BEFORE THE UNITED STATES
DEPARTMENT OF AGRICULTURE
AGRICULTURAL MARKETING SERVICE

In the Matter of:	Docket No.:
Milk in the Mideast	AO-166-A68
Marketing Area	DA-01-04
	VOLUME II

Wednesday, October 24, 2001

The Holiday Inn Express Motel
Galaxy Banquet Center
231 Park Centre Drive
Wadsworth, Ohio

BEFORE:

THE HONORABLE JILL CLIFTON
Administrative Law Judge

APPEARANCES:

GREGORY COOPER, Esq.
GINO TOSI
United States Department of Agriculture
AMS
14th & Independence Avenue SW
Washington, DC 20250
(202) 690-1366

MARVIN BESHORE, Esq.
Attorney at Law
130 State Street
Harrisburg, PA 17108
(717) 236-0781

BENJAMIN F. YALE, Esq.
Attorney at Law
102 West Wapakoneta Street
Waynesfield, Ohio 45896
(419) 568-5751

APPEARANCES (Cont'd.)

CHARLES M. ENGLISH, JR., Esq.
Attorney at Law
701 Pennsylvania Avenue, NW
Washington, DC 20004
(202) 508-4000

ALLEN WARSHAW, Esq.
Attorney at Law
305 North Front Street
Harrisburg, PA 17101
(717) 237-5500

RODNEY K. CARLSON
5367 Lance Road
Medina, Ohio 44256
(330) 723-3872

JIM HAHN
Land O'Lakes, Inc.
4001 Lexington Avenue
Arden Hills, Minnesota
(651) 481-2521

DENNIS TONAK
Mid-West Dairymen's Company
4312 West State Street
Rockford, Illinois 61102
(815) 623-8064

I N D E X

E X H I B I T S

P R O C E E D I N G S

JUDGE CLIFTON: We are on the record in day two of the hearing in the matter of Milk in the Mideast Marketing Area.

This is October 24, 2001 and we are beginning at approximately This record is being made in Wadsworth, Ohio. It's October 23, 2001. It's approximately 8:36 in the morning. The temperature is less than 70 degrees. Let me know if you get too cold.

Mr. Beshore, would you alert me as to how you would like to proceed?

MR. BESHORE: Mr. Hollon does have some further testimony, which involves proposal four that we haven't yet touched on and which is not a pooling proposal. It's the advance price proposal. And he also has some opposition to proposal eight and we haven't heard from the proponents on that yet.

We would like to further resume testimony until a later time and I believe that Mr. Herbein may be ready to proceed this morning and I don't know what other witnesses may be intending to comment on proposals one, two, three and five. So, we would like to defer Mr. Hollon's additional testimony to a later point in the proceedings and allow other witnesses to proceed at this time.

JUDGE CLIFTON: Thank you, Mr. Beshore, and I want to applaud your excellent presentation yesterday. You kept things moving. It was uncomfortable in here and I appreciate very much how well you had prepared everything.

We regard to those who would like to testify about proposals one, two, three and five, other than Mr. Hollon, would you identify yourselves so I will know how many of you there are. Mr. Carlson, Mr. Warshaw?

MR. WARSHAW: Mr. Herbein will touch on that.

JUDGE CLIFTON: Mr. Herbein. Mr. English?

MR. ENGLISH: I have Mr. Yates who will testify.

JUDGE CLIFTON: Mr. Yates will. Now, with regards to proposal four, how many intend to testify. Mr. Warshaw?

MR. WARSHAW: Mr. Herbein will testify on proposal four.

JUDGE CLIFTON: It's sounding like Mr. Herbein is our natural next witness, would you agree?

MR. WARSHAW: Yes.

JUDGE CLIFTON: Then with regard to the remaining proposals, how many witnesses expect to testify with regard to proposal six? I saw none. How many -- and this does not foreclose that, but I am just trying to get an idea. How many expect to testify regarding proposal seven? We kind of had it withdrawn partially, but I didn't know whether anyone else might like to speak to it.

With regard to proposal eight? Mr. Warshaw, all right. With regard to proposal nine? Mr. Hollon and Mr. Carlson. And with regard to proposal 10? Okay.

I don't know to what extent you can make your travel plans. I know that the weather is expected to turn severe this afternoon and this evening. I don't know how long this will take. It looks to me that we will be here until this afternoon.

Mr. Warshaw, would you like to call your witness at this time?

MR. WARSHAW: Yes, I will. Carl Herbein, please. And if I could have these marked as exhibits.

JUDGE CLIFTON: This is going to be Exhibit 20. This is Mr. Herbein's curriculum vitae. Mr. Herbein, while you are there, will you say your names and spell them and identify your employment, please.

THE WITNESS: Carl D. Herbein. C-A-R-L, D., H-E-R-B-E-I-N, and I am the CPA and managing partner of Herbein & Company, a certified public accounting firm headquartered in Reading, Pennsylvania.

JUDGE CLIFTON: Thank you. We will have your curriculum vitae marked as Exhibit 20.

(Exhibit 20 is marked for identification.)

MR. WARSHAW: And if I could have this marked in advance as Exhibit 21.

JUDGE CLIFTON: And Exhibit 21 is entitle Mideast Marketing Order, Federal Order 33 and it indicates presented by Carl D. Herbein, CPA.

(Exhibit 21 is marked for identification.)

JUDGE CLIFTON: Are there additional copies, Mr. Warshaw?

MR. WARSHAW: Yes.

JUDGE CLIFTON: We will go off record while you do that.

(Off the record.)

JUDGE CLIFTON: Do you wish to move the admission of Exhibits 20 and 21 before Mr. Herbein testifies?

MR. WARSHAW: I think if they are acceptable at this point, that would be fine.

JUDGE CLIFTON: Let's see if it is acceptable. It gives the witness more freedom with regard to covering his statement if he knows that the statement is an exhibit. With regard to Exhibit 20, which is Mr. Herbein's curriculum vitae, is there any objection to the admission into evidence that document? There is none and Exhibit 20 is hereby admitted into evidence.

(Exhibit 20 is received into evidence.)

JUDGE CLIFTON: With regard to Mr. Herbein's statement, which we have marked as Exhibit 21, is there any objection to the admission into evidence of that document? There is none and Exhibit 21 is also admitted into evidence.

(Exhibit 21 is received into evidence.)

JUDGE CLIFTON: Mr. Herbein, would you raise your right hand, please.

Whereupon,

CARL HERBEIN

called as a witness, after first being duly sworn, testified as follows:

JUDGE CLIFTON: Mr. Warshaw, you may proceed.

DIRECT EXAMINATION

BY MR. WARSHAW:

Q Mr. Herbein, what I would first like to do is go through your CV and let me ask you at the outset, does your curriculum vitae accurately set forth your educational and employment background?

A Yes, it does.

Q Does it also state accurately your specific dairy-related experience?

A Yes, sir, it does.

Q And your litigation support experience?

A Yes, it does.

Q Running through it very quickly, could you describe for us briefly your education background?

A Yes, I have a Bachelor of Science degree in accounting from Elizabethtown College in Pennsylvania in 1968 and I am a certified public account in the State of Pennsylvania.

Q And your employment background?

A I began my career in 1967 with the national firm of what is now Ernst & Young and in 1972 began what is now Herbein & Company and have actually had two jobs in my life.

Q Could you describe Herbein & Company for us?

A Yes, we are a CPA firm with offices throughout Pennsylvania and we are headquartered at Reading, Pennsylvania and we have a significant portion of our practice in the dairy foods industry.

Q Now, your curriculum vitae, and I don't think we need to go into this, also sets forth profession and civic associations and designations. I assume again that that is an accurate description of those activities?

A Yes, it is.

Q Moving then directly to your dairy-related experience, could you describe for us the experience that you have had that has been related to the dairy industry.

A Yes and I am proud to say is where my experience began. I was born and raised on a dairy farm in eastern Pennsylvania and learned the value of butterfat when my father smiled when his tests increased and was saddened when his tests decreased. So, that was the very start of it and our dairy practice actually began with the rate making process with the Pennsylvania Milk Marketing Board in representing processors beginning the mid 70s in presenting financial information to the milk marketing board for the rate making, the milk hearing process and that work led to being the being the regular accounts and auditors for dairy companies.

We developed some special expertise in cost accounting, which has taken us on somewhat of a -- what I will call a national ride. Our dairy practice now covers the vast majority of the United States in cost accounting and forensic and merger and acquisition areas.

Q Are you the accountant for a number of dairy processors, milk processors?

A Yes, we regularly do work for about 50 dairy companies located throughout the United States.

Q Then again, moving to your specific litigation support experience. Would you describe that for us.

A Yes, my litigation support experience is focused heavily in the milk industry and again, having appeared in Federal Order hearings, many PMMB, Pennsylvania Milk Marketing Board hearings and then outside of the milk business in other litigation matters such as contractual disputes, lost earnings, lender liability and professional malpractice.

MR. WARSHAW: Based on that testimony and his curriculum vitae, I would move that Mr. Herbein be accepted as an expert in accounting as it relates to the dairy industry and most particularly, although I move that he be accepted broadly, most particular in cost accounting and accounting as it relates to milk marketing.

JUDGE CLIFTON: Does anyone wish to voir dire the witness with regard to his qualifications as an expert in accounting as it relates to the dairy industry and particularly in regard to his cost accounting expertise related to milk marketing? Is there any objection to his being accepted as an expert in those fields? There is none and, Mr. Herbein, I accept your testimony as that of an expert in accounting as it relates to the dairy industry and particularly with cost accounting expertise in the milk marketing area.

THE WITNESS: Thank you.

BY MR. WARSHAW:

Q First of all, you were engaged by a group of dealers with regard to this particular hearing?

A Yes, I was.

Q Could you describe the scope of that engagement, the reason for it?

A Yes, the background, Mr. Warshaw, with this engagement was a contact by the Dairy Association of Western Pennsylvania, which is a group of fluid milk processors located in and around Pittsburgh, who are regulated by Federal Order 33, and their initial observation and concern was that they noticed that the Federal Order 33 PPD was decreasing and that there were increasing amounts of milk being pooled on Federal Order 33 and we had a meeting to discuss this matter as they saw it and they asked me to investigate this situation and determine what was happening.

Of course, by this time many of dairy publications were focusing on this phenomena that was happening in Federal Order 33 and we then put together a group of fluid milk processors and they are actually listed on the first page of my exhibit and for the record, they are Dean Dairy Products, Schneiders Dairy, Turner Dairy Farms, Marburger Farm Dairy, Inc., Fike's Dairy, Inc., United Dairy, Carl Colteryahn Dairy, Superior Dairy, Goshen Dairy, Smith Dairy Products and Reiter Dairy.

And we were asked to perform and analysis of what was happening in Federal Order 33 and at that point, spoke with the market administrator to determine was there going to be a hearing and was advised that it was expected that there would be a hearing.

We became an interested party, obtained copies of the various proposals that were submitted to the market administrator and then began our work to analyze the various proposals and to determine what positions our clients wanted to have presented at his hearing with respect to the activities in Order 33.

Q What was the nature of the analysis you conducted? In other words, what effect were you trying to study?

A The two primary effects were the potential financial impact on the fluid milk processors regulated by this order. In other words, if proposals are being put forward that have a negative financial impact, we were asked to analyze that and to determine if that was appropriate and if it was inappropriate, what sort of presentation should be made to present at the hearing the effects of that. And the second thing -- this was actually the first thing, was what is the effect of these various proposals on the independent producers that supply much of the milk to this group of fluid milk processors. That was really the initial concern, was the lower of the milk checks to the individual producers, which was causing strain on the producer community, the communities that supply many of these plants.

Q To put it in the vernacular, so what? I mean why did your clients care about that?

A They care about their producers, because the producers have to be successful so that their businesses can grow and prosper and their is a need for an adequate supply of milk in this market. Those of us who are in the dairy industry on a regular basis are seeing producers leaving the industry, retiring, selling out, going out of business for a number of reasons and some of those reasons are economics.

So, it's our client's position that to have a healthy producer, is a big step in having a healthy company. So, their concern is -- it is a little hard to see at first blush -- if your raw material cost is going down, why you would be upset about that as a businessman, but in the milk industry, when the costs go down, that could be a very temporary thing. You could lose access to your raw materials and you are quickly out of business, especially in the milk business because of the transportation and shelf life and so forth.

Q Have you had an opportunity to review the existing milk marketing order?

A Yes, I have.

Q Are you familiar with the orders which regulated the area which is now covered by Order 33 prior to January 1, 2000?

A Yes.

Q Are you aware of any changes in the manner in which producers were paid, which was affected by the enactment of Order 33 -- or the effectiveness of Order 33 on January 1, 2000?

A Yes, there was a change in when the producers were to be paid.

Q What was that change?

A The advance payment was originally the last day of the month and it was moved to the 26th of the month.

Q Did you have an opportunity to study the effect of that change?

A Yes, I have.

Q Turning to the first page after the title page of Exhibit 21, is that an exhibit which shows us the effects of the changes which took place on January 1, 2000?

A Yes, and there is actually a second change that I didn't complete my answer. At the bottom of the page, we also note that the final payment was changed from the 18th to the 17th, so in effect what happened with the Federal Order reform on 1-1-2000 for January of 2000 was that the regulated handlers had to pay the farmers earlier.

Q And again, this exhibit shows us the effect of that?

A Yes, what I have done in this particular exhibit is taking from September of 2000 through August of 2001 and taken the entire pool of Federal Order 33 and calculated the effect of the change in requirements to analyze for this hearing and for the record and for USDA what financial pressures this placed on the regulated handlers and there are two things that happened that are significant and the easiest to handle, which is kind of a by-product.

There is an annual interest cost associated with this for the value of the money cost.

When we pay something earlier, there is an economic cost associated with that. That economic cost in the advanced payment has been calculated using a seven percent value of money or interest rate at $823,335 and the final payment change has a cost of $1,840,363.

The effect that this has, Mr. Warshaw, upon the financial condition of the regulated handlers is that it's very typical in the dairy industry to have lines of credit, where the companies have arrangements with banks typically to finance their accounts receivable inventory. And when we have a raw material, as we do in the dairy industry of raw milk, with required payments on a certain date, you lose the opportunities that many businesses have in being able to juggle receipts and disbursements a day or two one way or the other. In the milk industry, of course, you can't do that.

So, when USDA advanced those payments, it caused the companies in many cases, to need to draw on their line of credit earlier, so it absorbed some of their credit worthiness and reduced their line of credit balances.

Q It cost them more.

A And cost them more interest. So, this first page shows the effect of that. So, for example, in the advanced payment which averaged 81 million dollars, essentially what we have done is moved 81 million dollars four days earlier from the processor to the farm and that four-day window of economic cost is the interest of $823,000.

Same is true with the final payments where we have a final payment movement of one day of 113 million dollars, so it's sizable and it's placed financial strain on the processors and I thought it was important to have this as a basis upon which USDA could review one of the proposals that is before this hearing.

Q You are not suggesting that these dates be changed back to the pre-January 1, 2000, are you?

A No, I am not suggesting that. Our clients have adjusted their financial affairs to accommodate these requirements and we believe that industry is in compliance with these payments requirements, but it is a fact that I believe this hearing should consider.

Q And in return, of course, there was a benefit to the farmers by being paid earlier.

A Yes.

Q And nobody is begrudging that benefit.

A No, there was a -- there has been an effort, especially in this order and with this group of companies to attempt to help the producer community in many ways and this is one of the ways that that has been accomplished.

Q Now, let me ask you to turn to proposal four. What do you understand proposal four to do?

A Proposal four is designed to increase the amount of the advanced payment.

Q Have you -- that would increase the amount of money which the producers would have to pay up front for the milk?

A That is correct.

Q Have you analyzed proposal four for what, if any, effect it will have on the processors?

A Yes, I have.

Q Is that set forth in the next page of Exhibit 21?

A Yes, it is.

Q Could you tell us what you found?

A Yes.

Q And refer to the exhibit obviously when you are doing that.

A First of all, the time period for my study was September of 2000 through August of 2001 using the information from Federal Order 33 website to analyze the effect of this change in this particular proposal.

Again, this exhibit shows my calculations of the higher advanced payment which averages just a bit over $8,000,000 and again, I have utilized a seven percent interest rate to analyze the cost and have calculated the number of days that this advanced payment would be outstanding until the next month.

And this is a monthly occurrence, because we are required to make these advance payments each month and the bottom line of this is that we will be extracting $8,130,882 from the processors. That goes to the producers in a higher amount and earlier than the final payment. The interest cost is actually the difference between the final payment -- the advance payment and the final payment and that is when this $8,000,000 would be outstanding.

And the annual cost to all regulated handlers in Federal Order 33 based on the year that I studied is $402,311.

Q Is that a cash flow issue or is that an actual revenue issue?

A Yes, to both, Mr. Warshaw. First of all, it's a cash flow issue, because as I mentioned earlier, the average regulated handler draws on a line of credit to make these payments, so we'll be drawing earlier on our line of credit of $8,000,000 on an aggregate for the 21 days between the advance and the final payment and that would be an $8,000,000 draw.

And there is also a cost associated with that and that is the economic cost that happens each month when we make these higher payments and at a seven percent interest rate, that amounts to $402,000.

Again, if USDA in analyzing this wishes use a lower or a higher interest rate, it's simply a matter of making that calculation and I believe that there has been a down tick in the interest because of the current economic circumstances since I made this analysis, but it's my understanding and reading that the current very low level of interest is not expected to be long, long term and these federal orders are expected to stay in place and operate in to the future, so I believe seven percent is a reasonable amount to use.

Q And this is an amount that would be repetitive each year into the future if proposal four were to be adopted?

A Yes.

Q The point of this is -- I guess the processors have already switched to the January 1, 2000 change. Why not just accept this change?

A The position of our clients and I believe the appropriate position is the way to fix the producer payment situation, to get the producers more money in Federal Order 33, is not to tinker with the payment mechanism, but to tighten up the pooling provisions in the order. So, we believe -- we understand the producer groups wanting to improve their economic circumstance because they have been harmed in, but we don't believe this is one of the ways it should be down, because that harms the processors and we are posted that.

Q Moving then to this pooling issue, did you have an opportunity to study the effect of paper pooling on the producer price differential?

A Yes.

Q And the next day to this exhibit, does that address that issue?

A Yes, it does.

Q Could you explain that exhibit to us?

A Yes, essentially what we have done here for the period January of 2001 through August of 2001 is to utilize information, again produced by the market administrator, to analyze the effect of milk that was not historically pooled in Order 33, that was pool during this age month period and we did a but for calculation. If it weren't for this not historically pooled milk coming in to this order, out what would be PPD have been?

And the effect, to cut to the chase, is shown in the far right column and we have during this eight month period an average reduction in the PPD of 55 cents per hundredweight with a fairly significant range from 31 cents at a low and a high a 72 cents.

This is really money out of the pockets of the producers that supply milk to our clients and we believe that a tightening of the pooling requirement should be accomplished and we believe that would be good for the producer markets and in turn, that is good for the processors.

Q Let me ask you about that. Why is a good for the processors?

A It's good for the processors because it affords a higher price of milk to the producers that are serving this market and is the main issue. The fluid milk industry is largely a localized market. Fluid milk travel several hundred miles fairly easily, but beyond that, it really doesn't, because of the cost and the shelf life situation.

So, a processor located in Order 33 likes to have a raw milk supply within his community. It saves on transportation leading that processor to be successful so that he can add cows. We have a need for milk, so the economics of the farmer are very critical.

Q Isn't it also true that this affects the amount of money that the processors have to pay for their milk, to attract milk into the area?

A Yes, that is another finding an hour review of this. When the PPD goes down, they need to pay voluntary premiums, quality premiums or just simply supplied premiums by the processors goes up and that has an economic impact on the processors where those premiums can't be passed on through to the customers. So, there is a downside that we have an inexperienced here recently.

Q Let me ask you whether or not you have any comments on the proposals, a couple of the proposals. First of all, turning to proposal number three, to you have any comments regarding the proposal?

A Yes, proposal number three has been reviewed with the processors that we are representing at this hearing and we believe that a requirement of three days of production would be in order to tighten up pooling requirements.

Q Other than that comment, are you in agreement with proposal three?

A Yes.

Q Let's turn then to proposal eight. That is a proposal submitted by your clients?

A Yes.

Q What does that proposal attempt to do?

A One of the issues that created some market instability in the past has been the ability to what I will call jump in and out of the pool and we believe and our studies have shown that causes instability, causes milk to want to move in directions that it wouldn't normally move.

So essentially what we are saying in this proposal is that we believe that if a handler elects out of the pool, they shouldn't be allowed back in for a six-month period of time.

Q Why is that?

A For stability purposes in the marketplace.

Q Why is there instability caused by being able to de-pool and pool?

A The experience we saw in the latter 1999. We had a very unusual class-price inversion. It caused the handlers, the Class III handlers to have an economic incentive to jump out of the pool because the blend price was lower than the Class III price and that cost the sale of surplus milk and the cost of milk to a Class III processor to be somewhat at odds with one another for a short period of time and that caused instability in the surplus milk market, particularly in western Pennsylvania where we saw this firsthand.

Q Did it have an adverse impact on those processors to stay in the pool?

A Yes, it did because the producers that were regulated by the processors who brought the milk from the producers that remained in the pool had a lower pool value than they would have had had that de-pooling not occurred, so it affected the producers as well.

Q Did it have any special effect on Pennsylvania processors?

A Yes, it did.

Q What was that?

A The Pennsylvania processors found out after the smoke cleared that the Pennsylvania producer payment requirements were that class price had to be paid and consequently we had one of the circumstances where a legal federal ordered price for Order 36 at this time was not sufficient to cover the Pennsylvania requirements.

So, the handlers had to pay their producers more than they originally anticipated. So, that was another, I guess, issue that caused instability in the marketplace and those handlers were then required by the Pennsylvania milk marketing board to make those payments and those payments were made.

Q Do you have any problem with DFA's proposal to do away with the free ride portion for section that is covered here?

A None whatsoever.

Q You would have no problem with their

proposal number two?

A No, we believe that is consistent with the position of the processors that we represent.

Q Then finally proposal number nine, essentially we agreed to replace that with proposal number three with the condition that we are in favor of a three-day touch base period instead of two?

A That is correct.

Q Do you have any opinion whether this should be handled as a emergency matter as opposed to allowing comment period on proposed changes?

A It's my opinion that USDA should proceed on an emergency basis. I was present yesterday and I heard the testimony yesterday and agree with the witnesses that requested emergency proceeding. I believe that the economic damage to the producers is something that should be dealt with as soon as possible.

MR. WARSHAW: No further questions at this time.

JUDGE CLIFTON: Thank you, Mr. Warshaw. Additional questions, please, for Mr. Herbein. Mr. Yale.

CROSS-EXAMINATION

BY MR. YALE:

Q Good morning. Ben Yale on behalf of Continental Dairy Products. I tried to write as fast as I could and still be able to read it, so I hope I don't misquote this. A couple times in your testimony you talked about the economic needs of the farmers and early on you said something about producers have to be successful so that their business can grow and prosper. Do you recall making a statement similar to that?

A Yes.

Q And you agree --

A Yes, it's been my experience in representing processing dairy companies that to have healthy producers in the marketplace is essential to good economics for a processor, because if you don't have an adequate supply if milk and you are in the dairy business, ice cream, fluid milk, whatever it might be, and you have to import that milk, there is a cost associated with it and there is also a quality issue. Somehow, milk that travels many, many, many miles doesn't seem to be quite as good as milk that is close at hand.

I am repeating what I have heard from our clients. The ability to help the farmer manage his business and produce a high quality milk is much easier if the farmer is within 30 or 50 miles of your plant that if he is 500 or 1,000 miles away where you really can't see him.

Q It goes along with the other statement made a little more recently that economics of the farmer is very critical, so the same thing --

A Yes, that is my personal opinion.

Q You would agree, would you not, that this issue of the advance payment is a question of really the time value of money, right?

A Yes, sir.

Q And it's a question in the sense of cash flow for business, right?

A It is an issue of cash flow for business.

Q And that applies equally to the farmer as it does to the processor, does it not?

A I'm glad I am testifying after the producers testified yesterday because it was pretty clear yesterday -- I believe a producer may be in a position to manage the timing during the month when they have their payment requirements a little differently hand a regulated handler, because as we heard from several of the farmer witnesses yesterday -- and I can remember my father when he got his milk check and when he paid his bills, the issue with the producer is that it appears from yesterday's testimony that they can schedule their bank payments according to when they receive their advance and final payments.

And the point that the processors can't

do, as I attempted to explain, is we have payments requirements by Federal Order 33 as to when we must pay and we can't call and say we would like to be a day late this week, this month. So, I think it is a little bit more severe on the processor side and that is part of why we are recommending that the payment formula not be changed.

Q But you would agree that even though they adjust their payments that they still have to pay for any delay in those payments at increased interest cost, even just a few days; is that correct?

A Yes, I am not at all disputing the point that it's a time value of money that is on both sides. Again, I think that the processor has a little less flexibility than the producer.

Q Do you have any knowledge as to whether in general the cost of money to farmers is higher or lower than the cost to your clients?

A I would say that there are some farm loan programs that result in slightly lower interest charges to farmers, but the difference between the cost of capital for a major farming operation or a major dairy operation would be pretty similar.

Q I want to go back. You made a comment that you had reviewed the previous order. Did you look at all five previous orders?

A I am most familiar with Federal Order 36, which is the order that regulated western Pennsylvania and eastern Ohio where we have done a lot of work for many years. I am less familiar with the other orders.

Q Are you aware that in Order 40 in southern Michigan that the payments for the last day of the month for the advance and he 15th for the final?

A Yes, I did actually kind of refresh my memory in seeing the schedule that was produced yesterday and when Federal Order reform was taking place, we did a review of what was going to happen or what we thought might happen in some orders where we had client concentrations, so we did look at those orders during the summer and fall of 1999.

Q Does your exhibit that talks about this additional cost of interest because of the change in the payment dates reflect the fact that for Michigan that the final was moved back instead of forward?

A No, it does not.

Q Even with an advance payment, you would agree that producers have delivered milk anywhere from 25 to 11 days prior to that payment, right?

A Yes, absolutely.

Q And that on a final -- of course they

haven't been paid in full for the first 15 days, but assuming that they had, that it runs 17 to 31 days that they wait for payment?

A Yes, the producer has a waiting period and it's been my finding that in the last 10 years the dairy food manufacturer, really through all of the classes, has a longer wait from his customers. We are seeing accounts receivable turnover in the dairy industry slow down somewhat.

Some of that is the health of the super market chains. Some of that is the consolidation and the muscle that the buyers of our clients products have. They just pay a little slower, so we are feeling the crunch and that is frankly part of why we present this, because we think it would be difficult for the processors who absorb more squeezing that they are already getting from their customers.

Q Have you ever seen the policy of the Class I price, the set up of the Class I price based upon the cost of money to handlers?

A No, I have not seen that, but I believe it should be an issue.

Q You in your table on the advance payments, on this change, you indicated a cost of $400,000, annual interest cost?

A Yes.

Q As compared to 165 million hundredweight?

A That's correct.

Q Did you do for a hundredweight computation of that?

A I did not.

Q Wouldn't you agree that it's about two to three tenths -- or one percent for a hundredweight?

A Yes, it certainly would be. I think that is a good estimate.

Q I want to talk here a minute about the pooling and your request for three days. Would you acknowledge that there are a significant number of producers that are picked up every other day?

A Yes, that is our finding and that is our client's experience.

Q So a three day pick-up may very well end up meaning the four day pick-up?

A For some producers, I believe it would, yes.

Q Now, I think that this gets back to kind of an understanding. I want to try to find out from you what you understand. If there is a distant supply plant. I mean, let's say one that is north and west of the marketing area in some of the states like Minnesota or

Wisconsin.

A Yes.

Q And is it your understanding that a producer in order to meet the touch base has to touch base to a pool distributing plant or to that plant that is in Minnesota or Wisconsin?

A To the plant in Minnesota or Wisconsin.

Q So, if this plant is 15, 20 miles a way, what dis-incentive is this extra day on the pool?

A I'm sorry, I mis-spoke. That is not the intention of the touch provision of -- to touch that plant, but to touch the pool plant.

Q But hat supply plant if it is a pool plant is eligible for touching base, is it not?

A Yes, it would be.

Q So, having a farmer 500 or 600 miles away from the market only having to go 10 or 15 miles to a supply plant to touch base another day, is not a very significant dis-incentive, is it?

A It has to be -- in an by itself, it's not. The position on the tightening of the pooling requirements that our clients suggest is that this is one of a part of a number of tightening requirements that would make pooling more difficult.

Q Did you do any analysis of what the extra day aside from anything else would do in terms of reducing the amount of what you need of the excess milk pool on the order?

A No, this, as I think -- the three day requirement was a matter of a meeting that all of the companies had and we discussed this particular touch requirement and three days was the majority opinion of our clients and that is how the three days was arrived at. There was no independent study done on that issue.

Q I want to move on to your proposal on the pooling. You indicated market conditions in 1999 because of some inversion in Class prices was a concern of yours, right?

A Yes, it was a historical occurrence in '99.

Q In 1999 the advance pricing was done different from what it has done today, right?

A Yes, absolutely.

Q And there is a whole month shipped in terms of bringing the two prices together, is there not?

A Yes, absolutely.

Q And there is also now the higher of three or four?

A That's correct.

Q And since 2000, have we seen any of these

Class inversions?

A No, we have not.

Q But we have had some rapid price increases in the commodities during that period, have we not?

A We have.

Q Have you done an analysis to determine the likelihood under the current advanced pricing formulas that we would have the kind of Class inversions that we saw in 1999?

A I believe that it's unlikely to occur and we discussed this at some length with the companies that we are representing. However, in an effort to do some, what I will call clean up work on Federal Order 33, we believe that it's a provision that should be removed and I say that recognizing the efforts and the study that went into Federal Order reform itself. I echo the testimony yesterday from some of the witnesses that thank USDA for the work and I participated as an observer to that process and again, we think this is unlikely to occur, the price inversion because of the changes in the formulas and the timing, but we believe it serves no useful purpose in the order.

MR. YALE: I have no other questions.

JUDGE CLIFTON: Thank you, Mr. Yale. Other questions for Mr. Herbein? Yes, Mr. Beshore.

CROSS-EXAMINATION

BY MR. BESHORE:

Q Good morning, Carl.

A Good morning, Marvin.

Q I want to start with the pooling proposals and make sure that I heard or understood the position of the dairies that you are representing today with respect to those proposals. Are you taking a position with respect to proposal number one, which is the proposal that would adjust the definition for distributing plant operations?

A Yes, we believe that we are in support of proposal number one.

Q Now, with respect to proposal number two, did I understand you to be also in support of that with the caveat that you would support the further revisions to the supply plant definitions set forth in proposal eight?

A That is correct.

Q Does your support include the modifications to proposal two that Mr. Hollon described yesterday with respect to changing the ability of a supply plant to qualify itself with producers distant from the supply plant and located closer to the market? do you support those adjustments?

A That was testimony which I did hear and have not had an opportunity to review with our clients, so I don't have an opinion on that.

Q And with respect to proposal three, you are supporting three days rather than two days increase on the touch base.

A Yes.

Q But you are supporting the 60 percent and 70 percent changes in the diversion limitations set forth in proposal three?

A Yes, our clients support the 60 and 70 percent.

Q Now, what about proposal five? Did you -- proposal five would eliminate the so-called split plant provisions in Order 33.

A We have no group position on that proposal.

Q Moving on to proposal four, I think you indicated in response to questions from Mr. Yale that you did not adjust your calculations on the first exhibit, expert for the fact that producers in the Order 40 portion of Order 33 have had a three-day delay in their final pay.

A That is correct. We did not consider that.

Q And the first calculation, your first exhibit with respect to the effect of payment dates in the order reform does not take into account the fact that the advance amount has -- or does it take in to account, the fact that the amount of the advance has been reduced?

A No. This -- let me qualify that. This is the calculation of the -- from September of 2000 through August of 2001, of the actual payment, so it does take into account -- I mean, these are real numbers.

Q Right.

A So, it would take into account the difference in the amount.

Q But it doesn't take into account that under the pre-reform scenario, the amount of the advance although later, was higher?

A That is correct. That is not in the calculation.

Q So, with that adjustment at least and the adjustment that wasn't made for the Order 40 delay in final payment, if you were showing fully accurate change in the financial effect of the cash flow provisions, you have to at least make those adjustments.

A Yes, and that would reduce this amount somewhat.

Q You are using a seven percent interest rate and I think you did explain that somewhat. Are you saying that that is the average marginal cost of capital for working capital for your dairies?

A Yes, think yes, during this time period of September through August that would be an estimate. Interest rates are slightly lower right now, but again, as I talk to bankers that are financing our clients, the anticipation is that five and a half percent prime is not going to continue. It's an economic stimulus effort by Washington, which the business communities certain need at this point.

Q And your clients are basically able to access lines of credit for working capital at the prime interest rate?

A I wouldn't say that. We have certainly in our client group, we have some that are at prime. We have some that are above prime and we have some that have room in their line of credit balance to advance additional finds and we have others that are juggling the ball to try to make ends meet, so we are concerned about those companies.

Q How many of your -- a couple of your groups are members -- your dairies are large public companies -- Dean Dairy Products.

A Yes.

Q And they have access to the public capital markets for capital, correct?

A Yes, Dean -- historically has had access to the public market. They are a public company.

Q Do you know any dairy farmers that have access to those capital markets in the way that Dean does for their marginal working capital?

A Dean's current access may be the same as dairy farmers. No, dairy farmers would not have access to the public markets.

Q By the way, in terms of the financing impact on --

A I think I just lost a client.

Q I think that they are looking at a major change in organization here anyway.

A That is what you would determine by reading the dairy publications.

Q By the way, with respect to these financial impacts here, would you agree with me that we are really talking about the marginal cost of capital for both dairy farmers and dairy handlers?

A Yes, we are talking about the time value of money.

Q But at the margin. In other words, if either the dairy plant or the dairy farmer does not have this amount of money that we are talking about here in their bank account, they are going to apply it to the most expensive account they have presumably. It's going to be applied in good management to the most expensive account, what you call marginal expenses, agreed?

A Yes, that would be the way business typically operates.

Q Now, are you aware of the cost of carrying accounts for farm supplies on dairy farms?

A Yes.

Q Fertilizer accounts, gas accounts, accounts like that?

A Yes, I am familiar with those sorts of open accounts that farmers have with their suppliers.

Q And typically, you would be aware then that the monthly cost of carrying those accounts is one percent or in that range per month?

A Many suppliers to dairy farms have monthly interest charges, yes. I have seen that.

Q That would be the, would it not, the best measure of the marginal cost to a dairy farmer of losing any cash flow by having his advance milk check less than it would be otherwise?

A Yes, that would certainly be one of the potential effects. Again, as I said in my direct testimony, we believe that the way to fix the farmer's accounts payable problem, if he has one, is by tightening the pooling provisions, so that more money is distributed to the Order 33 regulated producers, rather than trying to pull some money out of the processors, where I believe it is difficult and risky to do that.

Q Well, we are really looking at your second exhibit -- we are looking at -- assuming the accuracy of these calculations, which I am not questioning -- we are really looking at who is going to bear -- that is the dairy farmers in Order 33 or the handlers in aggregate in Order 33, who is going to bear the annual interest cost of $402,311.59 that you have calculated as the economic effect of proposal four.

A Yes, that is exactly the point, Mr. Beshore, who should bear that our client's position and my profession opinion is that since this is a requested change, it should not be granted. We should stay where we are, with the payments requirements. The market has adjusted to those payment requirements and we fully understand the farm community's desire to improve their economic position, but we believe that this is not the right way to do it.

Q In other words, you believe that dairy farmers should bear that interest cost rather than the milk handlers.

A We think that the dairy farmers should bear the costs that they are bearing now as to interest costs, because again, this is a reaction to DFA's proposal for changing the advance. And we are not recommending as Mr. Warshaw mentioned, we are not recommending any deterioration in amount or time to the producers. We believe that where we are now has been assimilated in the market and we think it's where it should stay.

Q Do you have any dispute with the comments that were made by the dairy farmer representatives yesterday, that the advance, the rate of advance payment has declined since January 2000?

A No, that is factual. I did have a slight difference of opinion with one of the producer representatives who gave a ratio between advance and final that I didn't think was accurate and believe that he was talking about a net check after some deductions in his case, but I think the regulations are clear as to how much you have to pay and when you pay it, so I think the USDA would be clear on that.

Q Let me move to proposal eight. Proposal addresses solely the supply plant pooling provisions in the order. That is correct, is it not?

A I believe so, yes.

Q So, to the extent that there may be economic reasons from time to time that handlers or producers would choose to de-pool producer milk that is not pooled at a supply plant, this proposal would not have any effect on that.

A That's correct.

Q So, if your handlers, for instance, any of the handlers you represent are pooling milk at their distributing plants by diversion, that is reporting it on their pool reports, but having it delivered to plants wherever they may be, processing Class II, Class III or Class IV products, it would have no impact on their ability to opportunistically pool or de-pool that milk, isn't that correct?

A Yes, and the objective here, Mr. Beshore, is to -- there is a balancing function that the Class II, III and IV processors in this market perform for the fluid part of the industry and we believe that that should continue. We believe that the experience that I explained in 1999 in response to Mr. Yale's question, we -- I believe it unlikely because of the new rules and the way the prices and the timing and the calculations that we will have that inversion, but we believe it's a clean-up kind of thing in the order.

Q But I am wondering whether it's cleaning up what you are identifying as a problem or not. I am not assuming it's a problem, but I want to explore what you have to clean up here. Are you aware whether or not the dairies you represent pool producer milk, report producers on that pool report and have their milk delivered, the producer's milk delivered to cheese plants on diversion?

A I believe that that does happen.

Q In fact, it happens in very substantial volumes on a regular basis, does it not?

A I believe so, yes.

Q And the particular problem that is supposed to be addressed by proposal eight wa a situation where the Class III cheese price was higher than the blend price, correct?

A That's correct. That's what occurred in 1999.

Q Now, if your clients are pooling milk that is delivered to cheese plants by diversion and they want to avoid making a payment into the Order 33 pool on that milk when the Class III price of cheese is higher than the blend price, proposal eight could be adopted and they could still avoid that payment by simply not reporting the milk on their pool report; isn't that correct?

A I believe that would be the effect.

Q So, proposal wouldn't affect that ability one whit for distributing plant to de-pool milk diverted to cheese plants if there were to be another price inversion, correct?

A That is my understanding of it, yes.

Q I have just one further question. Do you have a calculator?

A I do.

Q If you take your second exhibit, which is the one that calculates the annual interest cost for proposal four at $402,311.59 -- do you know what that -- how much that would be on a monthly basis to each distributing plant handler in Order 33? Could you do that calculation? Assume that there are 47 distributing plants according to the market administrator's documents in Order 33 -- 12 months of the year.

A What you are asking me to do is divide the 402,000 annual interest cost by 47 handlers and come up with an average cost per handler.

Q Per month.

A Per year it's $8,559 and per month it would be $713.

MR. BESHORE: Thank you.

JUDGE CLIFTON: Thank you, Mr. Beshore. Mr. Carlson, you have questions for Mr. Herbein?

CROSS-EXAMINATION

BY MR. CARLSON:

Q Mr. Herbein, in Mr. Warshaw's questioning of you, he talked about paper pooling and the additional milk supplies that have been attached to this market. Would you term that situation, that paper pooling as disorderly marketing?

A Yes.

Q In your discussions, as I understand it, you are basically supporting proposal three and withdrawing your support for proposal nine, but asking that proposal three go to three days of production being received from individual producers?

A Yes.

Q Is there a concern -- you talk about in questioning -- every other day shipments? In effect you are talking about four days production for those producers, right?

A Yes, we recognize that in our position of three and as I said earlier, Rodney, the three days was arrived at by consensus of the companies.

Q Any concern about fairness issues, about certain producers that are picked up every day now having to deliver only three days where every other day shippers have to deliver four days?

A There was some discussion about that and we arrived at three days frankly as a compromise. There were some twos and fours and that seemed to be in the middle, I believe.

Q Yes, three is.

A That is about as much humor as you will get out of numbers.

Q The biggest difference between proposal nine and proposal three probably is the requirement under proposal nine that milk be physically received before it can be used for diversion qualification purposes. Was there any discussion in your group about that situation, that difference between proposal three and proposal nine?

Q No, there really wasn't and I would like to just answer that by adding one other comment. The details -- and this is a very finite detail in this Order, our group's position was more from 20,000 feet -- we need to tighten the provisions to have a more orderly marketing situation and we really didn't drill down into all of this detail. However, we did review all of the proposals and those proposals that included those specifics were discussed and we agreed with some and some we decided not to have a position on and some we have a slightly different position, but that is a detail that was not discussed by our group.

Q The general thing is just to tighten up pooling requirements.

A Yes, that is the message from the fluid industry -- from the fluid handlers that we represent.

MR. CARLSON: Thank you very much.

JUDGE CLIFTON: Thank you, Mr. Carlson. Mr. Hahn, you may proceed.

CROSS-EXAMINATION

BY MR. HAHN:

Q Good morning. Jim Hahn, from LOL.

A Good morning, Jim.

Q Mr. Carlson referenced paper pooling and I would like to ask you a couple questions with regard to paper pooling. LOL sells a significant volume of milk to a number of your clients and that milk is received at supply plants and at least 30 percent of the milk received in those supply plants is delivered to some of your clients. All of that milk stays in those plants. None of it is back-hauled. Would you characterize that as paper pooling? That milk is destine for Class I markets. Would you classify that as paper pooling?

A The concept of paper pooling as we discussed it in our meetings and in our research dealt with milk that did not serve the market. The concept of milk serving the market, being part of the normal supply, was mentioned time and time again by our clients to me in those meetings, so I would say that milk that is serving the market would not be part of the generic paper pooling that we have been talking about here in the last two days.

Q We also heard references yesterday and today about the fact that Order 33 is a deficit market and the fact that LOL is servicing some of your clients and thereby alleviating some of their balancing costs, LOL is bearing some of those balancing costs, would you not agree in servicing that market?

A Jim, I haven't made any analysis of LOL's activities and I certainly know that there is activity in this market and I would imagine that what you have said based on my experience in other studies where we have looked at that that there would be a balancing cost that you would be bearing, but I made no specific study in this area.

Q I realize that. My point is that to the extent that some of your clients are buying additional supplies of milk means that they don't have adequate supplies of their own, so observations they are not faced with the fact that they have certain surplus supplies of milk that they have to dispose of on weekends or during a long season, so in other words, they are not bearing those costs of balancing the market and that comes at a cost savings to those handlers, wouldn't you agree?

A A balancing of milk with a fluid handler has costs. There is no question about that and someone in a market must bear that.

Q Thank you. Would you not agree that the purpose of the Class I differential is to attract supplies of milk for fluid use?

A That is certainly my understanding of Federal Order reform and the new rules that we have. That is the objective.

Q Thank you. One final series of questions. The last page of your exhibit, if you could turn to that, please. I have some questions relative to the assumptions that you used. The seventh column titled actual producer of price differential, I recognize those differentials. Are those the differentials that were announced in Cleveland? In other words, a basing point for Order 33?

A Yes, I believe they are.

Q The producer milk, the third column that produce milk not historically associated with Federal Order 33, did you arrive at the value in the second column from the right by multiplying the actual PPD per hundredweight times the volume of milk not historically associated with Federal Order 33?

A Yes.

Q You are aware, are you not, that the milk is priced where it is receive?

A Yes, plant point pricing.

Q So, if some of this milk was received in southeastern Wisconsin, at locations in southeastern Wisconsin, the credit from the pool would be something other than the $2 announced in Cleveland. In fact, in southeastern Wisconsin it would be $1.75.

A Yes, there would be that occurrence.

Q So to the extent that some of this milk at least was not received in a $2 zone or a $2 pricing point, and if you make the assumption that more of the milk was received in a lesser pricing point than $2 and was received in a higher pricing point than $2, then to that extent, isn't the third column from the right PPD excluding non-traditional producer milk overstated?

A It could be overstated and the reason for making the calculation the way I did was because of availability of information. There isn't any practical way of -- I didn't find any practical way of estimating the effect of that. But you are correct and I agree with you that there is that effect and it would slightly reduce the effect here.

Q You say slightly, but if the southeastern Wisconsin pricing location is $1.75 and I believe that in the market administrator exhibit Cass Clay was listed as a 9(c) handler and I that that area is $1.65. I don't know what volume of milk was associated with the pool. It doesn't make any difference, but to that extent, $1.65 is significantly different than $2, is it not?

A Yes, it is and if all of the milk would have been subject to that difference, then we have a material difference, but I believe that the difference is immaterial and I certainly didn't intend to mislead anyone with how I have done my calculations. I did them the way I did the-mail.

Q And I realize that. I just wanted to point out the fact that I believe that some of this milk was received in pricing points other than Cleveland.

A I would agree with you.

MR. HAHN: Thank you.

JUDGE CLIFTON: Thank you, Mr. Hahn. Mr. English?

CROSS-EXAMINATION

BY MR. ENGLISH:

Q In that last series of questions, when you concluded that -- it take it it was your opinion that any differences would be immaterial. That was what you said basically, that yes, those differences exist, but in terms of the purpose of the chart and evidentiary purposes for this hearing, you view those differences as immaterial ultimately as opposed to material?

A That is correct.

Q And in that instance, you used that term as an expert in accounting?

A Yes.

Q Would you explain what that term means effectively?

A The materiality concept is one chip that is dealt with by CPAs in determining if a set of financial data is acceptable for reporting purposes in a financial statement or in determining how a transaction should be reported and if it is materially wrong, an adjustment is necessary because it misleads the user. Something that is immaterial and doesn't require adjustment, the adjustment is not required because the user of that information isn't misled, so for that purpose and with that background, I use the term immaterial, because I believe the conclusion reached by this exhibit will not misled the user.

MR. ENGLISH: Thank you.

JUDGE CLIFTON: Thank you, Mr. English. Are there any other questions for Mr. Herbein before I ask Mr. Warshaw if he would like to ask additional questions? Mr. Tonak?

CROSS-EXAMINATION

BY MR. TONAK:

Q Good morning.

A Good morning.

Q Again, the on the table in your exhibit concerning effect on PPD, if some of the milk that was -- let me start over again. Those producer settlements are dollars are basically of the Class I, Class II, Class IV differences if any compared to the producer component values; would that be correct?

A Yes.

Q So, if any of this milk that is not historically associated with Federal Order 33 delivered to a Class II operation, the value for the difference between the component value and that Class II value would be included in the producer settlement fund dollars, would that be correct?

A I had a chance to, as we say in Pennsylvania, sleep on that concept because you asked Mr. Hollon that question yesterday, so you interrupted my sleep a bit and frankly -- I don't agree with that. It seems to me in thinking through the mathematics, that if components come into the market to be considered, they are paid out to those producers, so that it doesn't seem that that helps another producer in any way, in my way of thinking through how a producer's milk check is determined. So, I don't believe that that does help the PPD>

Q I do not disagree with you at all that components are paid out. As an example, the Class III butterfat price would be $2.40 per pound and the Class II butterfat price is $2.60 per pound and the payment into the pool for milk delivered as Class II milk from the non-traditional producers would be $2.60 per pound, the payment out of the pool to those non-traditional producers would be the $2.40 per pound. Would that be correct, that the 2.40 and 2.60 were the applicable numbers?

A I think that would be right.

Q And there is a difference there of .20 per pound that would remain in the pool. Would that be correct?

A I think so.

Q And that .20 per pound on the applicable volume would show up in the producer settlement fund dollars that is distributed to all producers in and out of the traditional order area on a pro rata basis in the PPD, would that be correct?

A I see your point differently than I did when I was sleeping on it.

Q I apologize for causing you a loss of sleep. A I was thinking just simply of the mathematics of the components and how they are dealt with and I wasn't focusing on the difference in the butterfat class and I believe you make a point. There would be some perhaps relatively small -- I'm not sure -- that quantify if it's material or immaterial, but I think your mathematics are right.

Q So, in effect, material or immaterial numbers, how materially they affect your exact calculation in the last column, it would change that calculation.

A It could change that calculation slightly.

Q So, in effect, what we have when we look at the PPD lost in that last column is, if you will, a maximum PPD and the actual loss is probably somewhat less.

A The actual loss could be somewhat less for a few of these circumstances and again, we didn't analyze those circumstances in our position of the need to tighten the pooling provisions to prevent this loss regardless of its amount doesn't change.

Q Thank you. If I understood correctly from your earlier response to some questions, your clients are concerned about the pricing the producers are receiving for the milk and that is probably the reason they have asked you to be here, because of the PPD impact.

A Yes, sir.

Q And the basic pricing they are looking at is that Federal Order regulated minimum price -- would that be a correct statement?

A Well, they are obviously looking at their total payment to producers including any premiums or other payments that they are making. They are looking at their cost of milk and they are looking at the mail box price received by the producers.

Q And that Federal Order price is perhaps a major component of that?

A Certainly that is the underpinning for the pricing structure.

Q I imagine some of them are concerned about the PMMB pricing?

A The Pennsylvanians that are part of our group, as a state association -- as part of the Pennsylvania Association of Milk Dealers recently supported the increase in the over-order premium in Pennsylvania and Attorney Warshaw was the person that delivered that good news in Harrisburg a few weeks ago.

Q I imagine your clients have different pricing mechanisms? In other words, they don't all pay exactly the same to their producers?

A Yes, there are lots of different ways of paying producers once you are at the legal requirements.

Q And they probably have different needs for balancing additional milk supplies and so on?

A This group of companies, there were many different methods utilized.

Q You had mentioned to Mr. Hahn in response to a question that you had done some other studies on balancing costs and so on. Do you recall anything of a range of costs involved in those studies?

A The study that I had in the back of my mind actually dealt with a client of our firm that is a balancing operation and when reviewing the costs of that balancing operation, that is really what I was referring to. It's a -- that's a hard number. People in the dairy industry like benchmarks because they don't like to hire accountants to do studies and the benchmark for balancing costs is one that I say you can get a rule of thumb with because of the tremendous effect on the cost from the capacity position. If a powder operation or butter operation is at 40 --operating at 40 capacity, the balancing cost is huge.

If the balancing operation is operating at 70, 80 or 90 percent of capacity, its fixed costs are spread over many more pounds and the balancing cost goes down, so it depends on the market as to what that balancing cost would be and it's a range of 25 cents to maybe a few dollars a hundred. There just isn't a benchmark.

Q Wide variability that somebody has to absorb.

A A wide range of costs and someone has to absorb it. There isn't any doubt about that. Generally accept accounting principles would say someone has to bear that cost.

Q Part of that cost could possibly be offset by milk pooled on the market, delivered to the market by outside the traditional supplies.

A The -- my opinion as to how to evaluate and deal with the balancing costs is to have the individual market handle that internally and I'm not so sure -- this is a personal opinion -- that the intent of the Federal Order system was to allow pooling to handle balancing costs. It seems like that is a little apples and oranges to me personally.

Q Do you have a copy of Exhibit 5 that was introduced yesterday with you?

A I don't have it here with me. Actually -- I do, yes.

Q If you could turn to page three, table two.

A I have it.

Q And under the $2 Class I differential rate, do you find the name of Goshen Dairy Company at New Philadelphia, Ohio?

A I do.

Q I believe they are a client of yours.
A They are a part of our group, that's correct.
Q Under the $2.30 Class I differential rate, do you find one of your clients listed as Fike's Dairy at Uniontown?
A Yes, I see it.
Q You have got other clients listed in those brackets between $2 and $2.30?
A Yes, the plant differentials there with a number of the companies are in different pricing situations.
Q Could that indicate that under the regulated minimum prices they have got as much as a 30 cent price difference in their milk supply costs and at the same time a 30 cent difference in returns paid to producers as far as the Federal Order's minimum regulated price?
A Yes, that is clearly the way the Federal Order of pricing requirements operates and there is -- somebody has an advantage and someone has a disadvantage. There is -- of course, when the differentials came out plant by plant, there was a lot of discussion about that.
Q You testified that you were here yesterday. Did you happen to hear a dairy farmer testify

to the need of a decision in this proceeding on an emergency basis?

A Yes, I heard that testimony.

Q I believe the one of them made indications that there was a large price drop coming and I am presuming because of the cheese and butter market declines that we have seen. Did you hear a statement to that effect?

A I heard that.

Q As your clients adjust pricing or look at various factors that are effecting the minimum price, minimum Federal Order regulated price, would this be one of them that they would take into consideration?

A I'm not -- somehow I lost the track of your question.

Q I may have lost it myself. I believe you made a statement that your clients were concerned about the loss of dollars because of milk being pooled on this order from outside the general order area and things they had to do to offset those dollar losses to help maintain producers in business.

A Yes, I made a statement along those lines.

Q Would you have an opinion as to if they will do something to make up for this loss of -- possible loss of dollars?

A So that we are tracking on the same line, your question is with an anticipated drop in the required price in Federal Order 33, do I expect that the fluid handlers that we are representing will increase their premium amount, the amount above the minimum -- is that the question?

Q Yes.

A It's been my experience that the premium amount does increase when the price drops, but it doesn't seem certainly that it is a dollar for dollar sort of situation and we have also seen that in Pennsylvania with the over order premium. The over order premium doesn't necessarily track with the base federal prices that are effective in the portion of Pennsylvania that is regulated by this order.

There would be some attempt to adjust and a fluid handler or an ice cream manufacturer is faced with competitive situations and I don't know that I have met a fluid milk handler in the recent past that wouldn't love to pay his producers more than he is paying them, but there is a limit to what can go through the pricing mechanism to the customer, because the customer sometimes says hold it, I am not paying any more and some of the processing formulas and contracts that exist in this marketplace are Federal Order plus a certain amount and that doesn't get adjusted every month.

So, a handler has to make a decision are they going to eat that extra -- some of that extra money and this is a small thin margin business that the processors are in, so they can't afford to do too much, but they certainly would try to do something.

Q To try to paraphrase that perhaps, the handlers adjust their pricing to reflect market conditions that the Federal Order system because of its supposed shortfalls or short comings or allowances in pooling don't address?

A You are describing the existence of premiums, which do exist in this market and they are for maintenance of supply, to reward producers for quality, and to maintain a supply of milk in the market and I guess if the Federal Order system were able to be perfect, you wouldn't have that.

MR. TONAK: Thank you.

JUDGE CLIFTON: Thank you, Mr. Tonak. I know there are some more questions for Mr. Herbein, but I would like for us to take a 20-minute break first. Please be back here at 10:40.

(Off the record.)

JUDGE CLIFTON: It's 10:43 and I would like to entertain additional questions for Mr. Herbein. I know Mr. Tosi has some questions, but before he asks them, I want to know if anyone else has additional questions. Mr. Warshaw, did you have any additional questions on what has been covered so far?

MR. WARSHAW: Yes.

REDIRECT EXAMINATION

BY MR. WARSHAW:

Q Carl, I just want to refresh your recollection or ask you to search your recollection for something you may have lost during your sleepless time last night. We regard to proposal one, I think you told Mr. Beshore that the dealers we represent are in agreement with the proposal. Have you had the chance to reconsider that proposal and refresh your recollection as to our position?

A Yes, the subject is the route distribution percentage and the DFA proposal is a 40-35 percent limitation and our client's position is that 30 percent is a sufficient restriction and I did mis-speak on that point, so 30 percent is the companies that we are representing -- their position.

Q That would be a year around requirement?

A Yes.

MR. WARSHAW: I have no further questions at this time. Yes, Mr. Hahn?

MR. HAHN: I just have a follow-up question.

JUDGE CLIFTON: If you will, Mr. Hahn.

CROSS-EXAMINATION

BY MR. HAHN:

Q Carl, in your testimony relative to questions by Mr. Tonak, you indicated it is your belief that balancing costs should be borne internally by the market? I am paraphrasing a little bit, but you made a statement to that effect?

A Yes, I believe that the balancing costs should be borne by the participants in a market.

Q And I don't disagree with that. Is it your belief that the Florida market handles all of their balancing internally?

MR. YALE: Objection, Your Honor, relevance of Florida.

JUDGE CLIFTON: I hear your objections. I don't believe it will take long for this witness to field the question. I'll overrule the objection

THE WITNESS: I haven't studied Florida's balancing, so I'm sorry, but I can't really respond. Can't answer that.

BY MR. HAHN:

Q Do you believe that the southeast market handles all of their balancing costs internally?

MR. ENGLISH: Objection, Your Honor. There are 11 of these, so it's not as fast as you thought.

JUDGE CLIFTON: Thank you, Mr. English. I'll allow this question.

THE WITNESS: I would like to answer it in this respect, simply by restating my opinion where the balancing costs should be borne. A market such as the southeast market which has participants in its serving of that market outside the geographic boundaries and I believe that that is the area, when I say market, that should bear that balancing cost, so that if there is a powder plant that is outside of the southeast order, that is part of that order, then the balancing cost for that plant should be included in the overall consideration.

BY MR. HAHN:

Q Then wouldn't you also agree that in the Appalachian market there are substantial supplemental supplies of milk that come into that market on a seasonal basis and there is balancing that is borne by those servicing that market from outside the area?

A I agree with you that there is milk going into the Appalachian market. I've not studied the balancing effect of that milk. That requires a study that I have not performed.

MR. HAHN: Thank you.

JUDGE CLIFTON: Thank you, Mr. Hahn. Are there any other questions before Mr. Tosi asks his? Mr. Beshore?

CROSS-EXAMINATION

BY MR. BESHORE:

Q Carl, with respect to proposal one, are you aware, have you done any study of the percentages of the operations of the dairies which you represent here, percentages that would applied in the local order?

A Our study, Marvin, in this area was simply a verbal survey or the companies when we met as to the 40 and 35 percent and the position of the group as a consensus ended up at 30 percent being they felt was an adequate restriction.

Q I understand. That is what they want. That is their -- let's keep it at 30, but my question was, have you done any study to provide any information for the record with respect to what the operating percentages are at the present time or have been for the dairies that you are testifying on behalf of?

A No.

MR. BESHORE: Thank you.

JUDGE CLIFTON: Thank you, Mr. Beshore. Any other questions before Mr. Tosi asks his questions?

No. Mr. Tosi.

CROSS-EXAMINATION

BY MR. TOSI:

Q Good morning.

A Good morning.

Q Just a couple questions. You testified earlier that you are familiar the PMMP, the Pennsylvania Milk Marketing Board?

A Yes.

Q Could you please explain for the record how PMMB prices milk? Where do they price milk? At what point?

A At -- what point meaning a producer price?

Q Would you of the opinion that under the Federal Order program milk is priced where is it received?

A Yes, plant point pricing.

Q Is that different from the Pennsylvania program?

A Pennsylvania has a plant pool basis currently for its pricing mechanism, so it is similar.

Q Would it be accurate to characterize Pennsylvania Milk Marketing Board pricing as milk is priced based on where it's sold?

A Yes. Correct. Area by area. Pennsylvania, as you know, has different areas and that determines the price.

Q Do any of your clients engage in what has been referred to throughout these proceedings as paper pooling, pooling distant milk that historically they had not pooled for example?

A Of the companies in our group, the participation in bringing milk into the market has been limited as we found to milk that we considered to serve the market.

Q Is it your opinion then that to the extent that your clients have a milk supply and divert milk during times when milk is not needed to satisfy the Class I market, that the milk that they are diverting is an integral part of that reserve supply of your client's plants?

A I would say that the vast majority of that diversion is part of the balancing of an independent milk supply which many of these plants have and to the extent that they may in the future decide to pool milk that would not be part of their normal supply, would you consider that to be milk that should be a legitimate part of the Order 33 pool?

A My personal opinion, Mr. Tosi, is that the level of milk that we need to serve the Order 33 market including the excess supply that becomes balanced, should be the milk that is in this pool and to the extent that there are -- that these regulations that we are talking about, are not tightened, the economics available to someone to pool distant milk may become more and more of an attraction for the paper pooling.

I mean, business is business and as I heard when I got into this business many years ago, money moves milk, so consequently, I would be concerned that we could have more of that type of activity in the future because of the economics of it. You can make a buck legitimately and legally. You try to do that. That is what American business is all about.

Q Regards your Exhibit 19, I think it is, where you are calculating your estimates on what interest costs would be because of changes in either the -- having the change in the partial payment and the change in the final payment --

JUDGE CLIFTON: Mr. Tosi, Mr. Herbein's statement is Exhibit 21.

MR. TOSI: Excuse me, Your Honor. Thank you.

BY MR. TOSI:

Q Regarding the interest costs, to the extent that orders provide for at a minimum two monthly payments, a partial and a final, and to the extent that order reform consolidated a number of orders to form the Mideast Order that had its own unique payment base and a decision had to be made for one partial payment date and one final date, would you be of the opinion to say that after making one adjustment in being paid twice a month, that to characterize that continuing on for a whole calendar and say these are the total costs that are borne by your handlers or your clients, as a practical matter, would you think that might be an exaggeration of what the real cost is of making this change?

A I would like to focus on the concept in answering that question -- I don't think it is an exaggeration, because once we -- forgetting changes in the price of milk, which of course, assuming a level price of milk, which is an awful assumption, but if we had the level price of milk and we as processors have to pay either more or earlier, that -- we never get that back. So, that advance of funds from processor to producer stays with an entity permanently. You have made that advance and it's like borrowing money -- and in this case, it's essentially lending money to the other side of the business transaction and unless it has a termination point, it is a forever kind of cost.

Q Would that perhaps be more characterized then as that cost, rather than it being an actual cost of our your client's pockets, that it would be perhaps more properly referred to as the opportunity cost of money?

A Yes, or time vale.

Q Time value.

A Yes, there are a lot of different handles one can put on that. It's my belief and the result of our economic analysis that if a handler, regulated handler has to be pay his advance payment to his producers at a higher amount, even if it is at the same time, there is a cost to that higher amount being paid at the advance date rather than at the final date. That time period costs us -- that opportunity cost to those clients.

Q Let's just assume the market is a 50 percent Class I market and would you agree that it would be reasonable then to assume that the milk that is represented in the first partial payment or the partial payment of the first 15 days delivery of the month, that half of that milk would likely be used in Class I uses and that your clients then are deriving the benefit of Class I sales and holding on to that money for a period of time before they are required under Federal Order to several dairy farmers?

A Yes, that is an accurate statement and our client's position is that the rules, as they exist today, have been assimilated in this market and we are agreeable with those changes that have taken place and we believe that the additional change just simply moves some economics from processor to producer and we thought that you should be aware of that and we have attempted to quantify that for you.

Q I appreciate that. Let's go the other way now. If for example, there were a proposal before us that would say -- let's just go to one paying at the end of the month and we do everything in one shot and handlers now are required to pay producers only once a month and it would be at whatever the blend price works out to be that month. Would the handlers take the position that they are receiving a windfall?

A The handlers, if they asked me to analyze that would quickly see that that would be, to use your term, a windfall and I suspect if that were a proposal before this hearing, we would have a few more farmers here. But it cuts both ways.

Q But you would have viewed it then as maybe not a windfall, but an enormous cost savings, for example.

A That sort of change would be an economic benefit to a regulated handler. There is no question about that.

Q Also, when you were in your Exhibit 21, where you were looking at your estimates there on the impact of DFA's proposal for increasing the partial payment rate, you indicated in your testimony, if I recall -- and please correct me if I am wrong -- that oftentimes your clients may need to have a line of credit and make sure that they are able to make these payments?

A Yes, that was my testimony.

Q And to the extent that you came up with an annual interest cost of about $402,000 --

A That is my calculation.

Q -- I'm trying to ask the question in a certain way here. One moment. Wouldn't this suppose that all of your clients are in fact all in a position where they have to borrow money and they are not relying on for example the money that they received from the sale of Class I milk to their -- whoever their paying clients are?

A No, and because the -- I mentioned the line of credit concern because when we look -- and I believe when you look at the handlers that you are regulating, you need to anticipate changes in the rules that have an effect on those that you are regulating and so I mentioned line of credit, because to the extent that a company that is -- as we say, maxed out on their line of credit or close to it, if we go to them and say you have to pay a little faster or a little higher amount, some may not be able to do that and they could have serious financial effects because of that.

Those that are not dipping into their line of credit to make their producer payments -- and that is a small minority, but those that aren't, there is still a value of that money and I estimated that value of the money, the monetary cost, the economic cost at seven percent.

Q One of the -- are you aware that -- of the law that allows us to have marketing orders requires that the marketing order also be in the public interest?

A Yes, I remember reading that and hearing that in the consolidation proceedings.

Q And to the extent that public interest becomes a concern, and I respect that you are representing the views of your clients, but to the extent that this $400,000 amounts to a very small fraction of a penny per hundredweight impact on your client versus the delay in payments, in what the total value of that actual use value of milk to dairy farmers and the cost that they are absorbing, which do you think from a public interest point of view do you think is more important -- the cost being borne by the handler or the cost of the time value of money that dairy farmers are incurring?

A I believe from the a public interest standpoint, there are two sides to this piece of paper.

On the processor side of things, I believe that -- again, the effort here on -- my analysis of this DFA proposal is that this is an effort to make things better for the producers in this order. And our client's position and my personal position is that this is the wrong way to do it. We really need to tighten up the pooling provisions. I have said that before -- not to be repetitive.

It is a small amount per hundred, but when you focus on the eight million dollars that is moving from one side of the milk equation to the other, from the processors to the handler, that eight million dollars is really the financial strain that is being placed on the regulated handlers, on the processors and I believe that that is something that from a public interest standpoint has to be considered.

If we have 47 plants -- someone mentioned earlier -- and of those 47, one or two are maxed out on their line of credit and can't make ends meet because of this movement -- and that is a possibility, that would not be in the public interest in the community where that plant is located.

So, that is the concern that I bring to your attention, for your consideration.

Q So, I think what you are saying is that you are presenting this information and in the context of a public interest argument, you are saying look, we argument a factor, it impacts my clients and that is what I am here to help show.

A Yes, that is what I am attempting to do and I appreciate your question.

MR. TOSI: Thank you very much. That's all I have.

JUDGE CLIFTON: Thank you, Mr. Tosi. Any questions before I turn again to Mr. Warshaw? Mr. Beshore.

CROSS-EXAMINATION

BY MR. BESHORE:

Q In preparation for your testimony, Carl, did you personally review the pool reports, market administrator reports made by the dairies that you are representing here today?

A We reviewed the summaries of the reports produced by the market administrator and we also reviewed selected Federal Order reports to -- frankly from my standpoint, to familiarize myself with the workings of this order. We didn't review every report submitted by every one of our clients.

Q My question is -- and I want to be very clear about it -- did you review monthly reports, receipts in utilization and producer payrolls filed with the Order

32 market administrator on behalf of each of the dairies that you testified on behalf of?

A No.

Q So, to the extent then that you responded to Mr. Tosi's question with respect to whether any of your clients were engaged in paper pooling, your answer is not based on any personal review of the milk that they reported on their distributing plant reports or the producer payrolls showing the location of the producers this milk was reported as diverted from? Correct?

A My answer was based upon inquiries made at general meetings that we had with the companies when we were all together.

Q Nobody publicly in the presence of their compatriots confessed to any of those activities, I take it.

A I heard none. I do want to say that when we had those discussions, the group unanimously supported the concept of the milk serving the market. That was a very important factor and I take that and present that here as meaning, even if we had someone who had economically been attracted to paper pooling, they knew that this was not good for the market and they didn't want to continue.

Q I understand that and I appreciate that.

In terms of economic attraction, you are aware, I take it, that there has been the possibility and actuality of distributing plants who have the ability to pool milk by diversion by reporting it on their plants, being paid substantial amounts of money by persons who would benefit from such poolings?

A I am aware of that economic attraction.

Q Now, I think you may have mis-spoken in response to one of Mr. Tosi's questions with respect to changes in the rate of partial payment. I want to make sure that the record is clear on this.

If I understood you right, you referred to the producers as -- I mean, the handlers -- if proposal four was adopted and the rate of partial payment was increased slightly as proposal four indicates, you I think referred to the handlers as thereby lending money to producers. Did you not mis-speak in that respect?

A I used the terms lending not meaning that there would be a repayment, but it was -- thank you for an opportunity to perhaps clarify the record -- certainly not a loan. What I was attempting to explain was that a larger advance payment means that money moved from a processor to the producer earlier than the final payment and that eight million dollars is -- and I characterized it as a loan so that everyone could focus on the fact that there is a cost to that. It's really an economic transfer that has a value to it and I used loan and interest to attempt to explain that.

Q In actuality, the substance of the transaction is the other way, is it not? That is that dairy farmers in Order 33 are providing on credit their milk to the handlers, their work, the product of their labors to handlers on credit. Handlers have it, process it, package it, sell it, collect for it perhaps and subsequently pay for it anywhere from 15, 25, 30 or as long as 45 days -- more than that -- 48 days after they have had the product. The farmers in this transaction are the persons extending the credit and the handlers are the ones who are receiving that credit from dairy farmers; isn't that correct?

A Yes, it is clear that when a handler buys milk from a farmer, he doesn't have to pay under most circumstances cash on the barrel head, so it is a way of financing a handler's business and my findings today are that the processor's customers are taking longer and longer to pay their bills, so they really are getting in a pinch and we don't want to be here fighting with farmers, but I do need to say one other thing and that is that from a general business standpoint, producers do have one very good thing on their side of an unsecured transaction and that is they have USDA telling the processors they have to pay their bills. And that is a good thing for the farmers, because they know they are going to get their advance payment and they are going to get their final payment, so I think it is unsecured, but it does have the US government behind it.

Q By the way, advance payment is really a total misnomer in this whole relationship, is it not?

A We happen to like that.

MR. BESHORE: Thank you.

JUDGE CLIFTON: Is there anyone else who would like to ask Mr. Herbein questions? Mr. Warshaw any follow-up redirect?

MR. WARSHAW: No.

JUDGE CLIFTON: Thank you. You have been an excellent witness.

THE WITNESS: Thank you very much for your attention.

(Witness excused.)

JUDGE CLIFTON: I am advised that we have another dairy farmer present who would like to testify.

Good morning.

THE WITNESS: Good morning.

JUDGE CLIFTON: Be seated and then you can be speaking so the microphone can pick up your voice.

First of all, would you state your names and spell your first and last names for us.

THE WITNESS: I am Charles Lausin from Gauga County.

JUDGE CLIFTON: Would you spell the county?

THE WITNESS: G-A-U-G-A.

JUDGE CLIFTON: And that is here in Ohio?

THE WITNESS: That is correct.

JUDGE CLIFTON: All right. I'll ask Mr. Beshore to assist us in getting started with your testimony and then you may go from there.

THE WITNESS: My name is spelled, C-H-A-R-L-E-S, L-A-U-S-I-N.

JUDGE CLIFTON: I would have gotten that wrong. Thank you. Would you raise your right hand for me.

Whereupon,

CHARLES LAUSIN

called as a witness, after first being duly sworn, testified as follows:

JUDGE CLIFTON: Mr. Beshore?

MR. BESHORE: Thank you.

DIRECT EXAMINATION

BY MR. BESHORE:

Q Mr. Lausin, what part of the State of Ohio are you located in?

A Very northeast corner of the State of Ohio.

Q How long have you been dairying in that county?

A Family, five generations. Myself since 1956.

Q And are you a producer under Federal Order 33 at the present time?

A Yes.

Q And previous to that under Order 36?

A That's correct.

Q Have you heard the comments and testimony today with respect to proposal number four, which would change incrementally the required rate of payment on the check that you receive on or about the 26th of the month?

A Yes.

Q Do you have thoughts with respect to that proposal?

A I sure do. As we all know, we have a very important industry here. The processor's side and the producer's side are very important to each other. As things change -- and I don't even have to mention the rate of change that we are experiencing in our industry and things around us, we are finding that a lot of our support has to come farther and farther distances to serve us.

We pay for that service from the time it leaves the point of that service to the time it gets there, does the service and then returns. We are faced with just as many problems, if not more problems, I think than the processors are.

Many of us are in fairly sound financial positions. Some of us, in generality I am speaking now, are pretty highly leveraged. With the cost of doing business today, anything that comes along to help give us a little more level income throughout the month is very important.

I heard the testimony yesterday and I agree with both people and it was very obvious to me how both those individuals dealt with that situation.

Q When you refer to the greater distance that you have to reach out for services, can you tell us more about that, for your farm?

A Well, as there are fewer and fewer of us involved in production agriculture, whether it be dairy or grain or whatever, we are finding many, many consolidations of dealerships that served our industry. Right now, our main source of service and equipment is down pretty much to the southeast corner of the state.

Likewise for other services that have to do with equipment as far as feeding and feed handling and so forth.

At the same time, those folks are demanding more current -- as producer prices go down, there is no question you have to analyze who is putting the most pressure on you to pay the bills and most of these suppliers have got a pretty -- if you haven't got a good line of credit, you pay pretty dearly today.

Q What do you mean by pretty dearly?

A Most of these dealerships now have at least a one percent carrying charge. A lot of them are one and a half percent.

And again, I will say there are good managers and there are those that aren't as good managers as has been mentioned in previous testimony as far as processors. And there are a lot of things that enter into what compels all of this.

But my point is, a lot of times we are very busy. We are stretched to do as much as we can with as few as we can and sometimes a producer gets a little negligent about getting his line of credit -- of course, this is his own fault, but he will pay that 18 percent rather than spending a day and a half going through a complete financial analysis and so forth, thinking, well, next month will be better.

Q Have you noticed any change in the year 2000 and 2001 in the rate of payment that you receive in the partial payment check?

A Yes, it was quite dramatic. It caused -- I am involved with a family corporation now and my brother says, my gosh, I didn't expect it to go that low. What we do, folks, generally we know when the final payment comes that we have to meet our obligations at that time one way or another and the advance more or less takes care of family needs and so forth.

Q And you support the proposed change in the advance payment rate that is in proposal four?

A Absolutely.

MR. BESHORE: Thank you.

JUDGE CLIFTON: Mr. Beshore, thank you. Mr. Lausin, I would invite you to make any other observations or comments that you have about any of the proposals or the needs of the dairy farmer as you see them.

THE WITNESS: Without question, it's been a deep concern, all the discussion about the new order and how it gives the ability for milk to flow from areas that weren't formerly part of our order. So, I am very much in support of reform.

I would also say that I would hope that

action could be taken on an emergency basis. I am totally in agreement that we in the business that expect to be in business look down the road and, you know, folks, it isn't just what we do tomorrow, because what we do today projects out over two years, sometimes three years. I am talking about the planning of herd replacements and so forth.

So, yes, we are as an industry on the producer's side looking at how we cope with -- shall I say the ups and downs that are more severe than what they used to be. They used to be much more stable.

Again, I want to say that I appreciate some of the testimony this morning about the concerns of handlers and from the producer's side. We are dependent on each other and I was pleased to hear that.

One more thing I would like to say though, that it does create a draw every once in a while when everything that we purchase to support the production side, we pay the freight to get it to us and we buy it retail. We pay part of the freight to get it to the handler.

JUDGE CLIFTON: Mr. Lausin, do you have an opinion as to which of the types of pool tightening proposals would be more apt to promote the stability that you would find favorable?

THE WITNESS: Well, I am in complete support of tightening up the regulations -- I know that this order is dependent on supplemental milk, but in the previous stated it has been stated that we have lost substantial dollars. One of the gentlemen that was here yesterday, a producer, shared with me a month ago that what we didn't realize in that 80 or 90 cents or whatever the case may be, probably if that would continue, would force that operation out of business. Now, that is an operation that has been in business for generations and it's not the average herd. Their herd consists of 250 head. It's a well-managed operation.

So, I say to you folks, that will make a difference. We are experiencing dramatic change on the producer's side. I can remember my little community, there used to be a complete load of milk come out of that community. Today we are the only Class I, grade A producer in that area. Granted we probably produce as much milk there and that community did before, but the pressure that we -- as I look to the next generation, it's not too hard to analyze, well, is there an easier way to make a living. I am so totally thankful that I have got a son that wants to carry on.

Whether any of your sons will want to do that, I don't know. I sincerely hope so.

JUDGE CLIFTON: Thank you, Mr. Lausin. Questions for Mr. Lausin? Mr. Warshaw?

CROSS-EXAMINATION

BY MR. WARSHAW:

Q Mr. Lausin, my name is Allen Warshaw and I represent a number of milk dealers in the Ohio and Pennsylvania area. Just a couple questions. Are you a member of DFA?

A No, I am not. I am a member of Upstate Farms.

Q So you are a member of a co-op?

A That's right.

Q How many head do you have on your farm?

A We have 115 mature milking herd and probably another 125 herd replacements.

MR. WARSHAW: Thank you.

JUDGE CLIFTON: Thank you, Mr. Warshaw. Any other questions for Mr. Lausin? Mr. Lausin, is there anything further you would like to add?

THE WITNESS: No, I think I have stated what I wanted to say. Thank you for the opportunity.

JUDGE CLIFTON: Thank you.

(Witness excused.)

JUDGE CLIFTON: Mr. English?

MR. ENGLISH: I believe the next witness

is Mr. Yates.

JUDGE CLIFTON: Very fine. Please be seated, Mr. Yates. If you would speak into the microphone your full name and spell it, please.

THE WITNESS: Ernest Yates, E-R-N-E-S-T, Y-A-T-E-S.

JUDGE CLIFTON: Would you tell us how you are employed?

THE WITNESS: Suiza Foods.

JUDGE CLIFTON: Spell that for the record.

THE WITNESS: S-U-I-Z-A.

JUDGE CLIFTON: Would you raise your right hand, please.

Whereupon,

ERNEST YATES

called as a witness, after first being duly sworn, testified as follows:

JUDGE CLIFTON: Mr. English?

MR. ENGLISH: This is not an exhibit, but the statement is obviously distracting, so why don't we wait a moment.

JUDGE CLIFTON: Let's go off the record.

(Off the record.)

JUDGE CLIFTON: Back are back on the record. Do you have a copy of this?

MR. ENGLISH: I would not make an exhibit of this. The statement in fact has changed slightly during the hearing. There are a few deviations that Mr. Yates will make as a result of the hearing. So, while the statement is provided as assistance, obviously Mr. Yates' testimony is the testimony for the record.

JUDGE CLIFTON: Thank you, Mr. English. Anything else preliminary for Mr. Yates?

MR. ENGLISH: Yes.

DIRECT EXAMINATION

BY MR. ENGLISH:

Q Mr. Yates, by whom are you employed?

A Suiza Foods.

Q And how long have you been employed by Suiza?

A Four years.

Q And before Suiza, by whom were you employed?

A Fleming Dairy.

Q What kind of work did you do for Fleming Dairy?

A Dairy procurement.

Q How long did you work for Fleming Dairy?

A Since '88.

Q Did you have previous experience in the dairy industry before 1988?

A Yes, before then, I worked for a regional cooperative and before then, I was raised on a dairy farm and have some knowledge of that.

Q Have you testified previously at federal order hearings?

A Yes.

Q A number of federal order hearings?

A A few.

Q Is it your position at Suiza Foods to understand federal orders as they apply to Suiza Foods?

A Yes.

Q What that also your job in your employment?

A Yes.

Q Why don't you go ahead and give your statement.

A My name is Ernest Yates and I am the director of dairy procurement for Suiza Foods. Suiza operates 10 predominantly Class I pool distributing plants on order 33: Broughton Foods, Marietta, Ohio, Burger Dairy, New Paris, Indiana, Country Fresh, Grand Rapids, Michigan and Embest in Michigan and Toledo, Ohio, Oberlin Farms Dairy in Cleveland, Ohio, London's Farm, Port Huron, Michigan, McDonalds Dairy, Flint, Michigan, Schenkel's

Dairy, Huntington, Indiana and Trauth Dairy, Newport, Kentucky.

We purchase and receive our milk from a number of sources at these facilities including independent dairy farmers and cooperatives, including, but not limited to Dairy Farmers of America and Michigan Milk Producers Association.

Our ability to obtain raw milk for Class I bottling and our resulting raw milk procurement costs are tied directly to pooling provisions of the federal milk orders. With some modifications, we therefore support proposals one through three and proposal five that are submitted by Continental Farms Cooperative, Inc. DFA, MMPA and Prairie Farms Cooperative.

As to proposal two, we are concerned that the proposed rewriting of 1033.7 (c)(4) may have unintentionally removed the requirement that a 1033.7(d), (e) or (f) pool plant which has chosen not to be a pool plant for a given month, must presently requalify for (d), (e), or (f) status by qualifying as a 1033(c) plant for six consecutive months.

We thus urge consideration of retaining the concept and, if possible, the language of the last sentence of 1033 (c)(4).

As to proposal three, we would modify the two days production provision in 1033.13 (b)(2) to read three days production and modify (b)(3) to require at least one's day production be delivered each month not list in (d)(2).

We necessarily oppose proposal six to the extent it runs counter to proposal three. We take no position on proposals four and eight. We favor the sentiment expressed in proposal seven, paragraph (b)(2) for a touch base requirements, but are concerned that the proposed paragraph (d)(3) lacks such a requirement for other months.

Without meaningful touch base requirements, individual producers suppliers do not actually have to perform. We favor such individual performance. By supporting proposal three, we have already addressed proposal nine.

As to pooling provisions, Federal Order reform of all federal milk orders through informal rather than formal rule-making at the individual market order level, appears to have been based largely on the theory that the most liberal pooling provisions that existed prior to federal order reform in any individual order would be adopted in the new larger order and quoting from the proposal rule 64 Fed. Reg. 16026 et seq. at 16158, c. 3 April 2, 199, to assure continued pool qualifications for all handlers who are currently associated with the Mideast markets, the pool supply plant definition of the consolidated Mideast order provides for all types of supply plants that currently qualify for pooling under the four principal orders.

Twenty-one months of operating under Federal Order reform has revealed that at least as to be Mideast order, this policy has resulted in significant erosion of producer returns to those producers actually serving the fluid market on a regular basis. Class one processors pay the same regulated minimum prices regardless. The difference is that less of that regulated minimum prices returned to the producers shipping to the Class I market as more of the money is spread more widely to producers not regularly serving the Class I market.

When this happens, producers serving the Class I market necessarily look to the Class I processors to make up the difference outside the federal order minimums and the Class I processors naturally seek to minimize these potential increase costs.

Nonetheless, by the very nature of the process, the assurance that federal milk orders give processors of uniform prices is thus compromise.

As to the proposals, we support the concept of eliminating the free ride months under paragraph 1033 (c). As a practical matter, once performance becomes a monthly requirement, both processors and producers will be better able to plan deliveries based upon the need for milk in the fall months when milk is short.

With respect to diversion limits and other rules affecting the shortfall months, we certainly concur that August should be a month with stricter limits. With the summer stress negatively impacting supply and the opening of schools increasing demand for fluid milk, it is wholly rational to include August among the fall months when milk is short.

With respect to the split plant definition, we support proposal five. We note that the provision in presently in Order 33 is a modification of a proposal that existed only in an old Order 49 prior to Federal Order reform. However, while there is the discussion above about maintaining pool status under all of the old orders, there is no discussion in that section of Federal Order reform regarding the need for the provision or the genesis of the read written language. See proposed rule 64 Fed. Reg. at 16026 to 16158.

Moreover, to our knowledge, there were no pool supply plants relying on the old Order 49 language at the time of Federal Order reform.

We understand that a plant in northern Indiana, not the Goshen facility, once relied upon this provision. And the provision was implemented in several orders in the past at the request of corporate those receding manufacturing grade milk to avoid accounting for receipts, especially butterfat, on the manufacturing side of the facility, primarily to avoid butterfat overages.

The manufacturing grade milk that was once received at the northern Indiana location is instead received today at Deutsch Kase Haus in Indiana. To our knowledge, the only other manufacturing grade milk from this area is received at Graham Cheese, also in Indiana.

Neither operation operates a grade A side to their plants. Therefore, the historical need for a split plant provision, a provision which does not exist in all market orders anyway, no longer exists. Indeed the provision was rewritten during Federal Order reform and the pre-2000 provision reads as follows; that portion of a plant that is physically separated from the grade A portion of such plants, is operated separately and is not approved by any health authority for the receding, processing or packaging of any fluid milk product for grade A disposition.

Now, 7 CFR 1049.7 (d)(5), which is revised January 1, 1999, if the department's goal was to permit pool plants that were pool plants in 1999 to continue as pool plants under Federal Order reform, 7 CFR Section 1033.7 (h)(7), is unnecessary and should be a eliminated as requested in proposal five.

For the foregoing reasons, Suiza supports proposals one that through three and side as modified by this testimony. Thank you for your time and consideration.

Q Mr. Yates, just a couple of additional follow-up questions. Yesterday there was some discussion that I had with Mr. Hollon and Mr. Rasch concerning the need for conformity of provisions, especially as it related to the month of August and with respect to the net shipments provision. Do you remember that discussion?

A Yes, I do.

Q Do you agree that if a net shipment provision is to be place in paragraph (c) that one also necessarily needs to exist in paragraph (d)?

A Yes.

MR. ENGLISH: Thank you. The witness is available for cross-examination.

JUDGE CLIFTON: Questions for Mr. Yates? You stunned them. Thank you.

(Witness excused.)

JUDGE CLIFTON: Now, I know that Mr.

Carlson has indicated he will testimony. We can have testimony on any of the proposals for or against. Who else will be testifying? Mr. Hollon again, of course. Are those the only remaining?

MR. ENGLISH: Your Honor, there was a woman from Leprino, Sue Taylor who I thought -- I don't know where she is right now, but I understand -- she is out copying her statement.

JUDGE CLIFTON: Then it's clear to me as should break for lunch. Would this be a good time to do that? Good. Let's come back at 1:00, please.

(Whereupon at 11:40 a.m. the hearing was recessed for lunch to reconvene at 1:00 p.m.)

JUDGE CLIFTON: We are back on the record at 1:04 p.m.

Who would like to testify next? We have Mr. Carlson, Mr. Hollon -- Ms. Taylor, would you like to go next? I don't know the order of the presentation -- I don't know who is the logical person to go next. Ms. Taylor, how many proposals will you be speaking to?

MS. TAYLOR: Just one.

JUDGE CLIFTON: Then I think perhaps if you will go next, that would be best. Ms. Taylor, if you have documents to distribute, we will go off record, while you do that.

(Off the record.)

JUDGE CLIFTON: We are back on record. Mr. Warshaw.

MR. WARSHAW: I think maybe we do have this a little messed up in terms of order. As I understand it, the testimony here is going to be in opposition to proposal four and we haven't heard the proponent for proposal four yet, so I would suggest that it makes a little more sense to call Mr. Hollon first to give his testimony in support of proposal four first. We did it because Carl is coming up on some other things, but if all she testifies to is proposal four, we probably ought to hear the testimony in support of it.

JUDGE CLIFTON: Mr. Beshore?

MR. BESHORE: That's fine. Mr. Hollon is prepared to go ahead with his testimony in support of proposal four. There are a couple of other topics that he was going to address. We can either take them at the same time or hear from the opponents of four, whatever.

JUDGE CLIFTON: Let's have Mr. Hollon just speak to four and then we will have Ms. Taylor just speak to four. I think maybe that is better. Then you can respond to what you hear.

Mr. Hollon, we will have you take the witness stand, please. We will go off record for just a moment.

(Off the record.)

JUDGE CLIFTON: Mr. Beshore?

Whereupon,

ELVIN HOLLON

recalled as a witness, having been previously duly sworn, testified further as follows:

MR. BESHORE: Mr. Hollon has resumed the stand and I assume he continues to be under oath. He is prepared to present his statement and supporting exhibits with respect to proposal number four at this time. And I would ask that the exhibit packet be marked with the next consecutive number.

JUDGE CLIFTON: It would be Exhibit 22. Shall we place 22 on his statement?

MR. BESHORE: I do not think there is any need to have the statement marked as an exhibit. He is going to present and it is available for everyone as reference. There is nothing in it that really requires it to be an exhibit.

So, if we would mark the exhibits as 22, I will be referring to them in the course of the testimony. It is available and without any further questions, Mr. Hollon is ready to proceed.

JUDGE CLIFTON: I will have the exhibits

for proposal four marked as Exhibit 22.

(Exhibit 22 is marked for identification.)

JUDGE CLIFTON: Is there any objection to Exhibit 22 being admitted into evidence? There being none, Exhibit 22 is hereby admitted into evidence.

(Exhibit 22 is received into evidence.)

JUDGE CLIFTON: Mr. Hollon, you do remain sworn, so you may proceed.

THE WITNESS: Proposal four reflects the need to alter the advance payment provisions of Order 33. The dairy farmer members of our group continue to request that they be paid an advance payment that more closely resembles the actual blend price. Their individual farm business needs a more consistent cash flow in order to remain viable.

The current provisions that call for advance billings at the prior month's the lowest class price do not provide sufficient funds to meet our member's cash flow objectives. The final rule makes the following statements about the uniform price and the advance price.

Payments to producers and corporative associations. The AMAA provides that the handlers must pay to all producers and producer associations the uniform price. The existing orders generally allow proper deductions authorized by the producer in writing. Proper deductions are those that are unrelated to the minimum value of milk in the transaction between the producer and the handler. Producer associations are allowed by statute to reblend their payments to their producer members. The Capper Volstead Act and the AMAA make it clear that the cooperative associations have a unique role in this regard.

The payment provisions to producers and cooperatives for the consolidated orders vary with respect to payment frequency, timing, and the amount. These differences generally are consistent with current order provisions and with industry practices and customs in each of the new marketing areas.

Each of the new orders will require handlers to make at least one partial payment to producers in advance of the announcement of the applicable uniform prices. The Florida order will require two partial payments, mirroring the payment schedule now provided in the three separate Florida orders.

The amount of partial payment varies among the new orders, reflecting the anticipated uniform price. Thus, for example, in the Upper Midwest order, the partial payment rate for milk received during the first 15 days of the month will be not less than the lowest announced class price for the preceding month. By comparison, the partial payment for the Florida order for milk received during the first 15 days as a month will be at a rate that is not less than 85 percent of the preceding month's uniform price, adjusted for plant location.

There is a wide variety of payment dates and payment levels among the various orders. The table identified as Exhibit 22, table nine presents the differing provisions. There is no precedent for a uniform payment level or terms across all orders.

Among the order system, there are three broad groupings. In the southern orders, payments are set at a percentage of the prior month's blend price adjusted for location. The northeast and central area of the country sets the advance payment level at the prior month's lowest class price. The western orders use an add-on percentage applied to the prior month's lowest class price.

The final rule supports the principle that all handlers pay a uniform price. We can see no reason why the advance payment should not come closer to approximating the uniform price. Examination of recent data shows that the advance price is getting further from the uniform price. See, Exhibit 22, tables one through eight and chart.

By examining the data, it is clear that there's been a change in trend in the advance price versus the blend relationship. The price measure is this month's blend price less last month's Class III price. For the period January 1997 to September 2001, which is 57 months, the monthly average spread between the two prices was $1.90. However, the first 36 months averaged $1.62 in 1997 through 1999 and the last 21 months averaged $2.38.

Graphically, this trend is shown in the charge of price trends which is Exhibit 22, where even after a three-month average was used to smooth out some of the fluctuations, a difference in trend can be noted.

In order to determine a better relationship between the prior month's lowest class price and this month's blend price, the lowest class price was inflated by five, six, seven, eight, nine and 10 percent. These ranges were chosen after testing several alternative ranges. This spread was measured and compared in the same manner as the existing blend versus class price data.

After examination, it appears that a 10 percent inflation of the prior month's lowest class price is a reasonable adjustment to approximating the spread that existed over the first 36 months.

It is a problem if the advance price is

larger than the final because some producers may not have enough funds to cover their deductions. Also, in some extraordinary cases, the advance may overpay the total amount due and result in the need for some type of collection proceeding, which is difficult and costly. However, as dairy prices are more volatile, this is an issue under the current system even if no adjustment is made.

Producer premiums are present in the Federal Order 33 procurement area and that should buffer the overpayment concerns. This concern needs to be balanced by a dairy farmer's right to a reasonable approximation of the blend price advance payment.

Thus, we would request that the rate for advance payments beset after 110 percent of the prior month's lowest class price.

DIRECT EXAMINATION

BY MR. BESHORE:

Q Mr. Hollon, would you turn to Exhibit 22, which consists of tables one through nine and chart one, which you have prepared in support of proposal four. I just want you to walk through the tables and review the data, which is depicted and how you prepared it.

A For the entire period, there are four different sets of comparisons, tables one and two form a unit, three and four, five and six, seven and eight. They all are comparisons of monthly numbers for the period January '97 through September of 2001.

The measure in the first column is the Class III-A or Class IV price. The measure in the second column is the Class III price. The third column is the lower of the two. And the next one is going to take whichever is the lower and inflate it my multiplying by 1.05 and 1.06, 1.07, 1.08, 1.09 or 1.1. And the final column is the blend price for the appropriate month.

For the period January '97, '98 and '99, there obviously was not a reform Order 33 blend price, because that order did not exist, so in order to create a proxy for that, we took the total pool pounds and the blend prices for each of the four predecessor orders, multiplied it out to get a total dollar value, divided that total dollar value by the total pounds and used that as an approximation for the blend price.

That methodology has been used in the reform process off and on and since reform, to derive some comparisons of pre and post blend prices.

So, that is the base data used to make all the various computations and these are the numbers where it came from.

In tables three and four, it is simply an arithmetic subtraction of the appropriate two numbers to get a difference both in an actual sense and then in a comparison of inflating the lowest price by five through 10 percent. So, those numbers would be a subtraction that is simply designed to reflect the absolute amount.

At the end of the time period, there is some statistics generated that are averages, minimums and maximums and for example, in the all 57-month period, the average difference between the blend and the Class III price was $1.90, the number referred to in our statement. The first 36 months, that average was $1.62 with the minimum and maximum, and the last 21 months, that average was $2.38 with a minimum and a maximum. Each of the alternatives have the same type of computations.

Q In the four sets of tables, one and two, three and four, five and six, seven and eight, in each case, is the first page the data for the chronological period January '97 -- for the months January '97 through December 1999?

A That is correct. The person who programmed the computer there had a glitch, but, yes, that is right.

Q And the second page in each case is the post reform period, the months of January 2000 through October and September of 2001.

A That is correct. Table five and six, take these absolute values and convert them, just another way of measuring, convert them into a percentage, so in each case, the Class III blend price reflects a percentage and then each of the various inflated levels reflects a percentage. So, down on the summary statistics, for example, in the all 57-months period, the Class III divided by the blend price represented 86 percent of value -- prior month's lowest price divided by the blend was 86 percent.

The first period, 36 months, it average 89 percent and the last 21 months, it averaged 82 percent.

Tables seven and eight, I take these percentages and attempt to smooth them just a little by computing a three-month moving average. Again, looking over the summary statistics then for the period, the average was 86 percent. The first 36 months was 89 percent and the last 21 months average 81 percent.

Graphically, these smoothed average percentages are shown in chart one.

Q That is the last page of Exhibit 22?

A Correct. The lines with the circles on them as a marker that goes over the entire period would -- would represent the blend price -- I'm sorry, the Class III divided by blend price.

And if you look at the first three month period, you can see that with one exception, on the high side, and one exception on the low side, the range of this was between 85 or 95 percent. And the right half of the page, you will see that the range began to drop off and after reform, it ranged from 75 to 85 percent. So, there has been some change in the relationship since Federal Order reform, which would make sense since the blend influence on the blend would be the higher of and the influence on the advanced is the lower of.

So, our proposal reflects this and the three lines that are denoted with -- two with no markers and one with the diamond marker, simply notes that inflating the lowest price by eight, nine or 10 percent gets you back into a range that looks the same or very close to the same as before reform.

So, we are not looking for additional revenues or increased revenues, but simply something that approximates the same trend and we hit the 10 percent level, but we expect that our proposal that we made earlier in the hearing, should those be found for, we will have a slightly higher blend price and that would make the spread on the high end, so that influence our selection of the 10 percent levels.

Going back the summary statistics and

begin at table seven and eight, the average over the first 36-month period, the average was 89 percent and under the 10 percent level, the average was also at the 89 percent range, same as the nine percent levels, 89 percent range. Again, we feel like as the result of the hearing, we will end up a somewhat higher blend price.

Q So, if I can summarize the intent of your proposal or if it's summarized in picture form on the graph, the three years before reform, the graph points were primarily between 85 percent and 95 percent band on chart one.

A Correct.

Q And after reform, they are mostly down between 75 and 85 percent.

A Correct.

Q And the proposal would basically move it back up into the pre-existing status quo or 85 to 95 percent.

A That is correct.

Q And that is the intent of proposal four.

A Yes.

Q Table nine of Exhibit 22 is referred to in your statement. Can you just describe that information and how it was assembled briefly?

A We went into the existing order

provisions, order by order, and I just pulled out some information about the advance payment requirements and the purpose of this is to show that there is a variety. They are not all identical and there is some variation, so you wouldn't necessarily expect one side -- the argument that everything should be uniform and the same is not supported by the way it's done now. The principle of what an advance is for would still be the same, but the actual price does vary some market to market.

Q In this post-reform period in the Order 33 marketing area, has DFA had requests from its producers and directions from its council board in this region with respect to the rate of advance payment being made to your Order 33 producers?

A That is correct. There have been several things that have fostered that and one is that -- evidence by the data and also by the spread, that it has widen some, so several -- I think all of the four dairy farmers who testified also acknowledged in that their opinion, the spread had widened between the advanced and the final. So, that was one reason why there has been a request for a rate increase. And second, that there were some periods of extremely low prices that the actual advance payment was very, very low, so there was a request for an increase.

So, when you look at the economics of doing that, your alternatives are to say no, that doesn't work or to say, yes, borrow some money to make that payment. Or you can go to your customers and ask them if they recognize that fact and interestingly enough, several do. In some cases, there is some additional payments, but the majority of the time, the response from the customer is that we recognize your problem, we think that it is a valid issue, but if the buyer down the street doesn't do the same thing, then I am at a disadvantage. That is a reasonable answer. Maybe not the one you like to hear, but a reasonable answer.

So, our approach is to go back in at the hearing process, because that way, we can put everybody on the same time and date and amount level footing and then it seems like that the competitive -- while you might not like to look at the levels, the competitiveness issue is now taking place.

Q And that is one of the objectives of proposal four.

A That is correct.

Q Just so we are clear, in 2000 and 2001, has DFA at the request or direction of it's members in the Order 33 area paid, at least in some months, rates on the advanced payment greater than required under the Order?

A Yes.

Q Are you aware of whether other cooperative associations, proponents of the proposals here, in Order 33, have found themselves in the same circumstances?

A Yes, they have.

Q And have they at the request or direction of their member-owners changed the rate of advanced payment to make it resemble more the level requested in proposal four than the level stipulated under the order regulations?

A Yes, that has been the case.

Q What organizations, to your knowledge, have been involved in that besides DFA?

A The proponents in our group -- Michigan Milk, Continental Dairy Products, Inc., Prairie Farms -- and Foremost and as we developed the language and the rationale, they were all in support of the concept.

MR. BESHORE: Thank you. I have no further questions on direct.

JUDGE CLIFTON: Questions for Mr. Hollon regarding proposal four? Mr. Warshaw?

MR. WARSHAW: Thank you.

CROSS-EXAMINATION

BY MR. WARSHAW:

Q Mr. Hollon, would it be fair to say that unless a business operates on a cash on delivery basis, every business in a sense lends its services and goods until the date on which its bill is paid?

A Yes.

Q And that is no different than what we are talking about with producers.

A That is correct.

Q And most industries have no law which guarantees them payment, let alone payment by a certain, does it?

A I don't know that we have a law that guarantees payments by date. The order system does specify dates on which payments are made and it does not guarantee that there will be funds there to make that payment, but the date specified is correct.

Q But doesn't the law require dealers to make payments into the pool?

A Yes, it does, but personally throughout my career, I have involved in situations where those payments were made by those businesses, so law or not, there have been times when they weren't.

Q But rather than having to sue, the federal government goes to bat for you to make sure that those funds become available.

A There is participation there, but the

ultimate loss, if there is one, falls back -- in my particular case, the cooperative that I was working for.

Q But there is a statute, which is intended to prevent that from happening.

A Yes.

Q And there is the power of the federal government, which is intended to prevent that from happening under that law.

A Yes.

Q And that is not typical of most other industries or businesses, correct?

A Yes.

Q You said that producers are able on some occasions to go to suppliers and ask for some relief in terms of cash flow requirements?

A I said that we as a seller went in some cases to some customers and asked if they would have a different payment schedule and some -- some did, most said for various reasons they could not or would not.

Q Let me ask you this. Is a producer able to do to its suppliers and on occasion negotiate some relief, some delay in payments with things get tight?

A I'm sure -- yes, any individuals -- they would do that.

Q Let me ask you this. Are dealers able to do that with regard to their milk supply? And the answer is no, because the federal law requires that there be payments made on a certain date in a certain amount, correct?

A Correct.

Q So, as to one of their major costs, dealers don't have that flexibility that might be available to producers.

A That is correct.

Q How many producers receive payments out of the pool in Order 33?

A All do.

Q Do you have any idea what the number is?

A In Order 33? Not off the top of my head?

Q Hundreds?

A I think there is a producer count in one of the exhibits in the records.

Q So, we are talking about hundreds of producers sharing in whatever the benefit is.

A Correct.

Q There are dates -- what are the dates on which the payments are to be made to producers?

A I think it's the 26th.

Q That is the final payment --

A The advanced.

Q The advanced. How about the final payment?
A I don't have that on my table. I just did the advanced, but 16, 17, 18, something in that range.
Q But the 26th, as to your members, the 26th is the date on which payment must be made to you?
A I think payments are the day before.
Q How quickly do you get that out to your members?
A Sometimes sooner than we get it, but it's not -- not every member is paid on the exact same pay schedule. It varies from order to order.
Q So, in fact, your producers may not be getting the benefit of the movement of the date?
A That in some cases could happen. In some they could get it faster.
Q And are there occasions in which your members do not get the full benefit of the amount being paid?
A Yes.
MR. WARSHAW: I have no further questions.
JUDGE CLIFTON: Thank you, Mr. Warshaw. Other questions of Mr. Hollon regarding proposal four? Mr. Yale?
CROSS-EXAMINATION

BY MR. YALE:

Q Ben Yale on behalf of Continental Dairy Products. I want you to look at tables one and two of your exhibit. You have January of '97 through 2001 -- October 2001 and you do this by this increment --

A Right.

Q Is there any relevance to an increment on this for the period of pre-reform?

A Yes, for comparison.

Q Just for a comparison basis.

A Yes.

Q Just going over here on the page -- well, the bottom three, you have the 57, 36 and 21 months.

A Okay.

Q The 21-month represents the post-reform period.

A Correct.

Q One other issue not raised -- it wasn't raised directly in your testimony, but is there not also a benefit by earlier payment of a reduced risk of not being paid?

A Absolutely. It's one of the reasons why I would suspect there are two payments processes. Some orders have three payment processes to do that.

Q And over the years, in what you indicated that there have been time when the payments weren't made --

A That's correct.

Q And the earlier that indication that payment isn't going to be made, the sooner DFA or even individual producers can take steps to reduce their loss; is that correct?

A Absolutely.

MR. YALE: No other questions.

JUDGE CLIFTON: Thank you, Mr. Yale. Any other questions on this issue for Mr. Hollon. Mr. Warshaw?

CROSS-EXAMINATION

BY MR. WARSHAW:

Q Are you familiar with Pennsylvania law that governs the milk industry?

A Vaguely.

Q Are you aware of the fact that in Pennsylvania there is a producer security fund?

A I'm not aware that there is one in Pennsylvania, but I am aware of the concept and how it works.

Q So you don't know that there is one in Pennsylvania that does guarantee payment?

A No.

MR. WARSHAW: No further questions.

JUDGE CLIFTON: Thank you, Mr. Warshaw. Any other questions? Yes, Mr. Tosi.

CROSS-EXAMINATION

BY MR. TOSI:

Q I have a couple of specific questions about how to interpret some of the tables. Could we please go to tables five and six.

A Okay.

Q And relating it to your proposal to have the advance payments be 110 percent of the previous month's lowest class price --

A Yes.

Q If on that first page, if you come down the far righthand column where is say Class III divided by blend and 10 percent, when I see that 103 percent, for example, and immediately before that there is 104 percent, could you please explain to me what that means exactly?

A That would mean in that particular month the advance would have been three percent more than the resulting blend price on a price level basis.

Q In that month, if we adopted your proposal, to the extent that the partial payment was exceeding the blend by three percent, what happens then at the end of the month with a full reconciliation? Is this a situation where in effect dairy farmers sort of go back to the handlers?

A It would depend on the relationship. Yes, you could get in a situation where there could be a net -- if assignments are greater than dollar value allows -- yes, you could get in that situation where there would be an OBEC or -- that's a difficult scenario and that has to be balanced against the overall -- maybe one month in so many versus the financial impact of raising the payment level.

Q And that is under a scenario using these months -- a long time before from reform was implemented.

A Yes.

Q If we could just turn the page then and on the top half of that page -- I guess it would be table six, we are showing since the implementation of reform, the far righthand column, Class III divided by blend at 10 percent. That 91 percent would mean that if we -- if your proposal had in in place at that time, the advance payment would have been 91 percent of that month's Order 33 blend prices.

A Correct.

Q And since order reform, the only time that advance payment would be equal to the blend would have been in August of 2001.

A That's correct. And that is certainly a function of volatility. If we could predict that, we would find better means of employment than what we are doing.

Q One other question in how you are using the term trend.

A Trend?

Q I think if I am understanding your correctly -- and please correct me if I am wrong -- your testimony says that since the adoption of order reform, there has been this trend away from -- that there is this increasing spread between what that final payment should be and what that partial payment works out to be.

A Correct.

Q In terms of the trend, can you attribute what you think is causing this to happen?

A I would guess that one of the factors is going to be that the blend price is by the higher of side of pricing and the advance is driven by the lower of. So, there will be some disparity and difference there and the volatility in prices may have some bearing and it may be the relationship with the formulas and I can't say with any specificity, but would be the three areas that would have some bearing.

Q Would you consider -- I am going to ask you to think of something in a little bit different way. To the extent that blends are enhanced a little bit more than say under the old pricing system, to the extent that we are using the higher of three or four, do you think that that offsets -- call it -- I am using this word in quotes -- the "loss" of going to the lowest month's Class I price?

A I suppose that argument could be made, but it doesn't seem to account for much when you are standing in front of somebody who is doing the cash flow in their businesses and saying I want a more reasonable approximation of the blend price. So, if we made a decision for this to be the blend price using these factors, it seems like the advanced ought to track along with it. That answer just doesn't seem to carry much in the real world.

Q And to the extent that you had mentioned price volatility and a change in class price relationships and all, what would -- how would you propose that the order handle a situation where the partial payment is made at such a rate, that when we have full reconciliation with the pool at the end of the month that you have this situation where dairy farmers in effect would owe back? How would that be handled?

A I'm not sure that that is something the order system could have a handle on. For one, you don't even know it until 20 days later, so I don't think -- the reconciliation of that has to fall further down the chain away from the order system. I don't think the order system could fix it, can be blamed for it or take credit for it. It's kind of out of bounds.

MR. TOSI: Thank you very much.

JUDGE CLIFTON: Mr. Cooper?

CROSS-EXAMINATION

BY MR. COOPER:

Q Looking at table six, which Mr. Tosi just went over with you, maybe I misunderstood, but the last column there shows what the Class III with 10 percent would that been that percent of the blend for those months; is that right?

A Yes.

Q Now, if you look at table two, the last two columns, it doesn't seem to jibe and I am just trying to figure out what the problem is and maybe I am misreading it.

A Okay.

Q For instance, there are two months in 2001 where the Class III plus 10 percent would have been more than the blend -- specifically May to July. I mean, is there supposed to be a coordination between those two tables?

A Which table?

Q Table two, the last two columns versus table six the last column.

A I would say the instance that you pointed out, 15.21 is clearly higher than 15.12 and on the percent column, it shows that, so I would have to go back and look at my formula.

Q And some of those other ones are very close and it doesn't seem like they should be that much percent difference. Maybe I am wrong.

A Your observation for May is correct.

Q The numbers on table two, are those done -- are you sure they are correct or -- versus table six?

A Again, all I can tell you is your observation is right and I will have to go back and take a look at the base number.

Q The other thing is, in table six, you say Class III, could that be the problem?

A It should be lower of.

Q That should have been lower of, so the fact that Class IV was lower a couple of times shouldn't have screwed that up.

A I should have picked the lowest one each month in order to make my comparison.

Q So, I mean even though table six says Class III, it should have been the lower.
A Right.
Q You mentioned the possibility of overpayment on the advance could be taken care of because of over order premiums. Are they historically paid in this order?
A Yes, the producers do get premiums above the blend price in this order.
Q Has that been true since Federal Order reform?
A Yes.
Q Could you give us what sort of a range it's been in since the reform?
A No, I can't give you an absolute number.
Q I'm not looking for an absolute number, but are we talking about 10 cents or a dollar or two dollars?
A I'll be on the stand one more time. Let me get with some local folks and get a number for you.
MR. COOPER: Thank you.
JUDGE CLIFTON: Mr. Warshaw?
CROSS-EXAMINATION
BY MR. WARSHAW:
Q Let me ask you this. When prices go up

from month to month, the effect of this differential would be exaggerated, would it not? In other words, if the price that is paid in advance is based on last month's prices, but this month's prices when it's all reconciled are higher, then that would exacerbate the differential between what is paid as an advance and what is due at final payment, correct?

A I imagine that would be right. The relationship that we are looking for mirror is a relationship that said the trends were such. And now we have a relationship that says the trend were such and it's time to move them back together.

Q Well, looking at table two, that almost uniformly since the Federal Order reform January 1, 2000, the prices have been going up. The blend price has gone up.

A Yes.

Q So that that is part of the reason why there would be the kind of differential between the advance and the final payment that you are complaining about.

A There would be some relationship.

Q And in a period where the blend price is falling, that differential would be affected the other way, correct?

A That's correct.

Q And if you were doing your analysis during that period, then your percentages -- that kind of a period, then your percentages in Exhibit 7 would be different.

A That's right.

Q And it would be higher.

A If the prices were falling, it would be closer together.

Q They would be closer to the final or above the final.

A Yes.

Q But you are proposing a rule that is in effect no matter what the pattern of prices, correct?

A That's correct.

Q And you are basing it on historical data that appears in January 2000 to date, a period during which prices were rising for the most part.

A And comparing those against a longer term period and saying that the trend lines -- the numbers that are used --

Q Well, let's look at your trend lines for the earlier period.

A Okay.

Q During the earlier period -- and this

would be exhibit -- table five.

A Every table has the same period.

Q I thought table five was the '97 through '99 period.

A Okay -- yes.

Q And during that period, don't we have as many -- without counting it exactly, wouldn't you say that there are significant numbers of months during which the difference was a positive difference? In other words, the payment at 10 percent would have been more than was actually due?

A Yes.

Q Would that suggest that perhaps 110 percent may not be the appropriate number during a time when prices are falling?

A During that period though, the way the blend prices were calculated and the advanced, they weren't based off of higher of and -- while the advanced was based on lower of, the blend price didn't have that influence, so that would color that judgment some.

Q But it's still the arithmetic truth of the proposition that as prices fall, the final has to come closer to the advanced.

A Yes.

Q Or exceed the advance. Would that be

true?

A Yes.

MR. WARSHAW: Thank you.

JUDGE CLIFTON: Mr. Beshore?

REDIRECT EXAMINATION

BY MR. BESHORE:

Q Mr. Hollon, Mr. Warshaw asked you -- first line of questions, about whether dairy farmers could go their creditors and ask for some forbearance because their partial payment milk check wasn't what they needed for their bills. I want to make sure we don't have any misunderstandings here. I think you indicated they could go and ask.

A Right.

Q Is there any assurance that they will be any forbearance?

A None.

Q What is the cost of forbearance?

A An additional bill of some kind usually.

Q Now, with respect to the possibility that the rate of partial payment is greater than the rate called for in the blend price at the end of the month, first of all, at the time that the end of the month's payment comes around is what -- the 17th of the next month?

A Yes.
Q So at that point in time, the check is -- for the prior month's payment and the dairy farmer has already delivered 17 months of milk --
A Seventeen days.
Q Seventeen day of additional milk for the next months, correct?
A Correct.
Q So that in the unlikely circumstance that there would actually have been a shortfall of funds -- that the farmer when you take assignments into account, as you related, that the handler would be short of money on that final payment. He has already got 17 days of milk into next month.
A That is true, but I am not sure that the market administrator would let that adjustment be made, so while, yes, factually that is true, I am not sure if you could use one month through the system you have. I think you have to go to a private transaction if you were going to try the collection process.
Q Okay.
A Or adjust your premium -- if you had premium room, that is something that you could do.
Q Okay.
A If you typically pay -- if your practice

was to pay a dollar over the blend price and for some reason, you discovered you were in the overpay situation, maybe you would only pay 75 cents over the blend price.

Q To even it out.

A To even it out.

Q But the circumstances in which that unlikely scenario could occur are with respect to producers who have large proportions of their paycheck pre-assigned to creditors for the payment of mortgages or line of credit or accounts.

A Yes, it's correct. That happens from time to time now.

Q I want to make sure there is no misunderstanding about DFA's payment policies in Order 33. Is it your testimony -- has DFA even paid in Order 33 to its dairy farmers, a rate on the partial payment less than that stipulated in the order, to your knowledge?

A The day to day practice, I don't know.

Q You are not sure.

A I'm not sure.

Q You know that they paid more, they were directed to pay more or requested to pay more by the dairy farmers.

A Correct. That question I took to mean as does the co-op ever reblend its price from time to time.

That happens, so the direct answer to that is that could happen.

Q You are not testifying that it has happened in Order 33?

A No.

Q Can you before you testify next time, can you check that out with your locals contacts, check it for other information so that we don't have any gaps in the record.

MR. BESHORE: That's all I have.

JUDGE CLIFTON: If there are no other questions for Mr. Hollon, regarding proposal four, I will allow him to step down. Are there any? There are none. Thank you, Mr. Hollon, we will see you again in a little bit.

(Witness excused.)

JUDGE CLIFTON: Mr. Warshaw?

MR. WARSHAW: May I recall Mr. Herbein for -- I really do think it's only going to be one question. It's his response to proposal four so I think it's appropriate and he has to leave.

MR. BESHORE: That's fine. I do want to recall Mr. Rasch for a very short testimony in support of proposal four.

JUDGE CLIFTON: All right. Mr. Herbein.

Whereupon,

CARL HERBEIN

recalled as a witness, having been previously duly sworn, testified further follows:

DIRECT EXAMINATION

BY MR. WARSHAW:

Q What percentage of a cost of a container of processed milk, the product that is sold to consumers and to retailers, what percentage of the cost of any given container of regular milk -- not a flavored -- let's take whole milk. What percentage of a container of whole, the cost of that container is the cost of the raw milk?

A It's approximately 60 percent.

Q Does that change significant for different products -- for different white milk products?

A Not substantially. There is a range of plus or minus three percent depending upon the products and the value of fat.

Q Under the Federal Order system are dealers able to negotiate in any way the timing of the payments for that raw milk?

A No.

MR. WARSHAW: I have not further questions. I apologize

JUDGE CLIFTON: That's fine, Mr. Warshaw.

Thank you. Any follow-up questions for Mr. Herbein in regards to that series of questions? There are none. Thank you, Mr. Herbein.

(Witness excused.)

JUDGE CLIFTON: Mr. Rasch?

Whereupon,

CARL RASCH

recalled as a witness, after previously having been duly sworn, testified further as follows:

JUDGE CLIFTON: You remain under oath. Mr. Beshore?

MR. BESHORE: Thank you.

DIRECT EXAMINATION

BY MR. BESHORE:

Q Mr. Rasch, what is Michigan Milk Producer's Association with respect to proposal four?

A At a recent board meeting, we took official actions to endorse proposal four.

Q What has been the experience in your cooperative during the years 2000 and 2001, under the current regulations with the rate of payment in the order for partial payments? How have your producers reacted to that and what has your cooperative with respect to that situation.

A For the year 2000 -- I guess you could go back and look at prices and you could probably typify it as saying prices were depressed for almost the entire year. And partly through the year, it became a very serious concern for our members on the advance issue. Because of the support price level for Pollard and the fairly high Class I and Class II utilization, we at least out of the blend price, the extent we go added value for Class I and Class II were somewhat isolated, protected from those low Class III prices, so we had a blend price that typically still averaged $12 or higher, but there were a number of months, the majority of the year, I just quit looking at Class III prices. It was $10 or less.

At some point during the year, our membership had expressed their concerns about the unequal, the uneven cash flow that they were experiencing between advanced and final prices. Our board did take action to put a floor under our advanced price of $11 and we paid -- I can't tell you the exact month that we started -- I am going to say it was prior to June and our position was that we were going to pay an $11 advance price until the lowest class price in the market exceeded that and it appears that that was until we got to the month of March. Class III finally got to $11.42.

So, we were paying $11 in a lot of months where the lowest class price was between -- it was $8.57

one month, wasn't it?

Q Yes, in November of 2000.

A Yes, $8.57 and $10. So, most months when we were paying an $11 advance, we were actually putting more than 10 percent of the lowest class price into that advance and we did not collect any additional money from any of our customers. That was done strictly out of our cash flow.

Q That was done by the cooperative because the producers -- your producer membership needed that cash flow to make their operations work.

A Yes, plus the $11 advance price. We don't have deductions out of the advance, whereas hauling, advertising promotion, dues, producer merchandise would all come out of the final check. None of those deductions are made out of the advance, so the $11 at that point fairly closely resembled what their final price was.

MR. BESHORE: Thank you.

JUDGE CLIFTON: Other questions for Mr. Rasch? There are none. Thank you, Mr. Rasch.

(Witness excused.)

JUDGE CLIFTON: Are there any other issues to address before Ms. Taylor testifies? No, Ms. Taylor, you may come forward.

Ms. Taylor, should your statement be

marked as an exhibit? Do you ask that it be admitted into evidence?

THE WITNESS: Yes, please.

JUDGE CLIFTON: All right, that would be Exhibit 23.

(Exhibit 23 is marked for identification.)

JUDGE CLIFTON: This was previously distributed when we thought Ms. Taylor would be the next witness, so I am going to ask now if there is any objection to the admission into evidence of Exhibit 23?

MR. ENGLISH: Your Honor?

JUDGE CLIFTON: Yes, Mr. English?

MR. ENGLISH: I don't know how you will take this and I don't want to jump the gun on what she is saying. Ms. Taylor warned me a little bit about what comments she made and in case that commentary or her conclusion should be taken as a proposal, notwithstanding the fact that she says she is not making this proposal, I want to know in advance are objections on the content of the hearing notice -- I don't think it means not taking this into evidence at this time, but I also didn't want to waive the opportunity and I will address it later.

JUDGE CLIFTON: Yes, thank you and I appreciate the advance alert on the issue, which you can identify more fully at a later time.

MR. ENGLISH: Thank you.

JUDGE CLIFTON: I appreciate that. I am deviating from normal procedure by taking these exhibits in before there is a foundation for them, but I do think it is useful for the purposes of what we are doing here.

All right, other than the qualification made by Mr. English, there is no other Objection to the admission into evidence of Exhibit 23 and I hereby admit Exhibit 23 into evidence.

(Exhibit 23 is received into the record.)

JUDGE CLIFTON: Ms. Taylor, would you identify yourself fully and then I will swear you in.

THE WITNESS: My name is Sue M. Taylor and I represent Leprino Foods Company.

JUDGE CLIFTON: Nothing unusual about the spelling your name?

THE WITNESS: No.

JUDGE CLIFTON: Taylor is T-A-Y-L-O-R?

THE WITNESS: Yes.

JUDGE CLIFTON: Would you raise your right hand, please.

Whereupon,

SUE TAYLOR

called as a witness, after first being duly sworn, testified as follows:

JUDGE CLIFTON: Thank you. You may proceed.

THE WITNESS: I am Sue Taylor, Vice-President of Dairy Policy and Procurement for Leprino Foods Company in Denver, Colorado. Our business address is 1830 West 38th Avenue, Denver, Colorado 80211.

Leprino operates 11 plants in the United States, manufacturing mozzarella cheese and whey products domestically and marketing our products both domestically and internationally. Our cheese is primarily used as ingredient by major pizza chains, independent pizza restaurants, as well as many of the nation's leading food companies.

Leprino operates two manufacturing facilities that receive milk regulated by the Mideast Order. These facilities are located in Allendale and Remus, Michigan

I am testifying today in opposition to proposal number four, the proposal to increase the partial payment rate from the lowest class prize to 110 percent of the lowest class price from the prior month.

The proponents of proposal four point to producer cash flow challenges that exist due to the disparity between the level of the partial payment and the level of the final payment. They suggest that the partial payment should be structured to more closely resemble the blend price.

We do not contest the concern regarding producer cash flow, however, our analysis shows that the proposal does not achieve the objective of more closely emulating the blend price. The proposed remedy does not address the root cause of the issue, but rather simply transfers the cash flow burden to processors.

The result of the proposal is that manufacturers of products in the lowest class, and in many months in the lowest two classes, will be forced to pay more than the classified value of their milk in the partial payment. This violates the minimum pricing intent of the order.

Additionally, the application of the proponent's logic across several orders results in inequities in the form of different prepayment levels amongst competitors in manufactured product markets. Addressing the concern expressed by the proponents of proposal four in this and manner is both a logical and in equitable.

Of the source of the differences between the prepayment rates and the final payment rate is twofold. First, the partial payment is based on the prior month's rather than the current month's market values. Second, the partial payment does not capture the incremental value contributed to the final payment by utilizations with higher classified values that the lowest class price. This incremental value is captured for the final payment through the pooling process administered by the market administrator.

The first source of difference, the use of prior market values rather than current market values in the setting the minimum advance price is generally not referenced as a concern since the resulting prepayment price sometimes above and sometimes below current market values.

To the extent that a concern exists, the processor obligation for the partial payment could be updated to current month market values. Since not all market values use for the full month are known at the time of partial payment, the partial payment could be calculated based on the factors for that portion of the month for which the data has been published prior to the partial payment deadline. This additional calculation and announcement would require additional administration due to the additional price calculations and the necessary communication to market participants.

The second and more important source of difference between the prepayment and final payment is the absence of contribution of the incremental value from the higher classes of milk and prepayment. Although they have not explicitly characterized it as such, this appears to be of primary concern to the proponents of proposal for.

Proposal four fails to address either of the sources of differences between the prices. The proposal does not result in an increased correlation between the prepayment and the blend price. Analysis of period from January 1997 through September 2001 is shown in Attachment 1. Key observations over this period are that the prepayment price has increased by $1.19 cents reducing the average shortfall of the advance relative to the blend from $1.80 to 61 cents.

However, the monthly differences between prepayments and blend range from an underpayment of $5.01 to over payment of $3.37, a clear indication that the proposal does not emulate the final payment. The standard deviation of the differences between the prepayment and the blend is increased from $1.37 under the current system to $1.46 per hundredweight under proposal four.

The graph in attachment two shows wide fluctuations in individual months differences between the proposed prepayment rates and the blend.

The proposal violates two basic tenets of pricing from milk manufactured into Class III and IV products. These are that the Federal Milk Marketing Orders establish minimum pricing and that since manufactured products are marketed nationally, the minimum regulated price level for Classes III and IV are consistent across all orders.

Proposal four violates the minimum pricing concept by setting regulated milk prices for the prepayment above the equivalent market value for Classes III and IV. For example, during the period from January 1997 through September 2001, the minimum prepayment obligation would have exceeded the Class III price by 80 cents per hundredweight on average.

The proponents of proposal four are advocating a similar provisions in other orders. However, the factor that is being proposed is different for different orders, resulting in disparate economic positions for competing Class III and IV manufacturers located different orders. For example, the proposed factor in the Upper Midwest Order is 103 percent, which would result in an average prepayment price that is 83 cents per hundredweight lower than that proposed for the Mideast order.

The logical conclusion from the above

analysis is that the most appropriate approach to the concern that the prepayment does not closely enough resemble the blend price is to implement a similar minimum payment and pooling structure for the prepayment that currently exists for the final payment.

Although this is a logical remedy, I am not proposing that it be adopted at this time. This remedy would require significant additional administration in terms of plant reporting, reports analysis, pool calculation and movement of funds into and out of the pool than the current system of minimum payment at the lowest Class price.

Additionally, such an approach would significantly impact many handlers who are not participating in the hearing today, since the concept was not properly noticed. A more comprehensive review of all provisions of the orders that would be impacted and the associated impacts were also be necessary prior to the serious consideration of such an approach.

Although we are sympathetic to the issue of concern that is cited by proponents of proposal four, we do not agree that the proposed solution is appropriate or equitable.

Although we have outlined a more appropriate approach to addressing the concern, that approach should not be considered a proposal as part of this rule-making process since it has not been properly noticed. USDA should reject proposal four since it does not appropriately address the issue it purports to remedy and it violates the minimum pricing concepts from manufacturers.

That concludes my statement.

JUDGE CLIFTON: Thank you, Ms. Taylor. Questions for Ms. Taylor.

MR. ENGLISH: If I may now address the point?

JUDGE CLIFTON: You may. Mr. English.

MR. ENGLISH: Your Honor, again, I think Ms. Taylor has more than expressly said that while she has this concept and this idea, she is not proposing that today for a number of reasons that she stated. I rise to the point and say that that is Ms. Taylor's position. That may not necessarily be the position of anybody else in this room and for that purpose, I rise to object to the extent that the department might decide to consider this as an alternative on the grounds that it is such a significant deviation from what was notice, because it would require a different administration, because it would very much have conceivably changed my client's position. My client is neutral on proposal four. We may very well have taken a different position had this been the proposal and we are unable to analyze it at this time, to put evidence in at this time.

I appreciate what Ms. Taylor is saying, but I want for the record to state our objection to considering it as a proposal at this hearing.

JUDGE CLIFTON: Mr. Warshaw?

MR. WARSHAW: I would simply note my joinder in the remarks. I think the testimony is pretty clear and makes clear that this idea is not ripe for consideration, but to the extent that that is not true, we would object to any consideration of the idea.

JUDGE CLIFTON: Thank you. Mr. Beshore?

MR. BESHORE: I understand the proposal is not being advanced and we are not advancing it either. The only concern I have for the objections is that modifications to proposals in the record and the possibility for the Secretary to adopt modifications to the proposals in the record is part of the ground rules for the whole hearing process. It's done all the time appropriately and the Secretary ability to appropriately adopt modifications that may reflect the record should not be constrained in any way by objections made with respect to this testimony.

JUDGE CLIFTON: Mr. English?

MR. ENGLISH: Case law, Your Honor, is abundant on this issue to the extent that what is a modification that is appropriate is certainly going to be an issue. I am rising to say that in our opinion, this is a significant enough modification, the parties would have altered their behavior entirely.

The witness is proposing -- and so far no one else has advanced it, but sometimes things have happened in these Federal Order proceedings that have surprised people, that a modification so significant that the witness who raises it herself has said it's not ripe, is by definition beyond the scope of the hearing and it certain is in our opinion and behalf of Suiza Foods Corporations, I state point blank that our position on proposal four would be different had this been noticed.

JUDGE CLIFTON: Thank you. Mr. Yale?

MR. YALE: I just want to support Mr. Beshore and just say a couple things. First of all, it is within the scope of the notice. The hearing said that we were looking at advanced pricing and it is within the range of the testimony. That is what gives the secretary the ability to exercise her wisdom. If we are going to tie her down to periods and dots and specific language before we go in, we could have just had notice that advanced pricing was noticed.

So, I think that in that regard, we are very much within that. We are not at this point supporting it, but I don't want to get the record set up now that once an issue is before the Secretary, that we can't modify it once we get here.

JUDGE CLIFTON: Thank you. Any other comments, first of all, with regard to whether or not the suggestion is properly a proposal and secondly, any further questions on any issue for Ms. Taylor?

MR. ENGLISH: Could we get this ruling first?

JUDGE CLIFTON: It's not my call. The record is very clear, both sides. I'm not going to rule on that issue, Mr. English.

Mr. Yale?

CROSS-EXAMINATION

BY MR. YALE:

Q Did you do an analysis of the cost if proposal four is adopted to Leprino and its Michigan plants?

A I did.

Q What is that cost?

A I would prefer not to share that proprietary information.

Q Is it fair to say that it relates to the cost of money?

A Yes.

Q As I understand your testimony, you are a regulated plant under the order?

A Yes.

Q So you have handler obligations to the pool.

A That are executed through MMPA.

Q Now, you indicate this idea -- in sum, you just don't want to pay more for milk on the 26th of the month for 15 days worth of milk than what the Class III price. Does that kind of sum up what you are saying?

A That's correct.

Q Even though you have an additional 11 days of milk on hand at that time, right?

A That's correct.

Q And the issue of the advance payment isn't so much to pay for 15 days worth of milk. It is to advance to producers funds, so that they can level out their cash flow through the month rather than just one payment, correct?

A I wouldn't agree with that. I think there is both purposes. It's an estimated payment on the first 15 days worth of milk and it does have the side-effect of providing multiple cash flows.

Q But is it a final settlement for the first 15 days?

A No, it's not.

Q Because it does not reflect -- as your testimony states, the incremental value from the higher Class I and Class II prices, does it?

A That's correct.

Q And in fact, of all the orders, it's somewhat of a approximation of value, right? I mean, nobody has a fixed formula that says it's one-half of the blend price, right?

A All of the Federal Orders that Leprino operates in currently use the lowest class price from the prior months. so it is a defined price reference in the order.

Q Have you considered just de-pooling your plants so you don't have to make this minimum payment and additional advance?

A We generally are not pooling our own milk. It's being pooled by our supplier. They have on occasion, I understand, de-pooled the plant it's to their economic advantage. That economic advantage has not flowed back through to Leprino.

Q Now, on page three, you say that proposal four violates the tenet by setting regulated milk price.

The advance is not a regulated price for Class III, is it?

A It is a price that is regulated in the sense that the order defines the minimum payment amount and it defines the timing of the payment, so it is a regulated price and Class III handlers are subject to it.

Q Subject to adjustment in about 10 days to get that payment back, right, if there is any over-payment, right?

A Right, there is a final settlement that occurs mid-month the following month.

Q So you would agree that by the time the month is over with, you are not paying any higher price for the Class III milk than you would under the current situation.

A There is a cost of money difference, but otherwise, the final Class III price is not impacted by this.

Q And then you talk about the disparities between regions and orders based upon their advance payment. Really the difference is in the cost of money for those higher or lower payments. Isn't that really the difference?

A That's correct. For example, in the Upper Mideast order, as I recall, the pre-payment averaged .83 below the pre-payment in the Mideast order, so the difference in the economic impact of the main factors would be cost of money and the .83 -- approximately .83.

Q I want to look at your tables. I have got some questions on those. First off, I want to go over to the far right column. You have got current and advanced less blend and, correct me if I am wrong, but isn't this the blend less the current advance?

A Let's look at January '97 and I believe that my title is correct. It would be the lower of, which is in the fourth column from the left, $11.50 less the blend price of 12.82 making it a negative 1.32. The parentheses connote a negative number.

Q So you are saying by this negative number, that you are paying less than the blend by the 1.32?

A That's correct.

Q And the same thing with proposal four.

A That's correct.

Q What are you trying to explain by that computation?

A I am trying to illustrate that the argument that proponents put forward in terms of making the pre-payment emulate the blend is not achieve through their proposal. In fact, we have wider disparities between the prepayment and the blend under their proposal than we do in the current system.

Q Let's talk about that under the current. As I look at it, I see the widest spread as $6.04 for February of '99; is that correct?
A That's the widest on the negatives side.
Q And on the positive side, what is it?
A $1.89.
Q And then what is it on proposal four? What is the widest spread? What is the extreme?
A On the negative side, 5.01 and on the positive side, 3.37.
Q And both of those occurred before 2000, didn't they?
A Yes, they did.
Q And you would agree, would you not, that there have been significant differences both in the formulas for Class III and Class IV as well as the advance pricing of Class I from January of 2001 as compared to prior to that time, right?
A That is correct, but part of the historic that we are seeing since January 2000 were the result of a Class IV price that was enhanced due to the butter powder tilt in the support program, so some of those disparities are automatically reduced. In fact, if you do look at the period since USDA adjusted the butter powder tilt in May of this year, you will see that once Class III became the

mover, we would have overpaid the blend I a pre-payment.
Q By how much?
A A minimal amount. The most would be 55 cents in June of 2001.
Q In fact, they would be almost approximating the blend, closer than any of the other formulas, right?
A That's correct.
Q In fact, if you look down here in your means for 2000 and 2001, the range there is relatively close, is it not?
A Yes, it is.
MR. YALE: I have no other questions.
JUDGE CLIFTON: Thank you, Mr. Yale. Those questions were very insightful. Mr. Tosi?

CROSS-EXAMINATION

BY MR. TOSI:

Q Thank you, Sue, for coming today. Just a couple of questions. In your testimony, you talked about -- to adopt the higher rate of partial payment would be a violation of pricing standards. You said minimum pricing concepts to manufacturing and at another point in your testimony, you suggest -- I think, correct me if I am wrong -- that because these products complete in a national market, that somehow it would be inconsistent with Federal Order policy. Were you available before when Mr. Hollon presented in his Exhibit 22 table nine, a comparison of payment provisions in Federal Orders?

A I'm not sure I was in the room at the moment, but I have reviewed the table on his testimony.

Q Would you happen to have that in front of you?

A Yes, I do.

Q To the extent that partial payment rates amongst the various orders are different -- for example, they range from lowest class price for the prior month, 90 percent of the prior month's blend, 1.3 times the lower price. Are you suggesting that Federal Orders are not in compliance with the minimum pricing concepts that you are talking about?

A Yes, I would. I would also point out that Leprino does not operate in any of those orders where the provisions are other than lowest class price and that is one reason why it's not been a point of contention in terms of our input to USDA previously.

Q And to the extent that you do have a plant that is regulated here of Federal Order 33, to the extent that an increase in the rate of partial payment would be applicable to all class -- manufacturing plants such as yourself, to the extent that it would all be identical.

You would still see that as a violation?

A If it were identical -- if all orders had identical provisions, then that would address the competitive position question. It would not address the question of overpaying the minimum price obligation, however.

MR. TOSI: That's all I have.

JUDGE CLIFTON: Ms. Taylor, before I ask Mr. Warshaw, is there anything that you would like to expand upon thus far?

THE WITNESS: Probably lots of things --

JUDGE CLIFTON: Mr. Warshaw?

CROSS-EXAMINATION

BY MR. WARSHAW:

Q Just so the record is clear, you are not purporting to submit a proposal today?

A You are correct.

Q And you would agree with me that there is no information about the impact of the idea you have would have on Class I handlers.

A That is correct. In fact, I would expand that to the point where I suspect there are other provisions within the orders that are impacted by concepts such as the timing of committing a producer to the pool on a particular month. And I have not done any of the research to balance the provisions and it could potentially be a pretty complex issue.

MR. WARSHAW: Thank you.

JUDGE CLIFTON: Mr. Tonak?

CROSS-EXAMINATION

BY MR. TONAK:

Q When I look at your attachment one and compare some of the numbers to those used by Mr. Hollon in his exhibits, I see some differences. Just to clarify, if we look at the last month in your series of numbers -- September, where you have the Class III price for September as 15.90 and that is the correct Class III price for September, right?

A Yes.

Q But that is not -- and the next column being the 15.59 for the Class IV price.

A That's correct.

Q And the lower of those two is the 15.59 as listed there.

A That is correct.

Q But that is not the advanced price used for September milk; is that correct?

A No, if you are interested in looking at the advance price, you would adjust the months by one increment, so the September price for Class III and Class

IV are at the advance prices used for October milk.

Q So, when we look at the comparative effects compared to the advanced prices and the difference in the blend price in the month of September, if we use the actual advance price, we would have a different number. Would that be correct?

A I suspect that you might have a point. Let me clarify on where I pulled my blends. I pulled the blends from the DFA exhibit. I did not go back to the original source, so I am unclear -- I assume that the blends were appropriately assigned to the class prices, but I did not research that. That is something I could follow-up with and comment on and clarify in the post-hearing brief.

Q That is fine with me as long as there is an understanding that in the DFA exhibit, the blend as indicated for September is 16.87 as it is in this attachment for September and reviewing those blend price numbers, were off one month throughout, so the differences between the current advance less blend and the proposed advance less blend are not those reflected in this attachment, nor are those averages correct and I would suspect that because of that, attachment two, the bar graph is not correct. And I have got concerns if this exhibit is allowed to stand if it is.

MR. TONAK: Thank you.

JUDGE CLIFTON: Ms. Taylor, anything further on Mr. Tonak's concern?

THE WITNESS: I do not have the original source data to clarify his concern at this particular moment, so I would have to follow up at a later point.

MR. TONAK: That is another question I have.

CROSS-EXAMINATION

BY MR. TONAK:

Q You will follow up and assure that it's either corrected or confirmed?

A Yes, my plan would be to follow up as part of the post-hearing brief process unless someone else has source data available where I could go back and look --

Q I'm not asking you to do it today, but could you perhaps circulate a corrected version -- if that is appropriate --

A Certainly.

MR. TONAK: Thank you.

JUDGE CLIFTON: Mr. Beshore?

REDIRECT EXAMINATION

BY MR. BESHORE:

Q With respect to the data questions on attachment one, let's assume, Sue, that the blend prices that you -- the blend price information that you obtained from the DFA exhibit is correct and that your information with respect to Class III or Class IV-3A prices is correct, in your exhibit, attachment one, which I think it is, were you -- you are comparing September's lower of price, which we don't know until October 5th and which is not the basis for the advance made on September 26th, with the blend that results from those prices in September, right?

A Yes.

Q So that is --

A If the 15.87 represents the September blend, which presumably it does because we don't know the October blend yet, then you are correct. I have a mis-match for months between my advance portion of the analysis and the blend portion.

Q So, the numbers are correct, but you are comparing them on a current month basis or the basis of -- just as they are presented. Was that because you were trying to determine whether the advance was emulating the blend price, the advance -- well, actually that wouldn't even work either.

A I did not intentionally mis-match the months. I was attempting to see if the advance emulated the blend, but I suspect based on the comments that you just made and the previous questioner, that probably I do have an error of a month.

Q Let's -- we can all sort that out as we analyze the documents with the official records of the announced prices. I want to explore just a minute or two your suggestion that proposal four was attempting to emulate the blend price. You heard Elvin's testimony today, correct?

A Yes.

Q Wouldn't it be more precise to say that the intention of the proposal was to emulate or restore the relationship to a relationship similar -- to restore the post-reform relationship to what it was pre-reform as opposed to emulating the price itself? It's to bring the relationship back to where it was before.

A Yes, that's the overriding objective it would seem.

Q And if you were able to precisely emulate the blend price at a certain level, you could write it that way, but emulating the blend price was not the end objective. It was reaching the 85 to 95 percent band on the graph that you testified to.

A The overall price level, I believe, is the overriding objective, price enhancement at the producer level.

Q Do you have competitors -- does Leprino have competitors in Idaho, cheese manufacturers in Idaho?

A Yes.

Q And in Arizona?

A It depends on how you define our competitors. There are cheese makers in Arizona and we consider all cheese makers our competitors.

Q On Exhibit 22, table nine -- Mr. Tosi may have addressed this, but I am not sure and I want to make sure it's noted -- your competitors in the Western Order, which would include those in the -- the large and growing cheese manufacturing industry in the State of Idaho is presently paying a partial payment at the rate of 1.2 times the lowest price for the prior month.

A That is correct.

Q And that is not as high as would be applicable to Leprino in Order 33 if proposal four was adopted.

A My understanding is that this is higher than would apply in the Mideast Order.

Q Correct. And in Arizona, it's 1.3 times the prior lowest price of the prior month and that is even higher yet.

A Yes.

MR. BESHORE: That's all I have.

JUDGE CLIFTON: Thank you, Mr. Beshore. Other questions for Ms. Taylor? Mr. English?

MR. ENGLISH: Your Honor, if I may -- maybe I was putting the cart before the horse earlier and perhaps at least for my part and my client, I could put this matter to rest. If the government will tell us whether or not they view the statements made as a proposal, it doesn't matter about the objection as to whether or not it's a logical extension if the government will say, as far as they are concerned there is no proposal on the table made by Ms. Taylor?

JUDGE CLIFTON: Mr. Cooper?

MR. COOPER: Ms. Taylor, about three times in her statement said she wasn't making a proposal, so we certainly don't have a proposal. Nobody else has gotten up and made one, so there is no proposal in that regard.

MR. ENGLISH: That is what I needed to hear.

MR. COOPER: That is our position. Since there is not proposal, there is no reason to get into questioning details of the proposal or whether it is apropos or not apropos. If there is no proposal, there is nothing to rule on.

MR. ENGLISH: I accept that, Your Honor. Thank you.

JUDGE CLIFTON: You are welcome, Mr. English. Any other questions for Ms. Taylor? There are none. Thank you, Ms. Taylor. You may step down.

(Witness excused.)

JUDGE CLIFTON: Mr. Carlson, do you want to take a brief break or are you ready to do.

MR. CARLSON: It's up to you.

JUDGE CLIFTON: Let me see by a show of hands. How many of you would like a 15-minute break right now? All right, let's take 15 minutes and come back at 3:00.

(Off the record.)

JUDGE CLIFTON: We are back on the record at 3:01. Mr. Carlson, would you state and spell your full name, please.

THE WITNESS: My name is Rodney, R-O-D-N-E-Y, C-A-R-L-S-O-N.

JUDGE CLIFTON: And would you state your employment, please?

THE WITNESS: I am self-employed as a dairy industry consultant. My home and office address is 5357 Lance Road, Medina, Ohio 44256.

JUDGE CLIFTON: How is Medina spelled?

MR. CARLSON: M-E-D-I-N-A.

JUDGE CLIFTON: Thank you, Mr. Carlson,

Would you raise your righthand, please.

Whereupon,

RODNEY CARLSON

called as a witness, after first being duly sworn, testified as follows:

JUDGE CLIFTON: Mr. Carlson, you may proceed.

THE WITNESS: First of all, a little background. I have a BS and an MS degree in agricultural economics from North Dakota State University in Fargo, North Dakota. I was hired out of school by the dairy diversion. I worked in the MA office in Denver for two years and the AM office in St. Louis, Missouri for eight years.

After that, I worked for five years for Land O'Lakes as an agricultural analyst and I worked for Milk Marketing, Inc. in Strongville, Ohio for 15 years as the director of marketing, director of member service and marketing and then the vice-president of member service and economics.

I worked for DFA after DFA was formed through a merger with Milk Marketing, Inc. and three other cooperatives. I worked for them for nearly two years as manager of fluid marketing member service and then another 20 months as a consultant.

In all of my positions since leaving Federal Order program in 1978, my responsibilities have included Federal Order activities including recommending amendments, developing proposals, preparing to present testimony, writing briefs, recommending methods of operating under regulations. I have continued to work as a dairy industry consultant since leaving the DFA six months ago. That is a little of my background.

I am appearing on behalf of Scioto County Cooperative Milk Producers Association. Members of Scioto milk producers have farms located in southern Ohio and northern Kentucky. Milk from these farms is pooled on the Mideast milk market area and other marketing areas.

It is quite likely that from the time the very first Federal Milk Marketing Order was instituted dairy division personnel, cooperative leaders, industry leaders, scholars and others have debated over which dairy farmers should be entitled to participate in the revenue generated through the establishment of Federal Milk Marketing Orders at classified pricing.

Since the Marketing Agreement Act of 1937 was passed by Congress and subsequently amended, provisions have been written which attempt to identify which producers can participate based on their participation in servicing the fluid or Class I needs within the market.

The less milk produced within a market or region in relation to the amount of milk required for fluid use, the higher the participation requirements of the individual dairy farmers, a milk plants and marketing organizations was established.

One of the primary purposes of the Federal Milk Marketing Order has been to assure customers and adequate supply of fresh fluid milk. Another primary purpose been to promote orderly marketing conditions. The purpose of the Federal Milk Marketing Order program seemingly has been lost during the past several years due to excessive political rhetoric and interference.

It is time to return the program back to work like the economic marketing tool it was intended to be instead of a social program some would like it to be. It is time to go back to basic principles and economics and ignore political rhetoric.

The economics of federal orders and classified pricing is relatively simple. Processors of fluid milk products, and the consumers of those products, pay a higher price for raw milk used to produce those products than what is charged to processors of less perishable and less bulky dairy products.

Producers, plants and marketing

organizations have been expected to meet the needs of fluid milk processors and fluid milk consumers within the marketing if they are going to participate in the additional revenue generated through classified pricing.

In today's economic environment and with the current order provisions, some producers, plants and organizations are taking great efforts to participate in the additional revenues of higher priced -- higher Class I utilization markets but, are avoiding servicing the fluid needs of the market.

Federal Order pooling provisions and the lack a logical location pricing principles within the order program have encouraged the addition of excessive amounts of producer milk to markets when participants who control that milk have no intention of meeting the ongoing Class I needs of the market and consumers of fluid milk products. The milk is committed to other purposes, is allowed to gain economic advantage due to this commitment, avoids the cost of servicing the Class I market and still participates in the revenue that the Class I market provides. The need for changes to provisions that allow such disorderly marketing conditions to occur is obvious.

Scioto County Cooperative Milk Producers supports those proposals that require higher participation standards of producers, plants and organizations benefiting by the revenue generated by the Class 1 markets.

In the year 2001, we have seen the amount of producer milk pooled in this market, Federal Order 33, increase as much as 42 percent from the same month of the previous year. Virtually all of this increase has been from producers in states not included as part of the Mideast marketing area. The amount of producer milk allocated to Class I has remained the same or decreased slightly from 2000 to 2001.

The addition of approximately 500 million pounds of milk per month to the pool, the subsequent reduction in Class I utilization and the resulting lower producer prices are not contributing to orderly market conditions, nor are they assuring fluid milk processors and consumers an adequate supply of milk. Amendments to the order are necessary to promote orderly marketing conditions. Those amendments should be made as quickly as possible. We support efforts to move the decision-making process forward on an emergency basis.

There is another item that needs to be addressed as quickly as possible. The industry and the department should not continue to ignore location economics in the Federal Order system. Milk received at plants located a long distance from the market simply does not have the same economic value as milk delivered to the market. Pricing provisions need to recognize this simple economic reality.

One of the positive aspects of additional milk from areas west of this markets being attached to the pool and reducing the local producer prices, has been the reduction of milk received at plants east of the market riding the pool. Tightening pool provisions will reduce the amount of milk from the West being attached to the markets, but without reasonable location pricing provisions, milk from east of the market may once again start riding the pool.

It is absolutely ludicrous that milk attached to this market received higher producer pricing when delivered to manufacturing plants in Waverly, New York or at a supply at plant in Grantsville, Maryland than it does when delivered to fluid milk processing plants in Indiana, Ohio, West Virginia or Northern Kentucky.

Pricing provisions in the Federal Milk Order system must be addressed to recognize location economics and take back the program from the pricing provisions forced on it by politicians and political lobbyists. Let's get back to the basic purpose of the program and promote the orderly marketing of milk.

As far as specific proposals, members of the Scioto County Cooperative Milk Producers support proposal number one, portions of proposal number two, and proposal number three, proposal number four and proposal number nine.

Proposal number one. Qualification requirements for distributing pool plants should be increased to a minimum of 40 percent from August through April and 35 percent in other months. Scioto Milk Producers would prefer that these percentages be another 10 percentage points higher.

There is no good logical explanation for the reduced qualification requirements of distributing pool plants written into this order during Federal Order reform. Distributing pool plants in this region of the country have typically been just that, distributing pool plants. The current relaxed provisions have encouraged fringe elements of the milk marketing industry, in conjunction with distributing pool plants to take advantage of this market without contributing to the needs of the market.

Contrary to normal expectations, distributing pool plants have been guilty of assisting others in their goals of riding the pool. Adoption of proposal number one will contribute to restoring orderly milk marketing conditions to this market.

Proposal number two. The current supply plant provisions have obviously been abused. Handlers are using the provision to draw money for the pool without increasing the availability of milk to meet the fluid milk needs of the market. Some distant supply plants and their brokers or agents have been solicited producers in the local area to help qualify the plants in the Mideast marketing area. Such actions used milk not normally or logically associated with their plant or the organization that owns the plant to meet qualifying shipments.

Milk that is normally logically associated with a plant or organization is only shipped to the market to meet token physical shipping requirements. This practice causes disorderly conditions in the local market as well as in the market with a supply plant is located. Section and 1033.7 (c) needs to be amended to enhance orderly marketing conditions.

The current provision, which allows supply plants to use shipments to distributing pool plants of other Federal Order markets for qualification purposes was useful at one time. Supply plants located within the market shipped milk to southern markets and contributed to the Class I utilization of the local market.

In recent months, this provision has been abused. Supply plants in lower utilization areas have use this provision to qualify by shipping milk to distributing pool plants in their local market and attaching additional quantities of milk to the Mideast market by using only token amounts of milk to supply the Mideast market.

We would suggest that the current provision be modified by allowing it to be used only by supply plants located within the marketing area. Changing this provision will enhance orderly marketing conditions.

The need for a provision to allow only net shipments from plants for qualifying purposes was well-documented at previous hearings for the former Federal Orders 1033 and 1036. Supply plants would shipped milk to distributing pool plants and would receive shipments of milk back from the distributing pool plants in return. In effect, the supply plants were contributing no milk whatsoever to the fluid markets.

The department agreed with the proposal at the time and a provision was put in both orders to prevent abuse. We believe this provision should be put back into the order to promote orderly marketing conditions and make more local milk available to the Class I market.

While there has been significant abuse of the supply plant provisions of the order, we question the advisability of eliminating the supply plant free ride months. Many times local milk supplies have been so burdensome during the flush milk production periods of the year that handlers have had to accept distress prices for surplus milk supplies in order to dispose of the surplus.

Requiring supply plants, especially those located outside the market, to ship when there is no obvious need for milk to meet fluid needs does not meet the definition of orderly marketing conditions by any interpretation. Such a requirement would just create unnecessary and uneconomic movements of milk. A net shipping provision would make the problem more onerous. Year-round shipping requirements would also discourage marketing organizations from pooling supply plants that actually do help meet the fluid needs of the market in late summer and early fall when production is at a seasonal low point and demand is strong.

In general, Order 33 is a deficit market for part of the year and surplus market for part of the year. Encouraging organizations to pool performing reserve supply plants is a positive move in our opinion.

We do support the addition of August as a month when additional shipments should be made, should be required and propose such an addition as an alternative to complete elimination of Section 7 (c)(4). The normal hot days of August have a significant impact on milk production and more and more schools are starting as early as the middle of August. This combined effect makes it quite difficult to meet the fluid market needs of the market. Supply plants should be expected and required to help meet those needs.

Proposal number three. Scioto County Milk Producers support increasing the number of days milk of individual producers must be physically received at pool plants to be eligible for diversion purposes. We believe the number of days milk should be received during the August through November time period be increased to four days equivalent and that at least two days equivalent be physically received impact December and January.

We strongly support the proposal that two day's production be required to be physically received at a pool plants in the other months if requirements of Section 1033.13 (d)(2) for the prior August through January periods are not met.

We would grant an exception to dairy farmers who marketed no grade A milk during the August through January period or who met the requirements for those months when grade A milk was marketed from the farm.

Proposal number four. Scioto County Cooperative Milk Producers strongly supports changes to provisions that will reduce the amount of time it takes to receive money owed to producers from the processors. Processors already have milk for up to 15 days before they have to make any payments. Increasing the partial payment to 110 percent of the lowest announced class price for the preceding month will improve cash flow for dairy farmers for product that has already been marketed. And adopting this proposal would give dairy farmers and little more protection from handler bankruptcy.

Proposal number five. Proposal number five is somewhat of a puzzle to us at this point and we are not sure if adopting the proposal will solve the problem that we see as a loophole that should be eliminated.

Supply plants located outside of the marketing area can easily pool milk on other Federal Order markets during the qualifying period of September through February. They can meet qualifying shipments on a reduced volume of producer milk pooled on the Mideast market during that period of time. Then in the amounts of March through August, they can add unlimited volumes of producer milk to their pool supply plants and still attain automatic pool plants status.

The best solution for this problem is to use location economics to reduce the value of producer milk based on where it is received in relation to the market. In other words, puts location pricing back in the federal milk order system. That would be their first recommendation.

Scioto County Cooperative Milk Producers would like to propose an alternative solution to proposal number five. Our proposal is to limit the amount of producer milk that can be added to a pool supply plant during the free ride months to a percentage -- we propose 110 percent-- of the daily average producer receipts qualified during the qualifying months.

Such a provision would recognize normal seasonal differences in milk production during the spring and summer months as compared to production during the fall and winter. We believe that such a provision would still allow supply plants from outside the marketing area to participate in the Class I returns of this market for the entire year, but would prevent plants from abusing the market by riding the pooled during the summer months with milk that did not service the market during the short production and high demand period of the year.

Proposal number nine. Four proposals at this hearing speak to the need to reduce diversion allowances. We support provisions that limit diversions to a percentage of milk physically received at a pool plant. We do not believe diversion allowances should be enhanced by adding additional diversions. Diversion allowances should not be so restrictive to completely discourage supply plant organizations from attaching milk to the market and supplying the market when needed. Of the proposals listed in the notice of hearing, we believe proposal number nine is the most acceptable for this market.

We do believe that August should be included as a month that requires more restrictive diversion allowances. More than ever, schools are opening in the middle of August and the typically hot days of August do have a negative impact on milk production. Diversion allowances of 60 percent during August through February and 80 percent during March through July are not overly restrictive and yet will assure consumers and fluid milk processing plants that their needs will be met.

And that is the end of my statement.

JUDGE CLIFTON: Thank you, Mr. Carlson. Questions for Mr. Carlson? Thank you, Mr. Carlson -- oh, Mr. Tosi was waiting to see if anyone else would ask.

CROSS-EXAMINATION

BY MR. TOSI:

Q I am just confused by a couple of statements you make in your statement, Mr. Carlson. You make several references in your statement about the lack of location pricing principles and specifically at least from hearing your testimony here, you make that a very strong feature about your position on proposal five.

Could you please explain a little bit more for my benefit and everyone else's and the record, what you mean by location pricing principles?

A It simply means that when you have a market, a defined market, milk that is received at locations distant from that market, certainly does not have the value to the market, the same value or even close to the same value as milk that is delivered to the market.

If Ohio, Michigan, Indiana is the market, then milk that is not received at plants located nearby that market doesn't have the same value to the market as milk that is received in that market.

Q In that regard, are you referring specifically to milk that is for Class I use or all milk?

A I am talking about producer pricing, not Class I pricing. Class I pricing -- I don't have any problem with Class I pricing that we have today. I have a problem with location pricing as far as it applies to producer milk and where it is received in relation to the market that it is attached to.

Q So, in your statement regarding proposal five and if I may quote, the best solution for this problem is use location economics to reduce the value of producer milk based on where it is received in relation to the market, in other words, put location pricing back in the Federal Order system?

A Yes.

Q What is it specifically that you are asking us to do in that regard?

A We in -- the markets used to have base pricing points. With the new markets, we have to establish new pricing points. And let's use -- because we are talking primarily about milk west of the market, let's say that Indianapolis maybe should be one pricing point. Any milk received at a plant outside of the marketing area should be priced at a lesser price to the tune of something like one and half cents for every 10 miles --

Q You are basically talking about a location adjustment to --

A On the producer pricing of that milk, yes, sir.

Q For example, if the pricing point is Cleveland, for example, what you are saying is reduce the amount of payment by, say, one and a half cents per hundredweight per 10 miles --

A Yes.

Q -- from the location where the milk was received.

A That's correct. Only I would use different pricing points than just Cleveland. Otherwise, it would be a little ridiculous if the market decides to use just one pricing point.

Q What is the relationship between that and the proposals that we are hearing here today regarding pooling issues?

A As I look at this, the pooling provisions did not change radically in order reform. Pooling provisions are somewhat relaxed on what they were on some of the markets, but in general, the pooling provisions did not change significantly during Federal Order reform. What changed was the pricing provisions. We eliminated location adjustments from when milk is received outside of marketing area.

Q Well, to the extent that in Federal Order reform, to the extent that every order had its own way of providing for adjustments, the department at that time concluded that we in effect had as many pricing systems as there were orders and to the extent that each county represents a location at which we have a reference price. I am having a difficult time understanding or seeing where we are not having this location pricing that you are advocating.

A I think the idea of establishing Class I differentials within each county is fine, but that does not help in trying to establish orderly marketing conditions for each individual market than has been established within the Federal Order system.

As a fine example, there was a hearing in Minneapolis. Milk from California attached to the Upper Mideast market. That milk that stays in California certainly doesn't have the same value to the market as milk that is located and delivered within the market. The same way as milk that is attached to this market, that stays in Kansas does not have the relative economic value to this market as milk that is delivered to Cleveland, Ohio or Indianapolis or to Cincinnati or any other location within the market.

Q In building off of your view on that, are you suggesting then that to the extent that some of the evidence has shown here -- or suggest that a lot of extra milk is being pooled on this market through diversion, that we no longer price diverted milk at the point which it is delivered or that we should be pricing it at the point from which it is diverted?

A No, it should be priced at the location to which it is diverted, but that price should be adjusted, depending on its location to the market that it is attached to.

And again, I will come back to the statement I made. I just find it absolutely ludicrous that milk can be diverted from this market to manufacturing plants in New York and Pennsylvania or some other place and end up receiving the entire producer milk than milk delivered to a bottling plant within the market. That just makes absolutely no sense, common sense whatsoever.

Q One other thing that confused me a little bit. In your statement regarding proposal number two in your last paragraph of your written statement, that paragraph seems to be suggesting -- or your position on proposal two seems to say we need to do something about performance standards and what it is that supply plants need to do to insure to be pooled and then you suggest that -- you take the position that year-round shipping would discourage organizations from pooling supply plants that actually do help meet the needs, the fluid needs of the market in late summer. In that regard, you are talking about year-round shipping requirements. How is it that if we are asking month in and month out for consist shipping requirements that somehow that is going to discourage supply plants from wanting to be pooled?

A I am talking in this case -- let's assume in this case, there is a supply plant in Wisconsin and we want -- we, the market, needs that supply plant to balance the market needs. In August through the middle of December, we need that supply plant shipping over to the market to meet the supplemental needs of the marketplace.

Now, you come to April, May and June and we have got too much milk in this market. We are shipping this milk in this market to Minnesota, to Wisconsin, to wherever we can find a place that will take the milk because there is too much milk -- and there is not enough capacity in this area to process all the milk that is produced.

We certainly don't need to have a supply plant shipping milk here, so we can turn around and ship other milk back up to Wisconsin. That doesn't make sense.

This is the value of having higher producer prices in this marketplace. You could attract organizations that are willing to meet those balancing needs of the market and they are willing to perform balancing functions in order to pay those attain those higher prices on a year-round basis. But they have to perform to get that advantage. They perform when the market needs the performance and that is August through December.

MR. TOSI: Thank you very much. I

appreciate it.

JUDGE CLIFTON: Other questions for Mr. Carlson? There are none. Thank you, Mr. Carlson.

(Witness excused.)

JUDGE CLIFTON: I believe Mr. Hollon is our only remaining witness. You may resume the witness stand, Mr. Hollon.

Whereupon,

ELVIN HOLLON

recalled as a witness, after having been previously duly sworn, testified further as follows:

JUDGE CLIFTON: Mr. Hollon, you remain sworn.

THE WITNESS: Yes, ma'am.

JUDGE CLIFTON: Mr. Beshore?

DIRECT EXAMINATION

BY MR. BESHORE:

Q Mr. Hollon, let's first address a few more points that were reserved the last time you were on the stand with respect to the information relating to proposal four. Have you determined the range of premium payments, over order payments in Order 33, which was requested of you by one of them?

A I think it was either Mr. Cooper or Mr. Tosi asked about the range of over order payments and that would be anywhere from zero to $2.10, would be a range. And in terms of a dairy market news report, it mostly would be 40 to 75 cents would capture the range of premium.

Q And that is within recent months and during the post reform period?

A Post reform period.

Q Now, have you also determined whether DFA has paid at least the minimum rates stipulated by the order on it's partial payments to producers?

A We have not in any month underpaid the minimum and many months over-paid the minimum and same on the final. We have not paid less than the final in any month.

Q Now, have you had the opportunity -- there were some questions that came up with respect to the information on Exhibit 22, tables -- well, the tables.

A That's correct.

Q Have you identified some things you want to clarify with respect to that data?

A Yes, I have. This table was updated since the Order 30 hearing and the updater, which was me, entered a number in the wrong row. I am going to point out that this would be --

JUDGE CLIFTON: Exhibit 22.

BY MR. BESHORE:

Q Yes, Exhibit 22.

A Okay, go to the page that has January 2001 and we will fax into the --

Q Well, describe the corrections you would like to make to the tables, please.

A All right. If you would look at the May Class III-A or Class IV column -- you see that $15.04? You see the next month is also $15.04. There was a copy that got put into the data, so when you correct that copy error, if you will turn to the percent page, table two of the percent page, I will give you the correct percentage number --

Q Let's make sure we are on the right page. Table two, the percent page would be --

A Would be table five-six -- or table six.

Q Now, you are going to which column?

A To the far right column, which is labeled Class III divided by blend at 10 percent.

Q And you want to make changes to the last five or six numbers in that column?

A That is correct. I am going to go from the most recent, which is 97, that should be 98.

Q Okay.

A The number that is 100 should be 98. The number that is 94 should be 102 and the other three numbers are the same above that.

Q Ninety-five, 88, 90 --

A Correct.

Q And going back to table two again, so we understand the error in the data, you have got a second set of entries. May and June show the same prices for Class IV and Class III.

A That's right. That row got repeated by mistake.

MR. BESHORE: We will supply Your Honor with permission of all concerned, the corrected Exhibit 22 for the record, if that will be helpful -- and I will send a copy to all interested parties, anyone who wants one.

JUDGE CLIFTON: Mr. Beshore, Ms. Taylor wants to send in some corrections to her exhibit. Mr. Hollon wants to send in corrections to his. There may be other parties as well. I think when we schedule the corrections for transcript, the briefing and so forth, you will build in a deadline for correcting evidence, for clarification of evidence presented and perhaps when is sent in could be posted on the website. Would that be appropriate, Mr. Tosi?

MR. TOSI: We can do that.

JUDGE CLIFTON: That may -- mail to

whomever you have the addresses conveniently available to you by e-mail or other, but that might not reach everyone.

MR. BESHORE: I understand.

JUDGE CLIFTON: Thank you, Mr. Beshore.

MR. BESHORE: And I would note that all of the data in the these tables, and correct me if I am wrong, the data is published statistical data.

THE WITNESS: That is correct.

MR. BESHORE: It explains the calculations that you have made, which numbers are added or subtracted or divided or multiplied by a given ratio and therefore, the final calculations can be checked or double-checked for published information by anyone. There is nothing in terms of the raw data here that is anything that you have generated as proprietary information or otherwise.

THE WITNESS: No, nothing.

BY MR. BESHORE:

Q Now, with those loose ends from prior issues, do you have a statement with respect to opposition to proposal eight and then a short summary and conclusion, concluding statement which also addresses the issue of the emergency status of the hearing?

A I do.

Q Would you proceed with both of those statements, please.

A The members of our group oppose proposal eight. Its purpose is misguided. The problem that it seeks to correct, commonly known as de-pooling occurs when one or more of the class prices is higher than the blend price and the handler reporting pounds of the higher valued classification does not put them on their pool report. Thus, the value derived from those poolings do not get entered into the blend price pool.

The problem that it seeks to correct is a function of advanced pricing. If the Class I sector of the market did not get the benefit of advanced price, simple arithmetic would guarantee and there would never be de-pooling.

Advanced pricing is a good practice as it allows the added value products to maximize their returns, which benefits all parties affected by the orders.

There can be no valid reason why the balancing sectors should have to pay into the pool on the occasional times when the advanced price causes a price inversion. Doing so could cause damage to the reserve and balancing sectors of the market here.

The reserve and balancing sectors would at times not be able to clear the market profitably if they wore advanced priced because of the volatility of dairy commodity markets.

If the proponents desire to change this happening, perhaps they should consider eliminating the advanced price provisions of the order

Proposal eight should not be adopted. This issue has been debated in other orders, but has never been found for by the Secretary.

Summary and conclusions. Data presented in this order indicates that milk from distant locations is being pooled on Federal Order 33 at increasing volumes. This milk volume reduces the blend price to local suppliers. Additional evidence shows that due to distance and economic return, this milk would never supply the market regularly.

Testimony from day-to-day operatives in the market and from bottling handlers in the market conclude that the dramatic increase in market reserve supplies as far beyond any level required to service the market.

We have demonstrated, on the basis of conclusions in the final rule, that milk such as these supplies generally and, in this case, from these specific locations was never intended to be a part of the Federal Order 33 marketing area. Geographically, it was never considered a part of the supply area and from a performance perspective, it cannot meet the requirements.

The fact that this milk is able to share in the blend price pool should not be corrected.

We have made several modifications to our proposals that correct pooling issues that were unclear to us until recently. However, these modifications are clearly within the realm of pooling regulations, the subject of this hearing.

Our testimony details the ramifications of the modifications and the manner that they contradict the intent of the Federal Order reform.

These solutions we propose are sounds and found in other sections of the order system and provide a rationale that can be consistently used for other orders. We have provided evidence that proposal eight would damage the market clearing sectors of the order. This could prevent the market from clearing excess supplies of milk weekly, that seasonally or holiday periods. This is disorderly and proposal eight should be denied.

Finally, we have demonstrated that the current provisions that set the advanced price paid to producers need modification.

Comments on the emergency status. Regarding the issue of an emergency decision, we have the following comments. The problems being discussed at this hearing are not unique to the Mideast marketing area. The problem when converted to cents per hundredweight off the blend price, this milk from distant areas taking advantage of open pooling type provisions and reducing the blend price for local producers who regularly serve the market.

The emergency is just as great in Kansas or Missouri, Indiana or Michigan, Colorado or Utah or Washington or Oregon.

DFA will ask for emergency decisions in hearing requests in the Upper Midwest, Central and Pacific Northwest Federal Orders. We cannot see and the fairness in a decision that favors one geographic area of the Federal Order system over another order area where the problem is the same issue.

What is important is that the decisions in each order area be either an announced over a relatively narrow timeframe or be implemented at the same time. If not, the problem that make a corrected in Minnesota or Iowa will just migrate to Ohio.

The likelihood will be that while there will be several hearings, the central focus of each will be similar. The dairy division should be able to process the hearings along similar tracks and produce decisions that look reasonably similar. They should speed the process.

Finally, for the purpose of voting on the record, we would expect the vote month to be a shipping, at the moment defined as September to November.

MR. BESHORE: Mr. Hollon is available for questioning.

JUDGE CLIFTON: Thank you, Mr. Beshore. Mr. English?

CROSS-EXAMINATION

BY MR. ENGLISH:

Q Mr. Hollon, you were here yesterday for the testimony of the dairy farmers who came to this hearing?

A Yes.

Q And you heard their request for emergency consideration?

A Yes.

Q They did not ask, did they, for this to be postponed, the decision on this matter to be postponed until hearings in the Central Order or hearings that have not yet been scheduled in the Pacific Northwest, correct?

A They did not.

Q They indicated in their testimony that this emergency was immediately important to them.

A That's correct.

MR. ENGLISH: Thank you.

JUDGE CLIFTON: Mr. Warshaw?

MR. WARSHAW: Thank you.

CROSS-EXAMINATION

BY MR. WARSHAW:

Q What is advanced pricing?

A Advanced pricing is the Federal Order language, the price in advance in the month in which the milk is delivered to the buyer and the buyer has knowledge of what that price is going to be before the milk is delivered.

Q Isn't that in place in order to allow the buyer to give prices to his customers?

A Certainly.

Q And it's necessary to that market because generally in that market, prices are established in advanced, are they not?

A I don't know that I would use the word necessary, but we think it's a good practice and should continue and should not be changed.

Q And in fact, it's not an arithmetic issue. It's a logical issue because you couldn't do the pooling if you didn't know the price in advance?

A No, no, it's an arithmetic issue because the Class I price is advanced and it becomes fixed and the reason why the pooling occurs is because Class III or IV, in some cases, Class II price is not advance and not announced in advance and therefore not fixed and the relationship between them is not fixed and the relationship changes and to do the extent that those prices are higher than the blend, in some ways, would make the decision to be pooled. But if those prices were all advanced, and all fixed, it would never ever happen.

Q When the blend price is higher than the Class III or IV price, the balancing sectors, as you call them, do receive a benefit from that?

A Yes, they do.

MR. WARSHAW: No more questions.

JUDGE CLIFTON: Thank you, Mr. Warshaw. Other questions? Mr. Tonak?

CROSS-EXAMINATION

BY MR. TONAK:

Q On your Exhibit 22, table two.

A Yes.

Q If we go to January of 2001, it shows a Class IV price of $12.13 and a Class III price of $9.99.

A Right.

Q What was the class price that was used under the Federal Order to calculate the minimum advance payment due to producers for milk produced in January?

A Be the -- produced in January -- $12.13?

Q As I look at this, and you answered it with a question, so I am taking it you are not sure that's it's $12.13?

A That is correct. I was trying to think through which would be which.

Q The way --

A It would be the lower of.

Q The way I view this, you use the lower of the previous month's Class III or IV price.

A Yes.

Q So, in effect for January advanced payment, you would use the Class III price for December of $9.37 --

A That's right.

Q -- and --

A Next time I use this chart, I am going to draw all these things on there.

Q And to actually compare a relationship of how the advanced price actually paid to producers for their January milk to the blend price for their January milk production, you would need to use that December Class III price and also use the January blend price in calculating any percentages or relationships or so on.

A That's correct.

Q And as we go through these, I'm not sure that that is what happened. I know there was some corrections made in some percentages. Could you clarify for me if the comparison is the current's month's Class III price or IV price, whichever is lower and the current month's blend price or the previous month's Class III?

A The relationship that you just described of $9.37 compared to $12.54 is the comparison that should be made and that is what my attempt was to do each month.

Q Do you know if that is actually what happened in these percentages?

A I think so.

Q Let's look at August 2001 then as a --

A Okay, when you get to last five months of the year -- I had a row that was August -- that was the correction that I made.

Q I mis-spoke the month that I wanted to look at. On July -- no, August 2001 --

A Again?

Q -- let's use -- let's look at June 2001.

A Okay.

Q And the lowest Class III price -- or the lowest price in Class III of 13.83 --

A Mm-hmm.

Q And as you compare this then, the 13.83 Class III price for advanced for June 2001, would be 13.83, I believe.

A Okay.
Q Now, as we compare that to the blend price for June of 15.97, and we go through your 110 percent calculations and come up with a 15.21 Class III price at the 110 percent, compared to the 15.97, now that is the actual comparison that we are really talking about making, isn't it? The -- the previous month's Class III used for the advanced payment with the current month's blend price, 15.21 to 15.97. And when we look at these percentages in table six, I'm just trying to -- without recalculating all these, know if the correction you gave us is the correct correction or if it actually as it appears in the table is correct.
A The month that you picked is the month that I had a data error, so when I went back and corrected those errors, that month would show 76 cents difference, 15.97 minus 15.21, 76 cents. That would be one, two, three, four from the bottom. So, if you went to tables three and four --
Q Let's take an earlier month, just so --
A Okay.
Q Take May of 2000. 9.37 is the lowest Class III price, the lowest price -- according to this. And that was the May of 2000 Class III price, would have been the advanced price used for June 2000 milk, so you

are calculating out the 110 percent. Be 10.31 and that would compare to a blend of 12.38?

A Yes.

Q And the percentages in this table did that even though the way these numbers are lined up, didn't pair that off --

A Right, the formula for -- that used the 12.38 number reached up one row above it to pick up the prior month's Class III relationship, which is the -- the one you asked me that I answered wrong and you --

Q Well, it's easy to confuse me. A couple of other questions. In your conclusion, the summary and conclusion, point two, emergency is just as great in Kansas or Missouri and so on and we have to keep this because the problem in Minnesota and Iowa may just migrate to Ohio and so on and so forth a little later on.

A Yes.

Q Do you have any concerns that that problem in Ohio may migrate to the Appalachian order?

A I could, but it would be a little more difficult because the standards are a little higher there. But that could be a possibility.

Q Does DFA have any plans of calling for a hearing in the Appalachian order to help off-set or prevent any possible problems down there?

A We have looked into that and concluded that the current pooling standards seem to be sufficient to keep that from happening.

Q Does DFA pool milk from the -- originating in the Mideast area and other northern areas in the Appalachian order area on an ongoing almost year-round basis?

A From time to time, we pool milk in that area.

Q Do you ever pool milk from the Mideast or other northern areas in the Appalachian area or the southeast area at the same time that milk is moving out of the Appalachian area or the southeast area back to the northern area for surplus disposal?

A That may happen Christmas, New Years, Thanksgiving, may happen some days. It's possible.

Q But you don't see it happening during May or June or the spring flush months?

A Doesn't happen as much.

Q It doesn't happen as much, but it may happen.

A It may happen. Plus Fourth of July, Memorial Day -- May and July.

MR. TONAK: Thank you.

JUDGE CLIFTON: Other questions for Mr.

Hollon? Mr. Beshore, anything further for Mr. Hollon?

MR. BESHORE: No, I have nothing further.

JUDGE CLIFTON: You may step down, Mr. Hollon.

THE WITNESS: Thanks.

JUDGE CLIFTON: You are welcome.

(Witness excused.)

JUDGE CLIFTON: That will not conclude the evidence to be received in that I will accept clarification evidence post-hearing. And I am not looking for anyone to expand on the evidence already presented, but to correct and to clarify any evidence.

Mr. English?

MR. ENGLISH: Shouldn't it be limited to correct or clarify those matters that have been expressly identified today, as opposed to any matter?

JUDGE CLIFTON: Start again, please.

MR. ENGLISH: Shouldn't that be limited to expressly clarifying and correcting those matters that have been identify today as in the Leprino Sue Taylor exhibit, the very explicit issue about what lines up and how that affects that document and the very explicit issues that Mr. Hollon has raised as opposed to being broadly any corrections?

JUDGE CLIFTON: I believe that the

decision-makers would be assisted if any errors are corrected, including those that we have already identified, but any others that may be identified.

So, any matter that, upon reflection turns out to be misleading or erroneous could be corrected by submitting additional documentation to show the revised information as far as I am concerned.

Mr. Tosi?

MR. TOSI: Yes, Your Honor, regarding that, the submission of those sorts of corrections, we are trying to make it as a regular practice now to post on the internet all exhibits that we receive, part of the proceeding. Do you want us to just post those, the corrected information rather than the information that was submitted that may be erroneous?

JUDGE CLIFTON: No, I think people should have access to the whole record --

MR. TOSI: All right, thank you.

JUDGE CLIFTON: -- including the wrong ones, so I think all these 23 exhibits -- actually, 22 that were received into evidence, because Exhibit 6 was rejected, so I don't know what you want to do with the rejected one. It was rejected only because it was a duplicate. But I think all of those should be posted in addition to what comes in to correct them.

Yes?

MR. COOPER: Your Honor, to clarify, I think we should be limiting the corrections that come in to actual tables and charts and exhibits, where there is erroneous data put in there. If people want to correct a number or something like that, that would be fine. But if, you know, wording just too broadly takes away people's right to cross-examination.

JUDGE CLIFTON: I think on balance, Mr. Cooper, we are better off to let people correct errors that they may have made in their testimony as well as in their charts, if they discover that they have in fact provided erroneous information and if I am going to allow the witnesses who have discovered their errors to do it, I think we need to allow everyone to. I don't think it will open up Pandora's box. I know that --

MR. COOPER: In both cases here, we are talking about information that is published information, both in Sue Taylor's case and in Elvin Hollon's case. They both published information that they took and subtracted and divided and this sort of thing with it. I mean, Class III prices, it's blend prices, it's Class IV prices and as far as I know, it's just subtraction and addition. It's not new information or some sort of information they dug up from somewhere where nobody is questioning the source. This is published dairy division information that they are using and they just improperly manipulated it. We all blame Bill Gates for it. None of us actually did it wrong.

JUDGE CLIFTON: So, Mr. Cooper, it would be the government's preference that I not allow correction of any erroneous evidence, but only Ms. Taylor's exhibit and Mr. Hollon's exhibit?

MR. YALE: May I be heard, Your Honor?

JUDGE CLIFTON: You may.

MR. YALE: There is a value to this record that goes beyond this decision and there are times, unfortunately, we go into what we call 15-A proceedings and the testimony that is given is very important and there have been times in the past where those of us who understood and were present at the record are sure that what the witness said wasn't what was in the testimony, only because of a homonym or a misunderstanding of a technical term by the reporter or something like that.

And I think you let the record -- people want to make objections after they correct it and if somebody thinks they have gone too far, they have changed their testimony, then they have a right to challenge that and the Secretary has the authority to make those rulings to clean it up.

My experience has been it has never been abused and knowing the people that have been here, it's not going to be abused. I think we are arguing about a possibility that will never occur.

MR. COOPER: What Mr. Yale is talking about is corrections to the transcript. That's not what we were talking about.

JUDGE CLIFTON: Well, with all due respect to your position, Mr. Cooper and yours, Mr. English. both of which I respect very much, I will invite any corrections to erroneous information and what I would like to do is place the deadline for correcting any erroneous evidence, whether it's testimony or exhibits, I would like that deadline to be the same deadline for suggesting revisions to the transcript. So, in other words, at the same time you scrutinize your testimony to see what errors may have crept in through the reporting process, you would also be looking for accuracy.

Now, we need to set that date and thereafter, a briefing date. Last -- the only time I have been involved in a milk hearing other than this one, it took a month before the transcript was available to people. That really surprised me.

Mr. Beshore, the schedule that you had suggested turned out to be the fastest it could be done even though that also was an emergency situation. So, I am going to invite counsel now to suggest to me -- I have got a calendar here -- 2001 and 2002 - suggest to me the dates that you would like for the two deadlines. The first deadline would be to correct transcript and evidence. Then thereafter, a deadline for submitting the briefs. You have got to allow the transcript to reach you first and be digested and as I say, last time, it took a month for the transcript to be available. I hope it won't take that this time. So, I will entertain proposals. Mr. Carlson?

MR. CARLSON: Can we have the reporter give us some idea how long it might take in her opinion?

THE REPORTER: My deadline is 10 days to the contract holder.

MR. ENGLISH: Then it has to be mailed.

JUDGE CLIFTON: And it normally takes a week thereafter, but Mr. English is absolutely right. The processing of the mail is becoming a more time-consuming process than it used to be. All the USDA mail is now opened off-site. Mr. Tosi?

MR. TOSI: Your Honor, when we order the type of transcript that we wanted done -- I appreciate what the court reporter is saying, but we ordered five working days and it's delivered to us. Maybe, Your Honor, you could order that it be done tonight or something.

But we ordered five days last time as well and we waited a month.

JUDGE CLIFTON: And it took a month. I think the very earliest you could expect to find it on the website would be 15 days from now and that would be amazingly fast and it may take a month.

MR. BESHORE: Your Honor, we never know the transcript -- but let's assume it's two weeks. Give us a week for corrections and then, what two weeks after that for a brief. I mean, we would like to get this rolling. I mean, there is some testimony here that there are some potential significant losses that producers can incur in January or at least February.

MR. COOPER: Your Honor, could I ask a question of the reporter. Is this 10 days from today or 10 working days that you are supposed to send it to Silver Springs, do you know?

THE REPORTER: I believe it's 10 business days.

MR. COOPER: Ten business days? Not 10 calendar days? I'm just -- that ends up being three weeks.

JUDGE CLIFTON: Let me do this. Let me say that three weeks from today.

MR. ENGLISH: Why don't we assume at least three weeks for the transcript, because we know it will be two and we will be playing this game anyway, so why don't we assume at least three weeks for the transcript, one week thereafter for the corrections and two weeks thereafter for the briefs.

JUDGE CLIFTON: Let me tell you how that would compute. That would mean you would receive the transcript on November 14th and your corrections and revised evidence would be due the day before Thanksgiving. Now, that is to be deposited in the mail and your corrections and revised evidence would be due the day before Thanksgiving. Now, that is to be deposited in the mail, so perhaps that's okay. These deadlines are when you deposit in the mail. And you may also want, as a courtesy, to e-mail, particularly Mr. Tosi. That would certainly help in his being able to make it available on the website.

MR. TOSI: All the hearing participants are very good about sending an official copy and a fax copy or e-mail copy or something like that.

JUDGE CLIFTON: Good. So, what do you all think about putting your transcript corrections and your evidence corrections into the mail by November 21, 2001? Mr. English?

MR. ENGLISH: It's fine.

JUDGE CLIFTON: Who else wanted to file a brief. Mr. Beshore?

MR. BESHORE: Yes, that's fine assuming we do have the transcript.

JUDGE CLIFTON: How long do you want for your briefs? Three weeks? That would be December 12th. Does that work? All right, briefs will be due December 12, 2001. That's to be deposited in the mail to the hearing clerk. The hard copy goes to the heading clerk even though you may be courtesy copy alert Mr. Tosi to what you are forwarding to the hearing clerk.

So, corrections to transcript, corrections of evidence are due the day before Thanksgiving, November 21, 2001.

Now, if the transcript is not available on the website by November 7th, you may extend these deadlines by the number of days thereafter before the transcript appears on the website without going through all of the rigmarole of having the marketing diversion have to tell everybody what their new deadlines are.

Anything further before we close for today? Nothing further, we will adjourned at 4:14 -- oh, Mr. Tonak.

MR. TONAK: There is a couple of USDA

documents that we would like to be able to refer to that are not submitted in their entirety. Mr. Hollon made extensive references to the -- I believe the recommended decision published in the end of April 1999 and the final decision published September 1, 1999 concerning Federal Order reform. And we would like to be able to incorporate, if necessary, other parts of those documents into some of our submissions.

Also, the market administrator's office for the central area compiles information on producer milk marketed under Federal Order for the months of May and December and that information is regularly available from them and we would like to be able to reference May 2000, December 2000 information and also within a few weeks May 2001 information should be available and we would like to be able to reference that.

JUDGE CLIFTON: Is there objection?

MR. COOPER: Is that the Central Order?

MR. TONAK: For all orders.

JUDGE CLIFTON: There being no objection, those being matters of public record, your request is granted.

Mr. English?

MR. ENGLISH: Your Honor, there has been some references in this record to the provisions within

Orders 5 and 7 having to do with the provisions there and I do not have the references we me, but I intend to make reference to at least for historical analysis purposes the language of the final decisions, recommended final decisions creating and expanding the Appalachian Order as well as the Southeast Order 7, just with respect to the limited issue of pooling, the history of why those pooling provisions are the way they are for comparison purposes.

In addition, there is one question that I still have. I know that Mr. Rasch and Mr. Walker are confident of the answer, but I have a question as to the historical derivation of 1033.7(c((4), the last sentence, that Mr. Yates referenced in his testimony having to do with the treatment of requalification purposes of a D, E or F plant under 1033.7(c) and I believe that we will find that the D plant is derived from an old Order 36 decision and I believe we will find the E facility is derived from an old Order 40, but I don't know which one right now and I will probably be making reference once I can dig back in history, but these are all public documents that I would be referencing, but for putting people on notice of what I would be looking at, these issues were addressed in testimony.

JUDGE CLIFTON: Thank you, Mr. English. Is there any objection? Mr. Beshore?

MR. BESHORE: If I might, Your Honor, I hate to get into an argument at this point about the need to -- an apparent need to note official acts of the Secretary, make them a matter of official notice on the record of this hearing in order to have the ability to refer to them in the briefing process. I --

JUDGE CLIFTON: Mr. Beshore, do not worry about that. It's not necessary. All these matters certainly can be referenced and broadened in your briefs, but I think Mr. English did it as a courtesy.

MR. ENGLISH: Yes, I was intending it as a courtesy to tell people in advance that I am going to do that.

MR. BESHORE: That's fine. So long as it's understood that publications in the Federal Register -- the Code of Federal Regulations and final decisions -- the Federal Register, historical actions of the Secretary, to the extent that they are pertinent to the briefing process, we are going to feel free to make reference to them

JUDGE CLIFTON: You are absolutely correct.

MR. BESHORE: Thank you.

JUDGE CLIFTON: You are welcome.

All right, I congratulate you on a very

well conducted hearing. I am particularly impressed with the way ideas synthesized and I think this was a very dynamic process and very helpful and very professionally presented. Thank you all.

(Whereupon, at 4:20 p.m., October 24th, 2001 the hearing was concluded.)

- - - - - - -

REPORTER'S CERTIFICATE

DOCKET NO.: AO-168-A68

DA-01-04

CASE TITLE: MILK IN THE MIDEAST MARKETING AREA

HEARING DATE: October 24, 2001

LOCATION: Wadsworth, Ohio

I hereby certify that the proceedings and evidence are contained fully and accurately on the tapes and notes reported by me at the hearing in the above case before the United States Department of Agriculture.

Date: November 1, 2001

Official Reporter