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February 9, 2006

The Honorable A.G. Kawamura, Secretary
California Department of Food and Agriculture
1220 N Street
Sacramento, CA 95814

Re: Dairy Institute Petition for a Class 4a & 4b Hearing

Dear Mr. Secretary:

Western United Dairy Men respectfully requests that the petition submitted by the Dairy Institute be denied. The Dairy Institute seeks adjustments to the manufacturing cost allowances for nonfat dry milk, cheddar cheese, and dry whey as well as adjustments to the f.o.b. price adjuster, dry whey component, and cheese yield. The requested adjustments will result in a substantial reduction in producer prices.

The timing could not be worse for the call of a hearing that seeks to lower producer prices. A brief review of recent history reveals that producers have already borne a significant reduction in their regulated minimum price to the direct benefit of the processing industry. It was just a year ago that a Class 4a and 4b hearing resulted in an average \$0.11 per hundredweight drop in producer prices. Now the Dairy Institute is asking for yet another, and even more drastic, reduction. In the meantime, producers have seen an additional reduction in their prices resulting from the settlement of the Hillside/Ponderosa lawsuit against the Secretary. Finally, although data supported a change, the petition by WUD and the Alliance to align California Class 1 prices with surrounding states was denied. The Institute has made the claim that we must increase California's plant capacity to deal with the increasing milk supply. However, a long-term policy of ratcheting down prices threatens the economic viability of the producers responsible for providing those plants with milk.

Given current conditions in the industry, the years ahead will undoubtedly be more challenging for California producers. Economic and regulatory pressures are mounting on producers in the state, and no reprieve is in sight. The Dairy Institute cites a "deteriorating business climate in California" and increasing business costs as part of their rationale for the current hearing. Though we acknowledge that processors are facing challenges, we must point out that the dairy families of California are already familiar with such pressures.

Current and proposed environmental regulations placed upon producers will lead to added costs. With no way to pass along added costs, dairy producers will be left with no option but to take on additional debt or find alternative funding sources in order to comply with a myriad of new regulations. For some, these additional costs will result in the demise of their dairy operation.

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As processing plants have experienced increased energy and labor costs, so too have producers. As processing plants have experienced rising transportation costs, so too have producers. However, processing plants have the ability to pass on some of these added costs, while dairy producers have no mechanism to do so.

As production costs continue to increase for producers, they are simultaneously faced with declining income as producer prices have begun a steady trend downward. The already declining producer prices, coupled with the reductions sought by the Dairy Institute (especially after their "step-two" of eliminating the dry whey component), is an untenable economic hit for many dairy families. Many will go out of business or acquire additional debt. Neither outcome would be positive for the industry as a whole.

Finally, we are aware that the California Milk Advisory Board has invested considerable time and capital, through the work of McKinsey and Co., in conducting an economic study to look at pressures facing the California dairy industry. The results of this study could help glean information helpful in resolving many of the issues outlined in the Dairy Institute petition. The issues put forth by the Dairy Institute are large, and they will require a coordinated effort by all segments of the industry to address them in a way that ensures that both processors and producers will thrive in California.

Adjusting the components in the Class 4a and 4b pricing formulas, as suggested in the Institute's petition, is not a long-term solution to the problems they have outlined. The industry would be better served by evaluating the results of the McKinsey study rather than attempting to deal with these issues now through a hearing. Doing otherwise would risk drastically lowering producer prices while at the same time providing no guarantee that the outcome would actually resolve any of the issues at hand.

In the Statement of Determination from the last Class 4a and 4b hearing, it was pointed out that "CDFA is committed to the long-term viability of the producer, producer-cooperative and processor sectors of the California dairy industry..." As outlined above, actions have been taken recently to maintain the health of the processing sector. We ask that action now be taken to protect the viability of producers by recognizing that this is an inappropriate time to call a Class 4a and 4b hearing. We thank you for your careful consideration of this matter.

Very truly yours,

Original signed & mailed

Michael L. H. Marsh, CPA
Chief Executive Officer

cc: A.J. Yates, CDFAs Undersecretary
David Ikari, Dairy Marketing Branch Chief
Board of Directors, Western United Dairymen