

**IN THE UNITED STATES DISTRICT COURT  
FOR THE DISTRICT OF COLUMBIA**

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Select Milk Producers, Inc., Elite Milk Producers,  
Inc., Continental Dairy Products, Inc.

Plaintiffs,

v.

Dan Glickman, Secretary  
United States Department of Agriculture,

Defendant.

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Civ. No. 1:01-CV-00060 (RCL)

**MEMORANDUM OF POINTS AND AUTHORITIES IN SUPPORT OF  
PLAINTIFFS' MOTION FOR TEMPORARY RESTRAINING ORDER  
AND/OR PRELIMINARY INJUNCTION AND FOR EXPEDITED HEARING**

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**MEMORANDUM OF POINTS AND AUTHORITIES IN SUPPORT OF  
PLAINTIFFS' MOTION FOR TEMPORARY RESTRAINING ORDER  
AND/OR PRELIMINARY INJUNCTION**

**I. Introduction**

Plaintiffs, Elite Milk Producers, Inc., Select Milk Producers, Inc., and Continental Dairy Products, Inc. (collectively "Milk Producers"), seek an injunction to maintain the status quo in the pricing of milk under the Federal Milk Marketing Orders until the Court has time to fully review the Milk Producers' challenges to the Secretary's creation of a separate Class III Butterfat Price provision. 65 Fed. Reg. 76832 (December 7, 2000) ("Tentative Final Decision") (Exhibit "A") and 65 Fed. Reg. 82832 (December 28, 2000) ("Interim Amendment of Orders"). (Exhibit "B").

Milk Producers were denied the most fundamental due process rights and an opportunity to be heard on an economically significant amendment creating a separate Class III Butterfat Price in the Federal Milk Marketing Orders. Without an order enjoining the implementation of this provision, the Milk Producers will be subject to irreparable losses in the form of non-recoverable reductions in minimum prices plants pay for new milk as required by various Federal Milk Marketing Orders and disorderly marketing conditions in which to sell their milk.

The Class III Butterfat Price is unlawful, and its implementation should be enjoined, because (1) it was never proposed as a possible amendment to the Federal Milk Marketing Orders nor was it made part of the scope of a formal rulemaking proceeding, (2) no less than three separate offices of the Secretary agreed at the public rulemaking hearing that a proposal for a separate Class III Butterfat Price was not within the scope of the hearing, (3) all participants in the rulemaking proceeding, including the Milk Producers did not analyze or address the merits and operation of separate Class III Butterfat Prices, (4) the adopted proposal for a separate Class III Butterfat Price surfaced only after the period for all public comment was closed, and (5) the Secretary failed to consider the

severe impact the proposal has on the Class I prices and the provision is otherwise arbitrary, capricious, and not in accordance with the law.

An injunction is urgently needed now to stay the implementation of this illegal rule and maintain the status quo because on February 2, 2001, the Secretary will announce, unless enjoined, the new separate Class III Butterfat Price along with the minimum prices for all classes of milk to be paid by plants for milk already delivered in the month of January 2001. Once the price is announced and this provision is implemented retroactively for January milk deliveries, it thereafter cannot be undone. Further, once implemented it cannot be “unimplemented” for future months.

Implementation of the separate Class III Butterfat Price will permanently, and irretrievably reduce the income to Milk Producers and other producers under the Federal Milk Marketing Orders by as much as \$400 million per year. The amount of Plaintiffs’ annual loss alone is estimated alone to be as much as several million dollars. Nationwide, the loss for January 2001 will be approximately \$5 million. (Declaration, Mary Ledman ¶¶ 3, 4, 5, 12, 13, 14, 16, 18, 19, 20 (Exhibit “C”)). These are losses directly resulting from reduced payments plants (buyers) will be required to pay the under the various Federal Milk Marketing Orders as a result of the rogue provision for Class III Butterfat Price. Once the plants pay the minimum price as announced for the month, the plants will not be liable for any additional payment for that month in response to subsequent correction of the minimum pricing regulations. The plants will have already, in turn, priced their products to their customers based upon that announced Federal Order price. No claim for damages will be against the government without a waiver of sovereign immunity.

As a matter of law, and of practicality, a subsequent judgment by this Court in favor of the Milk Producers cannot, and will not, redress the losses the illegal Class III Butterfat Price provision will impose upon the Milk Producers.

The Separate Class III Butterfat Price provision is not the product of lawful rulemaking. The Agriculture Marketing Agreement Act of 1937, 7 U.S.C. §601 *et seq.*, (AMAA) requires that all amendments to the Federal Milk Marketing Orders be made only as the result of formal, on the record, rulemaking. The Secretary has established regulations for holding these hearings. 7 C.F.R. §§ 900.1-900.18. As part of this procedure the hearings are limited to issues within the scope of the hearing— a scope that is delineated by the specific proposals noticed for hearing. The Notice of Hearing (Exhibit “D”) in this case did not identify any proposed amendment to those sections of the Federal Milk Marketing Orders that defined the butterfat price used for Class III milk. The Secretary agreed that it was not within the scope of the rulemaking proceeding when he said that a proposal to amend the regulations to create a separate Class III Butterfat Price was “not one of the proposals being considered at this hearing .”<sup>1</sup> (Transcript of Hearing, May 9, 2000, Exhibit “E”).

To avoid this litigation, the Milk Producers formally requested that the Secretary stay implementation of the Class III Butterfat Price provisions. (Exhibit “F”). The Secretary ignored the request and published the Interim Amendment to the Rules on December 28, 2000. (Exhibit “B”). Thereafter, on January 5, 2001, he denied the Milk Producers’ request for the stay. (Exhibit “G”). Upon receipt of that denial on January 11, the Milk Producers were unfortunately forced to file a complaint and seek this extraordinary relief in order to forestall irreparable loss to them and other producers.

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<sup>1</sup> The transcripts of the hearing can be viewed at the USDA/AMS Website at [http://www.ams.usda.gov/dairy/exh\\_hear.htm](http://www.ams.usda.gov/dairy/exh_hear.htm)

## **II. Background**

### **A. The Federal Milk Marketing Order Program**

Congress established Federal Milk Marketing Orders in the Agricultural Marketing Agreement Act of 1937, (“AMAA”) 7 U.S.C. § 601 et seq. in part “to raise producer prices”. *Block v. Community Nutrition Inst.*, 467 U.S. 340, 342 (1980). In 1999, Congress reiterated this purpose when it directed the Secretary to implement “Option 1A” or the higher Class I pricing option considered by the Secretary, found the Class III and IV prices unsatisfactory, and directed the Secretary to hold an emergency rulemaking hearing on Class III and IV prices with implementation on January 1, 2001. H.R. 3428. Consolidated Appropriations Act, 2000, Pub.L. 106-113, Div. B, §1000(a)(8), Nov. 29, 1999, 113 Stat. 1536, 1501A-518 (“2000 Act”).

The AMAA gives the Secretary the authority to fix minimum prices which all “handlers” (processors or buyers) must pay for milk purchased from individual producers or cooperative associations of producers. With this authority, the Secretary has established eleven Federal Milk Marketing Orders covering much of the United States population with the significant exception of California. The general regulations, including formulas, are spelled out at 7 C.F.R. Part 1000 and individual order provisions are found at 7 C.F.R. Parts 1001 through 1135. These provisions define: the “marketing areas”; buyers of milk who are “regulated” and subject to the minimum payments; the dairy farmers who are “producers” qualified to receive payment in the form of a “uniform price” from the “producer settlement fund”; how payments are made to and from that fund; what “minimum prices” buyers must pay to that fund; how producers are paid from that fund; and other related provisions.

The fundamental premise of the Federal Milk Marketing Orders has been, and remains, the use of a two-tiered pricing system, i.e., plants pay based upon the use of the milk (to make butter, cheese,

creams, bottled milk, etc.) and producers receive a uniform price irrespective of the end use of their milk.

As of January 2000, each of the Federal Milk Marketing Orders classified milk into four “uses” or “classes”— Class I is beverage milk, Class II is milk used in creams and yogurt and similar products, Class III is milk used in cheese production, and Class IV is milk used for non-fat dry milk and butter. Each month, the handlers must pay to a producer settlement fund the minimum price established for each use. *Zuber v. Allen*, 396 U.S. 168, 179 (1969) .

Historically minimum milk prices were announced as a price per hundred weight at a standardized 3.5% butterfat test (“3.5 price”). Plants paid the producer settlement fund a price that was adjusted by a “butterfat differential” to reflect the actual butterfat test received. This income from the handlers was blended and producers were paid at a uniform test, again expressed as a 3.5 price. Actual producer payments were adjusted to reflect their respective butterfat test by a producer butterfat differential. 7 U.S.C. § 608c(5)(A) & (B), *Zuber v. Allen*, 396 U.S. 168, 172-173, 177-178 (1969); *Stark v. Wickard*, 321 U.S. 288, 291-295 (1944).

Since January 2000, pricing for milk and the calculation of producer payments has become far more complex as prices are expressed in terms of skim or multiple component prices rather than the 3.5 price. Payment by plants for some classes of milk (not Class I) and to producers in some orders, is now made on the basis of per pound prices for the milk components – butterfat, protein, other solids, solids not fat and a small amount on a per hundred weight basis for the “water carrier” called a “Producer Price Differential.” This movement towards pricing more components than weight and butterfat test has led to increased complexity. So much complexity, as we explain later, that even the Secretary did his economic analysis on the basis of a 3.5 Price and a single Class I mover and,

as a result, failed to identify the severe problem with the implementation of the separate Class III Butterfat Price when applied to real world actual weights and tests.

To reduce some of the complexity, the industry still describes the class prices and the “blend” or uniform price in terms of a 3.5 Price rather than the component prices. The Secretary specifies in the regulations how to do just that. 7 C.F.R. §1000.50. Though comparison of such “statistical prices” with historical prices is helpful, these artificial prices mask what is actually happening in prices paid by plants and received by producers.

Since January 2000, the Class III and Class IV skim prices drive or “move” the other two classes. The Secretary determines the values for Class III and IV milk each month based upon a process called “component pricing” or “end product pricing” wherein the announced market prices of selected dairy commodities — butter, block and barrel cheddar cheese, dry whey, and non fat dry milk — are converted into four milk component prices — butterfat, protein, other solids, and solids-not-fat respectively. The Class III skim price is the sum of protein and, other solid values. The Class IV skim price is the solids not fat value. Prior to the Tentative Final Decision, the butterfat price was the same for Classes III and IV. They differed only in their skim price. The Tentative Final Decision proposes to establish separate butterfat prices for each class with the Class III derived from the cheese price and Class IV from the butter price. It is that decision that is the focus of this lawsuit.

The term “Class III Butterfat Price” refers to a price that is computed based upon the value of butter in cheddar cheese which is a function of the cheese price. “Class IV Butterfat Price”, on the other hand, is derived from the price of butter as a separate product. These are referenced respectively as the “cheese butter price” and the “butter price” which are more descriptive of the difference.

Prior to the Tentative Final Decision, the Class III and IV prices only differed in their *skim milk* value as they both used the same butterfat price. As a result, the “higher of” Class III or Class IV meant the higher of their skim price. As a result, use of the appropriate “mover” would always yield the highest price for Class I milk irrespective of the plant’s actual butterfat test.

Interjection of the new, separate, Class III Butterfat Price into the equation changes that. Now, the Class I “mover” is determined by comparing a theoretical Class III 3.5 Price with 3.5% butterfat with a Class IV 3.5 Price. Whichever of these is higher is the Class I mover. Because the ratio of skim value to butterfat value in Class III is much lower than that ratio in Class IV and because Class I milk only has a butterfat test in the range of 1.6 to 2.3%, *virtually everytime the Class III is chosen to be the Class I mover, the actual Class I prices for plants will be significantly lower.* (Ledman Decl. ¶¶ 14-15). The Secretary did not consider the actual impact of Class III as the mover and, as a result, did not comprehend the severe consequences of this pricing scheme. 67 Fed. Reg. 76832, 76846-47).

There are also losses in the Class III price itself, though not so severe. The use of a Class III Butterfat Price reduces the prices on all milk in the Federal Milk Marketing Orders by approximately \$5 million dollars per month. (Ledman Decl. ¶¶ 12, 19) .

## **B. The Rulemaking Process**

In order to address changing market conditions in the dairy industry, the Federal Milk Marketing Orders are routinely amended. The AMAA itself provides: “Whenever the Secretary of Agriculture has reason to believe that the issuance of an order will tend to effectuate the declared policy of this chapter with respect to any commodity or product thereof specified in subsection (2) of this section, he shall give due notice of and an opportunity for a hearing *upon a proposed order.*” 7 U.S.C. §608c(3) [emphasis added]. The term “proposed order” also means “proposed amendment to an

order”. 7 C.F.R. § 900.1(j) (“The term marketing order means any order or any amendment thereto...”).

The Secretary has promulgated regulations governing the amendatory process. 7 C.F.R. §§ 900.1- 900.18 . The regulations are promulgated in formal, on the record, rulemaking hearings. The hearings are commenced with a “Notice of Hearing” which “...*shall define the scope of the hearing* as specifically as may be practicable; shall contain either the terms or substance of the proposed ... [amendment to the] marketing order or a description of the subjects and issues involved...” 7 C.F.R. §900.4(a). It has long been the practice of the Secretary to specify the sections in the Federal Milk Marketing Orders that are subject to change in the rulemaking process. See, for example, the Notice of hearing proposed No. 1 which specified C.F.R. Section and proposed language. Thus, those provisions of the Federal Milk Marketing Orders not specified in the scope of the hearing notice are not subject to change as a result of that rulemaking proceeding.

An Administrative Law Judge (ALJ) presides at the hearing. Among his duties, the ALJ insures that the hearing is limited to the scope as defined in the Notice of Hearing. 7 C.F.R. §900.6(b). The regulations also provide that, “Evidence shall then be received with respect to the matters specified in the notice of the hearing...” 7 C.F.R. §900.8(c)(2). Witnesses testify under oath and are subject to cross examination. 7 C.F.R. §900.8(d)(1).

After the close of evidence parties are afforded an opportunity to file written arguments. 7 C.F.R. §900.9(b). The judge certifies the hearing transcript, (7 C.F.R. §900.10) and thereafter the Secretary issues a recommended decision. 7 C.F.R. §900.12. The decision shall contain an “appropriate proposed ...marketing order...” *Id.*

### **C. Proceedings Relevant to the Class III Butterfat Price**

The hearing that is the focus of this proceeding was indeed unique-- it was Congressionally mandated in special legislation to correct previous rulemaking errors by the Secretary. In response to 7 U.S.C. §7251-7255, (FAIR Act of 1996), the Secretary conducted a formal rulemaking and adopted the current component pricing and four class scheme on January 1, 2000. 64 Fed. Reg. 70867 (December 17, 1999). He continued the historic use of a single butterfat price for all classes.

Various producer groups, including the Milk Producers, challenged these proposed formulas for Class III and IV prices in the courts and in Congress. The litigation was in several courts around the country including this Court. *Southeast Dairy Farmers Association, v. Dan Glickman*, (Civ. No. 1:99-CV-02459 (EGS); dismissed as moot due to passage of the 2000 Act noted, *infra*). During the course of the litigation, one court enjoined the implementation of the regulations the Secretary had promulgated under the FAIR Act. *St. Albans Cooperative Creamery, Inc., v. Dan Glickman*, 68 F. Supp.2d 380 (D. Ct. 1999).

In the midst of this litigation, Congress itself addressed the producers' concerns legislatively. In the 2000 Act, Congress specifically found that the Secretary had, *inter alia*, erred in promulgating the Class III and IV prices. As a result, it ordered the Secretary to (a) conduct formal rulemaking to reconsider these prices; (b) publish a "final decision" in the Federal Register "on December 1, 2000," and (c) implement it by January 1, 2001. H.R. 3428, as part of Consolidated Appropriations Act,

Act) states in relevant part:

**SEC. 2. FURTHER RULEMAKING TO DEVELOP PRICING METHODS FOR CLASS III AND CLASS IV MILK UNDER MARKETING ORDERS.**

(a) CONGRESSIONAL FINDING- The Class III and Class IV milk pricing formulas included in the final decision for the consolidation and reform of Federal milk marketing orders, as published in the Federal Register on April 2, 1999 (64 Fed. Reg. 16025), do not adequately reflect public comment on the original proposed rule published in the Federal Register on January 30, 1998 (63 Fed. Reg. 4802), and are sufficiently different from the proposed rule and any comments submitted with regard to the proposed rule that further emergency rulemaking is merited.

(b) RULEMAKING REQUIRED- The Secretary of Agriculture shall conduct rulemaking, on the record after an opportunity for an agency hearing, to reconsider the Class III and Class IV milk pricing formulas included in the final rule for the consolidation and reform of Federal milk marketing orders that was published in the Federal Register on September 1, 1999 (64 Fed. Reg. 47897-48021).

(c) TIME PERIOD FOR RULEMAKING- On December 1, 2000, the Secretary of Agriculture shall publish in the Federal Register a final decision on the Class III and Class IV milk pricing formulas. The resulting formulas shall take effect, and be implemented by the Secretary, on January 1, 2001.

(d) EFFECT OF COURT ORDER- The actions authorized by subsections (b) and (c) are intended to ensure the timely publication and implementation of new pricing formulas for Class III and Class IV milk. In the event that the Secretary of Agriculture is enjoined or otherwise restrained by a court order from implementing a final decision within the time period specified in subsection (c), the length of time for which that injunction or other restraining order is effective shall be added to the time limitations specified in subsection (c) thereby extending those time limitations by a period of time equal to the period of time for which the injunction or other restraining order is effective.

\* \* \*

2000 Act §2.

On January 31, 2000, in response to the 2000 Act, the Secretary requested proposals for changes in the Class III and IV make allowances. (Exhibit H) Thirty two interested parties submitted proposals. The Secretary reviewed the proposals and noticed those that tended to effectuate the purpose of the AMAA. 64 Fed Reg 20094-20104 (April 14, 2000) (Notice of Hearing) (Exhibit D). The Notice of Hearing consolidated some of the proposals, and grouped them according to the provisions to be modified. In total there were 31 numbered proposals from the industry. The Secretary labeled these proposals as “proposed amendments”. Id. at 20100. There were no proposed amendments to create a separate Class III Butterfat Price.

Proposals number 1 through 29 all specified changes only to 7 C.F.R. §1000.50 with its specific provisions regarding product prices, make allowances and yields. Proposal 30 requested that any changes in the Class III and Class IV prices not increase the Class I mover. Proposal 31 suggested essentially the same thing as regards Class II. These latter proposals were rejected by the Secretary. 65 Fed. Reg. 76848. The noticed proposals were very specific as to what was to be changed. They were expressed as fine as single words or numbers in sub-subsections of 7 C.F.R. §1000.50.

The Secretary also issued his own proposal, (proposal number 32), which read, “make such changes as may be necessary to make the entire marketing agreements and the orders conform with any amendments thereto that may result from this hearing.” 65 Fed. Reg. 200094, 20103. This standard provision, the “conforming language proposal”, is typically included in all such hearing notices and is intended to put parties on notice that the Secretary may make technical changes in other provisions, not within the scope of the Notice of Hearing, in order to effectuate the approved amendments. This is not a carte blanche notice that all of the provisions in each of the eleven

Federal Milk Marketing Orders are subject to any modification the Secretary, himself, may divine.

As Gregory Cooper, Esq., Office of the General Counsel, USDA, stated at the close of the hearing:

17 MR. COOPER: We have Department Proposal No. 32,  
18 which is to make any necessary conforming changes and other  
19 provisions to the orders as a result of the amendments may  
20 take place as a result of this hearing, and it's a rather  
21 technical proposal and no testimony is necessary on it.

Hearing Transcript 1844.

Though none of the 31 proposed amendments in the Notice of Hearing included the creation of a separate Class III Butterfat Price, there were several that called for an adjustment in the price of butter used to compute the butterfat price for Class IV milk only. The butter price, not the cheese butter price, would continue to be the basis for all of the classes' butterfat prices. Nevertheless, the Secretary viewed a reduction in the value of the Class IV butterfat price as a deviation from the single butterfat price based on the butter price. As a result he added the following, very unusual, statement in the Notice of Hearing.

### **Class III and Producer Butterfat Prices**

Proposals to change the Class IV butterfat price that would not also result in changes to the Class III butterfat price raise the issue of whether the butterfat price for milk used in Class III should be based directly on the value of butterfat in cheese instead of the value of butterfat in butter. One of the primary considerations for incorporating some of the value of butterfat in cheese into the protein price was to maintain a single butterfat price for milk used in manufactured products. ***Changing the protein price calculation to reflect only the value of protein in cheese, with a separate Class III butterfat price calculation is an issue that should be considered at the same time as the proposals to reduce the Class IV butterfat price.*** Data and testimony concerning yield factors specific to butterfat in cheese would be appropriate additions to the hearing record.

65 Fed. Reg. 200094, 20103. [Emphasis added].

This statement did not identify any regulation proposed to be amended. Because this was not a “proposed amendment” and there was no specific formula advanced for such a separate Class III Butterfat Price the language appeared more as a statement that evidence or testimony to support changing the Class IV Butterfat price for Class IV only also needed to include evidence as to how that could be accomplished without undermining the existing single butterfat pricing scheme so as to justify multiple butterfat pricing provisions. In essence, a hurdle, nearly impossible, was raised for those proposing to the reduce the Class IV Butterfat Price while leaving the others the same.

As explained later, the only substantive proposed amendment to the Federal Milk Marketing Orders for a separate Class III Butterfat Price based upon a cheese butter price was ruled out of the scope of the proceeding. In the end, the Secretary in the Tentative Final Decision neither reduced the Class IV butterfat price nor did he change the yields in the protein formula.

#### **D. The Response to a Proposals for a Class III Butterfat Price at the Hearing**

Though the Secretary did not propose an amendment to the Federal Milk Marketing Orders that would create separate a Class III Butterfat Price and there was no such proposal from the industry in the Notice of Hearing, one person did attempt to propose in the hearing process a formula that would price butterfat used in Class III separate from that used in the other classes.

On April 24, 2000, two weeks prior to the hearing and after the deadline for submitting proposed amendments had expired, Dr. David Barbano, a Cornell University professor with expertise in cheese production, proposed his own cheese-butter price formula that would, if adopted, price Class III butterfat separately from Class IV. This proposal, which actually differed markedly from the cheese-price formula that the Secretary eventually adopted, included extensive discussion, explanatory and exemplary spread sheets, and a milk price “calculator.” He published this material on the Internet. *See*, <http://www.cpdmp.cornell.edu/CPDMP/Pages/FMMO>. (Decl. Dr. David

Barbano, Exhibit I). His proposal was not noticed as a proposed amendment in the Notice of Hearing nor did the Secretary supplement the Notice of Hearing to include it.

The five (5) day hearing convened on May 8, 2000 in Alexandria, Virginia with the Hon. James W. Hunt presiding. Several government witnesses took the stand to provide data and reports prepared by various agencies of the Secretary. Industry witnesses testified on behalf of their positions. No one proposed a separate Class III Butterfat Price on the first day of the hearing.

On the second day, Dr. Barbano took the stand to testify on behalf of his proposal. Several parties objected to his proposal as outside the scope of the hearing as delineated in the Notice of Hearing. Milk Producers specifically questioned whether it might be within the scope of the Notice of Hearing. That suggestion was soundly rejected by the ALJ and the Secretary's representative.

The transcript records the Secretary's position on those motions to strike as follows:

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19 JUDGE HUNT: *Well, we don't have unlimited*

20 *discretion to testify to anything that somebody wants to*

21 *testify. It has to be within the scope of the hearing. And*

22 *on that, I would like to have the Department address the*

23 *point, either Mr. [Gregory] Cooper [Office of General Counsel USDA] or Ms.*

*[Connie] Brenner [Order Formulation, Dairy Programs].*

24 MR. COOPER: . . .

25 . . . So I have no idea what Mr. Barbano -- Dr.

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1 Barbano is going to say today. From the few conversations I

2 have had in the last few minutes about what he is going to

3 say, it would seem to be that he may have labeled things as  
4 proposals which are beyond the scope of the hearing notice.  
5 But at the same time, the information that he is  
6 giving there may also be useful with regard to existing  
7 proposals or with the request at the end of the hearing  
8 notice as to studying the effects of how all this relates to  
9 the Class III price. And to the extent that there may be a  
10 proposal that wasn't noticed and is not just a modification  
11 of the other proposal, I agree that we can strike it at the  
12 end to that extent.

13 To the extent he has information that may be  
14 valuable in setting the butterfat prices and considering the  
15 yields and such, that information can be received. So I  
16 would suggest that we hear his testimony. And then anyone  
17 who wants to strike portions of it can fire away. And we  
18 will make up our minds then.

Transcript at 510-511. [Emphasis added]. Initially the ALJ reserved his ruling.

7 JUDGE HUNT: . . .  
8 . . .I will defer to Mr. Cooper as being the  
9 Department -- the Secretary's representative. And as the  
10 Secretary's representative here along with Ms. Brenner, I  
11 assume that they will know what is -- when they review the  
12 record what is within the scope of the hearing as

13 appropriate for consideration, what is not.

14 And after -- I will allow Dr. Barbano to testify.

15 After his testimony and questions, anyone can move to strike

16 and I will rule on those motions at that time. All right.

17 Dr. Barbano, if you would state and spell your name for the

18 record, please.

Hearing Transcript at 512.

At the close of Dr. Barbano's testimony, parties renewed their motions to strike his proposal for a separate Class III butterfat price. The ALJ ruled as follows:

16 JUDGE HUNT: *I'm going to rule that Dr. Barbano's*

17 *pricing formula is not one of the proposals being considered*

18 *at this hearing*. Although there's a lot of testimony and

19 comments on it, that is not a proposal being considered.

20 However, he has provided information in his

21 testimony that's germane to the proposals being considered,

22 and so I will allow Dr. Barbano's testimony to remain in the

23 record and, as Mr. Cooper suggested earlier, **leave it to the**

24 **Secretary's representatives who will make the determination**

25 **on the final rule to disregard that part of Dr. Barbano's**

1 **testimony that's not pertinent to the proposals under**

2 **consideration**.

Transcript at 790-791 [Emphasis added].

This ruling signaled to participants that the scope of the hearing did not include amendments that would create a separate Class III Butterfat Price. (Barbano, ¶5). Clearly, the ALJ, the Secretary's representative from the Office of General Counsel, and the Secretary's representative from Dairy Programs, stated that not only was Dr. Barbano's proposal out of order, any such proposal for a cheese butter price to set the Class III Butterfat Price would be out of order. Further, the Secretary had now given context to the paragraph following proposal 32 in his Notice of Hearing (see p. 13, *supra*) and explained that it was not a proposed amendment but merely instructive on what might be helpful testimony in relation to other amendments that were actually proposed.

During the balance of the hearing, no participant testified, or offered any evidence or argument promoting the use of a cheese butter price as a separate Class III butterfat price. See, *e.g.* Brown ¶6.

After the public hearing, written arguments were solicited, and the hearing record was closed. Thereafter, the Secretary issued a "Tentative Final Decision". 65 Fed. Reg. 76831 (December 7, 2000). Exhibit A. This Tentative Final Decision: (1) rejected all proposals to create a lower butterfat price for Class IV, (2) slightly modified the yields and make allowance for the product pricing formula, (3) conformed some product classifications to the reality of how they were made or used, and (4) to the surprise of all participants, broke from the historical use of a single butterfat price to establish a separate Class III Butterfat Price provision— an amendment ruled outside the scope of the hearing. 65 Fed. Reg. 76832 (December 7, 2000). Barbano ¶6, Brown ¶9.

The Tentative Final Decision not only proposed changes to 7 C.F.R. §1000.50 as indicated in the Notice of Hearing but also 7 C.F.R. §1000.40 (Classifications) and sections .60 (Handler's value of milk), .61 (Computation of producer butterfat price and producer price differential), .62 (Announcement of producer price), .71 (Payments to the producer settlement fund), .73 (Payments to producers and to cooperative associations) of each of the eleven parts that describe the various

Federal Milk Marketing Orders. 7 C.F.R. Parts 1001 - 1135. So extensive were the provisions related to the Class III Butterfat Price that of the approximately nine pages of amendments, less than one dealt with the changes to \$1000.50, the only one noticed for change. 65 Fed. Reg. 76852 - 76861.

In response to this extraordinary modification of sections not in the Notice of Hearing, nor otherwise proposed for scrutiny and comment, the National Cheese Institute (“NCI”) (a trade association which has over 75 member companies that manufacture more than 80 percent of the cheese consumed in the U.S. (Transcript 251)) and the Milk Producers formally requested an administrative stay of the Tentative Final Decision. (Exhibit F and J). The Secretary denied the NCI request on December 21, 2000 (Exhibit K) and denied the Milk Producers request on January 5, 2001. (Exhibit G). Milk Producers did not receive their denial letter until January 11 and, on that date, filed the instant lawsuit.

#### **E. Impact of the Tentative Final Decision**

The use of a Class III Butterfat Price in the pricing scheme that is now part of the Federal Milk Marketing Orders will reduce the value of skim milk used in Class I by more than any offsetting increase in the butterfat value. This reduction in skim value will severely reduce the minimum prices plants will have to pay for Class I milk during those months in which the Class III price moves the Class I price. Ledman ¶ 6, 14. Under normal marketing conditions, such as 1999, the Class III should “move” the Class I price for as many months as the Class IV acts as the mover. Ledman ¶ 17. The annual dollar impact on producers under the Federal Milk Marketing Orders is a loss approximating \$400 million per year! Ledman ¶ 16. This money cannot be recouped from the handlers nor is the Secretary because of his sovereign immunity liable to pay producers for these losses.

The losses come in two classes— Class I and Class III. There is a quantifiable loss associated with Class III and the Tentative Final Decision. When the Tentative Final Decision pricing formula are applied to the real content of producer milk rather than a hypothetical 3.5% butterfat, the value of Class III is reduced in all of the Federal Milk Marketing Orders by about \$6 million per month. Ledman ¶ 19. This is a loss that will begin for milk marketed in January 2001 when the Secretary issues his price announcement on February 2.

The loss in Class I arises in those months when the Class III price moves Class I. This should occur approximately one half of the time. (Decl. Ledman ¶ 17) . This is because the mover is chosen based upon the higher of Class III or Class IV prices at a theoretical 3.5% butterfat test. In reality, however, plants will pay for Class I milk at a test of 1.8% to 2.3% butterfat. At the actual butterfat test, the Class IV skim and fat price would exceed that of the Class III skim and fat prices. The estimated losses in Class I value average about \$65 million for the months that the Class III is the mover.

The Secretary totally missed (or simply ignored) this crucial result. According to his economic analysis, he never projected a blend price when the Class III was the mover. In “Economic Analysis for the Tentative Final Decision on Class III and Class IV Price Formulas,” December 2000, (Exhibit “L”) the Secretary never considered the impact of the new Class III Butterfat Price; particularly where Class III became the price mover. “With the decision formulas, the Class I base price is the Class IV price in all years of the analytical period.” *Id.* at p.8.

The economic loss is not subject to a legal remedy. Money damages cannot be obtained because it is third-party plants that pay the federally established prices, not the Secretary. No public money is used to fund the producer settlement fund and sovereign immunity shields the government from liability..

### **III. Milk Producers are Entitled to Injunctive Relief.**

#### **A. This Court has the Authority to enjoin the Secretary from implementing the Separate Class III Butterfat Test.**

The Administrative Procedure Act provides that the Court may enjoin implementation pending judicial review.

\* \* \*On such conditions as may be required and to the extent necessary to prevent irreparable injury, the reviewing court, including the court to which a case may be taken on appeal from or on application for certiorari or other writ to a reviewing court, may issue all necessary and appropriate process to postpone the effective date of an agency action or to preserve status or rights pending conclusion of the review proceedings.

5 U.S.C. §705.

The standards for imposing a stay under this statute are the same as those for a preliminary injunction. *Corning Sav. and Loan Ass'n v. Federal Home Loan Bank Bd.*, 562 F.Supp. 279 (E.D.Ark.1983).

Congress itself acknowledged that judicial review of the Secretary's actions here may be judicially reviewed and that injunctive relief might be sought. The 2000 Act acknowledges that possibility and accommodates it:

(d) EFFECT OF COURT ORDER- The actions authorized by subsections (b) and (c) are intended to ensure the timely publication and implementation of new pricing formulas for Class III and Class IV milk. In the event that the Secretary of Agriculture is enjoined or otherwise restrained by a court order from implementing a final decision within the time period specified in subsection (c), the length of time for which that injunction or other restraining order is effective shall be added to the time limitations specified in subsection (c) thereby extending those time limitations by a period of time equal to the period of time for which the injunction or other restraining order is effective.

2000 Act §2.

**B. Milk Producers are Entitled to a Temporary Restraining Order and/or a Preliminary Injunction Under the Law of the Circuit**

It is well established that to obtain a temporary restraining order or preliminary injunction the Plaintiffs must demonstrate (1) a substantial likelihood of success on the merits; (2) that Plaintiffs would suffer irreparable injury if the requested relief is denied; (3) that an order would not substantially injure other interested parties; and (4) that the public interest would be furthered by granting the order. *See, United States v. Microsoft Corp.*, 146 F. 3d 935, 943 (D.C. Cir. 1998) (citing *CityFed Financial Corp. v. Office of Thrift Supervision*, 58 F. 3d 738, 746 (D.C. 1989)).

The standard for granting a temporary restraining order in this Circuit was set forth in *Virginia Petroleum Jobbers Assoc. v. FPC*, 259 F. 2d 921, 925 (D.C. Cir. 1958). In *Washington Metro Area Transit Comm'n v. Holiday Tours, Inc.*, 559 F. 2d 841, 843-45 (D.C. Cir. 1977) the court held that although the factors outlined in *Virginia Petroleum Jobbers* controlled, “the view that a 50% probability is required by *Virginia Petroleum Jobbers* is contrary to both the language and spirit of that opinion.” *Washington Metro*, 559 F. 2d at 844.

The *Washington Metro* court made the standard for granting a temporary restraining order more flexible when it held:

Under *Virginia Petroleum Jobbers* a court, when confronted with a case in which the other three factors strongly favor interim relief, may exercise its discretion to grant a stay if the movant has made a substantial case on the merits. The court is not required to find that ultimate success by the movant is a mathematical probability, and indeed may grant a stay even though its own approach may be contrary to movant’s view of the merits. The necessary “level” or “degree” of possibility of success will vary according to the court’s assessment of the other factors.

*Washington Metro*, 559 F.2d at 843.

Finally, the court noted that temporary relief:

is preventative, or protective, it seeks to maintain the status quo pending a final determination of the merits of the suit. An order maintaining the status quo is appropriate when a serious legal question is presented, when little if any harm will befall other interested persons or the public and when denial of the order would inflict irreparable injury on the movant. There is substantial equity, and need for judicial protection, whether or not movant has shown a mathematical probability of success. *Id* at 844

As the demonstrated below, the governing standard is met in this case.

**1. Plaintiffs And Their Dairy Farmer Members Will Suffer Severe And Irreparable Injury Unless the Secretary Is Restrained Immediately From Implementing the Separate Class III Butterfat Price**

If the Court does not act to preserve the status quo and enjoin the Secretary's implementation of his drastic inclusion of a separate Class III Butterfat Price in the Federal Milk Marketing Orders, Plaintiffs' dairy farmer members will suffer severe and irreparable loss of revenue from the sale of their raw milk. Further, virtually every dairy farmer in the United States that benefits from the producer settlement funds of the Federal Milk Marketing Orders will, in the aggregate suffer an annual loss of milk sales revenue of as much as \$400 million according to the attached affidavit of Mary Ledman. (Decl. Ledman ¶3).

This is so because once the Secretary announces the January Class III Butterfat Price on February 2, 2001, Plaintiffs' dairy farmer members' raw milk will be priced under that new scheme and Plaintiffs' loss will be irreparable. Once implemented, the status quo will be altered and this court will be effectively precluded from granting meaningful relief on the Milk Producers claim.

Of particular concern is the anticipated impact on pricing Class I milk. Due to the complexity of the overall pricing scheme compounded by the new cheese butter price for Class III Butterfat Price, those months when when the Class III moves, or sets the base, for the Class I milk price,

extraordinary and volatile forces will work on the Class I price. Producer losses nationwide will approximate \$61 million. (Ledman Decl. ¶¶ 12, 13). That will come very suddenly and unexpectedly. The Class I mover is determined only seven days before the beginning of the month it takes effect. If the Class III Butterfat Price is implemented now, there will be no time nor ability for Milk Producers and this Court to avoid those losses. The event is certain to occur. There will be no other opportunity after February 2, for this Court to remedy that loss. Even if Plaintiffs prevail on the merits of their Complaint against the Secretary, the damage to Plaintiffs' dairy farmers will be complete; the handlers will have processed and sold the milk to their consumers at prices that reflect the Secretary's new Class III Butterfat Price. The Secretary's sovereign immunity will preclude an action for damages.

In contrast, neither the Secretary nor the public interest will suffer from the continuation of the existing use of the Class IV Butterfat price. The Secretary has used a single butterfat price for decades and it was a single butterfat price and its impact on Class I prices that was mandated by Congress to be implemented in the 2000 Act. While that Act directed the Secretary to hold a hearing on Class III and IV prices, there was no similar direction to lower dairy farmer prices contrary to the AMAA's purpose "to raise producer prices." *Block v. Community Nutrition Inst.*, 467 U.S. 340, 342 (1984). To the contrary, the 2000 Act directed the Secretary to adopt the Class I differential scheme that did not reduce producer prices instead of the one proposed by the Secretary, and reconsider the Class III and Class IV prices. It would be contrary to the 2000 Act for the Secretary to use the mandated hearing as a means to undo what Congress directed. If the Class III Butterfat Price is implemented, it is anticipated that its impact on Class I returns to producers will be a reduction by as much as \$400 million per year. Nothing in the 2000 Act, or its legislative history, suggests that the Secretary should perform the kind of radical surgery on the Class I Prices

by replacing the existing butterfat pricing formula with one that promises to substantially reduce Class I prices throughout the coming years.

**2. Plaintiffs Are Likely to Prevail On The Merits Of Their Challenge To The Secretary's Action Because He Did Not Follow the Proper Procedure and the Separate Class III Butterfat Price is Not in Accordance with the Law.**

The central thrust of Plaintiffs' case is that the Secretary has amended the Federal Milk Marketing Orders by adding a rogue provision, not lawfully promulgated, to substantially alter the pricing scheme with a separate Class III Butterfat Price. This amendment was never noticed for consideration, no testimony was given on its behalf, and it was not within the scope of the hearing. The Secretary's own delegates made it clear to all hearing participants that a separate Class III Butterfat Price was not within the scope of the hearing. Indeed, the ALJ so ruled. The Secretary does not have authority under either the AMAA or the 2000 Act to implement amendments to the Federal Milk Marketing Orders without full compliance with the rulemaking provisions of the AMAA, the APA, and his own regulations. Even if he had followed the procedural requirements, the separate Class III Butterfat Price will substantially reduce producer income on a scale equal to that which prompted a prior injunction and the Congressional remedy contained in the 2000 Act. These reduced prices violate the plain spirit and language of that Act.

Section 608c(3) of the Agricultural Marketing Agreement Act (AMAA) (7 U.S.C. § 608(c)(3)) and the regulations found at 7 C.F.R. §§ 900.1 - 900.18 prescribe and limit how amendments to the Federal Milk Marketing Orders are to be considered and adopted. A perusal of the administrative record of the challenged hearing will show that the Secretary never received a proposal for a cheese butter price formula for the Class III Butterfat Price, the Secretary never advised the industry that such a proposal would be considered, the Secretary at the hearing agreed that the only proposal for a cheese butter price for Class III Butterfat Price presented, by Dr. Barbano was outside the scope

of the hearing and no evidence was presented on behalf of the proposal the Secretary now seeks to adopt and indeed, the Secretary's current post-hearing proposal differs markedly from the Barbano proposal. In short, the Class III Butterfat Price was adopted in a manner contrary to the AMAA and the Administrative Procedures Act, 5 U.S.C. § 706 and should be enjoined.

**3. The Tentative Final Decision Is Contrary to Both the Procedural and Substantive Requirements of the Agricultural Marketing Agreement Act of 1937.**

The AMAA requires the Secretary to use formal, adjudication-type procedures for creating and modifying Federal Milk Marketing Orders. 7 U.S.C. §608c(5). *Lansing v. Espy*, 39 F.3d 1339, 1345 (6<sup>th</sup> Cir. 1994). The Secretary has implemented this requirement in the department's regulations at 7 C.F.R. §§900.8-10 for both the establishment and modification of marketing orders. These regulations call for formal evidentiary hearings before an Administrative Law Judge to create or modify a marketing order.

The Federal Milk Marketing Orders are complex. Their success and continuing vitality depend upon the experience, knowledge and input from the industry at these rulemaking hearings. The Secretary typically solicits input and issues a Notice which identified specific proposals for consideration at a hearing. The hearing is confined to those proposals and the Secretary must make his decision based upon the hearing record.

The new Class III Butterfat Price, however, was promulgated in a manner inconsistent with these regulations and procedures. The amendment created by the Secretary was not contained in his hearing notice, was never proposed at the hearing itself and was created by the Secretary *after* the hearing record was closed. There was no opportunity for meaningful evaluation, comment or debate.

The creation of the separate Class III Butterfat Price in the Tentative Final Decision is both “in excess of statutory ...authority” and “without observance of procedure required by law” (5 U.S.C. §706 (2)(C) & (D)) and should be struck down, provisionally and permanently.

**a. The Tentative Final Decision Is Arbitrary and Capricious**

The standard the Supreme Court has used in determining if an agency’s action is arbitrary and capricious is best described in *Motor Vehicle Manufacturers Association v. State Farm Mutual Automobile Insurance Company*, 463 U.S. 29, 43 (1983):

Normally, agency (action) would be arbitrary and capricious if the agency has relied on factors which Congress has not intended it to consider, ***entirely failed to consider an important aspect of the problem***, offered an explanation for its decision that runs counter to the evidence before the agency, or is so implausible that it could not be ascribed to a difference in view of the product of agency expertise.

*Id.* [emphasis added].

The aspect of the problem that the Secretary failed to explore or consider here was the real impact of the separate Class III Butterfat Price on the Class I price. As indicated by the affidavit of Mary Ledman ( Ledman Decl. ¶ 14), the impact is severe. A perusal of the Tentative Final Decision and its accompanying economic analysis shows the complete absence of any such Class I price impact analysis. Although the Secretary recognized that the separate Class III Butterfat Price could result in wide disparity between the Class III and Class IV butterfat prices (67 Fed. Reg. 76832, 76850), ***he never analyzed the change in pricing resulting from a separate Class III Butterfat Price on the Class I mover.*** Had he done so, he could not have logically or rationally concluded that: “In addition to slightly altering the sharing of manufacturing proceeds between manufacturing plants and producers, ***the decision’s formula changes have a small impact on Class I and Class II prices.***” (Tentative Final Decision). Some may argue that the economic model’s projections did not see Class III as the mover, but that does not excuse the egregious ignoring of such a fundamental

problem. Economic Analysis, p. 5, 67 Fed. Reg. 76835. As pointed out by Agricultural Economist Ledman, in 1999 the Class III was the mover 7 months, that 2000 was “atypical” and that in the future the two should move Class I the same amount of months. (Ledman Decl. ¶17) .

In short, this failure to consider at the most fundamental aspect of the radical use of another butterfat price is a result of the Secretary’s failure to follow the applicable law and procedures required for notice and comment rulemaking.

The Secretary’s failure to consider this impact is arbitrary and capricious.

**b. The Class III Butterfat Price is unauthorized by law.**

In passing the 2000 Act, Congress clearly directed the Secretary to adopt a higher Class I price. 2000 Act, §1. It would be incongruous for Congress on the one hand to mandate a higher Class I price but at the same time give the Secretary authority to reduce those prices by creating a default provision for the price calculation formula. Since the implementation of Class III Butterfat Price will result in reduced Class I income, implementation of such an amendment, even if procedurally proper, would not be in accordance with the AMAA, or the 2000 Act.

Additionally, in the 2000 Act, Congress mandated the implementation of the pricing formulas that included the historic use of a single butterfat price. There is nothing in the language of that bill that suggested that the Secretary should also consider a radical departure from the past and compound the complexity of the formulas with an additional butterfat price. Several times in the instant rulemaking, the Secretary soundly rejected proposals to alter the Class I pricing scheme and the price movers. 67 Fed. Reg. 76849. The inconsistency in what was said and the end result exemplifies the flawed decision making process.

**C. The Milk Producers Will Be Irreparably Injured If An Injunction Is Not Issued.**

Dairy producers' income is dependent upon, and directly correlates to, the uniform blend prices that are enforced under the milk marketing orders in the AMAA. These uniform blend prices are the function, in part, of the prices plants must pay for butterfat. Implementation of the Class III Butterfat Price provision will reduce these blend prices, in some months, severely. If these minimum prices drop, producer income drops.

There is no potential recovery from the Secretary as a result of his errors. No funds from the U.S. treasury are involved and sovereign immunity would pose an additional hurdle. Rather, the money comes from the handlers who are required to pay these minimum prices for raw milk.

Similarly, handlers cannot be held liable after paying a lawful price for the raw product and, in turn, selling it to consumers. Such retroactive application of price changes, unworkable at best, is plainly unenforceable. *See, St. Alban's Cooperative Creamery, Inc. v. Glickman*, 68 F. Supp 2d 380, 386 (D. UT., 1999).

Finally, though the economic impact is severe and irreparable, the Secretary failed to comply with the law and regulations and deprived plaintiffs of their fundamental a Due Process rights. Denial of due process in and of itself is irreparable.

**D. If The TRO Is Granted, The Secretary Will Not Suffer Any Undue Hardship.**

The Secretary has no pecuniary or vested interest in implementation of the regulations. Indeed, the 2000 Act itself contemplated the possibility of an injunction. Compelling the Secretary to comply with the law cannot be considered a "hardship."

If the Secretary truly believes that his new Class III Butterfat Price is necessary to effectuate the purposes of the AMAA, he can commence a separate rulemaking proceeding to do just that. 7 U.S.C. §608c(3) and 7 C.F.R. §900.3.

#### **E. Injunctive Relief Is In The Public Interest.**

The continuation of the historic single butterfat provision as found in the regulations prior to the Tentative Final Decision is consistent with the Congressional policy behind the AMAA.

In addition, producers or handlers will not be harmed. Plaintiffs anticipate that other producer organizations and handlers throughout the Nation will file *amicus* briefs in support of the Plaintiff's position. The Secretary misled the industry when he announced that there would only be slight changes in income to producers as a result of the amendments to the butterfat pricing. Coupled with the complexity of the pricing formulas, lack of proper notice and ability to analyze and comment, the anticipated volatility of milk prices and chaotic market conditions, the public interest will be best served by maintaining the status quo.

#### **IV. Relief Sought**

Milk Producers seek an injunction on implementing only those portions of the Secretary's Tentative Final Decision and Interim Rule which create the new Class III Butterfat Price. Such a stay will maintain the status quo with the use of a single butterfat formula pending final review.

The Class III Butterfat Price provisions can be readily identified and separated from the other provisions of the Tentative Final Decision. The implementation of the new Class III Butterfat Price can be delayed while the balance of the Secretary's proposal takes effect. (Ledman Decl. ¶22). Plaintiffs have attached as Appendix 1, an edited version of the Secretary's proposal with specific language governing the implementation of the Class III Butterfat Price stricken. An Order striking such language while leaving the balance of the Secretary's Tentative Final Rule Intact would provide adequate relief at this juncture.

## V. Conclusion

WHEREFORE, the Plaintiffs respectfully request that this Court grant a temporary restraining order and/or preliminary injunction ordering that the Secretary, his agents and attorneys and those persons in active concert or participation with them who receive actual notice of this order be restrained, until further order of this Court from implementing separate Class III Butterfat Price provisions in amendments to the regulations found at 7 C.F.R. Parts 1000 - 1135 as so identified at 65 Fed. Reg. 76832 (December 7, 2000) and 65 Fed. Reg. 82832 (December 28, 2000).

Respectfully submitted,

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