



PUBLIC HEARING  
STATE OF CALIFORNIA  
DEPARTMENT OF FOOD AND AGRICULTURE  
DAIRY MARKETING BRANCH

DEPARTMENT OF FOOD AND AGRICULTURE  
1220 N STREET  
AUDITORIUM  
SACRAMENTO, CALIFORNIA

THURSDAY, JUNE 1, 2005  
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JAMES F. PETERS, CSR, RPR  
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1 the basic supply of raw whey. And therefore all decisions  
2 to make various products will be based in both the short  
3 run and in the long run on the expected value outcome.  
4 Those values decisions will constantly pull the whey  
5 protein values toward each other.

6 Attached just after Exhibit A is a graph which  
7 shows the skim whey powder and the Whey Protein  
8 Concentrate 34 prices on a normal time line Y axis. The  
9 bottom two lines are the skim whey powder and the Whey  
10 Protein Concentrate 34 prices. The relationship is clear,  
11 but certainly not dramatic.

12 However, the upper two lines are based on the  
13 values of the protein portion of each product. This gives  
14 a clear visual image of what the correlation numbers show.  
15 And they clearly show that they track together.

16 With regard to the recent increase in skim whey  
17 protein prices compared to the drop in the whey protein  
18 concentrate prices which so concerns Dairy Institute, we  
19 point out that this too is correcting itself. Again,  
20 common sense tells you that if the skim whey powder prices  
21 are good compared to whey protein concentrate, it is time  
22 to shift production to skim whey protein -- skim whey  
23 powder. While these short run decisions happen quickly,  
24 it does take some time for the volume shifts to impact  
25 prices. But in time they always do.

1           Milk Producers Council suggests that there be a  
2 snubber included in whey formula so that the contribution  
3 of whey to the 4b price will not drop below zero. We  
4 cannot resist pointing out that the only part of Dairy  
5 Institute's whey proposal that we like is their offer to  
6 snub the formula at zero. They offered to stop applying  
7 the whey formula as soon as the make allowance matches the  
8 price. In that sense they agree that zero is as low as it  
9 should go. We emphatically disagree, however, with their  
10 ultimate snubber concept that once it reaches zero, it  
11 stays zero forever.

12           Good policy, however, is not generated by  
13 emotional negative reactions to the suggestions of others.  
14 There are we believe excellent reasons to include a  
15 snubber in the formula. The most compelling argument for  
16 having the snubber is that without it innovation in whey  
17 protein concentrate product pricing could well be stifled,  
18 as is discussed above. Without a snubber a plant could  
19 well decide that the risk -- that the risk free production  
20 of skim whey powder is all that makes sense, especially if  
21 the net payout is never less than the make allowance  
22 amount.

23           Secondly, we are bit concerned that only 14  
24 percent of the whey proteins are converted to skim whey  
25 powder. It seems to us that with so few plants producing

1 skim whey powder, that this entire area could be subject  
2 to manipulation. For every pound of whey protein sold as  
3 skim whey powder, another six pounds are sold as whey  
4 protein concentrate in all its forms.

5           The best of all worlds for a plant making whey  
6 protein concentrate is to have a high make allowance for  
7 sweet whey powder and a low sweet whey powder price  
8 ideally below the make allowance amount. Under these  
9 conditions and without a snubber at zero, producers will  
10 be subsidizing all whey product production. Not only will  
11 the sweet whey powder plant be getting the full make  
12 allowance for their product; every whey protein  
13 concentrate plant will be getting its whey at a negative  
14 price, as in less than zero. In this situation there is  
15 little incentive to become efficient in processing sweet  
16 whey -- skim whey powder, nor in selling it aggressively.  
17 The combination of using nonfat dry milk costs for the  
18 basis of costing and the western whey price reports for  
19 value and a snubber at zero will combine to remove the  
20 temptation to manipulate and, more importantly, leave in  
21 place the incentive to innovate.

22           Milk Producers Council's alternative proposal for  
23 this hearing contained a suggestion to add whey protein  
24 concentrate to the 4b formula. We offered this, not to  
25 enhance the value of whey, but to address the concerns

1 expressed in the Dairy Institute's petition that skim whey  
2 powder production is not broadly representative of  
3 California whey usage and that dry whey prices are not  
4 well correlated with other whey products. We were fooled  
5 by the clever phraseology of the Dairy Institute's  
6 petition and too easily impressed by the Department's  
7 statistical analysis. Our intent, as stated above, is not  
8 to greatly enhance the value of whey in the current  
9 formula. We find it to be at a sensible level now. The  
10 cost factor we proposed, while not unreasonable for a  
11 large specialized whey protein concentrate plant, does not  
12 seem to fit the conditions here in California.  
13 Particularly troublesome is how the -- how to account for  
14 the added cost of handling the lactose permeate. That  
15 being said, if the only other option for us is removal of  
16 the whey factor from the 4b formula, we would support  
17 adding Whey Protein Concentrate 34 with a manufacturing  
18 cost allowance that is calculated to have made whey  
19 pricing neutral over the past five years.

20           In summary on the whey issues, MPC urges the  
21 Department to leave in place the whey value portion of the  
22 4b formula, to continue to base that price on the value of  
23 skim whey powder, to apply a manufacturing cost in that  
24 formula that is based on the manufacturing costs of nonfat  
25 dry milk in plants of the size that that cheese plant

1 would have had if they had dried all their whey plus the  
2 added costs of drying whey and, last but not least, that  
3 the whey value be snubbed at zero.

4 HEARING OFFICER KRUG: The witnesses, if I may  
5 interrupt, you have about -- a little over two minutes  
6 left of your allotted time. I see that you have about  
7 another three pages of your testimony, which is in another  
8 section. Would you like to summarize now, use your two  
9 and half minutes to finish up, come back later. I'll  
10 leave it to you.

11 MR. VAN DAM: I think we'd prefer coming back  
12 later. This stuff doesn't summarize well.

13 HEARING OFFICER KRUG: That's fine.

14 At this time does any of the panel members have  
15 questions for the witnesses?

16 Mr. Gossard?

17 AGRICULTURE ECONOMIST GOSSARD: (Shakes head.)

18 HEARING OFFICER KRUG: Ms. Reed?

19 SUPERVISING AUDITOR REED: No.

20 HEARING OFFICER KRUG: Mr. Gossard, that's a  
21 "no"?

22 AGRICULTURE ECONOMIST GOSSARD: Yes. I'll  
23 reserve questions till they complete their entire  
24 testimony.

25 HEARING OFFICER KRUG: Okay. Thank you.

1 Ms. Reed?

2 SUPERVISING AUDITOR REED: No, I don't.

3 HEARING OFFICER KRUG: Ms. Gates?

4 RESEARCH MANAGER II GATES: No.

5 HEARING OFFICER KRUG: Mr. Ikari?

6 DAIRY MARKETING BRANCH CHIEF IKARI: No.

7 HEARING OFFICER KRUG: Okay. Thank you very  
8 much.

9 Just so we don't forget later, would you like the  
10 opportunity to present a post-hearing brief?

11 MR. VANDEN HEUVEL: Yes, we would.

12 HEARING OFFICER KRUG: And that request is  
13 granted.

14 MR. VAN DAM: Thank you for the water.

15 DAIRY MARKETING BRANCH CHIEF IKARI: The last  
16 one.

17 MR. VAN DAM: Saved my life.

18 HEARING OFFICER KRUG: And the final alternative  
19 proposal will be presented by Land O'Lakes now.

20 Will the representatives of Land O'Lakes please  
21 approach.

22 Okay. Are the representatives of Land O'Lakes  
23 ready?

24 MR. WEGNER: We are.

25 HEARING OFFICER KRUG: Okay. Will you please

1 state your full names and spell your last name the record.

2 MR. WEGNER: My name's Tom Wegner W-e-g-n-e-r.

3 DR. GRUEBELE: My name is James Gruebele  
4 G-r-u-e-b-e-l-e.

5 HEARING OFFICER KRUG: Mr. Wegner, do you swear  
6 or affirm to tell the truth?

7 MR. WEGNER: I do.

8 HEARING OFFICER KRUG: Mr. Gruebele, do you swear  
9 or affirm to tell the truth?

10 DR. GRUEBELE: I do.

11 HEARING OFFICER KRUG: Are you both representing  
12 Land O'Lakes at this hearing today?

13 DR. GRUEBELE: Yes.

14 MR. WEGNER: We are.

15 HEARING OFFICER KRUG: Do you have any written  
16 statements or other things that you would like entered  
17 into the record at this time?

18 MR. WEGNER: I do. The statement that's been  
19 handed to you previously.

20 HEARING OFFICER KRUG: Okay. I have a document  
21 here labeled "Consolidated Public Hearing to Consider  
22 Amendments - Testimony of Tom Wegner, June 1st, 2006." It  
23 will be labeled Exhibit 62 and is now admitted into the  
24 record.

25 (Thereupon the above-referred document was



1 marked as Exhibit 62.)

2 HEARING OFFICER KRUG: You may proceed with your  
3 testimony.

4 MR. WEGNER: Thank you.

5 Mr. Hearing Officer and members of the panel, my  
6 name is Tom Wegner and I'm here to testify on behalf of  
7 Land O'Lakes. My business address is 4001 Lexington  
8 Avenue North, Arden Hills, Minnesota. My current title is  
9 Director of Economics and Dairy Policy. We want to thank  
10 the Department for promptly calling this hearing to  
11 address these issues of critical importance to all of our  
12 dairy producer members.

13 Land O'Lakes is a dairy cooperative with over  
14 3,300 dairy farmer member-owners. The cooperative has a  
15 national membership base whose members are pooled in a  
16 California State Program and six different federal orders.

17 Land O'Lakes members own and operate several  
18 cheese, butter powder and value added plants in the Upper  
19 Midwest, East and California. Currently our 275  
20 California member-owners supply us with over 15 million  
21 pounds of milk per day that are processed at our plants in  
22 Tulare and Orland.

23 I'm here to testify in support of our alternative  
24 proposal filed with the Department on April 27th, 2006,  
25 involving the whey portion of the Class 4b formula.

1           LOL supports increasing the whey make allowance  
2 to the level reported in the CDFA cost study, adjusting  
3 the allowance with updated energy and labor costs from the  
4 period January 2005 through September 2005 and adding a  
5 variable component based on the prevailing whey market  
6 price.

7           Land O'Lakes believes that the whey study  
8 conducted by CDFA is valid and the results should be used  
9 to adjust the whey make allowance from 20 cents to a base  
10 of 27.42 cents. After the last hearing the Department  
11 chose to raise the make allowance for whey from 17 cents  
12 to 20 cents even though the cost study prepared for the  
13 hearing revealed that the adjustment should have been much  
14 larger.

15           The inadequacy of this 20 cent make allowance for  
16 whey has been further exacerbated by the fact that prices  
17 for whey protein concentrates have declined while whey  
18 markets strengthened.

19           Currently the Class 4b formula reflects whey;  
20 but, in fact, a much larger proportion of the whey stream  
21 is converted into whey protein concentrates. This has  
22 been particularly problematic this year because of the  
23 general strength in the whey markets while whey protein  
24 concentrate prices, including WPC with 80 percent protein,  
25 have been weaker.

1           Additionally, we propose that this whey make  
2 allowance be variable and change as the whey market price  
3 rises or falls. When the western dry whey price as  
4 reported by dairy market news exceeds 27.42 cents, the  
5 whey make allowance would be adjusted upward by adding 50  
6 percent of the difference between the whey market price  
7 and 27.42 cents. But when the whey market falls below  
8 27.42 cents, the whey make allowance would be adjusted  
9 downward by the same 50 percent factor.

10           Simply, when the whey market is above 27.42 cents  
11 both the producers and cheese plants share in the game.  
12 By contrast, when whey markets fall below the base make  
13 allowance of 27.42 cents, both the producers and cheese  
14 plants would share in the loss.

15           The formal plan would be as follows. And I've  
16 listed the sections with the language here. I'm not going  
17 to read those specifically because they're quite clear  
18 from the pros.

19           Unless the whey make allowance is adjusted to  
20 reflect the weighted average cost for whey reported in the  
21 CDFA study, updated for the changes in energy labor costs  
22 from January 2005 through September 2005 and adjusted for  
23 monthly changes in the whey price, Land O'Lakes recommends  
24 completely eliminating a whey factor from the Class 4b  
25 formula.

1           In this next paragraph I'm making several small  
2 adjustments to the wording. And I'll explicitly note that  
3 in my post-hearing brief if I'm granted permission to  
4 submit one.

5           Land O'Lakes supports adjusting the make  
6 allowance for cheese and powder based upon CDFA adjusted  
7 weighted average costs including the energy and labor  
8 updates for the period January 2005 through September 2005  
9 for cheese and nonfat dry milk powder. Land O'Lakes  
10 recommends a change in the price adjusters for butter and  
11 cheese based upon audited survey results by CDFA. We  
12 recommend the price adjuster of 1.68 cents for butter and  
13 a price adjuster of 2.52 cents for cheese. On make  
14 allowances we support a continued make allowance of 15.6  
15 cents for butter, an adjustment in the make allowance to  
16 15.91 for powder, and an adjustment in the make allowance  
17 to 17.91 cents per pound for cheese.

18           Land O'Lakes participated in the Federal Milk  
19 Marketing Order hearing held in January 2006 to consider  
20 changes in the make allowance used -- make allowances used  
21 in the Class 3 and Class 4 formulas. We supported changes  
22 to update the make allowances for cheese, butter, powder  
23 and whey on an expedited basis. Many cooperatives and  
24 proprietary firms from across the U.S. participated and  
25 testified in support of updating the Federal Order make

1 allowances.

2           At this time the USDA has not yet issued their  
3 decision on the January 2006 hearing, but we anticipate  
4 and are hopeful that the USDA will release their decision  
5 soon. We cannot predict what changes, if any, USDA will  
6 recommend be made in the Class 3 and 4 formulas. But  
7 there is a strong likelihood that their could be  
8 significant adjustments in the make allowances for cheese  
9 and other dairy products.

10           Capacity issues:

11           As you well know, California milk production has  
12 been increasing very rapidly. February 2006 milk  
13 production increased by 6.7 percent and March production  
14 increased 6.2 percent over 2005 levels. The production  
15 increase in these two months alone is enough to fill a 6  
16 million pound per day plant.

17           With this volume increase, it is not surprising  
18 to find that the state's plant capacity is being  
19 pressured. We have heard reports of distressed milk  
20 getting dumped because of plants being too full to process  
21 the milk.

22           The relatively new CPI plant is operating at  
23 full capacity. The same appears to be true for the new  
24 Leprino plant in Lemoore.

25           Loss of plant capacity:

1           Meanwhile, there has been a loss of plant  
2 capacity in California. The recent plant closings  
3 include:

4           In 2005, the Gustine plant that handled 30 loads  
5 per day closed.

6           In 2004, the DFA plant that handled 20 loads per  
7 day closed.

8           In 2003, the Sorrento plant that handled 32 loads  
9 per day closed.

10           And in 2002, the Suprema plant that handled 26  
11 loads per day closed.

12           The total plant capacity lost amounts to 108  
13 loads per day or about 5.5 million pounds of milk per day.  
14 This is roughly the capacity of the CPI plant Tulare.  
15 This volume of lost plant capacity is significant in light  
16 of the continued growth of California's milk supply. Any  
17 additional loss in plant capacity would put more stress on  
18 the milk processing sector.

19           Without a significant adjustment in the make  
20 allowances, including whey, it would not be surprising to  
21 observe further decreases in plant capacity in California.

22           Equity issues:

23           As a result of these inadequate make allowances,  
24 Land O'Lakes producers are not earning a reasonable return  
25 on their invested capital, and have in fact incurred

1 losses on their invested capital.

2           By way of contrast, producers, either independent  
3 producers or producers that belong to a captive  
4 cooperative or producers who belong to a cooperative that  
5 have not invested in cheese operations, have benefited at  
6 the expense of Land O'Lakes members who have made a  
7 significant investment in a new cheese plant.

8           To highlight, the addition of the whey factor in  
9 the Class 4b formula has been costly to Land O'Lakes. The  
10 accompanying chart, which is at the end of the testimony  
11 labeled Attachment A, shows the disparity in the  
12 distribution of benefits from the increased Class 4b  
13 prices to Land O'Lakes producers and producers outside of  
14 Land O'Lakes. The share of the benefits from the  
15 increased Class 4b prices going to producers outside of  
16 Land O'Lakes far exceeds the share of the benefits to Land  
17 O'Lakes producers. This chart does not show the cost to  
18 Land O'Lakes producers due to inadequate or even negative  
19 returns on the huge investment in a new cheese operation.

20           Land O'Lakes members -- excuse me -- Land O'Lakes  
21 member-owners took the financial risk of building a new  
22 modern cheese facility in California. We realized the  
23 risks involved in building a new plant, including product  
24 quality, start-up problems, running at less than full  
25 capacity, and other operational challenges.

1           But in our case, there turned out to be  
2 significant risk associated with the change in the Class  
3 4b formula involving the addition of a whey factor. The  
4 addition of the whey factor has increased the cost of  
5 milk.

6           When Land O'Lakes made the decision to build a  
7 new cheese plant the whey factor was not included in the  
8 Class 4b formula. However, the addition of the whey  
9 factor had a direct impact on the return on investment.  
10 The addition of the whey factor combined with inadequate  
11 make allowances led directly to inadequate returns on  
12 investment from our new cheese operations and losses  
13 experienced by Land O'Lakes members. This change in the  
14 ground rules for the Class 4b formula has had a direct  
15 impact on all of California's cheese plants.

16           Land O'Lakes not only processes its own producer  
17 members' milk, but also receives and processes milk from  
18 non-member producers. As such, Land O'Lakes is performing  
19 an important balancing function in the state.

20           Still another equity issue is that the current  
21 make allowances and formulas for Class 4a and Class 4b  
22 milk result in unbalanced returns. The returns on  
23 investment for Land O'Lakes butter and powder operations  
24 are clearly much higher than for cheese operations. This  
25 raises significant questions about the direction of the



1 future investments in new plant operations in California.

2 Will this imbalance lead to a shift from cheese  
3 to butter and powder in California?

4 Federal Order Cheese Operations versus California  
5 Cheese Operations:

6 As mentioned earlier, USDA has not yet issued  
7 their decision on Federal Order make allowances. Based on  
8 the hearing record and the overwhelming support from the  
9 proponents, there is a very strong likelihood that the  
10 Class 3 and Class 4 prices in Federal Order markets will  
11 be lower than they are now. This will make California  
12 cheese plants even less competitive than is currently the  
13 case. Not only that, cheese plants in Federal Order  
14 markets can depool, an option not available to California  
15 cheese plants.

16 Additionally, California manufacturing plants  
17 face different and sometimes higher level operating costs  
18 than costs faced by plants in other states.  
19 Environmental, labor, transportation, and energy costs are  
20 all areas where the Upper Midwest operations may have a  
21 significant cost advantage over manufacturing operations  
22 in California. The challenges associated with the  
23 construction of a new plant, such as obtaining permits, is  
24 likely more costly in California than for constructing a  
25 similar operation in other states.

1           We have stated previously that handlers whose  
2 milk is depooled do not have to share the Class III  
3 revenue with other producers. This cannot be done in the  
4 same way in California. Our testimony at the January  
5 31st, 2005, hearing clearly identified the positive  
6 benefits of depooling by cheese plants in Federal Order  
7 markets. The ability to depool provides cheese plants in  
8 federal Order markets a significant advantage over  
9 California cheese plants. In light of these advantages,  
10 we were not surprised to observe that Hilmar recently  
11 chose to build their new cheese plant in Texas over  
12 California and that Glanbia chose to build in New Mexico  
13 over California.

14           Conclusions and summary:

15           To conclude, Land O'Lakes recommends the removal  
16 of the whey factor in the Class 4b formula if, as a result  
17 of this hearing, the cheese formula includes a whey  
18 snubber or if there's a failure to adjust the whey make  
19 allowance to reflect a cost justified value. In other  
20 words, if the whey factor were removed, whey would have no  
21 impact in the Class 4b formula regardless of the price of  
22 whey.

23           To restate, Land O'Lakes recommends using a whey  
24 factor only if the whey make allowance is adjusted on a  
25 cost justified basis and no snubber is implemented.

1           Land O'Lakes manufactures butter, powder and  
2 cheese. Our recent experience within the California State  
3 Program is that the net returns for butter and powder are  
4 significantly higher than for cheese. Land O'Lakes is  
5 urging the Department to reflect a balanced approach. The  
6 returns on investment for cheese and for butter powder  
7 operations should be very similar and both need to be  
8 adequate based on economic factors within the marketplace.  
9 Based upon our experience at Land O'Lakes, that is not the  
10 case today. Returns on butter powder operations are  
11 clearly superior to returns on cheese.

12           Currently, California's manufacturing plants are  
13 operating at full capacity to process the continued growth  
14 in milk production. If long-term returns to producers'  
15 investments in cheese plants do not improve, more cheese  
16 plants may cease operations, putting even more stress on  
17 the remaining plants.

18           Several proposals emphasize short-term  
19 enhancement of producer returns. Land O'Lakes urges the  
20 Department to consider producers' long-term returns as  
21 well. Ironically by further reducing long-term returns to  
22 manufacturing plants, the Department risks losing more  
23 manufacturing capacity, which could lead to even lower  
24 short-term producer returns as milk ends up being dumped  
25 or shipped out of state and sold at distressed milk

1 prices.

2           This concludes my testimony. And I would like  
3 the opportunity to file a post-hearing brief.

4           Thank you.

5           HEARING OFFICER KRUG: Your request to file a  
6 post-hearing brief is granted.

7           Do we have any questions for the witnesses from  
8 the panel?

9           Mr. Gossard?

10          AGRICULTURE ECONOMIST GOSSARD: How was your  
11 testimony developed and approved by Land O'Lakes?

12          MR. WEGNER: It has been reviewed by our Senior  
13 Vice President Alan Pierson, shared with our California  
14 members and board, shared within the management of Land  
15 O'Lakes.

16          AGRICULTURE ECONOMIST GOSSARD: Did Land O'Lakes  
17 experience any problem with an inability to process all  
18 its members' milk any time this year? In Land O'Lakes  
19 operations in California, I should specify.

20          MR. WEGNER: We've been able to process all of  
21 our members' milk in California, as I understand it.

22          DAIRY MARKETING BRANCH CHIEF IKARI: Let me ask a  
23 follow-up question to that.

24          How close have you come to reaching maximum  
25 capacity?

1 DR. GRUEBELE: My understanding that plants are  
2 relatively full at Tulare and Orland. But we are also  
3 applying outside milk. And that is also included. In  
4 other words we're handling not only our own members' milk,  
5 but outside producer-members -- non-members as well. And  
6 a first call would be to reduce some of the non-member  
7 milk if we had a problem converting our own  
8 producer-member milk into products.

9 DAIRY MARKETING BRANCH CHIEF IKARI: So if we had  
10 a surplus situation in a given month, could Land O'Lakes  
11 California operations handle it? What's your ability  
12 to --

13 DR. GRUEBELE: Are you talking about our own  
14 producer milk?

15 DAIRY MARKETING BRANCH CHIEF IKARI: No.

16 DR. GRUEBELE: Well, I --

17 DAIRY MARKETING BRANCH CHIEF IKARI: Surplus  
18 production beyond your supply, how much could you provide  
19 in terms of providing capacity to handle that?

20 DR. GRUEBELE: We're just about at full -- I mean  
21 we're operating full capacity now, relatively speaking.

22 DAIRY MARKETING BRANCH CHIEF IKARI: Okay.

23 DR. GRUEBELE: So the answer is no more.

24 HEARING OFFICER KRUG: Any additional questions  
25 for the witnesses?

1           AGRICULTURE ECONOMIST GOSSARD: Yes. You  
2 mentioned the advantage that processors have in Federal  
3 Orders where they can depool. An earlier witness spoke to  
4 changes in some of the Federal Orders regarding depooling.  
5 What, if anything, will this do to the advantage of cheese  
6 plants in Federal Orders?

7           MR. WEGNER: Well, the decision is in the  
8 recommended status right now. And as I understand it,  
9 it's limiting the amount of milk that can be pooled after  
10 you have depooled, so that it's the monthly change. I  
11 think in most of the orders the Central, the  
12 Eastern -- yeah, the Central, the Upper Midwest -- and  
13 then I can't remember which -- it's one that's further  
14 east -- the varying amounts are as much as 25 percent --  
15 or 125 percent of the previous month can be pooled again.  
16 So you'd be allowed essentially to depool 20 percent and  
17 not have any loss in pooling opportunity the next month.

18           I don't speak as an expert in that. I'd suggest  
19 you check in with the Department of dairy programs to get  
20 those decisions a little bit more clearly stated. They  
21 will have an impact on the depooling activity though in  
22 those three orders.

23           AGRICULTURE ECONOMIST GOSSARD: Thank you.

24           HEARING OFFICER KRUG: Ms. Reed, do you have any  
25 questions for the witnesses?

1 SUPERVISING AUDITOR REED: No, I don't.

2 HEARING OFFICER KRUG: Ms. Gates?

3 RESEARCH MANAGER II GATES: Yes, I do.

4 I just have one question. On page 6 of your  
5 testimony you speak to the net returns for butter and  
6 powder are significantly higher than for cheese in  
7 California. And with your proposal you're talking about,  
8 you know, the cost increasing from the 20 cents to the  
9 27.42. Is that what you're explaining as the difference  
10 in the cost or the returns? Is it just to the whey factor  
11 or are there other --

12 MR. WEGNER: I think it's to the cheese  
13 business in -- the cheese -- how do you say? -- the cheese  
14 complex in general, the byproduct being whey. The  
15 byproduct being whey, it's combined. It's definitely the  
16 cheese and the whey.

17 RESEARCH MANAGER II GATES: Okay. But your  
18 proposal only spoke to the whey piece of it --

19 MR. WEGNER: Correct.

20 RESEARCH MANAGER II GATES: -- not the cost --

21 MR. WEGNER: It spoke to the make allowance,  
22 yeah, adjusting the make allowance to the level of --

23 RESEARCH MANAGER II GATES: Okay. Thank you.

24 DR. GRUEBELE: The cost justified that were  
25 developed by the Department are being used for cheese as

1 well as whey.

2 RESEARCH MANAGER II GATES: As well as whey.

3 Okay. Thank you.

4 DAIRY MARKETING BRANCH CHIEF IKARI: I have a  
5 question to follow up that.

6 In that section where you talked about your  
7 returns are greater on cheese than butter and powder --

8 MR. WEGNER: The other way around.

9 DAIRY MARKETING BRANCH CHIEF IKARI: I'm sorry.  
10 I misstated that.

11 But how is the efficiency of your cheese  
12 operations relative to the industry -- the California  
13 industry versus your butter powder operations relative to  
14 the rest of the California industry?

15 MR. WEGNER: I'm unable to speak to the specifics  
16 of efficiency of both operations. Perhaps Jim can.

17 DR. GRUEBELE: I'm not clear. Are you saying  
18 that we have a deficiency versus other cheese operations?  
19 Is that what you're suggesting or -- is that what your  
20 question was?

21 DAIRY MARKETING BRANCH CHIEF IKARI: Well, you  
22 just said that your returns are greater for butter and  
23 powder.

24 DR. GRUEBELE: That is a true statement.

25 DAIRY MARKETING BRANCH CHIEF IKARI: My question



1 is: Is your butter powder operation more efficient  
2 relative to the California -- you know, the balance of the  
3 California processors versus the relative position of your  
4 operations on cheese?

5 DR. GRUEBELE: That's probably true, particularly  
6 since we have a front-end loaded cheese plant, you know,  
7 recently built, a lot of depreciation and interest. And  
8 certainly that is a consideration. Our butter and powder  
9 plants are relatively efficient relative to other plants  
10 that operate in the State of California.

11 DAIRY MARKETING BRANCH CHIEF IKARI: Okay. On  
12 page 3 you indicated your position on the various butter  
13 and cheese -- I want to say, your price adjuster and a  
14 whole bunch of things in terms of make allowance. But I  
15 didn't really see, and perhaps you could file in your  
16 post-hearing brief, the rationale in how you got there. I  
17 see what you're recommending. But I didn't really  
18 understand what was your rationale for arriving at those  
19 points.

20 DR. GRUEBELE: We will certainly do that in  
21 post-hearing brief elaborate on -- I assume you're talking  
22 about the make allowance adjustments in cheese and powder  
23 and also the --

24 DAIRY MARKETING BRANCH CHIEF IKARI: Yes, the  
25 fourth paragraph down where you have --

1 DR. GRUEBELE: -- recommendation for the price  
2 adjuster?

3 DAIRY MARKETING BRANCH CHIEF IKARI: Yes.

4 DR. GRUEBELE: We could elaborate in the  
5 post-hearing brief on --

6 DAIRY MARKETING BRANCH CHIEF IKARI: On Page 3,  
7 your fourth paragraph, yes.

8 DR. GRUEBELE: We understand.

9 DAIRY MARKETING BRANCH CHIEF IKARI: Okay And  
10 then on page 5 you also talk about you do receive  
11 non-member milk. And I wondered if you could provide us  
12 with information as to the relative volume of non-member  
13 milk that your plant receives.

14 DR. GRUEBELE: We could do that in post-hearing  
15 brief. I don't have those numbers here directly at hand.

16 DAIRY MARKETING BRANCH CHIEF IKARI: Thank you.

17 HEARING OFFICER KRUG: Are there any additional  
18 questions for these witnesses?

19 Okay. The witnesses are excused. Thank you very  
20 much for your testimony.

21 At this time we'll just take a quick five-minute  
22 break.

23 (Thereupon a recess was taken.)

24 HEARING OFFICER KRUG: All right. Could everyone  
25 return to your seats. We're about to reconvene.

1           The day's getting late. So if we could move  
2 along, we can get a little bit more done.

3           If the people in the back would please find your  
4 seats. Thank you very much.

5           Now is the portion of the hearing where we  
6 typically go into statements -- or public testimony.  
7 However, we have recently received three additional pieces  
8 of written testimony that will be entered into the record  
9 by the Department's witness, Ms. Cheryl Gilbertson.

10           Could you please proceed.

11           STAFF ANALYST GILBERTSON: I have three  
12 documents. One dated May 24th, from the Center on Race,  
13 Poverty & the Environment. A second dated May 11th, '06,  
14 from Bacchetti & Silva Dairy. And a third dated March  
15 31st, from Circle H Dairy Ranch, Incorporated.

16           HEARING OFFICER KRUG: Thank you very much, Ms.  
17 Gilbertson. If you'll present those, I will mark them and  
18 admit them into the record. And we will have copies of  
19 those letters shortly, certainly by the end of today's  
20 session.

21           Thank you.

22           Okay. The letter from the Center on Race,  
23 Poverty & the Environment is labeled Exhibit No. 63, and  
24 it is admitted into the record at this time.

25           (Thereupon the above-referred document was

1 marked as Exhibit 63.)

2 HEARING OFFICER KRUG: The letter from Bacchetti  
3 & Silva Dairy is labeled Exhibit No. 64, and it is  
4 admitted into the record at this time.

5 (Thereupon the above-referred document was  
6 marked as Exhibit 64.)

7 HEARING OFFICER KRUG: And the letter from Circle  
8 H Dairy Ranch, signed by Margo Souza, is labeled Exhibit  
9 No. 65, and it's now admitted into the record.

10 (Thereupon the above-referred document was  
11 marked as Exhibit 65.)

12 HEARING OFFICER KRUG: We'll now proceed with the  
13 public testimony section of this hearing.

14 And our first witness is a Benjamin Yale.

15 Mr. Yale, will you please come forward.

16 Okay. Mr. Yale, will you please state your full  
17 name and spell your last name for the record.

18 MR. YALE: It's Benjamin F. Yale. And it's  
19 spelled Y-a-l-e.

20 HEARING OFFICER KRUG: Mr. Yale, do you swear or  
21 affirm to tell the truth?

22 MR. YALE: Yes, I do.

23 HEARING OFFICER KRUG: Are you representing any  
24 organization today?

25 MR. YALE: I'm here on behalf of Select Milk