VOLUME XIII

BEFORE THE SECRETARY OF

THE UNITED STATES DEPARTMENT OF AGRICULTURE

AGRICULTURAL MARKETING SERVICES

In the Matter of Proposed) Docket Numbers
)
Amendments to Tentative) AO-14-A77, et al.
)
Marketing Agreements and) DA-07-02
)
Orders)

National Public Hearing
Wednesday, July 11, 2007
9:00 a.m.
Sheraton Hotel Station Square
300 West Station Square Drive
Grand Station Ballroom I
Pittsburgh, PA 15219

BEFORE: JUDGE VICTOR W. PALMER
U.S. ADMINISTRATIVE LAW JUDGE
UNITED STATES DEPARTMENT OF
AGRICULTURE

TRANSCRIPT OF PROCEEDINGS

Reported by:

Monica R. Chandler
Court Reporter

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I N D E X O F W I T N E S S E S

I N D E X   O F   E X H I B I T S

P R O C E E D I N G S

ROBERT YONKERS, Ph.D.

a witness herein, having been previously duly sworn, was examined and testified as follows:

MR. PALMER: On the record give your name again.

MR. YONKERS: My name is Robert Yonkers.

MR. PALMER: And Dr. Yonkers, you had testified earlier, but we didn't get to your cross-examination. So we will start with cross-examination now. Who first wishes to question Dr. Yonkers?

CROSS-EXAMINATION

BY MR. BESHORE:

Q. Good morning, Bob.

MR. PALMER: Spell your name for the reporter.

MR. BESHORE: B-E-S-H-O-R-E.

Q. Bob, do you know the aggregate impact of the positions which IDFA is presenting in this hearing on the producer prices?

A. I have not conducted that analysis, and even if I had, on my previous testimony there has been testimony since then that changed that make allowance data, and I have not calculated that.

Q. With respect to the make allowance data, what make allowances is IDFA supporting on the basis of the present record, for the sake of cheese for starters?

A. Marv, I have not inputted to do data that Mark Stephenson presented into that. I didn't come here prepared to do that, because I previously testified on make allowances. I intend to do that on my brief, but I have not put that in the spreadsheet yet.

Q. How do you expect to incorporate it with the formulation? What weight do you expect to give it?

A. I expect to use the exact methodology that I testified to in my previous testimony in support of the make allowance proposal. I can't remember which number it was.

R. Yonkers - Cross by Mr. Beshore

Q. Using Dr. Stephenson's current numbers as to replace the Stephenson numbers in your previous equations --

A. Which would rate it with California and the rest of the U.S. data using the most recent NASS dairy product production that is available which is consistent with what USDA data tentative rule is. The only change that I had recommended in my previous testimony was that in addition to using the California data on butter, cheese and low fat dry milk, that they also use that data on dry whey.

Q. Let's talk about your testimony, Proposal XX, for a minute or two. Do you recall Ed Gallagher's testimony with respect to Proposal XX which identified the portion percentage of cheese transactions which NAA cheese represented? Do you remember that?

A. I remember generally. I don't remember the specifics that he testified to.

Q. Do you have any problems with his methodology in identifying -- I'm trying to isolate what portion of the cheese universe the NASS eligible production represents.

R. Yonkers - Cross by Mr. Beshore

A. I didn't review that part of his testimony, Marv.

Q. Well, you accept the fact that that is a minority of the cheese universe?

A. You are talking about total U.S. natural cheese production?

Q. Right.

A. I accept the fact that NASS represents less, considerably less than total U.S. natural cheese production recorded by USDA.

Q. In fact, the total American cheese production is only, what, about 30 percent of all cheese production?

A. I believe it's higher than that.

Q. What do you think it is, total of all American cheeses?

A. Marvin, I'm not going to give you a number because I don't have that, but I believe it's higher than 30 percent.

Q. In any event, the dairy products publications, for instance, like dairy products in their summary would have that number?

A. Yes.

R. Yonkers - Cross by Mr. Beshore

Q. And of course, cheddar is a subset of whole Americans?

A. Yes.

Q. NASS eligible cheddar is a subset of all cheddar; correct?

A. Yes.

Q. Do you recall about what portion of cheddar is NASS as reported in the NASS weekly summary?

A. I don't know that that can be calculated from data that has been entered or noticed.

Q. Whatever percentage that is, and the data is in the record in terms of weekly NASS volumes and monthly and annual dairy products volumes, you would agree; correct?

A. Yes.

Q. Now, it's only the NASS eligible product that has any pricing circularity issue; isn't that correct?

A. No; I disagree with that entirely.

Q. In the cheese market?

A. I disagree with that entirely, and my reason for that is all cheeses sold, whether

R. Yonkers - Cross by Mr. Beshore

they are NASS eligible or non-NASS eligible, however relationship to that NASS eligible type of cheddar, and as an economist any time you change relative prices in the marketplace, there are market responses on the demand side. If there is an established relationship in the marketplace based on what consumer demand is, and I'll use mozzarella because that is the second most produced type of cheese.

Q. Or is it the most produced type?

A. It may be. That is a recent change, but, once again, it has a relationship to cheddar prices in the marketplace. They are cheeses. They have different uses in food service and in retail, but they have a price relationship. And when you change that price relationship, consumers will change their consumption of those products based on changes in relative prices in the marketplace. So you can't just say that there is no relationship to the market for any other type of cheese than what is NASS eligible to be reported.

Q. Did I ask you whether there was any relationship?

R. Yonkers - Cross by Mr. Beshore

A. That causes the circularity issue with respect to other types of cheeses than NASS eligible cheddar. I was answering your question.

Q. You are using circularity in a much, much broader concept than it's being used in this particular proceeding with respect to the very particular price challenge that producers have -- that manufactured product sellers have who report their products to NASS and then have the NASS price set their milk price. You understand what I'm saying? Circularity has been defined particularly by Agri-mark, among others, in these proceedings. Do you accept that?

A. I disagree with that definition of circularity in the respect that you can -- that incorporated in that is an assumption that you can change relative prices for other cheese products relative to NASS eligible cheddar cheese and not have an impact on the marketplace and therefore our members of the mind for the IDFA who manufacture those other types of cheeses.

R. Yonkers - Cross by Mr. Beshore

Q. So you have a different definition of circularity than --

A. I do not believe that I have -- circularity, as several have testified in this hearing, is defined as when you sell a cheese product, does it impact your margin above what you have to pay producers based on the Class III price formula that incorporate the NASS eligible cheddar cheese. I believe that any time you try to sell a product in the marketplace and change a price relationship, assuming that you can change a price relationship, merely because you're not recording that price because it's not NASS eligible cheddar cheese, you do have an issue that affects your plant operating -- your ability to cover your cost of processing in your plant.

Q. Well, basically, you are just saying that if one party in a market moves a price and nobody else moves a price, that there is some impact in the marketplace, for their product. Isn't that what you are telling me?

A. If one party moves the price --

R. Yonkers - Cross by Mr. Beshore

Q. You are saying that your definition of circularity is, if you change your price and other parties don't so that, therefore, your relative price with respect to other parties has changed, that there is an impact. I think that's what you told me. Restate it.

A. Those who assume that you can make a price change without having an impact on the marketplace are incorrect. That's exactly what I'm saying.

Q. Are you saying that Proposal XX is proposing -- is basing that on the assumption that you can change prices without having an impact?

A. As I recall reading through the testimony and the transcript of cross-examination from Mr. Gallagher, he made it very clear that it's commonplace to have people use different relationships to a reference pricing in the marketplace, and I agree with that statement. However, he went on to say that it would be logical that the next logical step is to assume that you can change those price relationships with it, and that

R. Yonkers - Cross by Mr. Beshore

wouldn't have an impact. That you could just go in and add, as one of the examples that was used during cross-examination, three cents. If three cents is determined to be the cost increase through a hearing like this, or however the determined USDA uses, that you can go in and change a price relationship that exist in the marketplace today by three cents without having your customers think about using different suppliers or having impact and demand on the marketplace, and I disagree that that can happen in the marketplace.

Q. Does the CME change when the cost to produce cheese change? Do they eventually over time build into that pricing?

A. I think that the price that people pay for milk changes. When cost of production change, because if you look at the --

Q. That wasn't -- Bob, that wasn't the question.

A. No; I do not believe that CME prices change when cost of manufacturing change.

Q. So the prices of cheese in a supply demand marketplace do not change over time with the cost of producing cheese?

A. Now you asked me a different question.

Q. Well, I'm asking you a different question, yes.

A. In a supply and demand situation in which there is not a regulation that dictates the margins that plants can earn, then there are supply and demand dynamics that affect the marketplace, and you can look at that. You have to know what the supply and demand estimates are. Some of those costs may be passed each way, but they are not only passed one way in an unregulated supply and demand marketplace. That is not what we have here today.

Q. So is it your testimony today that the CME price for cheese is determined by the regulated minimum price for milk?

A. The CME price is determined by the supply and demand for cheese in the marketplace. However, because of the regulated minimum pricing, any plant which is regulated by Federal Milk Marketing Orders has a cheese

R. Yonkers - Cross by Mr. Beshore

product that is sold either on the merc or relative to merc prices, they can change that price all they want, and they will not change the contribution to cover their cost of processing because of the minimal price regulations that exist.

Q. If somebody is selling for CME plus five cents, are you saying they have a margin that is different than the cheese producer that is selling for the CME flat price?

A. Could very well, because your customer has a choice of buying from you at the CME plus five cents or by going to the CME at the CME price for five cents cheaper. There must be some advantage, whether it has to do with location value, whether it has to do with the quality of cheese, the particular specs of the cheese. There has to be something in there, and that can incur at a cost of manufacturing.

Q. The CME, buying off of CME you're buying a very specific and limited specification product at a very specific and precise location and packaging and all of those sorts of things; isn't that correct?

A. That is correct, but you ask me about someone buying at the CME plus which means it is not going through the CME.

Q. I understand, but I was comparing that to the CME. I mean, anyone who is buying a product that's not specified, not specifically the same specifications as a CME, can't buy from a CME; is that correct?

A. That is true.

Q. What percentage of cheese transactions meet the very precise specifications of a CME transaction?

A. I don't know that. I don't know that anyone knows that answer.

Q. But wouldn't you agree, speaking on behalf of your parties you represent, that it's a small percentage of the total transactions of cheese?

A. I think it could be a larger percentage if people wanted to adjust their production practices to make that specification. So I think the capacity exists to have a larger share, but currently unless

R. Yonkers - Cross by Mr. Beshore

people have -- unless their customers specifically want that specification or unless they specifically want to produce cheese to take to the merc, it's not likely to meet the exact merc specifications.

Q. So that presently in present trade practices in the industry only a very small number of people could actually displace the presence of supply transactions in the immediate with purchases off of CME; isn't that fair?

A. Could you define immediately. I mean, they can change their plant practices within a week, I would imagine. You probably should ask one of my other members to testify, but you can change what you are putting and have different specs of cheese come out in different packaging in your plant, I would assume rather quickly. But you should have asked one of my members when they were up here.

Q. What is your answer?

A. I think it can be done relatively quickly. If your plant has lost a customer and needs to have a market for milk that you are

R. Yonkers - Cross by Mr. Beshore

processing the cheese that you are producing, you better be producing at a specification that has a market outlet.

Q. I was asking a different question. I'm talking about cheese customers.

A. You are talking about cheese customers going somewhere else?

Q. Right.

A. I have it.

Q. My question is --

A. I have your question. It's a very competitive marketplace out there, and I know a number of my members that their current supplier wanted to increase their price relationship with the merc. They would look very seriously at changing their production line in order to satisfy that customer if the customer came to them.

Q. My question was, Bob, isn't it true that very few existing customers can go, as you postulated in your testimony, could replace a current supply arrangement with a purchase directly off of CME?

A. I don't know the answer to that

R. Yonkers - Cross by Mr. Beshore

question. Depending on whether they are using and cutting and wrapping the cheese directly or if they are further processing the cheese. Certainly for barrels it's always further processed. I don't know what else they could do. I do believe that they could find another supplier quickly to service their needs if there was a significant increase or any increase, for that matter. I mean, you're talking a penny per pound for cheese. Multiple pounds of cheese can make a big different. If people try to change those price relationships, there will be customer response.

Q. Now, your testimony pauses primarily the ability of customers to go to nonfederal sources?

A. Non-federally regulated.

Q. Non-federally regulated which are primarily in California.

A. Idaho. Even within federal order there is some cheese or some milk that is not regulated in terms of de-pooling plants have the opportunity to make a decision every month.

Q. Set aside de-pooling for a moment.

R. Yonkers - Cross by Mr. Beshore

A. Okay.

Q. Are you aware of any substantial volumes of non-federally regulated milk produced manufacturing cheeses to Idaho.

A. No, I'm not, but the potential exists.

Q. And by that you are suggesting that somebody, a cheese manufacture in eastern Idaho would get a supply of milk if it wasn't federally pooled in manufacturing cheese?

A. In the short range, sure. It would be very difficult.

Q. They would have to pay one price to get that milk?

A. In the short range, no. They probably -- I agree that in a short period of time if they are significantly underpaying, they would lose their supply of milk, unless there were alternatives for that milk.

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

MR. PALMER: Any other questions?

MR. YALE: Good morning.

R. Yonkers - Cross by Mr. Yale

Ben Yale for Select, Continental and Dairy Producers of New Mexico.

CROSS-EXAMINATION

BY MR. YALE:

Q. Historically IDFA has proposed the use of the CME as the price series; is that correct?

A. That's correct.

Q. In light of GAO's report on CME's, the IDFA made a change in its position?

A. That report just became available to us last Thursday. My initial reaction, and I have not discussed it with our member committees and our boards, but I did not see anything in that report that changes my opinion.

MR. YALE: I have nothing further.

MR. PALMER: Other questions? Mr. Beshore.

MR. BESHORE: I have another question or two.

R. Yonkers - Cross by Mr. Beshore

CROSS-EXAMINATION

BY MR. BESHORE:

Q. With respect to Dr. Stephenson's information about how IDFA would be applying it to proposed make allowances, would you be using the Stephenson four digit current July '07 calculated make allowances, do you expect, which have a different configuration of plants previously?

A. Since we only saw that this week, we have not had a chance to convene our member committee to discuss that, which piece of data in his testimony we will be using.

Q. So you have at least two choices. Maybe there are a whole slew of them?

A. I look at it as being two choices for cheese, and that is weighted average or apply the increase that he testified himself to is most representative of what change occurred in the population of cheese plants between his last survey and this one.

Q. Which is what?

A. That was 1.7 cents higher for the cost of processing for cheeses.

R. Yonkers - Cross by Mr. Beshore

Q. So those are the two options. With respect to the 1.7 cents option, you would agree, as he indicated, that that's skewed to the smaller plants? Seven of the eights plants were in the smaller strata?

A. When he was being cross-examined by Mr. Rosenbaum, he indicated that two of the large plants from the last time were in among those eight, and when Mr. Yale was cross-examining him, he said only one. So there was a difference that he had in his cross-examination. If you go back and you look at his testimony from last time, he said that all five of those large plants were in his data sets. So I have to go back and look at the record, Marvin.

I believe the last time by what I calculated from Mr. Rosenbaum's cross-examination that in the 16 plants from his survey that he testified to in September of '06 two of those were from the top 10 percent of plant by plant size and the other 14 were from the remaining 9 percent. Based on Mr. Rosenbaum's cross-examination at this

R. Yonkers - Cross by Mr. Beshore

hearing, I thought there were two plants from last time that were among -- I'm sorry.

Q. One large one.

A. Yes; one large one and seven small ones which is the small proportion as last time.

Q. Among the eight there was one large and seven small. That is what he told me.

A. There were two large and fourteen small. So it's exactly the same proportion as last time.

Q. So that would be your theory in using that cross-section or that set subset of plants?

A. They're exactly comparable to the distribution from the top 10 percent and the bottom 9 percent as he had in the 16 plants that he presented from what I understood his cross-examination is.

Q. Now, the IDFA recommendations with respect to whey cream, there is nothing in the hearing notice that said what your pricing recommendations were going to be on those; right?

R. Yonkers - Cross by Mr. Beshore

A. How to change the formula specifically.

Q. Right.

A. Ms. Taylor's testimony contains that, and she will be presenting that testimony for us.

Q. Because there is nothing in the hearing notice that USDA was unable to calculate the economic impact of those. You recall that?

A. Yes.

Q. Do you have an estimate for IDFA today on the economic impact of the proposal that you're now advancing on producing prices?

A. No.

MR. BESHORE: I would like to ask at this time, Your Honor, if the Department would -- that the Department do an economic analysis of the proposal which basically just surfaced with Ms. Taylor's testimony, as they've done with all other proposals upon which they can put numbers that have been in the hearing so far, that that be posted as the other economic analyses have been as part of this record.

MR. ROSENBAUM: Your Honor, before you get any response, I would like to correct the record as to when things happened. Ms. Taylor's written testimony was submitted in advance at the Indianapolis hearing which was in April. Ms. Taylor ended up not testifying in April because other witnesses took up that space, but her testimony was posted, and that portion of her testimony was those calculations were in terms of hundredweight impact were included in that testimony. So this is a request that could have been made months ago.

My understanding is that USDA ultimately performs an economic analysis of the proposals that its adopting when it puts out a recommended ruling. It seems to me that that would be an appropriate year that adopts our proposals that would include the impact on their analysis.

MR. BESHORE: I think the purpose of having an economic analysis that we have thus far, and I didn't mean to misstate it if I did at the time when we had

Ms. Taylor's testimony, but the purpose of the economic analysis that we have had in the records so far with respect to proposals is so that the industry participants, briefers, could note the potential impact of the proposals in the hearing and comment upon them in the course of the hearing, and I think it would be most useful to have that information, and I would make that request.

I would also just add to that request that the aggregate, to the extent it's possible, the aggregate impact of all of the IDFA positions and that's similar to a request I made earlier.

MR. PALMER: If the request had been made earlier, then, of course, the material would be before us. Now it's cross-examination that's being engaged, and it's made before the recommended decision produced in briefing. It's not made until a recommended decision. I guess you could do something on your objections to the recommended decision, but I would leave it up to the Department. Do you wish to respond to this or just take it under advisement?

MS. PICHELMAN:

heather Pichelman from the USDA. The economic analysis request has been noted.

MR. PALMER: We will take it under advisement.

MR. BESHORE: I don't have any other questions.

MR. PALMER: Any other questions? You are done.

Mr. Brown, would you take the stand, sir. Once again, for the record, this is Mr. Brown. You are under oath. You can give your name in a moment, but also so the record is clear, you are back now for cross-examination, because the way we had to proceed at this hearing we weren't able to get to cross-examination after you gave your direct examination the other day.

State your full name and identification one more time.

MR. VETNE: My name is John Vetne, V-E-T-N-E. I'm counsel for Agri-Mark, Northwest Dairy Associates and other

M. Brown - Cross by Mr. Vetne

cooperative components to the make allowances changes.

MR. BROWN: I'm Michael Brown with Northwest Dairy Association.

MICHAEL L. BROWN

a witness herein, having been previously duly sworn, was examined and testified as follows:

CROSS-EXAMINATION

BY MR. VETNE:

Q. Mr. Brown, you have previously been sworn and previously presented prepared testimony that was posted in advance on the dairy programs website; correct?

A. That's correct.

Q. And in your testimony that you provided on Monday you commented on an error in the way Dr. Stephenson used your numbers and allocated costs of various products, and you have since listened to the testimony of Dr. Stephenson. Do you have any additional comments after hearing Dr. Stephenson's testimony on changes in the way Cornell now is allocating cost between products that are surveyed and other products?

A. Yes, I do. As I noted in my testimony on Monday, NDA observed the problems with Cornell's allocation of cost among NDA's products and information supplied for the cost survey conducted in 2006. Unfortunately, we did not know this until the spring of 2007 when we were finally provided Cornell's calculations of NDA's performance data from the survey.

After hearing the testimony of Dr. Stephenson, I would like to comment further on his observations. Proposal No. 2 urges the Secretary to use the most current information on plant cost to fix a make allowance. USDA relied upon the 2006 Cornell survey in its tentative final decision on last year's hearing without being aware of the errors Dr. Stephenson has now explained.

The corrections disclosed in this record confirm our belief that USDA in the last round should have not relied so heavily on the results reported in 2006, particularly for butter churning which Dr. Stephenson at this time testified he was not confident to reveal true cost. The record of this brings Cornell's results in line with the results of Dr. Lane and the California Department of Food and Agriculture cost surveys for butter and nonfat dry milk which our cooperative coalition urge USDA to weigh more heavily following last year's hearing. Numbers of dollars are being lost to cooperative associations with butter and powder operations due to USDA reliance on erroneous results reported from the 2006 Cornell survey.

Based on the evidence of this week's hearing, we would urge USDA to place Proposal No. 2 on fast track and issue an emergency decision or expedited recommended decision on this proposal only.

Q. Does that conclude the remaining portion of your direct testimony?

A. Yes.

MR. VETNE: The witness is available. Thank you.

MR. PALMER: Questions? Yes, please.

MS. REED: Kristine Reed of

the Yale Law Office.

CROSS-EXAMINATION

BY MS. REED:

Q. Mike, on page 2 of your testimony you indicate that your manufacturing plants have struggled at times with profitability. Did any of those plants actually fail to make a profit in your last fiscal year?

A. In our last fiscal year our ingredients division actually had a net loss of slightly over a million dollars. Our consumer products division made money which resulted in a profit for the year.

Q. How about in the current fiscal year? I think you're just starting the second quarter.

A. Actually, our first fiscal year is April. The first quarter of the fiscal year is looking much better. It is in the black at this point.

Q. How much whey cream does Darigold sell approximately annually?

A. I don't have the pounds, but the

M. Brown - Cross by Ms. Reed

majority of it is sold. We do use some internally in making some butter products. We use a slight amount of cheese when we can.

Q. How about sweet cream?

A. Huge. I don't have the number but it's huge.

Q. So the whey cream sales are much smaller; right?

A. Yes.

Q. And it's fair to say then that the whey cream overall is probably an extremely small percentage of the sales you have?

A. I wouldn't say that. Relative to the cheese plant, the cream we remove from the cheese plant is all whey cream. We have, as you know, we have four powder plants and one butter plant. So just by ratio it's going to be a lot smaller, but it's significant. As earlier stated, it's gotten tougher to sell.

Q. With the whey cream, as I understand it, there are really like three things that can happen to the whey cream, it can be put back in the vat as far as cheese manufacturing. It can be sold and those aren't exclusive necessarily,

M. Brown - Cross by Ms. Reed

I don't think, and it can end up in the waste stream from the cheese plant; right?

A. That is correct.

Q. With the whey cream that you choose to put back in the vat, is all of the whey cream that is a by-product initially put back into the cheese vat?

A. No, it is not. There are several factors to determine; number one, if a customer will accept the product, and if they won't, and we don't use it.

Second is availability of cream when we are looking at protein fat ratios in the vat. If we don't have other creams available -- keep in mind our butter plant is a demand plant. We do a lot of consumer butter, although the majority is bulk. That meaning that we have orders to fill. So we don't necessarily have excess cream particularly in the vat. So when necessity requires us to use it, we will use some. Considering the lower recovery of the fat of that whey cream, its value in the vat is also much lower than fresh cream as a result of that. It's not even

M. Brown - Cross by Ms. Reed

necessarily an economic decision to use it. It's a function of it's the only cream we can find.

Q. Of the whey cream that you do recover can you give me an idea of how much of it percentage-wise is put back in the cheese vat based on what your testimony was?

A. It's seasonal. In the fall it will be a fair amount. Through spring and summer it's none.

Q. When you do have a need to put the whey cream back into the cheese vat, can you run it through more than once, or is it -- do you ever do that, I guess?

A. No. If you don't want to -- if you don't want to lose a customer, you don't run it through more than once.

Q. That is because of the quality issues?

A. Yes. In our case a fair amount of our cheese is sold actually through shred, and it makes it soft and it's more difficult to shred. So you have to be careful.

Q. So I assume once it's been run

M. Brown - Cross by Ms. Reed

through, it's set aside until you sell it in bulk, I assume?

A. Yes; we sell it bulk, FOB the plant.

Q. About how often do those sales occur?

A. Weekly, actually.

Q. In Ms. Taylor's testimony she identified I think eight plants that purchase whey cream. Do you know of any others, or are you in agreement with her testimony?

A. I would agree with her. In fact, our regular customers are on her list.

Q. In your testimony you gave some detail about the volume of product that you sell in various plants that is off spec or otherwise doesn't meet NASS specifications. I believe your testimony was that it was close to four percent in your cheese manufacturing?

A. Yes.

Q. What is Darigold doing internally to minimize that four percent?

A. Our plant guy gets beat up when it gets to our line. I did go back and check several years. We run between three and five

M. Brown - Cross by Ms. Reed

and a half percent off-spec cheese in our Sunnyside Plant. We did an expansion last year. So we were relieved that we didn't increase our off-spec. We do a lot of things. Obviously, quality control is very key. In the last three years we have been implementing in all of our plants -- I'm trying to think what the term is. I'm not directly a plant guy, but basically those procedures there is a lot of checks, a lot of measures. We are taking more data, interim steps within the plant so we can earmark where the problems occur. So that is a big thing, but some of it is inevitable. For example, fines which is part of that cheese because it's fine. Our biggest problem with the cheese is the majority of our off-spec cheese is just not quite up to NASS specs. It's often sold for shredding. So it's a discount off the market. It's not huge but it's significant.

Q. Do you know how Darigold's numbers for percentage for off-spec cheese compares to other plants?

A. I think we are similar from my

M. Brown - Cross by Ms. Reed

experience.

Q. Is there any type of national average for those plants or any kind of published information that gives those percentages?

A. Not that I'm aware of. It's one of those things where your plant consultants, you benchmark.

Q. What is the total volume of cheese that comes out of your Sunnyside Plant?

A. It's roughly now currently it's running about four and a half million pounds a day. So it's going to be roughly about 450,000 pounds of cheese a day, and of that about 10 to 12 percent of that is Monterey Jack versus Cheddar Blocks.

Q. So we understand from your testimony that there are times that the prices that you receive are below NASS. Is there a time that Darigold has ever sold products that you received a price that was above the full NASS price?

A. Keep in mind when I talk about NASS, I talk about our reported NASS, and our

M. Brown - Cross by Ms. Reed

reported NASS on cheese is pretty much always below the national NASS. So actually no, because what you report to NASS is cheese that meets NASS specs, and it's basically all of our -- obviously, the amount of Jack isn't the cheddar, but all of the cheddar that we sold full price is reportable to NASS.

Q. Do you sell any specialty or added value cheeses?

A. Well, Monterey Jack is kind of, but it's really a commodity. You get a slight advantage for moisture, but it also slows down the plant as far as --

Q. And all of the Cheddars come out of each other?

A. Yes. It's all 40 pound blocks.

Q. I understand that the Sunnyside Plant is a newer plant. It was opened in 2006, according to your testimony?

A. Excuse me. 1996.

Q. What did I say?

A. 2006.

Q. There are newer plants.

A. Right, but it does have the

M. Brown - Cross by Ms. Reed

horizontal vats, the more efficient vats.

Q. Would you expect that some of the newer plants in the federal orders would have cheese yields that were even higher than your's?

A. Only if their components were higher. I think we are pretty much up to date on technology. Our updates last year which was about a $12 million project making some changes, but those yields that we report would reflect those changes.

Q. Likewise, the butterfat recovery?

A. Yes.

Q. Now, you testified that your cheese yield approximates about a 92 percent butterfat recovery?

A. Yes.

Q. And that you do use some whey cream. I assume that the 92 percent butterfat recovery that you testified about reflects that --

A. It's the average for the year. It's simply milk and cheese out.

Q. If you were able to put all of your whey cream back into the vat, if you did that,

M. Brown - Cross by Ms. Reed

would you expect your butterfat recovery to increase?

A. On a fat basis it would go down.

Q. Why is that?

A. Because your recovery of that fat -- again, that 92 percent recovery includes using some of that butterfat basically twice. You have to remember that, because when you take that whey cream -- if you reuse that in the vat, the seasonal times of year that we do that, it gives a second chance to become part of the cheese, per se, even though the recovery is lower. So, actually, if you didn't use that whey cream, our recovery would probably overall be slightly lower, because it gives a second chance. Keep in mind I'm talking real world yield here. Total pounds of components that weigh in and how much cheese you get out. We do two things; we ultrafilter milk to fortify the vat so we get more cheese per vat. It's an efficiency issue, and again, when we can, when it's available, we will use whole cream on occasion. So you're basically almost giving that cream a second chance to become cheese.

M. Brown - Cross by Ms. Reed

So an individual vat the whey cream yields are lower. Overall you slightly increase your recovery because they ran it through twice. It sounds kind of weird, but that's how it works, total math.

MS. REED: That's all I have.

MR. PALMER: When you say you fortify, what do you use to fortify?

THE WITNESS: Actually, the farmer milk comes in and we actually run it through ultrafilter concentration. We concentrate the protein before the milk hits the vat, because when you are making cheese in the vat, the recovery of protein, the higher percentage of protein in the milk, it's a greater amount that gets recovered in the cheese just because the milk is thicker. So we basically thicken the milk before we make the cheese, but it's all fresh raw milk.

MR. PALMER: Questions? Mr. Beshore.

M. Brown - Cross by Mr. Beshore

CROSS-EXAMINATION

BY MR. BESHORE:

Q. Good morning, Mike.

A. Good morning, Marvin.

Q. The sweet cream prices that you've reported on the third page of your testimony, it's 73, how were those derived?

A. As you might imagine, our marketing people weren't very excited about reporting actual price. So what they allowed me to do is report differences. So what we did is I took our reported sales. We have a reported sale and a reported multiple for all of our cream sales both whey and sweet and like with most people they are from Chicago, part of the market.

Q. So the multiple market is something like 125 percent of the butter market?

A. That's correct. What these numbers reflect is the difference between the multiple we get for sweet cream versus whey cream. So, for example, in 2005 if the multiple on sweet cream had been 125 and the multiple on whey cream may have been 104, I know those aren't

M. Brown - Cross by Mr. Beshore

the right numbers, but that is how it would work.

Q. So do you use much of your sweet cream in your own churn?

A. Yes, we do, but we also actually market a fair amount of cream. We do both. Partly since we have a single churn and we have two dryers in Idaho a lot of times it makes more sense to sell that cream, use it and move it back as the product for Cheddar, and we look at the profitability to determine whether to sell it or churn it internally.

Q. Do the prices for sweet cream or the multiples for sweet cream does that reflect what you charge yourself internally?

A. No. It's just our external sales. We try to keep it clean. As you might guess, internally we get lots of prices between divisions on what components we can sell internally. So we try not to use that for analysis.

Q. On the table on page 3, just to make sure I understand this, whey cream versus multiple versus sweet cream multiple, you say

M. Brown - Cross by Mr. Beshore

minus 2.186 would be assuming you had a 125 multiple on sweet cream and 104 on whey?

A. That's correct. It's the difference in the actual multiple.

Q. The next column translates that into dollars per pound, per cents per pound of what?

A. It's cents per pound of butterfat. So, for example --

Q. Based on an average --

A. These are actuals. Our average in 2005 the difference in the price we sold our products for was a $0.34 difference between pound per butter between sweet cream and whey cream. So, again, if we sold our sweet cream for $1.50 and we sold our whey cream for $1.50.

Q. So the third column is whey cream versus FMMO Class III butterfat you're saying is $0.15 per pound under the Federal Order price?

A. Yes. The third column is the difference between the Federal Order butterfat value and the calculated whey cream -- the sale price for whey cream butterfat.

Q. If you had a fourth column, that is

M. Brown - Cross by Mr. Beshore

Federal Order value versus sweet cream, what would that be?

A. It would be positive.

Q. For 2005?

A. Yes. It would be positive probably -- I would say it would be positive for all years intended. It would be slightly positive just in the cost of churning and selling off cream. We prefer not to sell cream. We generally make more money churning butter, based on your transportation of cheese.

Q. Are there any churns in Idaho?

A. Not currently. There is lots of rumors but currently no. There is a churn in Utah, but most of our cream that we sell fresh cream either, in fact, almost exclusively to the Midwest, and we sell fresh cream.

Q. Do you ever churn any whey cream?

A. We do. We have some customers that want commercial products. So we can use some whey cream in our churn, but it's limited. Again, it's a stop/start thing. It's kind of a hassle to do it.

Q. You have on the fifth page of your

M. Brown - Cross by Mr. Beshore

testimony you report that your estimated internal yield for whey is 5.58 pounds of whey per hundredweight, towards the bottom of that page. That is per hundredweight of milk?

A. Hundredweight of raw milk, yes.

Q. What is the average nonfat solids in a test?

A. I don't have that, but I can tell you market-wise it doesn't vary that much. It's going to be roughly around, it's roughly 87, 871 maybe.

Q. Roughly the assumed level --

A. It's slightly above the Federal Order level.

Q. The yield you say you are not proud of it?

A. No, we are not.

Q. Much less than USDA assumed 5.86. Isn't the assumed yield of 5.86 based on a hundred pounds of skim?

A. No; 5.86 is the yield used to determine the value of whey, and it weighs 108 pounds.

Q. Are you sure about that?

M. Brown - Cross by Mr. Beshore

A. No, I am not. I'm not sure. So I would defer to someone else's expertise on that. If that is the case, then five weeks would be overstated.

Q. That is based on the price for the Class III skim per hundredweight?

A. Yes. That would be correct.

Q. In which case 5.58 would be pretty close?

A. Slightly lower. I'm less embarrassed by it. Whey is funny. It's not in here, but I'll give this number. Our overall solids loss in our cheese plants is 2.1 percent. The challenge we have is determining exactly what that loss is, but we do lose significant solids and a lot of it is in the waste stream, but that is where a lot of that loss it. We know that is the case.

MR. BESHORE: Thank you, Mike.

MR. PALMER: Mr. Rosenbaum.

MR. ROSENBAUM: Stephen Rosenbaum, International Dairy Foods Association.

M. Brown - Cross by Mr. Rosenbaum

CROSS-EXAMINATION

BY MR. ROSENBAUM:

Q. Mr. Brown, if you could turn to that table that's on the third page of your testimony which is Exhibit 73, the one that is Darigold Whey Cream Value Comparisons. You have a lot of information there. I just want to make sure I understand it's clear. The third column is the one entitled whey cream versus FMMO Class III butterfat; correct?

A. That's correct.

Q. Am I right in understanding that what you've done in that column is compare how much you're actually being paid per pound of fat contained in the whey cream versus how much you're being required to pay as a minimum price for that fat under the Federal Milk Market Order minimum price scheme; correct?

A. That's correct.

Q. And you are being required to pay for that fat as if it had a value equal to Grade Double A butter price; correct?

A. That is correct.

Q. But you're selling -- in the real

M. Brown - Cross by Mr. Rosenbaum

world you are selling for a multiple return off of the Grade Double A butter price that returns to you materially less money than that Grade Double A butter price; correct?

A. To say it's not a profit center would be an understatement, yes. We lose money on our whey cream.

Q. You told us exactly what that is. That is to say in 2005 you actually earned on your sales of whey cream $0.15.6 less per pound of fat contained in that whey cream than you were required to pay for that fat as a minimum regulated price; correct?

A. That's correct.

Q. And similarly, in 2006 that number almost doubled to $0.29.16; correct?

A. Right. That is when the market got thinner for sales.

Q. Market for the sale of whey cream; correct?

A. Yes, a big difference between '05 and '06.

Q. And that on a three-year average basis you have lost 24.44 cents on your sales

M. Brown - Cross by Mr. Rosenbaum

of whey cream in the sense of comparing what you actually were able to garner from the marketplace for that whey cream versus what you were required to pay at the minimum price for the fat in that whey cream; correct?

A. On a pound per fat basis, that is correct.

Q. And you were paid for whey cream entirely on a pound of fat contained of whey cream; correct?

A. Yes. Most all cream is marketed that way and whey cream as well.

Q. So you are not garnering any additional funds between beyond what you are showing here with respect to the sale of whey cream; correct?

A. No. Selling whey cream is kind of like being the patron of lost cause. It's just the cost of doing business you have when you sell it. You do the best you can.

Q. You testified that you sell your whey cream on multiple off of the Grade Double A CME price. Can you tell us what that multiple was on average for 2005 to '06?

M. Brown - Cross by Mr. Rosenbaum

A. The whey cream multiple?

Q. Yes.

A. Yes. It was .944.

Q. And I take it that it obviously -- it must have deteriorated in 2007?

A. If you look at a three-year average, it's .892. It weakened more.

Q. You are aware that Ms. -- you've seen Ms. Taylor's testimony; correct?

A. Yes, I have.

Q. And you are aware that she calculated the losses on the sale of whey cream based upon the .944 figure you just provided; correct?

A. That's correct.

Q. If she had used instead the .892 figure which is the three-year average that picks up calendar year 2007, obviously, the losses she calculated would be increased; correct?

A. That's correct.

Q. The lower the multiple the higher the loss; correct?

A. Yes. Sad, but true, but that is

correct.

MR. ROSENBAUM: That's all I have, Your Honor.

MR. PALMER: You say you are losing money on this whey cream but you continue to make it. Why?

THE WITNESS: It's a byproduct of making cheese. You have no choice but to make it.

MR. PALMER: If you didn't sell it --

THE WITNESS: It would be worse. It's one of those products that it's revenue that helps, but it's, like I said, it's certainly not a profit center.

MR. PALMER: But I presume the profits made on the cheese offset the losses on the whey?

THE WITNESS: They help, but it's important to recognize that that cream has a lower value when you are evaluating that.

MR. PALMER: Overall you are not losing money?

THE WITNESS: Well, actually,

last year we did. The year before we did.

MR. PALMER: I shouldn't have said a little bit. You did lose some money?

THE WITNESS: Yes. It's a very, very tough business. We do better than average on the yields. We have a modern plant. We are in the west where prices for products tend to be lower, but we have producers that have milk that expect it to be processed. So even if you lose money, you have to process it. Our owners expect us to turn that milk into something.

MR. PALMER: Somewhere along the line there is a profit being made or you wouldn't be in business?

THE WITNESS: Yeah, usually. You don't want to look at our balance sheet. It has gotten better in the business of consumer products. It has improved in the last couple of years. The ingredient business, the commodity is a very, very low margin. When a producer is a member of a cooperative, we look at it as two things; it's a fair market for milk and a fair price, and they understand that in our market that because of our location, particularly because we are long ways away from most people consumer products in the Northwest that the value of products is going to be lower because transportation affects that value.

MR. PALMER: Questions? Anymore questions? Mr. Yale.

MR. YALE: Just two follow-up questions

CROSS-EXAMINATION

BY MR. YALE:

Q. in that last round with Steve Rosenbaum you talked about your whey price. Now, in your cross-examination and even in your direct you indicated that you use whey butter some times in the vat?

A. That's correct, when we can.

Q. When you can, and you don't use it a second time?

A. No, you can't.

Q. But that the whey cream that has been used in the vat is worth less than the whey cream that has not been used in the vat?

M. Brown - Cross by Mr. Yale

A. Yes, because the recovery is lower. That's again kind of that thing we sell the whey cream at a discount. If we have a customer that will accept it in a vat, we use it if we don't have any other source of cream because the recovery is low.

Q. But the question is, you have whey cream that came out. You don't put it back in the vat, and you sell it as whey cream. You have whey cream that you took out of the vat, you put it back in the vat and it comes out and you sell that. Does that garner a lower price than the whey cream that came straight out of the vat?

A. No. We don't segregate our twice-used cream versus once-used cream. What they are paying us they don't deserve that.

Q. Then you were talking about standardizing your vats. Do you know what your casein to fat ratio is normally with vats?

A. Again, it depends on the product, customer requests has been, but it's going to run between generally .64 to .68.

Q. It depends on how much fat they

want?

A. Yes. It depends on what they want for an FDV.

Q. And the lower the casein the more fat; is that right?

A. That is correct.

Q. And then the final question is this: You indicated, and just again the answer you gave, that there is an economic decision that is being made to determine whether you are going to use whey cream or fresh cream or whether you are going to churn the cream and sell the cream; right?

A. Right.

Q. Isn't that fundamentally why we have one butterfat price for three and four is because the butterfat can move between the classes and does move between classes; right?

A. Yes. That's correct.

Q. So when you have a hundred pounds of butterfat arrive at the door of the cheese plant, you have the choice to put all of that butterfat into the vat and then bring your protein up so that you reach your casein to fat

M. Brown - Cross by Mr. Yale

ratio, or if the economics dictate, sell some of that cream because you can get more for the cream than you can from making cheese; right?

A. Yes. And those decisions will -- again, a lot depends on what your sale demand is, but, yes, when we can, we have flexibility, we will move milk between our powder and cheese plants and even proponents, depending on where the best returns are.

Q. So if the policy of the department is that the class or that the butterfat prices are to be relatively consistent between the classes, then the decision made by the user of that butterfat, whether they are going to make as much or not, is up to the user and let the market dictate how that works rather than having the producers take a discount on some uses of butterfat as opposed to others. Isn't that really the policy question that is being asked here?

A. No. I think the policy question that is being asked is what your return from your stream of products in a cheese plant, and you have to recognize the return from that whey

M. Brown - Cross by Mr. Yale

cream which is a byproduct of cheese that's going to be there no matter what you do with it. It has a lower value whether it's because the fat recovery in the vat, whether because it has a lower multiple when you sell it. If you churn it, your product has an inferior price. So the way that, as you know, the department has adjusted for the value of butterfat and cheese, added value of fat and cheese because of protein, is the -- protein value. Having that 3 1/2, roughly 10 percent of the butterfat that is assumed to go to whey valued at a whey value is part of that protein formula. It more accurately reflects the total value of the products in the milk, because there is always going to be some of that butterfat. You can't recover the full whey Double A fat value for whey cream and butter.

Q. But in your case it's not 10 percent; it's 8 percent?

A. It's roughly 8 percent. Keep in mind we are not average. We, fortunately, do a little better.

Q. But your protein is reduced as if it

M. Brown - Cross by Mr. Yale

was 10 percent. Your butterfat price effectively reduced your protein price?

A. That's correct.

Q. So there is compensation in the formula somewhere else?

A. Yes, but it's not full. Frankly, it's not full.

Q. At the end of the day you indicate that you are profitable?

A. Right now. A lot of that has to do with the market. As I think we all know, when the CME is moving up, it's easy to make money because of the NASS lag. The first quarter we have been blessed with the CME moving up. So it's helped up in the cheese plant, and we do dry whey which has helped us.

Q. You have a simple solution.

A. When you convert a artifact to a cheese plant you already had a dryer, you're blessed to have done that.

MR. YALE: I have no other questions.

MR. PALMER: Mr. Beshore.

M. Brown - Cross by Mr. Yale

M. Brown - Cross by Mr. Beshore

CROSS-EXAMINATION

BY MR. BESHORE:

Q. Mike, a couple of questions that I asked Bob Yonkers that I want to ask you also.

A. Sure.

Q. Do you have a position with respect to how Dr. Stephenson's current information should be used on the cheese pricing that, as he indicated, are basically two options; take the four digit average of the current, what's it, 11 plants or use the change in cost 1.7 cent change in cost for a smaller sample of different plants?

A. If you want apples to apples, the seven plant changes is going to better reflect that change in the cost, because the average size of the plant is going to be so drastic between the old and the new survey. So we would encourage the department to look at the 1.7.

Q. And with respect to what base?

A. Well, the base of the previous survey. The Department -- and again, I don't know where this -- the Department so far has

M. Brown - Cross by Mr. Beshore

not looked at size adjusting based on the population of plants. What that make, and I think everyone will acknowledge that larger units that process most anything are more efficient, and I think that is a mistake. California basically samples every plant that they have. So their sample is the population. In the case of USDA it's not a statistical adjustment of that population. Based on the actual average size just seems logical to me. Otherwise, if you over sample any of the higher plants relative to the current use of the total supply, you could affect the price. You could hurt a lot of people or may be help too many people, depending on how you do it.

Q. Based on the economist's scale or error in cheese making less anything, as you indicated, you would expect that the cost change in larger plants to be less than 1.7 cents per pound; would you not?

A. If plants get larger, the cost should go down. I will testify to this. Our plant got larger and our purported cost to merc went down slightly. We increased our

M. Brown - Cross by Mr. Beshore

production about 10 percent, not big but slightly.

Q. Now, are you, and I'll say either Northwestern Dairy or other groups of which you are a part here supporting the Leprino or IDFA proposal with respect to whey cream pricing, the reduction in the protein price for the ostensible value of whey cream?

A. I'm not sure I can speak for the group, but I believe the group supports it. We certainly support it.

Q. And your position is to eliminate the three cent barrel adjustment?

A. Yes. Our experience has been since the 2000 hearing and the final decision that came out in '03 from that decision that they are double counting when you went to the 38 percent moisture versus 39, and have the Class III. They are double counting that difference and you needed either to get rid of one or the other, because it definitely -- part of that Class III was, in fact, a moisture adjustment was in the trade. When they adjusted the 38, they kind of double counted.

M. Brown - Cross by Mr. Beshore

Q. You don't make any barrels, do you?

A. No. We are a hundred percent blocks, a hundred percent forty, actually.

Q. Have you done any calculations -- do you have any information on aggregate change in the Class III products production, Class III price that would come about by adoption of all of the positions that you've indicated you support?

A. No. We have not done those calculations. Our calculations, when we look at calculations, it's, basically, within plant. Again, 80 percent of our milk is run through plants that are members owned, and so those plants seem to be profitable for our members and they're successful.

Q. I'm talking about proposals in the hearing. You have not done classification?

A. No, I haven't. There has been a lot of work done on those numbers. I certainly looked at them with interest, but I didn't repeat anybody's work. I have not looked at that.

Q. Do you know if anyone in your group

M. Brown - Cross by Mr. Beshore

has attempted to calculate the impact on the, the aggregate impact on the Class III price for all producers of the group of proposals that you're supporting?

A. No, certainly not recently. Well, we did it after the end of last year's hearing. Because within our organization we have kind of two companies. We have the co-op and we have the processing division. The cooperative is given a fair amount of room to work on pricing, and we try not to have the plants dictate what we do, but at the same time the co-op owns the plant. So we need to look at our plant profitable and we have struggled. So we do believe there is room for increasing make allowances, yet the increase like the Department has done we think that the job is not finished. We think that there is more things to be looked at.

Q. Would you be willing to check your computer to get the answer to that prior question that I asked that you weren't sure about? That is whether the 5.86 --

A. Absolutely.

M. Brown - Cross by Mr. Wellington

Q. In case we have a break can you provide the answer?

A. Unless you have no questions for Sue. I should have a couple of minutes to look it up.

MR. BESHORE: I don't have any other questions right now.

MR. PALMER: Anything else?

CROSS-EXAMINATION

BY MR. WELLINGTON:

Q. Bob Wellington from Agri-Mark. Good morning, Mike?

A. Good morning.

Q. Just a few questions. How much money do your members have invested in equity in your operations in your cooperative?

A. Versus how much the bank has invested?

Q. No. How much in total?

A. Let me do the quick math in my head. It's approaching half a billion.

Q. So even if you make a profit, you could make a profit, but the return to your

M. Brown - Cross by Mr. Wellington

members on that as a percentage basis could be one or two percent, a very small amount?

A. Right.

Q. So it's not a profit as if that is pure profit beyond. That is a profit as a return for the investment that's been made; correct?

A. That is absolutely correct.

Q. So you need a significant amount of profit if you are going to have a reasonable return on that investment?

A. And if you are going to keep the plants moderately competitive, you have to. You have to have dollars at some point to reinvest to keep your -- replace depreciated items, if nothing else. At some point you have to make some money just to keep your plants working, and that's where we suffered. We let our plants go, and now we are borrowing money to get them up to date because we have to.

Q. During a 12-month period, what percent of your whey cream goes into the vat, and what percentage is sold as whey cream or into whey butter?

M. Brown - Cross by Mr. Wellington

A. I don't know exactly that number, but it would be less than half. That I'm sure of just because of the months involved. It's generally in the fall we do it.

Q. And the fact that you can't put it in twice?

A. No, not unless you want to make something nobody wants.

Q. Just in itself, if you use it all in the whey vat a hundred percent, you would still be at 50 percent changing it twice, and then you don't use it seasonal. So it should be significantly under 50 percent?

A. Yes, it would be. Certainly it ends up in cheese. It definitely would be under 50 percent.

Q. Can your plant make both whey powder and whey protein concentrate?

A. Yes. We made the decision several years ago to invest in WPC equipment.

Q. During the past year and currently, which product are you making?

A. Well, let me just put it this way. It's like buying a new car and parking it in the garage. Part of our upgrade is Sunnyside last year was UF equipment so you could dry WPC. We turned it on and made sure it worked and turned it back off.

Q. Why is that?

A. Because margin is so much better than whey. We would have lost money, significant money. In fact, last year, this is a rough back of envelope calculation, but given the WPC and then liquid permeate market which is what we were going to do with the WPC, it would have been close to a $10 million hit.

Q. Is it typical for most plants that you are aware of to have the capacity to do both products?

A. No. The fact that we started out as a powder plant compared to a cheese plant we happen to have a big dryer, and that's really the only reason we can do that. The WPC was put in as a capacity issue. We have an outside vender that we buy whey from, whey concentrate from, and they were expanding their plant, and our dryer couldn't have dried all of that product of whey. So we put it with WPC for

M. Brown - Cross by Mr. Wellington

capacity reasons. And that plant expansion has been delayed, but the equipment is there. We would have the luxury if WPC was a stronger market to make WPC but it's not. It's significantly worse. So we are rare. Most plants don't have the infrastructure to dry whey. Cheese plants simply don't have it. Because the move to WPC was made over the last 15 years, a lot of the times it's been a more profitable product. What we are seeing right now is because we selected one product for pricing, we got kind of winners and losers situations based on the investment decision that made perfect sense even three years. It's hanging people by their thumbs right now.

Q. So would you agree that most cheese plants right now if they can process whey, they process it into WPC?

A. If they can process whey, make whey.

Q. I'm just saying if they have a way to process the whey solid at their plants.

A. Most plants have WPC capacity, not whey capacity because of dryer size and design. Most plants have no choice but to make WPC.

M. Brown - Cross by Mr. Vetne

They can't make whey. They simply can't do it.

MR. WELLINGTON: Okay. Thank you.

MR. PALMER: Any other questions? Mr. Vetne.

CROSS-EXAMINATION

BY MR. VETNE:

Q. Mike, you referred early on to your practice of ultrafiltering incoming milk so you have a concentrated component product to put into the vat. The concentrated product that is called a retentate?

A. That's correct.

Q. And whatever goes on the other side of the filter mostly water is the permeate?

A. That's correct.

Q. Does the permeate goes into the waste stream, or what do you do with it?

A. The permeate can go several places. To some degree it can go and depending on what the customer want you can dry permeate. We also make skim milk powder in some of our plants because of world demands. So that

M. Brown - Cross by Mr. Schaefer

permeate is used to standardize protein in skim milk to make skim milk powder. That is a very common practice. We're certainly not alone in doing that.

Q. It doesn't go down the drain?

A. No. We do recover some value in it.

MR. VETNE. Okay. Thank you.

MR. PALMER: Other questions?

CROSS-EXAMINATION

BY MR. SCHAEFER:

Q. Good morning, Mike.

A. Good morning, Henry.

Q. I think I just have one question here. On the next to the last page of your statement you talk about your NFDM production, 54 percent of the total product volume represented in the survey. What survey are you specifically referring to?

A. That was the 2006 Cornell cost survey that was presented last fall. We had four plants in that survey. We looked at a total volume and we looked at our volume, and we were 54 percent in that volume survey.

M. Brown - Cross by Mr. Beshore

MR. SCHAEFER: I think that's all I have. Thank you.

MR. PALMER: Let's do this. I think you want to get some figures together to give to Mr. Beshore. Why don't we recess now till 25 of 11:00, a twenty recess. Do the figures, come back, give that and then we will hear from Ms. Taylor.

(Short recess taken.)

MR. PALMER: Back on the record.

Did you find that information that Mr. Beshore was interested in?

MR. BROWN: Yes.

MR. PALMER: Mr. Beshore, do you want to approach, please.

CROSS-EXAMINATION

BY MR. BESHORE:

Q. You searched your computer?

A. Yes. I'll walk through the calculation. Under the Federal Order calculations they assumed it's 5.69 pounds of solids, other solids, and 100 pounds of milk,

M. Brown - Cross by Mr. Rosenbaum

and they assumed it's 5.9 pounds of solids, other solids and 100 pounds of skim. The 5.8 number is simply from the whey yield formula they assumed that weighed at 3 percent moisture. If you take 5.69 divided by 97 percent dry matter, you come up with 5.86 pounds of whey.

Q. And that is in 3.5 milk?

A. That is standard test milk, yes.

MR. BESHORE: Thank you.

MR. PALMER: You have a question, Mr. Rosenbaum?

CROSS-EXAMINATION

BY MR. ROSENBAUM:

Q. Maybe this is obvious, but having done that calculation, does that mean that your written testimony was correct?

A. That is correct.

MR. PALMER: Anyone else?

CROSS-EXAMINATION

BY MR. SCHAEFER:

Q. When you talk about your sales of

M. Brown - Cross by Mr. Schaefer

whey cream, is there any marketplace that you deal with in kind of an open market that develop a whey cream price to develop that multiplier, or is this strictly a negotiation between you and a specific purchaser?

A. Since we are down to one purchaser, it's not a whole lot of marketing. For us it's a function of how bad a plant wants it and the transportation cost to move the cream. So our cream tends to stay further west. A lot of times it goes into Utah, because that is the closest churn that wants it. Again, there is not a lot of buyers. So there is not a lot of negotiations. We used to have two, and now we have one, and you know what that does.

Q. Does your whey cream price, using a multiplier, so it does go up and down with the CME Double A market?

A. Yes. The prices of the cream goes up and down. The multiplier varies less than the sweet cream multiplier. It has less variability month to month on the national multiple on whey cream versus sweet cream, although it does vary.

M. Brown - Cross by Mr. Schaefer

Q. Have you contacted a multiplier?

A. I don't know. Looking if it's like most of our products, we probably have a baseline guaranteed delivery at a fixed multiple, and then when we have more cream than that, we'll get a spot and they can be higher or lower, depending on demand, and that is true with sweet cream too.

MR. SCHAEFER: Thank you, Mike.

MR. PALMER: Anything else? Anything at all?

THE WITNESS: Can I make one more point of clarification?

MR. PALMER: Sure.

MR. BROWN: I want to make a point based on some of the questions. I hope I didn't confuse people, but talking about fat recovery and why when we use whey cream twice, our recovery actually -- we use whey cream again and the data recovery improves. The numbers I gave for components, I believe it was 5.6 something on butterfat, that is all milk and cream coming into the plant. That's

M. Brown - Cross by Mr. Beshore

everything that comes in. This is an in and out exercise. It's not a vat exercise. We bought this much milk. These were the components last year. These were the products that came out. So it's essentially farm weights and tests. So when you do use whey cream twice, when you use it a second time in the vat after you took the cream off, even though the recovery on that cream itself is lower, it actually increases your overall recovery of cream because you basically gave it a second shot at becoming a part of cheese. So if we didn't do that, our fat recovery would actually be slightly lower than the 92 percent than it is.

MR. PALMER: Yes, Mr. Beshore.

CROSS-EXAMINATION

BY MR. BESHORE:

Q. Since your information, Mike, as you just indicated, is based on everything coming into the vat, you indicated you ultrafilter milk prior to the vat. What portion of the milk is ultrafiltered?

M. Brown - Cross by Mr. Beshore

A. About 20 percent, but it's internal. It's ultrafiltered when inside the plant. What we simply do is try to get more pounds of solids in the vat so we get more pounds of cheese out of the vat. Actually, our vat protein is close to 4 percent, but we basically take that 3.2 milk and US hold it to get it up that high.

Q. Now, the permeate, and you testified previously, the permeate from the UF process that goes to the drying plants?

A. Yes. It either can be dried as permeate depending on your customer. It can be mixed with whey or it can become part of skim milk powder.

Q. If you are looking at the total yield for milk coming in the door at the cheese plant, you need to add that permeate back in to the total yield picture, do you not?

A. You would.

Q. Twenty percent of your milk is ultrafiltered by how much permeate do you get?

A. That is about 20 percent. So it would be 800,000 pounds a day, roughly 8 to 9.

M. Brown - Cross by Mr. Beshore

You are getting out of my league on that, UF math. That is all too new.

Q. Whatever it is, that if you were comparing this whey yield 5.58, you ought to have that permeate in there, shouldn't you?

A. That could affect it, yes.

Q. It would affect it in terms of the total --

A. Yes, it would. Keep in mind not all of that permeate leaves the plant and goes elsewhere. Some of it does get dried and that would be part of that number and it gets added back in.

Q. Right, but whatever it is the permeate from 20 percent of the milk needs to be part of the total equation in terms of what that farm milk generates in total products at your cheese plants?

A. That's true, no matter whether it's in whey or any other products. That would be correct.

Q. When it goes into skim milk powder -- by the way, how is that classified?

A. Skim milk powder?

M. Brown - Cross by Mr. Beshore

Q. No. The permeate.

A. It's Class III milk.

Q. So the Class III, the pounds of Class III that goes to powder, and presently that works out pretty well, I guess?

A. Yes, but most of the time it doesn't.

Q. Other times it's more equivalent -- it's Class III and the return on it is more equivalent to the return on -- well, it's better than the return on dry whey, right, most of the time?

A. Not necessarily.

Q. Well, powder is higher than dry whey most of the time; right?

A. You have to remember every powder vat that we move it moves at a minimum of 180 miles to get to a dryer.

Q. What's the percentage of moisture in the permeate?

A. Someone else here probably knows better than me. It's going to be 70 percent.

Q. But you've got a bunch of the waters out of it?

M. Brown - Cross by Mr. Beshore

A. Some of it. Seventy percent is still a lot of water. Again, processing S and P is more expensive than processing powder, and the price of means is a different product, and we make it because it's a demand for it. It's a customer's demand.

Q. And it's been a pretty good market?

A. Yes. It got us in the world market because the world market likes S and P.

Q. And it's a better return than whey?

A. It's a better return than throwing it out. I'm not sure it's a better return. Again, it depends on the market. Most of the time, yes. When you have $0.70 whey, it isn't quite as obvious. When you have $0.70 whey and $2, yes. There is a greater return. There is cost. Every time you make something that is nonstandard your cost goes up.

Q. And the price goes up as well?

A. Yes, it's better. You're crazy to make it.

MR. BESHORE: Thank you.

MR. PALMER: Thank you, Mr. Brown. Ms. Taylor.

S. Taylor - Cross by Mr. Beshore

Ms. Taylor's statement was Exhibit 69. You are still under oath. Give your name again just so the reporter can have it. That's right. It's cross. Let's get your full name and identification one more time.

MS. TAYLOR: I'm Sue Taylor with Leprino Foods, L-E-P-R-I-N-O, Company.

MR. PALMER: And you've already given your direct testimony, as I said. It's embodied in this statement as well, and we are now going to take cross-examination. Who has questions? Mr. Beshore.

SUE M. TAYLOR

a witness herein, having been previously duly sworn, was examined and testified as follows:

CROSS EXAMINATION

BY MR. BESHORE:

Q. Good morning, Sue. Let me ask a couple of questions, background, in terms of your testimony. Is it present on behalf of Leprino, I assume?

A. Yes, it is.

Q. And on behalf of IDFA?

S. Taylor - Cross by Mr. Beshore

A. I state my support for many of the proposals of IDFA. I'm not speaking on behalf of IDFA in this testimony.

Q. Only on behalf of Leprino?

A. Yes.

Q. Now, Leprino makes no cheddar cheese; correct?

A. At this point we do not.

Q. Nevertheless for the six of the nine plants that are associated with the Federal Order System in terms of the source of milk, the price of protein or Class III milk for your Italian cheeses is being determined in part for this proceeding; correct?

A. That's correct.

Q. Now, what's the average fat content of your Italian cheeses produced by Leprino?

A. I don't know. It would be lower fat than cheddar.

Q. And lower than the producer of milk you receive?

A. Yes, it would be.

Q. Is it roughly -- can you give us any idea. Is it one percent? Do you standardize

S. Taylor - Cross by Mr. Beshore

milk to a fat content going into the milk fat?

A. Yes, we do. I don't know our precise fat levels. My recollection is that mozzarella at large typically if any on order is part skim or whole milk product would be somewhere in the 2.2 to 2.5 range.

Q. So you're not using all of the butterfat -- do you use all of the butterfat that you get in farm milk in your cheeses?

A. We do not.

Q. What do you do with the butterfat that you do not use in cheese production?

A. We sell it.

Q. For what uses?

A. It goes to a variety of cream users.

Q. Mostly Class II?

A. Class II, III and IV.

Q. Now, that butterfat which is skimmed from farm milk and sold for those other uses is classified at those uses, and it's not an issue with respect to the Class III pricing formula; isn't that correct?

A. That fat will be re-priced at the ultimate end use. So that fat does not get

S. Taylor - Cross by Mr. Beshore

raised under the federal order as Class III.

Q. So it's not being addressed at all with respect to your testimony about the Class III formula?

A. The fat price is connected between those classes. The skim portion of that cream would be priced differently. There is a connection on the fat component.

Q. Because fat is priced at essentially the same price in all classes in the system?

A. Essentially, yes.

Q. So the milk going into the Italian cheese vat is perhaps 2 percent butterfat rather than 3.6 or 3.7 farm milk, something like that; is that fair?

A. Yes.

Q. How much whey do you generate that from Italian cheese production?

A. I don't know the precise yields. My understanding is they are comparable to cheddar yields.

Q. I asked the wrong question. I meant how much whey cream do you generate in Italian cheese production? Since there is less

S. Taylor - Cross by Mr. Beshore

butterfat per hundredweight going in, your production of whey cream would be less than a full fat cheddar process?

A. There are two factors; the fat going into the vat, you are correct, is at a lower level than if you were producing a full fat product. However, the fat capture rates on mozzarella are far lower than on cheddar. They are generally considered to be around 85 percent.

Q. Is that Leprino's experience?

A. Yes. Our fat captures are closer to industry norms. Obviously, that mean you have 15 percent of a vat fat that comes back out in the form of whey cream.

Q. What's the average moisture content of the mozzarella you produce?

A. Again, there is a very wide variety in terms of moisture level depending on the market that you are going into and the final application. I would guess that nationally it's probably in that 46 to 48 percent range.

Q. So what you have is more milk in the cheese then pounds of yields yielded in hundred

S. Taylor - Cross by Mr. Beshore

per weight and mozzarella production or higher than cheddar production; correct?

A. Yes, they are.

Q. We can estimate, if we can use the 46 to 48 percent versus 3 and 37 percent in cheddar?

A. In combination with the lower fat capture. There is a specific mozzarella theoretical yield formulas out and available from the epidemic sector.

Q. What does it generate from 35 milk fat, how much pounds of cheese?

A. My recollection when I have run the industry, the more generic formula it's somewhere in the neighborhood of 10.5.

Q. Is Leprino's mozzarella cheese generally sold off the cheddar cheese price benchmarks?

A. Yes, it is.

Q. Let's talk about whey cream volumes. It's just curiosity to some who are distant from the industry, not involved in hands-on day to day such as you. With what would appear to be a very large volume just of whey cream

S. Taylor - Cross by Mr. Beshore

generated by the cheese making process in the United States there is no data series published by anyone on whey cream volume ups price or anything else. Are there any -- I mean no one has testified about any. Are there any that haven't been testified about?

A. There are none that I'm aware of. There are several issues that I think have been arrived at. One is there is very little demand, very few users who desire whey cream. The one piece of data that I'm aware of that has not been entered into the record is dairy.com does from time to time trade whey cream. I sought out information and over a period of several years my recollection, this is several months ago, I looked for it, but my recollection is there were somewhere less than 25 loads over a multi year period, and the multipliers were at a severe discount to even the multipliers that have been presented at this hearing, and we did not present them because we expect time to perceive them as a divested sale, it sounds like they were. They're divested sales or they may be

S. Taylor - Cross by Mr. Beshore

reflective of the marketplace at the particular times that they actually went through that market.

Q. In your knowledge of the industry are there no users of whey cream in California, other than the plant themselves, to the extent that they use it in their cheese production?

A. I was not able to identify a buyer of whey cream in California, a bulk of whey cream, and I did ask California cheese makers. They told me that they send them to the Utah plant, the higher Utah Plant.

Q. Is that what Leprino does with its whey cream in California?

A. No.

Q. Do you use it for other -- do you send it further than Hyrum, Utah?

A. No. We do it in our mozzarella production.

Q. After reuse what portion of your butterfat are you able to utilize in the mozzarella? Eighty-five percent first time through, you said, but you can reuse it. How much do you ultimately use, what percentage?

S. Taylor - Cross by Mr. Beshore

A. We do not sell any whey cream. So ultimately all of our fat, all of our whey fat is reincorporated into the cheese. Our excess fat is sold sweet cream.

Q. So for Italian cheese makers which represent, what, about 40 percent of the cheese volume in the Federal Order System?

A. I would narrow it to mozzarella, and it's probably a little over a third of the cheese produced in the U.S. I don't know precisely within the Federal Order System what it represents.

Q. Assuming the Federal Order System is approximate usage which is equivalent to national usage, you've got about a third of Class III milk that's in mozzarella production; correct?

A. Based on that assumption, yes.

Q. And if the USDA were persuaded to adopt the proposals that you've put forward with respect to protein value based on whey cream values, the protein price based on whey cream values, that would be helpful to the bottom line of Italian cheese production where

S. Taylor - Cross by Mr. Beshore

all of your cream goes into cheese; would it not?

A. It would be helpful to the bottom line of any Class III users.

Q. But in mozzarella production you don't have the problem of de-valued whey cream, the cheddar?

A. I would not make that statement broadly. Leprino Foods has invested a great deal of money over the years in research and development in quality systems to the point where we feel we can manage the bacteriophage issues that some other folks have not been able to manage. I believe that there was testimony by Great Lakes Cheese at this hearing that, for example, at their Cuban, New York mozzarella plant they had a fryer lower multiplier that even out of their Adams plant because it's a mozzarella plant because of the contact with water in the wash process, they cannot sell that as kosher cream. So it's not eligible for any of the northeast markets, and they end up shipping it to Nebraska. I think that that is a relatively common scenario for many mozzarella makers.

Q. But for Leprino you can get cheese value out of all of it?

A. Yes, we do.

Q. Let me ask a question or two about the in-plant losses. Again, not running the plant, I don't have the kind of day-to-day knowledge that might be implied in these processes, but I was curious just thinking about your testimony on page 3 with your statement which in the middle paragraph says, "During start-up and shutdown, milk components that are diluted with water (milk pushing water at start-up and water pushing milk at shutdown) are lost, generally to the floor drain where they are disposed of as waste." Do you see where I'm referring to?

A. Yes.

Q. Now, I understand the clean-out process, I think intuitively. That is when you are done with a cheese making process, you wash the lines out, and whatever solids are sticking in there you flush down the drain. I understand that. But what I don't understand

S. Taylor - Cross by Mr. Beshore

is how you have losses at start-up. When you start up, do you run milk through and down the drain before you start up?

A. Yes. There is water that resides in the line after the CIP cycle, and that water in parts of the system, some parts you can drain, some parts you cannot drain. It has to be pushed by another substance from the back to get through those ups and downs of the loop systems, and so in my discussions both with the Leprino folks and with Dean Sommer, Dean's comment was that that's adulterated milk that everybody tends to put to the waste stream. My interpretation of the conversation was legally that is what's expected under the regs.

Q. That if you got a point where there is water, you've got to, are you saying you flush that out with milk?

A. Yes. If you flushed it with another substance, you would still have a problem where once you started putting the milk through, there would be an adulterated volume. So regardless, you can't get it through some parts of those systems without sacrificing some --

S. Taylor - Cross by Mr. Beshore

Q. Some parts of the system?

A. Correct, and the pasteurizers is one of those specific parts of the system.

Q. When you have cheese yields, and you talk about cheese yields, and let's just talk about mozzarella, let's say just for purposes of discussion that a mozzarella manufacturer can experience a yield of 10.5 pounds, that is pounds of actual product at the end of the production process; correct?

A. Yes.

Q. When you say it's a yield of 10.5, typically you would be -- what you mean is that 100 pounds of milk going into the vat -- before it goes into the vat, you have 100 pounds of milk. At the end of the total process you have 10.5 pounds of fat. That is what we talk about when we talk about yield; right?

A. Yes.

Q. Now, my question is, doesn't that yield incorporate de facto all of the in-plant losses?

A. It would be based on, as you said, the finished product versus the product in the

S. Taylor - Cross by Mr. Beshore

vat. Not all of the milk reaches the vat.

Q. But yields are based on milk going into the vat; correct? I'm not talking about farm to plant. Factor that out of it completely. You've got milk to go into the vat. You've got 100 pounds of milk to go into the vat. So when we talk about yields, we talk about the pounds of product that come out the other end after that 100 pounds of milk was presented to be put in the vat; correct?

A. That would be correct, but before that milk gets into the vat, there are losses in a receiving room in the separation pasteurization process.

Q. So it's your testimony that, for instance, the VanSlyke formula --

MR. PALMER: I get a little confused too. When you take your measurement of how much milk came into the plant before the process starts, do you take it on the basis of when it's picked up to farm or what arrived at the door or what you have after some of the initial process? Where do you get your first number from? Where do you start?

S. Taylor - Cross by Mr. Beshore

THE WITNESS: We have the measurement at the farm which is what we were paid for based on the Federal Order regulations. We also measure the milk at the plant, and so we do have a farm-to-plant loss. Then we also I think at most plants do have metering systems. I know we have the metering systems throughout our plant processes.

MR. PALMER: When you are figuring out what comes out the plant door, what do you compare it with? What's the start-up point that you use? What's the first number that you use to see what you started with?

THE WITNESS: The theoretical yield equations which I used on the 10.5, that assumes the milk in the vat. What Leprino does, I believe, in terms of our own Y and E system is we are looking at the milk as measured on the in-bound side, in other words, our scales in our test, and we are then tracking how much cream was separated, and assuming that the volume was not separated, went into the vat. I believe that is our own production of accounting system.

BY MR. BESHORE:

Q. And so separate, you assume the volume is not separated. It goes into the vat, and then you have a yield?

A. Yes.

Q. That being the case, and I think that probably tracks except for the separation process, most of the cheese makers in this hearing have testified that they base their yields on either farm pounds, many of them, or plant received pounds, base their yields on that. Assuming you base it on plant received pounds, then you have a yield, my question is, does that yield, that actual yield, not theoretical, that actual yield factor in all of the losses in between?

A. Well, it depends on what you are considering as your finished product, whether you are considering also --

Q. I'm not talking about whether the product meets any specs finished product. I'm talking about finished product yield. I mean pounds out the back.

S. Taylor - Cross by Mr. Beshore

A. Yes. That would factor in the losses.

Q. What is the impact on the Class III price, I think this is in your statement, I couldn't find it, of the proposed changes in the evaluation of butterfat related to whey cream?

A. 16.9 cents.

Q. And that is where --

A. It is at the top of page 17.

Q. And that 16.9 cents is generated by effecting the changes to the protein formula on page 16; correct?

A. That would be correct.

Q. The proposed changes that you advocate are represented by the .922 number times the effective component price part of the equation; correct?

A. Yes.

Q. You would increase that from what is presently, what, .9?

A. Correct.

Q. .922?

A. Correct.

S. Taylor - Cross by Mr. Beshore

Q. Then the addition of the minus $0.1.6 factor; correct?

A. Correct.

Q. Now, in reaching those, in adding those factors, you've done basically two things, as I understand it; factored in a lower value for the butterfat and whey cream?

A. Correct.

Q. And factored in a reduced yield of dry whey?

A. No. The .922 reduces the yield of whey cream. It's assumed.

Q. Factored in a reduced amount of whey cream?

A. That's correct.

Q. Now, your reductions in the whey, in the volume, volume whey cream, that's not based upon any actual plant yield studies, is it?

A. That's correct.

Q. It's based upon the theoretical sort of yield table that you have on page 14 of your testimony?

A. Correct.

Q. There are two elements in the table

S. Taylor - Cross by Mr. Beshore

on page 14, there are two elements to reducing the assumed yield of whey cream. The first is the amount of butterfat believed to be in the dry whey?

A. Correct.

Q. Now, the first question about that is, that butterfat is presently priced, in essence, -- what's the price of that at present? Is it in the whey?

A. It currently is valued at the Double A butter value. It's part of the 10 percent that is left at the fat component price.

Q. But it's a portion of the pounds of dry whey which are valued at the other solids price; correct?

A. That's correct. That's not how it's assumed in the Class III formula, but in practical reality it is part of the dry whey as a finished product.

Q. The other element of reduction in yield whey cream is what you calculate to be the portion of the butterfat in whey that is just disposed of, period, not part of dry whey or whey cream which is basically poured out of

S. Taylor - Cross by Mr. Beshore

the field or dumped down the drain; correct?

A. It would be the solid whey which in the cheddaring process, as you recall from Dean Sommer's description, in the salting process there is a further way that is expulsed from the curd that has such a high solidity content that it is not recoverable generally into a marketable stream.

The fat that I'm representing here is not all of the fat in the solid whey. What many cheddar makers do is they will collect that solid whey throughout the processing day, and at the very end of the run they will put it through a separator and try to recover the fat portion. The salt generally stays with the other solids piece, and it is that piece you can't recover a commercial value and there is a little bit of fat in that piece. So the fat that I'm talking about losing on salt whey piece is as you noticed is a very small portion. It's only 4 percent. If you look at my two additions, the dry whey and salt whey, it's only 4 percent of that change that I'm proposing. It's .0029 pounds.

S. Taylor - Cross by Mr. Beshore

Q. Have you compared your theoretical yield whey cream with any of the actual yield whey cream information that is in the record such as it is?

A. I don't recall what's in the record at the moment. From my discussions with various parties, my sense is that this is on the high side of what's actually recovered, because we still have not accounted for other losses in the system. These are the only ones that were quantifiable, easily quantifiable.

Q. Have you calculated the total aggregate effective the various positions that Leprino is supporting with respect to Class III price?

A. Not of the make allowance changes I have not updated it for that, but as we just reviewed the change in the whey cream volume amounts to 16.9 percent of the Class III products, and the elimination of the three cents in addition to the barrel price, I estimated it at 16.2 cents, totaling 33.1 cents per hundredweight.

Q. What do you think the make allowance

S. Taylor - Cross by Mr. Beshore

proposed changes are going to be?

A. I believe what they should be is based upon last year's study with a population adjusted weighting that's north of $0.20. The survey was a stratified random sample, and to do anything other than do a population adjustment is incorrect statistically.

Q. We don't have the current population parameters.

A. That's why I'm starting with last year's base, and Mark Stephenson was very clear that on the same set, he had a subset of plants that were common to both study periods, and the increase in cost on that group was 1.7 cents. So I would use last year populated weighted number, plus 1.7 cents on cheese.

Q. And that's something in excess of $0.20 per pound of cheese, the result?

A. That would be correct.

Q. And the make allowance is currently, what, 16.8 cents?

A. I have lost track, 16.8, 16.38, somewhere in there.

Q. Let's assume there is a $0.4

additional adjustment advocated, that is roughly, what, $0.40 on the Class III price?
A. Yes.
Q. Roughly. So 16.9, 16.2, that's $0.33, so $0.40 we are looking at reducing the Class III price by 70 to $0.75 in aggregate. Is that about right?
A. That seems reasonable, based on those rough numbers.
MR. BESHORE: Thank you.
MR. PALMER: Questions?
MR. MILTNER: I'm Ryan Miltner on behalf of Select Continental and Dairy Producers of New Mexico.

CROSS-EXAMINATION

BY MR. MILTNER:
Q. Good morning.
A. Good morning.
Q. A lot of my questions were taken care of by Marvin. So I will cross them off as I go through my list here.
I wanted to ask questions on two particular areas, the first of which is the

S. Taylor - Cross by Mr. Miltner

expected butterfat recovery in a cheddar plant. In your testimony you advocated the retention of a 90 percent butterfat recovery. That is a fair summary?

A. Yes.

Q. Based on your experience and your discussions with others, do you believe that a butterfat recovery higher than that is reasonably achievable by a cheddar plant?

A. It's achievable by some cheddar plants, depending on the technology that they are using.

Q. Even if they didn't add any whey cream back in their vat, they're still achievable?

A. With certain vats, yes.

Q. Do you recall the testimony from Mr. Greenway earlier in the session?

A. Some, not completely.

Q. It's referenced in your statement that he had an average butterfat recovery of just over 90 percent. Do you recall that he broke out the recovery by month in his testimony?

S. Taylor - Cross by Mr. Miltner

A. Could you repeat your question.

Q. Overall he testified that his plant had a butterfat recovery of approximately 90 percent. Do you recall in his testimony, however, in his statement that he documented the monthly butterfat recovery at his plants?

A. I do not.

Q. Are you familiar at all with his operations?

A. No.

Q. If his testimony, his statement showed that in months they had recoveries of as high as 92 percent, is that something that could be reasonably expected in the industry?

A. It could be expected in certain plants with certain technology.

Q. You refer to Dr. Barbano's studies in your testimony as well were the issues of protein hydrogen and some other issues.

A. Yes.

Q. The exhibits that were already admitted, Exhibits 59 through 61, on that issue, at least Exhibit 59 refers to butterfat recoveries, and he surmises that a number of 93

S. Taylor - Cross by Mr. Miltner

percent is achievable in a modern plant. Do you have any opinions as to whether his statement is correct or incorrect on that point?

A. I have no reason to believe that he's incorrect and giving the certain technology.

Q. You testified on cross-examination that Leprino, in fact, adds all of its whey cream back into the vat and incorporates it into a finished product; is that correct?

A. That's correct.

Q. You also state in your testimony that at least Mr. Sommer believes that doing so in cheddar manufacturing is unadvisable?

A. That's correct.

Q. Do you personally share Mr. Sommer's belief that that is unadvisable?

A. In cheddar production, yes.

Q. Why is it that in Leprino's case and in the manufacturer of mozzarella that practice is advisable but it's not in cheddar production?

A. The kind of cheese and the handling

S. Taylor - Cross by Mr. Miltner

of that cheese after it's produced are different, and I'll once again reiterate, as I shared with Mr. Beshore, I don't believe that adding whey cream back to mozzarella is a broad practice in the mozzarella industry. Leprino Foods, as I already stated, has invested a great deal of money in figuring out how to manage that process. And so although we can do it, and I fully believe that we do it in a quality way, I don't believe that most people can.

MR. MILTNER: Your Honor, I have an exhibit that I would like to have marked, please.

MR. PALMER: Our exhibit number now is 78.

(Exhibit No. 78 was marked for identification.)

Q. Is it fair to assume you are familiar with the University of Wisconsin Center for Dairy Research?

A. I am aware of them. I wouldn't say that I'm highly familiar with them.

Q. In fact, Mr. Sommer, the expert

S. Taylor - Cross by Mr. Miltner

witness that your organization sponsors is employed by the Center for Diary Research; correct?

A. Mr. Sommer is employed by CDM.

Q. Have you ever had an opportunity to see the document that we are looking at now prior to today?

A. No.

Q. For the sake of the record, I will state that it's a technical update for diary product manufacturers from the University of Wisconsin Center for Dairy Research, entitled Efficient Use of Whey Cream in Cheese Making. I'll characterize it as such. If you disagree or people want to disagree on brief, they may, but it lays out generally pros and cons of incorporating whey cream into cheeses, predominantly in cheddar cheese. If the paper summarizes the efficient use of such of whey cream and cheddar cheese and concludes that there is a -- it can be effectively managed, Leprino effectively manages in the corporation of whey cream, does that change your opinion at all on whether a whey cream can be effectively

S. Taylor - Cross by Mr. Miltner

incorporated as cheddar cheese?

A. It does not change my opinion on the prevalence of it in the country or the acceptability to customers.

Q. In your statement you say most cheddar manufacturers don't incorporate whey cream into their vat. Do you have an estimate or any knowledge as to what, in fact, how many, what percentage of cheddar manufacturers do or don't incorporate?

A. I do not. Based on the hearing record and what I included in my testimony, you'll note that 85 percent of the cheddar cheese purchased by the largest marketer within the United States prohibits use of whey cream, and there are several cheddar manufacturers who testified at this hearing that don't use whey cream, and my belief is to the extent that people do use whey cream, it may be on a limited volume, depending upon their customer base. For example, they may make the bulk of their cheddar without the whey cream addition but have one or two customers who will accept the whey cream addition.

S. Taylor - Cross by Mr. Miltner

Q. But that doesn't mean most -- it's not a definite most. You cannot say we can't tell from the record that the majority of cheddar cheese, commodity cheddar cheese, in the country is made without the incorporation of whey cream?

A. I believe that the report does show that, based on all of those pieces of information I just outlined.

Q. Could you calculate -- I'm not asking for a definitive number. I don't want you to say 55 percent. But you cannot mathematically say the majority, more than 50 percent of commodity cheddar doesn't incorporate whey cream?

A. There has not been a survey that's been enumerated specifically in the volume. It's based on the testimony that has been entered into this record.

Q. Of course, you would conclusively establish whether someone does or doesn't. You would actually have to bring them to the stand and have them testify, yes, I do, or, no, I don't?

S. Taylor - Cross by Mr. Miltner

A. That would be correct.

Q. And there are how many cheddar manufacturers? A couple of hundred dollars? Is that a fair estimate?

A. I would have to refer to a number of other documents to be able to tell you that.

Q. Because Leprino does use whey cream in their cheese, of the milk that goes into your vat, the butterfat that goes into your vat, except for the losses which you outlined in your statement, all of that butterfat ends up in a finished product going out the door; right?

A. There are several losses that I refer to in my testimony that have not been quantified. So the fat going into the vat will end up in the finished mozzarella, in the whey that is processed. It will end up in fines that are unrecovered. It will end up in product that hits a surface that's ineligible for human use and therefore needs to go through our waste stream. We have a disposal cost for that. It will go into, if we are making protein concentrate and lactose, it will go

S. Taylor - Cross by Mr. Miltner

into the DLP that is essentially a disposal product. It will go into any of those aspects of loss or finished product but not all commercially viable finished products.

Q. Would you care to quantify those losses?

A. No.

Q. Are they more or less than two percent of the product that you produce? Let's say the fat that goes into your vat.

A. I don't know. We measure unaccounted for fat. There are many places where we're accounting for it that would not necessarily be considered commercially viable. Of the fat that goes into the vat that we have not accounted for -- well, actually -- the way they do their accounting I can't get a clean answer because they do unaccounted for fat, I believe. So fat going into the whey, so it would be inappropriate to use that number.

Q. The amount that goes into your whey is extremely small?

A. I can tell you our unaccounted for fat number is much larger than what you would

S. Taylor - Cross by Mr. Miltner

like to hear, but it includes some fat that does end up in commercially viable product. So I don't think it's an appropriate number to disclose anyway. It's well north of two percent.

Q. Let's walk through a hypothetical, if we could, for a second. I want to assume for this hypothetical that we have a cheddar manufacturer that has a 90 percent butterfat recovery. From your statement I want to assume that 7.8 percent of the butterfat in the vat can be recovered in the whey cream that comes from your page 14, your table. Okay?

A. Yes.

Q. Then I want you to assume that that cheddar manufacturer incorporates the whey cream back into their vat. I want you to assume based on Mr. Brown's testimony that they can get 75 percent recovery out of their whey cream. So I have run the math here, and I'll do it again as I'm talking, but we end up with about 95 1/4 percent, probably more than that. If you take the percent of fat in the whey cream times 75 percent recovery and add it to

S. Taylor - Cross by Mr. Miltner

the 90 percent recovery of the fat making, its first pass through, you can expect a recovery of 95.8 percent. Does that math work with the way you would calculate that?

A. I'm not sure that is the way I would think about it. The actual vat capture on that fat would be a weighted average of your 90 percent fat recovery on the initial fat run and the 75 percent. So your fat capture on that vat would be less than 90 percent.

Q. On the entire vat it would be?

A. If you are looking at the fat captured in the cheese versus that fat that went into the vat.

Q. Yes, I agree with that. But if you are accounting for the recovery of the whey cream you put back in and add that to the recovery of fat from the first run of the milk that was put into the vat on the first run, including that which was reincorporated through the whey cream, you'll recover about 95.8 percent of all of the fat that came into the vat initially?

A. I believe your math works. I'm not

S. Taylor - Cross by Mr. Miltner

close enough to the actual process. I don't have any experience to say that that's how it works in reality.

Q. And, of course, if like Mr. Greenway's plan, you have a 92 percent butterfat recovery without the corporation of whey cream. Now you can recover, if my math is correct and my methodology is correct, 97, 98 percent of the butterfat that that plant purchases could end up in finished product on that pass?

A. You would have to reduce. You would only have instead of 10 percent that wasn't captured in the initial run, you would have 8 percent. So there would be some adjustments and some reduction in how much whey cream would be generated and how much whey cream could be captured again, but it would increase the number.

MR. MILTNER: Your Honor, could I move the admission of Exhibit 78?

MR. PALMER: Is there any objection?

MR. VETNE: John Vetne for

Agri-Mark and other cooperative components. It's apparently being submitted in evidence without limitation for the truth of its contents. It was a subject of questions to the witness to illustrate her awareness of various technologies and uses and limitations of fat, the way fat is introduced. For that limited purpose I do not object.

For its broader use as though presented by the authors who are not present, I would object to that. So my objection is to its unrestricted use, not to its limited use in the contents of examination.

MR. PALMER: What do you say to that? Are you willing to accept that restriction on its use?

MR. MILTNER: No. I mean, obviously, it's admissible for those uses, but I think it's also a statement from the industry by well-qualified scholars in the industry from a respected institution and, in fact, a group of that institution that has been relied upon in this hearing, and we have admitted similar papers throughout the hearing for whatever use the Department deems fit, and so I would request that it be admitted with the usual restriction that the Department will give it the weight and to which they deem its entitled.

MR. PALMER: I notice the date on it is October 1997. So it's not exactly.

MR. MILTNER: I think that Dr. Barbano's statements if you look back, date even further back than that which the Court has already admitted and, if anything, technology has improved ten years. It hasn't gotten any worse.

MR. PALMER: Mr. Rosenbaum.

MR. ROSENBAUM: I'm going to join in Mr. Vetne's objection. I don't think it's appropriate to put in a document like this through cross-examination. If they had wanted to put a witness on as to the practices in this field, so be it, but they chose not to, and we can't cross-examine these people as to what current values are. So I think it's inappropriate.

MR. PALMER: Anybody else? Mr. Beshore.

MR. BESHORE: Just a couple of comments. I think it's equivalent, as Mr. Miltner said, to the Barbano publication that has been presented, and he's not here.

The other point I would make with respect to Mr. Rosenbaum's comments, they sponsored an expert witness from this institution on cheese making in this proceeding.

MR. ROSENBAUM: Your Honor, on that score I might have had a different view had they chosen to use this document in examining someone from their own institution but they chose not to. It's sandbagging, really is what it is, because, obviously, Mr. Sommer who works for this Center could have adequately commented upon it, but instead we have on the last day of the hearing when Mr. Sommer is not in the room or within hundreds of miles of this room in attempt to introduce this document.

MR. PALMER: Mr. Vetne, do you wish to speak again?

MR. VETNE: Just one point.

Mr. Miltner referred to the authors of this report as highly qualified. I'm not exactly sure of the words he used, but the point is that Mr. Sommer and Dr. Barbano both appear and disclose their qualifications and were available for voir dire. In fact, of the three authors that we have here we know nothing about their background there, whether they are graduate students working on a paper, whether they are professors, what the database was. We can't ask. So I maintain the limited usage objection.

MR. MILTNER: I just have two comments. First of all, Dr. Barbano is not here, and the record will reflect that.

And secondly, I would like to -- I do take exception to the notion that we're sandbagging here. Personally I think that is an uncalled for comment. All we are asking for is that this particular exhibit be treated the same way the court has treated the other similar exhibits used in cross-examination, and that is the extent of my statement.

MR. PALMER: I was trying to

find out who Johnson Bradley and Windor are. There seems to be a footnote, but I don't find a footnote. I looked at the page of footnotes. An MJ Johnson it says one. So I would assume it's all about one but the fact there is a reference page. It doesn't seem to have a footnote, so I don't really know who they are. And as somebody said, they might be graduate students.

Did you have something else, Mr. Beshore?

MR. BESHORE: I was only noting that the footnotes are right below the names. They identify the institution with which the individuals are associated.

MR. PALMER: Did I miss it?

MR. BESHORE: I had a lot of trouble finding it also. Dr. Cryan was helpful.

MR. PALMER: Where is it now? I'm looking down.

MR. BESHORE: It's immediately below the names.

MR. PALMER: Oh, I see, Center

For Dairy Research. But we still don't know who they are, do we?

MR. CRYAN: The first name is Mark Johnson who is a Ph.D., one of the, considered one of the best cheese graters in the country.

MR. PALMER: This is a professional person. Our problem is we don't have him here for voir dire and the usual thing, and I have been somewhat restricted, I guess, in that ruling I made a few weeks back about reference material, whether or not it's relevant. It's certainly relevant material, and we do receive -- we do take official notice of government publications, university publications. I'll receive it, but I will allow and I would expect counsel to on brief in the use of it to question as much as they can because the witnesses weren't here to bring that out. So it will be received.

MR. MILTNER: Thank you. I don't have any further questions at this time.

MS. PICHELMAN: Just based on that, USDA will give it the weight deemed appropriate to that piece of evidence.

MR. PALMER: That is basically what it's coming down to, what weight should it be given?

MS. PICHELMAN: Yes, that's correct.

MR. PALMER: Other questions? Yes, Mr. Rosenbaum.

CROSS-EXAMINATION

BY MR. ROSENBAUM:

Q. Ms. Taylor, Mr. Beshore asked you some questions regarding whether your calculation of expected national yields for mozzarella are a reflection of how many pounds of cheese would be expected to be recovered based upon the pounds of milk that went into the vat. Do you recall that question?

A. Yes.

Q. And he asked whether that kind of calculation accounted for losses of milk in the process; correct? Do you recall that question?

A. Yes.

Q. And your answer was, yes, when you

S. Taylor - Cross by Mr. Rosenbaum

are doing that kind of calculation, you were accounting for losses in the process; correct?

A. Yes.

Q. The question, though, I would like to have you address is Federal Milk Marketing Order perspective which is when the Federal Milk Orders are used in the VanSlyke formula to predict the yield based upon pounds per milk -- first of all, the Federal Order System measures the pounds at the farm, and you already talked about there being farm to fat loss; correct?

A. Yes.

Q. And that's accounted for in the formulas as they now exist; correct?

A. The farm-to-plant piece is captured in the current formula.

Q. But the question is, do the current formulas capture the plant-in-plant losses?

A. They do not.

Q. Do the federal formulas assume that every drop of milk that hits the plant actually makes it into a finished product?

A. Largely, yes. They assume that

S. Taylor - Cross by Mr. Rosenbaum

every pound of fat makes it into a finished product, either those finished products either being cheddar or right now sweet cream and every pound of other solids and sweet whey and largely the same on protein.

Q. And the reason why you believe there needs to be the adjustments made to the formula that are set forth on the table I think it's on page, is it 16 where you attempt to show various adjustments that you think are necessary that is a reflection, in fact, to the current formula which assumes that all of the fat ends up either in the cheese or in the whey cream when, in fact, as you've shown, some of it gets lost in the processing; is that correct?

A. That's correct.

Q. Did Mr. Beshore's questioning regarding how Leprino itself judges its own yields have any impact on the need to make the change as you outlined on page 16?

A. None whatsoever.

MR. ROSENBAUM: That's all I have.

S. Taylor - Cross by Mr. Yale

MR. PALMER: Questions? Yes, Mr. Yale.

Your testimony was the other day, and I hear different witnesses, and I do get a little confused. Leprino, are you using whey cream?

THE WITNESS: Yes.

CROSS-EXAMINATION

BY MR. YALE:

Q. Good morning, Sue.

A. Good morning, Mr. Yale.

Q. I want to follow up on a question of Mr. Rosenbaum and just kind of summarize this whole thing. Is it the position of Leprino and IDFA that 10 percent of the butterfat throughout the Federal Order System that enters into Class III is to be priced at a whey butter price?

A. No.

Q. How much is it to be priced at that?

A. Our position is no more than 7.8 percent.

Q. That assumes that throughout the

S. Taylor - Cross by Mr. Yale

entire Federal Order System that all of the milk received, all of the fat received at Federal Order plants that are in the aggregate seven plus percent of that fat goes into whey?

A. No. It's a policy application. The Federal Order set minimum milk prices. Therefore, they need to reflect the value that is achievable within the system. There are going to be some plants that can achieve something greater, but there are many, many plants that cannot achieve something greater, and so just from a policy perspective it's very important to set the Federal Order prices at a level that is achievable for cheddar plants across the country.

Q. You've been here throughout the hearing?

A. Yes.

Q. There is no evidence in the record in terms of what actual yields and recovery of butterfat for all plants what that is; isn't that correct?

A. Not for every plant in the United States. There is substantial evidence from

S. Taylor - Cross by Mr. Yale

some plants.

Q. I want to change the subject. At page 32 of your statement you compared the current formulas with the 2000 decision for use in 2004, is that correct, to show that it would have made money for producers?

A. I believe it was in the 2001 formula, not the 2004 formula, using the 2004 market prices. That is correct, it was announced in 2000, took effect in 2001?

Q. You're aware, are you not, that in 2004 there was a substantial amount of de-pooling of Class III milk?

A. The years run together. I don't recall specifically. I know that there have been several periods of de-pooling over the last five years.

Q. And for Federal Orders, just using the numbers in the Federal Orders, that could have a very significant bearing on the impact, could it not? The volume of Class III milk is substantially different from other periods?

A. The analysis that I did in the 2004 data used the same utilization that was used in

S. Taylor - Cross by Mr. Yale

your original analysis. I did not change the Federal Order utilization numbers whatsoever. My only change was to use the 2004 commodity price values.

Q. Do you have any reason to disagree with USDA's economic analysis when it issued the interim final order in December 2006, effective February, March of this year, that there was an impact on Class III in excess of $0.20 hundredweight?

A. No. My calculation is it was $0.24.8.

Q. Now, you are familiar with the VanSlyke formula; are you not?

A. Generally, yes.

Q. Generally the formula is to determine what the yield is, based upon given the butterfat, the protein and the moisture from that you can determine a yield of pounds of cheese per that milk that's in that vat; right?

A. That's correct.

Q. Now, you can also alter that, can you not, and say if I know the amount of

S. Taylor - Cross by Mr. Yale

protein and I know the moisture and I know the yield, I can back in and determine how much butterfat was used; can I not?

A. Yes. You would have to know the fat retention rate and the fat components. You would have to know one of those pieces to back into the other.

Q. I'm sorry. I forgot to add the fat component. So, in other words, you can make any one of those to be the unknown and the others the known and begin to calculate it; right?

A. If you have precise enough data.

Q. Now, I'm not going to ask you to compute this, but I'm going to give you two set of numbers, and if you want to write them, you can. The question is, whether one could compute using the VanSlyke. Like, if you were told that you have 11.53 pounds of cheeses of yield and a moisture of 37.04 percent and butterfat of 4.02 percent and the amount of casein is 2.814, can you from that information compute the butterfat recovery?

A. Yes, you could.

S. Taylor - Cross by Mr. Yale

Q. Now, your testimony regarding the amount of casein in milk is based upon, and I believe you submitted two exhibits, 60 and 61; is that correct?

A. I have attachments to my testimony.

Q. Well, I guess maybe they were --

A. There are tables, 2, 4 through 9. They would be marked as Addendum C.

Q. There are pages --

MR. PALMER: Let me interrupt you for a second. Go off the record for a second.

(Short recess taken.)

MR. PALMER: Back on the record.

Q. Your Addendum C comes out of a report entitled Trends and Milk Composition and Analysis in New York by David Barbano, is that not correct?

A. Yes.

Q. And I believe that that was marked as Exhibit 61. So it's page 36 in Exhibit 61. It starts there. I'm going to look at page, it's Table 5 in your Addendum C, and I believe

S. Taylor - Cross by Mr. Yale

that is page 36 in Exhibit 61. Before we look at that, I do want to ask some questions. First of all, how is nitrogen or protein measured for purposes of paying producers? Do you know how that process is done?

A. Typically it's measured by infrared equipment. That infrared equipment is calibrated against some merc calibration sense that it has wet chemistry run on them.

Q. And the infrared measures what? Do you know what that measures?

A. They use a spectrum to measure the, as I understand it, displacement in the light, and it interprets then what the composition is to achieve that level of bending in light.

Q. And the number of the raw number that comes out is the total amount of nitrogen that is in the milk?

A. I believe, but I don't recall specifically.

Q. Let's start for the moment when we talk some times of total nitrogen of milk, that is also accrued protein or total protein is another word for that. Would that be correct?

S. Taylor - Cross by Mr. Yale

A. Right. Actually, my recollection, but we would have to go back to one of your exhibits, is that the equipment actually measures the true protein and historically when we use true protein, it is an assumed add-on.

Q. So let's talk about that for a second. But out of that protein there is nonprotein nitrogen. You're aware of that term, NPN?

A. Yes.

Q. What is that? Just exactly what it says?

A. That's exactly what it says. It's nitrogen that is not protein.

Q. And there is also non-casein nitrogen or NCN; right?

A. Yes.

Q. Which would include everything else other than the casein. That would include the whey protein as well as NPN; correct?

A. Right.

Q. Is it not true that in the composition of the total nitrogen or the total protein that the amount of the percentage of

S. Taylor - Cross by Mr. Yale

casein in total protein, that that percentage increases as the amount of total protein increases?

A. You're asking if the casein percent increases as the total protein increases?

Q. That's correct.

A. I don't think that that is an accurate conclusion. One of the reasons why we went away from total protein to true protein is because of the fact it is easy to impact the level of nonprotein nitrogen by feeding additional urea and other management practices in the farm levels. So you can increase the true protein without increasing the yield capabilities of that milk.

Q. In Table 5 of your addendum the average true protein test is 2.94 percent; is that correct?

A. Yes.

Q. Also, in your Table 6 it shows that the percentage of nonprotein nitrogen is .192?

A. Yes.

Q. Now, during cross-examination and myself, I believe there was another exhibit

S. Taylor - Cross by Mr. Yale

that was submitted, and that's Exhibit No. 60 which was labeled the indirect and direct determination of casein content of milk by the Cadol Nitrogen Analysis Study. Are you aware of that that was submitted by your counsel?

A. I'm aware of it, but I am not familiar with the contents.

Q. Do you know the difference between direct and indirect measurement of casein?

A. I would be guessing.

MR. YALE: Your Honor, we would move that the entire Exhibit 61 be admitted. I don't think that it was as well as just the tables that she has in Addendum C.

MR. PALMER: I reserved the ruling on that for some reason. It was Exhibits 59, 60 and 61. I have here I preserved the ruling. Does anybody remember all of this?

MR. YALE: Yes. That is why I asked that it be admitted?

MR. PALMER: Does anybody have any problem with 61 being admitted?

MR. BESHORE: What is it?

MR. PALMER: Trends and Milk Composition Analysis in New York by Dean and Barbano.

MR. BESHORE: What is the year?

MR. PALMER: '99, I guess.

MR. YALE: This was '99.

MR. BESHORE: I would say they ought to be received on the same basis as the last one.

MR. YALE: We would accept that, Judge.

MR. PALMER: We would receive it on that basis.

MR. YALE: And 60 on the same basis.

MR. PALMER: How about 59? There were three of them.

MR. YALE: That is the testimony because there were questions asked of her about that and I think of even myself. On the limited purpose dealing with the cross-examination in reference to Dr. Barbano.

MR. PALMER: So 59, 60 and 61?

S. Taylor - Cross

MR. YALE: On the limited basis.

MR. PALMER: Yes; we will do all of them. So done.

BY MR. YALE:

Q. Yesterday you were here when Dr. Stephenson was cross-examined?

A. For most of the period.

Q. Were you there when he was asked for the high and low range of make allowances?

A. I don't recall.

Q. Do you recall him saying that the low range of the plants are in the neighborhood of $0.10 per pound of cheese?

A. No.

Q. You weren't here then?

A. No. I don't believe I was at the moment or I wasn't paying attention.

Q. Does that represent approximately what Leprino's cost to manufacture cheese is?

A. No.

Q. Is it higher or lower?

A. Higher. Our cost would be higher than that.

S. Taylor - Cross by Mr. Vetne

MR. YALE: I have no other questions, Your Honor.

MR. PALMER: Do we have other questions? Mr. Vetne.

MR. VETNE: Before I ask a few questions, Your Honor, I'm confused, I want some clarification. Fifty-nine, 60 and 61, the recent ruling on that and the term limited basis, was that limited basis ruling intended to be equivalent to the recent ruling on the 78?

MR. PALMER: Seventy-eight, if anybody can understand it, I'm not sure if I understand my ruling, but we received it and there is a question as to the weight it should be given. Obviously, we don't have the sponsored witnesses available.

CROSS-EXAMINATION

BY MR. VETNE:

Q. Sue, you've indicated that in your California operation you recover what otherwise would be sold as whey cream by introducing it back into the vat and doing it sequentially.

S. Taylor - Cross by Mr. Vetne

It keeps going back; correct?

A. Yes.

Q. And you indicated that you did that on a couple of occasions. You used the word great deal of cost, great deal of money and another occasion higher cost. I want to address that part of your testimony. If you did not make those investments and technology to enable you to do that, you would then be selling that whey cream, and the net revenue to your plant for all operations would be less; is that correct?

A. That's correct.

Q. But as a result of investment in those technologies, you have a measurably higher manufacturing cost for the cheese that you do produce than you would otherwise have if you simply sold the whey cream?

A. Yes.

Q. And that would be true for anybody else who is either implementing or considering technologies to recover some of the whey cream by reintroducing it back into the vat. That comes with an additional cost?

S. Taylor - Cross by Mr. Vetne

A. I believe so.

Q. So we are here on various proposals that address cost of manufacturing and revenue from product produced. If one were to attribute a yield from the reintroduction of whey into a stream hypothetically for regulatory purposes, one would also have to attribute an additional cost and the manufacturing costs for purposes of make allowances?

A. That would be correct.

Q. Are you aware of any evidence that isolates that so far in the record?

A. No.

Q. Now, I want to go back to Mr. Miltner's hypothetical and the 95 percent recovery thing just to see if I understand, and I went back to your page 14 of your testimony and tables there. Let's see if I understand your testimony. You start with a plant receiving 3.5 percent butterfat of standardized milk, and from that milk upon making cheddar it's 95 percent fat recovery. So 3.1, et cetera, 1.286 pounds per fat covered in the

S. Taylor - Cross by Mr. Vetne

cheese on the first run?

A. Yes.

Q. And then there is whey cream left over. There is whey cream that is lost in the process, but there is .27 pounds of whey cream in the process of the first run?

A. Yes.

Q. As I understood your dialogue with Mr. Miltner, it was that .27 pounds of whey cream that would be reintroduced into the vat on the second run?

A. Under Mr. Miltner's scenario, yes.

Q. Based on your understanding of the testimony by Mike Brown, that whey cream has a lower recovery, 75 percent rather than 90 percent. So you take 75 percent of the whey cream and attribute that as recovered in the second vat; correct?

A. Yes.

Q. In addition, in the second vat you attribute the same 90 percent recovery to the fat that is in producer milk that comes into the vat?

A. Correct.

S. Taylor - Cross by Mr. Vetne

Q. And you get those totals and then average them out over two vats?

A. Yes.

Q. You have -- it's hundredweights. You have 7 pounds of milk going in and then 3.1 pounds, plus 3.1 pounds, plus roughly .2 pounds, 75 percent of the whey cream recovery, and that's your total cheese fat recovered from cheese for the two runs?

A. I believe so. I'm still trying to track your math.

Q. 3.1 is 90 percent fat recovery of producer milk?

A. Correct.

Q. Plus 3.1, again 90 percent recovery from the second vat of producer milk, plus .2, roughly 75 percent of the fat in the whey cream?

A. Correct.

Q. My math here comes up with 9.2 percent at the end of the process, not 9.5 percent. So I'm wondering where in the process you understood enough to agree with Mr. Miltner that there is 95 percent recovery somewhere.

S. Taylor - Cross by Mr. Beshore

A. I believe that it was my omission of the -- I failed to recognize in my math as he led me through that that you're not able to add the whey cream under Mr. Brown's scenario into every vat. It's a one reuse only. So you always have one initial, essentially, that does not have any whey cream in it, and so I believe that the difference is averaging across the two vats versus that single vat that has the whey cream we used?

Q. And you understand or is it your understanding that all of that hypothetical discussion omitted in any real world reference to the marketability or acceptability of that product?

A. That's correct.

MR. VETNE: That's all.

MR. PALMER: Questions? Mr. Beshore.

CROSS-EXAMINATION

BY MR. BESHORE:

Q. Sue, in terms of the dialogue with respect to whether the current Federal Order

S. Taylor - Cross by Mr. Beshore

formulas represent real world yields or just assume theoretical yields --

Let me ask you this. The VanSlyke formula was, what, about 125 years ago, late 1800's?

A. It's been a long time.

Q. But it was before the twentieth century?

A. Yes.

Q. Do you think that formula had any relationship to the practical yield available with cheese making technology at that time?

A. My recollection is that it was more of a research setting as opposed to a commercial setting. So it wasn't, I don't believe, achievable broadly in the industry at that point in time.

Q. But it's been used since that time as a benchmark for what may be achieved in cheddar cheese production; has it not?

A. It's routinely used with modifying factors that are more realistic to commercial settings. My understanding is probably every cheese maker in the country compares their

S. Taylor - Cross by Mr. Beshore

actual yields to it. Some theoretical target is customized to their plant.

Q. And has for years?

A. Yes.

Q. And the fact that the modified VanSlyke formulations is what we have used in these hearings?

A. Yes.

Q. So to the extent that the -- well, isn't it correct that as technologies evolve over the years, the VanSlyke pure theoretical has been modified for production realities, that it's been and it is and has been an overall real world return. It represents a real world; does it not?

A. The VanSlyke used properly with realistic factors doesn't emulate real world targets. Now, there are a number of factors in the production cycle that may result in a variance in a given production, but it's an important management to compare to.

Q. In fact, no one is suggesting in these proceedings that the yield of cheese represent a formula is not a real world yield,

S. Taylor - Cross by Mr. Beshore

are they?

A. I am not aware of any proposals to lower the yield. There are some proposals to increase the yield in this proceeding.

Q. Well, if it was not a real world yield, more than likely we can assume that the organization such as the National Cheese Institute or IDFA which represent cheese makers would be suggesting that the yield be lower to the real world factors; isn't that fair?

A. I've probably been a little bit confused by your term real world. If you are using it in the context of it's an achievable yield, I would say that for most manufacturers it probably is an achievable yield.

Q. So if it's an achievable yield of cheese, back to what I asked you about in cross, isn't it correct that that achievable yield factors in everything that goes on in the plant, including the types of in-plant losses that we have discussed?

A. As they relate to the components that end up in the cheddar cheese. It does not factor in losses that occur elsewhere in the

S. Taylor - Cross by Mr. Beshore

system, in terms of fat -- essentially, everything that doesn't end up in the cheddar cheese.

Q. So you're saying it doesn't factor in. Essentially, what your testimony comes down to is, it doesn't factor in to the protein value equation appropriate yields for whey cream?

A. That would be correct. The yield of whey cream, the yield of other solids have no relationship to the VanSlyke formula. The VanSlyke is strictly used to estimate a yield for the cheddar cheese.

Q. Just to tie it up to understand it, the factors relating to yield of whey cream in the Federal Order Class III formula are simply elements that are used to reduce the price for protein?

A. I wouldn't put it in those terms. Currently the assumption in the Class III formula is that 10 percent of the fat goes into Double A butter.

Q. That is all in the protein formula, though, the protein price; right? That is on

S. Taylor - Cross by Mr. Beshore

page 16 of your testimony.

A. It's a combination of the fat component price and the adjustment within that protein component. The fat component is actually a credit of currently 90 percent -- the adjustment in the protein component is a credit of 90 percent of the fat. So the actual enhancement of value in the Class III formula actually resides in the fat component. The protein formula fails to fully, essentially, give credit for as much fat as should be given.

Q. It's all in the protein formula, whether you call it credit or enhancement. It's all in the price of protein, and the point is the price of protein is too high as far as --

A. Yes. That would be correct.

MR. BESHORE: I have just one other question while you are on the stand and it's for USDA, but I don't want her to get away.

Is there any information that might be needed for calculations of the economic impact of that IDFA proposals that I requested

S. Taylor - Cross by Mr. Wellington

before that may be needed?

MR. SCHAEFER: We don't know. I mean, we can't give you an answer right now.

MR. BESHORE: I don't have an answer to that, but that is the best I can do, I guess.

MR. PALMER: Any other questions for Ms. Taylor?

MR. WELLINGTON: Bob Wellington from Agri-Mart. Just a couple of questions for you, Sue.

CROSS-EXAMINATION

BY MR. WELLINGTON:

Q. Are there some manufacturers out there that probably cannot achieve the VanSlyke formula because of older equipment or procedures?

A. I believe there are.

Q. Is the technology that's used by Leprino for the use of -- the reuse of the whey cream in the vat? Is that a proprietary technology?

A. I don't know whether it's

S. Taylor - Cross by Mr. Schaefer

proprietary and patented or not.

MR. WELLINGTON: That's it.

MR. PALMER: Other questions? Yes, Mr. Schaefer.

CROSS-EXAMINATION

BY MR. SCHAEFER:

Q. Good morning, Sue -- or I guess we are into the afternoon.

In your testimony you indicated an opposition to Proposal 13 and Proposal 15 that is on page, I believe, 28 of your testimony, and you had some discussion there on why you oppose on Proposal 13 but really no discussion on your opposition to Proposal 15. Could you elaborate on why you are proposing Proposal 15? Proposal 15 is the proposal by Dairy Producers of New Mexico to use CME rather than the NASS?

A. I believe that the volume that is traded on CME is narrow enough that I have concern about it. I think that a more robust volume as represented by the NASS survey is far superior than the volume that is rated on the CME.

S. Taylor - Cross by Mr. Rosenbaum

Q. This has been talked about earlier in this discussion. Does the lag in the NASS concern you at all?

A. As a company we feel that it's something that we should be able to manage. I know that it concerns many cheese makers, but we feel that it's a predictable lag if you are doing risk management. You should be able to be smart enough to figure it out. So it's not an overriding concern to us.

MR. SCHAEFER: Thank you. Sue?

MR. PALMER: Other questions? Mr. Rosenbaum, do have some questions?

MR. ROSENBAUM: Yes.

CROSS-EXAMINATION

BY MR. ROSENBAUM:

Q. Ms. Taylor, obviously, the Federal Order system has made the determination for some years now to base the Class III price on cheddar cheese; correct?

A. Yes.

Q. And accordingly, the NASS survey of

S. Taylor - Cross by Mr. Rosenbaum

product prices only looks to what the price is in cheddar cheese; correct?

A. That's correct.

Q. Accordingly, for the purposes of determining make allowances yield, et cetera, it's appropriate to look at cheddar cheese; correct?

A. Correct.

Q. Whether or not mozzarella manufacturers are or are not able to use whey cream in ways that cheddar cheese manufacturers are not ultimately does it have an impact on appropriate factual considerations here. Do you agree to that?

A. I agree.

Q. Are there reasons why you are able to use whey cream in mozzarella that are simply inapplicable in cheddar cheese?

A. Yes. Some of it, as I had said earlier, the use of the ultimate finished product and how we handle that finished product as well. Some of it is the -- well, the vast majority of our mozzarella is frozen, and so in terms of any microbiological concerns they are

S. Taylor - Cross by Mr. Rosenbaum

much lower in our product than they would be either for a cheddar cheese maker or a standard mozzarella maker. There are some other factors along that line.

Q. This is implicit, but does that make it easier for your company to use whey cream in the cheese as compared to what a cheddar cheese manufacturer effects?

A. Yes, it does. One other thing I would like to elaborate on is this issue of mozzarella versus cheddar and the suggestion that has been made by some in the hearing process that the only products we should be concerned about in terms of the profitability levels are NASS eligible cheddar or the NASS reportable products with an inference that everybody else in cheese industry can just add on to their premium level and recapture their cost. I would argue that that is absolutely wrong, because ultimately what drives the net economics on mozzarella as competition with the net economics of cheddar there are many cheddar plants in the U.S. that also produce mozzarella. So to the extent that you end up

S. Taylor - Cross by Mr. Rosenbaum

with compressed margins on cheddar, that volume and that capacity migrates over to the mozzarella side, and you end up with the same compressed margin on the mozzarella side. So any implication or any suggestion that the only products to be concerned about would be NASS eligible products to me is a falsehood.

MR. ROSENBAUM: That's all.

MR. PALMER: Anything further? Thank you very much. Do we have any other witnesses? That concludes everything? Let's go off the record. Yes, sir.

MR. MILTNER: I have a couple of documents for official notice.

MR. PALMER: All right. We'll do that. Let's go back on the record and do the official notice documents.

MR. MILTNER: Your Honor, there are two documents both posted, I believe, to the AMS website, both federal publications came up in the past couple of weeks. The first is titled Impacts of NASS Nonfat Dry Milk Price in Sales Volumes Revisions on Federal Order Prices. It's an AMS publication.

The second is from NASS Dairy Products Pricing Special Report on Nonfat Dry Milk Revisions. Mr. Yale is handing out copies, but they are both available on the website.

MR. PALMER: Do you have the website? Can you state the website.

MR. MILTNER: I believe it's AMS.usda/government/dairy.

MR. PALMER: We'll take official notice of those for everybody's convenience. You are giving them out to the parties.

Anything else before we get to briefing?

MR. ROSENBAUM: On these two documents --

MR. PALMER: Is there a problem with the official notice? Let's go off the record.

(Discussion held off the record.)

MR. PALMER: Back on the record. It looks like we have one more

witness. Do we have anything more on this, because this looks like government publications, and I think we take official notice of it,
Mr. Rosenbaum.

MR. ROSENBAUM: I'm not asserting objection.

MR. PALMER: We'll take official notice of those. I understand Mr. Brown wants to return to the stand for a second.

MR. MILTNER: Your Honor, we also have a couple of items which normally we take official notice of, and I don't know if we have yet on the record, but we would request the ability to cite to any statistics compiled by AMS through Dairy Mart at news or NASS through the day briefing.

MR. PALMER: That will be allowed. Mr. Brown, I thought you had left the hearing. I saw you go out the back door, and I assumed that was it. Now I understand you went out to do more work.

MR. BROWN: Yes. I went to

confirm with our plant people to make sure I gave a correct answer.

MR. PALMER: You are still under oath.

MR. VETNE: So you have a correction, and what is it?

MR. BROWN: The correction is what we do with our permeate in our Sunnyside Plant. That permeate almost exclusively stays within the plant and goes back to the waste stream. Our skim milk powder permeate comes out of our ultrafiltering facility of Jerome Plant. The permeate for that comes out of our Jerome Plant, and that is hauled back to London, and some is left up in Jerome to make S and P in those two plants. So our UF facility in some of our cheese plants in Sunnyside that permeate actually does ends up in the whey and it is part of that whey yield. That's my correction.

MR. PALMER: Does that provoke any questions? It appears not. Thank you so much.

Let's go off the record.

(Discussion held off the record.)

MR. PALMER: On the record. We had an off-the-record discussion about when briefing and corrections, et cetera, should be made, and it's been decided that by September 14, 2007 briefs and any proposed corrections to the transcript should be fought with the hearing clerk. We're assuming in that that the transcript will be ready on a certain date that we discussed, and if that isn't so, if it's later than that, it will be appropriate motions made and we may extend it, but that is going to be on all proposals. The briefing date is September 14th. And that I believe, if there is nothing else, concludes the hearing. Thank you all very much.

(Whereupon, the above-entitled matter was concluded at 12:45 p.m. this date.)

C E R T I F I C A T E

I hereby certify that the proceedings and evidence are contained fully and accurately in the stenographic notes taken by me on the hearing of the within cause and that this is a correct transcript of the same.

S/Monica R. Chandler

Monica R. Chandler