UNITED STATES DEPARTMENT OF AGRICULTURE

BEFORE THE SECRETARY OF AGRICULTURE

In re: [AO] Docket No. 15-0071
Milk in California

VOLUME IX
TRANSCRIPT OF PROCEEDINGS
October 2, 2015

Myra A. Pish, CSR No. 11613
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UNITED STATES DEPARTMENT OF AGRICULTURE

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) Docket No. 15-0071
) Milk in California

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BEFORE U.S. ADMINISTRATIVE LAW JUDGE
  JILL S. CLIFTON

  Friday, October 2, 2015
  9:00 a.m.

  Clovis Veterans Memorial District
  808 4th Street
  Clovis, California 93613

TRANSCRIPT OF PROCEEDINGS

VOLUME 9

Reported by:
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1748
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INDEX - VOLUME 9

WITNESSES IN CHRONOLOGICAL ORDER

CLIFFORD CARMAN:

DIRECT EXAMINATION BY MS. BECKER 1765
CROSS-EXAMINATION BY MR. ENGLISH 1768
CROSS-EXAMINATION BY MR. Beshore 1768

DR. ERIC ERBA:

DIRECT EXAMINATION BY MR. VLAHOS 1770
CROSS-EXAMINATION BY MS. HANCOCK 1839
DIRECT EXAMINATION BY MR. VLAHOS 1853
CROSS-EXAMINATION BY MR. ENGLISH 1855
CROSS-EXAMINATION BY MR. SCHIEK 1888
CROSS-EXAMINATION BY MR. VETNE 1898

---o0o---
<table>
<thead>
<tr>
<th>NO.</th>
<th>DESCRIPTION</th>
<th>I.D.</th>
<th>EVD.</th>
</tr>
</thead>
<tbody>
<tr>
<td>41</td>
<td>USDA LONG TERM PROJECTIONS, FEBRUARY 2015</td>
<td>1765</td>
<td>1766</td>
</tr>
<tr>
<td>42</td>
<td>TESTIMONY OF DR. ERIC ERBA</td>
<td>1772</td>
<td>1835</td>
</tr>
<tr>
<td>43</td>
<td>EXHIBITS OF DR. ERIC ERBA</td>
<td>1772</td>
<td>1835</td>
</tr>
<tr>
<td>44</td>
<td>DCI LETTER TO DAVID IKARI FROM DR. ERIC ERBA -- NOVEMBER 9, 2009</td>
<td>1882</td>
<td>1884</td>
</tr>
<tr>
<td>45</td>
<td>PUBLIC HEARING STATE OF CA DEPARTMENT OF FOOD &amp; AGRICULTURE DAIRY MARKETING BRANCH THURSDAY, JUNE 3, 2015</td>
<td>1886</td>
<td>1888</td>
</tr>
<tr>
<td>46</td>
<td>PUBLIC HEARING STATE OF CA DEPARTMENT OF FOOD &amp; AGRICULTURE DAIRY MARKETING BRANCH THURSDAY, JUNE 30, 2011</td>
<td>1924</td>
<td>1928</td>
</tr>
<tr>
<td>47</td>
<td>DCI LETTER TO MS. CANDACE GATES RE: POST HEARING BRIEF TO JULY 11, 2011</td>
<td>1929</td>
<td>1932</td>
</tr>
</tbody>
</table>

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FRIDAY, OCTOBER 2, 2015 — MORNING SESSION

JUDGE CLIFTON: We're back on record on October 2, 2015, 9:00 a.m. on Friday. My name is Jill Clifton, I'm the United States Administrative Law Judge who is assigned to take in evidence at this milk hearing. This is Day 9 of our hearing.

The docket number as contained in the Hearing Clerk's Office in the United States Department of Agriculture is, in brackets, [AO], and then the docket number is 15-0071. The transcript pages of today will be numbered in sequence to those of yesterday.

I would like to take appearances of those participating, beginning first with other employees of the United States Department of Agriculture. I am one such employee. I would like the others to line up, please, at the podium and please, again, include the spelling of your name.


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

MR. NIERMAN: Good morning, Jason Nierman, N-I-E-R-M-A-N,
Assistant Market Administrator for Federal Order 5, on detail with AMS Dairy Programs.


JUDGE CLIFTON: And now we'll have proponent's teams, beginning with those for Proposal Number 1.


MS. OLIVER THOMPSON: Good morning, Megan Oliver Thompson, Megan is M-E-G- A-N. I'm also with the Law Firm of Hanson Bridgett and co-counsel for the proponents of Proposal Number 1.

MR. SCHAD: Good morning, Dennis Schad, S-C-H-A-D, Land O'Lakes.


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

JUDGE CLIFTON: And Mr. Hollon, your last name, please.

MR. HOLLON: H-O-L-L-O-N.


MR. SCHIEK: Good morning, William Schiek, S-C-H-I-E-K. I'm an Economist with the Dairy Institute of California.


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


MR. VETNE: John Vetne, V-E-T-N-E, representative for Hilmar Cheese.

JUDGE CLIFTON: And now I'd like those who also have been or expect to be participating -- I'm sorry, Ms. Hancock.

JUDGE CLIFTON: Now I'd like those who may not be aligned with a particular proposal, but either have been or will be participating to identify themselves, please.

MR. MILTNER: Good morning, Ryan Miltner, M-I-L-T-N-E-R, counsel for Select Milk Producers, Inc.

JUDGE CLIFTON: And I know of two people testifying, they were identified yesterday. Is there anyone else here who would like to testify today? All right. I see no one identifying himself at this time, but we'll ask again later.

I would like now to address some preliminary matters.

As you know, next week we return to the Liberty Room and we'll have a normal Monday through Friday schedule, except Friday. On Friday we'll stop early Friday. Is the 9th of October 2015. We will go off record no later than 12 noon on October 9th. When we leave the Liberty Room on October 9th, we will not resume the hearing until the 14th of October, at 9:00 in the morning, that's a Wednesday. That week will be a three-day week -- Wednesday, Thursday, Friday, all in the Liberty Room. My other preliminary announcement is with regard to exhibits.

If I have rejected an exhibit, it goes onto the website in the same timely fashion as if I had accepted it. And if I have rejected an exhibit -- I have only done one so far -- I expect that rejection to be temporary, I'm just waiting for some additional foundation so that I understand the document.
I don't have any quarrel with its authenticity, but I find that its relevance will be more clear to all of us if we have some more testimony about it, so that's the reason I rejected it.

Mr. English?

MR. ENGLISH: Chip English. And just for clarity, as we're discussing these kinds of things, your Honor, there is also one exhibit, Number 30, that I never offered, therefore, you didn't have the opportunity to reject it, and so I assume it will be similarly going up since it's sort of shown up. But I -- it doesn't matter to me, I just thought the record could be clear about what's happening to it, and we did not offer it yet because we did not have a witness who recognized it. That was the Chicago economist power point presentation that Mr. Hollon did not recognize.

JUDGE CLIFTON: Let's decide what we think about that. I was thinking that things would go on the website when they have either been accepted or rejected, not when they have been identified, but I'm flexible on that.

MR. ENGLISH: And I'm indifferent. I just didn't want it to be -- I'm fine with not doing that, the only question it seems to me that if you are looking at the website and you see sequentially, and then you see a number 30, and there's -- or you don't see a 30, you will see 29, 31, there might be some mystery for those who aren't attending. But I don't have a few other than that.
JUDGE CLIFTON: But another view that I just thought of, and hadn't thought of before, is that people who can see the transcript and see references to that exhibit, will want to look at it. I would. So I think you are right, I think our best course is to put them all on the website if they have been identified and have been referred to in the transcript. So I'll see what other people think about that.

MR. BESHORE: Marvin Beshore. The only concern I would have would be that the website also reflect whether they have been accepted or rejected or what their status is, so that way when somebody's looking at it they know what's going on.

MR. ENGLISH: I think that's entirely fair and if I could identify, not offer, or whatever -- whatever makes sense, I think that that obviously clarity, I have no disagreement with counsel for cooperatives. Clarity in the record should be there. So listing it shouldn't, somebody shouldn't be misled into thinking it has been admitted, so we need to designate it in some way as not yet offered or something.

MR. VETNE: John Vetne. I agree with all the exhibits that have been identified ought to be on the website. It may be -- it may be difficult, logistically difficult or tedious to indicate for each exhibit what's been offered or accepted. I suggest an easier alternative is simply in the caption of the exhibits, these are the exhibits that have been offered, and some may not have been received, or something like that, so
that the reader knows that just because you see an exhibit, it may or may not have been accepted as in evidence. Thank you.

JUDGE CLIFTON: I don't want to make it more difficult for the posting on the website, so I'm going to leave that part entirely up to AMS and its coordination with the part of USDA that puts these things on the website, however it's most convenient for you is fine. If it ends up most convenient is just the exhibits are there, all 30 of them or whatever, no explanation, that's fine with me. People can see them if they are -- if they are not reading the transcript and don't know the status of them, I don't think any real harm is done. If they get to the point they are writing the briefs, of course, they should find out which ones are in evidence and which ones are not, but by then it could be that they are all in evidence for all I know.

If in coordination with the part of USDA that puts them on the website, you decide you do want to categorize them, then I would say there are three categories; one is accepted, one is rejected, and one is identified. All right.

Now, let's continue on with preliminary matters. And at this time I would recognize someone from USDA to identify all preliminary matters.

MS. MAY: Good morning -- Laurel May.

As always, welcome. It is a beautiful morning out there. I was thinking as I was driving over here that it would
be a great day for harvesting black-eyed peas because you have
a little bit of dew out there, no shatter.

Anyway, as always, if you would like to testify today
and you have time to do so, please notify Meredith, who will
put your name down and make sure that you get a chance to do
that.

If you would like to ask questions of any witness, you
may do so, just approach the microphone and let the Judge know
that you would like to ask questions.

We are broadcasting a live audio feed but it is not
being recorded by us. If you would like to tune into it at
home, it is tinyurl.com/camilkhearing.

The court reporter is recording an official transcript
which will be available approximately two weeks after the end
of each hearing week, and the exhibits, like we were just
mentioning, are numbered in order of presentation. So copies
of those will be available on our website, and there are some
still copies available in the back of the room if there are
some that you have missed.

We do have refreshments in the back that have been
provided, and you are welcome to enjoy those.

Today, as Judge Clifton mentioned, we are going to be
breaking down this room and leaving, so you will need to take
your things home with you. And then we'll be returning to the
Liberty Room on Monday.
At the end of the day yesterday, Mr. Wegner was
testifying. And today, I believe, that USDA would like to
begin with Cliff Carman, who is going to provide a USDA
response to Ms. Taylor's data questions, and then I believe
Dr. Erba is next up for testimony.

JUDGE CLIFTON: Thank you. Are there other preliminary
matters?

MR. ENGLISH: Good morning. Chip English. I guess this is
the end of the week. I would ask, going back to sort of the
awkwardness issue about CDFA, I would ask the Department where,
in this case, the Department of Agriculture of USDA -- where we
are with respect to timing and what may or may not happen with
CDFA data. And again, I understand fully that this is not in
any way, shape, or form, a problem created by, or, and I know
just the opposite, that USDA has done everything it can to
resolve this issue. So this is more of a sort of where are we,
where are we going, because I do think that it really would be
useful to find some way to get the CDFA data in, especially as
we're moving forward with substantive witnesses, so I would
like a report on that.

MR. RICHMOND: Bill Richmond, USDA. Unfortunately, we
aren't able to provide any kind of update at this time.

MR. ENGLISH: I thank you. Again, this is one of those
places where industry -- and this is actually, I think USDA as
well, we're all sort of on the same page of trying to get this
resolved, and I know you are doing everything you can. And thank you.

Again, I think my -- I'm just saying, we're in agreement. We're just trying to figure out where we are. I understand you don't have a report, but it's -- at some point, I think the hearing record is going to get a little messy.

MR. BESHORE: At some point we're going to be at a point of no return with respect to dealing with this and I guess I'm a little concerned about that. But do we expect to have some report maybe like next week from AMS on this further?

MR. RICHMOND: Bill Richmond, USDA. Absolutely. We can -- we'll keep you apprised of any additional information that we obtain.

MR. BESHORE: And I'm not sure where left this, but at one point AMS was going to request that official notice be taken in some fashion if we were unable to have a CDFA witness. Is that still the plan?

MR. RICHMOND: At this point, I don't think we have decided.

MR. BESHORE: Okay.

JUDGE CLIFTON: Mr. Beshore, why is it that AMS Dairy Programs has a better avenue to get a CDFA witness than you?

MR. BESHORE: It's our understanding that there was, and is, I assume, an agreement of some nature between the agencies, we haven't seen it, but, in fact, I know, it's been stated
publicly that there was an agreement of cooperation of some
nature between USDA and AMS and CDFA with respect to this
proceeding, so I think that's the answer to your question.
Which is not to say that we have not, that is, the,
Mr. English's clients and my clients, made extensive efforts to
communicate with, and see if we could appeal to, and prevail
upon CDFA to be a non-partisan participant in the process.

JUDGE CLIFTON: And is that still a possibility?

MR. BESHORE: I'm looking to the persons who personally
made the appeal and getting shrugs. We -- it is still a
possibility of some sort, I think, but can't say any more than
that.

JUDGE CLIFTON: Okay. I can appreciate, Mr. Beshore, you
not wanting to add any extra work if CDFA is already working
with AMS, of course you would not duplicate their request, I do
understand that.

MS. HANCOCK: Nicole Hancock. We, on behalf of the
Producer Handlers Association, made a formal request to CDFA
for certain data, and the letter response that we received back
is that they wouldn't be providing any response to the parties,
but they would respond to the USDA.

So they have told us to go through the USDA. I think
after that point in time, maybe that USDA has not been
successful in obtaining the same information. But nonetheless,
CDFA has directed us to go through the USDA to obtain the data.
MR. RICHMOND: Bill Richmond. I wish I could provide additional clarification and explanation at this point, but I'm just not able to.

MR. ENGLISH: And, believe me, your Honor, Mr. Richmond, if I may -- look, we know that. We get that. And we understand it. And we're going to just -- we're not getting any farther today, I'm not going to labor it, and we have got to get some resolution of this, and I don't know how to do that. But, you know, I think that as you have heard, everybody on our side -- and I realize that you as well on your side of the aisle -- speaking for Mr. Carman, that when he used that term yesterday for the Judge -- but I don't want to belabor it any longer, I just wanted to raise it up and try to get resolution.

JUDGE CLIFTON: That phrase "point of no return" is frightening.

MR. BESHORE: Well, all I meant by that is at some point in the proceeding we just have to decide how we're going to handle CDFA data. And if there is no possibility of a CDFA witness, we're going to have to say, okay, here are the data compilations, publications of CDFA, and they were requesting that official notice be taken of them, and they be identified fully and completely and made part of the hearing record. That's sort of what I had in mind about a point of no return.

MR. ENGLISH: And Chip English. And I agree, and I think, again, we know what the ideal is. The ideal is to get a CDFA
witness. But if we're getting to that point where that's not
going to happen, what we need, I think, is an exhibit, an
exhibit number such as the next exhibit is 41 -- well, I maybe
I'm talking to somebody else -- but an exhibit number with all
of those attached so that then for testimony purposes, people
with can do as we have with Exhibit 9 and say, will you look at
Table 5 of Exhibit 41, and that's going to make the testimony
of Proponents 1 and Proponents 2, and people who are opposed,
much easier to understand going through the transcript, rather
than say, I would like to take, I want to look at the official
noticed document labeled X. That's -- that ultimately is sort
of, I think, where we're we are.

But that doesn't -- but that doesn't change the fact
that the ideal situation is to have an, and I absolutely agree
with Mr. Beshore, a neutral witness from CDFA. We're not
looking for CDFA to show up and give any other testimony.

MR. BESHORE: I agree, and I agree with Mr. English's
comments.

JUDGE CLIFTON: Mr. Richmond?

MR. RICHMOND: Bill Richmond. I understand and appreciate
gentlemen's request. Can we plan to perhaps revisit the issue
early next week, and if we have any kind of update we will be
more than happy to provide one?

JUDGE CLIFTON: Very good. All right. Are there any other
preliminary matters? I see none.
We have a new document, and I assume that the statistics that are about to be presented by Carman will be Exhibit 41; is that correct?

MS. FRISIUS: Correct.

JUDGE CLIFTON: That will be Exhibit 41. I would ask that they be distributed now.

(Thereafter, Exhibit Number 41 was marked for identification.)

JUDGE CLIFTON: Is there anyone who wants a copy of Exhibit 41 who did not get one? All right. Is everyone equipped with 41? Good.

Mr. Carman, you remain sworn. Would you again, state and spell your name?

MR. CARMAN: Clifford Carman, C-A-R-M-A-N.

JUDGE CLIFTON: Who, for Office of General Counsel, will proceed?

MS. BECKER: Lauren Becker for USDA.

JUDGE CLIFTON: Thank you. You may proceed.

DIRECT EXAMINATION

BY MS. BECKER:

Q. Good morning, Mr. Carman.

A. Good morning.

Q. Can you tell us why you are taking the stand this morning?

A. We were requested to provide some additional
information about the preliminary impact analysis that was done for the proposals in this proceeding.

Q. Okay. And will you summarize for us what the first question was that you will be responding to?

A. Those are requests, as I understand it, for the baseline numbers that were used in the analysis for wholesale product prices.

Q. Okay. Your Honor, I would like to introduce what's been marked as Exhibit 41.

JUDGE CLIFTON: Does anyone want to question the witness before determining whether you have any objection? No one does. Is there any objection to the admission into evidence of Exhibit 41? There is none. Exhibit 41 is admitted into evidence.

(Thereafter, Exhibit Number 41 was received into evidence.)

BY MS. BECKER:

Q. Mr. Carman, will you describe what that table shows?

A. This sheet is Table 35 taken from, it's published on page 84 of USDA's Long-Term Projections published in February of 2015. The particular pieces of information that were asked for are the prices on the bottom of the table. They lay out the cheese, butter, nonfat dry milk, and dry whey prices that the model solves for in terms of equilibrium prices for the years indicated, except for 2013, which is an actual number,
the model solving 2014 through 2024.

Q. Can you go ahead and summarize for us, please, the second question that you will be responding to?

A. My understanding was that Ms. Taylor was trying to verify the numbers in our baseline relative to the results which she was seeing for different proposals. I would point out that reviewing the model for the regional part of the model for California, we added one cent to the butter price, and one cent to the cheese price in these formulas for the baseline in California.

If you will remember, California has a 26 to the 25th calculation on the CME butter price. Our prices are reported to be what we consider the National Dairy Product Mandatory Reporting Prices, and a historical review from 2003 through 2014, shows a price difference between those two series of approximately one cent.

And in the case of cheese, we also added one cent. California uses a block cheese price at the CME, we use a weighted-average of butter -- pardon me -- of blocks and barrels reported to us in that mandatory reporting program.

And again, that's approximately a one-cent difference. We did not make any adjustments in nonfat dry milk and dry whey.

Q. Okay. Mr. Carman, are you available for further questions?

A. Yes. I intend to be at all sessions of the hearing.
JUDGE CLIFTON: All right. Good. Who would like to begin questions of Mr. Carman with regard to what we have got so far today?

CROSS-EXAMINATION

BY MR. ENGLISH:

Q. Chip English. First, thank you very much.

Second, we don't have questions at this time, what we need to do, of course, now, is go run those numbers. It may raise questions -- it may or may not raise questions in the future. But, you know, for now, that answers the questions that Ms. Taylor asked. Thank you.

CROSS-EXAMINATION

BY MR. BESHORE:

Q. Marvin Beshore. Good morning, Mr. Carman.

A. Good morning.

Q. I need you to take me through the one penny difference in prices. Tell me what -- what prices, what product prices, the penny was added to or subtracted from and why that was done.

A. We compared the California butter price that they use, which is the CME over the 26 to the 25th of each month, compared to the reported prices that we are estimating, which are the National Dairy Product Prices Mandatory Reporting.

Q. Can I just stop you right there. You compared the CDFA calculated CME price?
A. For the month.

Q. With or without the adjuster -- FOB adjuster?

A. Without.

Q. Okay. And you found -- then -- okay. So continue.

A. We found approximately a one cent difference, i.e. the prices that we use are one cent lower than what the CME adjust price for that time period is. I will admit that we are using weighted average prices of exchanges, while the CME is a spot price, there's no weighting to that over that time period, but we found the one cent difference, so we're trying to duplicate the California current pricing structure in creating a baseline. So we felt we needed to adjust that price by one cent.

Q. Okay. And the adjustments were made to -- how many commodity prices were adjusted one cent, and which ones?

A. The butter price and the cheese price.

Q. Okay. Both of them one cent?

A. Yes.

Q. Now, I think you said your prices were weighted average exchanges. By that, do I understand you to mean by that they were weighted average of actual transaction prices?

A. Yes.

Q. Thank you. Thank you very much, Mr. Carman.

JUDGE CLIFTON: Are there other questions for Mr. Carman now with regard to the testimony so far this morning? All
right. I expect to see you again Mr. Carman. You may step down.

MR. CARMAN: I hope not.

JUDGE CLIFTON: Is there anything preliminary to Dr. Erba taking the stand? There is not. Dr. Erba, you may come forward.

MR. VLAHOS: John Vlahos on behalf of the cooperative proponents, Proposal Number 1.

JUDGE CLIFTON: I'll swear him in. Did you want to distribute any documents?

MR. VLAHOS: Yes. I'm going to. I was going to do the preliminary first and then distribute the documents, if that's okay.

JUDGE CLIFTON: All right. That's certainly fine with me. I'll swear you in, Dr. Erba. Would you raise your right hand? Do you solemnly swear or affirm under penalty of perjury that the evidence you will present will be the truth?

DR. ERBA: I do.

JUDGE CLIFTON: Please state and spell your name.

DR. ERBA: Eric Erba, E-R-I-C, E-R-B-A.

JUDGE CLIFTON: Mr. Vlahos, you may proceed.

DIRECT-EXAMINATION

BY MR. VLAHOS:

Q. Dr. Erba, by whom are you employed?

A. California Dairies, Inc.
Q. And what is your position with California Dairies, Inc.?
A. Senior Vice President and Chief Strategy Officer.

Q. What is your business address?

Q. And you're appearing today to support the Proposal Number 1 put forward by the cooperatives?
A. That is correct.

JUDGE CLIFTON: Let me stop you there. Until we finish distributing the documents, let's stop questioning so that people can pay attention to the testimony.

Now, right now I won't deal with marking them or the like, but I just want to see if there's anyone who did not receive two different documents who wants them. Two different documents. One is marked Cooperatives' Exhibit 4 down at the bottom, and then the other has exhibits. All right.

I would like to go back to Dr. Erba's testimony. So he had mentioned his work with California Dairies, and I would like you to go back to just after that, if you will,

Mr. Vlahos.

MR. VLAHOS: I'm not sure what -- just after that?

JUDGE CLIFTON: Yes, please.

MR. VLAHOS: I think I asked for his business address?

JUDGE CLIFTON: Yes, would you start there?
BY MR. VLAHOS:

Q. And you did give your business address?

A. Yes, we are still at 2000 North Plaza Drive, P-L-A-Z-A in Visalia, California, V-I-S-A-L-I-A.

Q. Your Honor, may we have the document that's been distributed and called Cooperatives' Exhibit number 4, marked as the next in order for identification? I believe it is 42?

JUDGE CLIFTON: Ms. Frisius, would this be Exhibit 42, the one that says Cooperatives' Exhibit 4 down at the bottom?

MS. FRISIUS: It would be.

JUDGE CLIFTON: All right. I'd ask everyone to mark that as Exhibit 42. 42.

(Thereafter, Exhibit Number 42 was marked for identification.)

MR. VLAHOS: And we would like to have marked for identification the next document, the exhibits of Dr. Erba as Exhibit 43 for identification.

JUDGE CLIFTON: And I have marked mine as Exhibit 43, exhibits of Dr. Eric Erba.

(Thereafter, Exhibit Number 43 was marked for identification.)

MR. VLAHOS: Your Honor, as has happened sometimes in these proceedings before, there has been an inadvertent error in that some of the sections referred to that's contained in the Cooperatives' proposal under the Series 1050 or 1050. Some
other sub number, should have been 1051. 1051. And we will
ask that in every instance in which in Exhibit number 42 that
has occurred, that we be allowed to interline so that it reads
1051. whatever subsection it is. I have already alerted
Ms. Frisius to that and told her that we would provide her with
a document that makes those changes, and interlineated.

JUDGE CLIFTON: So you don't want to go through and
identify them now page by page?

MR. VLAHOS: Well, I can, your Honor, and I hope I haven't
missed any. And if I have, I'll rectify it later. But the
first one that I have is on page 22, it is the second line
under the heading Continuation of Quota Program Under a
CA-FMMO.

JUDGE CLIFTON: Wait, I expected you to be more specific.
You want us to strike the numbers after the section symbol,
that are 1050.17(a), and instead, write 1051.17(a)?

MR. VLAHOS: Exactly.

JUDGE CLIFTON: Okay.

MR. VLAHOS: Next we would go to page 26.

DR. ERBA: You skipped page 25.

MR. VLAHOS: Pardon?

DR. ERBA: Page 25 also has some issues.

MR. VLAHOS: Oh, I have it marked, too, somewhere. Yes.

DR. ERBA: First paragraph off the bottom, starting with, "As a practical matter."
MR. VLAHOS: Thank you, Dr. Erba. On page 25, your Honor, the paragraph that begins near the bottom of the page, "As a practical matter," in that sentence, the reference to Section 1050.61 should be stricken and should be changed to Section 1051.61.

And the next line, the number there, Section 1050.62 should be stricken and changed to Section 1051.62.

Then on page 26, the third line from the top of the page, the reference here in words, Section 1050.30, the numbers should be stricken, and inserted instead, 1051.30.

Two lines below that, the section number, Section 1050.31, that number should be stricken and changed to Section 1051.31.

Then at the bottom of the page, paragraph, the last paragraph which begins with the section number Section 1050.61, that should be stricken and changed to 1051.61.

Three lines down in the paren's there's a section reference to Section 1050.60, that should be stricken and changed to Section 1051.60.

Two lines below that, in the sentence that begins "As specified," the section that appears there, Section 1050.62, should be stricken, and in its place there should be inserted Section 1051.62.

Turning to page 27, in the first full paragraph, four lines down, the reference to Section 1050.71, should be
stricken, and substituted in its stead, Section 1051.71.

Three lines below that, there appears Section 1050.72, that should be stricken, and in its place, Section 1051.72 should be substituted.

I believe that's all, your Honor. And if it turns out that I have missed one, I will supplement what I asked for on the directions.

JUDGE CLIFTON: Excellent. That's very helpful. I'm glad you did it on record so it is perfectly clear, and that way the record copy was created during the proceeding. So if you find anymore, we'll address them on the record.

MR. VLAHOS: Fine, your Honor.

JUDGE CLIFTON: Thank you so much.

BY MR. VLAHOS:

Q. Dr. Erba, were you requested to prepare testimony reflecting the California quota system and the interface between that system and a California Federal Milk Marketing Order, should such an order be adopted?

A. Yes, I was.

Q. Okay. Let's start out with some preliminaries. Would you detail for us your educational background?

A. Sure. I have a Bachelor's of Science degree in Animal Science from University of California, Davis, and that was received in 1988. I have a Master's degree in Animal Science from UC Davis, University of California, Davis, received in
1990. And then I have a Ph.D. in Agricultural Economics from Cornell University, received in 1997.

Q. Could you also detail for us your professional employment background?

A. Certainly. I started with the California Department of Food and Agriculture in 1997, just after I finished up at Cornell. Employed by the Dairy Marketing Branch as an Agriculture Economist and, in fact, Dairy Economist. And I worked in that position for eight years. I spent two years as the Assistant Director at the Division of Animal Health, also at the Department of Food and Agriculture -- California Department of Food and Agriculture. Then I was employed by California Dairies starting in September of 2006.

Q. Could you detail for us your responsibilities and duties during your term at the California Department of Food and Agriculture?

A. As I said, I was a Dairy Economist with Department of Food and Agriculture, and so I worked with the, within the Dairy Marketing Branch to assist the Division Director, as well as the Secretary, to implement and administrate the dairy marketing, dairy marketing in California.

Q. And what are your duties and responsibilities with your current employer?

A. I'm a part of one of the managing team for the cooperative, the executive team, and assist with the management
of the cooperative, as well as some of the strategic thinking plans that are being developed for California dairies. I oversee the field staff and oversee the Milk Quality Program. I do, on occasion, quantitative analysis and policy development and analysis for, not only dairy, but the cooperative itself. And I have also been a bit of a historian.

Q. Thank you very much, Dr. Erba. You indicated in answer to my question, that you have prepared testimony. Is that Exhibit 42?

A. That is Exhibit 42.

Q. Now, Dr. Erba, you have been here enough to realize that both of us earn point if we speak slowly and clearly and particularly when you are reading, so with that -- and I'll probably violate that, too, by the way, especially if you can, adhere to that admonition.

With that, your Honor, I would request permission for Dr. Erba to deliver his prepared testimony.

JUDGE CLIFTON: Thank you, Mr. Vlahos. Dr. Erba, you may do so.

DR. ERBA: Thank you. I was alarmed to hear you describe Mr. Wegner as being so articulate, because I know he's a lot better than I am. I'm going to try to follow suit, but don't hold me to his standard, if you would, please.

MR. VLHOS: Excuse me one second. For the benefit of court reporter, when you are reading your testimony, if there's
a heading, read the heading and indicate that it is a heading, and when there are things in parentheses, so indicate that they are in parentheses.

DR. ERBA: I will try.

Introduction

Good morning. My name is Eric Erba and I hold the position of Senior Vice President and Chief Strategy Officer for California Dairies, Inc., whom I'm representing here today. I have worked for California Dairies since September 2006. Prior to that, I worked for the California Department of Food and Agriculture for ten years, with eight of the ten years employed as a Dairy Economist for the Dairy Marketing Branch. California Dairies is a full-service milk processing cooperative owned by 390 producer-members located throughout California, and collectively producing 18 billion pounds of milk per year, or 45 percent of the milk produced in California. Our producer members have invested over five hundred million in large processing plants at six locations.

JUDGE CLIFTON: Let me stop you. That's five hundred million what?

DR. ERBA: Dollars, sorry.

JUDGE CLIFTON: Thank you.

DR. ERBA: Should I start that sentence again?

JUDGE CLIFTON: Please.

DR. ERBA: Our producer-members have invested over $500
million in large processing plants at six locations, which will produce about 385 million pounds of butter and 785 million pounds of powdered milk products in 2015.

I will be describing the history, structure, and importance of the California quota program, and how we propose that the quota program be incorporated into the California Federal Order as specified in the proposal submitted by the three California cooperatives.

Introduction to the California Quota Program

California maintains a two-tiered milk pricing program for producers where ownership of a financial instrument (also recognized as an asset) termed "quota" entitles a producer to an incrementally higher milk price that is paid on the amount of milk covered by quota ownership. Conversely, milk production that is not covered by quota is subject to a lower regulated price -- milk price -- this is termed the "overbase" price. The concept of a tiered pricing system was developed in the late 1960's as California State Milk Marketing Order -- as the California State Milk Marketing Order -- was attempting to address a producer milk price equity issue.

In an economic sense, quota fits the description -- sorry -- quota fits the definition of an economic rent. That is, it represents an excess payment above that required to induce or provide production, or a payment for the services of an economic resource which is not necessary as an incentive for
its production. Furthermore, quota is an asset that was
created by a regulatory agency with the intent of constructing
an official privilege over national opportunities, a secondary
descriptor of economic rents.

Quota payments to producers are an important component
of revenues to many California dairy operators. In fact,
paramount to any consideration of a California Federal Milk
Marketing Order, (FMMO) was the assurance that the quota
program would not in any way be diminished or affected.
Congress recognized this, and in the 2014 Farm Bill language
dealing with the promulgation of an FMMO in California,
directed that the marketing order provisions allow for the
continuation of the quota program in California.

The 2014 Farm Bill (Section 1410(d)) references the
1996 Farm Bill (Section 143(2)),

"Upon the petition and approval of California
dairy producers in the manner provided in the
Section 8c of Agricultural Adjustment Act
(7U.S.C.608c), reenacted with the amendments by
the Agricultural Marketing Agreement Act of 1937.
The Secretary shall designate the State of
California as a separate Federal Milk Marketing
Order. The order covering California shall have
the right to reblend and distribute order receipts
to recognize quota value."
Quota has an extensive history and has had a significant role in the California industry for over 45 years, and was integral part of the Milk Pooling Plan when it was introduced in 1969. The program has been modified since its creation, but the foundation of the program has remained intact since its introduction. Under the Pooling Plan, producers were no longer paid directly in accordance with a class utilization of the handler that received the producers milk. Instead, producers were paid on the basis of his or her allocated quota base and overbase at prices which reflected --

JUDGE CLIFTON: Let me ask you to read that sentence again, if you will.

DR. ERBA: I inserted a word that's not typed.

JUDGE CLIFTON: True. Now, maybe that's on purpose, maybe there is base and overbase, but if not, what -- you just tell me what is true here.

DR. ERBA: What I said, not what I wrote is correct.

JUDGE CLIFTON: Okay. This is important.

DR. ERBA: I will read it again for you.

JUDGE CLIFTON: Yeah, and you may want to explain it, too.

DR. ERBA: I do explain it later on.

JUDGE CLIFTON: Okay. Good. Thank you.

DR. ERBA: Instead, producers were paid on the basis of his or her allocated quota, base, and overbase at prices which reflect the poolwide utilization of all classes.
Is that okay?

JUDGE CLIFTON: Perfect.

DR. ERBA: Okay. Great.

Pool quota was established for each producer by milk fat and solids-not-fat on an average daily based on historic production at Class 1 usage. Any production in excess of a signed quota constituted overbase production. Periodically, the California Department of Food and Agriculture (CDFA) has issued additional quota to producers, but none since 1992. CDFA has issued about 2.2 million pounds of quota solids not fat on a daily basis (about 66.2 million pounds of solids not fat monthly).

Quota enjoys a special status in that its existence is protected by state law. The importance of maintaining stability with a quota program was recognized by the California State legislature. In fact, Code Section 62712 of the Food and Agricultural Code, specifically states that all pool quota must be recognized and shall not be diminished in any way as long as the Milk Pooling plan is in effect. Thus, quota cannot be eliminated by eliminating -- can only be eliminated by eliminating the entire Milk Pooling program.

The proposal submitted by California Dairies, Inc. Dairies Farmers of America, and Land O'Lakes ("the Cooperatives") recognizes the history of quota, the financial investment made by dairy producers in quota, and the federal
directive to recognize the value of California quota. Thus, the Cooperatives propose the quota program be left intact without significant modifications and continue to be administered by CDFA through a Memorandum of Understanding with the United States Department of Agriculture.

Before Quota – An overview of the California Dairy Industry

The milk marketing laws passed in the 1930's, especially the Young Act of 1935, helped to regulate the minimum price, the minimum price paid for milk by processors to producers by establishing classified milk prices. Class 1 utilization, which was used for beverage milks, beverage products, usually commanded the highest price. Progressively lower prices applied to milk devoted to the manufacturing classes of milk.

However, establishing minimum prices did not address the concerns of equitable prices among producers or composition of similar milk. Plants processed an array of products, and consequently, class utilization among plants varied. In addition, processing plants were well on their way to becoming "specialized" by processing fewer products. Some plants processed 100 percent of the milk received as Class 1 products, but other plants tended to specialize in manufactured products, producing little or no milk as Class 1 products.

JUDGE CLIFTON: Let me interject here, for court reporter, all of these references to Class 1 thus far have an Arabic 1
because we're talking about California's Class 1. And you may continue, Dr. Erba.

DR. ERBA: Should I say that every time I see an Arabic 1, say Arabic 1?

JUDGE CLIFTON: I think because every time you have seen it, said it so far, it's always been Arabic. Let's just assume that it will be Arabic unless you alert us that there's a change, that you are taking about a Roman numeral instead.

DR. ERBA: Okay. I can do that.

JUDGE CLIFTON: Thank you.

DR. ERBA: Where would you like me to restart?

JUDGE CLIFTON: No, no, you are good. Oh, where?

DR. ERBA: Where?

JUDGE CLIFTON: Not would you but -- where would you. Yes. Start, please, with the phrase "these characterizations."

DR. ERBA: Yes.

These characterizations represented the extremes, and it was more typical to find plants with moderate Class 1 utilizations. Nonetheless, a producer shipping to a plant with all Class 1 utilization fared well financially, while neighboring producers -- while a neighboring producer selling milk of like quota to a plant with low Class 1 utilization, typically received a considerably lower price.

In the late 1950's and early 1960's, disparate prices among producers in the same region were a source of frustration
and led to destructive marketing practices. Clearly, a producer's financial welfare was impacted by his or her ability to secure a contract with a handler with high Class 1 utilization. This placed producers in a weak position to bargain with handlers, and many would agree to excessive haul charges or make other concessions to obtain or retain the coveted sales to Class 1 handlers. The lack of long-term commitments between producers, between producer and handler, added to the instability of the milk market. Most contracts were subject to cancellation by either party upon 30-days' notice.

It was difficult for producers to obtain new contracts, especially with plants that maintained high Class 1 utilization year round. Not surprisingly, the loss of a contract to an individual producer was a severe economic blow. Producers often accepted contracts with handlers that gave the handler the permission to divert milk shipments to manufacturing facilities. Besides receiving a significantly lower milk price, producers were also expected to pay for the additional cost of hauling their milk to the designated plant. An alternative was to locate another fluid milk plant that was accepting milk, but this did not eliminate the high cost of shipping the milk from the dairy to a distant plant. The uncertainty of obtaining or continuing favorable contracts restricted many producers' future planning horizon and
financing capability.

During the early and mid-1960's, several events combined to place even more pressure on producers. Some dairy processors began to alter the traditional framework of milk production, of the milk production sector by acquiring herds and supplying their own processing facilities with milk, thereby reducing the number and volume of Class 1 contracts available to existing producers.

Producers realized the necessity of developing a system that would bring relief to their problems and provide a more equitable allocation of the revenues generated from Class 1 milk sales. Producers and producer organizations concluded that such a system would have -- could be brought only through legislation and introduced a number of Milk Pooling bills in the California Legislature. These early efforts to establish a revenue distribution program were not successful because the producer community could not agree on the basic concepts of the program.

In 1967, the Legislature passed the Gonsalves Milk Pooling Act and it was signed by the governor --

MR. VLAHOS: Excuse me, Dr. Erba, for the reporter, would you spell that Gonsalves?

DR. ERBA: Oh, I thought you were going to have me spell milk.

MR. VLAHOS: I could do that.
DR. ERBA: I'm just trying to add a little levity here, Mr. Vlahos. Gonsalves, G-O-N-S-A-L-V-E-S.

MR. VLAHOS: Thank you.

DR. ERBA: I'm going to start that sentence again.

In 1967, the Legislature passed the Gonsalves Milk Pooling Act, and it was signed by the Governor into law on November 8th, 1967. This act required the California State Secretary of Agriculture to formulate aPooling Plan via the public hearing process. The Pooling Plan became active in November of 1968, after an affirmative vote of eligible milk producers. Developing mechanics of a pool price calculation delayed implementation until July 1969. The pool area covers the entire state.

Production Base and Pool Quota

During the preliminary stages of formulating a plan, basic milk production data were gathered to establish two benchmarks for each eligible producer -- a production base and pool quota. A producer's history was based on his or her milk production ("production base") and a producer's Class 1 usage during July 1966 through December 1966 or the 1967 calendar year became the benchmark to establish a producer's quota.

Production base and pool quota were established for each producer by milk fat and solids not fat on average daily basis. Pool quota was established at 110 percent of Class 1 usage, and the amount by which production base exceeded pool quota was
designated "base".

BY MR. VLAHOS:

Q. Excuse me, Dr. Erba, just one little interruption there. When you said that the pool quota was established at 110 percent of Class 1 usage, am I correct that the Class 1 usage you are referring to was the base period in which the producer opted for, either the July 1996 through December 1966 or the 1967 calendar year?

A. You said July 1996, and that would not be correct.

Q. If I did say that, I meant 1966.

A. Yes, 1966. Yes, you are right. You are correct.

Q. Please proceed.

A. Okay.

With the implementation of the Pooling Plan, producers were no longer paid directly in accordance with class utilization of the contracting handler. Instead, producers were paid on the basis of their allocated quota, base, and overbase at prices which reflect the poolwide utilization of all classes. The monthly quota and base quantities were computed for each producer to the extent he or she produced these quantities. The maximum monthly quantity of quota was determined by the current quota allocation. The maximum monthly quantity of base was the difference between production base and quota. Any production in excess of a total of these two figures, constituted the overbase production.
Pool Value, Pool Prices, and Pool Obligations

Under the California regulatory structure, each handler submits to the Pooling Branch a monthly report detailing the amounts of milk purchased from producers and other handlers, and the amounts used in their various classes, which is then used to determine each handler's pool obligation. The total value of each class is determined by multiplying the class utilization by its appropriate class price as announced by CDFA. Summing these respective amounts across all pool handlers results in the pool value.

The Department prepares and mails the statement for each handler on or before the 28th of each month, showing the gross amount the handler owes each producer. The statement itemizes the handler's class utilization and the gross amount the handler is directed to pay producers for their quota, base, and overbase milk. ("Pool prices"). The statement does not include authorized deductions the handler may claim, for example, milk hauling cost. If the total value of milk used is greater than the amount the handler owes the producers for their milk, the handler pays the difference into the pool equalization fund. On the other hand, if the amount owed producers is more than the value of the milk used, the handler draws the difference from the pool via the pool equalization fund.

/////
Determining Pool Prices 1969 - 1994

Minimum prices for milk purchases are announced by CDFA each month. Prices are determined according to how the milk was used, meaning that milk was made into cheese might have a different price than milk that was made into butter or into ice cream. Typically, although not always, classified prices follow a typical and descending scale. In other words, the price for Class 1 (fluid milks) carries a higher price than Class 2 (yogurt, cottage cheese), which carries a higher price to Class 3 (ice cream and frozen dairy desserts), which carries a higher price than class 4 (butter, milk powders, and cheese).

The Pooling Plans specified that the highest value of milk was allocated to the quota pool first, then to the base pool, and then finally to the overbase pool, in descending order of class value. The amount of component in each pool, i.e., quota, base, and overbase, was determined by pounds available. Once pounds of components were determined, they were multiplied by the applicable class component prices to determine revenue contained in each pool. Pool revenue was divided by pool pounds -- I'm sorry -- pool revenue divided by pool pounds provided the pool price per pound. The order of priority for fulfillment was quota fat/solids not fat, base fat/solids not fat and overbase fat/solids not fat. Thus, the Class 1 pounds of fat were used to offset the quota fat obligation. If the Class 1 fat pounds were insufficient to
offset the obligation, then Class 2 fat pounds were used, and
so on, until the quota fat needs were met. The same process
was repeated for quota solids not fat, base fat and base solids
not fat. All remaining milk sales revenue was assigned to the
overbase pool.

Determining Pool Prices After 1994.

By the late 1980's, overbase milk production had
increased considerably in relation to quota milk production.
There was also the growing concern among producers about low
milk prices. The California dairy industry generally
recognized that there was room for some milk price enhancement
for Classes 1, 2, and 3. However, because of the methods in
place for distributing milk sales revenues from the pool, the
difficulty of increasing prices for those classes was that
nearly all of the price increase would be funneled into higher
quota milk prices without materially affecting overbase prices.

Following a directive from the California legislature,
CDFA appointed a committee of dairy producers in 1991 to
conduct listening sessions throughout the state to receive
comments and input on the milk pricing regulatory system. The
stated goal of the committee was to strengthen the Milk Pooling
and quota systems. During industry listening sessions held
throughout the state, the committee concluded that overbase
producers became uneasy when the spread between the quota price
and the overbase price became too high. For example, a
difference of $2 dollars per hundredweight or more.

Q. Dr. Erba, that last phrase was in parentheses?

A. Yes. I'm sorry. I shall start that sentence over.

During industry listening sessions held throughout the state, the committee concluded that overbase producers became uneasy when the spread between the quota price and the over price became too high.

JUDGE CLIFTON: I'm sorry, when the spread between the quota price and --

DR. ERBA: The overbase price became too high (for example, a difference of $2 per hundredweight, or more). Conversely, the quota producers were similarly troubled when the spread got too small or even became inverted. Several producers who testified at the listening sessions, proposed some type of "known" spread between quota and overbase prices. Some proposed a floor and ceiling concept, where the spread could fluctuate within a predetermined range, while others proposed a fixed spread. The committee favored the differential concept as a way of strengthening the quota system. The committee engaged in considerable discussion before settling on the fixed $1.70 per hundredweight (for milk testing 3.5 percent fat and 8.7 percent solids not fat). At $1.70 per hundredweight level, the committee felt they could reasonably conclude that the overbase milk would not subsidize the quota milk, and the quota owner would receive a reasonable return for his investment.
This also represented the approximate average spread between the quota and overbase prices for the prior five years.

The committee submitted a formal report to the California Legislature that addressed several items, including the recommendation from the committee to implement a fixed differential between the quota price and the overbase price of $1.70 per hundredweight. Rather than implement the change using the regulatory public hearing process, the fixed differential was written into the California Food and Agricultural Code, i.e., state law. Consequently, as of January 1, 1994, Chapter 3.5 of the California Food and Agricultural Code established the quota premium paid to producers who own quota at 19 and a half cents per pound of solids not fat.

Do you want me to read that differently?

JUDGE CLIFTON: No, that was perfect.

DR. ERBA: 19 and a half cents per pound for Southern California counties without regional quota adjusters (RQA's are discussed in the next section) and at 19 and a half cents per pound solids not fat, minus the assigned RQA for all other California counties.

BY MR. VLAHOS:

Q. Dr. Erba, let me interrupt just for a moment. That figure of 19 and a half cents per pound solids not fat, does that calculate to a hundredweight basis at the 3.58.7
standardization to $1.70 per hundredweight?

A. Yes, at standardized milk testing, 3.5 percent butter fat and 8.7 percent solids not fat, the 19 and a half cents a pound, solids not fat calculates out to a $1.70 per hundredweight.

Q. Please continue.

A. I have lost my place.

Q. Starting with the sentence that says "the quota premium is discounted," I think that's where you were.

A. Yes.

The quota premium is discounted in all other counties of the state by the assigned RQA. The move to a fixed differential also changed the allocation of quota value by component in that all of the price differential above the overbase price was assigned to solids not fat, i.e., the price of quota fat was set equal to the price of overbase fat. Finally, Chapter 3.5 of the California Food and Agricultural Code also provided that the fixed differential would remain operative until the Secretary certifies that producers had voted, via a referendum, to suspend the operation of the chapter. At that point, the fixed differential would be suspended and the quota of milk price calculation would revert to the methods used prior to 1994.

JUDGE CLIFTON: I'm going to stop you there. We're at the top of page 10, we have only read the top two lines. I would
like to take a 15-minute break. So it's about 10:21. Please be back and ready to go at 10:36.

(Whereupon, a break was taken.)

JUDGE CLIFTON: Back on record at 10:40. We're going back to Dr. Erba's testimony. We're at the top of page 10, and Mr. Vlahos, you may proceed.

BY MR. VLAHOS:

Q. All right. Dr. Erba, will you continue your testimony?

A. Quota premium payments are deducted from total pool revenues and average between $12.5 million and $13 million per month, depending on days in month and eligible production marketed. RQA's -- and that is regional quota adjusters -- by construction, are a deduction in quota payments out of the pool and consequently, RQA's actually return revenue to the pool. After the appropriate deductions to the quota premium are taken via RQA's, the quota premium are paid out of the pool amounts to monthly cost of about 37 cents per hundredweight on all pooled Grade A milk marketed in California.

Producer prices are paid on the basis of pounds of fat and pounds of solids not fat. The producer fat price per pound is equivalent for both quota and not quota milk, a result of adding Chapter 3.5 to the Food and Agricultural Code in 1994. Consequently, the producer fat price for quota and not quota milk is basically a weighted average of the individual per pound fat prices that were determined for each of the five
classes of milk. Prior to the computation of the weighted
average, small pool adjustments, such as plant gains, maybe
made.

The calculation of quota and non-quota solids not fat
prices is only slightly more involved than the calculation of
quota and non-quota fat prices. After the quota premium is
determined and set aside, and pool adjustments for
transportation allowances are made, an average of the remaining
solids not fat revenues is computed, weighted by pounds
associated with each class of milk. This becomes the overbase
or base price per pound of solids not fat. The quota price for
solids not fat is determined by adding the 19 and a half cents
to the overbase or base solids not fat price per pound.

Adjustments to Quota Value

When pooling was instituted in 1969, location
differentials were established to encourage the movement of
quota milk to Class 1 plants. Location differentials were
added to or deducted from quota payments to producers, and were
determined by the location of the plant that first received the
milk. Location differentials applied only to the hundredweight
milk equivalent of quota. In following the traditional
movement of milk from supply areas to deficit areas, the higher
hauling cost tended to be offset by a more favorable
differential. Conversely, if milk was needed locally for Class
1 usage, a lower location differential tended to be offset by a
lower haul cost.

Over time, overbase milk became a larger and larger share of the milk produced by individual producers. Consequently, location differentials based solely on quota milk were no longer able to ensure that an adequate -- that adequate milk supplies were made available to Class 1 plants. In June 1983, location differentials were replaced by transportation allowances and RQA's. Transportation allowances partially compensate producers for the cost of hauling milk from a producer's ranch to qualified plants. Those allowances apply to all market milk moving from dairy farms to processing plants which process more than 50 percent of the production into Class 1, Class 2, and/or Class 3 products. In addition, cooperative members receive transportation allowances on shipments to their plant if the plant is located in a deficit area, and if the plant supplies 40 percent of its receipts to Class 1 usage.

Q. Dr. Erba, excuse me for interrupting, but in your testimony you just read, you referred to a phrase of market milk. That may not be a familiar term to others here, so could you tell us what market milk means in the California context?

A. It's a little bit vague in the terms of what market milk actually is, but it is essentially Grade A milk, although not specifically Grade A milk. There are other things that may be Grade A milk that are not market milk, but Grade A milk is
Q. Thank you, doctor. Sorry for interrupting. Proceed.
A. The purpose of RQA's is less transparent because they
do not provide any direct incentive to move milk to Class 1
plants. They were developed to address equity issues arriving
out of the elimination of location differentials, and are
deducted from the quota payments to producers. RQA's are
determined by geographical location of the producer's dairy
farm (currently accomplished by designating RQA's by county of
dairy farm location) and apply to the hundredweight milk
equivalent of quota produced at 3.5 percent butterfat and 8.7
percent solids not fat. Presently, these range from zero cents
per hundredweight for dairy farms located in Southern
California counties, to a minus 27 cents per hundredweight for
dairy farms located in Fresno, Kings, and Tulare counties (see
map at Exhibit 4.A hereto).

Q. Dr. Erba, since you have indicated to see the map, why
don't we turn to Exhibit 43, which are the exhibits to your
testimony, in, to Exhibit 4.A which is the map, and let's wait
a second so people can find it. Just from glancing around, it
looks like everybody's got it, so can you describe what Exhibit
4.A shows?
A. Certainly. It is a color-coded map of California by
county, and the colors correspond to the different RQA areas.
For example, along the north coast, which is shown, at least on
my copy, in gold are there color copies or not?

Q. Yeah, there are.

A. Great. The north coast, which is in gold, those counties have an RQA of minus five cents per hundredweight. The largest geographic area is basically the North Sacramento Valley in most of Northern California, the RQA in that green shaded area is 11 cents per hundredweight. The red area, which is the South Valley, the three counties that make up the South Valley, shown in red, 27 cents per hundredweight deduction.

The counties designated in blue include San Luis Obispo, Kern, and I think it is Santa Barbara, although I can't quite read it -- Santa Barbara -- 20 and one-half cents per hundredweight, and all remaining counties which largely are Southern California and eastern counties, including Mono and Inyo, zero cents per hundredweight for a deduction.

Q. Thank you. Let's return to your text on page 12.

JUDGE CLIFTON: Before he does, Dr. Erba, just so it's perfectly clear, all the categories are a minus, reflecting that there's something deducted, except for the white areas; is that correct?

DR. ERBA: That is correct.

JUDGE CLIFTON: All right.

DR. ERBA: There were no pluses.

Producer-Handlers and Exempt Quota

A producer-distributor (PD; also called a
producer-handler) is characterized by simultaneous ownership of both the milk production and milk processing facilities. In California, there are two types of PD's. Fully exempt PD's (Option 66 PD's), do not account to the pool for any other Class 1 production, but there are significant restrictions on production and sales.

I have a list of five bullet points.

- The entity must own both the milk production and milk processing facilities;
- The own-farm production must average less than five hundred gallons per day for a 12-month period;
- Sales must average less than five hundred gallons per day for a 12-month period;
- The entity may not receive more than 25 percent of total fluid milk sales from sources other than its own dairy farm;

And the last point, last restriction;

- The entity must have retail sales for his or her own account of not less than 50 percent of total Class 1 sales.

Historically, very few Class 1 processors have qualified for this designation, and the amount of milk processed by fully exempt PD's has represented far less than one percent of a Class 1 milk in the state.

The second type of PD, the option exempt PD, (Option 70
PD's) does not qualify for full exemption, but have common
ownership of production and processing enterprises. The option
exempt PD's have no restrictions on retail sales or outside
purchases, and are subject to pool obligations, at least in
part -- they do not account to the pool for the Class 1
production that is covered by exempt quota owned by the PD, but
they do account to the pool for all other production.

There are four option exempt PD's operating in
California and their combined Class 1 exemptions are 57,914
pounds per day. That equates to about five percent of the
Class 1 milk produced in the state. There is no opportunity to
establish additional option exempt PD's without a change in
state law. Furthermore, the option -- excuse me -- the exempt
quota owned by the PD's is not transferrable without a loss of
the exemption. In other words, exempt quota converts to
"regular" quota if it is transferred to another production
entity.

Prior to January 1, 1978, the option exempt PD's could
deduct their original pool quota from their Class 1
obligations. Any purchased quota could not be deducted and was
treated like quota owned by a producer. In 1994, the option
exempt PD's were allowed to include the quota they had
purchased after January 1st, 1978, and before March 1st, 1995,
toward their Class 1 obligations. All four operating exempt --
all four operating option exempt PD's qualify -- should say for
-- a further daily deduction of 150 pounds of fat and 375
pounds of solids not fat from Class 1 pool obligation because
none have transferred production base and pool quota after
February 9th, 1977.

By construct, exempt quota establishes an economic
benefit beyond the value of standard quota. Standard quota
entitles the owner to a higher price that is established at 19
and a half cents per pound of solids not fat per day. Exempt
quota waives the obligation of the owner to account to the pool
for the equivalent amount of Class 1 production. The
additional benefit of exempt quota is then, the difference
between the announced Class 1 price and the announced RQA
adjusted quota price for the same month. From January 1970 to
December 2014, the additional value to exempt quota owners
averaged about 58 cents per hundredweight in Southern
California (RQA of zero dollars per hundredweight).

JUDGE CLIFTON: Shall we have these record copies marked on
page 13 with the insertion of the word "for"?

MR. VLAHOS: Yes, that would be a good idea, your Honor.

JUDGE CLIFTON: All right. So I'm going to ask that the
record copies be changed, page 13, in the middle of the page,
the sentence will read with the word "for" inserted -- "all
four operating option exempt PD's qualify for a further daily
deduction of 150 pounds fat", and so on.

MR. VLAHOS: Thank you, your Honor.
DR. ERBA:

Producer Responsibility

Although producers have gained considerable independence, they are still charged with responsible performance standards. Quota payments apply to only milk produced on a dairy farm located in California. A producer must produce milk of the required quality standards or lose quota entitlement as a consequence. For each day milk is rejected for not meeting the quality standards specified in the contract, the monthly quota eligibility is reduced by one day's quota amount. Rejected milk is still eligible to be accounted for in the base pool.

A producer may not have quota and simply hold it without producer milk. Failure to ship milk to a pool handler for a period of 60 days shall result in the forfeiture of all production base and pool quota. A proportionate of monthly entitlement will be lost for any milk shipped directly to a nonpool plant.

Allocating New Quota

One of the declared purposes of the Gonsalves Milk Pooling Act is to equalize gradually the distribution of Class 1 and Class 2 utilization among California producers. Allocation of new quota based on Class 1 and Class 2 quota, was a necessary provision instrumental in obtaining this goal. Class 1 and Class 2 sales for the most recent 12-month period,
September through August, is compared to that of a previous highest identical 12-month period to determine the amount of increase necessary. The resulting amount is made available for new for allocation as new quota. New quota allocation to existing producers is made effective January 1st, following the 12-month period, during which the available new quota is determined.

Prior to 1985, the amount of new quota --

MR. MR. VLHOS:

Q. Excuse me, Dr. Erba, it is prior to January 1, 1985?

A. Yes.

Q. Yes. Sorry. Go ahead.

A. Prior to January 1, 1985, the amount of new quota to be allocated was determined by comparing Class 1 and Class 2 sales for the most recent September through August period to the of the preceding period. The increase was then adjusted to for the estimated Class 1 and Class 2 requirements for the seceding year, less such estimates made the prior year, and further adjusted by -- further adjusted to add standby requirements.

After January 1st, 1985, the amount of new quota to be allocated was determined by comparing Class 1 and Class 2 sales to the highest 12-month period (September through August) on record, which was 1991 to 1990 -- sorry -- 1990 to 1991. The new quota became available in January of --

JUDGE CLIFTON: Start that again, please.
MR. VLAHOS: Start at the beginning of the sentence, Dr. Erba, the last new quota.

DR. ERBA: Yes.

The last new quota became available in January 1992, and 80 percent of it was issued to existing producers. Because there were few new producers during that time, it took over four years to distribute the remaining 20 percent of the new quota.

Prior to 1979, when new quota was issued, 40 percent of the new quota available was allocated to producers holding unequalized production base and pool quota. Unequalized meant that the quota held by the producer was below 95 percent of the production base. The allocation was based on a formula that gave a higher percentage of new quota to those producers having low quota in relation to a production base. No quota could be allocated to an unequalized producer that would be in excess of that needed to bring quota to the equalized level. Any such excess quota was reallocated to the qualified producers still below the equalization point.

The unequalized quota are those allocated to new producer entrants after the start of the pooling program. All of the original issue of production base and pool quota was brought to equalization effective January 1st, 1978, as directed by --

JUDGE CLIFTON: Read that date again, please.
DR. ERBA: January 1st.

JUDGE CLIFTON: One more time.

DR. ERBA: July 1st -- how'd I get June -- July 1st, 1978 -- thank you for correcting me -- as directed by statutory requirement amended. This one-time direct issue of quota was not conditioned on any increase in Class 1 or Class 2 sales.

After 1979, 40 percent of available quota was allocated to equalize producers (those producers whose quota is 95 percent or more of production base) prorated according to the quota held by each, 40 percent is allocated to unequalized producers.

20 percent of the new quota available is allocated to qualifying new producer applicants who do not have production base and pool quota. In order to apply for this allocation, a new producer must have been in continuous production for one year, and on the date of application, must be shipping market grade milk to a pool handler. Available quota is allocated to these producers on a priority basis, first priority being determined on the basis of the date the application was received. Ties are broken by the longest period in continuous commercial production, and further ties are decided on the basis of the longest period in market grade production. In addition, any quota that was -- any quota that has been forfeited after April 30th, 1981, is allocated on a continuing basis to qualifying new processors.
Allocations to New Producers

The amount of quota to be allocated to new producers is based on the daily average of fat and solids not fat produced during the most recent three-month period from September through November, a maximum of 150 pounds of fat, and 375 pounds of solids not fat can be considered. Allocation is made at either 95 percent of the qualifying production of each component, or 60 pounds of fat and 150 pounds of solids not fat, whichever is less. If a producer enters at the equalized 95 percent level, he or she, is given the qualifying production as production base, and only qualifies for further quota allocation as an existing equalized producer. If the producer enters at less than the 95 percent level, the production base is granted at 111 percent of the quota allocated.

After holding this initial allocation for a minimum of one year, a new producer qualifies as an existing producer to participate in future -- in future allocation of new quota. In the subsequent allocations, the qualifying period of production will be used in determining the amount of quota received. Additional production base will be allocated equal to 111 percent of the additional quota, until the producer eventually has quota equal to 95 percent of the qualifying period production. At that point, the qualifying period production will be assigned as production base.

Prior to January 1st, 1977, the maximum allocated new
producers as production base was the average daily production
during the 12-month period preceding the application, or 90
percent of the average production base of all existing
producer, which ever was less. The maximum quota that was
allocated was 20 percent to the allocated production base, or
the lowest percentage of pool quota to production base of all
existing producers, whichever is -- whichever was less.

Transferability of Production Base and Pool Quota

Subject to certain restrictions, production bases and
pool quotas are transferrable. The restrictions are imposed to
prevent quota from becoming a commodity for speculation. For
example, a quota owner must be a market milk (Grade A) producer
that ships to a pool plant at least once every 60 days. Also,
a quota owner who buys quota may not sell any quota for two
years, and a quota owner who sells quota, may not buy any quota
for two years. A producer may sell to another producer in the
pool area, or change locations within the pool area and carry
the quota to the new location. Quota that moves from one dairy
location to another may be subject to a different RQA. All
transfers must be approved by the Secretary of Agriculture
before the transfer can be made effective and all quota
transfers are made effective on the first day of the month.

The published average price per pound of quota solids
not fat (without the inclusion of cows) reflects the true value
of the quota sold. Although the price is expressed in terms of
quota solids not fat, the transaction carries with it the
related production base solids not fat, production base fat,
and quota fat.

Pool quota has been transferred among producers
continuously since quota was introduced in 1969. (See Exhibit

Q. We'll do it at the end of --we'll do the exhibit at the
end of that paragraph.

A. Okay.

In the first year alone, 342 producers sold at least
some quota, 624 producers bought some quota, and 273
transactions disbursed 100 percent of a producer's quota. In
addition, 51,176 pounds of quota fat and 127,504 pounds of
quote solids not fat were transferred. Since 1969, there has
been an average of 10 quota sellers and 13 quota buyers every
month.

Q. Now that you have finished, that would be an
appropriate time to turn to the table that's on Exhibit 4.B,
and that is a document of some 16 pages, I believe. We'll wait
for a minute while everybody gets a chance to turn to that
section of the exhibit. And that's Table 4.B of Exhibit 43. I
think people have gotten it now.

Dr. Erba could you explain what the this document
deicts?

A. There are several columns and I'll go through and
explain what is contained in each column.

   The first column is the dates, and it's, in fact, the first entry says 1969, 08, that would be August, 1969. And it is a continual monthly recounting of all the transactions since August 1969 through August 2015.

   The second column you see a number of sellers with quota transactions.

   The third column is number of buyers for quota transactions.

   The fourth column recounts the number of sales at 100 percent, meaning the entire -- producer's entire amount of quota was distributed or disbursed.

   The next three columns are covered under a single heading, sales without cows, and has individual columns below that, a low, average, and high, and these are the prices ranging from low to high, with an average in the middle of the price per pound of quota solids not fat since August 1969. And again, these are sales without cows, meaning that the, basically there was a paper transaction.

   The next three columns which are also under a single heading, says sales with cows. Those would be transactions of quota transfers that included the cows. Again, would be a three separate subheadings of low, average, and high prices.

   The next two columns after that are under a single heading that says total production based fat transferred as one
of the subheadings, and total quota fat transferred is the
other one.

And then the last two columns also under a single
heading of total. The subheadings are production base solids
not fat transferred; and the final column, total quota solids
not fat transferred.

Q. Dr. Erba, you had earlier testified that the pooling
plant went into effect in July of 1969; is that correct?
A. That's correct.

Q. So the very next month, August 1969, people began
purchasing and selling quota; is that correct?
A. That is correct.

Q. Thank you. Let's return then, to page somewhere --
page 18.
A. Quota transactions continue to occur nearly every
month, underscoring the importance and prevalence of quota to
the California dairy industry. While transacted monthly sales
volumes range widely (for example, from a minimum of 0 pounds
of quota fat and solids not fat, to a maximum of 13,345 pounds
of quota fat, and 99,574 pounds of quota solids not fat) on
average 2,668 pounds of quota fat, 6,603 pounds of quota solids
not fat, are transferred each month. Over the 552 month
period, which commences with August 1969, the average price for
quota sold was $370 per pound of quota solids not fat. Since
the introduction of quota, the price has ranged from $236 to
$570 per pound of quota solids not fat. (See "Average Selling
Price for Quota" chart below).

Q. Stop right there. The chart below actually appears
after the text, under the heading Fiduciary Review Board, and
that chart is actually on the next page, page 19; is that
correct?

A. That's correct.

Q. And it is sort of out of order, but you had to do that
because of the formatting of the text?

A. I couldn't get the, unless I made the chart very small,
couldn't get it to fit in that text area.

Q. Okay. So let's skip to page 19 now, to that -- that
chart. And does that chart in the general, what it does is
depict in sort of a visual way, the information that's
contained in Table 4.B in Exhibit 43?

A. That's correct.

Q. Okay. Let's turn, now go back to page 18 and continue
with your testimony.

A. For the most recent 12-month period, quota has sold for
an average of $525 per pound of quota solids not fat, thus, at
current market prices, the total value of the 66.2 million
pounds of quota solids not fat owned by California dairy
producers is $1.2 billion.

JUDGE CLIFTON: I'm wondering, Dr. Erba, shall we amend
this page to include those words "not fat"? The way you read
the sentence, you said "quota solids not fat".

DR. ERBA: Yes, I think that would be appropriate.

JUDGE CLIFTON: All right. So I'm going to ask that the two record copies include two words that aren't there, the two words are "not fat". So looking at page 18, the line that's just above the heading called Producer Review Board, that line will read, "of the 66.2 million pounds of quota solids" and then here is where we insert two words, "not fat". And then the sentence continues, "owned by California dairy producers is $1.2 billion."

Would that be consistent with what you said to us, Dr. Erba.

DR. ERBA: Yes.

JUDGE CLIFTON: All right. Good.

DR. ERBA: Shall I proceed?

JUDGE CLIFTON: You may.

DR. ERBA: Okay.

Producer Review Board

The Gonsalves Milk Pooling Act required the Director of CDFA to appoint a Producer Review Board consisting of twelve producer members. The function of this board is to hear appeals of producers seeking hardship relief due to conditions beyond their control and make recommendations to the Director to either approve, disapprove, or modify the request. An example might be a producer who purchased quota and was
subsequently impacted by fire or flood and forced to liquidate his assets (including quota), thus violating the prohibition of selling quota before two full years of quota ownership.

The Board, since 1978, consisting of twelve producer members and one public member, also gives counsel, assistance and recommendations on administrative matters and problem areas of the pooling program. Since its formation, it has made numerous recommendations on producer appeals and administrative issues.

BY MR. VLAHOS:

Q. We can now skip the chart on the bottom of page 19, which you have already explained, and go to page 20.

A. Verification of Records

Personnel within the Milk Pooling Branch perform comprehensive audits of the records of handlers to determine their compliance with the reporting and payment procedures required by the Milk Stabilization and Marketing Plans and the Pooling Plan. Monetary adjustments are made to a handler's account to correct discrepancies revealed by the audit, with such adjustments being reflected in the quota price calculation. The payments to producers are also monitored to ensure that payments are made in the correct amount and at the proper intervals and that no unauthorized deductions are made.

Quota Ownership

At least some quota is owned by more than half of the
dairy producers in California. Conversely, about 42 percent of California dairy farms own no quota. However, the percentage of dairies that own no quota has increased considerably in the last 20 years. (See Table 1 below).

Q. We'll take a look at that table when we get to it in the next page, Dr. Erba.

A. Very well.

In 1995, the distribution of quota ownership was relatively uniform across all six categories. However, as the industry changed in terms of annual milk production (increased by 57 percent) and number of Grade A dairies (decreased by 35 percent) the distribution of quota ownership has changed as well. The most striking change is the percentage of California dairy farms with no quota. Most of the other categories have not changed much in the last 20 years.

Q. Now, Dr. Erba, we're at the top of page 21 at the table labeled Table 1. Would you please explain what that table depicts?

A. Sure. This would be the percentage of dairy farms ranked by quota ownership as of January of each year listed, which starts in 1995 and ends in 2015. The quota ownership categories are 0 percent quota, or no quota owned; 1 percent to 20 percent; 21 percent to 40 percent; 41 percent to 60 percent; 61 percent to 80 percent. And then the last category is those producers who own over 80 percent of the milk production
covered by a quota.

There are several rows that follow that data. One is, the first one is number of dairy farms, which is the number of Grade A farms, again, as of January of the year indicated. And then the corresponding number of dairy farms with quota is the following row after that.

Q. Both the total number of dairy farms and the number of dairy farms with quota have decreased from 1995 as opposed to 2015; is that correct?

A. That is correct.

Q. You may proceed.

A. Okay.

Milk production in California over the past 35 years has become more concentrated within the counties that make up the Central Valley (see Table 2 at Exhibit 4.C hereto).

Q. You may proceed, we'll get to that table.

A. Okay.

From 1980 to 2015 (estimated) milk production increases in the Central California counties has ranged from 230 percent to 1,211 percent. At the same time, milk production decreased in the counties representing Southern California and the North Coast (minus one percent to minus 53 percent).

Q. This would be an appropriate time to take a look at Table 2 at Exhibit 4.C, we'll give some time for people to locate that. It's right after that 16 pages of quoted
JUDGE CLIFTON: So we're going to Exhibit 43.

MR. VLAHOS: That's correct, your Honor. Exhibit 43. And it's the document at the bottom in the right hand corner that says Exhibit 4.C.

BY MR. VLAHOS:

Q. I think everybody has probably got it now, Dr. Erba, so would you please continue and explain what that document which is entitled Table 2 Annual Milk Production by County Thousand Times Represents -- although that sort of tells you what it represents.

A. Yeah, you just took my thunder from me. It's annual --

Q. I'll give it back to you.

A. Annual milk production -- I appreciate that, thank you.

Annual milk production by selected counties, they are not all the counties, and they are listed, counties are listed in alphabetical order. And there are ten counties and there's a reason for the ten counties which will be revealed in the next table, which I will get to. These are in five-year increments starting in 1980 and going to 2015, and 2015 is an estimated number.

The last column in the table represents the percentage change from 1980 to 2015 for the milk production in each one of those ten counties. And then toward the bottom of the table there is a comparison to total milk production for the state,
and they have those ten counties compare. And those ten counties represent between 85 and 1980, 85 percent of the milk produced in California, all the way up to 92 percent of the milk produced in California in 2015.

Q. Okay. Let's return to your text then, on page 21. You are in the -- we're in the middle that bottom paragraph starting with the sentence "as the geographic footprint".

A. Yes.

JUDGE CLIFTON: Now, before he goes on, I want to relate the words on page 21 to the table now that I'm looking at both of them.

So of your ten counties on Exhibit 4.C they are listed in alphabetical order.

DR. ERBA: Correct.

JUDGE CLIFTON: And in your text on page 21 you break them into three geographic areas. You've got a representation from Central California, you have got a representation from Southern California, and a representation from the North Coast. Is it easy for you to tell me which counties go into those geographic areas or do you do it later?

DR. ERBA: I can tell you right now. It is probably best that I do that now.

JUDGE CLIFTON: All right. Great.

DR. CLIFTON: So Sonoma County would be the county that represents the North Coast. There are two counties that
represent Southern California. The first is San Bernardino and the second county representing Southern California is Riverside. The remaining seven counties would be Central California counties.

JUDGE CLIFTON: Excellent. Thank you very much.

DR. ERBA: You're welcome.

As the geographic footprint of milk production (shrank even as California's milk production increased) quota tended to follow dairies as they relocated to the Central Valley, particularly from Southern California. This is evident in Table 3 (see Exhibit 4.D hereto) --

Q. We will do that, Dr. Erba, when you finish this testimony in the next page.

A. Very good.

-- which shows that from 1980 to 2015, quota holdings increased for all Central Valley counties listed but decreased for the counties representing Southern California and the North Coast. Thus, quota has tended to become more concentrated in a small number of counties, most of them located in the Central Valley. In fact, the top ten counties for quota holdings account for over 92 percent of all quota allocated (see Table 3 at Exhibit 4.D hereto).

Q. Let us then turn to Exhibit 4.D, that's a one-page exhibit with the heading, Table 3, Pounds of Quota SNF, Holdings by County (as of January of the listed year).
Tell us what this table depicts.

A. Table 3 was constructed similarly to Table 2 in that we have the same representation for the columns for the dates 1980 through, or for 2015 in five-year increments. The counties match up identically and the counties were selected as the top ten quota holding counties starting in 1980, and then keeping those counties the same as the years progressed to see what the trend would have, or what the trend was for quota holdings among those same ten counties over time.

The total quota held among all counties, not just these ten, is represented as one of the entries, as are the sum of the top ten county quota holders for the top ten counties, and then the percentage of quota holders of those top ten counties compared to total quota holders.

Q. So if I read this correctly, for example, the total quota held by these top ten counties is in the last, second to the last column, excuse me, with 2015 at the head of it, that would be 2,215,998, and that is in the -- excuse me, that's the --

A. That's the total for all counties.

Q. Excuse me, just opposite. That's the total for all counties, the top ten counties of that number had 2,046,422 pounds, correct?

A. That is correct.

Q. Okay. Now let's return back to page 22, and you may
continue your testimony.

A. Thank you.

Continuation of Quota Program Under a CA-FMMO

The proposal from the Cooperatives describes several operative definitions that are necessary to carry out the administration of the quota program. These are found in Section 1051.17(a) through (d).

"CDFA" refers to the California Department of Food and Agriculture, which is the agency of the State of California responsible for the administration of the California dairy producer milk quota program as established in the California Food and Agricultural Code.

"Quota premium" means the value established pursuant to the California Food and Agricultural Code -- how do I read that?

JUDGE CLIFTON: Sections.

DR. ERBA: Sections 62715 --

JUDGE CLIFTON: No.

MR. VLAHOS: 750. Read it again.

DR. ERBA: Sections 62750 et seq. "Quota premium" and "quota premium value" mean the value per pound of nonfat solids which, and include adjustments by applicable RQA's.

"Quota nonfat solids" means the pounds of nonfat solids of a producer as determined and reported by CDFA, which qualify for the quota premium. "Non-quota milk" means pool milk not
eligible for the quota premium.

While the California dairy industry's State Milk Marketing Order is unique in many respects, the California Food and Agricultural Code contains language that anticipates that the state order may be replaced by an FMMO, eventually, and specifies how to reconcile the two orders.

From Section 62726 of the California Food and Agricultural Code, the following discussion is found:

"Notwithstanding other laws to the contrary, in the event a milk marketing order under the jurisdiction of the United States Department of Agriculture or other appropriate federal agency is created by referendum or under the applicable laws and procedures relating thereto in the state or in any geographical area within the state, the provisions of this chapter, or any part thereof, which is in conflict with such Federal Order or which is unnecessary or is a duplication thereof, shall be suspended in the geographical area covered by and during the existence of such Federal Order.

The director shall take such steps and procedures as are necessary to wind up and conclude the administration and enforcement of the provisions of this chapter, or any part thereof, prior to this suspension date."

In effect, if an FMMO is approved by a referendum of California producers, those aspects of the California State Statutes that are in conflict with the FMMO, or are duplicative
of the FMMO, shall be suspended. Clearly, the quota program is
not duplicative of any aspect of an FMMO.

The California quota program is regarded as a valuable
investment option by California dairy producers. Producers who
have decided to invest more money in their dairy enterprises
may, for example, increase cow numbers, remodel their
facilities, buy more land for crop production, or buy quota
which entitles owners to a higher milk price.

As I mentioned earlier in my testimony, quota payments
to producers are an important source of revenues for many
California dairy operators, and preservation of the quota
program to the greatest extent possible is an objective of the
Cooperatives proposal. The objective is consistent with the
Congressional language found in the 2014 Farm Bill language
dealing with the promulgation of an FMMO in California,
specifically Section 1410(d) of the 2014 Farm Bill references
the 1996 Farm Bill (143(2)) and states:

"Upon petition and approval of California dairy
producers in the manner provided in Section 8(c) of the
Agricultural Adjustment Act (7 U.S.C.608c) reenacted with
amendments by the Agricultural Marketing Agreement Act of 1937,
the Secretary shall designate the State of California as a
separate Federal Milk Marketing Order.

The order covering California shall have the right to
reblend and distribute order receipts to recognize quota
value."

MR. ENGLISH: Your Honor? Chip English. Before he reads
the next sentence and gets to other written testimony, I object
to the next sentence on the ground that contains a legal
conclusion.

JUDGE CLIFTON: Thank you.

MR. VLAHOS: In answer to that, we have a, the witness has
his understanding of the law and he's entitled to testify to
it.

JUDGE CLIFTON: The objection is noted. The witness may
continue.

DR. ERBA: In language from Congress makes it clear that
the quota program should have at right to exist within the
framework of an FMMO.

JUDGE CLIFTON: And, Mr. English, how would you suggest
that sentence would read to be consistent with the legislation
as you understand it?

MR. ENGLISH: Your Honor, I think the legislation speaks
for itself, we're going to have a statutory construction
argument. The language in the statute is recognized quota
value, it does not say right to exist, it doesn't say
incorporate, so I think that that's our objection, the right to
exist is different from recognized quota value.

JUDGE CLIFTON: Thank you.

MR. VLAHOS: And the witness is not attempting to quote the
statute. He is giving his understanding as an Economist and as
the official a dairy cooperative in California, his
understanding of what the statute is.

He obviously is not -- we're going to have an argument
for sure, very vehemently I'm sure about what the statute
means, but this witness is entitled to testimony as to his view
of the statute.

JUDGE CLIFTON: Yes, and Mr. English is entitled to object.

MR. VLAHOS: He sure is, and I know he will take every
opportunity to do so. It doesn't mean he's right, though.

JUDGE CLIFTON: And I received both of those as
constructive and helpful.

Thank you, Mr. Vlahos. Begin again, not to rub it in,
but just to read the sentence again.

MR. ENGLISH: Do I get to object again?

JUDGE CLIFTON: Beginning with the words "the language".

DR. ERBA: Your Honor, I, too, am trying to be helpful,
just for the record.

The language from Congress makes it clear that the
quota program should have the right to exist within the
framework of an FMMO. The Cooperatives' proposal recognizes
the importance and sensitivity of maintaining the quota program
virtually intact within the California FMMO. Recall from
earlier discussions, that over half of California dairy
producers own at least some quota, and the total market value
of all quota owned is nearly $1.2 billion. Thus, we propose that the continuation of the quota program be made possible through a joint effort with CDFA and USDA via a Memorandum of Understanding (MOU). Joint administrative apparatuses have been established previously between USDA and State agricultural agencies. USDA maintains MOU's with CDFA for data collection and dissemination. For example, an MOU exhibits between USDA-National Agricultural Statistics Service, CDFA at the California Agricultural Commissioners and Sealers Association to collect and share agricultural statistics for California counties. Furthermore, USDA has had established written agreements with the states of New York and New Jersey to jointly administer coterminously the rules and orders for milk marketing areas in New York and New Jersey (see Exhibits 4.E and 4.F hereto, respectively).

Q. Excuse me one moment. Those are rather long documents, your Honor, and I don't intend to go into them. But in general, would you agree that 4.E is an agreement between the US Secretary of Agriculture in the New York Commissioner of Agriculture, and that 4.F is an agreement between the Office of the Milk Director Industry, Industry Director of New Jersey and the US Secretary of Agriculture?

A. Yes, I believe those are accurate descriptions.

Q. Now proceed.

A. The purpose of the agreements is captured succinctly in
the New Jersey agreement:

"The procedure outlined (in this document) is hereby adopted by the Secretary of Agriculture of the United States and the Director of the Office of Milk Industry, State of New Jersey, as the framework within which the parties hereto will cooperate with each other in connection with milk orders applicable to the handling of milk in marketing areas located in the State of New Jersey."

The expectation is that the MOU for CDFA and USDA would pursue a similar degree of cooperation and understanding. In effect, the CA-FMMO does not disturb the quota program. Instead, the Cooperatives' proposal, under the Cooperatives' proposal, the quota program becomes embedded within the CA-FMMO with full information transfer between the two governmental agencies. Each month CDFA will communicate to CA-FMMO Market Administrator (MA) all financial calculations relative to the net cost to the pool of quota payments. The MA would then take all steps to assure that quota values are deducted from pool revenues and paid to producers properly. Also, the MA would remit any necessary information regarding quota payments back to CDFA to allow ongoing administration of the quota program. Thus, the proposal leaves all jurisdiction over quota administration, calculations, recordkeeping and regulatory changes to CDFA. As such, the laws, regulations, and policies in operation at the time of adoption of a CA-FMMO would remain
unchanged. There are no provisions in the Cooperatives' proposal that would alter quota payments. The quota premium of 19 and a half cents per pound of quota solids not fat is maintained, as are the applicable RQA's.

As a practical matter of providing the MA with the information specified in Section 1051.61 and 1051.62, CDFA would have to determine, obtain, and/or verify each month:

- The active California dairy producers;
- The amounts of quota owned by each producer after reviewing and applying quota transactions that occurred as of the 15th day of the prior month;
- Location of each producer (to verify applicable RQA);
- Number of days of eligible production; and
- Individual producer quota payment after taking into consideration applicable RQA's and eligible production for the month.

According to the handler reporting requirements contained in Section 1051.30 of the Cooperatives' proposal, pool handlers shall report to the MA as of the 9th day after the end of the prior month, the pounds of milk, butterfat, protein, and other nonfat solids contained in producer milk.

Q. Stop right there.

JUDGE CLIFTON: Can you hear him as easily as you could in the back? So we may have to change. Let's go off record.

(Whereupon a break was taken.)
MR. VLAHOS: Back on the record, I guess. At the end --

JUDGE CLIFTON: Yes, back on the record.

MR. VLAHOS: Regain my composure.

BY MR. VLAHOS:

Q. When you stopped your testimony there was a footnote at that point. I would like you to read a footnote and explain it, why the footnote is there which identifies a certain change.

A. Yes. There's a footnote on the bottom of page 26, and it says:

The dates referenced for reporting information to the MA have changed from the proposal submitted in February of 2015. Three days has been added to each deadline to accommodate actual accounting practices for milk receipts and utilization.

Q. And actually, for the record, we'll represent that that was also a change from the Cooperatives' proposal as contained in the Notice of Hearing. Three days were added to each of those deadlines. Why was that done, Dr. Erba?

A. Well, after we talked to the staff at the three coops involved in the proposal, Proposal 1, the accounting staff, and the finance groups, they said they did not think they could consistently hit those deadlines as specified in our original proposal, and that the addition of three days would give them a little more flexibility to hit those reporting deadlines.
consistently.

Q. So we can call this footnote cutting slack for them, right?

A. I think that's probably an accurate statement, yes.

Q. Okay. Please continue.

A. Section 1051.31(a) and (a.1) also allow the MA the flexibility to acquire additional producer information as deemed necessary by the MA, including information pertaining to producer degraded milk for the month. This producer data is to be shared with CDFA along with the applicable class prices (announced by the fifth day after the end of the month). The intention is that before the 14th day after the end of the prior month, CDFA can term and report to the MA of the CA-FMMO the applicable individual producer quota payments. At the same time, CDFA shall report to the MA the quota pounds associated with the milk supply received by each handler, which will be used to determine possible payments into (or draws from) the producer-settlement fund. To be clear, only information is exchanged between the two regulatory agencies; no money will move between CDFA and the MA.

Section 2051.61 provides detailed steps describing how the MA shall determine producer component prices for pound of butterfat, protein, and other solids. After combining all values into a single milk sale revenue pool and making the necessary adjustments to that revenue pool (described in
Section 1051.60), the MA shall deduct from the revenue pool an amount equivalent to the quota premium as reported to the MA and by CDFA prior to calculating any milk component prices. As specified in Section 1051.62, the MA shall announce publicly, the applicable quota premiums for solids not fat to be paid to quota holders on eligible milk production and the statistically uniform price for non-quota milk, as well as other relevant prices by the 14th day after the end of the prior month.

The producer-settlement fund is established and used by the MA as a repository for all payments made by handlers and the fund from which payments are made within the Federal Order. Payments due any handler shall be offset by the payments owed by the handler. Payments into the fund by handlers shall follow the steps provided in Section 1051.71 and reflect announced minimum prices and utilization of the components of milk. If any payments are due by a handler, they are to be received no later than the 16th day after the end of the prior month. The procedural steps for payments due handlers from the producer-settlement fund are specified in Section 1051.72. Payments from the producer-settlement fund reflect monies due producers based on each handlers producer payroll, which closely follows procedures followed in other FMMO's. One significant difference for the California FMMO, is if the additional value resulting from a handler receiving milk covered by quota is credited to the handler from the
producer-settlement fund. This allows handlers to pay
appropriate amounts for all milk received no matter how the
milk is used and no matter if the milk is covered by a quota.
Payments from the producer-settlement fund, if any, shall be
made by the 16th day after the end of the prior month.

Q. Does that conclude your prepared testimony, Dr. Erba?
A. It does.

Q. And that also concludes, your Honor, my direct
examination of Dr. Erba. At this time, I would move for
admission into evidence of Exhibit 42 with the corrections that
have been noted on the record, of the Code 1050 references have
been all changed to 5051 references. And with those changes,
and I'll assure your Honor, if you so direct, that Meredith
does have those changes in the official copy. And with that, I
would like to move admission into evidence of Exhibit 42.

JUDGE CLIFTON: I have two additional changes that I would
ask you, Mr. Vlahos, and you, Dr. Erba if you would like to
have me make, and have Ms. Frisius make also on the record
copies.

The first one is on page 26, and I am looking at a line
that is about eight lines from the top.

MR. VLAHOS: Starting "degraded milk for the month"?

JUDGE CLIFTON: Yes, that line starts that way. Yes.

Now, the way Dr. Erba told us the sentence that begins
with "this producer data" he said, "this producer data is to be
shared with CDFA along with the applicable class prices," and if both of you mean that, I would like for us to insert on the record copies, the word "with".

MR. VLAHOS: I enthusiastically support that.

DR. ERBA: As do I.

JUDGE CLIFTON: All right. So I'm going to ask Ms. Frisius to make that change on page 26, eighth line down, you are inserting one word, the word "with", following "CDFA along."

And the other is also a change to conform with what the reader told us, and it's just a typographical error on page 24, going from the bottom, moving up about seven lines, there is a word there that the -- that the reader told us is "coterminously" and that made sense to me, and it's just typed wrong. It has an "N" that doesn't belong there. And I would suggest that we'll just have the record copy have a little slash through the "N." And does that meet with your approval?

MR. VLAHOS: Agreed, your Honor.

DR. VLAHOS: As do I.

JUDGE CLIFTON: All right. Is there anyone who wants to ask any questions of the witness before determining whether you have an objection to the admission of Exhibit 42 into evidence?

MS. FRISIUS: Did we want to do the corrections on page 13 and 18 that were mentioned during the testimony?

JUDGE CLIFTON: Let's see, 13?

MS. FRISIUS: We added the word "for."
JUDGE CLIFTON: Yes, that's in. Correct. Oh, not officially, is it? I wrote it on my copy, but yes, thank you so much.

Yes, please go to page 13, and about in the middle of the page, the sentence reads, "all four operating option exempt PD's qualify for a further daily deduction." And so that is how it was read by Dr. Erba, "qualify for," and he pointed out that we should correct that, so I'm asking that the record copy be marked accordingly.

MS. FRISIUS: The next one is on page 18, same situation.

MR. VLAHOS: Just above producer review board heading?

JUDGE CLIFTON: All right. So we're adding the two words "nonfat" so the record copies will read, "quota solids not fat." Good.

MR. VLAHOS: Your Honor, if I may, just another question or two.

JUDGE CLIFTON: You may.

BY MR. VLAHOS:

Q. Dr. Erba, in Tables 2 and 3, and those are the tables within the text. You prepared those tables?

A. Yes.

Q. Where did -- what was the source of your information?

A. The information on each of those tables came from the Department of -- California Department of Food and Agriculture.

Q. Thank you. That concludes my direct testimony, your
Honor.

JUDGE CLIFTON: All right. Is there any objection --

MR. VLAHOS: Dr. Erba's direct testimony.

JUDGE CLIFTON: That is an important correction. Is there, is there any objection of the admission into evidence of Exhibit 42?

MR. VLAHOS: Yes. I withdraw my objection.

JUDGE CLIFTON: There never was one.

MR. VLAHOS: No, I know.

JUDGE CLIFTON: All right. Exhibit 42 is admitted into evidence. Vlahos?

(Thereafter, Exhibit Number 42 was received into evidence.)

MR. VLAHOS: Yes. Mr. English has kindly pointed out to me that in my haste to sit down again, I forgot to move for admission of Exhibit 43, which I now so move.

JUDGE CLIFTON: Does anyone want to ask any questions of the witness before you determine whether you have any objections to the admission into evidence of Exhibit 43? There is no one. Is there any objection to the admission into evidence of Exhibit 43? There is none. Exhibit 43 is admitted into evidence.

(Thereafter, Exhibit Number 43 was received into evidence.)

MR. VLAHOS: Thank you, your Honor.
JUDGE CLIFTON: It is it is 11:55. This is amazingly complex.

Dr. Erba, I thank you for this presentation. I think it's extremely valuable. I wish I could say I understood it. I tried very hard. It is extremely complicated. I know most of the people in this room had to get their heads around it to some extent already, but I suggest that perhaps cross-examination should be after lunch. Is everyone in agreement?

MR. ENGLISH: I agree. It's very complex stuff, and I think cross-examination will be more efficient if we had maybe an extra 15 minutes, so an hour and 30. And I think the witness and the court reporter might need the break as well. So I propose an hour and 30 minutes today.

JUDGE CLIFTON: All right. Good. I like the idea.

I have an idea that I want you all to think about, and you don't have to give me an answer today, but I want you to think about it. You will remember I mentioned as a preliminary matter, that there is one organization that is recording the audio feed and making it available to its members on a website. And I thought that was an excellent thing, in that we won't have the transcript immediately, and this opportunity to listen to some of the testimony again would be valuable.

The idea that I want you to think about is that that website is Agribusiness Publications. And we would all be
welcome to use it. Anyone would be welcome to access the information there.

The gentleman whose been here with us for part of the hearing, he's not in the room right now, who is the owner, publisher, is Tom Van Nortwick. What he would like to do to make it even more helpful and useful, is he would like to post on that same website copies of the exhibits.

Now, the easiest way for him to upload them to the website is if he had a PDF of them. Many of those that we have marked on by putting an exhibit number on them or making corrections to them, don't look like what you might have available to convert to a PDF. I don't -- we could perhaps just gather for his use, a hard copy that's been corrected and let him scan them and put them up. Perhaps we -- perhaps we don't want that. The main thing is, we don't want any exhibit posted anywhere that's not a hundred percent accurate. So that's number one concern.

I'm not asking for any response now. I want you to think about it. I'm very grateful that the audio feed would be available for people who aren't listening between 9:00 and 5:00 Pacific who might want to hear some of the testimony and might not want to wait for the transcript.

So like I said, I'm not asking for a response right now. I do want you to talk about it and think about it, and see what you would prefer, what you would suggest. All right.
Is there anything further before we break for lunch?

12:00 now. Please be back and ready to go at 1:30.

(Whereupon the lunch recess was taken.)

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FRIDAY, OCTOBER 2, 2015 –— AFTERNOON SESSION

JUDGE CLIFTON: All right. We're back on record at 1:34.

Who would like to begin cross-examination of Dr. Erba?

CROSS-EXAMINATION

BY MS. HANCOCK:

Q. Nicole Hancock for California Producer Handlers Association.

Good afternoon, Dr. Erba.

A. Good afternoon.

Q. Do you still have Exhibit 42 in front of you?

A. Yes, I do.

Q. If you can turn to, you wrote it so you probably know what it says, on page 22 of Exhibit 42 you talk about Section 62726 of the California Food and Agricultural Code.

A. Yes.

Q. And it goes on, your discussion goes on to page 23. And you summed it up by saying, "If an FMMO is approved by a referendum of California producers, those aspects of the California state statutes that are in conflict with the FMMO or a duplicate of the FMMO, shall be suspended." Is that right?

A. That's correct.

Q. Okay. And then clearly the quota program is not duplicative of any aspect of the FMMO, and so that's how you preserve the quota program as it is written in the California Agricultural, the California Food and Agricultural Code?
A. Yes, that would be our position.

Q. Okay. And as you know, the California Producer Handlers Association holds exempt quota that's also discussed in the California Food and Agricultural Code. You are aware of that?

A. Yes.

Q. And the reason that as the Cooperatives' proposal has drafted Proposal Number 1, the reason that that proposal does not preserve the exempt quota that the California Producer Handlers currently hold under the state order system, is because of the producer handler definition that you have within Proposal Number 1. Is that your understanding?

A. I don't know if it was quite that way. I would say that our proposal just simply didn't address exempt quota, and I don't know that we necessarily linked it to the federal definition of producer handler, we just didn't address how exempt quota might be preserved.

Q. Okay. So you are just silent on the treatment for the current California Producer Handlers Association's treatment of exempt quota. Right?

A. Right.

Q. But it is your understanding that at least as written right now, that your Proposal Number 1 would not allow for that exempt quota to be carried forward?

A. Right. There's no mechanism in what we would propose
that would do that.

Q. And similar, there's no, similarly, there's no mechanism for the treatment of quota in Proposal Number 1 either, right?

A. I'm not sure what you mean with that one.

Q. Well, in the proposal for the federal regulatory language, the Cooperatives have not proposed any quota language.

A. I guess sort of yes. Looking, I guess explain that one. We haven't, what we have entertained, what we've proposed is a working relationship between CDFA and USDA, so that the quota remains at the, in the jurisdiction of CDFA, and not necessarily is found in our proposed language for the Federal Order for California, so there has to be a working relationship between the two agencies to make sure that the quota program is preserved as we have proposed.

Q. Okay. So but what you are talking about right now is just the administration of how it would be calculated; is that right?

A. Yes. Yes. We'll just leave it at yes.

Q. Okay. And maybe I'm -- I might be making this more complicated. I'm just trying to kind of lay the background for the rest of our discussion. So in laying that background, I just want to make clear that there's some -- let me say it differently. Under the Cooperatives' proposal, you proposed a
definition for producer-handler that's different than how it is
currently defined in the California state order system?
  A. That is correct.
  Q. Okay. And because it's different, it would be in
conflict with what's in the state order system?
  A. Seemingly, yes.
  Q. Okay. Or potentially could be?
  A. Yes.
  Q. Unless we fixed it somewhere along the way?
  A. Correct.
  Q. Okay. And in your testimony you described quota as an
asset or a financial instrument for your members, your producer
members?
  A. Yes.
  Q. And I think you said that there is -- there is two
aspects to the value. There's a value in the pool treatment,
and then also the asset sale value. Is that -- is that a fair
characterization of how you describe those values?
  A. I don't recall breaking it into two pieces. The
descriptor as I presented it, entitles the holder to a higher
price for milk. I don't recall that I made that necessary to a
sale value, but obviously it is an asset that can be sold. So
if that's what you mean, then yes.
  Q. And I'm referring back to the chart where you had, in
Exhibit 43, I think it was 1.B or 1.C.
A. The long table?

Q. The table that was showing the trading values.

A. Yes.

Q. Okay. So there is the value in holding quota because you receive the higher price from the pool, that's one part of it.

A. Yes.

Q. And then the other part of it is the value that you hold as a tradable asset that you can freely exchange it, you can sell the quota.

A. Okay. I understand what you are saying now. So yes. Correct.

Q. So two different types of value that that quota holds for your members?

A. Right.

Q. Okay. And do you understand how exempt quota works under the California state order system currently?

A. I think I tried to articulate that, although maybe I did not succeed, but yes.

Q. I thought you did a great job. I thought you saved me a lot of work, so I appreciated that.

But there is the same, I think you described it as an economic benefit for exempt quota beyond that of the regular quota.

A. Correct.
Q. Can you describe for me what you meant when you said "an economic benefit beyond the regular quota?"

A. The exempt quota has all the characteristics of standard or regular quota, in that it holds the 19 and a half cents per pound advantage, per pound solids not fat per day, advantage over for -- well, I screwed this up. It has the same application as a 19 and a half cent per pound of quota per day, as your regular or standard quota.

The exempt quota -- so it would -- exempt quota can default to regular quota, so it still has that value, even if your members were to sell it, which has happened. It still takes on that quota value. It has the additional value of the holder not having to report to the pool those Class 1 sales covered by that quota. So that's the additional benefit that I talked about.

Q. So that additional economic benefit to the exempt quota would be the same attributes as regular quota, so you have a tradable value if you ever sell it?

A. Correct.

Q. And then if you treat it as it is regular quota, you would receive the higher quota price.

A. Right.

Q. But if you, the added benefit is it if you treat it as exempt, you don't receive that higher quota price, you just don't, you get whatever price you are able to negotiate with
your end customer without regard to the pool. Is that what
your understanding of how it works?

A. For the exempt quota?

Q. For the exempt quota.

A. No, I would not say that. I would say that it's -- it
waives the obligation for the reporting of those Class 1 sales
to the pool and actually comes out as a, I believe a credit,
and you report it and you get credited back. So you basically
don't have to pay the Class 1 price for that milk that was
produced as a Class 1 product. That's the exemption part of
it. I'm not sure if that's what you had in mind or not, but
that's my understanding.

Q. So if I can simplify the numbers. Let's say you own a
hundred, let's say you hold a hundred -- is it a hundred -- I
have lost the term.

A. How about just units.

Q. Units of exempt quota and you produce two hundred units
of Class 1. A hundred of the units would not be counted toward
the pool, but your second hundred would. Is that what you are
saying?

A. Right. So you would not have to report to the pool any
of that Class 1 sales that are covered by your exempt quota.

Q. And so the additional economic impact is that you get,
you don't have to count those towards your Class 1 sales, any
regular quota that you hold, you still get to keep and count
that towards your pool?

A. Right. It isn't applied, the regular quota would not apply to Class 1, just on the production side.

Q. And I think you described in here that as of March of 1995, producer-handlers, at that point, were capped at the exact quota that they could receive.

A. As far as I know, that is the last date that, March 1995, the last date that exempt quota was allowed to be counted. So you would basically change in -- exchange your quota for exempt quota. And after that date, it was not allowed.

Q. And if a producer-handler were to acquire quota after that date, they would acquire that as regular quota?

A. Correct. That's my understanding.

Q. So producer quota -- excuse me, producer-handler could own exempt quota and regular quota at the same time?

A. Correct.

Q. At least Option 70 producers?

A. Yes.

Q. Producer-handlers?

A. Yes.

Q. And just quick clarification on that. Are you aware of any Option 66 producer-handlers?

A. When I worked for the Department from 1997 to 2004 when I got out of the dairy side of things, there were two operating
at that time. I don't know if either one of those continues to exist.

Q. What year was that?
A. From '97 to 2004.

Q. And I'll represent to you that my four producer-handlers that I represent are Option 70 producer-handlers.

A. Yes, I know.

Q. Okay. So for purposes of my discussion, that's the part that I'm talking about, just so our record is clear.

A. Yes.

Q. And may I --

JUDGE CLIFTON: May I interject? I want Dr. Erba to be specific about his use of the word "report". So if there is exempt quota and there's no financial obligation as to that exempt quota to the pool, does the person holding the exempt quota still have to report it to someone and get the credit on someone's books?

DR. ERBA: I believe that's how it works. It doesn't -- I'll go from memory here, and I was not intimately involved with the reports that were filed, but my understanding is that those sales, all sales are reported, and then there's a credit back out for the milk that's the Class 1 sales covered by exempt quota. Now, that may not be entirely right, maybe none of it is reported, but I think that's the way it works.
JUDGE CLIFTON: Thank you.

MS. HANCOCK: AND I think it is deducted from the pool.

DR. ERBA: Deducted. Okay.

BY MS. HANCOCK:

Q. You gave an overview of how location differentials, and then later on transportation credits, operate in the pool in California, or under the California order. Is it your understanding that, or is what is your understanding of whether the exempt quota holders are able to utilize any transportation credits?

A. I think the word you are looking for is actually transportation allowances. There's credits as well, but this is an allowances issue. And as I understand it, they are not eligible for transportation allowances. Exempt quota is not eligible for transportation allowances.

Q. Did you conduct any kind of financial evaluation or analysis of what the transportation allowances would be if those exempt, if that exempt quota were treated as regular quota and was then entitled to transportation allowances?

A. I did not but our counsel did, and we reviewed it. And over all of the Option 70, the exempt producer-handlers, what we calculated, of course, so this is going to be, require some estimation and so far forth, but it is a very small effect on the pool. So if the exempt quota piece were to go away and the quota would still exist as regular quota, and now that milk be,
some of that milk be eligible for transportation allowances, the cost on the pool was very small. I don't remember if it was a plus or minus, but it is a very small number.

Q. You can turn to page 13 of Exhibit 42. And in your document it says that, "a combined Class 1 exemption, there are four," -- let me start at the beginning of the sentence.

"There are four option exempt PD's operating in California, and their combined Class 1 exemptions are 57,914 pounds per day."

Do you see that?

A. Yes, I do.

Q. That would be what you -- where did you get that number from?

A. I got it from Department of Food and Agriculture.

Q. Okay.

A. California Department of Food and Agriculture.

Q. And if you -- do you by chance have your phone up there with you?

A. No, I purposely did not take it with me.

Q. Can I give you my phone to use for my calculator?

A. Do I have to give it back?

Q. You could answer all the e-mails, then.

So if there are 57,914 pounds of exemption, and you can sell that quota at, I think, what is it, $525 is what you have averaged for today's price?
A. Right.

Q. Let's quantify that. Make sure that my math is correct. So 57,914 multiplied by the $525, do you get $28,829,850?

A. No, I did not. Which means I probably hit the wrong button here.

Q. Or I did.

A. I got $30,404,850.

Q. I trust the Economist. And then let's compare that. I wrote the number down, so hold onto that for one second. You have on page 24 listed, that the market value of all of the quota is 1.2 billion on page 24.

A. Yes.

Q. Exhibit 42.

A. Yes.

Q. So I took my incorrect number, but let's use your number and divide that, what I'm ultimately trying to get is the percentage of the exempt quota as compared to the total quota pool.

A. I have rounded slightly, but about two and a half percent is what I get.

Q. So just so the record's clear, the exempt quota under these calculations, the exempt quota makes up about two and a half percent of the total quota in the State of California under the state order system?
A. Oh, I'm sorry, yes, that appears to be correct. It is a small percentage.

Q. Okay. And you have in here that it equates to about five percent of the Class 1 milk produced in the state. Do you know what the percentage is of the total pool?

A. The exempt quota?

Q. As compared to the total pool?

A. Something a lot smaller than five percent, but no, I have not calculated that.

Q. Do you know what percentage the quota makes, the total quota makes, of the total pool?

A. I believe it is around the 22 to 25 percent range, although I'm not totally certain of that.

Q. And that's of the total pool, not of the Class 1 milk?

A. I think that's right.

Q. So other than the restriction for having to deliver quota milk to the pool within a 60-day window, are there any other restrictions on quota holders and their ability to transfer or operate within the pool that you are aware of?

A. Yes. And I went over those somewhere. Under producer responsibility on page 14, "quota holders have to produce milk on a dairy farm located in California, and they also must meet certain quality standards, or the milk, even if covered by quota, is not eligible to receive it." And that may be it because the other one you already listed here.
Q. Are there any requirements for maintaining ownership within a family lineage?

A. For regular quota?

Q. For regular quota?

A. No.

Q. Any restrictions on sales other than selling to another producer that you just described?

A. Sale of quota, you mean?

Q. Sale of regular quota?

A. Well, there are the restrictions about, have you bought or sold any within a two-year period on both sides of the transaction, but other than that, I don't think so.

Q. So the restrictions for exempt quota are more severe on, the restrictions against transfer, are more severe for exempt quota than for regular quota?

A. Right. So if you -- if the -- if any of the four producer-handlers, the option exempt producer-handlers, were to attempt to sell their exempt quota, it would lose its exempt status.

Q. On page 24 you have a statement that says, "the Cooperatives' proposal recognizes the importance and sensitivity of maintaining the quota program virtually intact within the California Federal Milk Marketing Order."

Do you see that?

A. I do.
Q. Would that include the treatment for exempt quota as well?

A. Well, as I said earlier, our proposal doesn't specifically address exempt quota, but that is part of the quota program as it exists today.

Q. So assuming that you are presented with language from the California Producer Handlers Association that would preserve the exempt quota as it exists today under the California system without altering any other provisions within the Cooperatives' proposal, would the Cooperatives be supportive of that proposal?

A. We certainly would like to see that language and we would absolutely consider it, although I can't give you a definitive statement until I at least see the language, but excepting unintended consequences of trying to preserve the exempt quota, we would absolutely consider adopting that language, or at least working with you to develop that language.

Q. Thank you. I have no further questions.

DIRECT EXAMINATION

BY MR. VLAHOS:

Q. John Vlahos, your Honor.

Just a couple of points of clarification. On the issue of transfer, I just want to make sure the record is clear. An exempt quota holder is not restricted in any way from selling
his or her quota, they just lose the exemption; is that correct?

A. I think generally your statement is correct, and of course you would have to sell it to an eligible buyer, you couldn't just sell it to anybody on the street, but yes.

Q. Okay. The other thing Ms. Hancock asked you if there was anything in the coops' proposal that dealt with quota, and I just want to call your attention to Section 1051.17 of the coop proposal as contained in the Notice of Hearing.

May I show the witness, your Honor, that section?

JUDGE CLIFTON: You may.

BY MR. VLAHOS:

Q. That's actually -- the coop proposal does have references to the quota; is that correct?

A. Yes.

Q. Can you just briefly describe what, they speak for themselves, but briefly describe how it does so.

A. Sure. It's just a -- from the -- from what it says, a definitional section of the proposal, the language proposed that addresses items such as quota premium, quota nonfat solids, and non-quota milk.

Q. Does it also deal with the CDFA having some role in this?

A. It defines that CDFA would be the administrator of the California quota program.
Q. Thank you.

CROSS-EXAMINATION

BY MR. ENGLISH:

Q. Chip English. Good afternoon, Dr. Erba.

A. Good afternoon.

Q. So let me first, just for efficiency purposes, if possible, ask, are you -- is this your one time on the witness stand or are you going to be here on other subjects, to your knowledge?

A. I don't know. I'm looking at my counsel and they are throwing their hands up in the air as if they don't know either.

Q. So to your knowledge, this may be the one time that you are on the witness stand?

A. This maybe the one time.

Q. Okay. Thank you. So let me maybe actually reverse myself and start at a different place than I might have, but since Ms. Hancock asked you some questions, let me go to some of those materials and ask about some of the linkage.

With respect to the quota, do you understand that under the Cooperatives' proposal, out-of-state milk that is received at a plant in California, that today receives whatever it receives as a price, would instead, on a regulatory basis, the handler would receive a credit at the overbase price for that milk?
A. I believe that's correct.

Q. Okay. And that out-of-state milk, under California law, cannot own quota, correct?

A. Yes, you have to be a dairy farm producing milk in California to own quota.

Q. So if you are a dairy farm in Arizona and you ship to a Southern California facility, I'm sorry, yes, a dairy farm, you ship to a Southern California fluid milk plant, you cannot own quota, correct?

A. Not on that Arizona.

Q. On that Arizona volume?

A. Right.

Q. So on page 24, when Ms. Hancock read the sentence to you, you say the Cooperatives' proposal recognizes the importance and sensitivity of maintaining the quota program virtually intact within the California Federal Milk Marketing Order. In fact, you are effectively expanding it to include out-of-state milk that ends up being pooled on the California order, correct?

A. Well, I don't see it that way. Maybe the words of that sentence aren't exactly correct, although I kind of think they are. Basically, what it says is the quota program stays as it is, as it is today, which would be that California dairy farms are the only potential owners of quota, and we're not expanding it beyond that.
Q. Well, except that today, that out-of-state milk that is received by a California pool distributing plant is effectively held harmless on the quota value, correct?

A. Correct.

Q. Okay. And the change is that instead, the handler receiving that milk will get a credit at the lower overbase price. Correct?

A. I could see, correct, I see where you are going with this, but I suppose maybe it is just a difference in how you view it. I don't see that as an expansion of the quota program. There may be some changes in how milk is priced to pool, but I don't see quota being expanded by this.

Q. Doesn't it effectively mathematically enhance the value of quota?

A. By -- can you finish the thought? By?

Q. So milk that presently washes out of the system because it is out-of-state milk, and after the Hillside Dairy case it is treated effectively as if it is just not there in terms of accounting purposes. By including the milk in the volume but now giving it a credit at the overbase price, doesn't that increase the value of quota?

A. I don't think it increases the value of quota.

Q. Does it increase the value of the -- I'm sorry, does it increase the quota price? All other things being equal, does that by itself increase the quota price?
MR. VLAHOS: Objection, maybe it's more a request for clarification than an objection.

Mr. English, if I may ask, when you say the quota price, do you mean the price at which quota is sold from a seller to a buyer?

BY MR. ENGLISH:

Q. No, I meant the milk price. I'm not speaking, and I'm not speaking about what quota transfers for, although one could argue that that might change, I'm not there. I'm talking about in a given month, today, in October of 2015, when that milk that comes in from out-of-state to a California pool distributing plant receives a credit, at the end plant blend, correct? That's effectively what happens when it goes to a pool distributing plant, correct?

A. Out-of-state milk?

Q. Goes to a California pool distributing plant. The California, effectively on accounting mechanism, gives that a credit at the end plant blend, correct?

A. That I'm not sure of. I would not have said that, but you maybe right on that one. I'm not sure about that.

Q. Assuming I'm right and the credit is effectively at the end plant blend, if instead for the same month, the credit becomes the overbase price, and assume that prices are in normal relationship so that one is the highest price, we don't have any inversions, with that credit now at the overbase
price, doesn't that mean that the overall value of what is left
over to be distributed for quota has increased?

A. I think the value of the pool increases and all pool
prices would increase, but quota price would not increase
independent of the overbase price or the base price.

Q. But the credit that's been permitted to the handler is
at the overbase price, and so it is now going to pay more into
the pool, or pay more to account for that quota value, isn't
it?

A. I guess I'm just simply not following you.

Q. Okay. We'll try it a different way.

The in-state fluid milk processor, let's assume for a
moment that it receives one hundred percent of its milk from
out-of-state. And let's assume a much more simple pool where
you only have basically two Class 1 handlers, and both are the
same size. Under today's scenario, that processor which
obtains a hundred percent -- hypothetical processor receiving a
hundred percent of its supply of out-of-state milk has no
obligation to the California pool, correct?

A. I believe that's correct.

Q. If your proposal is adopted, the credit that instead,
that handler now will have a pool obligation identical, they
have got same Class 1 utilization, will have identical pool
obligation to the handler that receives a hundred percent of
its milk in-state, correct?
A. Correct.

Q. And it will receive a credit for the milk that is received from out-of-state at the overbase price, correct?

A. Correct.

Q. That difference is brand new money for the California pool, correct?

A. Yes.

Q. Okay. And because you deduct the quota value before you calculate the value of the pool, that larger pool value will be first proportionately distributed to California dairy farmers with quota, correct?

A. Correct.

Q. Thank you. Now, let's take a different example. Hypothetically, actually, let me first take you to when you do your calculation of the producers who don't own quota. Is that, is that calculation based upon California producers shipping to California plants or does it include California milk that is received at plants outside of California?

A. Are you talking about Table 1 on page 21?

Q. Yes.

A. I have already forgotten your question. Could you re-ask the question, please?

Q. Yes. For the line that is number of dairy farms --

A. Yes.

Q. -- is that a number of dairy farms, all dairy farms
located in California with Grade A milk, or is that number of
dairy farms in California shipping to California plants?

A. It's on the same report that gives the information from
which this table was generated and it doesn't specify. It just
says California dairy farms on it, and it doesn't tell what
those dairy farms are. I think it is simply California dairy
farms with Grade A permits.

Q. Okay. So in that case, if a California farm has been
selling say to a plant in Arizona for more than 60 days, by
definition from your discussion in your testimony, it no longer
qualifies, it hasn't qualified its quota, correct?

A. If it -- yes. If it owns any quota, which it may not,
it would not have maintained its eligibility to continue to
hold that quota, but that doesn't mean it is not a Grade A
facility.

Q. I understand that. We understand that Grade A is a
different designation for this purpose, correct?

A. Yes.

JUDGE CLIFTON: So Mr. English, your hypothetical has the
farm selling all of its milk out-of-state?

MR. ENGLISH: Yes, thank you, your Honor.

BY MR. ENGLISH:

Q. So selling all of its milk to an Arizona plant, day in
day out, for more than 60 days, and it has Grade A status so
we're not talking about any non-Grade A issue.
It either didn't own quota, or if it did own quota, it hasn't qualified as quota at that point, correct?

A. That's why I interpreted that, yes.

Q. Okay. So now if that producer today ships to an Arizona facility, and that Arizona facility is today regulated on the Arizona Federal Order, but if your proposal was adopted, and I think there was some testimony about this from Mr. Hollon, it is instead regulated on the California Federal Order. That plant's milk, whether it's received from Arizona or California, non-quota milk, because that's what it was, will be all credited at the overbase price, correct?

A. I'm not sure about that. I mean, we have performance standards in there that would dictate which plants are and aren't pooled on the California order, but I'm not sure how that meshes with your question.

Q. Okay. So -- and I know you are not, at least that's why I asked the question earlier if you are coming up again and which witness you are and all of that. And I know you didn't talk about the pooling provisions and I'm not trying to overlap them here. But assume for a moment that such a facility would meet the performance standards of the California Federal Order under Section 7. And today it is regulated under Arizona, but because of the new California Federal Order, will instead be regulated on California. Do you understand that so far?

A. Yes.
Q. Okay. That plant today, let's say it receives milk from two dairy farmers, one farmer from Arizona and one farmer from California who owns no quota. Today, that handler accounts to the Arizona Federal Order pool and its producers are paid the Federal Order blend price in Arizona, correct?

A. Okay. Yes, I guess.

Q. And if my hypothetical is correct and instead, the plant after adoption of the California Federal Order, meets the performance standards under Section 7 and is regulated under the California Order, the credit for the handler will instead be on those two producers, the overbase price for the milk, correct?

A. I believe that would be correct.

Q. And the California pool will, therefore, gain the difference between the credit on the overbase price and the minimum price for the milk at the plant blend, at the plant values, correct?

A. Would the gain include a loss?

Q. If the prices are a normal relationship and it is a pool distributing plant Class 1, isn't that new revenues for the California pool?

A. Sorry, didn't link in Class 1 part. Yes.

Q. Now, I asked the question earlier of Mr. Wegner, and I'll ask the same of you, are you a witness to whom I should discuss 1000.76, partially regulated, or is there a witness I
should discuss that issue with?

A. I'm pretty sure that's not me.

Q. I wouldn't call that a leading question, but it certainly had a leading answer. Okay.

So that section was really designed to tie in with Ms. Hancock's section, so I will change subjects now.

JUDGE CLIFTON: So, Mr. English, I think I understood, but what you are saying is if, if as a result of Proposal Number 1 there's more value in the pool, that's going to help quota holders? Is that your question?

MR. ENGLISH: I think it was -- it's more than that. It's, in essence, that out-of-state milk is going to be treated different differentially than it is today, and that differential treatment inures to the benefit of in-state dairy farmers.

DR. ERBA: You know, if you had said that, we could have been done with this section 20 minutes ago.

MR. ENGLISH: Would you agree with that?

DR. ERBA: I think that wasn't --

MR. ENGLISH: You would agree with that?

DR. ERBA: I think that's an accurate description.

MR. ENGLISH: Fine. Sometimes you got to lead to explain it. Thank you, your Honor, for explaining it.

JUDGE CLIFTON: Together we are making progress.

BY MR. ENGLISH:
Q. So let's talk about the history here a little bit more of what happened and why. And turning to page 4, it maybe simplify it a little bit for me, in essence, what California had prior to the adoption of the Gonsalves Milk Pooling Act, was classified pricing without pooling; is that correct?

A. That is correct.

Q. Okay. And as with the history of federal orders, you can have classified pricing, but without pooling, that created economic incentives that you have described as destructive competition, correct?

A. I think I called it destructive marketing practices, but I think it encompasses the same things.

Q. All right. Now, when you say on page 5, the second to the last paragraph, that "early efforts to establish a revenue distribution program were not successful because the producer community could not agree on the basic concepts of the program," by revenue distribution program, you effectively mean pooling, correct?

A. That's right.

Q. Okay. And when you say "the producers could not agree on basic concepts of the program" that's because those producers who had contracts for Class 1 that they thought were secure, didn't want to give up the value of that Class 1 milk, correct?

A. Well, since I wasn't born when this was all happening,
I would say that from the history, that, yes, that is exactly what the problem was.

Q. And so effectively, the negotiation -- yes, thank you for pointing out that you are younger than I am.

A. I know there was some question about that.

Q. You wanted to clarify that?

A. Yes, I did.

Q. So effectively, the Gonsalves Milk Pooling Act was the compromise that brought those people with the Class 1 contract, those dairy farmers with the Class 1 contracts, to the table and agreeing to pool it, correct?

A. That is correct.

Q. And so that is why, once it was adopted, there was a fairly direct tie between quota being issued and Class 1, correct?

A. Right.

Q. Okay. Thank you. So turning to page 6, and I had a couple questions that literally are just trying to, in my mind, clear things up, because I may have been alive, but I wasn't in California practicing milk law at the time.

The producers had the choice, I think it was the producers choice between taking July 1966 through December '66 for the '67 calendar year?

A. Yes, I believe that's correct.

Q. And was that effectively a choice that would give them
the higher of whichever those two were?

A. Yes, I think that's correct.

Q. A rational, a rational dairy farmer would have chosen
the higher of those two numbers, correct?

A. I think so, yes.

Q. And then the pool was established at 110 percent of the
Class 1 usage. Now, was the 110 percent of the Class 1 usage
as of the 1967 or was it 110 percent of whatever those
producers picked and they added them all together, and then you
multiplied that by 110 percent?

A. Well, you said pool, and not pool quota, and I'm pretty
sure that's what you meant, pool quota. I believe it is what
-- now that I have corrected you, I've forgot what I was going
to say exactly, but yes, I believe it was the 110 percent of
whichever those numbers they picked from those two periods.

Q. So, in essence, it really it was more than 110 percent
of Class 1, wasn't it? If you, if everybody picked the higher
of their volumes between July of '66 and December of '66 or the
calendar '67, wouldn't that almost sort of the sum of those
numbers, picking the higher of, be greater than the actual
Class 1?

A. Seemingly, yes.

Q. Okay. And in which case, the 110 percent would
actually be, when you multiply all of that, it is probably more
than 110 percent, correct?
A. I think so. But I have to assume that the people at the time knew what they were doing. Seems funny we look back on it now, but obviously it worked at that time.

Q. Now, on page 10 -- and I just got lost -- you are talking about the RQA's. And you say in the middle of that first full paragraph on page 10, "the RQA's actually return revenue to the pool."

And when you say it returns revenue to the pool, which pool do you mean, the quota pool or the total pool?

A. Total pool.

Q. Okay. So is that byway of saying when you take the $1.70, but if a producer is in the minus 27 cent zone for all of its quota value, for all its quota pounds, that 27 cents gets put back into the pool?

A. Well, they actually never get it.

Q. Sorry?

A. They never get it. It is -- when they get paid out, they don't get paid $1.70 and then put money back in, they just don't get the full $1.70.

Q. For accounting mechanism, they would initially get accounted for $1.70 and subtract 27 cents, that adds to the overall pool?

A. Right. So if you were take all the RQA's and set them at zero, the entire pool value would go down, which means the quota price and the overbase price and the base price would all
go down.

Q. Okay. And you talk about, on page 11, that location differentials based solely on quota milk were no longer able to ensure that adequate supplies, milk supplies, were made available to Class 1 plants.

How could all that link to the RQA's?

A. The location differentials were a precursor to the RQA's, and location differentials were either deducted from or added to quota payments, depending on where that quota milk was shipped. So when, as I said in that paragraph, as overbase became a larger share and quota milk was no longer able to ensure adequate supplies, they got rid of the location differentials and replaced it with transportation allowances and regional quota adjusters.

Q. But as you say, the RQA's do not provide direct incentive to move milk to Class 1 plants?

A. That's correct. The transportation allowances provide some of that incentive. The RQA's, I think you can look at this, I don't know if this is exactly correct, but I would look at it and say the folks who are in areas that were furthest away from those plants, were accustomed to getting a location, a negative location differential, and when those went away, they replaced them with RQA's, which were just an automatic ding depending on where you were located, regardless of whether that milk actually went to that plant or not.
Q. You said it was an automatic ding, it doesn't actually have an economic impact of whether or not you were going to move the milk?

A. Right. That's why it becomes even more difficult to explain its existence, but it's kind of like we're used to getting a ding, so we just put in something -- the system put in something that replaced the ding essentially at the quota price, depending on location of the farm.

Q. So on that, along that line for a moment, turning to page 14, at the top under Producer Responsibility, you say, "although producers have gained considerable independence, they are still charged with responsible performance standards."

Now, when you use the phrase "performance standards" on page 14, how do you use that term?

A. Performance standards is, are you, as a quota holder, and a dairyman with quota, are you doing anything that would service the market? That would be the performance standard I was talking about.

Q. Okay. Now, do you understand that the term performance standards has a very specific meaning under Federal Milk Marketing Orders?

A. I understand that to be the case, yes.

Q. And that in Federal Milk Marketing Orders it normally means supplying the Class 1 market directly or indirectly. Do you understand that?
A. Yes.

Q. Okay. Now, the producer, in order to maintain quota as we discussed a little while ago, must ship milk to a pool handler at least once every 60 days, correct?

A. Correct.

Q. But a pool handler is much broader than a pool distributing plant, a fluid milk processor, correct?

A. Correct.

Q. So there isn't actually, in the California system, a performance standard to ship the Class 1 processors as we understand that term in Federal orders, is there?

A. It's not equivalent, that is for certain. But there is a performance standard such that the shipment every 60 days to a pool handler, and that a pool handler in this case is a plant that has direct, or derived Class 1 or mandatory Class 2 utilization, so it is a very low threshold.

Q. What do you mean by direct or derived?

A. So you ship to a plant that actually is producing a Class 1 product, or a plant that diverted to another plant that is producing Class 1 or mandatory Class 2 product.

Q. Which is a little similar to the Federal Orders?

A. It is a little similar, but it is a very low threshold.

There's no volume --

Q. No volume at all.

A. -- no volume associated with this. It could be
literally a bucket full of milk every 60 days.

JUDGE CLIFTON: Well, we got to fix that.

BY MR. ENGLISH:

Q. I agree, your Honor.

So turning back to quota, and you have a nice discussion of the changes over time, and the opportunity to gain quota, but when I look at Exhibit 43, I'm sorry, I don't have Exhibit 43, I apologize. Just one second. You did have a lot of material here.

A. Thank you?

Q. I didn't say what the quality of it was.

A. That was not very nice.

Q. It wasn't also -- it was a neutral statement, Dr. Erba.

A. Shall we ask --

Q. Oh, it is excellent material.

A. Oh, I wanted to ask the Judge if she wanted to weigh in on your neutrality.

Q. Under Exhibit 43, Exhibit 4.D, if you go to the total quota Exhibit 43, Exhibit 4.D, well table, Table 3. Table 3. I believe at the bottom it is labeled Table 3 in your very excellent material.

A. Are you trying to make up for your earlier comments?

Q. Absolutely.

A. Okay.

Q. Is it working?
A. Very much so.

Q. In 1995, the total quota is 2,215,945 pounds, correct?
A. Correct.

Q. And it goes up and down a little bit. And in 2015, it is 2,215,988, correct?
A. Yes.

Q. Which is basically 43 pounds more in 20 years, correct?
A. Sure. I have done the math, but it looks about right, yes.

Q. So, and I do appreciate all the history, but all that history being there, nonetheless from 1995 to 2015, there's no statistically meaningful difference between the quota that was in 1995 and that in 2015, correct?
A. I think that's an accurate statement, yes.

Q. Now, would that be because Class 1 and Class 2 have not increased as a total volume within the California system?
A. Yes, that's correct. And that's something covered in my testimony earlier, that the comparison now for issuing new quota is linked to the highest period, which would have been 1990, 1991, and has not exceeded that level since that time.

Q. On page 21, actually, let me divert, so to speak, for a second.

And look at Exhibit 43, your 16-page Exhibit 4.D does not have a, I don't believe it has a separate table number.
A. No, it does not.
Q. Okay. What is the significance, if any, when I, when I look at the sales without cows as opposed to the sales with cows? Do you have a quick explanation as to why the value would be lower for sales with cows than sales without cows?

A. Well, most of the sales recently have not included cows, which you see as you go through the exhibit itself, that they rapidly grow smaller and you very rarely see a transaction that would include cows.

Q. And I accept that, I guess I looked at the first five or six pages, and I hadn't gotten so far.

A. Right. But I believe what it is is if you buy the cow with the quota, the cow price and the quota price somehow are figured together where there's some slight discount to the quota price is how I would determine. If you want to buy the quota separately from the cows, it's a higher price.

Q. As an Economist, would you then look at the sales without cows as being sort of a more representative value since it is delinked?

A. Yes, I would say that. And again, most of the sales have occurred recently without cows.

Q. Is there a particular reason quota has tended to follow dairies as they relocate in the Central Valley, as opposed to being sold without the cows?

A. Yeah, I think so. I think what you could say is that the folks that own, the producers that own quota see the value
of quota, and it does provide a good and stable return on their investment if they bought it. If they were just granted it, even better. I mean, that return on their very small investment. So it does not surprise me that the quota moves as dairy farmers move, although you will get the occasional producer who, for one reason or another just decides to sell part of their quota or all of their quota. But I think for the most part, they recognize it as being a good investment and provides a good return to them.

Q. So just a couple questions. You referred to --
A. Are we done with this exhibit?
Q. Yes, we are. Thank you.

You have discussed both the California statute and the language from the 2014 Farm Bill. And you reached some conclusions, I objected, and your attorney persisted, and that's fine.

I'd just like to ask you to note, because you actually said it a couple of times, the California provision has additional language after recognize, and it says, "not in any way diminished," "quota value shall not in any way be diminished", correct?
A. I'm sorry, is there a place I should be looking here?
Q. Well, you could look at page 2, where you say, "in fact, paramount to any consideration of the California Federal Milk Marketing Order, FMMO, was the assurance that the quota
program would not in any way be diminished." And you, I think in another place, have actually quoted from the statute, and maybe that's back on --

A. Middle of page 3? Are you talking about the California?

Q. Yes.

A. Yes, middle of page 3.

Q. "Shall not be diminished. Recognized and shall not be diminished." Correct?

A. Yes.

Q. Okay. The language "shall not be diminished" is not in the Congressional Enactment, is it?

A. I don not believe that -- the only place I have seen it is in the Food and Ag Code. Now --

JUDGE CLIFTON: If I could ask, so going back to Ms. Hancock's concerns, does this particular code, Dr. Erba, suggest to you that that term "shall not be diminished" would also apply to the exempt quota?

DR. ERBA: It would be hard to say that it does not.

MR. ENGLISH: But my point, your Honor, again, is that that language doesn't appear in the Congressional Act.

JUDGE CLIFTON: I know, but we were dealing with a California statute here.

MR. ENGLISH: I understand.

DR. ERBA: Can I also add that diminished doesn't refer to
value, it's amount. So if you have --

JUDGE CLIFTON: Oh, that is --

DR. ERBA: -- ten units, you still have ten units.

JUDGE CLIFTON: I see. So there's a -- so the amount, the
number of units of quota has remained constant throughout?
Well, except when new producers come on, they can get quota.

DR. ERBA: Not anymore. They have to -- it's in my
testimony, but there's a comparison done every year to see if
any shall be issued, and none has been issued since 1992. So
if you are on the waiting list, you are still on the waiting
list.

MR. ENGLISH: Your Honor, I merely point out that the
language he is got on page 3 says that "all pool quota must be
recognized and shall not be diminished." It doesn't parse it
the way he just did, but we can get into that, I am not trying
to get a legal fight, I just wanted to point out the language
"shall not be diminished" does not exist in the Federal Statute

JUDGE CLIFTON: Right. But it's an important word here.

MR. ENGLISH: I agree, and it's missing from the
Congressional Enactment. And, your Honor, and I know
Mr. Vlahos, if you want to have a quick conversation with me
about this, but this witness has discussed some issues and not
others. For instance, the issues with respect to pricing and
things like that, and on the one hand, counsel could say that
it is beyond the scope of direct for me to go ask questions
about that. On the other hand, I would then, under 801(a) 
rule, Federal Rule of Evidence, be entitled to put in 
statements made. And out of fairness, I thought I would ask 
the witness the questions about that, rather than simply in our 

And so if that's okay with Mr. Vlahos to go in that 
direction, that's how I propose to proceed.

MR. VLAHOS: Mr. English, for me to say whether it is okay 
or not okay, I really have to kind of understand it. So would 
you mind articulating again, because I don't quite follow it.

MR. ENGLISH: As with witnesses before, CDI and Dr. Erba 
have provided testimony and post-hearing briefs to CDFA about a 
number of the issues that are identical to the issues in this 
proceeding. Those are party admissions under 801(a) and they 
are, therefore, admissible regardless of whether I

cross-examine this witness.

What I propose doing, is rather than simply putting 
them in my case-in-chief and then forcing Dr. Erba to come back 
or otherwise, I propose asking him those questions now and 
giving him an opportunity to explain or respond even as 
Mr. Beshore had Mr. Wegner do yesterday, rather than having 
been off the stand, and three weeks from now as part of our 

That's what we propose to do.

JUDGE CLIFTON: So let me ask you this, Mr. English. The
reason you didn't just go ahead and do it, is that when you
were dealing with Mr. Wegner, the subject matter was the same.

MR. ENGLISH: Well, he had already, Mr. Beshore had opened
the door by asking questions about competitive situations. I
would, I immediately say that Dr. Erba has not done that in
this testimony, so I'm trying to be -- instead of simply going
into it, I'm pointing out that this is different in that
respect. And I could have simply sat down and asked no further
questions, and three weeks from now come up, and under Federal
Rule of Evidence 801, simply put the statements in the record.

I'm trying not to do it that way, precisely because
that strikes me as a little bit by ambush. And so, you know,
here I am prepared to do it with the witness on the stand.

MR. VLAHOS: Well, Heaven forbid that you ambush us. But
could we -- would we be able to see in advance what you propose
to show Dr. Erba?

MR. ENGLISH: Well, no, and you wouldn't see them in
advance if I simply put them in my case-in-chief, and it sort
of destroys the cross-examination, so no.

MR. VLAHOS: That was the point. Let Mr. Beshore and I
mull over this for a minute or two.

JUDGE CLIFTON: I think a break would be lovely. Let's
see, please be back and ready to go at 3:03. 3:03.

(Whereupon, a break was taken.)

JUDGE CLIFTON: Back on record at 3:06. Mr. Vlahos?
MR. VLAHOS: Yes. In our discussions during the break with Mr. English, we have said it is okay to go ahead with this now. That's not to say I may have objections to any exhibits or on the testimony, but in terms of okay to go ahead with the examination, I agree.

JUDGE CLIFTON: Thank you. And Mr. English, I very much appreciate your method of acknowledging what rules are and explaining why you are doing them, and giving people the option, and in such a way that I had to rule on nothing. Thank you.

MR. ENGLISH: A break helped too, your Honor, but yes, thank you. And I thank Mr. Vlahos and Mr. Beshore.

BY MR. ENGLISH:

Q. Dr. Erba, this is not your first day at this hearing, correct?

A. That is correct.

Q. Okay. And so you have already seen a little bit of this where I ask questions about what people have said before?

A. I have seen that, plus some other things, yes.

Q. Are you sure your dairy farmers really want to do this?

One of your many job duties at CDI is to prepare testimony and appear at CDFA hearings; is that correct?

A. I have done that, yes.

Q. And to offer post-hearing briefs; is that correct?

A. I have done that, too.
Q. Do you recall a hearing in the late fall of 2009 with respect to Class 1, 2, 3, 4a and 4b pricing?
A. I do.
Q. And did CDI offer an alternative proposal at that proceeding?
A. Well, if you've got documentation that says we did, we probably did. Although I couldn't tell you exactly what it was.
Q. All right. Do you recall over a number of proceedings, making a statement either asking for a hearing in the transcript, or in a post-hearing brief, along the following lines:
"CDI's proposed changes are consistent with objectives stated in previous hearings. The Class 4a formula should reflect the most currently available cost-justified changes."
Is that a sentence, a statement with which you are familiar?
A. Yes.
Q. And you agree with that?
A. Yes.
Q. Okay. "This applies to not only the manufacturing allowances for butter and nonfat dry milk, but to the FOB price adjuster for butter as well."
Do you remember making that statement?
A. Yes.
Q. Thank you.

A. You're welcome.

Q. It will go easier that way.

Now, after that proceeding in 2009, and we have heard some testimony about the CDFA process. Did you, on behalf of CDI, a file a post-hearing brief?

A. That's not a usual practice, but I may have.

MR. ENGLISH: Your Honor, I have handed the witness, the court reporter, and yourself, and Ms. Vulin is now passing out copies of a two-page letter on California Dairies, Inc., letterhead, dated November 11th, 2009, addressed to Mr. David Ikari -- we have heard his name before -- I-K-A-R-I -- Chief of the Dairy Marketing Branch, RE: November 9th Class 1, 2, 3, 4a and 4b Hearing -- Post-Hearing Brief, purported to be signed by Dr. Erba.

And I would like to ask for this document to be marked.

JUDGE CLIFTON: Will this be Exhibit 44?

MS. FRISIUS: It will be.

JUDGE CLIFTON: It will be Exhibit 44. You may mark your copy as Exhibit 44.

(Thereafter, Exhibit Number 44 was marked for identification.)

MR. ENGLISH: And your Honor, we got this off the CDFA website. Dr. Erba, do you recognize this document?

DR. ERBA: It looks familiar.
BY MR. ENGLISH:

Q. Does that mean you wrote it?

A. Yes, I did write this.

Q. And you submitted this to CDFA after the hearing, correct?

A. Yes.

Q. Could you read the paragraph that is the last paragraph of the first page, carrying over of the next five lines of the next page, please?

A. The entire paragraph.

Q. Yes, please.

A. Sure.

"Why not increase Class 4a and 4b prices? One panelist asked for -- asked for an explanation as to why Class 4a and 4b prices should not be increased to give producers more revenue. Another question was asked as to why Class 4a and 4b prices should not be raised to equal the Federal Class III and Class IV prices. While the questions were not asked of me, I would like to amplify the explanation provided in my testimony. First, Class 4a and 4b are market-clearing classes of milk and process 75 percent of the milk produced in California. The products from these plants compete in national and international markets where price is a dollar consideration for buyers. The California dairy industry is wholly dependent on continued operation of its manufacturing facilities. To burden
these plants with higher minimum prices that cannot be extracted from the market, even for a brief period, would have potentially devastating consequences. From our own perspective, higher minimum prices for Class 4a would put California dairies at an immediate disadvantage in trying to sell products domestically and internationally, leaving us no option but to sell products at a loss. In addition, because nearly all butter and powder processing facilities are owned by producers, a Class 4a price increase only functions to redistribute money inequitably among different producer factions. Money would simply flow from the producers who have made investments in processing facilities, to those producers who have not.

Q. Thank you, sir. Your Honor, I move admission of Exhibit 44.

JUDGE CLIFTON: Does anyone want to question the witness before determining whether you have an objection? No one. Is there any objection to the admission into evidence of Exhibit 44? There is none. Exhibit 44 is admitted into evidence.

(Thereafter, Exhibit Number 44 was received into evidence.)

BY MR. ENGLISH:

Q. Dr. Erba, I don't want to belabor the record, but there's other hearings, and you would agree that you made
similar statements, say for instance, back in 2007, as in the
2009 statement, correct? As your brief?

A. I think, correct, although there was a period where I
was not able to participate in hearings, and I'm not sure which
2007 you might be referring to, but if it has my name on it, it
is probably mine.

Q. I'm referring to September 26, 2007, and a statement
with your name on it.

A. Yes, that would have been past my eligibility period.

Q. So let's -- since you said that, why don't we, for the
record, clear up what that means.

You were -- you had been an employee of CDFA before you
joined California Dairies, correct?

A. Correct.

Q. And so for some period of time after you joined CDI,
because of Rules of California or the agency, you were not
eligible to be the person participating in those proceedings;
is that correct?

A. That is correct.

Q. And that is what you meant by your eligibility period?

A. That's correct.

Q. Okay. Now, there's been a fair amount of testimony
with respect to the most recent proceeding held with CDFA, for
CDFA, in June of this year, correct?

A. Yes.
Q. And did you participate at that proceeding?
A. I did.
Q. And you testified?
A. I did.

JUDGE CLIFTON: If you do not yet have a copy of this portion of a transcript, would you raise your right hand so one could be given you? It appears they have been distributed. Shall we mark this as Exhibit 45?

(Thereafter, Exhibit Number 45 was marked for identification.)

MR. ENGLISH: Yes, your Honor, I'll describe what it is, please. This is a portion of the transcript with the cover sheet, State of California Department of Food and Agriculture Dairy Marketing Branch, Consolidated Public Hearing to Consider Amendments to the Stabilization and Marketing Plans for Market Milk for the Northern and Southern California Marketing Areas, California Department of Food and Agriculture, Sacramento, California, Dated: Wednesday, June 3rd, 2015.

And we have attached the pages of the entire testimony of Dr. Erba from page 107 to page 123. And I would like you to turn to page 110, Dr. Erba. And while I am most interested in the lines 22 through 24, in fairness, why don't you read the entire paragraph that starts on line 22 page 110 and runs through line 7 of 111.

DR. ERBA: Line 7?
MR. ENGLISH: Line 7 of 111.

DR. ERBA: "An acceptable level of price difference exists for most of the classes of milk when comparing California milk prices to Federal Order milk prices. The exception is Class 4b, and it is past time for the appropriate adjustment to occur. We believe a modification to the method for valuing whey in the Class 4b formula would not only restore equity in what our manufactures pay for milk relative to comparable manufacturers around the country, but would also generate much needed additional revenue for dairy farmers who are facing some of the lowest milk prices seen since 2010."

BY MR. ENGLISH:

Q. Thank you. Now, when you provided this testimony in June of this year, the Cooperatives had already submitted their proposal in February and the revised proposal in May, correct?

A. Yes.

Q. And by that I mean proposal to the USDA, correct?

A. Yes, that's correct.

Q. And at that time, and contemporaneously in June, your testimony was that leaving aside Class 4b there was an acceptable level of price difference with classes of milk when comparing California milk and Federal milk, correct?

A. That had been the historical trend in California.

Q. Thank you very much, sir. That concludes my cross-examination. I move the admission of Exhibit 45.
JUDGE CLIFTON: Does anyone want to ask questions of the witness before determining whether you object? No one. Is there any objection to the admission into evidence of Exhibit 45? There is not. Exhibit 45 is admitted into evidence.

(Thereafter, Exhibit Number 45 was received into evidence.)

MR. ENGLISH: Thank you, Dr. Erba.

DR. ERBA: Thank you.

JUDGE CLIFTON: Who will next cross examine Dr. Erba?

CROSS-EXAMINATION

BY DR. SCHIEK:

Q. William Schiek, for the record.

A. Dr. Schiek.

Q. I just have a few clarification questions on the testimony that you gave today.

A. Okay. Are you talking about Exhibit 42 testimony?

Q. Exhibit 42, that is the one.

A. Thank you.

Q. Just to make sure I understood what you were referring to on page 3, starting, let's see, five lines down, you said, or what was written here anyway, "any production in excess of a signed quota constituted overbase production." Is that correct or is it assigned quota and base?
A. Quota and base. Did you see how much trouble I got into when I tried to add base a few moments before that.

JUDGE CLIFTON: I know, but I think we should do this.

DR. SCHIEK: I just wanted to make sure I was understanding it.

JUDGE CLIFTON: I really do think we should do this. So I'm going to ask Ms. Frisius to pull out her Exhibit 42, and let's first go page 3. Let's go to page 3, and on that second line, should that be "quota, base, and overbase?"

THE WITNESS: Yes.

JUDGE CLIFTON: All right. And should it similarly be shown where Dr. Schiek has just shown us, which is on line 5?

DR. ERBA: 5.

JUDGE CLIFTON: And if so, would you read that sentence for us, Dr. Erba?

DR. ERBA: Sure.

"Any production in excess of assigned quota and base, constituted overbase production."

JUDGE CLIFTON: All right. So I would ask that the record copy show those additional two words in line five, as shown by Dr. Erba. So "and base" will be inserted in between quota and constituted. All right. Thank you. Dr. Schiek, back to you.

BY DR. SCHIEK:

Q. Okay. On page 8, under the section, Determining Pool Prices after 1994, I guess I'm -- this is just a question. By
the late 1980's, overbase milk production had increased considerably in relation to quota production. What, I was just wondering if you had a comment on what was driving that increase in overbase production?

A. Well, that's a good question. I would suggest that the introduction of the pool program in general for that 20-year period, approximately 20-year period, was a big driver into stabilizing prices and stabilized prices led to higher milk production. If there was something in the '80's other than the occasional bump up in prices that would have caused this, I couldn't tell you without looking at some data. But I think that's probably the underlying foundation for that increase.

Q. Do you think that perhaps the increase in support price, CCC purchase prices, was a driver as well?

A. Well, in the late 1980's -- hmm -- don't know about that. Maybe.

Q. Okay.

A. Seems awfully late to have an increase.

Q. You are correct. You are correct. Thank you.

Page 13, I think second paragraph, one, two, three, four, five, lines down. You mentioned four operating exempt, operating option exempt PD's, and I count five. So I want to make sure that it's one or other, unless there's one that's closed. But I have one in San Bernardino County, one in San Diego County, one in LA County, and one in Fresno County,
and one in Stanislaus County.

A. One of the Southern California ones is not anymore.

Q. Okay.

A. And that --

Q. That's new information for me, thank you.

A. Yes.

Q. Okay. Page 16. By the way, I want to unequivocally say thank you for all this history on the quota program. I very much appreciate it. I thought it was very helpful.

A. You're welcome.

Q. Page 16, that first paragraph at the top, you're talking there about, I guess the last line of that paragraph, "in addition, any quota that has been forfeited after April 30th, 1981, is allocated on a continuing basis to qualifying new producers." And I guess the question is, how -- based on your impression, does that happen very often? Does quota get forfeited or is it usually sold before --

A. It is usually sold. I can't -- I was there for, as I indicated, eight years, and I never had an instance where it was forfeited and I don't know that there are any recently. Because of the value, I think it makes a whole lot more sense to sell it before you forfeit it.

Q. It would probably be a major oversight if someone forfeited it?

A. I would think so. I would think so.
Q. Page 17, last paragraph, "published average price per pound of quota solids not fat, without the inclusion of cows, reflects the true value of the quota sold." And I'm -- I want to make sure I understand what you are referring to here. Are you referring to market value of the asset at that point in time, or are you referring to the sort of intrinsic value in use?

A. That would be the market value, the former of your statements, and I'm trying to distinguish that from the cows without quota, cows with quota.

Q. Okay.

A. Kind of like what we talked about with Mr. English earlier.

Q. Okay. Thank you. Page 18, in this paragraph you talk about first year alone, 342 producers sold at least some quota, 624 producers bought some quota, and 273 transactions disbursed a hundred percent of producers quota, and then you talk about a certain number of pounds were transferred.

I just want to make sure, is there a distinction between transfers and sales of quota? Or -- I'm looking at those two as the same, but am I wrong on that is?

A. No, that's -- no, you are correct.

Q. Okay. Just wanted to make sure. Page 19, and also you might want to open up Exhibit 43. And I think it is -- well, it is just the one that says Exhibit 4.B on the bottom, it is
the quota transaction list.

    A. Yes.

    Q. Okay. So the first question is, are these average prices, because you are graphing the average selling price per quota, and then you have got, there's an average on this table with a low and a high listed for with cows and without cows. Is that average a simple average of all transactions or is it a weighted average?

    A. No, it is a simple average.

    Q. Simple average?

    A. Yeah.

    Q. Okay. So that then the average selling price per quota in the chart is, is that a combination of the with or without cows or is it --

    A. No, this is only without cows.

    Q. So this is without?

    A. Did not include the with cows, this is only without cows.

    Q. Okay. Looking at that chart again, and there's a lot of movement in it, kind of starting back in the '70's, but I'm more interested in the period say from the 90's forward. There's a lot of gyrations here sometimes, and particularly this drop in from the mid '90's down to the late '90's in the selling price -- looks a little bit like my 401k does sometimes. What drives that?
A. Well, there's a number of things I would think, and I wouldn't say they all combine together, but they are certainly considerations. For one thing, what would be the milk price at that time and what are the margins at that time. That would affect it. What are the discussions in the industry, which is probably as big an effect as anything as the continuation of quota, shall we keep it, shall we not keep it.

There have been some committees appointed to looking at this, and it seems like when those committees convene, the price reacts. Sometimes positively, sometimes negatively. And that would have an effect as well.

Q. Okay.

A. General health of the dairy industry would be another aspect of that. Do I see future as a dairyman in the dairy industry or do I not?

Q. So you had reported a little bit earlier, or actually, maybe later in your testimony, but what when you entered this statement earlier today, you talked about the provisions in the mid-'90's I guess, where it allowed option exempt PD's to exempt quota that they had purchased in a particular time period. Could that have been a factor influencing the demand for quota and driving prices maybe a little bit higher during that period?

A. I won't say it's not, but it was a fairly short period of time, and if there's any effect that you would see in this
graph, I think it would be fairly small. Some of these big ups and downs are a period of a year or two, and I wouldn't think that the amount of time involved with the additional exemption, plus the volumes that we're talking about, I don't think they would affect this very much.

Q. Okay. When you talk about producer margins as an influence there, is that pretty much a function of funds that producers have available for quota, and are you, is it your contention that during times when margins are tight, dairymen don't have the funds available to purchase more quota? And after a period, maybe a good period, they have more money to use to purchase quota?

A. In general, I think that's accurate. Although you -- you will find producers sometimes taking the opposite of what you just said.

Q. It's a good time to sell quota, too.

A. Or a good time to buy it. If it happened to be low price and there are people who are dairymen who are selling it, maybe if I have the ability, it may be a good time to buy it. So maybe the price is better than it would be a year from then or a year earlier. So I think you get all kinds of -- as you can see from that list on on Exhibit 4b, the transactions happen every month, and there's a lot of them. I don't know that you can make a general statement about what's causing all that.
Q. Thank you. Moving on to, I would like you to look at page 21 of your Exhibit 42. And just to make sure I understand the percentages and what they refer to here, when you say percentage in parentheses under the title of the table, it says, "percent of quota relative to milk production." Is that, I guess as I look at this, my understanding is that that's total California milk production, is that right? Or is this individual milk production or -- so when you say over quota, for example, over 80 percent, and you have a figure under 1995 of 11 percent, that means -- does that mean 11 percent of all the quota, 11 percent of -- what does the 11 percent number stand for?

A. That's the percentage of dairy farms.

Q. Okay. So there are 11 percent of dairy farms that own or have over 80 percent of their milk production covered by quota?

A. Yes.

Q. Would that be the way --

A. I think that's an accurate description. It's a table that's, it's important, it's generated by the Department of Food and Agriculture every month. And these numbers, although their table doesn't look quite like this since I condensed it some, but this is a representation of what -- what that data looks like.

Q. Okay. So I am comparing now, the numbers on this
table, particularly the line that says number of dairy farms. And Table 2 of Exhibit 43, which is Annual Milk Production by County. And if I look at Annual Milk Production by County for 1995, which will be the same year for which you reported 2,161 dairy farms, I come up with a total milk production. I assume that line, total milk production is total for the state?

A. Yes.

Q. Okay. So I come up with roughly 24.7 billion pounds, is that accurate in 1995, with 2,161 dairy farms?

A. Where did 24 --

Q. 1995 Annual Milk Production by County, if you read down there's total milk production it says, 24,671,402?

A. Yes.

Q. So you know, rounding that to a billion pounds, that would be about 24.7 billion pounds.

A. I thought you said 24.4.

Q. 24.7?

A. Okay.

Q. And during that same year there were 2,161 dairy farms.

A. Yes.

Q. According to your table. Then looking ahead to 2015, which you have an estimated production of 40.8 billion pounds for that year.

A. Yes.

Q. Is that right? And the number of dairy farms, 1,407?
A. Yes.

Q. And that number came from CDFA. Is that mid-year, beginning of the year?

A. Which number?

Q. 1,407 dairy farms?

A. That's from January's, the January report for 2015.

Q. Okay. So is it a fair statement to say that even though dairy farm numbers declined fairly substantially from 1995 to 2015, milk production still grew fairly substantially?

A. Yes.

Q. Okay.

A. Yes.

Q. That's all the questions I have. Thank you.

A. Thank you, Dr. Schiek.

CROSS-EXAMINATION

BY MR. VETNE:

Q. John Vetne, representative for Hilmar Cheese Company. In your introductory remarks, before you started reading, you referred to yourself as a bit of a historian. I liked that.

A. A bit of a historian, that's correct, by default.

Q. I just have a couple of things, not a couple, honestly it's more than a couple. And I, too, loved your history of the quota program.

When it was -- when the quota program was first created -- I'm trying to dumb this down a little bit -- I'm
going to publish a yellow-cover jacket book called Milk Pooling for Dummies.

A. I'm sure it will be a big seller.

Q. When quota was first issued, the folks that were issued quota were those that had existing contracts with Class 1 milk dealers. Correct?

A. That's correct.

Q. And it was based on some portion, some representative period, choose the better of their Class 1 share of the market, correct?

A. Right.

Q. And prior to Milk Pooling, those producers were paid a plant blend price because regulated classified prices were regulated, but not market-wide pooling?

A. Yes, that's correct.

Q. And the quota that they were issued did not return to, in the early stage of the Pooling Program, did not return to the quota holders a Class 1 price, but rather something more akin to a plant blend where they received a Class 1 revenue plus some revenue from lower classes; is that right?

A. That's right.

Q. Okay. Do you know when it was first started in relationship of that Class 1 plant blendish, initial quota, whether the exempt quota and the regular quota had essentially the same relationship in the Class 1?
A. Oh boy, yeah, I don't really know that. I have not heard that asked about before.

Q. Okay. Nevertheless, at some point as years passed there was an expectation that more quota would be issued as Class 1 sales and Class 2 sales increased; is that correct?

A. That is correct.

Q. That was the expectation?

A. Yes.

Q. And there was perhaps after that time, some minor increase in Class 1 and 2 sales of milk produced in California, correct?

A. That is correct.

Q. And when that happened some additional quota was, in fact, issued?

A. That's correct.

Q. And there was some additional quota issued because farmers requested it without a corresponding increase in Class 1 and 2 sales, correct?

A. I think so, although that wasn't -- it was something I covered in my testimony, there's a period where they were equalized, and there was no corresponding increase in sales for Class 1 and Class 2.

Q. And that would dilute the value of quota relative to what percentage of Class 1 was represented in quota when it was first issued?
A. Right. So the additional quota without the additional
sales offset, would have diluted it, yes.

Q. Okay. Would it be fair to say that the current fixed
value of quota which we translate to $1.70 per hundredweight is
a further dilution compared to its value when the quota was
first issued?

A. I don't know if I can say it was a dilution. You know,
the quota price was -- the quota versus the non-quota price
moved around before 1994. And the fixed value stopped that
from happening. So sometimes that quota value was quite large,
and sometimes it was quite small, perhaps even negative.

Q. So, yeah, there was -- and happened actually more, in
years more recent than that, there has been some upside down
pricing, there was some upside down pricing where Class 1 may
have been the lowest, or one of the lowest classes?

A. Certainly not the highest class, I know that. I
wouldn't say it was the lowest, but I know it wasn't the
highest.

Q. And quota holders then, reacted with "that's not what
we expected."

A. That's correct.

Q. And where the price spread went the other way and the
quota price was really high, overbase producers would say, "we
didn't expect to receive this much less," would that be the
opposite side of the reaction?
A. Yes. Yes. They did not expect that to happen.

Q. Okay. You had referred in your testimony, and this is of interest to me, I have always heard of the words quota, base, and overbase. And I have been trained since I first heard those words in the mid-'90's when I attended the Dairy Institute School on Milk Pricing in California, I was told that there was no difference between base and overbase. Is it true that there one time was?

A. Yes.

Q. Okay. So there were, in fact, three prices at one time, higher quota, price; base representing the remainder of production volume at the time quota was first created; and then overbase, meaning production in excess of that volume.

A. Right, and they were paid, generally, in descending order. So quota at the highest, when you filled up the so-called quota buckets, you went to the base buckets which is, actually was a fairly small bucket, filled that up with the remaining value out of the pool, and the overbase took the residual. So there were three separate prices that were calculated.

Q. Okay. When there were three such separate prices, did the relationship between quota and overbase function in a way to discourage expansion in a way similar to the private base in overbase plans that we have discussed at this hearing?

A. I do not think so. I would not make that
characterization, no.

Q. Because the overbase, regulated overbase price was probably higher than would discourage expansion?

A. I think you can look at the history and see that the production increase California, despite having that quota based and overbase pricing.

Q. Okay. I'm Mr. Schiek asked you some questions about the things that drive values represented for transactions in quota up and down over the years.

A. Yes.

Q. And to me, it seems like one of the most significant driving factors would be interest rates return on investment. Wouldn't that be the case?

A. That would be maybe one the factors. There is clearly a, there's a value of money in there that may be a factor. However, I don't think that is a big enormous factor. There are other things, the ones that I mentioned to Dr. Schiek would probably be the ones that are prevalent in my mind anyway. So interest rates may have a place in this, but I wouldn't think a huge place.

Q. Quota values are, more recently, are relatively high compared to prior periods. And interest rates are pretty low more recently compared to prior periods. So let me ask you this, isn't the purchase of quota somewhat like the purchase of an income stream through an annuity?
A. Yes, I'd say that's accurate.

Q. Okay. And an income stream from an annuity, the annuity would cost a lot more when interest rates are low, than comparable stream of income when interest rates are high?

A. It could. Again, it could be a factor, but maybe a confounding factor. So other things are happening at the same time, these things are moving together, they are correlated but maybe now there's no direct relationship.

Q. Do you know of anybody that studied the relationship between quota prices and interest rates?

A. You know, I don't think I know anybody whose done that.

Q. Middle of page 10, word usage question. The sentence that ends the second full paragraph on page 10, "prior to computation of the weighted average small pool adjustment such as plant gains may be made." Is your use of the term "plant gains" synonymous with what Federal Market Administrators previously referred to as overage?

A. I'm not sure.

Q. Not sure. Okay. In that case, just what is plant gains mean for purposes of this testimony?

A. So there are adjustments made, and it has to do with how things are being reported by the handlers. And part of that would be what is determined by the Department of Food and Agriculture as a plant gain or sometimes a loss, and that comparison is something that they would do every month. So
that was something that has to do, is determined by the
Department of Food and Agriculture, and it's related to however
the, whatever the reports are that are being filed by the
handlers. Beyond that, I couldn't tell you exactly how it is
done.

Q. Okay. It may, plant gain my include adjustment there
for an obligation determined that was somehow left out of a
previous report?

A. It may be, I am not sure. That sounds like a logical
place for it to go, but I'm not sure that's the exact place
where I would look.

Q. In the section beginning at the bottom of the page,
"adjustments to quota value," you refer to location adjustments
or location differentials to move quota, quota milk to Class 1
plants. Were the location differentials in California similar
to the use in the federal system of the location differentials
when applied to producer milk, a different value from milk
delivered to different locations depending upon proximity or
distance to demand markets?

A. I have never actually seen these. I know that they are
pluses and minuses, it has to do with location of the receiving
plant, but other than that, I have never actually seen these.
They were out of the system by the time I got there. There's
another reference to age, I was in high school when these were
omitted. Deleted.
Q. This is the product of your historical inquiry, not your life experience.

A. That's correct.

Q. Okay.

JUDGE CLIFTON: Dr. Erba, what year did you graduate from high school?

DR. ERBA: Would you like to take a guess?

JUDGE CLIFTON: No.

DR. ERBA: 1983.

JUDGE CLIFTON: Oh my. So they held you back, right?

DR. ERBA: I think it's actually pretty advanced.

BY MR. VETNE:

Q. We talked about regional quota adjusters. The application of regional quota adjusters is based on an economic presumption that milk produced by farms located, let's say, close to say Los Angeles, San Bernardino, for example, or Riverside County, it is worth more there than milk in Tulare County, for example.

A. Again, it was a little difficult to figure out how exactly they were determined and applied, but I think in general you are going down the right path. And again, but my discussion earlier with Mr. English about replacement of the location differentials had a flavor of that, too. They are trying to preserve a historic action that occurred on the quota price.

1906
Q. Okay. If I were somebody who was eligible to purchase
quota, my income stream is better if my farm's in San
Bernardino County or Riverside County because the quota
payments are higher, correct?
A. If you, yes, if you had quota and you were located down
there, you would have the highest possible value associated
with quota.
Q. On the other side of the decision-making equation is
the fact that it cost more to produce milk down there than it
does in Tulare County, correct?
A. I think that's generally true, but I wouldn't say it is
universally true. Every dairy has its different cost of
production.
Q. And average costs are higher in the south than they are
in the north, correct?
A. They typically are.
Q. Would the growth of portion of quota in Central
California, in your opinion, be attributed to aggregate
decision making that it's, even though it's a reduced value,
it's a better reduced value in the Central Valley than 19.5
cents a pound in Los Angeles. Do you understand what I mean?
A. Not exactly. I think I'm almost there, but try me
again, please.
Q. As an Economist you observe market behavior of many
participants, and although some may make irrational decisions,
you assume that in the aggregate you can see a rational
pattern, correct?

A. Yes.

Q. So the growth of the portion of the pool that
represents quota residing with producers in the valley, could
you conclude that producers in the aggregate have decided it's
not worth it to own quota that produces only a little bit extra
in the RQA being down south?

MR. VL AHOS: Your Honor?

MR. VETNE: Am I being too obtuse? Okay.

MR. VL AHOS: Your Honor, there have been a lot of questions
of this witness asking what was in the mind of producers that
caused them to do something. And this witness doesn't, has
not, to my knowledge, surveyed all the producers, nor have they
phoned him or e-mailed him or anything. How can he answer what
motivated all these producers? There maybe economic guesses as
to why they do, but he certainly can't testify what their
reasons were.

JUDGE CLIFTON: Mr. Vetne?

MR. VETNE: I agree with Mr. Vlahos that he can't, you
can't guess or even foresee what happens in the mind of
individual farmers. But Economists can consider remarked
behavior and make rational conclusions about what motivates
aggregate market decisions. And that's my question.

JUDGE CLIFTON: If you want that kind of opinion, you will
have to give him more specifics, which I don't think really you
want to do.

MR. VETNE: Okay. Based on that, I probably don't want to
do it.

BY MR. VETNE:

Q. Are you familiar with -- with the publication entitled,
"Report to the Secretary of Agriculture by the Federal Milk
Order Study Committee," a committee headed by Dr. Nourse
published in 1962?

A. Yes.

Q. Commonly referred to as the Nourse report?
A. Yes.

Q. Have you read that?
A. I actually have.

Q. Yes.
A. A long time ago.

Q. But it was while you were at Cornell, right?
A. That's correct.

Q. Would you characterize that report as a credible and
reliable source of information concerning the evolution and
history of Federal Milk Marketing Orders, the situation that
caused the creation of them, their operation at the time the
report was written? You're a historian, I'm asking about
credible source.

MR. VLAHOS: I would object to the question if the witness
is being asked that each and every thing, statement, conclusion and opinion in that report is credible. If he's going to ask the report is credible, I want to know what parts of the report he's talking about, because some may be credible and some may no longer be credible.

JUDGE CLIFTON: Mr. Vetne, a lot has changed since the report was published. For what purpose do you want him to acknowledge this as some sort of authority? Is there a portion of it you want him to look at and see if he agrees with it?

MR. VETNE: Well, I do not want to go through that exercise, your Honor. He said he's looked at it. The Secretary of Agriculture, in various places has said they looked at it. And I did not ask him about whether it continues to -- a lot of time has passed. My question ended with at the time it was published. And he's read it. I assume if there's something in it that he thinks is not credible, which would be my next question, he would have noticed it and brought, and will bring it to my attention. But I'm looking particularly at, we have gone through the history now, of California. This is the first witness in detail that's discussed the history of California.

This is the kind of resource that will provide us with a comparative history of how things evolved in the Federal system so we can compare that side to side.

JUDGE CLIFTON: Do you have it here?
MR. VETNE: I have it in my computer, and it is available on Cornell and University of Wisconsin website. It is very long. I can make it available and the URL available to anybody, including the witness, if they want to look at it.

JUDGE CLIFTON: If it is very long, please pinpoint the sections you want him to consider in giving you an answer to your question.

MR. VETNE: I have no specific section.

JUDGE CLIFTON: Come on now, this is not helpful.

MR. VETNE: There is a long section, and Dr. Erba can help me, there's a long section there in that report about the disorder from the 1920's and '30's for which the Federal system was created. There are sections in there about how the government intervention dealt with that disorder, which classified pricing, classified pooling, and how they worked in 1962. Probably 70 or 80 pages is devoted to that.

But, you know, if that authority is not credible to an Economist who studied that publication as part of his studies at Cornell, and this record can't reveal whether the Economist believes it to be credible or not, we may have a problem.

JUDGE CLIFTON: I haven't let him respond to your question, so don't be presuming what his response is going to be.

Mr. Beshore?

MR. BESHORE: Well, I just want to point out, Mr. Vetne actually said that he's asking Mr. Dr. Erba to say what
portions of that 1962, you know, 150-page publication he might disagree with, for Pete's sake.

JUDGE CLIFTON: That's what I think for Pete's sake.

While we have got you stopped, Mr. Vetne, I believe, I remember that Dr. Nourse's name is N-O-R-S-E; is that correct?

MR. VETNE: N-O-U-R-S-E.

JUDGE CLIFTON: Thank you, and --

MR. VETNE: Edwin J, I believe.

JUDGE CLIFTON: And you mentioned your study at the Gary Institute. Would you spell Gary.

MR. VETNE: My study at the Dairy Institute.

JUDGE CLIFTON: Oh, you said Dairy Institute.

MR. VETNE: The Dairy Institute has offered courses in how milk is priced in California, I, at one time, took advantage of it.

JUDGE CLIFTON: All right. Good. That helps. You know, we could go off record while Dr. Erba looks at the report.

MR. VETNE: Let me go on to another publication.

JUDGE CLIFTON: Good. Thank you.

BY MR. VETNE:

Q. Are you familiar with a publication, going back to Cornell, entitled "The Evolution of Milk Pricing and Government Intervention in Dairy Markets?"

A. Sounds like something I co-authored.

Q. Yes. You co-authored that with Andy Novakovic?
A. That's correct.

Q. N-O-V-A-K-O-V-I-C, the C is pronounced like an H but

CH. Okay.

And in that publication, somewhat like I have described
for the Nourse publication, you and Dr. Novakovic provided
historical description of dairy markets in the United States,
chaos of the '20's and the '30's, and the evolution of the
federal milk order system, correct?

A. That is correct.

Q. And in that -- in that publication, for which I have
been grateful ever since, you provided a definition of
disorderliness, and I'm going to read it to you -- or actually
I'll give it to you and ask you to read out loud, paragraph on
page 6 of that publication, which is also available online. I
didn't produce a copy here, but let me give this to you. Would
you read out loud, please, that paragraph?

A. "Disorderliness, which refers to the lack of a
predictable, sustainable, and efficient flow of a product to a
specific market, ultimately led to the break down of dairy
markets." The whole thing?

Q. Sure.

A. Okay. "If fluid milk markets were to have orderly
supply, orderly production -- orderly supply, orderly
production was required which further depended on orderly
provisions for assembly and distribution. In addition, an

1913
orderly relationship between different markets in terms of price and supply was required. Without State or Federal governmental intervention, there was little chance of creating orderly marketing beyond the local level. The 1933 Agricultura Adjustment Act (AAA), sought to correct these failures in dairy markets by including provisions for milk and dairy products."

Q. That concludes the paragraph I asked you to read?

A. Yes.

Q. Okay.

JUDGE CLIFTON: Would you further identify the publication, Dr. Erba?


BY MR. VETNE:

Q. Published in 1995?


Q. Okay. Thank you.

A. My old friend.

Q. Turning to the definition of disorderliness that was used in this publication, is that a definition that you feel continues to be applicable to disorderliness?

A. I think it is helpful as a guide, although the way that it appears in that document was more descriptive of, again, what you have already pointed out, the history of the markets
and how government got involved with them. I don't think it is completely untrue today, but I wouldn't say that it is completely true the way it is today, it was back then.

Q. Okay.

A. That's a very tight definition to me.

Q. Okay. Can you --

JUDGE CLIFTON: A very what definition?

DR. ERBA: Tight.

JUDGE CLIFTON: Tight. Yes. Succinct, is that what you mean? What do you mean by tight?

DR. ERBA: I thought it was a good term to use, maybe not. Tight meaning it is very structured in the way it is laid out. And again, at the time it was, in the context it was discussed in that publication, it was applicable to the time it was, at the time of those markets and how they were functioning.

BY MR. VETNE:

Q. Let me see if I can interpret tight. By tight you mean under inclusive?

A. No, I don't think I would say that.

Q. You wouldn't say that?

A. I like -- tight to me means, what I meant to mean, was very structured.

Q. Is there a better definition, whether from a published source, preferably if you have one, but you can make it up as you go along on the witness stand, do you have a better
definition for me?

A. You know, I don't. And I have heard the term disorderly marketing used quite a lot in the last few days, and that seems to me everyone's got a different interpretation of what that actually means today. And I think, I don't think if you ask people in this room if that definition is correct and accurate, I doubt you'd get a hundred percent agreement.

Q. Okay. Thank you.

A. Besides, I think Andy wrote that section.

Q. Are you familiar with publication — actually, two publication in two parts by University of California Davis, which resulted from a committee deliberation, but authored by Bees Butler, called "Maintaining the Competitive Edge in California's Dairy Industry?" Are you familiar with that?

A. Yes, I read that about the time or shortly there after it was published, but that was quite a few years ago, as I recall.

Q. Okay.

A. But I am familiar, I've heard of it.

Q. Okay. During the course of your employment with CDFA or thereafter, has that publication been used to guide policy and application of regulation of milk and dairy products in California?

A. I don't think so.

Q. Okay. In 2007 there was something called the McKinsey
report. Are you familiar with that?

A. Yes.

JUDGE CLIFTON: Spell it for us please, Mr. Vetne?

MR. VETNE: Mc, K-I-N-S-E-Y.

JUDGE CLIFTON: K-I-N what?


BY MR. VETNE:

Q. And that report was also the product of a study group looking of dairy industry members, participants and stakeholders, looking at the California dairy industry?

A. Yes. A consulting group was hired to put together those two booklets that were turned out eventually.

Q. Okay. Do you know whether that publication has been used as a guiding or instructive document for either CDFA policy or participants appearing before CDFA?

A. In that broad description you just gave, I would say, yes. The McKinsey report, although it's name hasn't been mentioned all that much lately, was used quite a bit to initiate discussions among industry participants.

Q. Okay.

JUDGE CLIFTON: I know we haven't gone terribly long, but I need to move around a little, if we could. How about we take a 14-minute break and resume at 4:30? Okay. All right. Be back ready to go at 4:30.

(Whereupon, a break was taken.)
JUDGE CLIFTON: We're back on record. It is only 4:29, but we may as well get started again.

Before Mr. Vetne resumes his cross-examination of Dr. Erba, I wondered if anyone would like to comment on the possibility of Agribusiness Publications uploading exhibits prior to the time we actually have the official record copy on the USDA website.

Would anyone like to comment on that prospect and the difficulties entailed?

MR. BESHORE: Marvin Beshore. As long as they are the official exhibits, I don't have any view on it one way or the other. That's my comment. If they are the official exhibit documents, I think that's up to the government whether they wish to have them pre-published by a private party. I don't have any opinion one way or the other.

JUDGE CLIFTON: Logistically I don't want them to leave Meredith Frisius' hands before she turns them to court reporter, and then scans them and makes the scans available to AMS. At which point, they will promptly go on the USDA website.

I don't want, in any way, to interfere with that custodial relationship. Which means there isn't really a way prior to them appearing on the AMS website, there's not really a way to have the official copy available, in my opinion. Does anyone else have a comment?
MR. VAN NORTWICK: If it is in the public domain, does it really need to be the official --

JUDGE CLIFTON: I'm sorry, come to the microphone, if you would.

MR. VAN NORTWICK: My question would be that --

JUDGE CLIFTON: Go ahead and identify yourself, please.

MR. VAN NORTWICK: My name is Tom Van Nortwick with Agribusiness Publications. From the media side, we don't, we're not trying to purport the official, Mr. Beshore, copy, we're just simply trying to facilitate the dissemination of information to a larger base of people, especially dairy producers.

If it is convenient for the people working through this hearing that those would be available in their unofficial form, then -- then we see no harm in that, as long as you do not see a harm in that, your Honor.

But -- but my feeling is that we're not trying to be the official cite. We're simply trying to help. As that testimony is given, we recorded it, we're going to break it down by individual giving the testimony in chronological order, and even identify who crossed in chronological order, so that a dairyman or anyone else could visit that location and hear the tremendous testimony on quota today -- what a learning experience for everybody -- and I doubt that there are very many dairymen or others outside of this room that have ever
heard that kind of dialogue. So we just think it needs to be available and the exhibits go with it, unofficial, we're not trying to be official, we're just trying to get information out there from a media standpoint.

JUDGE CLIFTON: I love that you are doing it. I am concerned because when you say the exhibits are in the domain, public domain, because people have picked them up, well, yes, true. But we work on them while we're here, and it does make a difference, so I'm concerned about that. Mr. Hill?

MR. HILL: Brian Hill. Yes, our issue is to the issue that you have cited. If someone has, is here and has, picks up copies of the documents, you know, they are free to do whatever they want to do with those documents. However, as the USDA AMS, we have an interest in making sure that the documents are complete and are properly put out into the public. And we can't be affiliated, we don't think that we should be affiliated with another party and putting those documents out there prior to the time that we would otherwise do it through the contractor that we have.

So I think that is our big issue. We don't feel that we should be doing that. I think we should put them out at the same time.

Now, once again, if they want to pick up documents and do what they want to do with them, there's nothing stopping them from doing so. If they want to call them unofficial

1920
whatever, we can't do anything about it. Just like they are making their videotape, audio taping this and presenting it to the public. We can't do anything about that, but I don't think we should be involved as AMS, in facilitating that and having our name involved with that even in an unofficial role.

MR. VAN NORTWICK: We have no problem with that at all, your Honor. And in fact, we would like to have on this presentation that we'll give, let people know that this is totally unofficial, we're just simply trying to provide a public service to those that might not have been able to hear at the time it was delivered or attend this hearing process.

JUDGE CLIFTON: Which I love. I think it is a service that lots of people will make use of. I appreciate it.

MR. VAN NORTWICK: Thank you.

JUDGE CLIFTON: All right. Good. Now, let's go back to the cross-examination by Mr. Vetne. You may proceed.

BY MR. VETNE:

Q. I just want to ask you about a couple of publications, see if you are familiar. I pulled off the web, a 2010 publication called "Challenges and Opportunities for California's Dairy Economy," published by the California Center for Cooperatives' Development, assembled by Justin Ellerby, Cooperative Specialist. Are you familiar with that publication?

A. Actually, I'm not.
Q. So if your name appears in the forward and acknowledgements with gratitude, you wouldn't know why it appears?

A. Well, I spoke to him, but I'm not one of the authors or anything like that.

Q. No.


Q. Familiar with the publication, that's what my question to you? And then --

JUDGE CLIFTON: Why don't you show it to him, Mr. Vetne, I think that might help.

MR. VETNE: What I've given the witness is the cover page and the forward matter and the summary, not the entire 170 pages.

JUDGE CLIFTON: So your question is whether he's familiar with the whole thing and including the 170 pages?

MR. VETNE: With that publication, that was my question, yes. I haven't gone beyond that yet.

JUDGE CLIFTON: All right. You may retrieve your pages that you showed him. What is that, about five or six pages?

MR. VETNE: Yes.

JUDGE CLIFTON: Okay.

BY MR. VETNE:

Q. That was my question, are you familiar with this publication?
A. I remember talking to him. I don't know that I ever saw the publication after it was put out. I know I never read it.

Q. That ends my questions. Okay.

A. Okay.

Q. There seems to be a proliferation of committees and tasks force. There's something called a Dairy Future Task Force in California. Are you familiar with that group?

A. Yes.

Q. Is that something that's ongoing?

A. It was disbanded.

Q. To sort of continue along the same line as Mr. English earlier, I'm giving the witness a copy of an excerpt from a transcript of a CDFA hearing of June 30, 2011. Mr. Dejong is passing them out. Please give three first -- one to the reporter, three to Ms. Frisius, one to the Judge, and then everybody else.

JUDGE CLIFTON: Ms. Frisius, I believe we would be marking this as 46. Is that what you have?

MS. FRISIUS: That's correct.

JUDGE CLIFTON: All right. This will be Exhibit 46. Is there anyone who wants a copy of Exhibit 46 who does not have one? Did that come out exactly right?

BY MR. VETNE:

Q. Dr. Erba --
MS. FRISIUS: Mr. Vetne, is this different than Exhibit 38 under the, introduced by Mr. English earlier?

MR. VETNE: Yes, because that's different testimony.

JUDGE CLIFTON: Good eye. Yes, they do have somewhat different pages, but you are right, it is from the same hearing. All right. So we can mark this as Exhibit 46, and Mr. Vetne, you may proceed.

(Thereafter, Exhibit Number 46 was marked for identification.)

BY MR. VETNE:

Q. Okay. You previously indicated remembering this hearing and you remember being a witness at this CDFA hearing for California Dairies at the time, correct?

A. Yes.

Q. And your testimony begins on page 9 of the excerpt of this transcript that includes your testimony. Do you see that?

A. Yes, I do.

Q. Would you turn to numerical page 11, beginning of the paragraph "we recognize" on line 10, and read to -- and read till sentence ending on that page, so line 25.

A. Yes.

"We recognize that many of the factors that companies consider before investing in new facilities or expanding current facilities, will not be influenced by the Department's decision. However, the results of this hearing do" -- I think
it is supposed to be determine but -- "determination whether or not plan" -- plant, should be plant -- "margins are adequate to ensure each plant's continued operation. The California dairy industry is not far removed from a critical tipping point where milk production outpaces processing capacity. While we have not reached the crisis that we experienced in 2008, we do see pockets of imbalance. Since the Spring of this year, we have verified with processing facilities outside of California, that some California milk is, in fact, moving out of California to other states for processing. It seems clear that California cannot afford to lose anymore of its processing capacity."

Q. Stop there, please. The statement and you verify again, that the statement made in June of 2011 was accurate when made? Correct?

A. I believe this is a reflection of my testimony given at that hearing in 2011.

Q. And what, if anything, of significance in available processing capacity has changed since 2011 when you gave this testimony?

A. On processing capacity I really probably can't speak all that fluently, other than what our own is at CDI, and we haven't had any market changes in our processing capacity. What has changed is how much milk is available to process.

Q. Meaning that milk is not growing at the rate it had been prior to 2011?
A. That's correct.

Q. Okay. On the next page, starting on line 12, that's page 12 of the excerpt of the transcript of your testimony, and line 12, sentence beginning "more recently" can you read to the end of that paragraph?

A. Certainly.

"More recently, the Department has collected and published information on the prices actually received by cheddar cheese manufacturers and butter manufacturers in California, so that a comparison to the average prices at the Chicago Mercantile Exchange can be made. The results of these comparisons are manifested in the pricing formulas as FOB price adjusters. We fully support the regular review and updating cheese and butter FOB price adjusters based on the most current information available."

Q. Okay. Now, if you'd move on to the following page, page 14, starting sentence beginning on line 14, "we make."

A. And then to the end of the paragraph?

Q. Please, yeah.

A. Okay.

"We make our proposal with full understanding that our proposed manufacturing cost allowances will leave some of our manufacturing plants uncovered. However, we think it is appropriate that the manufacturing cost allowance be set so that our largest and most efficient plants are covered. It is
axiomatic that establishing manufacturing cost allowances that
do not cover the cost incurred by the largest and most
efficient plants has grave ramifications for processing
capacity in the state."

Q. Did -- well, that's the end of what I asked you to
read. What are the grave ramifications that you had in mind?

A. You have a manufacturing cost allowance that doesn't
match up with the average cost, manufacturing cost of those
larger facilities, which would suggest that not only those
facilities, but other facilities as well, be operating at a
loss.

Q. Meaning that the available capacity would be reduced
and new capacity would not be attracted, correct?

A. I don't know if it would be reduced, particularly
again, I'm going to speak from our cooperative point of view,
we do maintain plants in operation that aren't necessarily
profitable all the time, but it would not be particularly
attractive for certainly new plants.

Q. Okay. Let's read, go to the next page, page 15,
starting with line 14, might elaborate a little more about why
continue to operate a plant at a loss. Page, line 14 through
the end, please.

A. "Changes in the Class 4a manufacturing cost allowances
that do not allow the results of the Departments -- do not
follow the results of the Department's cost studies, that is to
say, increasing them by less than what is justified reduces the value of the investment in milk processing facilities made by our member owners. It would also differentially benefit those producers in California who do not have investments in butter and nonfat dry milk processing facilities, and therefore, carry no responsibility of cost in balancing and stabilizing the states enormous milk supply."

Q. Thank you. By that conclusion in that paragraph, do you mean that if allowances and price references are set in a way so that you cannot recover your costs in the marketplace, you operate a loss, your producers must share the burden alone of that loss, and those costs are not borne by other producers in the marketplace, even though they get the benefit of those prices that are insufficient for your plant? Is that -- am I restating that correctly?

A. I think for the most part that's what this paragraph says.

Q. Thank you. I ask that Exhibit 46 be received.

JUDGE CLIFTON: Does anyone want to question Dr. Erba about Exhibit 46 before determining whether you have any objections? Is there any objection to Exhibit 46 being admitted into evidence. There is none. Exhibit 46 is admitted into evidence.

(Thereafter, Exhibit Number 46 was received into evidence.)
BY MR. VETNE:

Q. Thank you. Now following the hearing in June, CDI had the opportunity, and took it, to file a post hearing brief. Let me ask if you recognize it.

I have handed the witness a copy of a letter brief dated July 11, 2011.

JUDGE CLIFTON: Would you like those to be distributed?

MR. VETNE: Yes, distributed marked as Exhibit 47.

(Thereafter, Exhibit Number 47 was marked for identification.)

JUDGE CLIFTON: I have marked this document as Exhibit 47. Anyone still need a copy, please raise your hand. Appears everyone who needs one has one.

Would you identify it further, Mr. Vetne, as to what we will call it.

MR. VETNE: Okay. Exhibit 47 is a letter brief dated July 11, 2011, submitted by California Dairies, Inc., to CDFA, following the hearing of June 30, 2011, which was the subject of the transcript from Exhibit 46.

JUDGE CLIFTON: Excellent. Thank you.

BY MR. VETNE:

Q. Do you recognize this, Dr. Erba?

A. I do, but it's quite a lot longer than I normally write, so I'm surprised.

Q. Yes. And in your letter briefs you get a chance, you
get a chance to re-emphasize some things you said in your testimony, and that's what you did here; is that correct?

A. That's correct.

Q. Okay. And then, you use the opportunity to vent a little bit about some challenges that were raised at the first time during the hearing?

A. Yes, I got a little carried away, didn't I?

Q. Okay. The pages of this are not numbered, but two, three, the fourth page has a heading "Milk Shipped Out of California."

A. Yes.

Q. There's a quote from your testimony concerning milk shipped out-of-state, apparently on which you were challenged. And then you elaborated factually and descriptive and continuing with sentence beginning "I was asked." Can you read "I was asked" to the end of that paragraph?

A. Certainly.

"I was asked to estimate the volume of milk that has been moved out-of-state for processing, by the panel. I contacted the processor outside of California that stated in the month of June they had received 81 loads of milk and 12 loads of condensed milk from California. This was described as distressed milk by the out-of-state processor, not milk that was fulfilling a contract as a regular sale. I make this distinction because some hearing participants appear to be
confused about what milk is actually moving out-of-state and
for what reason. I believe these facts dispel the notion that
California processing capacity is more than adequate as claimed
by some hearing participants, and that California milk can
always find a home in-state."

Q. Thank you. That concludes what I asked you to read.
Correct?

A. Yes.

Q. And with reference the month of June there, in
California the month of June represents a month in which the
flush is over and the reduced production in summer heat stress
is starting?

A. Yes, it is starting, but it is clearly not the low
point the year.

Q. The low point would be July and August?

A. Probably more like September, maybe even October
sometimes.

Q. Okay. And there was reference here to distressed milk
and contract milk. Are you aware of milk that regularly flows
out of California for contract reasons?

A. Today? We don't sell any milk regularly out of -- I
can only speak from my company's point of view. We don't sell
any milk regularly out-of-state. We do sell, however, cream
and condensed out-of-state, pretty regularly.

Q. Okay. Are you able and willing to disclose who the
processor you called was?

A. I can't even remember to be quite honest with you.

Q. That's even better. Okay. Thank you. I ask that Exhibit 47 be received.

JUDGE CLIFTON: Does anyone wish to question the witness about Exhibit 47 before determining whether you have objections? There is no one. Is there any objection to the admission into evidence of Exhibit 47? There is none. Exhibit 47 is admitted into evidence.

(Thereafter, Exhibit Number 47 was received into evidence.)

JUDGE CLIFTON: It is time to begin the weekend. It's 4:57.

MR. VETNE: I can continue on Monday or I can wrap it up in 15 minutes, either way.

JUDGE CLIFTON: We want to go home.

MR. VETNE: Okay. That's good. Thank you.

JUDGE CLIFTON: Mr. Vetne, I truly appreciate what you have brought to our attention so far, and you're still working, so I thank you. I applaud all of you on how hard you have worked to be prepared.

Mr. Hill, did you have something you wanted to add right now?

MR. HILL: Yes. Brian Hill. We do have a statement to read on the record here. I think Mr. English is pleased, and

1932
have not fallen on deaf ears.

"CDFA" -- here's the statement -- "CDFA will be present on October 8th for the limited purpose of entering reports into the hearing record developed in response to requests from interested parties. CDFA will only answer questions regarding the compilation of the data contained in these reports in order to remain neutral and avoid being associated with a particular proposal."

And that is a statement passed along to AMS from CDFA.

JUDGE CLIFTON: Excellent. Thank you. Mr. Hill, I'm going to ask that you read that again when we're -- when we convene on Monday as a preliminary matter, for you to read it again.

That's excellent. So that's October 8th.

MR. HILL: Thursday.

JUDGE CLIFTON: Good. It is Thursday. All right. Good. Is there anything further before we go off record today?

Dr. Erba, were you already planning to be here Monday?

DR. ERBA: It seems I might have some leverage here. Yes, yes, I was.

JUDGE CLIFTON: Thank you. All right. That concludes our record for today. We go off record at 4:59.

(Whereupon, the evening recess was taken.)

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STATE OF CALIFORNIA  )  ss.
COUNTY OF FRESNO  )

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I am a duly qualified Certified Shorthand Reporter, in
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I am not financially interested in this action and am
not a relative or employee of any attorney of the parties, or
of any of the parties.

I am the reporter that stenographically recorded the
testimony in the foregoing proceeding and the foregoing
transcript is a true record of the testimony given.

DATED: October 19, 2015
FRESNO, CALIFORNIA

[Signature]
MYRA A. PISH, CSR
Certificate No. 11613

1934

TRANSCRIPT OF PROCEEDINGS - VOLUME IX
alarmed (1) 1777:20
alert (1) 1784:7
alerted (1) 1773:4
aligned (1) 1755:1
alive (1) 1866:19
allocated (22) 1781:9,24; 1788:17;1909:13; 1804:14,21;1805:10, 16,20;1806:7,10,12, 17,24;1607:2,14,20, 25;1808:5,5; 1819:21,1891:14
 Allocating (1) 1803:19
 allocation (12) 1786:11;1788:22; 1794:13;1803:23; 1804:4,4;1805:13; 1806:14;1807:6,12, 15,17
 Allocations (2) 1807:1,18
allow (5) 1780:12;1827:21; 1830:6;1840:23; 1927:24
 allowance (2) 1926:24;1927:7
 allowances (19) 1796:8;1979:8,8, 10,14;1848:12,13, 14,15,17,19;1849:1; 1869:13,17;1881:22; 1926:22;1927:1,23; 1928:9
 allowed (5) 1773:3;1801:22; 1846:5,11;1894:19
 allows (1) 1832:1
 almost (2) 1867:19;1907:22
 alone (3) 1809:10;1892:15; 1928:11
 along (10) 1798:25;1830:10; 1833:1,8;1842:9; 1870:9;1881:11; 1915:25;1923:12; 1933:9
 alphabetical (2) 1817:17;1818:13
 alter (2) 1786:4;1828:2
 altering (1) 1853:9
 alternative (3) 1757:23;1785:21; 1881:4
 although (21) 1790:6;1797:23; 1799:11;1803:3; 1808:25;1817:10; 1818:43;1813:5; 1853:13;1856:21; 1858:8;1870:11; 1875:5;1881:7; 1883:5;1895:13; 1896:21;1900:19; 1907:25;1914:23; 1917:17
 always (6) 1758:24;1759:3; 1784:6;1790:6; 1902:3;1931:5
 amazingly (1) 1836:1
 ambush (2) 1789:12;1794:14
 amend (1) 1812:24
 amended (1) 1806:9
 amendments (3) 1780:19;1823:21; 1886:15
 America (2) 1754:3;1782:23
 among (10) 1783:16,18; 1784:25;1791:9; 1803:22;1809:4; 1820:9,10;1848:10; 1917:19
 amount (24) 1779:13;1787:25; 1789:13,14,19,21; 1790:15;1800:22; 1802:10;1803:11; 1804:2,3,8,13,20; 1807:2,19;1810:11; 1814:22;1831:2; 1877:4;1885:22; 1895:3
 amounts (6) 1789:4,5,9; 1795:16;1828:9; 1832:2
 amplify (1) 1883:19
 AMS (13) 1753:2,5;1758:5; 1761:10,15,21; 1762:2,15;1918:19, 23;1920:14;1921:4; 1933:9
 analysis (5) 1766:1,6;1777:4, 5;1848:17
 and/or (2) 1797:13;1828:7
 Andrew (1) 1914:14
 Andy (2) 1912:25;1916:9
 Angeles (2) 1906:16;1907:21
 Animal (3) 1775:22,24; 1776:10
 announce (1) 1831:4
 announced (6) 1789:8;1790:2; 1802:12,12;1830:11; 1831:15
 announcement (1) 1755:19
 annual (8) 1815:10;1879:7, 12,14,15;1897:2,3, 11
 annuity (3) 1903:25;1904:23
 anticipates (1) 1822:4
 anymore (4) 1775:11;1877:7; 1891:2;1925:11
 apologize (1) 1872:8
 apparatures (1) 1826:4
 apparently (1) 1930:13
 appeal (2) 1762:6,10
 appeals (2) 1813:22;1814:8
 appear (3) 1876:21;1880:22; 1930:25
 appearing (3) 1771:7;1917:15; 1918:23
 appears (9) 1774:21;1775:2; 1812:3,1851:1; 1886:7;1914:24; 1922:1,3;1929:12
 applauded (1) 1932:20
 applicable (13) 1790:18;1821:22; 1822:12;1827:7; 1828:4,12,15; 1830:10,14;1831:5; 1833:1,1914:22; 1915:14
 applicants (1) 1806:13
 application (6) 1806:16,19; 1808:2;1844:7; 1906:14;1916:22
 applied (5) 1783:13;1796:20; 1846:2,1905:17; 1906:20
 applies (1) 1881:21
 apply (6) 1797:10;1798:10; 1803:5;1806:14; 1846:3;1876:18
 applying (1) 1828:10
 appoint (1) 1813:20
 appointed (2) 1791:18;1894:8
 appreciate (8) 1762:13;1764:20; 1817:14;1873:10; 1880:7;1891:9; 1921:13;1932:18
 appreciated (1) 1843:21
 apriised (1) 1761:12
 approach (1) 1759:8
 appropriate (9) 1789:8;1795:15; 1809:18;1813:2; 1816:23;1822:11; 1832:2;1887:5; 1926:24
 approval (3) 1780:16;1823:18; 1833:16
 approve (1) 1813:24
 approved (3) 1808:20;1822:23; 1839:17
 approximate (1) 1793:1
 approximately (5) 1759:14;1767:16; 21;1769:5;1890:7
 April (2) 1806:24;1891:14
 Arabic (5) 1783:25;1784:3,4, 6,7
 Area (11) 1753:4;1787:12; 1797:16;1799:5,7,7; 1808:17,18;1812:11; 1822:14,17
 areas (11) 1796:22,22; 1798:24;1799:19; 1814:6;1818:16,20;
argue (1) 1858:9 1869:20; 1886:16
argument (2) 1824:20; 1825:4
Arizona (13) 1856:6, 10:11; 1861:9:23; 1862:5, 6, 9, 22; 1863:2, 4, 5
around (6) 1798:20; 1836:6; 1851:12; 1887:9; 1901:19; 1917:22
array (1) 1783:17
arriving (1) 1798:5
articulate (2) 1777:21; 1843:18
articulating (1) 1878:10
aside (2) 1796:7; 1887:20
aspect (3) 1823:2; 1839:23; 1894:14
aspects (3) 1822:24; 1839:18; 1842:16
assembled (1) 1921:22
assembly (1) 1913:25
asset (7) 1779:12; 1780:1; 1842:12; 17,22; 1843:9; 1892:5
assets (1) 1814:2
assigned (7) 1791:4; 1793:20; 1794:12; 15; 1807:24; 1791:4; 1793:20; 1797:4; 1803:23; 1907:3; 1810:25; 1811:23; 1812:1; 1892:1; 1893:3, 4, 5, 7, 7, 8, 9, 8, 10; 12; 1904:14; 1907:14; 1926:10; 1927:8
average (2) 1802:15; 1849:25
avoid (1) 1933:7
aware (4) 1840:4; 1846:22; 1851:19; 1931:19
away (4) 1848:24; 1869:21; 22; 1930:7
awfully (1) 1890:18
awkwardness (1) 1760:10
axiomatic (1) 1927:1
Bachelor's (1) 1775:22
back (40) 1759:18; 20; 1760:9; 1762:19; 1771:18; 20; 1795:2, 4; 1812:17; 1817:13; 1820:25; 1827:20; 1828:24; 1829:1, 2; 1838:2; 1839:2, 8; 1842:24; 1845:8; 1847:23; 1849:21; 1868:2, 14; 1887:2; 1887:6; 1887:15; 15; 1878:18; 1879:23; 25; 1885:1; 1889:22; 1893:20; 1906:10; 1912:21; 1915:3; 1917:23; 1918:1; 1921:15
background (4) 1775:21; 1776:4; 1841:22; 23
balancing (1) 1928:6
Barbara (2) 1799:11; 12
bargain (1) 1785:5
barrels (1) 1767:20
base (57) 1781:10, 15, 24; 1784:7, 14, 19, 22, 25; 1788:1, 6, 17, 19, 23, 24; 1789:15; 1790:13, 16, 22; 1791:3, 3; 1796:11, 13; 1802:3; 1803:12; 1810:5, 11, 13, 15, 22; 1811:9, 14; 1807:11, 20, 24; 1808:1, 3, 5, 6, 8; 1809:2, 2; 1811:4; 1859:5; 1868:25; 1888:25; 1889:1, 29; 1893:5; 1906:14; 1909:3; 1926:14
based (16) 1782:5; 1787:18; 1797:4; 1803:23; 1805:13; 1807:3; 1810:25; 1831:21; 1860:16; 1869:3; 1891:16; 1899:8; 1903:5; 1906:14; 1909:3; 1926:14
behavior (2) 1907:24; 1908:23
belabor (2) 1763:12; 1884:24
believes (1) 1911:20
belong (1) 1833:14
below (9) 1774:11, 20; 1775:2; 1805:12, 19; 1810:14; 1812:23; 1815:4
benchmark (1) 1787:21
benchmarks (1) 1787:17
benefit (11) 1777:24; 1802:6; 11; 1843:23; 1844:2; 14, 16, 23; 1864:14; 1928:3, 13
Bernardino (4) 1819:1; 1890:24; 1906:16; 1907:3
Beshore (25) 1753:12, 12; 1757:8, 8; 1761:7, 14; 20, 21, 23; 1762:9, 13; 1763:16; 1764:15, 17;
IN RE: MILK IN CALIFORNIA

TRANSCRIPT OF PROCEEDINGS - VOLUME IX
October 2, 2015

1865:8;1869:18; 1876:25;1877:6,15; 1895:22,24;1901:7; 1903:4;1908:1,15, 22;1910:24;1911:3, 10;1915:6,17,24; 1924:6;1926:4,11; 1930:15;1931:4,22; 1932:14,17
cancellation (1) 1785:10

capability (1) 1786:1
capacity (9) 1925:5,11,18,20, 22;1927:4,12,13; 1931:3
capped (1) 1846:5

caption (1) 1757:23
captured (1) 1826:25

carman (15) 1760:3;1763:11; 1765:2,12,14,14,21; 1766:18;1767:23; 1768:2,14;1769:23, 24;1770:1.3
carried (2) 1840:24;1930:7
carries (4) 1790:8,9,10; 1809:1
carry (3) 1808:17;1821:5; 1928:5
carrying (1) 1883:8
case (9) 1760:11;1767:17; 1857:17;1861:8; 1867:23;1870:22; 1871:14;1903:13; 1904:19
case-in-chief (4) 1878:5,18,23; 1879:19
categories (5) 1758:18;1799:18; 1815:9,14,22
categorize (1) 1758:17
category (1) 1815:24
causation (3) 1890:10;1908:13; 1909:22
causing (1) 1895:24

CCC (1)

1890:14

1756:13;1926:11

Chief (3) 1771:3;1778:7; 1882:13

Chip (7) 1754:6;1756:5; 1760:8;1763:24; 1768:6;1824:2; 1855:4

C-H-I-P (1) 1754:7

choice (3) 1866:21,22,25

choose (1) 1899:9

chosen (1) 1867:3

chronological (2) 1919:20,21
cite (1) 1919:18
cited (1) 1920:11

claim (1) 1789:17

claimed (1) 1931:3

clarification (5) 1763:2;1846:22; 1853:23;1858:2; 1888:16

clarify (1) 1866:6

Clarity (3) 1756:5;1757:14, 15
class (139) 1781:7;1782:6; 1783:10,18,21,23, 25;1784:1,18,20,22; 1785:3,7,13;1786:7, 11;1787:19,24; 1788:5,5,15;1789:7, 7,8,14;1790:8,9,10, 11,15,18,24,25; 1791:1;1796:10,17, 24;1797:6,13,13,13; 1798:4;1800:5, 20,21,24;1801:5,9, 11,19,24;1802:2,10, 12;1803:22,22,23, 23,25,25;1804:14, 14,17,17,21,21; 1806:6,18;1830:10; 1833:1;1844:13; 1845:6,9,10,18,22, 24;1846:3,1847:23; 1849:5,8;1851:4,14; 1859:15,23;1863:20, 22;1865:22,23; 1866:9,10,14;
1867:7,7,17,21; 1869:5,16;1870:24;

Cheese (14) 1754:17,17,20; 1766:23;1767:9,17, 18,1769:16;1790:4, 9,11;1898:17,19; 1926:9,14

Chicago (2)

1781:10,15,15,19,20, 20;1873:15,15; 1881:2,14;1882:14; 1883:13,14,16,17,18, 20;1884:9;1887:4, 7,10;1899:5,9,18,19, 23,25;1900:5,5,10, 18,22,22,24;
1901:14,16;1905:14; 1927:23
classes (12) 1781:25;1783:14; 1788:19;1789:5; 1791:12,14;1796:1; 1883:20;1887:3,21; 1889:20;1901:15
classified (7) 1783:10;1790:6; 1865:5,8;1899:13; 1911:15,15
clear (14) 1756:2,10;1775:9; 1799:18;1824:12; 1825:19;1830:18; 1841:24;1847:10; 1850:22;1853:24; 1866:19;1885:11; 1925:10
clearly (6) 1777:12;1785:1; 1823:1;1839:22; 1903:14;1931:13
clients (2) 1762:5,5

Cliff (1) 1760:3

Clifford (1) 1765:14

CLIFTON (176) 1753:10;1754:4, 21;1755:1,6; 1756:15;1757:1; 1758:3;1759:22; 1760:6;1761:21; 1762:8,13;1763:14; 1764:24,1765:5, 9,15,18;1766:10; 1768:1;1769:24;

1770:4,9,19,21; 1771:10,23,25; 1772:8,11,18; 1773:7,14,18;
1775:8,13;1777:18; 1778:19,22,24; 1781:11,14,18,20, 22;1782:7;1783:24,24; 1845:5,10,12,14; 1792:8;1793:16; 1794:24;1795:4;
1799:17,22;1802:17, 20;1804:25; 1805:25;1806:2; 1812:24;1813:3,14,
contention (1)

considerable (3)
9720:20;1803:3;1870:11

considerably (4)
1784:23;1791:8;1815:3;1890:2

consideration (4)
1780:7;1828:15;1875:24;1883:23

considerations (1)
1894:3

considered (1)
1807:6

consistent (4)
1813:11;1823:13;1824:16;1881:13

consistently (2)
1829:23;1830:1

consisting (2)
1813:20;1814:4

Consolidated (1)
1886:14

constant (1)
1877:5

constituted (5)
1782:7;1788:25;1888:24;1889:18,22

construct (1)
1802:5

constructed (1)
1820:2

constructing (1)
1780:2

construction (2)
1795:13;1824:19

constructive (1)
1825:12

consulting (1)
1917:11

contacted (1)
1930:20

contained (9)
1772:24;1790:19;1810:1;1812:15;
1828:18,21;1829:17;1854:9;1933:6

contains (2)
1822:4;1824:4

contemporaneously (1)
1887:19

contention (1)
1762:17,17;1839:5,6;1848:2.4;1854:6;1855:18;1856:13
H-A-N-C-O-C-K (1) 1754:23
Hancock's (2) 1864:6;1876:16
hand (7) 1770:15;1789:21;1817:4;1877:24;1881:1866:6;1929:12
handed (2) 1882:8;1929:5
handle (1) 1763:17
handle's (3) 1755:16;1759:15;1761:6;1763:22;1767:25;1787:9;1793:8;1798:12;1805:1;1901:21;1903:21;1904:4;1905:24;1906:6
higher (26) 1779:13;1790:8,9,11;1791:15;1906:22;1907:2;1908:14;1923:8;1924:20;1943:5;1944:21;1967:1;4;17;20;1874:15;1884:1;1908:8;1909:22;1902:11;1903:3;1907:4;1908
highest (10) 1783:12;1790:12;1907:2;1919:20;1921:11;1923:14;1924:6;12;12.25;1925:16;1929:2;1.38;1930:6,25;1931:4;1933:4
hearings (4) 1880:22;1881:14;1884:25;1885:4
heat (1) 1931:11
Heaven (1) 1879:14
held (9) 1791:22;1792:4;1805:12;1806:10;1820:10;16;1857:3;1885:23;1906:10
help (4) 1864:9;1911:10;1919:18;1922:11
helped (2) 1783:8;1880:11
Henry (1) 1753:3
H-E-N-R-Y (1) 1753:3
Hollon (6) 1754:3;3.4.5;1756:13;1862:8
H-O-L-L-O-N (1) 1754:5
home (4) 1759:12;24;1931:5;1932:16
honest (1) 1932:2
honestly (1) 1898:21
Honor (42)

I
ice (2) 1790:5,10
idea (4) 1802:19;1836:15;16,24
ideal (3) 1763:25,25;1764:14
identical (4) 1804:2;1859:22,23;1878:13
identically (1) 1820:5
identification (10) 1765:8;1772:7,14,
In re: Milk in California Transcript of Proceedings - Volume IX
October 2, 2015

K

Kaldor (2)
1754:11,11
K-A-L-D-O-R (1)
1754:12
keep (4)
1761:12;1845:25;1894:7,7
keeping (1)
1820:6
Kern (1)
1799:10
K-N (1)
1917:5
kind (12)
1760:22;1764:22;1841:22;1848:16;1856:21;1870:5;1878:9;1892:1;1916:3
kindly (1)
1835:14
kinds (2)
1756:6;1895:21
Kings (1)
1798:15
K-N-S-E-Y (1)
1917:4
knew (1)
1868:2
knowledge (3)
1855:9,13;1908:14
known (1)

L

LA (1)
1890:25
labeled (3)
1764:11;1815:17;1872:20
labor (1)
1763:7
lack (2)
1785:7;1913:17
laid (1)
1915:12
Land (4)
1753:23;1754:2;1782:23;1823:7
language (23)
1780:10;1822:4;1823:14;1824:12;20;1825:16;19;1841:7,13;1853:6,12,17,18;1854:19;1875:14,19;1876:11,21;1877:13,16
large (3)
1778:18;1799:1;1901:10
largely (1)
1799:13
larger (6)
1797:2,2;1860:9;1869:11;1919:11;1927:9
largest (3)
1799:5;1926:25;1927:2
last (21)
1754:4;1774:14;1779:2;1800:17;1805:2;1815:22;1819:25;1828:1;1829:1;1832:23;1836:1;1839:2;1847:13;1848:1;1854:11;1861:9;1864:7,24;1872:2;1876:15;122;1877:2,4,18;1878:25;1879:22,25;1880:6;1882:17,19;1884:16;1886:5;1888:1,10;1889:3,6;11,14,19;1906:5,8,10;1908:19,25;1910:6,25;1911:5,9,21;1912:3,7;1912:12,16;1914:10;1915:7,9;1917:3,5,21;1918:1,6;1919:3,6;1920:5;1921:12,15;1922:10,15,19,22;1923:16,18,21;1924:19;1928:19;1929:7,11,20;1932:5,12,16,18;1933:10,15,20

Min-U-Script®

Barkley Court Reporters

(16) investing - level

(179) investing - level

(15) investing - level
IN RE: MILK IN CALIFORNIA

TRANSCRIPT OF PROCEEDINGS - VOLUME IX
October 2, 2015

not (19)

1782:9;1802:3; 1835:21;1847:24; 1877:9;1884:19; 1928:22;1932:8

nonetheless (3)

1762:24;1784:19; 1873:11

nonfat (10)


non-Grade (1)

1861:25

non-partisan (1)

1762:7

nonpool (1)

1803:18

non-quota (7)

1796:4;6;1821:25; 1831:7;1854:21; 1862:10;1901:8

noon (1)

1755:14

nor (1)

1908:14

normal (3)

1755:12;1858:24; 1863:19

normally (2)

1870:23;1929:23

N-O-R-S-E (1)

1912:5

North (10)

1771:5;1772:3; 1798:25;1799:3.5; 1816:21;1818:18.25; 1819:17;1907:15

Northern (2)

1799:6;1886:16

Nortwick (7)

1837:5;1919:1.5,7; 7;1921:6,14

note (1)

1875:17

noted (2)

1824:10;1832:11

notice (5)

1761:15;1763:21; 1785:11;1829:18; 1854:9

noticed (2)

1764:11;1910:17

notify (1)

1759:4

notion (1)

1931:2

Notwithstanding (1)

1822:9

Nourse (3)

1909:8.11;1913:5

N-O-U-R-S-E (1)
TRANSCRIPT OF PROCEEDINGS - VOLUME IX
October 2, 2015

1837:6;1929:3
posted (1)
1837:16
post-hearing (5)
1878:12;1880:24;
1881:11;1882:6,14
posting (1)
1758:4
potential (1)
1856:24
potentially (2)
1842:7;1848:3
pound (24)
1790:21;1793:13,
17,20,24;1794:4;
1795:20;25;1796:11,
13;1802:8;1808:23;
1810:17;1811:24;
1812:1,20;1821:21;
1828:3;1830:22;
1844:5,5,7;1892:2;
1907:21
pounds (47)
1778:15;1779:2,3;
1782:10,11;1790:16,
17,20,21,24,25;1791:
1,1759:15;190:20,
1796:9;1801:10;
1802:1,2;1807:5,
6,8,1809:13,13;
1811:1,18;19,20,21,
21;1812:22;1813:7;
1819:24;1820:23;
1821:23;1828:20;
1830:15;1849:9,23;
1868:13;1873:2,7;
1892:18;1897:8,14,
15,22
powder (2)
1754:18;1848:4
powdered (1)
1799:3
powders (1)
1790:11
power (1)
1756:13
practical (3)
1773:25;1774:3;
1828:5
practice (1)
1882:7
practices (3)
1785:1;1829:14;
1865:11
practicing (1)
1866:20
preceding (2)
1804:16;1808:2
precisely (1)
1879:11
preceptor (1)
1869:7
predetermined (1)
IN RE: MILK IN CALIFORNIA

TRANSCRIPT OF PROCEEDINGS - VOLUME IX

October 2, 2015

producer-distributor (1)
1799:25

producer-handler (4)
1800:1;1842:1; 1846:12,15

Producer-Handlers (9)
1799:24;1846:5, 20;1875:15;2013:2; 1879:10;2015:2;17 1876:15;1868:12; 1780:10;1871:2; 1875:6;1884:10; 1895:6;1905:17

producer-members (2)
1778:14,25

Producers (111)
1755:5;1779:11; 1780:5,17;1781:6,8, 9,23;1782:9,25; 1783:10,16;1784:21, 25;1785:4,8,12,15, 19;1786:3,9,12, 1787:11;1788:14,16; 1789:4,15,19,22; 1791:9,18,24; 1792:5,12,13; 1793:13;1794:19, 1796:18;1797:3,9; 1797:8;1803:3,22; 1804:5;1805:5,6,10, 14,18;1806:8,11, 1807:1,2;1808:1, 7;1809:4,10,11; 1812:23;1813:9,22; 1814:21;1815:1,25; 1822:24;1823:4,4; 10,19;1825:25; 1827:19;1828:8; 1831:21;1839:18; 1846:18;1860:15,16; 1863:4,11;1865:20, 22;1866:21,22; 1867:9;1870:11; 1874:25;1877:6; 1883:15;1884:9,11,

12;1891:15;1892:15, 16;17;1895:8,14; 1899:12;1901:23; 1908:5,6,12,14,16; 1919:12;1928:4,11, 12 producers' (1) 1785:25 producer's (8) 1785:2;1787:18, 19;21;1979:10; 1789:8;1809:12; 1810:11 producer-settlement (6) 1830:18;1831:9, 19;20;1832:1,4 produces (1) 1908:7 producing (5) 1778:15;1783:23; 1856:4;1871:18,20 product (10) 1766:7;1767:13; 1768:17;23;1845:10; 1871:19;20;1906:1; 1913:18;1917:8 production (108) 1779:15;24; 1780:1;1782:6,6,7; 1786:5,5;1787:14, 16,17,19,19,22,25; 1788:23,24,25; 1791:7,8;1795:11; 1797:12;1800:2,5,6, 8,10;1801:2,6,7,16; 1802:3,10;1803:16; 1805:11,15,15,22; 1806:9,13,15,21,22; 1807:7,10,11,13,18, 20,23,23,24;1808:1; 1,3,5,6,8,9 le10:2:22; 1810:25;1811:14; 1815:1;1815;1816:13, 18,20;1817:9,14,15, 23,25;1819:7,8; 1823:7,1828:13,16; 1831:6;1846:3; 1888:23,24;1889:17; 1891:2,4,9; 1895:7,8,15; 1897:2,3,5,6,11,12, 22;1898:9;1902:12, 13;1903:5;1907:13,17; 1913:23,24,1925:5; 1931:11 products (14) 1754:18;1779:3; 1783:12;1787:20,21,22; 23;1797:13; 1883:22;1884:6,7; 1914:6;1916:22 professional (1) 1776:3

profitable (1) 1927:17 program (50) 1767:20;1773:12; 1777:3;1779:5,6,9, 10;1780:9,13; 1781:4,5;1782:15, 21;1783:24;1786:16, 18;1805:21;1814:7; 1821:3,11;1823:1, 3,12;1824:13; 1825:20;22;1826:2; 1827:11,13,21; 1839:22;24;1841:15- 1852:22;1853:5; 1854:25;1856:15,22; 1857:11;1865:15,17, 17,21;1876:1; 1890:6;1891:8; 1898:23,24;1899:17 Programs (3) 1753:2,5;1761:22 progress (1) 1864:24 progressed (1) 1820:7 Progressively (1) 1783:12 prohibition (1) 1814:2 Projections (1) 1766:20 proliferation (1) 1923:6 promptly (1) 1918:19 promulgation (2) 1780:11;1823:15 pronounced (1) 1913:2 proper (1) 1814:23 properly (2) 1827:19;1920:15 proponents (7) 1753:13,17,20; 1754:8;1764:8,8; 1770:8 proposer's (1) 1767:7

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3 (19)
1790:10;1791:12; 1797:13;1819:11,21; 24;1820:2;1834:19; 1872:19,19,20; 1876:4;1877:13; 1881:2;1882:14; 1888:22;1889:8, 8th (3)
1910:12

30-day's (1)
1785:10

30's (2)
1911:12;1913:7

30th (2)
1806:24;1891:14

31 (1)
1756:23

342 (2)
1809:10;1892:15

35 (3)
1766:19;1815:11; 1816:13

37 (1)
1795:17

375 (2)
1802:1;1807:5

38 (1)
1924:1

385 (1)
1779:2

390 (1)
1778:14

3rd (1)
1886:18

4 (5)
1771:16;1772:6,9; 1790:11;1865:2

4:29 (1)
1918:1

4:30 (2)
1917:23,24

4:57 (1)
1932:13

4:59 (1)
1933:21

40 (5)
1797:16;1805:9; 1806:7;10;1815:23

40.8 (1)
1897:22

401k (1)
1893:24

41 (12)
1764:3,7;1765:3,5, 7,10,11;1766:9,13, 13,15;1815:23

42 (23)
1772:7,8,12,12,13; 1773:1,2;1777:9,10; 1815:1;1832:10,15; 1833:21;1835:6,10, 12;1839:10,13; 1849:4;1850:14; 1888:18,19;1889:7; 1896:2

43 (22)
1772:17,18,20; 1798:18;1809:21; 1812:15;1817:2,3; 1835:16,19,21,21, 23;1842:25;1872:7, 8,18,19;1873:7,23; 1892:24;1897:2

44 (8)
1882:17,19,20,21; 1884:15,19,19,21

45 (8)
1778:16;1781:2; 1886:8,1887:25; 1888:4,4,6

46 (11)
1923:19,21,22, 1924:6,8;1928:18, 20,21,22,24;1929:19

47 (9)
1929:8,9,11,16; 1932:4,6,8,9,10

4A (13)
1798:16,19,22; 1881:2,14;1882:14; 1883:13,14,16,20; 1884:4,9,19,27,23

4B (15)
1809:6,18,21; 1812:15;1881:2; 1882:14;1883:13,14, 16,20;1887:5,7,20;

4C (4)
1816:15,24; 1817:5,1818:12

4D (6)
1819:11,22,23; 1872:18,19;1873:23

4E (2)
1826:14,18

4F (2)
1826:15,20

401k (1)
1837:20

5 (5)
1753:1,1764:7; 1865:13;1889:12,13

5:00 (1)
1837:20

50 (2)
1797:12;1800:19

5051 (1)
1832:12

51,176 (1)
1809:13

53 (1)
1816:22

552 (1)
1811:22

57 (1)
1815:11

57,914 (4)
1801:9;1849:8,23; 1850:3

58 (1)
1802:15

6 (2)
1866:17;1913:14

6,603 (1)
1811:21

60 (9)
1803:15;1807:8; 1808:13;1815:23; 1816:9,24;1871:4, 13;1872:1

60-day (1)
1851:17

61 (1)
1815:24

624 (2)
1809:11;1892:16

62712 (1)
1782:16

62715 (1)
1821:17

62726 (2)
1822:7;1839:14

62750 (1)
1821:20

66 (5)
1800:4;1846:23; 1866:22;1867:18,18

66.2 (3)
1782:11;1812:21; 1813:7

67 (2)
1866:23;1867:19

7 (6)
1823:20;1862:22; 1863:9;1886:24,25;

70 (5)
1800:25;1846:18; 1847:6;1848:21;

70's (1)
1911:16

75 (1)
1883:21

750 (1)
1821:19

785 (1)
1779:2

7USC608c (1)
1780:19

8 (1)
1889:24

8.7 (3)
1792:22;1974:3; 1798:11

80 (6)
1805:5;1815:24, 25;1896:9,15;

801 (1)
1879:10

801a (2)
1878:1,14

80's (1)
1890:9

81 (1)
1930:21

84 (1)
1766:20

85 (2)
1818:2,2

8c (2)
1780:18;1823:19

8in (1)
1910:12

8th (3)
1787:7;1933:3,13

9 (2)
1764:6;1924:15