to any dairy farmers.
JUDGE CLIFTON: Excellent. Thank you, Mr. English. Thank you, Mr. Blaufuss, you may step down now.

MR. ENGLISH: And I thank Ms. Hancock and her team.

JUDGE CLIFTON: And we are distributing documents. All right. If documents are being distributed, the Judge needs them. And who else? All right. So we have a witness in the witness chair. Before I swear him in, let's talk about the documents.

Ms. Hancock, if you would identify yourself and tell us what we have here?

MS. HANCOCK: Nicole Hancock for Stoel Rives. We have the testimony of Richard Shehadey, that will be the first exhibit we mark. What number are we on?

JUDGE CLIFTON: I believe that will be 152. So that will be the testimony of Richard Shehadey.

MS. HANCOCK: And then the exhibits to the testimony of Richard Shehadey will be Exhibit 153.

(Thereafter, Exhibit 152 and Exhibit 153, were marked for identification.)

JUDGE CLIFTON: All right. Is there anybody who does not yet have copy for your use of Exhibit 152 and 153? It appears everyone has a copy.

Mr. Shehadey, I'll swear you in at this time. I believe this is the first time you have testified in this hearing; is that correct?
MR. SHEHADAY: Yes, it is.

JUDGE CLIFTON: All right. Well, we have appreciated your being here. We have also appreciated the products that you brought for us to enjoy.

MR. SHEHADAY: We're happy to do that.

JUDGE CLIFTON: Thank you. All right. Then if you would raise your right hand.

Do you solemnly swear or affirm under penalty of perjury that the evidence you will present will be the truth?

MR. SHEHADAY: Yes, I do.

JUDGE CLIFTON: Thank you. Ms. Hancock, you may proceed.

MS. HANCOK: Thank you, your Honor.

DIRECT EXAMINATION

BY MS. HANCOK:

Q. Mr. Shehadey, Exhibit 152 is your prepared statement?

A. Yes.

Q. And if you wouldn't mind, can you read that into the record, please?

A. Read the statement?

Q. Yes.

A. Okay.

Introduction

My name is Richard Shehadey and I am the Chief Executive Officer of Producers Dairy Foods ("Producers Dairy") and an owner in Bar 20 Dairy, LLC, ("Bar 20 Dairy"). I'm
submitting this testimony in support of Proposal Number 3
submitted by the California Producer Handlers Association
("CPHA") regarding a potential Federal Milk Marketing Order for
the State of California. I support the adoption of a Federal
Milk Marketing Order as proposed by the Cooperatives in
Proposal Number 1, preserving the quota system "intact" as
Dr. Eric Erba testified to in this hearing in Exhibit 42. With
the addition of CPHA's Proposal Number 3 to the Cooperatives'
proposal, the quota system will be preserved "intact" because
it will include both types of quota, regular and exempt.

Producers Dairy History

I wish to start by explaining the Producers story --
Producers Dairy Story, excuse me. It first began as Producers
Dairy Delivery Company in December of 1932 by a group of
ambitious men wanting to package and deliver high quality milk
products in the local community here in Fresno, California. It
started with a small milk processing plant and a few trucks to
deliver fresh milk directly to people's homes in glass bottles.

In 1949, my father, Larry Shehadey, bought an interest
in that then small milk delivery business. By 1955, my father
bought out the other two partners such that Producers Dairy has
been an entirely family-owned independent company ever since.
And though my father did not have a college degree, he worked
incredibly hard to make Producers Dairy the number one dairy in
the area in a very short period of time.
One of his creative and pioneering marketing decisions was to associate Producers Dairy with Hopalong Cassidy, who, for the benefit of younger generations, was a well-known and respected fictional cowboy who was also just called "Hoppy" in TV shows that ran in the 1950's and 1960's. This helped build up Producers Dairy's market of its Class 1 products by marketing and creating brand recognition of our products, with efforts such as putting photos of Hoppy on Producers Dairy milk containers and trucks, distributing product coupons available at grocery stores to attend Hoppy's Saturday matinees, and creating a Producers Dairy radio jingle that ran on local stations. All these efforts helped develop Producers Dairy's Class 1 sales. These unique efforts really encouraged people to not only think positively about Class 1 milk and drink it, but to also look for Producers Dairy products in the stores where they shopped. I have included Exhibit A to my testimony a picture of our early advertisements with Hoppy and a picture of my father with one of our Hoppy-branded delivery trucks.

In 1957, my father decided he could better control milk quality and help when supplies were tight by having his own dairy farm. As a result, he built our first dairy cow milking operation which he named Bar 20 Dairy after Hoppy's ranch. Over the years, our family continued to invest and expand our Bar 20 dairy cow milking operations to continue to control the quality of the milk that goes into Producer's Dairy products.
Operating a vertically integrated business allows us to protect the quality of our product, and in turn, the quality of our brand. Bar 20 Dairy's operations have been key and fundamental to Producers Dairy's reputation of providing some of the highest quality milk available in the market. Our first dairy farm included a glass viewing room to accommodate busloads of school children taking field trips there. We have connected our brand equity to Bar 20 Dairy's farm operations by our unwavering commitment to "healthier, happier cows" on our farms and exceptional milk quality. We are Validus certified for our farm practices and animal welfare. Attached as Exhibit F is an explanation of this certification.

We pride ourselves on operating an efficient plant, distribution system, and supply chain. We understand that price is critical component to our -- is a critical component to our business and we work hard to control and manage our operating costs. We re-invest in assets and technology to remain as efficient and as lean as possible in our operations. But we have great deal of urban market customers (in deficit areas), and we have to absorb the costs of shipping to those markets. We do not, and will not, receive any transportation funds for delivering to these deficit areas. The net impact is that it saves the pool money and this is a regulatory disadvantage to us as compared to our competitors.

Our customers appreciate our family-owned status, our
high-quality products (including our ability to effect and ensure quality all the way from our farm to our customers), our focus on customer satisfaction, the strength of our brands, our knowledge of the industry and farms, our reinvestment into the future, our philosophy and direction as a business, our control over our supply chain. These are the factors that will utilize, excuse me, these are the factors that we utilize to secure our customer base and compete against other fluid processors.

Personal Background

For more than 50 years, I have been involved in our family dairy business. I have done everything in our operations from running tractors, milking cows, and holding various leadership roles. I received my Bachelor of Science degree in Business Administration from Fresno State College in 1965. I'm currently on the Board of the Dairy Council of California (30 years), California Milk Processor Board (a founding director and Board Member for 22 years), the local California Milk Advisory Board (District 8 Committee for 15 years), and the Milk Industry Foundation, a member organization of International Dairy Foods Association (for over 25 years and I was the past Secretary).

I have been a member of the Holstein Association for more than 40 years. I also sit on numerous local community and non-profit boards. Can I ad lib for a minute?
JUDGE CLIFTON: Certainly. You may depart at anytime and add to what we have in the exhibit.

MR. SHEHADY: Okay. When I heard this availability was open at 3:00 today, I was supposed to be at the Valley Children's Hospital, I'm on the Foundation Board out there, so when it mentioned numerous local community and non-profit boards, I thought of that because that's where I'm supposed to be sitting right now.

JUDGE CLIFTON: And I see you are wearing the proper shirt to be there.

MR. SHEHADY: To be there, right. But I'm happy to be here and fill in the time.

JUDGE CLIFTON: Thank you so much.

MR. SHEHADY: Thank you.

I have previously been appointed and served on the California Department of Food and Agriculture ("CDFA") Quota Review Committee. That committee was tasked with reviewing the quota system and whether any feasible options existed to reasonably end it. The analysis done included an evaluation of quota, which was found to be worth over a billion dollars in value. The committee evaluated various options but concluded that the cost to buy out all the allocated quota and potential impact to the pool was too great. Therefore, no further action was taken.

The California Producer-Handler Association
Today, I present this testimony on behalf of not only Producers Dairy, but also the three other exempt quota holders. The CPHA is made up of: (1) Foster Dairy Farms, Inc.; (2) Hollandia Dairy, Inc.; (3) Producers Dairy Foods, Inc.; and (4) Rockview Dairies, Inc. Their farms own exempt quota, also known as "Option 70" producer-handlers. Option 70 producer-handlers are fully-regulated, reporting to the pool for the Class 1 sales.

One CPHA is member is located in Fresno --

BY MS. HANCOCK:

Q. Mr. Shehadey, that last sentence was footnoted down at the bottom of page 3. Can you read that footnote as well?

A. Yes.

In contrast, "Option 66" producer-handlers are fully exempted from the pool for their entire production and do not participate in the quota system. CPHA members are not Option 66 producer-handlers.

Q. Thank you.

A. One CPHA member is located in Fresno County, one is located in Stanislaus County. The other two CPHA members are located in Southern California (San Diego County and San Bernardino County), which are deficit areas of milk production, which it is increasingly more -- where it is increasingly more difficult to maintain milk supply and dairy operations. These four members of the CPHA are California's final exempt quota
holders (out of the original 49) and we seek to preserve our asset, along with preservation of the rest of the quota system. Gonsalves Milk Pooling Act - Exempt Quota

When the Gonsalves Milk Pooling Act was enacted in 1967, Producers Dairy had already been operating for many years, both its own dairy farm and processing plant, as well as carrying its own marketing efforts and building up demand for its Class 1 products.

During those years that preceded the Gonsalves Milk Pooling Act, the California milk industry was otherwise in a state of upheaval and turmoil as the extreme competition for Class 1 contracts existed among other producers. The Gonsalves Milk Pooling Act was primarily created to address industry problems that did not affect producer-handlers because all the milk from their dairy operations flowed to a dedicated Class 1 plant.

JUDGE CLIFTON: I would like you to read that again because you wrote it "our dairy operations" and you read it "their dairy operations". So start again with that sentence, please.

MR. SHEHADEY: Okay.

The Gonsalves Milk Pooling Act was primarily created to address industry problems that did not affect producer-handlers because all the milk from our dairy operations flowed to a dedicated Class 1 plant. And what I meant by "our" there was "our", all four of us.
Legislators fashioned the California quota system under the Gonsalves Milk Pooling Act to provide for exempt quota in consideration and recognition of a producer-handler's unique structure in creating its own Class 1 market.

Through legislation, producers and producer-handlers, were allocated quota and exempt quota, both assets that over the last 50 years have become a valuable part of our business operations. Producers were issued regular quota that was assigned base on their historical production of raw milk that was sold to Class 1 handlers. Producer-handlers were likewise issued exempt quota for the historical production and sale of Class 1 milk. The producers were also assigned a base production volume, and anything produced beyond the base and quota assignments it was paid as overbase production. CPHA farms hold exempt quota, regular quota, and assignments for base. The majority of the milk produced by CPHA members is paid as overbase production. All of this milk and all handler sales are reported to the pool, including those volumes covered by exempt quota. Exempt quota is treated as a deduction from, or credit to, the pool. I have included as Exhibit B to my testimony, a document issued by the Department of the -- excuse me. I have included as Exhibit B to my testimony, a document issued by the Dairy Marketing Branch of the California Department of Food and Agriculture that more fully discusses the policy considerations that ultimately led to the existing
quota system in California.

Exempt quota can be converted to regular quota through relinquishment of exemption treatment (by notifying CDFA), through the sale of quota to another producer, through the sunsetting of the consanguinity requirements, or by falling out of compliance with the legislative limitations. If exempt quota is converted to regular quota, it is then entitled to the regular quota premium payments. So just as the farm side of our business (Bar 20 Dairy) holds the exempt quota value, it cannot receive other benefits from the pool.

Quota as a Producer -- excuse me -- Quota is a Producer, Not a Handler, Benefit

Producer-handlers operate two separate and distinct business units. Bar 20 dairy is our farm that is a stand-alone separate business entity that produces the milk. Producers Dairy is a processing plant that is a separate distinct business entity that processes the raw milk into a consumer product. They are separate legal entities and we operate them as separate business units with separate financial books. As with regular quota, Bar 20 Dairy, our producer side of the business, receives all of the value and benefit of exempt quota. Exempt quota is an asset for Bar 20 Dairy. It is a transferrable asset that holds accounting book value, and one to which Bar 20 assigns an asset value on its balance sheet. The California --
JUDGE CLIFTON: It's a very small difference, but just read again the ending of that sentence, beginning, second, second line up, "and one to which".

MR. SHEHADYE: And one to which Bar 20 Dairy assigns an asset value on its balance sheet.

JUDGE CLIFTON: Thank you.

MR. SHEHADYE: The California State Order regulates and audits the handler side of producer-handlers and Option 70 producer-handlers are fully accountable to the pool in a California State Order system. Each of the CPHA members reports to the CDFA for all of the product that is processed by our handler arm of the business through the monthly CDFA 800 report. The exempt quota is a deduction from, or credit to, the pool as a benefit to our dairy farms. Since the inception of the quota system in California, Producers Dairy pays Bar 20 Dairy the Class 1 price for the milk received up to the amount of the exempt quota. The plant doesn't care where they buy their milk from, as long as it's quality milk. It costs the same whether they buy it from our farm as exempt quota milk or whether they buy it from CDI. Bar 20 Dairy receives the full benefit of the exempt quota value, other milk received from Bar 20 is paid at pool prices.

JUDGE CLIFTON: Now, anytime you read, anytime you say Bar 20 but you have written Bar 20 Dairy, we know that it's Bar 20 Dairy; is that correct?
MR. SHEHADEY: Yes.

JUDGE CLIFTON: Is there any other entity in the neighborhood also called Bar 20 other than the Bar 20 Dairy?

MR. SHEHADEY: No.

JUDGE CLIFTON: Okay. Good. All right.

MR. SHEHADEY: Not that I'm aware of. I'm used to calling it Bar 20, so correct me if you need it in the record properly, I'm happy to do that.

JUDGE CLIFTON: Okay. Well, then I would like you to do that sentence again, beginning just after CDI, period.

MR. SHEHADEY: Sure.

Bar 20 Dairy receives the full benefit of the exempt quota value; other milk received from Bar 20 Dairy is paid at pool prices. Approximately two-thirds the milk we receive from Bar 20 Dairy is paid at overbase price. Proposal Number 3 preserves the quota system intact, allowing the quota benefit to the dairy farms who hold it to continue to preserve the investment they have made into that asset.

As an Option 70 producer-handler, Producers Dairy has never used the benefits from holding exempt quota to undercut or bid for fluid milk contracts with customers, because it does not have it to give. It is critically important for me to communicate that the plant side of our business (Producers Dairy) does not receive a price advantage from our exempt quota, as the plant does not have it to give.
BY MR. SHEHADEY:

Q. Mr. Shehadey, I want to pause there for just a moment. You have bolded text in that paragraph and in the preceding paragraph. Can you tell me what the purpose is of having the bolded language there?

A. Well, for the last 40 years I have heard from our competitors that we have a price advantage, and I'm trying to make it about as solid with my hand in the air and swearing to God as I can that this is a fact, and it's a fact, and it's a fact. We pay our dairy farm Class 1 for the milk, they have the exempt. The only thing they can do is give a load of manure with every new account we get. They don't have anything to give, all they have is cows and manure and milk.

    They get the advantage, Producers Dairy does not have the advantage from a price standpoint. We pay the same price as everybody else that we compete with.

Q. And have you verified that that's the case with the other producer-handlers as well that have Option 70 exempt quota?

A. They have told me that that's the case, yes, and they will have a chance to verify that themselves.

Q. You can continue on.

A. Thank you. Producers Dairy pays the Class 1 price to Bar 20 Dairy. Bar 20 Dairy receives the full benefit of the exempt quota. Producers Dairy includes the Class 1 prices in
the cost of production for our fluid milk and it competes in
the marketplace to sell our fluid products with customer
service, with branding recognition, and based on the
efficiencies we can build into our plant and distribution
systems. We operate on a level playing field with all of the
other handlers in the industry. Our exempt quota has never
given Producers Dairy a competitive advantage over other
handlers, as it is a benefit held by Producers or Bar 20 Dairy,
and the two are operated as separate business units.

JUDGE CLIFTON: May I ask a question about that right here?

MR. SHEHADEY: Surely.

JUDGE CLIFTON: So we're almost to the bottom of page 4 of
your testimony, which is Exhibit 152. Is there different
ownership of Bar 20 Dairy than there is of Producers Dairy?

MR. SHEHADEY: There's a little different family ownership,
but the way consanguinity works, it is the same family, so I
would say yes and no.

JUDGE CLIFTON: All right.

MR. SHEHADEY: It's the same family. It's the Shehadey
family and it is within the consanguinity, so it is all -- my
brother and his children, and me and my children.

JUDGE CLIFTON: Thank you. And you may resume, you're at
the last part paragraph, the bottom of page 4.

MR. SHEHADEY: Scott Hofferber with Farmdale Creamery
tested about a hypothetical situation in which a
producer-handler could use the financial benefit from having exempt quota and using that to secure customers and displace other handlers. Other handlers testified that they worry that the CPHA has used its exempt quota price advantage to undercut bids or secure customer bids. That has never been the case with Option 70 producer-handlers. No Option 70 producer-handler has ever used their exempt quota to win any customer account.

Simply put, the suggestion that CPHA members use their exempt quota to secure customer bids is not based in reality. Any sales we have won were not attributed to our exempt quota holdings, because that benefit goes entirely to the farm operations. Any sales that we have gained is because of our hard work, quality of product, and customer service. Price is always a factor in any competitive arena, and we work hard to ensure that we build in efficiencies to our business. We offer our customers a high-quality product with impeccable customer service. We have control over the quality of our product from the farm through to the final product that is sold to our customers. We have invested in modern technology, we control our cost through operating an efficient distribution system and supply chain. Hard work and dedication toward improving efficiencies on the handler side of our business is what provides the ability to submit competitive bids for customers business; it is not exempt quota and never has been
because the benefit goes to the farming operations. As Producers Dairy's mission has stated for over 20 years, it is to produce --

JUDGE CLIFTON: Let he have you start that sentence again, please.

MR. SHEHADEY: As Producers Dairy's mission statement has stated for over 20 years is "To produce the highest quality products, at the lowest cost per unit, while meeting customer expectations every time."

Producer's Dairy -- Exempt Quota Impact and Meaning

Producers Dairy was initially issued exempt quota in 1969 and later purchased quota that was allowed to be converted to be exempt quote under the last '93 amendment to the Gonsalves Milk Pooling Act.

JUDGE CLIFTON: All right. So I'm confused. So Producers Dairy at that time was a dairy farm rather than a processor?

MR. SHEHADEY: No, we're calling my statement Producers Dairy, but it is both, the statement is for Producers Dairy and Bar 20 Dairy Farms.

JUDGE CLIFTON: Okay. So just look at this sentence with me. "Producers Dairy was initially issued exempt quota in 1969."

MR. SHEHADEY: It should be our Bar 20 Dairy Farm operations.

JUDGE CLIFTON: Okay. Was it in existence then, that long
ago?

MR. SHEHADY: '69, yes, it was.

JUDGE CLIFTON: Okay. So do you think that sentence should strike Producers Dairy and instead insert Bar 20 Dairy?

MR. SHEHADY: Yes, I do.

JUDGE CLIFTON: Ms. Hancock, any objection?

MS. HANCOCK: No, not at all, your Honor, thank you.

JUDGE CLIFTON: All right. Ms. Frisius, we'll do that on page 5, right in the middle of the page. First two words under the heading Producers Dairy -- well, the first word. Let's look at the heading. Does the heading also need to be changed or no?

MS. HANCOCK: We can change the heading as well, your Honor. I guess this was meant because it's the party entity for the CPHA proposal member is Producers Dairy, but Bar 20 is the entity that owns it, so I think that that's more accurate if we change that as well.

JUDGE CLIFTON: All right. So Ms. Frisius, we'll replace Producers Dairy with Bar 20 Dairy in two places, the heading right in the middle of the page and the first two words that begin the paragraph. All right. And I have marked my copy accordingly.

So start again, if you will, in the middle of page 5, and begin to read the heading as we have amended it and continue on from there, if you will.
MR. SHEHADEY: Yes, that was a nice catch. That's makes accurate now.

JUDGE CLIFTON: You just drilled it into me.

MS. HANCOCK: She's known for those.

MR. SHEHADEY: Thank you. Appreciate it.

Bar 20 Dairy -- Exempt Quota Impact/meaning

Bar 20 Dairy was initially issued exempt quota in 1969 and later purchased quota that was allowed to be converted to be exempt quota under the last '93 amendment to the Gonsalves Milk Pooling Act. Over the years, we have invested millions of dollars to acquire additional quota. However, since the '93 amendments as of March '94, we, along with all of the other Option 70 producer-handlers, have not been allowed to expand or grow the amount of exempt quota that we hold. As a result, the exempt quota we have had since '94 has remained fixed without the possibility to ever increase the exempt quota volumes. I have included as Exhibits C to my testimony, a redacted version of Bar 20 Dairy Dairy's Exempt Quota History.

JUDGE CLIFTON: That's probably fine. You probably, it's probably called.

MS. HANCOCK: Let's take a second and turn to Exhibit C in Exhibit 153, and we printed these before we realized we should have numbered them, so I apologize.

JUDGE CLIFTON: That's fine. No problem. Well, you have even got folio numbers on it, that's quite helpful actually.
MS. HANCOCK: Kinda fancy.

JUDGE CLIFTON: Yes, it is. So let's see, all right. So, Exhibit C, pretty much --

MS. HANCOCK: It has a big black block in the middle of the page. Mr. Shehadey, can you explain for us what Exhibit C is here?

MR. SHEHADEY: Exhibit C?

BY MS. HANCOCK:

Q. To your exhibit.

A. With the blocked out section?

Q. Yes.

A. Those are the purchases of quota we made over the years.

Q. And it starts with January 1 of 1996. Do you think that that is supposed to be --

A. That's wrong, it should be '69 instead of '96, that's a typo. It started, it's progressive from 1969 on through '95.

Q. And who produced this document? Where did you get this document from?

A. I think that came from the CDFA. I think that's from their records.

Q. Okay. And so, we have, can you tell us what is blocked out there in the black box?

A. Oh, it would be the, it says up at the top, the seller, fat, solids, quota, and the dollars paid, what it cost over the
Q. And why is it blacked out there?
A. It was confidential information that we didn't think
that was necessary. The discussion was to present the amount
or the years that we bought it and that we did buy it.
Q. So if this wasn't blocked out it would have numbers in
each one of these columns?
A. Yes, it would.
Q. And including dollar amounts as well?
A. Yes, it would.
Q. Okay. And so we've blocked it out to protect the
confidentiality of the information that you have that's
individual to you, but we have totaled up the total sum paid by
all of the Option 70 producer-handlers who we represent in this
case, to get the number that we'll see in your testimony?
A. Yes, that's correct.
Q. Okay. And then if we walk down the second column there
next to the date, tell me what those descriptions represent?
A. Well, that was, those are just original issue, that's
what the pool issued, then the others are purchased.
Q. And then it has in November 1st --
A. The growth, excuse me, growth would be when Class 1
went up and then purchased is when we purchased.
Q. Okay.
A. Now, the growth issued was probably, I don't have the
amounts here, but it was, there were nominal amounts. It was because they pretty much divvied it out to everybody, so there was small amounts that went out to everybody.

Q. That was part of the equalization?
A. It is the increase in Class 1, yeah.

Q. Okay.
A. I don't know what they called it, but when the Class 1 went up, they had, and since quota was based on Class 1 sales, they gave out additional quota because Class 1 went up.

Q. And then if you move down, you have, on January 1, 1978, converted to exempt 1, do you know what that refers to?
A. Yeah, that would be the legislation that went through in '77 or I think it was finalized in '78, that we could convert what we had purchased up to that time to exempt quota.

Q. And then it's asterisks. There's the asterisks as a cross-reference at the bottom, could you read that into the record?
A. Excuse me, which one?
Q. Where it has "January 1, 1978, converted to exempt,"
and it has an asterisk and then a 1?
A. Oh, number 1?
Q. Yeah, on the bottom. Can you read what that legend says there?
A. It says, "Converted to exempt, number 1, quota purchased as non-exempt from '69 through '77 and converted to
exempt in '78." From that legislation or because of that legislation.

Q. So that would correspond to the 1978 amendments to the Pooling Act?

A. Yes, it would.

Q. Okay. And then you have additional growth down through March of '94 when it says that there were several purchases made. Do you see that?

A. Yes.

Q. And what does that reflect?

A. Just purchased quota from different sources, different people.

Q. So that's the window of time when you have a financial investment into your exempt quota, that's what that's referring to is that time period where you actually had dollars that were outlaid to purchase and acquire that quota?

A. Yes.

Q. Okay. And what does the, what does the asterisk refer to on January 1 of '96?

A. Lost exemption. That we bought some and it was passed the date, so it wouldn't qualify, so it's regular quota, it is not exempt quota.

Q. And then that refers to, I think Mr. Gonsalves testified this morning that it went retroactive where anything purchased after a certain date in March of '95 --
A. '95, I believe.

Q. Lost its exempt quota treatment?

A. Right. That's correct. So we do have a small amount of regular quota, Bar 20 does, owns a small amount of regular quota in addition to the exempt quota.

Q. And if you look at the top of that page, what does it say up there on that title?

A. Bar 20 Dairy Exempt Quota history.

Q. So who does it show owns that exempt quota? Which entity?

A. Bar 20 Dairy.

Q. Okay. All right. Let's --

JUDGE CLIFTON: Let's not leave this yet. Ms. Frisius, would you amend on this exhibit, the date that says '96 to '69 on the record copies. All right. That's done.

All right. And now, Ms. Hancock, you may take us where you will.

BY MS. HANCOCK:

Q. Thank you, your Honor. I think we were at the paragraph beginning. "Exempt quota is a valuable asset" on page 5.

A. It's right after the comment on Exhibit C there.

JUDGE CLIFTON: Yeah, but don't go there yet because we want to make sure we have the right words that end the previous sentence. So do you think you should say, Mr. Shehadey, "I
have included as Exhibit C to my testimony, a redacted version
of" and then do you think we should just have the very title
that's on Exhibit C?

MR. SHEHADAY: Bar 20 Dairies -- Exempt Quota.

JUDGE CLIFTON: Okay. The title actually says Bar 20 Dairy
Exempt Quota History.

MR. SHEHADAY: Uh-huh.

MS. HANCOCK: If we just strike the possessive Dairy's off
of that sentence, I think it will read correctly.

MR. SHEHADAY: Take this word that has the 's off?

JUDGE CLIFTON: All right. So Ms. Frisius, that's what
we'll do, we'll just strike one word, "DAIRY's". Thank you.

All right. Good. Otherwise we have to say Bar 20 Dairies, Bar
20 Dairy's Exempt Quota History, which is cumbersome.

MR. SHEHADAY: Well, this way it ties in with the
Exhibit C directly.

JUDGE CLIFTON: Very good. All right. Thank you. So now
you may continue to read with the words exempt quota.

MR. SHEHADAY: Thank you.

Exempt quota is a valuable asset owned by Bar 20 Dairy.

In addition to exempt quota, Bar 20 also owns regular quota.

JUDGE CLIFTON: That's Bar 20 Dairy.

MR. SHEHADAY: Bar 20 Dairy also owns regular quota. We
agree with Dr. Erba and Lon Hatamiya that quota has a value
that is both measurable and immeasurable, as noted in
Exhibit 42 and 54 respectively. Regular quota has a two-fold value, (1) the value that comes from the premium pricing received for Class 1 milk production; and (2) the value that can be had as a transferrable asset in buying or selling regular quota. Exempt quota not only holds the values of regular quota, but also has an additional value in that the value of that volume of milk is deducted from the pool. The measure of the exempt quota value for our farm is the difference between Class 1 and quota prices that the farm would receive if it were paid from the pool.

MS. HANCOCK: So I want to pause for one second, your Honor. It is ten to 4:00 and I don't know if you want to sneak in a break or if you want us to plow through.

JUDGE CLIFTON: I think a break would be a really good idea. All right. So let us be back ready to go at 4:10. 4:10. Brian wants you back at 4:05. We'll come back at 4:05. Good. Ms. Hancock, you may resume.

BY MS. HANCOCK:

Q. Mr. Shehadey, you were reading on your exhibit, prepared statement, that's in Exhibit 152, we're on the bottom of page 5, beginning with the title Quota and Exempt Quota Required Investments to Acquire.

A. Yes, found it.

Q. Do you want to go ahead and continue?

A. Yes.
Quota and Exempt Quota Required Investments to Acquire

Producers and producer-handlers incurred a cost in acquiring their respective quotas within the quota system. The original assignment was based on the historical production of milk used for Class 1 milk sales, so the investment came in the form of creating markets for the milk or the buyer relationships for that milk with the processor of that milk.

As the quota system evolved with the 1978 and 1993 amendments to the Gonsalves Milk Pooling Act, regular quota and exempt quota were assigned to producers and producer-handlers relative to their additional production and sales volumes reflecting additional market expansion of Class 1 sales. Producer-handlers were also allowed to acquire exempt quota by purchasing it through legislative allowances that were ultimately capped in 1994.

Q. I think that we established that that was March of 1995 so should we change that?

A. That was capped in, yeah, March of '95.

JUDGE CLIFTON: All right. Ms. Frisius, do you see where he is at the top of page 6? All right. Five lines down we're going to strike 1994 and insert March '93; is that correct?

MR. SHEHADEY: '95.


MR. SHEHADEY: Thank you.

Bar 20 Dairy invested millions of dollars in acquiring
exempt quota. The California producer-handler (CPHA) has collectively invested an additional $9,298,677.84 to acquire this exempt quota.

JUDGE CLIFTON: Now, let me refer back to page 1, I think that's where you tell us who is in CPHA. You will have to help me find it.

MS. HANCOCK: It is a little further on, your Honor. It is on --

JUDGE CLIFTON: The top of page 3.

MR. SHEHADAY: Page 3.

JUDGE CLIFTON: Okay. So when you say that the CPA has acquired or has invested, collectively invested, if we look to the top of page 3, is what we look at there the farms, the producers? Is that what's named there or are processors named there?

MS. HANCOCK: Your Honor, those are just entity titles for the members of the Producer Handler Association, but they will talk about, the individual witnesses will talk about their farms that actually made the acquisition, which have different names.

JUDGE CLIFTON: Okay. So that's a little confusing, folks, just sayin'.

BY MS. HANCOCK:

Q. Okay. So Mr. Shehadey, would it be more accurate then to say, "the farms of the CPHA have collectively invested" in
that last sentence that has --

A. You could say, "the dairy farms of CPHA have collectively invested an additional 9 million to acquire this exempt quota."

Q. Okay.

JUDGE CLIFTON: So let's do that, Ms. Frisius, we'll strike "the CPHA" and we will insert "the dairy farms" and help me with the wording, Mr. Shehadey.

MR. SHEHADEY: Of the CPHA.

JUDGE CLIFTON: Of the CPHA.

MS. HANCOCK: And I think we need to strike an additional, because I think the total for the four is that 9 million number.

JUDGE CLIFTON: Mr. Shehadey, do you agree that the word "additional" should, that we should strike it?

MR. SHEHADEY: Yes, it is inclusive of our purchases also, so it shouldn't be additional.

The dairy farms of the CPHA have collectively invested and, invested, instead of an, we should take that out, and additional, and it would just be "they have invested 9,298 to acquire this exempt quota."

JUDGE CLIFTON: All right. Does that include all of the money spent throughout the history of the each of these dairy farms to acquire the exempt quota?

MR. SHEHADEY: That's what I understand, yeah. It would be
over that same period of time that I had on Exhibit C was it?

JUDGE CLIFTON: Yes.

MR. SHEHADEY: Yes.

JUDGE CLIFTON: Okay. Thank you. So read the sentence
again so Ms. Frisius can check the corrections she made.

MR. SHEHADEY: The dairy farms of the CPHA have -- I should
say have instead of has -- have -- collectively invested
$9,298,677.84 to acquire this exempt quota.

JUDGE CLIFTON: Thank you.

BY MS. HANCOCK:

Q. Mr. Shehadey, before you get started again, just to be
clear, has your plant ever invested any money in acquiring your
exempt quota?

A. No.

Q. And so all of the funds that came out of an account to
pay for the exempt quota came from which entity?

A. Bar 20 Dairy Farms.

Q. Okay. You're free to continue when you are ready.

A. Preservation of exempt quota also requires compliance
with ongoing business structural limitations. In order to
maintain exempt quota treatment. The producer and handler
business units must be over 95 percent common ownership as
compared to the original issuance of the exempt quota in 1969.
Because of the original ownership requirement for exempt quota
holders that is benchmarked against the original issuance of
quota, we have been prohibited from selling any part of our
business, either the farm or plant side of our business.
Knowing that we had to keep our business units intact to
preserve our exempt quota treatment, we instead have made
strategic business decisions, both at the farm and at the plant
in order to ensure that the business units stay within the
original 95 percent ownership requirements. All of these have
been investments into obtaining, maintaining, and preserving
our asset: Exempt quota.

In evaluating to adopt --

Q. I think we skipped a page. Should be a heading, Quota

System is Integral.

A. Oh, excuse me.

Quota System is Integral to Operations

Exempt quota has essentially allowed us to maintain the
business structure that my father had already created when the
Gonsalves Milk Pooling Act was enacted. It has allowed us to
continue to not only exist, but survive in an increasingly
competitive industry that has consolidated significantly since
the 1960's.

When Producers Dairy began, there were numerous
producer-handlers in the Central Valley of California. But
today, we are one of the few remaining in the Valley. When the
Gonsalves Milk Pooling Act was originally enacted in 1967,
there were 49 producer-handlers in California, but today there
are only four. Each of the four remaining producer-handlers is an independent, family-owned, and privately-held company, which is rare in today's dairy industry landscape that is otherwise composed of large corporate conglomerates and grocery-owned captives. If the exempt quota holders held such a price advantage, you would not have seen such a decline in these numbers for the 45 that are not here today. Farmers do not usually go out of business because they are making too much money.

Q. Mr. Shehadey, I have a question that I don't think we have covered so far in this hearing. When the exempt quota holders were originally granted in 1969, and then later on where there were opportunities to grow or increase exempt quota holders, could new exempt quota holders be created?

A. No.

Q. Okay. So --

A. It's a grandfather from 1969 and prior, but not after. No one could come in and become a producer-handler under Option 70.

Q. And then after March of '94 you couldn't expand any of your exempt quota holdings either?

A. That's correct.

Q. Okay.

A. Go on?

Q. Yes, please.
A. Quota system is integral to operations —

Q. Oh, you read that. We're on the paragraph, "in evaluating".

A. I'll get the right page here.

In evaluating whether to adopt a Federal Milk Marketing Order in California, Congress tasked the Secretary with recognizing quota value. 7 U.S.C. Section 7253(a)(2) ("California shall have the right to reblend and distribute order receipts to recognize quota value.") The Joint Explanatory Statement of the Committee of Conference reiterated the intent behind preserving the quota value, which meant recognize the quota system:

The managers intend for the Secretary --

JUDGE CLIFTON: Now, it appears that you're quoting here. Is this a quote?

MR. SHEHADEN: Yes.

JUDGE CLIFTON: Okay. Begin the quote then.

MR. SHEHADEN: It's taken from the statement of the committee. Should it be a quote?

MS. HANCOCK: Yes. You are just, she just wants you to identify it as a quote for the record.

MR. SHEHADEN: Right, because it's inset in here as a quote.

JUDGE CLIFTON: Right, inset, and then when you finish that inset, you can tell us that you have finished it.
MR. SHEHADEY: Unquote? Okay. To start:

The managers intend for the Secretary to conduct a
hearing prior to the issuance of an order
designating the State of California as an FMMO.
The provisions provides --

JUDGE CLIFTON: Now read it exact.

MR. SHEHADEY:

The provision provides the Secretary of
Agriculture with the discretion if a California
FMMO is requested, to recognize the long-standing
California quota system.

MR. ENGLISH: Your Honor?

JUDGE CLIFTON: Mr. English?

MR. ENGLISH: I'm going to object to the next sentence with
the legal interpretation of the only means to recognize.

JUDGE CLIFTON: Or "the only way by which"?

MR. ENGLISH: Yeah, is to preserve. I object to that for
the reasons stated in the past, and I also know what your
ruling is going to be.

JUDGE CLIFTON: Thank you, Mr. English, your objection is
noted. I will ask that the United States Department of
Agriculture employees utilize your objection as a caution.

Nevertheless, I will accept into evidence this witness's
interpretation as stated in this exhibit. So you may continue
to read, Mr. Shehadey.
MR. SHEHADAY: The only way by which to recognize, "recognize the long-standing California quota system," is to preserve the value of both regular quota and exempt quota together, as they are both granted at the quota system's inception. The inception of the quota system granted to both regular producers, the value of regular quota, and granted to Option 70 producer-handlers the right to hold exempt quota. The value of quota for Option 70 producer-handlers is found only in their exempt quota, and if exempt quota were not adopted as part of the quota system, it would diminish the CPHA's quota value.

The California Food and Agriculture --

JUDGE CLIFTON: And should we conform that to what we did on the previous page? The quota value is actually not owned by the entities that you have identified as the CPHA, is it?

MS. HANCOCK: So it would be the dairy farms of the.

MR. SHEHADAY: It would be "the CPHA dairy farms".

JUDGE CLIFTON: Good. So Ms. Frisius, do you see where we are, end the first full paragraph on page 7? We'll just add, after CPHA, apostrophe "s", dairy farms, and then an apostrophe after the "s" on farms.

MR. SHEHADAY: Yes, that explains it.

JUDGE CLIFTON: And if you would now read that sentence again, Mr. Shehadey,

MR. SHEHADAY: Yes.
The value of quota for Option 70 producer-handlers is found only in their exempt quota, and if exempt quota were not adopted as part of the quota system, it would diminish the CPHA's dairy farms' quota value.

BY MS. HANCOCK:

Q. Thank you, your Honor.

A. The California Food and Agricultural Code has long since provided that the exempt quota value would not be diminished and we (Option 70 producer-handlers) as an ongoing business operation, have relied on that protection to continue to invest in the structure and business model that will allow us to preserve our exempt quota.

Cal. Ag. Code Section 62716(e) ("All pool quotas initially determined pursuant to Section 62707 shall be recognized and shall not in any way be diminished."); Section 62707 ("There shall be no downward adjustment of pool quota below the quota initially established pursuant to this chapter.")

As noted in the CPHA additional proposal, the producer-handlers quota exemption is relatively insignificant in terms of overall production in California. In July 2015, as reported by the CDFA, only .65 percent of total pooled milk fell under the exempt quota.

To look at the exempt quota through all perspectives based on the CDFA data, today exempt quota can be viewed as follows:
* 0.65 percent of the total pool milk in California, 
(note that exempt quota is calculated in the total pool 
and then deducted.)

* .26 percent of quota --

JUDGE CLIFTON: Now, read that second bullet point again, 
please?

MR. SHEHADAY: Second bullet point, 2.6 percent of quota, 
which is a 10 percent drop since 2007.

Next bullet point, 4.6 percent of the total Class 1 
pooled.

And the fourth bullet point, 17.4 percent of the CPHA 
Class 1 production (compared to 1985 when exempt quota made up 
66 percent of CPHA members' Class 1)

BY MS. HANCOCK:

Q. Now, Mr. Shehadey, if we could turn to Exhibit D in 
Exhibit 153?

A. Yes.

Q. You have a table there. Is this a table that you and 
your staff completed?

A. Yes, it's from the CDFA information.

Q. And when you say CDFA information, it's in part from 
Exhibit 61 table AC?

A. Some of it is, yeah.

Q. Okay. And then you have some additional information on 
1985 in there?
A. Yes.

Q. And what was that information from?

A. Well, it would all be from CDFA information we received at different times.

Q. And how is it that you had information from the 1985 time period?

A. I don't recall the reason why we gathered it at that time.

Q. This is information you have been tracking over the years?

A. Yeah.

Q. And you have sat on various committees with the CDFA?

A. Yes.

Q. Review committees, reviewing, in effect, I think you testified earlier you reviewed a quota, the quota program as a whole?

A. That was in 2007, I believe.

Q. And prior to that you have attended other CDFA committee meetings as well?

A. Yes. Or if there was proposed legislation or some discussion, we might have gathered more information from CDFA at these different times.

Q. Okay. You can go ahead and continue on your testimony.

JUDGE CLIFTON: Let me ask about that last bullet point. So we're talking here about Class 1 production, and so that,
does that Class 1 production actually come from the handlers?

MR. SHEHADAY: Yeah, it's actually their sales.

JUDGE CLIFTON: Okay. Thank you.

MS. HANCOCK: So it's not the total pool, it's just the
total Class 1 production for the producer-handlers?

MR. SHEHADAY: Yes, sales. Class 1 sales.

JUDGE CLIFTON: Thank you.

MR. SHEHADAY: If you go to the Exhibit D --

JUDGE CLIFTON: Yes.

MR. SHEHADAY: That number is on here so it shows how it is
calculated.

JUDGE CLIFTON: And just show me where to look for --

MR. SHEHADAY: Okay. That 17.4 percent is over to the left
on the bottom, there's three lines; total producer-handler
Class 1 sales, total producer-handler exempt quota, and then
percent of the exempt, which is a calculation of those two.
And that came from the Table AC, which I think was Exhibit 61.
A prior exhibit.

BY MS. HANCOCK:

Q. Mr. Shehadey, is out-of-state milk production factored
into this calculation?

A. No, I don't believe so.

Q. And if you added out-of-state milk Class 1 sales to
this number, what would that do to your percentage?

A. Well, it wouldn't affect this percent, because this one
is just producer-handler sales.

Q. Okay. Oh, that's right.

A. But if you took it of the total sales, it would go down because the number would be bigger that you are dividing into.

Q. Okay. So the 4.6 percent of the total Class 1 pool, if out-of-state milk, and I'm back on Exhibit 152, you have 4.6 percent of the total Class 1 pool, if out-of-state milk were factored into the Class 1 pool, what would that do to your percentage of the Class 1 pool?

A. That would go down.

Q. Okay. You would have an even smaller percentage of --

A. Percentage of the total pool including out-of-state, right.

Q. Okay.

JUDGE CLIFTON: Now, you may continue, Mr. Shehadey, just below the bullet points.

MR. SHEHADEY: Okay. Thank you.

These numbers reveal that the exempt quota as a percentage of the pool Class 1 production, and even as a percentage of Class 1, CPHA Class 1 production is shrinking as the years go by.

Over the years, many of the other 45 producer-handlers have relinquished the benefit of their exempt quota in order to make changes to their business structure or to sell the quota as regular quota to qualify, liquefy their asset. Exempt quota
holders have declined more than 91 percent since the enactment of the Gonsalves Milk Pooling Act, with 49 exempt quota holders in '69, 27 in 1975, but only four today.

Q. If we look back at Exhibit D one more time in your Exhibit 153, what you have calculated there on that bottom box is, it has January of 1985, March of 2009, and then there's a percentage. What does that percentage reflect?

A. Which one?

Q. On Exhibit D in that bottom box?

A. Yeah.

Q. You have the first column, which is January of 1985; is that right?

A. Yes.

Q. Then the next column is March of 2009; is that right?

A. Yes.

Q. So does that help you recall, you must have had this data in March of 2009. Is that the time that you were sitting on the committee with the CDFA evaluating quota?

A. I don't remember the date. I mean, why that was that. It seems like that committee was earlier than that, '07 or '08.

Q. Okay. And then the third column, you have change '85 versus '09, what are you reflecting there?

A. That would be the growth from '85 to '09, of Class 1 producer-handler sales.

Q. Okay. And then if we look at the next column for
August of 2015, has the total producer-handler Class 1 sales
grown since March of 2009?

A. It is almost the same. The sales and the exempt quota
has actually gone down some.

Q. Okay.

A. So the percentage went from 17.7 in '09 to 17.4 in
2015.

Q. Okay. You are free to continue on with your statement.
I think it starts with "as the number of exempt".

A. As the number, yeah. Okay. The reason I'm having
trouble on these pages is, I had them print a large print for
me so I could easily read it, but the pages don't coincide with
everybody else's, so I'm going back and forth trying to be sure
everybody understands what I'm trying to say.

Well, thank you. As the number of the exempt quota
holders have decreased, so has the producer-handlers percentage
of Class 1 sales. Between '85 and today, the exempt quota
holders percentage of our total Class 1 sales has decreased
from 66 percent to 17.4 percent since 1985, a 48.5 percent
decrease in 30 years.

I have included in Exhibit D to my testimony, a
document entitled, "Key California Milk Market Facts Regarding
Producer-Handlers," which shows the decline of producer-handler
production during various periods between '69 to 2009.

Exhibits E are the Class 1 prices that we used to calculate the
average over the last 20 years.

Q. And if you turn to Exhibit E, can you tell me where you received this information from?

A. That was all, it says at the bottom it is source CDFA, and that gives the website, it came off of their website.

Q. Okay. And over the past 20 years that you have charted here, what was the average Class 1 price?

A. If you go to the last page, the average is $1.14 difference between a Class 1 and quota, so that would be the exempt quota value average for 20 years.

Q. And how did you factor that amount?

A. How did I factor it?

Q. Yeah, how did you calculate that amount?

A. We added it up and just divided it by all of those months and came up.

Q. Tell me what the columns that are represented in Exhibit E are that you used to calculate that exempt quota difference?

A. Well, on the first page, the first column is a month, then the year -- the month, the year, Class 1 Northern California, Quota Hundredweight, and the difference.

Q. Okay. So then you took, you took the Class 1 amount, and you added that column up?

A. Well --

Q. Or did you do it month by month?
A. I think we added it all up.

Q. You have the difference there at the end of each month, right? So you have -- you have taken Class 1 price and subtracted the quota price for each, for each month?

A. Yeah, it's the average difference for the 20 years.

Q. So the average on the bottom there is just the average of the difference reflecting what the exempt quota value was for that 20 years?

A. Yeah, as you can see, some months it's positive, some months it's negative. If you go to July 1998, it was a minus 177. So that's where the $1.14 came in, it's a total of, total difference for 20 years for all those months.

But the $1.14 is a hundredweight for the 20 years that the exempt quota would have been as a premium over quota to the producer-handlers.

Q. So some months --

A. In value.

Q. So some months exempt quota is a greater value than in other months?

A. Yes.

Q. And this is the value that Bar 20 receives?

A. Yes.

Q. And what about your plant, does your plant receive any of this value?

A. No, the plant pays it.
Q. Pays the Class 1 price?
A. Yes, for the exemption.

Q. Has there been a month ever since you have owned exempt quota that the plant did not pay that Class 1 price?
A. No. Every month it's been paying Class 1 price since the outset in 1969.

Q. Okay. We can continue on with your next heading.

JUDGE CLIFTON: Before you go there, Mr. Shehadey, looking at Exhibit E, is the Fresno area in the Northern California portion of the state?

MR. SHEHadeY: Yes, it is.

JUDGE CLIFTON: And of your three other holders of exempt quota, how many of them are in the Northern California portion of the state?

MR. SHEHadeY: One other, Foster Farms Dairy.

JUDGE CLIFTON: All right. So half of you are in the Northern California?

MR. SHEHadeY: That's correct.

JUDGE CLIFTON: And the other half are in the Southern California?

MR. SHEHadeY: That's correct.

JUDGE CLIFTON: Go ahead, Ms. Hancock. No, go -- you go ahead, Mr. Shehadey. You are starting with a new heading.

MR. SHEHadeY: New heading:

California Exempt Quota is not the Same as Federal Order
Producer-Handler Exemptions

Exempt quota is not the same as Federal Order producer-handlers exemptions that were addressed in the 2010 final rule from the USDA Agricultural Marketing Service. The quota system is a benefit asset held by a producer and it was the compensation and recognition given to the producers for creating a Class 1 market: regular quota was assigned to producers, and exempt quota was assigned to producer-handlers. This is a legislative grant of an asset to producers and producer-handlers who had created the Class 1 market.

The exempt quota is a booked asset for the producer business units, not the handler side of the business, and the financial value for the exempt quota is held by the producer. The handler side of our business is fully regulated and reports all sales to the pool. Exempt quota is treated as a deduction from (or credit to) the pool. Exempt quota is a finite amount that cannot be expanded or sold. The CPHA members cannot sell their business or transfer it to anyone outside of the original ownership family line. The exempt quota will eventually cease to exist once the generational transfers have been met, and the exempt quota will then be converted to regular quota.

Federal Order producer-handlers, on the other hand, were operationally and factually different from California exempt quota holders. In the Federal Order system, producer-handlers used to be fully exempted from the pool.
This was a benefit to the handler side of the business and there was, as there was no pool obligation for producer-handlers. There was no financial investment required to obtain their exemption benefit and they did not have any asset value for their exemption rights which the California quota system offers. Producer-handlers could sell their businesses as long as the joint ownership requirements were met. They did not have any legislative rights to a transferrable asset with book value. The exemption did not expire or sunset with the tables of consanguinity, as in the case with the CPHA. The sky was the limit and their exemption was unlimited as to scope, time, volume and potential. There was tangible evidence revealing that they had created disorder markets in the markets by their unlimited growth and market penetration.

As explained by Dr. Erba and Mr. Hatamiya, all of the justifications for preserving quota also apply to preserving exempt quota. Indeed, if the Secretary is going to preserve the quota system, he logically must include both regular and exempt quota. The Cooperatives have presented no evidence of disorderly market conditions created by the quota, and the Dairy Institute of California has repeatedly stated that there are no disorderly market conditions in California.

At most, some handlers have alleged perceived competitive concerns that have never materialized into an
actual evidence ("paranoia" as one handler described it).

Preserving exempt quota does not present a risk of disorderly market conditions that were present in the Federal Order producer-handler hearings. Indeed --

JUDGE CLIFTON: Wait, wait, wait, okay. All right. I'm with you.

MR. SHEHADEY: Want me to restate that?

JUDGE CLIFTON: Yeah, would you just start with preserving exempt?

MR. SHEHADEY: Sure.

Preserving exempt quota does not present a risk of disorderly market conditions that were present in the Federal Order producer-handlers hearings. Indeed, after 50 years of exempt quota being part of the California State Order system, to my knowledge, there has never been a finding of disorderly market conditions, and no reports that any CPHA member has improperly priced product below cost because of the exempt quota. This is a further acknowledgement that the quota system, including the exempt quota, presents no significant disruption to the market.

Financial Impact Analysis

As the USDA economic analysis noted, there is essentially no economic impact or change from baseline if exempt quota is preserved. This makes sense, given that preserving the exempt quota simply preserves the status quo of
what has existed under the California State Order system since
the inception of the Gonsalves Milk Pooling Act. Further, if
exempt quota were to be eliminated, the net effect on the pool
would be minimal, if any, for other producers. The exempt
quota would be converted to regular quota so it would be paid
at a premium and also qualify for transportation allowances.
Based on our calculations, and a confirmed in Dr. Erba's
testimony, this would result in plus or minus a penny a pound
to the pool. A penny a hundredweight -- should that be
hundredweight, I think?

MS. HANCOCK: Yeah.

MR. SHEHADAY: A penny a hundredweight to the pool.

JUDGE CLIFTON: So shall we change that? Are you sure?

MR. SHEHADAY: It should be cwt.

JUDGE CLIFTON: All right. Ms. Frisius, do you see where
we are on page 9, the last part of the first paragraph under
financial impact analysis? We're going to strike LB, and
insert CWT.

MS. FRISIUS: Yes.

JUDGE CLIFTON: Thank you.

MR. SHEHADAY: If the Cooperative's proposal were adopted
and exempt quota were not preserved, presumably the exempt
quota would be converted to regular quota. CPHA would receive
quota premium prices for its Class 1 milk, Class 1, over the
last 20 years of that -- period.

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MS. HANCOCK: That should say Bar 20 there or the dairy farms of the CPHA?

MR. SHEHADEY: CPHA dairy farms would receive quota premiums. Yeah, you should add dairy farms, I guess, just to clarify it.

JUDGE CLIFTON: All right. Ms. Frisius, do you see where he is? All right. So we're inserting, right after CPHA we're inserting "dairy farms" and would you read that sentence again, Mr. Shehadey?

MR. SHEHADEY: Yes, thank you. That's the start of a sentence, so: CPHA dairy farms would receive quota premium prices for its Class 1 milk (Class 1). Over the last 20 years, the difference between the Class 1 price and the quota price has averaged $1.14 a hundredweight. That's in that Exhibit D I think it is, the one we were just looking at. By converting the exempt quota to regular quota, the California Producer Handler Association would then be entitled to transportation allowances, to which they are currently not entitled. In effect, the CPHA farms would lose a significant value that they obtained through investment and organizational structure preservation in return for near zero benefit to the pool. There is no financial explanation for eliminating exempt quota, there is only a financial justification to preserve exempt quota for its holders who have invested millions in obtaining and preserving those assets.
MS. HANCOCK: I think we have one more "dairy farms" that needed to be inserted in the middle there, "by converting the exempt quota to regular quota, the CPHA dairy farms," do you agree?

MR. SHEHADEY: By converting the exempt quota to regular quota, the CPHA dairy farm would then be entitled to transportation allowances.

JUDGE CLIFTON: Do you want us to insert dairy farms there, Mr. Shehadey?

MR. SHEHADEY: Yes, please.

JUDGE CLIFTON: All right. Ms. Frisius? Thank you.

MR. SHEHADEY: For clarification.

JUDGE CLIFTON: All right.

MR. SHEHADEY: Okay.

CPHA Proposal

The CPHA Proposal Number 3 seeks to supplement the Cooperatives' Proposal Number 1 by preserving the treatment for exempt quota as part of a California Federal Milk Marketing Order that attempts to preserve the quota system "intact."

CPHA proposes to provide for an express definition of exempt quota in Section 1051.17 by ensuring the value and calculations contained in the California Food and Ag Code Sections 62708, 62708.1, 62708.5, and 62722 are preserved. CPHA then proposes to modify the Cooperatives' proposal in Section 1051.60 to allow for a deduction of exempt quota
volumes prior to making any pool calculation payments for quota
premium payments. CPHA believes that making these changes,
along with any other changes that USDA deems necessary to
effect preservation of exempt quota, will preserve the exempt
quota along with the regular quota, for a collective
preservation of the quota value and the California quota
system.

Based on my discussions with representatives of the
Cooperatives' proposal, we believe the Cooperatives will not
oppose preservation of the exempt quota along with preservation
of the quota system.

Conclusion

In conclusion, any California Federal Milk Marketing
Order that recognizes a quota system must also recognize the
California quota system as a whole, including exempt quota for
the State's exempt quota holders.

Exempt quota has been part of the Gonsalves Milk
Pooling Act from the start and must be part of any quota system
going forward. All of the justifications for preserving
regular quota equally apply to preserving exempt quota as well.
The exempt quota is critical for the last independent
family-owned producer-handlers that remain in the California
dairy industry. It's not only family-owned, but also
family-invested -- and I should add family-run.

Thank you for your time and attention and consideration
of this testimony given.

JUDGE CLIFTON: I think we should add family-run. Is that true of all four of the family farms?

MR. SHEHADY: Well, there's family involvement in all four of them.

MS. HANCOCK: It's required, isn't it?

MR. SHEHADY: Ownership is a requirement, but in this case, they are all involved in the business at one point or other.

MS. HANCOCK: Where would you like to insert that?

MR. SHEHADY: Right after family-invested it should say, not only family-owned, but also family-invested and family-run.

JUDGE CLIFTON: Ms. Frisius?

MS. FRISIUS: Yep.

JUDGE CLIFTON: Good. Thank you. All right. Done.

MS. HANCOCK: Your Honor, I would move for the admission of Exhibits 152 and 153.

JUDGE CLIFTON: You had one more sentence, Mr. Shehadey.

MS. HANCOCK: I thought he read it.

JUDGE CLIFTON: Oh, you already read that before we went back?

MR. SHEHADY: Thank you for your time and attention and consideration of this testimony given.

JUDGE CLIFTON: Very good.

MR. SHEHADY: Thank you.
JUDGE CLIFTON: All right. I have a whole different viewpoint. Why did they call it "exempt"? It caused me much consternation.

MR. SHEHADLEY: I think it is because you actually take those sales and equivalent sales of a quota, and they call it exempt quota, but they take that sales out of the pool calculation, and the rest of it you pay into the pool for your Class 1, or 2, or 3, or 4 sales. But the exemption, you get to pay your own farm for your Class 1 sales. So if we had a hundred pounds of Class 1 sales, and let's say 20 of those pounds were exempt to our own farm, then we would pay the farm Class 1 for the 20 pounds, and we would pay into the pool for the other 80 pounds, which our processing plant is 95 percent Class 1, so that other 80 pounds would be 95 percent Class 1.

JUDGE CLIFTON: So you don't contribute to the pool for your own dairy farms' production?

MR. SHEHADLEY: Exempt.

JUDGE CLIFTON: The exempt portion of the production.

MR. SHEHADLEY: Yes, that's correct.

JUDGE CLIFTON: And that's why they call it exempt.

MR. SHEHADLEY: That's correct.

JUDGE CLIFTON: It is exempt from a requirement to the pool?

MR. SHEHADLEY: Yes.

JUDGE CLIFTON: Okay. All right. So could you expand,
Mr. Shehadey, on a footnote that you have? I know we're running out of time, and cross-examination we'll never get finished today, but -- or a different day if not tomorrow. But when you -- when you explain the difference between Option 70 and Option 66 --

MR. SHEHADEY: Yes.

JUDGE CLIFTON: Could you explain to me a little bit about what you are not, that other option?

MR. SHEHADEY: Yeah, Option 66 are producers that are totally exempt, but it is a very small amount, I can't remember the exact amount, but it is very, very small, and they are exempt. They would be similar to the three million pound equivalent in a Federal Order. They stay under that amount. We are --

JUDGE CLIFTON: Did you say 300 million pounds?

MR. SHEHADEY: 3 million pounds. Is it per month? Or I think it is per month.

JUDGE CLIFTON: Right.

MR. SHEHADEY: I'm not that familiar with the Federal Order. But so they are exempt from reporting to the pool, and on a Federal Order I imagine they are exempt if they are under that 3 million pounds of reporting to the pool just have to prove they are under.

JUDGE CLIFTON: They have to report. They have to report.

MR. SHEHADEY: Do they?
JUDGE CLIFTON: Yeah. Okay.

MR. SHEHADEY: But the Option 70 is ourselves, and we are over that minimum, so that's why our quota is called exempt.

JUDGE CLIFTON: Over what minimum?

MR. SHEHADEY: We're over the minimum of the 66, Option 66. We're Option 70, so we fall under a different category.

JUDGE CLIFTON: Do you know what the minimum is that allows you to remain Option 66?

MR. SHEHADEY: No, I'm not sure what it is. It's very small though. Very small.

JUDGE CLIFTON: All right. So, Ms. Hancock, you move the admission of both these exhibits?

MS. HANCOCK: I do, your Honor.

JUDGE CLIFTON: All right. Is there anyone who wishes to question Mr. Shehadey before determining you have objections with regard to Exhibit 152 or 153? No one. Is there any objection to the admission into evidence of Exhibit 152? There is none. Exhibit 152 is admitted.

(Thereafter, Exhibit 152, was received into evidence.)

JUDGE CLIFTON: Is there any objection to the admission into evidence of 153? There is none. Exhibit 153 is admitted into evidence.

(Thereafter, Exhibit 153, was received into evidence.)
JUDGE CLIFTON: All right. Let's look at what time it is. It is eight minutes to 5:00. I just think starting cross would be foolish. Does everyone agree with me?

MS. HANCOCK: I have a little direct first, your Honor, so --

JUDGE CLIFTON: Okay.

MS. HANCOCK: -- I really do agree.

JUDGE CLIFTON: Very good. Ms. Hancock, you may resume.

MS. HANCOCK: Do you want me to continue now or do you want?

JUDGE CLIFTON: Yes.

BY MS. HANCOCK:

Q. Okay. Mr. Shehadey, you prepared your testimony several days ago; is that right?

A. Yes.

Q. Okay. And since then we have had some additional testimony here that you have been present for portions of it; is that right?

A. Yes, some of it.

Q. Okay. And we had Dean Foods present testimony. Were you here that day?

A. Yes, I was.

Q. Okay. And I think they described, Mr. Williams -- are you familiar with Mr. Williams?

A. Yes.
Q. Do you know him personally?

A. Yes.

Q. And what --

A. I have met him at industry meetings, I don't know him very well.

Q. And what about Mr. Blaufuss?

A. First time, really.

Q. Okay. And they have discussed in their testimony a national account that your entity and another entity, another producer-handler entity won against them in both 2012 and 2015. Do you recall that testimony?

A. Yes.

Q. And the national account, as your understanding is the same account for both those bids?

A. Yes.

Q. Okay. And without naming it, are you familiar with what national account is?

A. Yes, I am.

Q. Can you tell me what your recollection, what your recollection is about that bid process, and how you were able to win that bid?

A. Well, I think it was more than price because it was a national situation, and a national decision by the people in, that own that group of stores, and California was a small, relatively small percentage of the total stores that were
affected by it.

Q. And did you, in any way, have an opportunity to apply any of the benefits that you receive from exempt quota to help you price that bid to win that national account?

A. No, because the farm had that money, and the farm doesn't sell milk, they sell tanker loads of milk. The process, Producers Dairy acquired a portion of that bid and they didn't have any exempt quota to utilize, it went to the farm.

Q. And Mr. Williams identified several categories of information in his testimony that he believes are the variables that can be used in order to price bids, and made comments about which ones are flexible and which ones are inflexible. Can you talk about those categories as well?

A. Well, there's a lot of numbers that go into the cost of distribution, the cost of processing, your cost per gallon, gallons per man hour in your plant, and your distribution cost. Just how efficient your people are in doing their job. There's a lot of parts that go into that formula and the numbers that you put in on a bid.

He also mentioned that they took $20 million worth of from the producer-handler association, or that we took 20 million from them, and I can think of 10 million they took from us in the last five years, that's just one of the four producer-handlers. So I think if the other producer-handlers
are willing to put a number out there, it will probably be more than the 20 million they got back.

Q. So you are saying that Producers Dairies has lost bids to Dean Foods?

A. I can think of two, one in about 2010 and one in, let's see, what is it, about five years ago, so yeah, about 2010 and about 2013, each one was about five million.

Q. And do you Producers, does Producers Dairy lose bids to other handlers in the market?

A. Yeah, from time to time.

Q. And do you have any kind of price advantage that you are able to apply to those bids based on any profitability from your farms, even if it is not the exact exempt quota, are you able to apply the profits that you earn on your farm to your overall plant operations in making those bids?

A. No, it's a separate business, it's a separate P&L, it's a separate balance sheet, and the money that goes to them stays there. They will reinvest it in the farming side, but not in the processing side.

Q. And you were here for Mr. Rien Doornenbal's testimony, do you remember that?

A. Yes, I was.

Q. And he had asked for some comments about some losses to farms and to Producers. Do you recall that as well?

A. Yes, I do.
Q. And you actually stood up and testified, right?
A. He asked if there were any producers in the audience that would like to comment on the year 2009. I think I got up and supported him in his thoughts, because it's -- it's true.
Q. And tell me about 2009. Did you -- did your farm lose a lot of money that year?
A. Yes, we did.
Q. Do you recall how much you lost?
A. It was a round number, around a thousand dollars a cow.
Q. Okay. And how many cows do you have on the farm?
A. We milk about 7500.
Q. So approximately $7.5 million in 2009 you lost in the farm?
A. Yes, that's correct.
Q. And that's even withholding exempt quota; is that right?
A. Yes.
Q. So how did you cover those losses for the farm?
A. Our family put money in, personal money into the business, into the farming business.
Q. Was your plant profitable that year?
A. 2009? Yeah, I think it was.
Q. Were you able to allocate any of the profits from your plant side to help offset the losses at your farm?
A. No, it's a separate business. You can't allocate
because they were separate businesses. And they -- they did not loan money to the farm, they did not give them any money, there was no money interchanged. Our family owns both businesses, so our family was responsible to take care of the farm when it was in trouble.

Q. How much of the milk that your farm produces is paid as overbase production?

A. About two-thirds.

Q. And the rest is either exempt quota or quota?

A. Yes.

Q. What impact does that two-thirds paid as overbase have on your farm?

A. Well, the impact, it puts us in the same position as a lot of other dairymen out there that don't have much quota. We have about 32 percent quota, which is a third. And with us, it's exempt quota, almost all exempt quota, so we were, are able to pay the Class 1 price as opposed to quota price, that helped us out some, but it was tough. We built a new dairy in 2005, and so we were just building the herd, and so when you build a new dairy with, I'll call them "foreign" cows, cows that you have had to purchase, it takes many years for the genetics to work and for you to be self-sufficient where you are raising your own heifers for your own replacements. You know, the normal time period is about ten years. In fact, it's true, here we are at 2015 and we're just about to where we were
raising all our own replacements.

And in 2009 was only four years after 2005, so our dairy was inefficient on top of having the market crash. And yet, we had a highly modern, efficient operation, it just was not, you know, sorted out yet and perfected.

Q. Thank you. I have no further questions, your Honor.

JUDGE CLIFTON: I'm going to leave it to Mr. English and Mr. Beshore and Ms. Hancock to determine when the cross of this witness should occur. And I don't think we need to decide that right now. And for now, you may step down, Mr. Shehadey.

Thank you so much. We'll need you back, though.

Mr. English, do you have any preview for tomorrow?

MR. ENGLISH: That preview would be the aforementioned discussion that you just said we would have off the record. Obviously, I would love to get my witnesses on, on the other hand, Ms. Hancock and Mr. Shehadey did a nice favor for us and the whole hearing by showing up this afternoon, so if they want to get started in morning and go first thing. Obviously, I would still like to get Rob Blaufuss on tomorrow, and off. If Sue Taylor doesn't, she understands what happened, and I know we have four dairy farmers tomorrow afternoon. But, you know, I, Mr. Shehadey and Ms. Hancock did a favor and if they want to go first tomorrow, I'm not going to object to that, but if they want to delay it, that's fine, too.

MR. BESHORE: Just in terms of the schedule tomorrow, I'm
notified that the four dairy farmers will be here about 3:00 in
the afternoon. So I had asked them to come towards the end of
the day, it might work, and that's when they are expected.

MS. HANCOCK: Nicole Hancock. I think we'll finish up with
Mr. Shehadey in the morning, and then we can move to
Mr. Blaufuss, and I think that still gives us time to have them
off before we get to the producers tomorrow afternoon.

JUDGE CLIFTON: So have we given up all hope of finishing
Ms. Taylor tomorrow?

MR. ENGLISH: No, I never give up hope. You know, the fact
of the matter is, I will be more organized and hopefully
shorter with any cross-examination of Mr. Shehadey tomorrow.
We understand the risk by doing what we did, but our goal will
be move ahead. We did well today, and you know, I would like
to think that we can get Ms. Taylor done tomorrow.

JUDGE CLIFTON: Okay, then.

MR. ENGLISH: And I may be wrong.

JUDGE CLIFTON: Have a good evening. I'll see you all
tomorrow morning at 9:00. We go off record at 5:03.

(Whereupon, the evening recess was taken.)

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IN RE: MILK IN CALIFORNIA

TRANSCRIPT OF PROCEEDINGS - VOLUME XXXIV
November 10, 2015

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