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Inc., and Hilmar Whey Protein, Inc.

**BEFORE THE
CALIFORNIA REGIONAL WATER QUALITY CONTROL BOARD
CENTRAL VALLEY REGION**

In the Matter of Hilmar Cheese
Company, Inc., and Hilmar Whey
Protein, Inc. (Merced County)

Administrative Civil Liability
Complaint No. R5-2005-0501

**PREPARED DIRECT TESTIMONY OF JOHN JETER
IN SUPPORT OF HILMAR CHEESE COMPANY, INC.,
AND HILMAR WHEY PROTEIN, INC.**

Purpose and Qualifications

1. My name is John Jeter, and I am the Chief Executive Officer and President of Hilmar Cheese Company, Inc. and Hilmar Whey Protein, Inc. (collectively, "Hilmar"). My business address is Hilmar Cheese Company, 9001 N. Lander Avenue, P.O. Box 910, Hilmar, California 95324-0910.

2. One purpose of my prepared direct testimony is to provide an overview of Hilmar's prepared direct testimony and a summary of the defense positions presented by Hilmar in response to the allegations set forth in Administrative Civil Liability Complaint ("ACLC") No. R5-2005-0501, issued by the Executive Officer of the California Regional Water Quality Control Board, Central Valley Region ("Regional Board"), on January 26, 2005. The ACLC alleges, among other things, that Hilmar discharged wastewater to land in violation of the Regional Board's waste discharge requirements over a three-year period from January 27, 2002, to November 30, 2004.

3. Another purpose of my testimony is to address the allegations of the ACLC based on my own personal knowledge, and to outline Hilmar's long history of cooperation with the Regional Board and its unprecedented compliance efforts over the years.

4. To the extent my testimony contains statements of fact, those statements are true and correct to the best of my knowledge, information, and belief. To the extent my testimony contains statements of opinion, those statements are predicated on my best professional judgment.

5. While some of my testimony presents a high level overview of Hilmar's case without the detail contained in the testimony of certain other Hilmar witnesses in this proceeding, all of my testimony is based on my own personal knowledge, information, and belief, as well as upon documents appended hereto and otherwise in the record, and, when sworn to, will constitute competent and admissible evidence relating to the matters addressed. Where matters are better addressed by other witnesses, I will refer the matter to the witness best able to address it.

Overview of Prepared Direct Testimony

6. In addition to the public file relating to this proceeding, and such additional documentary and oral evidence as may be presented at or before the hearing of this matter, Hilmar presently submits to the Regional Board five pieces of prepared direct testimony, along with supporting exhibits. The first piece of testimony is this testimony – the Prepared Direct Testimony of John Jeter in Support of Hilmar Cheese Company, Inc., and Hilmar Whey Protein, Inc. – which I am sponsoring.

7. The second piece of testimony is the Prepared Direct Testimony of Tedd Struckmeyer and Warren Climo in Support of Hilmar Cheese Company, Inc., and Hilmar Whey Protein, Inc. This piece of testimony is jointly sponsored by Tedd Struckmeyer, Hilmar's Vice President of Engineering, and Warren Climo, Hilmar's Director of Environmental Management, and addresses in detail, among other things, Hilmar's wastewater treatment history as it relates to a number of the factors that are statutorily required to be considered in assessing a civil penalty in an ACLC proceeding such as this one.

8. The third piece of testimony is the Expert Report and Prepared Direct Testimony of Kennedy/Jenks Consultants in Support of Hilmar Cheese Company, Inc., and Hilmar Whey Protein, Inc. Regarding Nature, Extent, Gravity, Toxicity and Susceptibility to Cleanup. This testimony is sponsored by Kennedy/Jenks witnesses Paula Hansen and Leslie Chau, and similarly addresses a number of the factors that are statutorily required to be considered in assessing a civil penalty in an ACLC proceeding such as this one.

9. The fourth piece of testimony is the Expert Report and Prepared Direct Testimony of Kennedy/Jenks Consultants in Support of Hilmar Cheese Company, Inc., and Hilmar Whey Protein, Inc. Regarding Unfair and Inconsistent Regulation and Enforcement. This piece of testimony is sponsored by Kennedy/Jenks witness Paula Hansen and addresses the Regional Board's regulation and enforcement applied to Hilmar in comparison with that applied to other dischargers which, likewise, bears on factors that are statutorily required to be considered in assessing a civil penalty in an ACLC proceeding such as this one.

10. The fifth piece of testimony is the Expert Report and Prepared Direct Testimony of Mark Berkman, Ph.D., and David Sunding, Ph.D., in Support of Hilmar Cheese Company, Inc., and Hilmar Whey Protein, Inc. This piece of testimony is jointly sponsored by Mark P. Berkman and David L. Sunding, both of whom are principals in Charles River Associates International, and addresses the merits of the ACLC and proposed penalty from an expert economic and public policy perspective, again factors that are required to be considered in assessing a civil penalty in an ACLC proceeding such as this one.

Summary of Defenses

11. In this proceeding, Hilmar has asserted various defenses, including the following:

- The ACLC was issued without analysis supporting the proposed \$4 million penalty;
- The ACLC unlawfully seeks to find Hilmar in violation of the waste discharge requirement for EC despite Hilmar's exercise of every reasonable precaution to prevent or mitigate the discharge;
- Compliance with the EC waste discharge requirement that Hilmar is alleged to have violated was not technically feasible during the violation period;
- Compliance with the EC waste discharge requirement that Hilmar is alleged to have violated was not economically feasible during the violation period;
- Compliance with the EC waste discharge requirement that Hilmar is alleged to have violated is not economically or environmentally sustainable, and the Regional Board and its staff never considered these facts in implementing regulatory or enforcement policies with regard to Hilmar;

- Compliance with the EC waste discharge requirement that Hilmar is alleged to have violated compels the use of technology, the environmental cost of which exceeds the environmental benefit;
- The nature of the discharge, and the extent and gravity of the alleged violations, do not warrant the imposition of a significant civil penalty, if any is imposed;
- The discharge of EC at the levels discharged by Hilmar has not been shown to be either toxic or hazardous, and hence a significant penalty is not warranted, if any is imposed;
- There have been no demonstrated impacts to the beneficial uses of ground water, namely human health or agriculture, from the discharges;
- The impacts from Hilmar's discharges have largely been confined to Hilmar's site;
- The discharge is entirely susceptible of cleanup and abatement and hence a significant penalty is not warranted, if any is imposed;
- A significant penalty is not warranted, if any is imposed, because in view of the totality of the circumstances, Hilmar's culpability is de minimis or non-existent;
- A significant penalty is not warranted, if any is imposed, because Hilmar derived no economic benefit or savings as a result of the alleged violations;
- Rather than deterring "bad actors" and "bad conduct," the finding of violations and the imposition of this unprecedented civil penalty against Hilmar will deter companies from cooperating and working with the Board to bring themselves into compliance with the Board's requirements;

- The imposition of a significant civil penalty will have an adverse effect on Hilmar's and other California businesses' competitive position and ability to continue to do business in the State of California;
- Treating other companies the way Hilmar is proposed to be treated by the ACLC would drive many other companies out of business, cause them to leave the State, or cause them to build new incremental facilities outside the State, resulting in the loss of jobs and other benefits, and will make products produced in California non-competitive in national and international markets;
- The ACLC seeks to find Hilmar in violation of the EC waste discharge requirement despite the existence of an understanding between the Board staff and Hilmar that Hilmar would not be subject to an enforcement action seeking civil penalties so long as it worked diligently and in good faith with the Board staff to bring itself in compliance with the Board's requirement;
- In early 2002 Regional Board staff told Hilmar that with the failure of the V-SEP® system approach, Hilmar would be given a new time schedule within which to achieve compliance (with no enforcement unless and until Hilmar failed to achieve compliance within the required period); thereafter Hilmar proposed a time schedule that staff accepted and with which Hilmar has complied;
- A significant penalty is not warranted, if any is imposed, for equitable reasons based on the totality of the circumstances presented.
- The ACLC against Hilmar was issued due to political pressure from public officials to make an example of some company and not for any legitimate enforcement purpose;

- The ACLC was issued due to pressure caused by press and media scrutiny and not for any legitimate enforcement purpose;
- The ACLC was issued by Executive Officer one day prior to a scheduled Regional Board closed hearing to determine whether the Executive Officer's employment should be terminated and was issued to save the Executive Officer's job rather than for any legitimate enforcement purpose;
- The EC waste discharge requirement that Hilmar is alleged to have violated are predicated on an unlawful Basin Plan and otherwise is invalid;
- The EC waste discharge requirement that Hilmar is alleged to have violated is discriminatory, unlawful and violates the constitutional requirements of equal protection of the laws and due process of law in that such requirement has not been imposed on any other California food processor;
- The EC waste discharge requirement that Hilmar is alleged to have violated is discriminatory, unlawful and violates the constitutional requirements of equal protection of the laws and due process of law in that the attempt to comply with such requirements has compelled Hilmar to make economic expenditures of a significantly greater magnitude than any other California food processor;
- The EC waste discharge requirement that Hilmar is alleged to have violated is unlawful in that it compels Hilmar to reduce the salt and mineral content of its wastewater to a level below that in its pre-processing intake water;
- The EC waste discharge requirement that Hilmar is alleged to have violated is unlawful in that it compels Hilmar to reduce the salt and

mineral content of its wastewater at the end-of-pipe point of discharge to meet the lowest value in the permissible range of Maximum Contaminant Levels (“MCLs”) established for finished drinking water at the tap;

- The EC waste discharge requirement that Hilmar is alleged to have violated fails to specify a valid duration or averaging period upon which to judge compliance;
- The ACLC is discriminatory, unlawful and violates the constitutional requirements of equal protection of the laws and due process of law in that it seeks to find Hilmar in violation of the EC waste discharge requirement on a daily rather than a monthly or longer average basis, where the drinking water standard being used is a long-term average based on many years of exposure;
- The ACLC unlawfully seeks to find Hilmar in violation of the EC waste discharge requirement on the basis of the volume of the wastewater discharged rather than on the basis of the volume of the waste discharged; and
- The ACLC unlawfully seeks to find Hilmar in violation of the EC waste discharge requirement for discharges that are the result of the unlawful actions or negligent acts or failures to act on the part of the State of California or a department or agency of the State of California.

Background

12. Hilmar is a privately-owned company established in 1984 by twelve local dairy families. The company currently employs more than 600 individuals, making it one of Merced County’s largest employers. Since its inception, Hilmar has been dedicated to processing high-quality cheese and whey products, while recycling wastewater flows in a way that minimizes and/or avoids any negative impact to the environment or to the local community.

To achieve this goal, Hilmar has invested many millions of dollars in research and treatment technology.

13. Hilmar has consistently sought to be a good corporate citizen and has maintained close ties with the Hilmar community and the broader Central Valley community. True copies of letters from members of these communities in support of Hilmar in this proceeding are attached hereto as Exhibit A.

14. In 1994, the Central Valley Regional Board began to impose strict groundwater regulatory requirements in the San Joaquin Valley. Since then, the Regional Board has applied progressively more restrictive limits on dischargers in an effort to provide greater protection for underlying groundwater supplies and to eliminate odor nuisances for nearby residential developments. From a practical viewpoint, the technology available to meet these requirements has not kept pace with the stricter standards imposed by the Regional Board.

15. Since its inception, Hilmar Cheese Company has recognized its responsibility to consider and develop innovative treatment technologies in order to respond effectively to current and evolving water quality standards. Both regulators and Central Valley businesses agree that technologically sound and practical solutions must be found to assure Central Valley citizens a safe environment in which all can thrive, and as a result the Regional Board has worked closely with businesses it believes are making a good-faith and conscientious effort to implement innovative yet unproven wastewater treatment technologies to meet regulatory standards. It is within this context that Hilmar Cheese Company has been working diligently to bring our facility into compliance.

16. In 1996, Hilmar developed a long-term Conceptual Compliance Plan (which has undergone periodic updates to keep pace with regulatory requirements). Recognizing that future water quality standards would become more restrictive, we have worked diligently to provide a recycled water supply for full beneficial agricultural use. As a food processing plant, Hilmar does not deal with toxic materials like heavy metals or human wastes in our treatment system. The purpose of Hilmar's water treatment system is to separate, treat and utilize the three major components of our wastewater:

a. Organic materials derived from milk – fat, protein and lactose. These are a potential source of animal feed if they can be successfully separated, but are a potential source of odors if not treated or removed.

b. Minerals derived from the milk and equipment cleaners. These are a potential source of soil nutrients if successfully separated and appropriately applied.

c. Water from two sources – the first originally part of the milk, captured and recycled once to use as wash water, the second from wells under the site. After treatment, this would be cleaner than the groundwater and good for full beneficial agricultural use.

17. In 1997, the Regional Board adopted waste discharge requirements (“WDRs”) for Hilmar in Waste Discharge Requirements Order No. 97-206. The WDRs required that the mineral content (identified as “Electrical Conductivity” or “EC”) of Hilmar’s end-of-pipe discharge not exceed 900 $\mu\text{mhos/cm.}$, less than the EC level of Hilmar’s intake water and the lower end of the *secondary* drinking water maximum contaminant level (“MCL”) for EC at the drinking water tap. No other California food processor had ever had such strict waste discharge requirements imposed upon it. Without considering natural attenuation and the fact that not all discharged minerals will reach the groundwater, the Regional Board’s standards mandate that our end-of-pipe discharge to land is of better quality than water that community water systems are allowed to serve, and in fact serve, to their customers. Not only is the basis for the standards inappropriate, but penalizing a company that has spent millions of dollars working with Regional Board staff to bring itself into compliance with such an unprecedented standard is a serious misuse of regulatory authority.

18. Although there were no available off-the-shelf technologies for meeting the Board’s requirements, Hilmar believed it could ultimately attain compliance with the Board’s requirements through an aggressive, and likely very costly, program of research and development. It also believed that so long as it worked cooperatively and in good faith with the Board’s staff in order to achieve compliance, it would not be subject to enforcement action seeking the imposition of civil penalties. As a result, Hilmar did not challenge the Board’s

requirements, even though the requirements have proven to be economically and environmentally unachievable and unsustainable over the long term.

19. As Hilmar has been forced to raise in legal proceedings, the Regional Board's requirements were and are unlawful not only because they are unachievable, are without scientific or analytical basis, and are discriminatory but also because, *inter alia*, they are predicated on an unlawful and invalid Basin Plan. (See the true copy of Hilmar's petition for a writ of mandate challenging the Basin Plan, which is attached hereto as Exhibit B; see also the true copy of Hilmar's State Board petition challenging the denial of Hilmar's request to modify the waste discharge requirements in its permit, which is attached hereto as Exhibit C.)

20. The Regional Board's requirements were unprecedented at the time they were adopted and largely still are today.

21. Although land-based application of food processing wastewater was and is widely recognized as a legitimate form of treatment, it became difficult to manage and sustain under increasingly stringent Regional Board requirements. Initial efforts by Hilmar to utilize innovative technologies (1997-2002) were not as successful as we and the staff of the Regional Board had hoped, so our plan was modified to its current form which includes conversion of the organics to renewable energy (biogas) and an option to use deep-well injection for pre-treated waste water flows.

22. Hilmar has spent many years and many millions of dollars in a good-faith effort to implement our modified Conceptual Compliance Plan, actively researching, designing and building various advanced treatment technologies to manage and recycle our water supply. Hilmar has also recently submitted a Deep Well Injection Control permit application to the federal Environmental Protection Agency. The costs associated with treatment of our wastewater amount to more than \$85 million from 1998 to the present.

23. Today, Hilmar operates the largest single-site cheese and whey products manufacturing facility in the world, and employs more than 600 Californians. It specializes in the production of cheddar and American cheese utilized by private label and national brand companies, and produces several other varieties of cheese for use in food service, ingredients,

retail, and restaurants. Hilmar Ingredients, a division of Hilmar, manufactures a wide range of whey protein concentrates, whey protein hydrolysates, and three grades of edible lactose. Hilmar's Pharmaceutical Lactose division produces products for the global marketplace.

24. With respect to the amount of milk processed annually by HCC, increases have occurred in virtually every year that the company has been in business. To meet the operating challenges posed by these increases, Hilmar has, at various times, directed resources to capital improvement projects intended to expand Hilmar's capacity for processing milk. In 1990, Cheese Plant 2 was added to the original Cheese Plant 1. In 1991, construction was completed on the Protein Plant. In 1994, Lactose Plant 1 was completed. In 1996 and 1997, Cheese Plant 1 and Cheese Plant 2, respectively, were remodeled with new belts and towers. In 1999, Lactose Plant 2 was completed. In 2000, Cheese Plant 4 was added and, also in that year, the Protein Plant was expanded.

25. Hilmar has always believed that environmental compliance, especially water quality compliance, is an inseparable component of the capital improvement/planning process. Hilmar has never undertaken to plan for and construct capital improvements without also determining and allocating the amount of money needed for improvements that would allow the company to meet applicable water quality requirements. Expansion of milk processing capacity has always been attended by the informed expectation that increased production would not interfere with Hilmar's ability to meet applicable water quality requirements.

26. True copies of documents detailing the planning for Hilmar's most recent expansion, which began in 1998 and involved the construction of additional facilities and the incurrence of additional capital costs, are attached hereto as Exhibit D. These documents were prepared by Hilmar's CFO, Jay Hicks, during the capital improvement planning process to serve as information resources for Hilmar's financial lenders.

27. As the documents illustrate, water treatment costs were incorporated into the planning process from the very beginning. Hilmar projected in February 1998 that it would spend \$3.8 million on wastewater treatment facilities over the course of the expansion. Hilmar thus entered the expansion phase fully anticipating that it would need to spend several million

dollars in capital costs alone on water quality compliance costs. In July 1999, after the decision was made to increase the scope of the expansion, the wastewater treatment capital cost projection was nearly doubled to \$6.8 million. Hilmar has spent far more than these projections. Through the end of 2005, Hilmar projects that it will have spent nearly \$90 million in capital and operating costs related to water quality compliance since 1998.

28. The bottom line is that Hilmar has continually worked to meet California's water quality objectives and planned its most recent capital improvements with an eye toward ensuring compliance with Waste Discharge Requirements Order No. 97-206. While not all of Hilmar's efforts have been successful, we have demonstrated a willingness to innovate and direct the necessary resources towards finding water quality solutions that may one day be models for other food processing companies.

29. Hilmar worked hard both to comply with the increasingly restrictive regulatory requirements for land application imposed by the Regional Board and to implement innovative technologies to treat our wastewater. Hilmar is aware that, despite our best efforts, our past operations impacted nearby residents, impacts which we have addressed. As a good neighbor, we remain fully committed to continuing to eliminate and avoid impacts on our neighbors.

History of Regulation and Compliance Efforts

30. Hilmar was one of the first land dischargers in California to have any type of mineral discharge requirements for wastewater imposed upon it. The Board's waste discharge requirements for minerals and salts are addressed in its requirement for Electrical Conductivity ("EC"). Hilmar's current EC standard under its 1997 permit is 900 $\mu\text{mhos/cm.}$, less than the EC level of its intake water and the lower end of the secondary drinking water standard for EC. The Regional Board's requirements were unprecedented at the time they were adopted and largely still are today. Hilmar was the first California food processor required to meet drinking water quality standards with respect to EC in its wastewater. No other California food processor has been asked to do what Hilmar has been required to do by the Regional Board.

31. The 1997 permit required Hilmar to make use of technology that had not been used before in the food processing industry or with respect to cheese processing wastewater such as Hilmar's. There were no proven or off-the-shelf technologies available that Hilmar could turn to in order to meet the Regional Board's requirements. Accordingly, in an effort to meet the requirements, and with the encouragement of the Regional Board staff, Hilmar undertook a pioneering research and development project. Hilmar since has invested more than \$85 million to develop and operate its own on-site, four-stage water treatment system, which represents the single largest investment in water treatment technology made by any food processor in California.

32. Hilmar undertook this research and development project consistent with its corporate philosophy of being an innovator and problem solver. After the permit was issued in 1997, Hilmar chose to cooperate with the Board and to attempt to meet the permit requirements, rather than pursue legal challenges to the permit that would have been available to Hilmar (and which Hilmar has now been forced to raise and pursue due to the grossly excessive and unfair penalty proposed in the ACLC). Specifically, as contended in Hilmar's legal pleadings, the permit's requirements are based on a basin plan that is unlawful and they otherwise fail to comply with State law. Perhaps even more importantly from Hilmar's perspective, the requirements are neither economically nor environmentally sustainable over the long term and have never been achieved by anyone else – ever. We never understood or even dreamed that the Regional Board would issue WDRs that were not grounded on a sound scientific and analytical basis, that were not supported by a lawful Basin Plan, that were not reasonably achievable or sustainable with honest, good faith efforts, that were unprecedented and far out of line with the requirements being imposed on other dischargers, including our competitors, and that the Regional Board staff would seek to impose millions of dollars of penalties on us in the face of our extraordinary efforts to achieve compliance in cooperation with the Regional Board.

33. As is described in more detail in the Prepared Direct Testimony of Tedd Struckmeyer and Warren Climo, Hilmar initially proposed, with full support of Regional Board

staff, to treat its wastewater through a patented V-SEP® vibrating membrane system using nanofiltration membranes. It was anticipated that this technology not only would enable Hilmar to meet its permit requirements by removing both minerals and organics, but also would allow for beneficial use of the retained minerals and organics for animal feed, thereby solving a greater problem – finding a “home” for the retained minerals.

34. The manufacturers of the V-SEP® technology assured Hilmar that this equipment would meet unprecedented performance standards in wastewater treatment, achieving a level of below 900 EC in the treated water, and producing a byproduct of feed grade quality. The trial runs employing this technology were concluded in April 1997 with very favorable results. The 1997 permit provided that Hilmar meet the 900 EC requirement by March 15, 1999.

35. Encouraged by these trial results, and with the support of the Regional Board staff, Hilmar installed the V-SEP® system with seven nanofiltration units in 1998. Unfortunately, the V-SEP® system was only moderately successful and did not meet the expected reduction in total dissolved solids in Hilmar’s wastewater. Consequently, during the third quarter of 1999, Hilmar installed a V-SEP® system using different technology, with six Reverse Osmosis (“RO”) membranes and converted the original seven nanofiltration membranes to ultra-filtration. Under this configuration, half the wastewater with higher Total Dissolved Solids (“TDS”) levels was treated and blended with the untreated half of the wastewater to yield a recycled water supply of less than 900 EC, as required by the permit.

36. The Regional Board Staff subsequently changed its interpretation of the 1997 Waste Discharge Requirement provisions and imposed a new requirement on Biological Oxygenation Demand (“BOD”) limits. In order to meet these BOD limits, Hilmar, in October 2000, installed and commenced operation of a large crossflow RO unit and converted the six RO membranes to ultra-filtration units. This configuration of RO and ultra-filtration units, however, did not meet the new BOD limits. In view of this, in July 2001, Hilmar installed and initiated the operation of another large crossflow RO unit and seven additional V-SEP® ultra-filtration units.

37. Despite this extensive effort and capital investment by the company, the reconfigured system did not perform to design expectations. Because of the V-SEP® system

failure, excessive organic loads were placed on the RO system and it, too, failed. Ultimately, higher organic loads in the wastewater dispersed on land resulted in odors, corrective measures, and apologies to the community. The water treatment facility was very innovative and would have been a major technological breakthrough for the entire agricultural and food processing industries in the valley, had it worked.

38. Because the V-SEP® system ultimately proved unsuccessful, it was technically infeasible for Hilmar to have met its unprecedented permit requirements as of 2002 or at any time prior to the issuance of the ACLC.

39. In 2002, Hilmar retained the services of an internationally renowned wastewater treatment consultant to determine why the on-site water treatment facility was not meeting the performance criteria predicted by the equipment manufacturers and to develop a new process. Hilmar embarked on a different approach in its efforts to comply with its permit, including the addition of physico-chemical dissolved air flotation thickeners, anaerobic treatment, and aerobic polishing along with reverse osmosis membranes. Hilmar had utilized reverse osmosis systems in conjunction with the V-SEP® process starting in December of 2000 and has continued to treat a large proportion of its wastewater through reverse osmosis systems since that time.

40. On or about January 2, 2002, after conducting a tour of the Hilmar waste treatment facilities for Regional Board staff, I received a letter from Gary Carlton, then Executive Officer of the Regional Board, who had participated in the tour. I understood the letter to mean that Hilmar would be receiving a new permit covering Hilmar's increased flow and providing a reasonable time schedule for compliance. A true copy of that letter is attached hereto as Exhibit E. My understanding of the letter has been confirmed by the testimony of prosecution staff witnesses in deposition. (*See* excerpts from the deposition of Bert Van Voris, a true copy of which is attached hereto as Exhibit F.) Indeed, Mr. Van Voris testified in his deposition that had the staff done what it said it would do in that letter, Hilmar would not be defending this ACLC proceeding now.

41. In 2002 Hilmar also explored the alternative approach of building a pipeline to send its wastewater to the City of Turlock for processing at Turlock's pre-treatment plant. This approach would have enabled Hilmar to become compliant by 2003.

42. In May 2002, a draft Wastewater Service Agreement between the City of Turlock and Hilmar was prepared, under which the Turlock sewage plant would process 50 to 60 percent of Hilmar's wastewater. Wastewater service under the Agreement would have commenced on or about June 2003. In a February 24, 2003 letter, however, Cliff Martin, Municipal Services Director of the City of Turlock, wrote Warren Climo (Hilmar Cheese Company's Environmental Director), stating that although the City then had capacity to handle Hilmar's discharge for a short period of time, it could not provide treatment without developing additional facilities, since it would impact potential community growth within its service area. After Hilmar took into consideration the time required by the City to prepare an Environmental Impact Report and construct new wastewater facilities, waste disposal at the Turlock plant was not a viable option for the near term. It is my understanding that the reduction in capacity available to Turlock, which reduction obviated the possibility of Hilmar's utilizing Turlock's treatment facilities, was the result of changed waste discharge requirements imposed on Turlock by the Regional Board.

43. Despite the set-back with Turlock, in 2003 Hilmar presented Regional Board staff with a schedule for meeting the permit requirements by mid-2005. Hilmar also immediately commenced detailed engineering design and construction for the project. Staff accepted the schedule and led Hilmar to believe that Hilmar would be afforded the time to meet the permit requirements in accordance with the schedule without the imposition of penalties.

44. In October 2002, Hilmar installed the first of two Physico-Chemical Dissolved Air Flotation ("PCDAF") systems. Subsequently, in March 2003, two Sand Filter ("SF") systems were installed. During this period, interim process operations involved treatment of the high-suspended solids wastewater streams through the PCDAF/SF/RO system removing the fat and protein components, which have the potential to create the greatest odors during land application. At the same time, the final design plan for the new treatment plant was being

developed. Also, in order to enhance the performance of the interim treatment system, a second PCDAF unit was installed in November 2003.

45. In December 2003, construction began on an Expanded Granular Sludge Blanket ("EGSB") anaerobic digester to convert organic loads into methane gas. In April 2004, construction began on Sequenced Batch Reactors for the removal of residual BOD and nitrogen. The installation of the above units clearly indicate that Hilmar was taking the necessary interim corrective measures directed toward bringing its facilities into compliance and eliminating nuisance odors, while at the same time designing a new treatment system to provide a long-term solution for handling wastewater flows.

Current Compliance Efforts

46. Since August 2002, alone, Hilmar has spent more than \$30 million to construct a new water treatment plant. By the end of 2005, Hilmar will have expended nearly \$90 million on capital and operating expenses related to the facility.

47. Hilmar's on-site, state-of-the-art water treatment system is in many ways more advanced than larger, municipal wastewater treatment systems. It represents the single largest investment to treat wastewater made by any food processor in California. The system consists of a four-stage process. All wastewater has been processed through the first three stages to remove milk organics since September 2004. These three stages are (1) dissolved air floatation to remove suspended milk solids, (2) anaerobic digestion of most organics to biogas, which produces energy, and (3) aerobic polishing to remove residual organics and nitrogen. Nearly all organics are successfully removed through the first three stages, eliminating odors and dramatically reducing organic loads in the discharge. Ultrafiltration has been recently added to the third stage to aid the final treatment stage.

48. The fourth stage features an extremely expensive and energy-intensive reverse osmosis and evaporation system to reduce salts resulting in clean irrigation water for beneficial agricultural use. This stage has been in operation since 2001. Integration of additional filtration equipment will increase capacity for this final stage. A true copy of an aerial

schematic of Hilmar's state-of-the-art wastewater treatment facility in color is attached hereto as Exhibit G.

49. Since September 2004, Hilmar Cheese Company has removed over 99% of the organic components in its wastewater, while continuing to achieve significant and unprecedented reductions in salts and other natural minerals. Hilmar's aim has always been to maximize the use of resources. Recycled water currently accounts for nearly 60% of the water used in Hilmar's operations. Managing the proper treatment of Hilmar's wastewater is a full-time endeavor. Research and development continues on a daily basis as Hilmar continuously seeks to fine tune and improve its innovative systems.

50. Despite promising results, Hilmar recognizes significant challenges for itself and ultimately the entire food processing industry. In particular, Hilmar is required to treat wastewater at the point of discharge to land to a higher standard of quality than its incoming, drinking-quality water supply – an unprecedented standard in California. The company has been required to utilize unproven, very costly technology to attempt to meet these unprecedented standards. And it has spent more money per pound of cheese to process wastewater than any other California cheese-maker, leaving the company at a significant competitive disadvantage in its primary business.

51. Through more than four years of research, development and experience, Hilmar believes that the reverse osmosis technology required to meet the EC limit in its permit is neither environmentally sustainable nor economically viable on a long-term basis. The technology is both difficult to use and extremely expensive to maintain. The process consumes large quantities of scarce energy. Furthermore, the salts that remain in the brine following filtration must be trucked to a municipal utilities district in the San Francisco Bay Area where the brine is further processed and returned to the ocean. This transportation requirement contributes to air pollution, use of non-renewable energy supplies and increased traffic congestion on some of the busiest roads in the Central Valley. None of these costs and circumstances were considered when the permit was adopted in 1997, even though such factors are statutorily mandated to be considered. (See Water Code § 13263(a).)

52. On July 11, 2005, in Modesto, the State Water Resources Control Board conducted a workshop on whether statewide standards are needed to protect the beneficial uses of groundwater from the discharge of minerals to land by food-processors. A true copy of an accurate transcription of the audio-tapes of that workshop is attached hereto at Exhibit H. True copies of the written comments submitted by the participants in the workshop are attached hereto as Exhibit I. I attended the workshop, and in my judgment there was a strong consensus among industry participants and regulators that reverse osmosis processes are not the answer to groundwater salinity issues that may be engendered by food processor discharges of wastewater to land. Based on Hilmar's experience with reverse osmosis, that consensus is absolutely correct. This consensus was best captured by Harvey Packard of the Central Coast Regional Water Quality Control Board, who stated at the workshop: "There's no treatment technology that's economically feasible to remove salts from the wastewater. Our general order focuses on source control ... [and] is designed to encourage wineries to recycle wastewater into the largest area possible to spread out the water and prevent localized impacts to water." Exhibit H at 21.

The ACL Complaint

53. After Hilmar worked cooperatively and openly with the Board and its staff for many years in a good faith effort to achieve compliance with the Board's requirements, the Executive Officer issued the instant ACLC on January 26, 2005, proposing that an exorbitant fine of \$4 million be assessed against Hilmar for its alleged violation of its EC discharge limit.

54. This ACLC – the largest ACLC in the history of the California Regional Water Quality Control Board system – cannot fairly be discussed without addressing the circumstances under which it was issued.

55. The ACLC appears to have been issued due to political pressure and media scrutiny arising from a series of highly inaccurate Sacramento Bee articles commencing in December 2004 that were critical of both Hilmar and the Regional Board, and to forestall termination of the Executive Officer's employment. The ACLC was issued the day prior to the Board meeting at which the Board had announced it would hold a closed session to consider termination of the Executive Officer's employment. The Executive Officer issued the ACLC

without waiting for the supporting staff report (that was ultimately prepared and issued some ten weeks later), without waiting for information staff had requested from Hilmar, and without providing any explanation of how he arrived at the unprecedented \$4 million proposed liability.

56. Prior to and after the issuance of the ACLC, without hearing any of the evidence, Regional Board Chair Robert Schneider and other members of the Board made public statements quoted in the Sacramento Bee purporting to validate the credibility and veracity of the December 2004 Sacramento Bee articles and erroneously characterizing Hilmar – a company that has consistently cooperated with Regional Board staff in an effort to bring itself into compliance with the Board’s WDRs – as a “bad actor.”

57. At the closed January 27, 2005 hearing the Board rewarded Mr. Pinkos for issuing the ACLC with compliments and the retention of his job. Moreover, the Regional Board staff took some ten weeks *following* the issuance of the ACLC to draft, revise and ultimately release a staff report purporting to justify Mr. Pinkos’ action in issuing the ACLC in the first place.

58. True copies of an email memo from Bert Van Voris to Loren Harlow and Thomas Pinkos dated October 8, 2004, entitled “Media Contact regarding HCC” and an email note from Ken Landau to Tom Pinkos dated October 19, 2004 entitled “Hilmar Cheese EO Report” (RWB-023816-023819, -023534) are attached hereto as Exhibit J. True copies of an email note from Thomas Pinkos to Loren Harlow, Jo Anne Kipps, and Bert Van Voris, dated October 13, 2004, entitled “HCC” and an email note from Thomas Howard to Thomas Pinkos, Robert Schneider, and Craig Wilson, dated December 13, 2004, entitled “Re: hcc talk points” are attached hereto as Exhibit K. A true copy of the Central Valley Regional Water Quality Control Board Website Notice setting the personnel hearing (Dec. 30, 2004) is attached hereto as Exhibit L. A true copy of the article, “Official in Trouble Over Cheese Waste,” Sacramento Bee (Jan. 1, 2005), is attached hereto as Exhibit M. A true copy of the article, “Open Water-Panel Meeting Urged,” Sacramento Bee (Jan. 26, 2005), is attached hereto as Exhibit N. A true copy of the article, “Hilmar Co-owner Quits his State Post,” Sacramento Bee (Jan. 27, 2005), is attached hereto as Exhibit O. A true copy of an email note from Jo Anne Kipps to Michael Cook, dated

February 11, 2005, entitled "Re: WLAP 2005! Annual Meeting" is attached hereto as Exhibit P. A true copy of Buff Sheet, Agenda Item 22, Central Valley Regional Water Quality Control Board Meeting of March 17/18, 2005, is attached hereto as Exhibit Q. A true copy of the article, "Hilmar Fiasco Spurs Changes," Sacramento Bee (Mar. 19, 2005), is attached hereto as Exhibit R. A true copy of Hilmar's First Request for Production of Documents from Regional Board Chair dated May 5, 2005, is attached hereto as Exhibit S. A true copy of a Letter Ruling from Steven Blum to Mark Fogelman dated May 16, 2005, denying request for discovery from Regional Board Chair, is attached hereto as Exhibit T. A true copy of a partially redacted memorandum from Thomas Pinkos to the Regional Board dated December 31, 2005, is attached hereto as Exhibit U. A true copy of an email note from Thomas Pinkos to Alson Brizard, Christopher Cabaldon, Karl Longley, Lucille Palmer-Byrd, and Robert Schneider, dated January 14, 2005, entitled "Hilmar Addenda" is attached hereto as Exhibit V. A true copy of excerpts from the deposition of Thomas Pinkos, taken on August 17, 2005, is attached hereto as Exhibit W.

59. More specifically, in early October, 2004, members of Regional Board enforcement staff, unbeknownst to Hilmar, had discussions with Chris Bowman, a staff writer for the Sacramento Bee, inaccurately portraying the conduct of Hilmar. (*See* Exhibit J, RWB-023816-023819, -023534; *see also* Exhibit K, emails from Thomas Pinkos and Thomas Howard.) In the discussions, staff failed to inform Mr. Bowman of certain key facts, including: (1) that Hilmar's WDRs were significantly more restrictive than those imposed upon other Central Valley food processors (Hilmar was supposed to make its end-of-pipe discharges to land meet the low-end salinity standard for drinking water at the tap and reduce the EC level of its end-of-pipe discharge water below the EC level of its pre-processing intake water), (2) that the WDRs were both technically and economically unachievable at the time they were issued and at the present time, (3) that Hilmar over the years had consistently and in good faith embarked upon compliance strategies supported and encouraged by Regional Board staff, and (4) that Hilmar had spent millions of dollars, far more than any other Central Valley food processor, attempting to bring itself into compliance with the largely unachievable and unsustainable WDRs applied to

Hilmar. (Some of these matters were finally acknowledged by Regional Board staff in the ACLC Staff Report in this ACLC proceeding issued on or about April 8, 2005.)

60. After the publication of a slanted and highly inaccurate newspaper article in the Sacramento Bee authored by Chris Bowman entitled "From Cheese to Pollution: Environmental Injustice," Sacramento Bee (Dec. 12, 2004), a true copy of which is attached hereto as Exhibit X, which article criticized Hilmar's conduct with respect to the alleged discharge of wastewater to land, Chairman Schneider apparently concluded, based on that article and not on any evidence, that Hilmar was guilty of violating the Board's waste discharge requirements and that the Board was being perceived as a weak enforcer and should defend its reputation by imposing an unprecedented large civil penalty against Hilmar.

61. Regional Board Chairman Schneider then caused a Notice to be posted on the Regional Board's website in late December 2004, about two weeks after the article was published, indicating that he wished to have a closed session of the Board at its meeting on January 27-28, 2005, "to evaluate the performance of its executive officer and other employees relative to the operation of the Fresno office." (See Exhibit L, Central Valley Regional Board Web Site Notice (Dec. 30, 2004); Exhibit M, "Official in Trouble Over Cheese Waste," Sacramento Bee (Jan. 1, 2005).)

62. Chairman Schneider stated: "Our goal is to ensure that our board is doing the best job possible to protect the waters of this state. [The Bee story] makes it clear that hasn't occurred. We want to find out why." (See Exhibit M, "Official in Trouble Over Cheese Waste," Sacramento Bee (Jan. 1, 2005).) Board member Alson Brizard stated: "We were not aware of 90 percent of what was reported. I as a board member would have liked to have known before I read it in The Sacramento Bee." (*Ibid.*) Mr. Brizard also stated: "I want to hear from staff why this occurred, why it wasn't brought to us, why enforcement actions weren't taken before now." (*Ibid.*)

63. According to the Bee, another unidentified Board member stated that "he and the board chairman were angry to learn from a Sacramento Bee story rather than board staff that the politically connected Hilmar Cheese Co. has been flooding acres of fields daily with

putrid wastewater from its sprawling plant south of Turlock” (a statement which Hilmar disputes). (*Ibid.*)

64. Chairman Schneider told reporters he wanted “to ask employees why the cheese maker’s violations went unpunished for so long under their watch.” (*See* Exhibit N, “Open Water-Panel Meeting Urged,” Sacramento Bee (Jan. 26, 2005).) He said: “I want the public to feel that we are aggressively addressing this problem, and that we don’t want to have reoccurrences.” (*Ibid.*)

65. The Board’s closed-door personnel hearing was scheduled in order “to evaluate the job performance of their executive officer and other employees relative to enforcement, particularly in the Hilmar case.” (*See* Exhibit O, “Hilmar Co-owner Quits his State Post,” Sacramento Bee (Jan. 27, 2005).) According to the Bee, Chairman Schneider said “the board may hold a public hearing at a later date to further explore the failure to penalize the cheese maker.” (*Ibid.*) The Bee further noted that “[t]he board’s probing comes as a result of The Bee’s investigation of the cheese factory.” (*Ibid.*)

66. At a meeting on January 21, 2005, I was asked by Bert Van Voris to provide additional information concerning Hilmar’s conduct to take “the guesswork” out of the Regional Board staff’s evaluation of Hilmar. However, later that same day, after the request for the information was made, Mr. Van Voris called to advise me that enforcement action against Hilmar was going to be initiated immediately and that the additional information would not be required.

67. On January 26, 2005, just one day prior to the scheduled personnel hearing and without the benefit of the information requested by Mr. Van Voris, Executive Officer Pinkos issued the ACLC, proposing an unprecedented \$4 million civil penalty for Hilmar. However, the “skeleton” two-page ACLC was not issued simultaneously with a supporting Staff Report. Instead, Regional Board staff took an additional (and apparently unprecedented) ten weeks after the ACLC was issued to prepare and issue its supporting Staff Report.

68. Executive Officer Pinkos’ issuance of the ACL complaint in the face of the impending personnel hearing and without a supporting Staff Report appears clearly to have

been accomplished to save the Executive Officer's job. Regional Board enforcement staff have acknowledged that the ACL complaint was "rushed". (See Exhibit P, email from Jo Anne Kipps to Michael Cook.)

69. On January 27, 2005, a month after the Notice scheduling the personnel hearing was issued and just one day after the Executive Officer issued the ACL complaint, the previously scheduled closed personnel hearing occurred. What happened at the meeting was described as follows: "Recent articles in the Sacramento Bee regarding the Hilmar Cheese Company, its waste discharges and regulatory actions by the Regional Board gave rise to a perception and/or concerns held by some observers that the Regional Board does not enforce against dischargers causing pollution. In response to this, the Regional Board met in closed session at its 27/28 January 2005 meeting to evaluate the performance of its Executive Officer and other employees relative to the operation of the Fresno Office. When the Board returned to open session, the Board Chair stated that the Regional Board expressed its confidence in the leadership of the Executive Officer, and directed staff to prepare a written report evaluating the enforcement and communications policies of the Regional Board to be discussed in open session at the March (2005) Regional Board meeting." (See Exhibit Q, Buff Sheet, Agenda Item 22, Central Valley Regional Water Quality Control Board Meeting of March 17/18, 2005.)

70. Indeed, Executive Officer Pinkos acknowledged under oath at his deposition that he issued the ACLC the day before the January 27, 2005 closed session, because he was aware that the outcome of the closed session might be the termination of his job. (See true copies of excerpts of Mr. Pinkos' deposition taken on August 17, 2005, attached hereto as Exhibit W.)

71. Mr. Pinkos also acknowledged at his deposition under oath that the subsequently drafted Staff Report did not present all the evidence. Instead, the Staff Report presented the prosecution staff's position in an effort to justify, after the fact, the \$4 million proposed penalty, and excluded evidence and considerations that might weigh in favor of Hilmar. Mr. Pinkos testified that he expected Hilmar to present its defense position in the ACLC proceeding, and the Regional Board to weigh the evidence and render a just decision. (See true

copies of excerpts of the deposition of Thomas Pinkos taken on August 17, 2005, appended hereto as Exhibit W.)

72. At the Board meeting of March 17/18, 2005 , Board member Christopher Cabaldon stated: “The thing so frustrating about Hilmar is that we employed so many staff on that operation, and we hadn’t achieved the enforcement objective.” (*See* Exhibit R, “Hilmar Fiasco Spurs Changes,” Sacramento Bee (Mar. 19, 2005).) And Chairman Schneider “cited the Hilmar case . . . as he opened a public hearing on changes under way to improve enforcement.” (*Ibid.*)

73. Under these facts, it appears abundantly clear that Chairman Schneider (and perhaps other members of the Regional Board) used the threat that the Board would terminate Executive Officer Pinkos’ employment or take other adverse employment action against Executive Officer Pinkos at its January 27, 2005 closed session meeting to pressure Executive Officer Pinkos into initiating unprecedented strong enforcement action against Hilmar. That is precisely what Executive Officer Pinkos did, issuing a complaint proposing the largest ACL penalty in Regional Board history. The public statements made by Chairman Schneider reported in the press well before any hearing and, in several cases, before the filing of the ACLC, as well as internal communications Hilmar has obtained in discovery, appear to show that Chairman Schneider has prejudged the question of Hilmar’s guilt with respect to the allegations of the ACLC without hearing any of the evidence. Further, I understand that at his deposition Mr. Pinkos indicated that Mr. Schneider told him, without having heard any of the evidence in this ACLC proceeding, that prosecution staff should settle the case for at least \$2.5 million. (*See* true copies of excerpts of the deposition of Thomas Pinkos taken on August 17, 2005, attached hereto as Exhibit W.)

Conclusion

74. The unprecedented proposed penalty, which Hilmar believes to be grossly excessive and unfair, is plainly at odds with Hilmar’s having worked closely with the Board staff to accomplish what no other company has been asked to do or tried to do in terms of removing minerals from wastewater. Hilmar remains greatly concerned by the magnitude of the proposed

fine and the precedent it sets. Hilmar has been working in cooperation with the Board and Board staff for the past decade. During this period, Hilmar has attempted to be a good environmental steward by investing tens of millions of dollars in improved water treatment technologies. Having a fine of the extraordinary magnitude of the fine proposed here retroactively levied against Hilmar for a period in which the company was working diligently toward compliance – and had been promised a time schedule within which to deploy additional technologies and processes in an effort to achieve compliance – ignores the significant efforts and unprecedented financial resources the company has invested in water treatment technologies. This action also sends a message that businesses risk punishment for consulting and cooperating in good faith with regulatory authorities.

75. This concludes my prepared direct testimony in this matter.

List of Exhibits

Exhibit A	True copies of letters from community members in support of Hilmar
Exhibit B	A true copy of Hilmar's petition for a writ of mandate challenging the Basin Plan
Exhibit C	A true copy of Hilmar's State Board petition challenging the denial of Hilmar's request to modify the WDRs in its permit
Exhibit D	True copies of documents prepared by Jay Hicks detailing planning for Hilmar expansion beginning in 1998
Exhibit E	A true copy of a letter from Gary Carlton, Executive Officer of the Regional Board, providing that Hilmar would be receiving a new permit covering Hilmar's increased flow and providing a time schedule for compliance
Exhibit F	A true copy of excerpts from the deposition of Bert Van Voris, taken on August 24, 2005
Exhibit G	A true copy of an aerial schematic of Hilmar's state-of-the-art wastewater treatment facility in color
Exhibit H	A true copy of a transcription of the audio-tapes of the July 11, 2005 State Board workshop on food-processing discharges
Exhibit I	True copies of the written comments submitted by the participants in the July 11, 2005 State Board workshop on food-processing discharges
Exhibit J	True copies of an email memorandum from Bert Van Voris to Loren Harlow and Thomas Pinkos dated October 8, 2004, entitled "Media Contact regarding HCC" and an email note from Ken Landau to Tom Pinkos dated October 19, 2004 entitled "Hilmar Cheese EO Report" (RWB-023816-023819, -023534)
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