REVIEW OF THE MARKET STRUCTURE OF THE LIVESTOCK INDUSTRY

HEARING

BEFORE THE

SUBCOMMITTEE ON LIVESTOCK, DAIRY, AND POULTRY

OF THE

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HEARING TO REVIEW THE MARKET STRUCTURE OF THE LIVESTOCK INDUSTRY

TUESDAY, APRIL 17, 2007

HOUSE OF REPRESENTATIVES,
SUBCOMMITTEE ON LIVESTOCK, DAIRY, AND POULTRY
COMMITTEE ON AGRICULTURE
Washington, DC.

The Subcommittee met, pursuant to call, at 11:00 a.m., in Room 1300 of the Longworth House Office Building, Hon. Leonard Boswell [Chairman of the Subcommittee] presiding.

Members present: Representatives Boswell, Gillibrand, Kagen, Baca, Costa, Hayes, Rogers, King, Smith, and Walberg.

Staff present: Chandler Goule, Scott Kuschmider, John Riley, Sharon Rusnak, Debbie Smith, Kristin Sosanie, John Goldberg, Alise Kowalski, Pam Miller, Pete Thomson, and Jamie Weyer.

STATEMENT OF HON. LEONARD BOSWELL, A REPRESENTATIVE IN CONGRESS FROM THE STATE OF IOWA

Mr. BOSWELL. We will call the meeting to order, and we thank you for coming and the interest and the presence here today. We appreciate you joining us, Mr. Hayes and myself. I would like to give a special thanks to our witnesses for the preparation you have made and for testifying before us today to offer insight into the market structure of the livestock industry. I appreciate this opportunity to hear what the current issues facing the market structure of the livestock industry are and how those issues are affecting producers across our country. The overarching issues that I hope this hearing does not forget is that we, as the agricultural community, must ensure that we have a safe and plentiful food supply. We need assurances that producers can make a living, while the processors and packers have enough product available to provide consumers in the United States with a reliable and safe food supply.

With land prices at record numbers, the livestock industry is one of the last sectors of the agricultural industry that young, first-time farmers are able to get involved in. We need to ensure that there is adequate market access for those producers to make a living. The livestock industry has been extremely beneficial to rural development. I see this all over my home State of Iowa. We must ensure that the livestock industry stays strong and continues to contribute to rural communities.

Over the last 20 years, the livestock industry has become more and more consolidated. A prime example is in the poultry industry. This concentration in the livestock industry raises many concerns on what the future may hold for independent producers. Unfortunately, this is not a cut-and-dry issue. There are many factors that contribute to the structure of the livestock market, and today I hope this hearing will address many of those. We will hear testimony today that the packing industry not only influences the livestock market, but dominates it with over 80 percent of beef, 60 percent of swine and almost 60 percent of the poultry markets, dominated by four packers. After reading through the testimony submitted today, many argue that there is adequate competition in the livestock industry. But when 60 to 80 percent of the respective livestock industries are dominated by four packers, when is this concentration cause for concern? Now or when it hits 90 percent?

Independent livestock producers often contend that the lack of buyers of their livestock and the use of captive supplies for packers has a negative impact on the price they ultimately receive for their animals. Because packers can utilize their own animals for daily slaughter needs, they purchase fewer animals on the spot market. Some contend the reported price for livestock does not accurately reflect prices paid to the producers. A concern I hear over and over again from producers in my district is that large packers can control market prices using the packer ownership. Let us say a packer owns tens of thousands of heads of cattle. That packer buys on the open market for four days, but when the prices get too high, they go and slaughter the cattle that they own, thus depressing market prices. How is this not manipulation in the open market? And how do we as an industry regulate this?

We also looked at study done by USDA to review the issue. RTI International was contracted to study the market structure of the livestock industry and recently published their Livestock and Meat Marketing Study. I am interested to hear what RTI has to say and was very interested in the results of the study. I also look forward to hearing what our producer panels have to say. I understand this is a difficult issue to discuss, especially when the industry is extremely concentrated, but I appreciate your willingness to share your story and your candor.

After reading through the testimony for this hearing, two issues grabbed my attention, animal identification and country of origin labeling. There are various opinions out there about both of those topics and some discussion has centered on merging the two together. This is a new approach in attempting to address these issues and we welcome discussion on this issue. One thing that many of the witnesses focused on in their written testimony was alternative marketing arrangements (AMA), such as forward contracts, making alliances between packer ownership. I have concern if these AMAs actually help the market or suppress the market price. I welcome conversation about these issues and their problems and concerns of, or lack thereof, regarding these issues.

As we started this farm bill discussion, there has been much talk if there will be a competition title in the farm bill. I welcome the opportunity to further that discussion with varying opinions. Thank you again for joining us here today. At this time, I would like to turn it over to my friend and colleague, Mr. Hayes, from North Carolina, for opening remarks he would like to make.

STATEMENT OF HON. ROBIN HAYES, A REPRESENTATIVE IN CONGRESS FROM THE STATE OF NORTH CAROLINA

Mr. HAYES. Thank you very much, Mr. Chairman. We are friends and it is a pleasure to work and serve with you, particularly on behalf of agriculture and the livestock segment that we are looking at this morning. Chairman Boswell has called today's hearing to discuss the structure of the livestock and poultry industry. We will hear from the US Department of Agriculture's Grain Inspection, Packers and Stockyards Administration, GIPSA, whose role is to regulate and maintain fair competition among the livestock industry. Also joining USDA is RTI International, based in Research Triangle Park, North Carolina, who conducted an extensive study on livestock and meat marketing. Our other two panels consist of producer groups and various associations interested in the economics of the livestock sector, who will share their perspective on these issues.

Let me start off by assuring all of those present, and listening today, that I support the full and rigorous enforcement of all laws intended to ensure a fair, orderly and transparent livestock market function. While we may differ about the future shape of policy in the area of market structure, I know of no disagreement about the fundamental need for strict enforcement of the authority under the Packers and Stockyard Act.

After resisting the temptation in the last farm bill to further insert the Federal government into the structure of livestock markets, Congress made a commitment in the conference report to look into this matter further. For this reason, in June of 2003, I took this subcommittee to Grand Island, Nebraska to examine this topic. While most of the testimony that day centered on the specific idea of banning packer-owned livestock, discussions ranged across virtually all the ideas regarding industry structure and we had a very informative hearing. For me, the most important impression from that hearing was a wide divergence of views held by the witnesses. We had testimony from both producers and packers from Nebraska and my home State of North Carolina, and while all witnesses shared a common desire for a profitable livestock production sector, with an orderly market operation, there was virtually no consensus along any lines about whether the proposed changes would improve conditions or harm those they were intended to help. In 2003, Congress has recently appropriated $4.5 million in funding to produce GIPSA's Livestock and Meat Marketing Study, which was just published on February the 16th by RTI International. We did not have the benefit of this report at our hearing in Nebraska and I look forward to today's testimony on the study's findings.

Mr. Chairman, as you and other members of the committee, the industry structure issues invoke passion and long-held beliefs from livestock producers across the country. What producers in the 8th District of North Carolina want, and what producers in the 3rd District of Iowa want, can be two completely different things. I personally believe the complexity and intricate details of marketing and competition issues deserve more than one hearing before any decisions are made. I do not believe these issues should be considered as part of any farm bill discussion, as the laws governing the industry structure are completely separate from that of the farm bill and should be kept that way. These issues should be considered in their form and given the proper attention they deserve. And I appreciate all of the witnesses for here today to discuss this important issue and I appreciate the chairman calling the hearing.

Mr. BOSWELL. Thank you, Mr. Hayes. And I would request that, I see we have Mr. Smith here, any statements you want to be included for the record? We will proceed on to get on to our testimony. So thank you very much. I would now turn to the panel. I would like to remind our witnesses that you have five minutes for your oral testimony, and due to the number of witnesses and other time constraints, it will be important that we try to stay within those guidelines. I think we have—down there ready to take care of the timing, so we don't have to worry about that, and then we want to get to our questions. So we would like to welcome our first panel to the table. Administrator James Link, Grain Inspection, Packers and Stockyards Administration, the Department of Agriculture, along with Ms. Mary Muth, Program Director for Food and Agricultural Policy Research, RTI International, Research Triangle Park, North Carolina. Administrator Link, we would be happy to hear what you have got to share with us. Thank you for being here, just hit your button there.

STATEMENT OF JAMES E. LINK, GRAIN INSPECTION, PACKERS AND STOCKYARDS ADMINISTRATION, UNITED STATES DEPARTMENT OF AGRICULTURE

Mr. LINK. Mr. Chairman and members of the subcommittee, good morning. My testimony will provide an overview of trends in the critical components of the US livestock market and changes that GIPSA has made. Although I am relatively new to Washington, DC and the US Department of Agriculture, I am certainly no stranger to the agriculture industry. Growing up on a farm and devoting my entire professional career to agriculture has given me a rich and diverse background from which I speak to you today. Shortly after my arrival at GIPSA, I was briefed on an ongoing audit from the Office of the Inspector General. In response to that audit, over the past year we have worked extensively to enhance GIPSA's ability to regulate livestock marketing and procurement practices. Now I would like to discuss the current market trends that we are monitoring.

In the beef cattle, the four largest steer and heifer slaughter firms have accounted for 82 percent of the total annual slaughter in the year of 2006. In pork, the four largest slaughter firms account for about 64 percent of the total slaughter. Sheep and poultry are relatively constant at 70 percent and 53 percent, respectively. Let me share with you the current marketing tools used in the livestock industry. Producers and packers use multiple marketing methods to market the livestock for slaughter, but the methods commonly fall within two categories: cash sales or spot market, and committed procurement or alternative marketing arrangements, which include the variations of formula pricing, forward contracts and packer ownership.

In 2006, the four largest firms that slaughter fed cattle purchased 70 percent of their supply on the cash market and 30 percent through alternative marketing arrangements. In the same time period, approximately 10 percent of hogs were sold on the spot market, 20 percent was packer owned and 70 percent were through forward contracts and alternative marketing arrangements. In the poultry industry, the spot market is virtually nonexistent. Now that you have had a brief summary of the livestock industry, I want to give you an overview of the improvements we have made to better ensure farmers and ranchers are protected.

We have taken positive steps to change and improve our organization. At headquarters, we have eliminated a complete layer of management in the Packers and Stockyard Program by dissolving the Regional Operations Division and having our regional managers report directly to our deputy administrator. We established a unit called Management Shared Services to eliminate duplication and improve our efficiency. In the past year, we have undertaken a top-to-bottom review of all of our regulations and policies. As a result, several regulatory work plans affecting the livestock and poultry industries have been developed for public comment. We have also issued over 40 internal directives and policies, which provide instructions and guidance to our employees. We are sending all of our investigators to the Federal Law Enforcement Training Center for basic investigative and interviewing training. We have made this course available to several attorneys from the Office of the General Counsel. We are also working on additional training activities with the Department of Justice to be conducted later this year.

We have developed a new business plan and we have laid out four primary goals and 33 strategic activities with related measurable outcomes to evaluate the results. An example of our business plan includes inspecting scales and carcass evaluation devices in all packing plants that kill over 1,000 head of livestock per year. In April of this year, we implemented the new standard operating procedures nationwide. Investigations are our top priority. For example, in the year 2005, there were 37 cases referred to the Office of General Counsel. In 2006, we referred 75 cases and in the first six months of this year, we have referred 53 cases. As our efficiency is improved, I expect the case numbers to continue to increase.

There are significant cases that we are working on currently. Five open investigations are on manipulation of cash prices and we are working with the Department of Justice on one of the investigations. There are two open investigations involving allegations from cattle sellers using formula or non-cash market arrangements that were not paid properly. We have three open investigations focusing on allegations of unfair and discriminatory behavior. We will continue to adjust our regulatory efforts to more efficiently and effectively monitor the regulated industries as the industry changes.

I am proud to serve as the administrator for GIPSA in a time where not only the industry, but also the organization, is being evaluated, assessed and improved. It is exciting to be part of these such fundamental changes. With the continued work and efforts of individuals within GIPSA, we will look forward to improving and becoming even better. Mr. Chairman, thank you again for the opportunity to appear before you today, and I will be happy to answer any questions that the members might have.

Mr. BOSWELL. Thank you for your introduction and comments. Before it comes to questions, we would first like to hear from Ms. Muth.

STATEMENT OF MARY MUTH, PROGRAM DIRECTOR FOR FOOD AND AGRICULTURAL POLICY RESEARCH, RTI INTERNATIONAL

Ms. MUTH. Good morning, Chairman Boswell and members of the subcommittee. My name is Mary Muth and I am Director of the Food and Agricultural Policy Research Program at RTI International, an independent, not-for-profit research organization in North Carolina. I was the project manager for the congressionally-funded GIPSA Livestock and Meat Marketing Study that was completed earlier this year. I am an agricultural economist and have a Ph.D. in economics from North Carolina State University. I have been conducting analyses of the livestock and meat industries for almost 15 years. In addition, my husband's family owns a cow/calf operation in western Kentucky. I am pleased to be here and thank you for the opportunity to provide an overview of the findings of the Livestock and Meat Marketing Study.

The study was conducted from July 2004 through January 2007 by a team of researchers at RTI International, Iowa State, North Carolina State, Montana State and Colorado State Universities and the Wharton School. The study addresses the economic effects that alternative marketing arrangements have on the livestock and meat industries. As you know, the cash for spot market includes auctions, direct trade and use of dealers and brokers. In contrast, alternative marketing arrangements include all other marketing methods, such as marketing agreements, marketing and production contracts, packer ownership and forward contracts.

In the final report for the study, we analyzed the extent of use and price differences of marketing arrangements and the effects of using alternative marketing arrangements on cash market prices, the costs and benefits of various marketing arrangements, particularly as they relate to product quality, cost of production and risk, and finally, the implications of using marketing arrangements on livestock producers, meat packers and meat consumers. We used state-of-the-art economic modeling and statistical analysis methods to address the requirements of the study, using industry survey data, transactions data and profit and loss statements from packers, industry interviews and publicly-reported USDA data, including mandatory price reporting data.

In general, the study found that use of alternative marketing arrangements provides benefits, not only to meat packers, but also to livestock producers and meat consumers. Therefore, restricting their use would have negative economic consequences on most segments of the industry. However, the cash market serves an important role in the industry, particularly for smaller producers and packers. Next, I would like to give a broad overview of the specific results of the study.

First, regarding the volumes and prices of livestock under different types of marketing arrangements. Based on the data available for the study, we estimate that alternative marketing arrangements represent 38 percent of the volume for fed cattle, 89 percent for finished hogs and 44 percent for fed lambs sold to packers. Furthermore, we estimate that packer ownership volumes represent less than five percent of fed cattle and fed lamb volumes, and 20 to 30 percent for finished hogs. Based on the industry surveys and interviews we conducted, we expect the use of alternative marketing arrangements in the beef and pork industries to remain similar to past use but to increase somewhat in the lamb industry.

In the beef industry, prices for fed cattle are similar for direct trade and marketing agreements, higher for the small percentage of auction barn cattle and lower for the small percentage of forward contract cattle. We found that a reduction in the volume of spot market transactions, assuming that volume is shifted into alternative marketing arrangements, results in an extremely small decrease in the spot market price. In the pork industry, prices for finished hogs are higher for marketing contracts and lower for packer-owned hogs, relative to the cash market, and we found that there would be a relatively large effect of further increases in the use of alternative marketing arrangements on cash market prices for hogs.

Second, regarding the costs and benefits of alternative marketing arrangements related to cost of production in the beef industry, procurement of cattle through alternative marketing arrangements is associated with lower production costs per head than through cash markets, but this result does not hold for all packing plants in the data set. In the pork industry, procurement of hogs through alternative marketing arrangements is associated with a small decrease in production costs at the packer level. Related to quality of beef and pork in the beef industry, we found that cattle sold through marketing agreements were higher quality and had less variation in quality than cattle sold through direct trade. Similarly in the pork industry, we found that hogs sold through marketing contracts were higher quality than hogs sold through direct trade. Related to market access and price risk across all species, we found that alternative marketing arrangements offer some guaranteed market access for both livestock producers and meat packers. And furthermore, the alternative marketing arrangements generally reduce price or income risk for cattle and hog producers.

Third and finally, regarding implications of the use alternative marketing arrangements, we conduct simulations of various hypothetical scenarios in which alternative marketing arrangements were restricted. Across all species, the results for economic modeling simulations indicate losses to livestock producers, meat packers and consumers due to losses in efficiencies in the market. These losses in efficiencies translate into higher prices for consumers purchasing meat, and lower prices for producers selling livestock.

Mr. Chairman, I would like to enter into the record Volume I of the report for the Livestock and Meat Marketing Study. This volume contains the executive summary and the overview for the study. Thank you. I would be happy to answer any questions.

Mr. BOSWELL. Thank you for your testimony and your submitted testimony that we received. With no objections, we will enter it into the record. We will turn to our questions now for a little bit. I will start off addressing you, Mr. Link. Stated in your written testimony, you mentioned that marketing agreements account for 24 percent of the total procurement in 2006 by the four largest steer and heifer slaughter firms. Do you know the number or percent of grid cattle and Canadian cattle imported by packers?

Mr. LINK. No, sir, I do not have a breakdown of that. I can get that information for you and return it, but I don't have a breakdown. We lumped all of the alternative marketing arrangements into the one percentage figure and I don't have a breakdown of it.

Mr. BOSWELL. Okay. Do you have any comments you would want to make about it? Although, we will be happy to receive any further information. Do you have any comments you want to make on that issue?

Mr. LINK. Well, it would be pretty dangerous for me to speculate on it. I would assume that the larger volume would be the livestock that are sold on some type of a formula basis, but I would hate to venture a figure on to that.

Mr. BOSWELL. We will look forward to get that information. You recognized the enforcement of the Packers and Stockyards Administration. In your testimony, you briefly mention having complaints from producers. What is currently going on to address these things. Where are you at in that process?

Mr. LINK. We have what we refer to as a rapid response team that is available. Any time a producer calls in with a specific complaint, we initiate a rapid response to that complaint to look into it to see if it is valid and whether it warrants a follow-up investigation.

Mr. BOSWELL. So you are satisfied with how it is working out, or do you have any——

Mr. LINK. As we develop more confidence in our producers, we will probably have more complaints. Now, we have a 24-hour hotline plus all of our regional field offices that operate on normal hours and I am a little bit surprised that we don't have more complaints come in directly to us that we can respond to.

Mr. BOSWELL. Okay. Thank you. I may come back to you in a minute, but I would like to direct a question or two to Ms. Muth. Thank you for your testimony. In my opening statement, I mentioned a reoccurring concern I hear from producers, not only in my State, but across the country. Large packers can control market prices using packer ownership. Let us say a packer owns tens of thousands of heads of cattle. The packer buys on the open market for three days, but when prices go too high, they go out and slaughter their own, the cattle that they own, which of course would depress market prices. Is this not manipulation of the open market? Is it in your opinion?

Ms. MUTH. Well, based on what we looked at for our study, we conducted statistical analyses to look at what the effects are of use of alternative marketing arrangements on cash market prices, and what we found in the beef industry is that the packer ownership actually represents a fairly small percentage of the volume of cattle that are purchased and that the effects of that packer ownership is actually relatively small, in a statistical sense, in the cash market.

Mr. BOSWELL. What percentage would that be?

Ms. MUTH. Based on the data that we have for the study, approximately a 10-percent increase, additional increase, in the use of alternative marketing arrangements would depress cash market prices by about 0.1 percent.

Mr. BOSWELL. Okay. I am just kind of hip shooting here, but on your methodology, how you went out to get that data, is that available for us to look at?

Ms. MUTH. The data that we collected for the study was collected under CIPC, which means that it is protected data, that it can only be used for statistical purposes. And so we have followed very strict data security protocols in using that data.

Mr. BOSWELL. What percentage do you think of all the market data out there did you actually look at then?

Ms. MUTH. For the beef cattle industry, our estimate is that the data represents probably around 90 percent of the volume of transactions that occurred over the 2 1/2 year period. For hogs, the data that we looked at represented about 75 percent of the volume of the transactions.

Mr. BOSWELL. I may come back to that. Well, I think I will stop here and defer to Mr. Hayes, then I will come back. Mr. Hayes.

Mr. HAYES. Mr. Link, in your statement, you suggest that larger packers have lower operating income due to them paying a higher average price for livestock. With the buying power they have, why would these packers pay more for livestock?

Mr. LINK. Well, basically, it gets down to being able to better utilize their facilities. You have a set fixed cost on any kind of a processing plant and the more they can run that at its optimum operational standpoint, the less their production cost is going to be overall and so they are able to pay more for the livestock to make sure that they stay up at that optimum level of production.

Mr. HAYES. Ms. Muth, as I understand your study, you generally assert that alternative marketing arrangements, on balance, benefit the livestock sector. What I want to clear up is this. Do these benefits go solely to those who participate in arrangements, or do others in the production sector benefit as well?

Ms. MUTH. Well, based on the analysis that we conducted, we were looking at the aggregate effects of the use of these alternative marketing arrangements, and because packers can realize efficiencies in using alternative marketing arrangements, that can benefit producers that also do not participate, because it helps the functioning of the packing plant itself.

Mr. HAYES. So it is across the board. How does one reconcile the often-heard assertion that packers manipulate the market with the fact that cattle and hog prices move up and down?

Ms. MUTH. I am sorry. Could you repeat that?

Mr. HAYES. Often you hear the assertion that packers are manipulating the market. The fact that cattle and hog prices move up and down, how do you reconcile——

Ms. MUTH. Right. For the analyses that we conducted, we were looking at the relationships in the data. We did not look at the intent. There isn't a way for us to analyze what the intention of people are when they are making their buying and selling decisions. We assume that they are operating in an economically efficient manner for their operations, whether they are producers or packers. And so in terms of manipulation and saying whether particular individuals were doing things to manipulate the market, that goes beyond what we looked at in our study, which focuses on the statistical and economic relationships in the data.

Mr. HAYES. Thank you, Mr. Chairman. I have no further questions for this panel.

Mr. BOSWELL. Okay, thank you. The chair at this time would recognize the gentleman from Nebraska, Mr. Smith.

Mr. SMITH. Thank you, Mr. Chairman. When I meet with representatives from the livestock production sector, specifically producers, we ask about the status of the regulatory process to implement the reauthorization of mandatory price reporting. Mr. Link, could you update the subcommittee on that subject?

Mr. LINK. I can just give you a ballpark update, because that is really through the Agricultural Marketing Service. It is in the process of going through the steps that it has to be for reauthorization and I can't tell you exactly where they are in it. I would assume that, you know, it is in the channel, but I couldn't give you a date as to when that will be completed.

Mr. SMITH. Okay, thank you. Let me see what hasn't been covered already. I think that is good for now. Thank you.

Mr. BOSWELL. Thank you. The chair would recognize the gentleman from Wisconsin, Mr. Kagen.

Mr. KAGEN. Thank you. It is nice to be here in this wonderful new room. Administrator Link, we are all familiar with the decision in Pickett v. Tyson, which the jury ruled that the packer was guilty of price manipulation and assessed a fine of $1.2 billion. Even though it has been tossed out, how has GIPSA responded to the price manipulation and prevented it from occurring in the future?

Mr. LINK. Well, as I mentioned earlier, we are monitoring the market basically on a daily basis. We are utilizing Agricultural Marketing Service price reporting data. We are also monitoring the different prices that are available in different regions and we look for any anomaly that may appear from there. And of course, if there is any kind of complaint that comes in, we instantly respond to that. But we are really basing it by looking at economic analyses of the information that we receive to see if there is any anomalies that would warrant an investigation into it.

Mr. KAGEN. So with the Pickett v. Tyson case being the only antitrust case in the past 80 years, being that I am from Green Bay Packerland and Packerland had a great deal to do with the naming of our football team, how can our packers and our producers have confidence that your bill will ensure a fair marketplace for them? One case in 80 years?

Mr. LINK. Well, sir, that wasn't a case that GIPSA brought forth. That was a private individual case against a packer and we really weren't involved in it.

Mr. KAGEN. So you are monitoring the situation?

Mr. LINK. Yes, sir.

Mr. KAGEN. Do you feel that mandatory arbitration is an equal arrangement for both the packer and the producer?

Mr. LINK. I am not familiar with that, sir. I can't give you an intelligent answer.

Mr. KAGEN. All right, we can get back on that.

Mr. LINK. Yes.

Mr. KAGEN. Thank you very much, Mr. Chairman.

Mr. BOSWELL. Thank you. The chair would recognize Mr. Walberg from Minnesota.

Mr. WALBERG. Thank you, Mr. Chairman. I hail from Michigan and I don't want to——

Mr. BOSWELL. Oh, excuse me.

Mr. WALBERG. —put an aspiration on Minnesota because of me.

Mr. BOSWELL. I stand corrected and we welcome the gentleman from Michigan.

Mr. WALBERG. Being a freshman, I expect those mistakes occasionally, so no problem at all. Let me ask, Dr. Muth, a two-point question. What impact has consumer demand had on the usage of alternative marketing agreements? And secondly, what potential impacts would the consumer face if alternative marketing agreements were limited?

Ms. MUTH. I guess, related to your second question, based on the simulations that we conducted from our models, if alternative marketing arrangements were restricted, consumers would actually be faced with higher meat prices and probably also reduced quality of meat products, that there would be much more variability in the quality of products. And I am sorry, what was your first question again?

Mr. WALBERG. What impact has consumer demand had on the usage of alternative marketing agreements?

Ms. MUTH. Okay. In terms of the effect of consumer demand on use of alternative marketing arrangements, it is our understanding, based on looking at the relationships in the data, that in order to supply sufficient quality of livestock to meet consumer demand, that packers use alternative marketing arrangements to ensure that they can supply the quality that consumers would like to buy in their grocery store.

Mr. WALBERG. Okay. So you say it is better for the consumer all along the process?

Ms. MUTH. Right, consumers do benefit. And when we conducted simulations of our economic models, where you put a hypothetical restriction on the use of alternative marketing arrangements, we did find that consumers would lose under those scenarios.

Mr. WALBERG. Okay, okay. Again, customers frequently want to buy meat that has a certain characteristic, such as grade or antibiotic free or organically produced.

Ms. MUTH. Right.

Mr. WALBERG. Packers frequently use marketing agreements to draw out the appropriate product from the producers. If these methods are curtailed, how would a packer ensure that they have a supply of cattle that meets their customers' specifications?

Ms. MUTH. I guess, based on what we looked at for our study, it would be much more difficult for packers to ensure that they could go out into the cash market and buy the animals of the specified quality that they need to meet those requirements, if they could not have an agreement with the producer that specifies those as requirements.

Mr. WALBERG. So you contend that it leaves it up in the air, that it is debatable whether there would be those specialty opportunities for consumers, then?

Ms. MUTH. Yes, it is my understanding, from what we looked at in the study, that it would reduce those opportunities for the packer.

Mr. WALBERG. Okay. Okay, thank you. Mr. Link, based on your experience and knowledge of this industry, what would be the economic costs or benefits to cattle producers if Congress were to prohibit packer ownership?

Mr. LINK. Well, I will speak from the cattle industry more than the pork because I am more familiar with that. With the small percentage that packers actually own in the cattle industry, I think it would be very insignificant. I think it would be more harmful if the alternative marketing arrangements were eliminated, because it would get more of a variability of quality of livestock on to the market.

Mr. WALBERG. Now that, again, is just based upon the limited activity at present in the cattle industry, but you can't use a crystal ball to infer what would be if it moved in the future to more aggressive action with packers being involved. I mean, it would just——

Mr. LINK. Well, it would be a tremendous business psychology change for most of them, because it would take a tremendous capital investment that they currently are not involved with to get to extend out very much into the actual raw material purchasing and ownership of them, and that would take a significant capital investment. You would have to ask the packers whether they are willing to make that type of an investment or not.

Mr. WALBERG. Okay, okay. Thank you.

Mr. BOSWELL. Thank you, Mr. Walberg. And I think that completes our first round. We will take you in a moment. I don't want to be disrespectful to the second panel, but just a couple things. Mr. Link, has the Department of Justice supplied enough staff to take care of the cases that you have referred to them? What is your status there?

Mr. LINK. Well, sir, most of our cases go through the Office of General Counsel. There are a few cases that get forwarded up to the Department of Justice and then they obviously have enough for our demand, because we don't have that many that go before the Department of Justice. Most of our active cases are handled by the Office of General Counsel.

Mr. BOSWELL. So you are getting all of the support from the DOJ, then?

Mr. LINK. Currently, yes, sir.

Mr. BOSWELL. Ms. Muth, maybe give us an estimate or an evaluation, if you could, of the use and value of mandatory price reporting. Who gains the most?

Ms. MUTH. Well, I am not certain if I can respond to exactly who gains the most, but I can tell you that mandatory price reporting is pretty crucial for the industry, that it increases the transparency of prices. A lot of the data that we looked at, formula prices, under lots of different types of marketing arrangements, including both cash marketing arrangements and alternative marketing arrangements, depend on mandatory price reporting as the base for the formula. So mandatory price reporting is crucial for the functioning of the market.

Mr. BOSWELL. So you evaluated that it is very important. And your final question is, you found that putting restrictions on alternative marketing arrangements of beef would affect the producer, packer and consumer negatively. But in pork, it would only affect the producer and the consumer, but it would cause a slight increase in economic surplus for the pork packer. Why is there such a difference and why would the packers see a slight increase?

Ms. MUTH. Right. Well, one of the things you have to consider when you are looking at the pork industry is that the volume of alternative marketing arrangements is already extremely high. It is 89 percent. So when you look at further increases beyond that point, the packer is already realizing the benefits that they would receive from using alternative marketing arrangements. So in the simulations that we conducted, if you restrict alternative marketing arrangements in the pork industry, the packers will gain in the short run, but in the long run, we actually don't really see any advantage to them one way or another. And that is looking at comparing it from current levels. And so it is important to consider that the structure of the market is very different for the pork industry versus the beef industry and that is why you see differences in those results.

Mr. BOSWELL. All right, thank you. We touched on this earlier, but where would someone go to review the data and statistical information used by the RTI study?

Ms. MUTH. The data that we have will be turned over to GIPSA by the end of May. The data is currently kept in a secure room. It is encrypted data, data sets. We will be giving them to GIPSA and at that point, then it is their determination of how that data will be used.

Mr. BOSWELL. Mr. Hayes, do you have any further questions?

Mr. HAYES. No, sir.

Mr. BOSWELL. Any other members of the committee have any other questions? Yes, Mr. Walberg.

Mr. WALBERG. Thank you, Mr. Chairman. I would like to ask Dr. Muth a final question here. As I am sure you know, individual producers have different production practices and market goals with respect to the animals they raise. Your testimony talks about the price differences across marketing arrangements. In your view, do these slight price differences occur because of the given marketing arrangement itself, or does it reflect the nature of the livestock that finds its way to a particular marketing arrangement?

Ms. MUTH. I think, in general, it does reflect differences in the quality of the animals that are coming through different types of marketing arrangements, but you do still see, even after you make the adjustments for differences in quality, that there are still slight differences, that prices for animals that are purchased through marketing contracts in the hog industry are through marketing agreements, and the beef industry has slightly higher prices than cash market prices.

Mr. WALBERG. Okay, okay. Thank you.

Mr. BOSWELL. Thank you. Well, thanks to Mr. Link and Ms. Muth. Am I pronouncing it correctly?

Ms. MUTH. Yes.

Mr. BOSWELL. Thank you. Thank you for coming and sharing with us. There is a chance you will hear some more from us, so we will be in contact with you and we appreciate your presentation here today. We would like to excuse you at this moment and we ask the second panel to take their place. We are sorry for the delay. I thank you very much for your patience. We appreciate your presence with us today and so we will just take your testimonies and we will probably start with Kay and start right down the line and hear what you have to say. Then we will have some questions for you. So Ms. Doby, you have the floor.

STATEMENT OF KAY DOBY, POULTRY GROWER, ON BEHALF OF CAMPAIGN FOR CONTRACT AGRICULTURE REFORM, RAFI

Ms. DOBY. Chairman Boswell, Ranking Member Hayes, Members of the subcommittee, my name is Kay Doby and I am a poultry grower from North Carolina, Cameron. Thank you for this opportunity to present this testimony.

The structure of US agriculture is rapidly changing and the focus of the farm bill should be broadened to keep pace with that change. Unfortunately, farmers are rapidly losing their independence, as one-sided contractual arrangements between farmers and vertical integrators became more common. For example, a potential grower must take out a loan of over $200,000 per poultry house to have houses built to the company's specifications, but the grower is the one that borrows the money to build them. When a grower goes into the debt to this extent, they must often put their farm up as collateral for the loan. Poultry growers sign the first contract thinking that it is good for the length of the loan, until one day a new one is presented that must be signed before the next flock is delivered. This contract can have a mandatory arbitration clause added. Also, the length of the contract can go from years to a flock-to-flock contract, which means no guarantee beyond one week flock. Talk about job security.

As a grower, you get the message very quickly. With your livelihood on the line and the future of your business controlled completely by the company, it is not a surprise that growers are reluctant to speak out about their circumstances. Plain and simple, they fear retaliation. Growers are ranked against each other for their pay. Basically, this means who can grow the heaviest bird on the least amount of feed. This is called your feed conversion. The company controls all the inputs that determine your success in adding weight to the bird, the quality of the chickens and the feed and the length of time you keep your birds before they go to processing. The difference in being at the top of the ranking versus the bottom of the ranking for one flock is thousands of dollars. It puts growers in a position not to want to rock the boat, because the company can directly influence where you fall in this ranking. The grower works for the day that he will have the loan paid off, but the grower will never get to that day because the company wants new or upgraded equipment in the houses or they will cut you off. So the grower has two choices, go back even deeper in debt or just sell your farm and salvage what you can. Growers must upgrade or companies threaten to not bring them any more birds.

Poultry houses are single-use structures and currently there is nothing else that can generate the revenue to equal poultry growing. You are completely at the company's demands. I personally know growers that have been cut off. Others have given in and borrowed the money to do the upgrades and are struggling under the additional debt to the point of bankruptcy. The small additional pay that the companies offer you to convert these houses does not even pay for the interest on the loans.

A question often asked is, if returns are so low, why are people lined up to become contract producers? Well, there are few other job opportunities in the areas where poultry operations are located. Information presented to potential producers by some integrators is deceptive, in that not all costs are shown or they are underestimated. Many potential producers feel that they can be above average and they will never be below that, because they don't understand how little control they have over their ranking. The growers don't want anything that they are not entitled to, but they want things to be fair. I have a few suggestions in that regard.

1) The Packers and Stockyards Act needs to be updated to give USDA Grain Inspection, Packers and Stockyards Agency full authority, like in the red meat sector, to crack down on unfair, deceptive trade practices. Their authority is very limited to poultry and excludes any authority to provide protections for breeder hen and pullet growers.

2) Pass legislation to prohibit certain abusive contract clauses. Arbitration should be voluntary for both parties, not something forced on growers by the company. Companies should be required to bargain in good faith with grower associations instead of dealing with growers individually. This could be done at the national level by changing the Agricultural Fair Practice Act to require good-faith bargaining in contract negotiations.

If large agribusinesses are allowed to control the terms of these take-it-or-leave-it contracts, companies will continue to shift the poultry model into other parts of agriculture, as we have already seen in many other commodities, like hogs, tobacco, identity-preserved grains and peanuts. In January of this year, over 200 organizations wrote to the House Agriculture Committee to support eight legislative initiatives to help restore competition to agriculture markets, to benefit of producers and consumers alike. A copy of that is attached to my written testimony.

It is my hope that the committee will see fit to include a broad competition title in its version of the 2007 Farm Bill. I would like to thank you for your time and willingness to listen to what is going on with today's poultry growers. The contract producer has been transferred into a mere servant of a corporation or, as some have said, contract producers are serfs with a mortgage. Thank you.

Mr. BOSWELL. I appreciate your testimony. Mr. Crabtree, you have five minutes.

STATEMENT OF JOHN CRABTREE, DEVELOPMENT AND OUTREACH OFFICER, CENTER FOR RURAL AFFAIRS

Mr. CRABTREE. Mr. Chairman, Ranking Member Hayes and members of the committee, my name is John Crabtree. I represent the Center for Rural Affairs in Lyons, Nebraska. Beginning in 1996, I led our work on livestock market structure and I just want to thank you for holding this hearing on these really important issues.

As a livestock sector has become increasingly concentrated and integrated, packers and processors increasingly control production at all stages. In many rural places where livestock are raised, there are only a few or even just one packer or processor for a given livestock species. At the same time, there has been a dramatic increase in the use of production marketing contracts to further diminish the bargaining power of farmers and ranchers. Currently over 80 percent of hogs, for example, are either owned outright by packers or tightly controlled through various contracting devices, and many farmers and ranchers face price discrimination and severely limited market access as a result.

The USDA has demonstrated nearly complete inability to enforce the Packers and Stockyards Act and other livestock market competition laws. The audit of the Packers and Stockyards Administration performed by USDA's Office of the Inspector General that was released in February 2006, revealed that the Packers and Stockyards Administration has utterly failed to enforce the law, the very law that gives the agency a reason to exist. Over 1800 so-called investigations were documented between 1999 and 2005, and according to the Inspector General's audit, 1739 of those so-called investigations could not be traced to a specific complaint, producer or packer. That is why Congress should act to define the rules of livestock market competition and provide clear direction for USDA's enforcement. Congress should not let another farm bill go by without making changes in the Packers and Stockyards Act and the Agricultural Fair Practices Act that are necessary to breathe some life and competition back into livestock markets.

Specifically, a couple provisions we would recommend. The Packers and Stockyards Act should be amended to prohibit packer ownership of livestock more than seven days prior to slaughter; to prohibit the use of production contracts that do not fix base prices with adjustments or quality, grade or other factors outside of packer control at the point of sale; and to require the Secretary to write regulations defining the statutory term on reasonable preference or advantage, to ensure that small and midsized farmers and ranchers are not forced to accepted volume-based price discrimination.

Likewise, the Agricultural Fair Practices Act should be amended to make it unlawful for any firm to refuse to deal with a producer for belonging to a producers association or cooperative, prohibit the use of binding mandatory arbitration clauses, and expand prohibition on confidentiality clauses to cover all agricultural marketing and production contracts, not just those in livestock and poultry. And finally, an amendment to the Ag Fair Practices Act that requires a contract to include clear disclosure of producer risks.

Just to highlight a couple of these provisions, major meat packers use packer-owned livestock as a major tool for exerting market power over farmers and ranchers. This practices fosters concentration in industrialized livestock production, and packer-owned livestock artificially lowers farm gate prices to farmers and ranchers while consumer food prices continue to rise, as demonstrated repeatedly by USDA land grant and nonprofit research analysis, most recently the GIPSA livestock and meat marketing or RTI study. And despite their support for vertical integration, the researchers that conducted that report concluded that the use of captive supplies is associated with lower cash market prices.

The packers and processors claim that vertical integration increases production efficiency, but it is simply not true. Small and midsized farms and ranches have demonstrated, time and again, they can match or beat the costs of production of the packers industrial facilities. Prohibiting packer ownership dramatically reduces the ability of packers to manipulate livestock markets and helps secure increased market access for small and midsized family farms and ranches. Access is often severely limited today by the levels of vertical integration, particularly in hog production.

In the end, it comes down to this: in a nation where packers and processors own and control all of the livestock, what need is there of farmers and ranchers? And what hope do we have for revitalizing family farming and ranching in rural communities if we have no hope of revitalizing family farm and ranch livestock production? What hope if we cannot breathe some life and competition back into the livestock markets? My father always told me to say what you mean and mean what you say. If we hope to create a farm bill that can be held up as a solution to some of the challenges that family farmers face, then we should all support a Federal ban on packer ownership of livestock and a comprehensive competition title in this Farm Bill. In other words, we should mean what we say. Thank you.

Mr. BOSWELL. Thank you, Mr. Crabtree. We would like now to give five minutes to Mr. Buis of the National Farmers Union.

STATEMENT OF TOM BUIS, PRESIDENT, NATIONAL FARMERS UNION

Mr. BUIS. Thank you, Chairman Boswell and Ranking Member Hayes and members of the subcommittee. It is great to have the opportunity to be here today. The National Farmers Union represents family farmers, ranchers and family fishermen around the country, with a mission of protecting and enhancing the economic wellbeing and quality of life for rural America.

First, I would recommend, as you move into the new farm bill, to keep the focus on creating a structure to help farmers and ranchers receive a profit from the marketplace. It is the key component that is often missing. Farm bills tend to focus on the symptoms and not on the cause. The two most promising economic opportunities in rural America that I hear about as I travel the country are the production of renewable energy and the second related to the food industry and that is the increasing consumer demand for source-verified, direct-from-the-farm fresh foods. The latter is something that I hope this subcommittee will address as we debate the future structure of our livestock industry.

Yesterday, the National Farmers Union released our updated concentration tables for the top four firms in each sector. This report continues to show an increase of consolidation in most agriculture sectors. The top four beef packers dominate almost 84 percent of the market. The four pork packers control 66 percent of hog processing. The top four poultry companies, roughly 60 percent of the broiler industry. However, ethanol production is the only agriculture sector in which concentration has steadily decreased. Ten years ago, the top four companies owned 73 percent of the ethanol market. Today, the top four companies control 31 1/2 percent of the ethanol produced. Farmer-owned ethanol plants account for the single largest production of ethanol, 39 percent. That has been driven by public policy, Federal policy. So for those who say concentration is inevitable, we might as well get used to it, everyone is going to get bigger, the market is more concentrated, I think the renewable energy experience that we have had in the country is clearly a win for rural America and clearly shows that we can make a difference.

And if we also look at the farmers' share of the food dollar, and I think I distributed both a chart on that and one on the concentration levels of the livestock industry going up and the ethanol industry coming down that you can look at, but if we look at that farmers' share of the food dollar in each of these concentrated sectors, it clearly shows farmers are getting less of the food dollar in the concentrated markets, and more of the total amount spent on food and feed and fiber in the ethanol and renewable energy sector. Competition is clearly the key to profitability for farmers and for rural communities. Those profits are retained in those communities, they are invested in those communities and it creates a tax base and jobs, as well as it is the only communities in rural America where you really see the storefronts, the boards coming off the storefronts instead of going back up. So we need to replicate this policy in the livestock industry.

This study that we have been funding since 1999, unfortunately, will probably be our last, because the data and the information from the companies involved is getting more difficult to obtain. However, this information is important for policymakers to know. It just shouldn't be retained with private groups that do studies, it shouldn't be retained outside of the policymaking arena, and we would urge that this Congress, in the farm bill, direct USDA and the Department of Justice to start obtaining this information so you can make good policy decisions to ensure fair and open markets.

Second, we recommend that the farm bill include a new title to help restore competition. A noncompetitive marketplace is just another way of saying farmers and ranchers are not being paid a fair price. Many cite the free market as a basis for not taking action. Yet I ask, how can you have a free market when there is little or no competition? How can we rely upon a free market without recognizing when it needs fixing? We believe the competition title should include most of the same items that Mr. Crabtree just mentioned, but a couple others. I think we have to immediately implement mandatory country of origin labeling. We are opposed to merging country of origin labeling with Animal ID, because I think Animal

ID, certainly in the countryside, farmers and ranchers aren't there yet. It is very controversial, it is very confusing and it is very expensive. There is a lot of fear. That is going to take quite some time to ever fix.

We also believe that the Mandatory Price Reporting Act should be reformed, and the enforcement and the oversight suggested by the GAO should be implemented. And we feel that you should end the ban on interstate shipment of meat to increase competition in the economic marketing and trade opportunities for rural America. And finally, I think the one other thing in the competition that I would add to what Tom mentioned is to prohibit forward contracting of dairy products, within the Federal Milk Marketing Order system.

In summary, Mr. Chairman, I would again urge you to keep the focus of the new farm bill on profitability for producers. As we have seen with ethanol, competition leads to profitability on the farm and economic opportunities in our rural communities. Thank you, Mr. Chairman.

Mr. BOSWELL. Thank you, Mr. Buis. We would now like to recognize Mr. Stallman from the Farm Bureau.

STATEMENT OF BOB STALLMAN, PRESIDENT, AMERICAN FARM BUREAU FEDERATION

Mr. STALLMAN. Mr. Chairman and Ranking Member Hayes and members of the committee, thank you. We appreciate the opportunity to provide comments on the changing market structure of the livestock industry. Our organization represents over six million member families with many cow/calf operators, hog farmers, sheep and goat producers and poultry growers. I, myself, am a rice and cattle producer from Texas.

Increasing producer competitiveness and access to a transparent marketplace is vital to sustaining domestic production agriculture for farmers and ranchers. The landscape has changed for both crop and livestock producers in recent decades, both in purchasing inputs and in marketing finished livestock, grain and fiber. I won't reiterate the concentration figures that Administration Link provided, because ours are the same numbers from USDA, but it does point out that the degree of concentration that exists, particularly in the livestock sector.

The story is really the same with input providers and I will give you two quick examples. The three largest soybean processors control more that 70 percent of the US market in 2003. The four largest ag chemical companies had 62 percent of the total world market share, based on 2004 data. The Grain Inspection, Packers and Stockyards Administration's recently released Livestock and Meat Marketing Study revealed significant information specific about the use of alternative marketing arrangements in the beef and pork processing sectors. During late 2002 through 2005, the use of AMAs were estimated to cover 38 percent of fed cattle volume, 44 percent of the fed lamb volume, and 89 percent of the finished hog market. Packer ownership accounted for only five percent of fed cattle and lamb volume, but between 20 and 30 percent of fed pork volume.

It is also important to recognize that, while AMAs are voluntary, we question whether they are truly voluntary in every region of the country, for every packer or for every species. Our producers often strongly remind us that one cannot just look at concentration in the aggregate for the entire country. A region-by-region review of AMAs would likely yield some different results.

AFBF supports the following changes to enhance competition of the current livestock marketplace: we support enhancing USDA's oversight of the Packers and Stockyards Act. GIPSA investigations need to include more legal expertise within USDA to enhance anti-competitive analysis on mergers. USDA, in conjunction with the Department of Justice, should closely investigate all mergers, ownership changes, or other trends in the meat packing industry, for actions that limit the availability of a competitive market for livestock producers. We would also support establishing an office of special counsel for competition at USDA. We support amending the Packers and Stockyards Act to grant USDA jurisdiction and enforcement over the marketing of poultry, meat and eggs, as already exists for livestock. This includes breeder hen and pullet operations so they are treated the same as broiler operations. We support efforts to provide contract protections to ensure that the production contract clearly spells out what is required of the producer. In addition, we support prohibiting confidentiality clauses in contracts so that producers are free to share the contract with family members or an outside advisor, like a lawyer or a lender. We support legislation to prohibit mandatory arbitration clauses in contracts. Farmers and ranchers should be able to choose between arbitration, mediation or a civil trial in disputes. We support establishing GIPSA as the lead authority over livestock contracts.

I want to note that we appreciate the work by the House Ag Committee to reauthorize mandatory price reporting last fall. This program has worked well for our producers in providing increased price and market information. There are additional issues that are indirectly related to competition and the changing market structure. Farm Bureau has long supported allowing meat and poultry inspected under State programs, which are equal to Federal inspection and approved by USDA, to move in interstate commerce. All other products, such as milk, dairy products, fruit, vegetables, fish, shellfish and canned projects, which are inspected under State jurisdiction, are allowed to be marketed freely throughout the United States. Movement of these products across State lines will increase marketing opportunities and provide more of a competitive marketplace for our farmers and ranchers.

Farm Bureau supports voluntary country of origin labeling. The cost associated with implementing a mandatory program, especially for meat products, would create a competitive disadvantage for our producers. We also support the establishment and implementation of a voluntary national Animal ID system capable of providing support for animal disease control and eradication. Any program put into place must adequately address the cost, confidentiality and liability concerns of our producers.

Thank you for the opportunity to discuss our views on these issues and I look forward to answering questions.

Mr. BOSWELL. Thank you, Mr. Stallman. We would like to recognize Dr. Taylor from Auburn. Mr. Taylor.

STATEMENT OF ROBERT TAYLOR, ALFA EMINENT SCHOLAR, AUBURN UNIVERSITY

Mr. TAYLOR. Thank you, Mr. Chairman and members of the committee. I am an agricultural economist at Auburn University and today I am going to restrict my remarks to fed cattle marketing alternatives.

I would like to identify four options for marketing: Option one, AMAs, as they have been used and structured in the past 10 or 15 years; Option two, cash on the hoof, the old way of doing business; Option three, require that all transactions be on a cash basis and moreover, that there be a negotiated quality grid; Option four, prohibit AMAs tied to a cash market or to the futures market, but do not prohibit all AMAs.

The RTI study only compared Option one and two. They compared eliminated AMAs to basically cash on the hoof, the old way of doing business. To me, this is an inappropriate comparison and it would be better to look eliminated AMAs, or certain features of AMAs, as they are now done to Option three or Option four. In the RTI study, "beef quality is expected to decline and decrease primary demand with AMA elimination." This assumption totally ignores significant cash transactions that occur now with a quality grid. In fact, precisely the same quality incentives can be achieved in the cash market if the packers so choose. What is the net effect of eliminating AMAs? Assuming they were replaced by cash transactions, with a negotiated base price and a negotiated grid, all I can identify is 40 cents per head. That is .04 percent, not four percent, .04 percent of the value of a fed steer, not the four percent to 16 percent negative effects identified in the RTI study.

Option four, let me emphasize again. Don't prohibit AMAs all together, just prohibit tying a base contract price to either the cash market or to the futures market. Such ties distort buyer incentives in concentrated markets. If we had a very large number of buyers, there wouldn't be a problem with a contract tied to cash or to futures. But with concentrated buyers, there is a problem. Theoretically in economics, this leads to inefficiency. I repeat, aggregate inefficiency, because these types of arrangements worsen the market power effects of size. Economists agree on the need to eliminate contract features that distort buyer incentives, such as the marketing agreements tied to the cash market. Economists made debate endlessly on whether the past effect has been big or small, significant or insignificant, but they are in agreement that such arrangements have the potential to distort markets and therefore should be prohibited. In my opinion, Option four would not destroy the cattle and beef industry, as suggested by the RTI comparison. Combine Option four with pursuit of new innovative ways of trading cattle, I think this option would actually strengthen the industry and also eliminated the more contentious features of AMAs. Thank you.

Mr. BOSWELL. Thank you, Dr. Taylor. I appreciate all of your testimonies. We will move to our questions now and I will start off with directing a question to Ms. Doby. In your testimony, you mention that oftentimes your original contracts are rewritten before they run out and when they do rewrite them, they add a mandatory arbitration clause. Are there currently any protections for the producers for that not to happen?

Ms. DOBY. No, sir, that happened in my contract. I did not have arbitration when I started in the poultry business and it changed. They brought the contract out. I had thousands of dollars left on a loan. So to sign that contract to continue getting birds, the arbitration was in there. The only thing in that contract that says you get a two-week notice for cancellation, but that is the only thing. They have nothing else.

Mr. BOSWELL. I was going to follow up by asking you about how it works with your poultry production, but I think you just told us it doesn't. It puts a lot of stress on your operation.

Ms. DOBY. Yes, sir, it certainly does.

Mr. BOSWELL. Okay. Well, thank you very much. Mr. Buis, attached to your testimony, you attached some charts regarding the concentration of agriculture markets. Can you walk through how those numbers were formulated? And also, can you talk about some of the trends that have been seen in the concentration of the industry?

Mr. BUIS. Yes. Thank you, Mr. Chairman. Since 1999, we have been contracted this study and I think it was the first of its kind done back in 1999 by Dr. William Heffernan and Dr. Mary Hendrickson at the University of Missouri. We do so because oftentimes we would get these anecdotal comments about how big or who is controlling what and really to sort of set the plate for how much competition really exists in the marketplace, and that was a continuation of those numbers.

The second part is that trends clearly are going up in all sectors of agriculture on concentration and I think the complete CR-4 tables that we put in there are charts, I think, pork, beef, broilers and ethanol, but that trend is throughout the industry. As Mr. Stallman mentioned, it is in the grain industry, the soybean processing industry, it is elsewhere, except ethanol. That is the one exception. And two years ago when we did this study, the ethanol number had dropped down to 40 percent and now it is down to 31 percent and it is all a result, I think, of public policy, encouraging producers to get together to own these plants. The local ownership is really key because the profits stay there. They are retained in those communities, reinvest it in those communities, and I think it is just a perfect example that concentration is not inevitable and that competition leads to a fair, profitable price on farming. Ask any corn farmer today what is driving the increase in corn production or corn prices and that has been the increase in domestic demand, new domestic demand for corn and that has been into ethanol. It is owned by local people. I think it is a good thing, Mr. Chairman.

Mr. BOSWELL. Thank you. Maybe a moment later we can talk a little bit about it. I have been very elated about the fact that farmers have been able to participate and cooperate together and start up the ethanol plants, but I know of a case or two already where they are being bought out by, as they refer to it, big money.

Mr. BUIS. Yes.

Mr. BOSWELL. And it is distressing and I don't know what we can do about that, because I would hope that we might respond. I know, in my life, my father and my grandfather, we have always lamented about not being part of the value-added and I would guess that you and Mr. Stallman and all of us, we have been there and here is one place where we can be part of the value-added all the way up, if you will, and I just have a concern that it may get away from the people, our farmers or producers, and I don't want that to happen.

Mr. Stallman, I think you know distinguished Professor Neil Harl. You have heard of him before. But a fundamental concern that he termed "towering concentration on the input side and towering concentration on the output or product side in the agricultural sector, with producers in between, in perfect or nearly perfect competition. The result is vulnerability of producers as buyers, with regional dominance exercised their market power to reduce the price paid to the producers indifferent between selling to the local buyer, with regional dominance for shipping to the next available competitive outlet. Thus, producers become almost captive suppliers or their regionally dominant purchaser of products." What would you say about that? Would you say that assertion is correct? Why or why not? Would you comment on that? You come from a lot background experience, as Mr. Harl did, so what would you say to that?

Mr. STALLMAN. Well, I do have a lot of background and experience, Mr. Chairman, but I do not have a degree in economics. I would observe that, you know, when you look at what is happening, not with just the agriculture industry, but with all industries, you have concentration and consolidation occurring. That, in and of itself, is not necessarily bad. The question is, do you still have competition? And there again, that is where our proposals focus for agriculture specifically, on greater oversight of mergers and acquisitions, particularly within USDA and in conjunction with the Department of Justice. Now, farmers are their own worst enemies. You know, you talk about the middle where the producers are. I have told many farmers who are complaining about the market structure, well, all you have to do is get together and you have all the market power you want. The problem is producers are reluctant to get together and that is an inherent nature, I guess. Maybe it is in the genetic pool for farmers and ranchers, that we want to be independent. We don't want to work with somebody else to accomplish a greater goal. And if we have any challenge or struggle as agriculture producers, it is that we are independent and we don't want to come together into the kind of structures that we could come together in to gain that market power which we do not have, given the concentration that is occurring on the input side and the processing side, currently.

Mr. BOSWELL. Thank you. I violated my own rule here by the time, so I am going to stop now, but Dr. Taylor, I will get back to you in a little bit. At this time, I would like to recognize my colleague, Mr. Hayes.

Mr. HAYES. Thank you, Mr. Chairman. Dr. Taylor, you stated a number of times in your prepared testimony that economists generally agree about one point or another. In other areas, you criticized the work of the RTI report and the investigations and studies conducted by USDA regulators and market experts. Do you believe there is anything like a consensus among economists, livestock interest groups, or market experts, about whether or how Congress should intervene in the livestock market structure?

Mr. TAYLOR. Two ways to answer that question. One is empirical, based on the studies and whether the effect is big or small, significant or not. A second way is theoretical. Economists do generally agree that with concentrated markets, tying AMAs to a cash price distort buyer incentives and should be prohibited. In my written testimony, I have cited several livestock economists who have gone on the record with a similar statement, going back to the mid 1990s.

Mr. HAYES. But in answer to the simpler question, is there a broad consensus either among the economists or the producers? I think I heard you say no.

Mr. TAYLOR. There is a broad consensus among economists that tying AMAs to a cash price has the potential to distort the market and should be prohibited.

Mr. HAYES. Okay. So I think I heard you say this time there is some consensus among economists, but you haven't spoken to the livestock community. Is there consensus there, in your opinion? If you don't want to get into that, that is fine. All right, let me back up to Mr. Stallman. Does the American Farm Bureau Federation support legislative efforts to prohibit packer ownership for beef, pork and lamb?

Mr. STALLMAN. No, sir, we do not. We have had that policy discussion and have come down on the side of not supporting that prohibition.

Mr. HAYES. Okay. One of the alternatives to a complete ban on packer ownership has been discussed, and perhaps compromised, is a requirement that packers purchase 25 percent of their daily slaughter from the cash market. What is the Farm Bureau's position on that?

Mr. STALLMAN. I do not think we have a specific policy position on that. We talked about the benefits of having more the cash, more product purchased in the cash market to help support that market.

Mr. HAYES. Okay. All right. Mr. Buis, as I understand the National Farmers Union position, you support mandatory country of origin labeling and oppose mandatory Animal ID unless the government pays the entire cost. Can you reconcile how imposing the cost of mandatory COOL on livestock is acceptable to your members, but imposing the cost of mandatory Animal ID is not?

Mr. BUIS. Well, we support mandatory country of origin labeling and we feel that the shift in consumer preference, which if you even used USDA's more exaggerated cost, which we they had to revise when they first came out with the rule, it was around $4 billion, to implement COOL. If you had a one percent shift, and their OMB analysis said this, one percent shift in consumer preference towards US products, it would more than offset that $4 billion, so I think the market could absorb it. As far as mandatory animal ID, this was suggested and encouraged by the Secretary of Homeland Security, worried about terrorists distorting our food production or risking our food production, and if you are going to impose that cost on the two percent of society that produces the food to benefit the other 98 percent, I think it is a government cost. I do not think——

Mr. HAYES. Okay. Let me stop you. I have just got 30 seconds left. I don't necessarily agree with you. Ms. Doby, in your testimony, you talk about the poultry companies, that there is a large waiting list of farmers who are interested in adding their grow-out capacity and the question that comes to that, if the current system were not favorable, would the waiting list exist year after year and decade after decade?

Ms. DOBY. Well, I am not sure there is a long waiting list, but I have heard people to say there is a waiting list of people to build poultry houses and that is one of the things that I pointed out. A lot of people don't understand the business when they are getting into it. They may be somebody that is up north and they come down and buy some land and they want to be a farmer. Sometimes they think, okay, all I have got to do is do these chicken houses and they don't understand that I have got to buy a tractor with a front-end loader. I have got to have a spreader truck. I have got to have the land to put the litter on. They don't understand all of these things until they get so far deep in debt that, I have got to get out of this somehow or another.

Mr. HAYES. Thank you, ma'am. Is that the doctors or lawyers that do that? Excuse me. I couldn't resist, Mr. Chairman. I yield back.

Mr. BOSWELL. You are forgiven.

Mr. HAYES. I will be back in just a minute.

Mr. BOSWELL. The chair recognizes the gentleman from Wisconsin, Mr. Kagen.

Mr. KAGEN. Thank you, Mr. Chairman. And since you brought up the reference to doctors, being one myself, I have to say this session has been a bit distressing to hear the reference to the AMA that way, Dr. Taylor. Do you want to get rid of the AMA? That is a different committee. You are in the wrong place. Well, I am not a farmer but I know how to listen and it seems to me that there is a tremendous amount of concentration and vertical integration in the agriculture business, and I guess the question has to do with how can we in Congress, in the 2007 Farm Bill, reduce vertical integration without increasing costs to consumers for the price of food? And I will throw that straightway to Mr. Buis.

Mr. BUIS. Thank you, Congressman. I think you can take a number of positive steps. One is the competition title to address some of these structural barriers to having fair, open, competitive markets. But the other thing, sort of on the positive front, that I think this committee could really serve a huge role in helping rural America is the consumer demand for fresh, source-verified, direct, natural organic products straight from farmers. It has a long way in improving the income of farmers and ranchers, because their then allowed to price their product based on quality, not walk in there on a wounded knew to a concentrated market and say, what will you give me for this commodity? And I think addressing some of those structural barriers to distribution and marketing, that it is not reinventing the wheel, it is kind of going back to the way food used to be distributed before we insisted on everything looking the same, tasting the same, costing the same and lasting for a lifetime on the shelf. But consumers are willing to pay for that freshness and that quality and I think that is a home run waiting to happen.

Mr. KAGEN. Along those same lines, I am very interested in your opinion about a meat packer locally in the State of Wisconsin being allowed to ship his or her product across the State line. Don't you think it is time that if a local producer could put together some salami and bologna that meets Federal standards, is State inspected, shouldn't that small company be allowed to transport something across the State line?

Mr. BUIS. Absolutely. We have supported that for a number of years. I think it increases competition with the big concentrated markets that currently control it. And you know, the products are safe. They are inspected under the same standards. It is just this sort of carved-out market and some are refusing to want to compete with those people and I think it would be a great thing.

Mr. KAGEN. Since your microphone is on, you mentioned that your organization is opposed to forward contracting, but isn't that a way for a local farmer to guarantee a steady stream of revenue, that he has some security, he is going to get paid some money to pay for his cost of living?

Mr. BUIS. We are opposed to adding forward contracting for dairy and part of the reason is some of the experiences in the past and allowing those markets to become further concentrated, and I think rather than just piecemealing in this dairy provision or that dairy provision, we need to take a total holistic look at all of dairy and how we can help this hard-working people receive a profit from the marketplace.

Mr. KAGEN. Thank you very much. Now about mandatory arbitration, a few moments ago, maybe a half-hour ago, the Administrator really failed to give me an adequate answer about the concept of mandatory arbitration. Would anybody at the panel like to comment about those clauses and contracts?

Mr. BUIS. Congressman, I would just say that mandatory arbitration, I am originally from Indiana. That is where I grew up and on basketball, we always wanted the home court advantage, and a mandatory arbitration clause is like giving the company a home court advantage because they write the arbitration clauses and stick them in there. I don't see how that benefits producers at all.

Mr. KAGEN. Thank you very much and I yield back my time. Thank you, Chairman.

Mr. BOSWELL. Thanks, Mr. Kagen. The chair would now recognize the gentleman from Nebraska, Mr. Smith. He stepped out. Let us see who we got in the next order here. It would be Mr. Walberg from Michigan.

Mr. WALBERG. Thank you, Mr. Chairman. Mr. Crabtree, in your testimony, I read a statement here that says the Packers and Stockyards Administration has become anything but an enforcer of competition in livestock markets. Later, you state that USDA has proven, again, that they lack the wherewithal, courage and political will to effectively enforce the Packers and Stockyards Act, and they certainly cannot be trusted to use the considerable authority vested in the Packers and Stockyards. With these two statements, you yet recommend expanding their statutory authority. If you believe this agency cannot perform its mission, then why do you want them to have more responsibility?

Mr. CRABTREE. Thank you for the question. Actually, I would argue that what we recommended is that we help them define their statutory authority. The Packers and Stockyards Act provides the agency a rather expansive authority, which they have not used, and this is not a current thing. I mean, we have seen studies, USDA studies that go back to the red meat study in the early 1990s, the National Commission on Small Farms, two GAO studies, the recent Inspector General's audit, which have all said that the Packers and Stockyards Administration is not fully utilizing their authority. So what we have suggested is to help them define and clarify and to have a little better record in the courts, where they have not done well, and that is certainly not their fault, either. Very specifically, clarifying what is meant, the statutory language, by undue preference is, I think, crucial. Packers use unjustified preferential deals. To really gain a lot of economic power, they give sweetheart deals to very large producers and it gives them a lot of market power over small and midsized family farms and ranches. What we have suggested here is that those preferential pricing structures should be based only on real differences in product value or actual and quantifiable differences in transaction costs and not just based on a volume premium. So I think what my testimony is to you and my suggestion to the committee is that let us help them do their job better by clarifying and defining the statutory authority that they have and help the Administrator move forward in better enforcing the Act.

Mr. WALBERG. Okay. Thank you for clarifying. Mr. Taylor, it is all well and good to assert that Congress could legislate solutions to the problems you cite. Specifically, how would Congress dictate the law in three different ways, one, an index that is superior to cash prices for use in alternative marketing arrangements, or two, the provision of perfect market knowledge for buyers and sellers, and three, a mechanism for managing the duration of the market's open trading window?

Mr. TAYLOR. Well, I am not sure if this should be done through legislation or under Packers and Stockyards Act, through regulatory action. But to me, it would be to simply prohibit tying any AMA to a cash market or to the futures market. On the second point, there are 2 broad sources of market power and one of those is based on size alone. There is no—that 81 percent concentration is too much and 79 is okay. A second broad category of market power deals with deception, asymmetric information and market failure. The asymmetric or one-sided information is the second point and MPR, mandatory price reporting, has, in my opinion, partially leveled up the information that both sides have. But under the 70/30 rule, large transactions are not required to be reported. It is large transactions that move market cash or future and in cattle markets, it is akin to insider trading not being reported, and insider trading must be reported for stock market transactions and the legislation there might be a model to apply to cattle markets.

Mr. WALBERG. Thank you. I see my time has ended.

Mr. BOSWELL. Thank you. The chair would recognize the gentleman from California.

Mr. COSTA. Thank you very much, Mr. Chairman. To Mr. Buis. In your testimony, you spoke of public support for COOL, for the country of origin labeling efforts and this has been something that I think is much discussed about in the agriculture community and obviously there are different schools of thought on this. The opponents have noted that there currently is not restriction on labeling food products and there is therefore no need for the USDA to implement the legislation that was passed, so I would like to get your response on that, please.

Mr. BUIS. Well, if you just look at who has the market controlled and concentrated, and then if you look at what kind of products come into the country and who is bringing them in and the benefits that are derived by bringing these products into the country and putting the USDA inspection sticker and a USDA grade stamp on it so that the consumer assumes it is a US product, it is more like following the money. They are probably not going to do it because they are not going to make the revenues they could off of bringing in less expensive product, and duping the consumer into believing that it is a US product.

Mr. COSTA. The grocers have often argued that it is time consuming and costly. My experience has been that these kind of things, the costs have a way of being passed on. Some of us have visited Europe and other places where labeling is not only required but it is a value-added because consumers want to know. Your reaction?

Mr. BUIS. It doesn't need to be that way. I mean, obviously, in my opinion, the Department of Agriculture wanted to do everything they could to make this as ugly a program and distasteful as possible when they rolled out the rule.

Mr. COSTA. Do you think they succeeded?

Mr. BUIS. And they succeeded. But we can work out the problems with the retailers, and the State of Florida has a good program. The sky didn't fall there. Forty-eight other developed countries have labeling.

Mr. COSTA. Do you think there should be an exception for hamburger?

Mr. BUIS. Pardon me?

Mr. COSTA. Do you think there should be an exception for hamburger? They have talked about blending meats.

Mr. BUIS. There should not be an exception.

Mr. COSTA. There should not be any exception?

Mr. BUIS. No.

Mr. COSTA. Okay. Mr. Stallman, you have heard the response by the gentleman sitting next to you. You take on the mandatory efforts. I think it is a significant part of the marketing issues. I thought I understood, and maybe I was incorrect, you had indicated that it should be voluntary? I would like you to elaborate. I mean, it just seems to me, and we have had experiences in California, that if it is voluntary, you have no program, per se, outside of those who are maybe using it as a marketing tool for higher-end products for niche consumers. And please elaborate.

Mr. STALLMAN. This is one of the most debated issues we have had internally, probably throughout the history of the organization.

Mr. COSTA. I expect you have heard a lot about it within your house of delegates and so forth.

Mr. STALLMAN. But our producers come back to determining our position based on does it provide more income back to the producer. There are three criteria and all three have to be met before that can happen with a mandatory country of origin labeling program. The first criteria is, is that a consumer, for an equal-quality product, has to be willing to pay more just because of the label that is on it. The second criteria that has to be met is that that extra price paid for by the consumer has to be greater than the cost of implementation. Now, we can argue about what those costs are, but there will be some cost. Then the third thing that has to happen, if there is a net return from the difference between what the consumer is willing to pay and the cost of implementation, then that has to get all the way back to the producer. So all three of those criteria have to be met.

Mr. COSTA. Before my time runs out, where do the grocers mix in all of this?

Mr. STALLMAN. Well, they would be in the position of having to work at implementation, but not just the grocers, the whole chain.

Mr. COSTA. Obviously. Clearly. You don't think the costs ultimately get passed on to the consumer?

Mr. STALLMAN. In my experience, the cost will ultimately be pushed down to the producer, one way or the other.

Mr. COSTA. Up and down?

Mr. STALLMAN. Probably down more than up.

Mr. COSTA. I don't think the grocers will absorb those costs.

Mr. STALLMAN. No, I don't think they will, either.

Mr. COSTA. My time has run out. Thank you very much, Mr. Chairman.

Mr. BOSWELL. Thank you. The chair now recognizes Mr. Rogers from Alabama.

Mr. ROGERS. Thank you, Mr. Chairman. I want to start with Mr. Buis. You made a reference a little while ago that an arbitration clause would give one party a home field advantage or a home court advantage. Tell me how.

Mr. BUIS. Often, they are written into the contracts and if the person offering the contract writes the arbitration clause, obviously, they have the advantage. I call it the home court advantage. But if the clause is being written by the person you are signing the contract with——

Mr. ROGERS. By clause you mean the requirement that a dispute has to be resolved by arbitration?

Mr. BUIS. The dispute has to be resolved and what the parameters of that resolution can entail. When you take away the person's right to seek legal recourse, then I think you are putting all your faith in that company.

Mr. ROGERS. Well, as a plaintiff's attorney in my former life, it has been my experience, and my colleagues would probably consider this heresy, but it has been a pretty equitable means of dispute resolution and usually results in lower litigation expenses and more timely dispute resolution, and I have yet to see an arbitration clause that outlined the rules in favor of one party or the other. But in any event, Ms. Doby, I have a got large poultry production in my congressional district. I am from Alabama and it is big in my State and in my district and I am curious. You talked about subtle retaliation methods that the company might impose on growers. Tell me more about that. What do you mean?

Ms. DOBY. Well, if a grower speaks out and in some instances just like with GIPSA, with the hotline, when you call that hotline, it will say, automatically, you don't have to leave your name. Well, if there has not been passed down that there is retaliation somewhere or a threat of it or the thought of it, why do they even suggest you don't have to leave your name? And it is because—and some growers have called me and they have said, I even went to speak to my representative about this to see what he would say and left this paper. And then my service person came out and said, what do you mean? You went and complained to your representative about this and so on and so forth? They are in shock. I went to speak to someone about my problem and then the company says, why do you do this?

Mr. ROGERS. Yes.

Ms. DOBY. And they hold that retaliation. They can hold you out of birds, which, personally, I have had that done to me. The service person made the mistake of telling me. I said, why am I being held out of birds? If you are held out of birds, you are not making any income. It is just like you being sick from your job.

Mr. ROGERS. Yes.

Ms. DOBY. You are not getting any money out of it and you still have your loan payment. The bank is still saying, okay, I don't care if you were out of birds a month. This loan payment is due. Well, that person with the company said, yes, that is probably why you are being held out, because you won't have your houses upgraded or something. And I said, isn't that an unfair trade practice? She said, it might be, but that is the way it is. That is retaliation.

Mr. ROGERS. Okay. Also, you said earlier today, you said that if growers aren't able to continue to make a profit, that this poultry production is going to go elsewhere. Where else did you mean? You said elsewhere in the agricultural sector. I didn't understand what you were talking about. Assuming growers like you ultimately say, enough. I am not signing that contract with that arbitration clause in it, or whatever provision that you don't like. Where would that growing capacity gravitate to, in your view?

Ms. DOBY. Do you mean the companies would go somewhere else?

Mr. ROGERS. What you do. No, no, no. Assuming growers like you just stopped all over the country and just said, we are not doing this anymore, what would happen? Who would start growing?

Ms. DOBY. I don't know, but I don't think that will ever happen because people are so far deep in debt. You got your farm that belonged to your grand dad.

Mr. ROGERS. Well, you made the reference earlier, that if we can't work this out and we can't renew these contracts and be profitable, this production is going to go elsewhere in the agricultural sector, and I didn't know where else you were talking about it would go.

Ms. DOBY. I am not exactly sure.

Mr. ROGERS. But also Mr. Hayes made the point earlier about waiting lists. I do have some of those folks that are on a waiting list, but I will tell you who mostly is on the waiting list, are other growers, people who are already in the sector who are wanting to get more chicken houses authorized and the companies won't let them. Now, if they are so bad, and they have been in the business for years, why do they want more houses?

Ms. DOBY. Well, one thing the company will—they will tell you and most companies, it used to you could build, two houses. Well, they are saying now, we don't offer a contract to anyone unless you build four or more houses, because they are not cash flowing.

Mr. ROGERS. Right.

Ms. DOBY. And that is one reason I think growers, they have, maybe two houses and they build more houses so that the cash flow will be better. If I can put in——

Mr. ROGERS. But my point is I have got growers who may have 4 or 6 houses and they are wanting to get 8 or 10 and the companies won't let them.

Ms. DOBY. Yes.

Mr. ROGERS. So it just seems to me incongruent with what you are talking about, to say that only naive folks who don't know what they are doing get into this business, when I have got established successful farmers who are willing to expand their operations and they are aggravated because the companies won't let them have or authorize them to have additional houses.

Ms. DOBY. Well, not necessarily, but I think if you also talk to those growers, I feel like they would agree with these things that I have brought out.

Mr. ROGERS. Several things you said I have heard from them. I agree.

Ms. DOBY. Yes. They would like to have those. I am not saying——

Mr. ROGERS. But I have never heard anybody talk about organizing the chicken growers in my district. I have never heard about that. I am sorry, Mr. Chairman.

Mr. BOSWELL. Thank you. Well, it is the first round. I guess there is not too many of us left, so we may do another little round here very shortly. But Mr. Taylor, I noticed in your testimony, your footnotes, you made a reference to Peterson.

Mr. TAYLOR. Yes, sir.

Mr. BOSWELL. Does that reference the late Bob Peterson of IBP?

Mr. TAYLOR. Yes.

Mr. BOSWELL. Can you explain the quotation in more detail?

Mr. TAYLOR. There are transcripts available of three talks he gave to Kansas cattlemen, one in 1988, before IBP got involved in captive supply, and then two in 1994, after IBP did some AMA arrangements. And he basically outlined how AMAs gave the buyer leverage in the marketplace and went on to say, do you think this will have an impact on the cash price? And he said you bet.

Mr. BOSWELL. It kind of follows the money.

Mr. TAYLOR. Yes.

Mr. BOSWELL. Okay. I was curious about what you meant by that, so thank you for elaborating on that. I guess you were making a point that is clear. I think you said in the RTI report, you said it contains fundamental flaws because the study ignores about 20 percent of cash transactions, ignores about 20 percent cash transaction that occur with a negotiated grid. So first, do you agree with this statement, and if so, can you elaborate on what it means and how it would affect the RTI's data?

Mr. TAYLOR. MPR has several categories for reporting cash transactions. One of those is on a negotiated grid, and in the last year or so, that has fluctuated some but been on the order of 10 to 20 percent. In looking through the RTI study, I did not see where they had recognized those cash transactions with a negotiated grid; that they lumped all cash together.

Mr. BOSWELL. Thank you. Mr. Walberg, do you have any other questions?

Mr. WALBERG. I do, Mr. Chairman. A couple more if I could. I am aware of arguments that packers have disproportionate market power and therefore they are able to manipulate prices, though I am not aware of any study or investigations that have ever shown that to occur. Perhaps maybe some of our witnesses could provide the subcommittee with that information. But Mr. Stallman, I guess my question is, what prevents producers from banding together in cooperative arrangements and agreements to exert market power over packers?

Mr. STALLMAN. Nothing. It is a matter of will and desire. You know, the laws regarding cooperative structures were put in place to help assist the producers to do that and there have been examples of producers successfully getting together in cooperative structures and they have more market power. But there are stories that were not quite so successful and there is a reluctance of producers to do what it takes to put their producing power together to get more market power, but there is nothing to prevent them from doing it.

Mr. WALBERG. It is their choice and it is a struggle. They can join it or let it go.

Mr. STALLMAN. That is correct.

Mr. WALBERG. Okay, thank you. Mr. Taylor, you stated that there has been a lack of innovative effort by the USDA to identify new ways of doing business that are economically efficient.

Mr. TAYLOR. Yes.

Mr. WALBERG. Fair to both sides of the transaction and do not distort buyer or seller incentives and would result in beef with the quality attributes that the consumers desire. Let me ask you, are you suggesting that the government is responsible for how livestock in this country should be bought and sold?

Mr. TAYLOR. No.

Mr. WALBERG. That is what it sounds like.

Mr. TAYLOR. The point I want to make is, over the years, there has been a bipolar debate, AMAs versus the cash market.

Mr. WALBERG. Don't get back into medicine with me or anything.

Mr. TAYLOR. Okay.

Mr. WALBERG. The doctor has left.

Mr. TAYLOR. And what I am suggesting is that we need to think of innovative ways of handling these transactions that do not have objectionable features like being tied to a cash market. And there are some electronic possibilities, I think, that have not been investigated, but if we get into full electronic marketing, there could be antitrust issues. So I am just suggesting that all of us need to give more thought to innovation rather than sticking with this bipolar debate.

Mr. WALBERG. Well, I am not sure it is a bipolar debate. Philosophically, there is some significance to those that would say that the government is expanding their power and taking control, what it sounds like, I don't know if there is a mechanism without expanding it if you are going to walk away from the market. So well, we will agree to disagree at this point, but thank you.

Mr. BOSWELL. I see no further questions. I want to thank the panel for your spending the time with us today. We appreciate it very much and we will look forward to talking to you in the future. Thank you very much. We will take a short moment here and let the third panel take their position. Well, I thank the panel for arriving. I see that Ms. Philippi, that you are back and it is good to see you again, my neighbor to the west. And we appreciate the time of day it is, so we will get right to business and thank you for your patience, being willing to come and share with us. As you see, these are discussion points on a lot of people's minds, so I think it is good that we talk about it. So that is what we are trying to do and listen carefully and that is what this is, a listening session for us. So I would like to welcome the third panel, all of you, and we will get right down to business and we will start of with Ms. Philippi. Help me pronounce. I want you to pronounce your name, Joy.

Ms. PHILIPPI. Philippi.

Mr. BOSWELL. Philippi. I got it. Philippi. Okay. So we will start off with you for five minutes and we are happy to have you here.

STATEMENT OF JOY PHILIPPI, PORK PRODUCER, ON BEHALF OF NATIONAL PORK PRODUCERS COUNCIL

Ms. PHILIPPI. Okay, thank you. Chairman Boswell and Ranking Member Hayes and members of the subcommittee, I am Joy Philippi, a pork producer and row crop farmer from Bruning, Nebraska, and I am the immediate Past President of the National Pork Producers Council. NPPC is an association of 43 State pork producer organizations and represents the interests of America's 67,000 pork producers.

The US pork industry has enjoyed unparalleled prosperity over the past three years. Average farrow-to-finish producers completed their 35th consecutive profitable month in December and made an average profit of $22.17 over that time period. New data indicates that the industry will remain profitable through March of this year, despite of near record feed costs. It is against this backdrop of financial success that we offer our views on market structure.

First, we would ask, is legislation that would limit producers market access options a solution in search of a problem? There is no doubt that the structures of the US pork industry and the pork and hog markets have changed over the past 10 years. We urge Congress to focus, not on structural issues, but on the more important market efficiency measures of conduct and performance as you deliberate the wisdom of government intervention. Congress has invested significant taxpayer resources in researching the current livestock markets. Much of that research, including the $4.5 million GIPSA Livestock and Meat Marketing Study, is relatively new. We have had little time to consider what it tells us, so we urge Congress to move slowly, as USDA and the industry digest and consider those findings.

We also would like to know the status of GIPSA's report to the 2005 audit conducted by USDA's Office of Inspector General. We believe GIPSA Administrator James Link has made substantial changes in the way GIPSA performs its duties. However, we do believe Congress should know specifically what has been done and how that is going to change GIPSA's future efforts to enforce the Packers and Stockyards Act. The Federal government sought to approve livestock price reporting and enhanced the transparency of the markets by implementing the Livestock Mandatory Reporting Act. We believe that system has made markets more transparent and that refinements enacted in 2006, including new swine reporting enhancements, will further that cause. Let us work to make the system better before we proceed with other actions.

The focus of most debates regarding the competition has been in the number and market shares of various participants. The key is whether sufficient competitive pressure exists to make packers and producers behave in a way that approaches competitive norms and yields competitive prices and quantities. This can only be measured by looking at actual transactions to determine how firms act and what the results of those actions are. The new GIPSA study did just that. Instead of looking at changes in ownership and market shares, it examined transactions and looked at conduct and performance. We now need to step back and consider the methods and results of that research, perhaps even ask and answer, there is no question on the results.

Now there are always unintended consequences to virtually all public policies and part of the art of public policymaking is balancing the costs and the benefits of any proposal. In the areas for competition and industry structure, there are a number of pending proposals that will have an adverse effect on the pork producers and will give little benefit to anyone. As an example, consider the idea of requiring packers to buy at least 25 percent of their hogs on the spot market or through negotiated sales. The new GIPSA study found that such requirements would make producers and consumers worse off and would not leave packers better off. Additionally, the practical implications of such a requirement are challenging, to say the very least. Would the 25 percent be measured daily, weekly? Would producers be required to sell 25 percent of their hogs through negotiated trades to provide the 25 percent that packers are required to buy through negotiated trades? If not and since only 11 percent of all hogs are sold through negotiated trades now, which producers would have their contracts terminated to force their hogs into the negotiated trades? And what happens when those contracts are terminated? Would the financing that was contingent on those contracts be withdrawn by risk-adverse lenders?

Pork producers face many challenges today and those include the rising corn prices driven by ethanol production, impending mandatory country of origin labeling costs, the specter of animal rights-driven legislation dictating on-farm production practices, and increasingly stringent and costly environmental regulations that are almost universally better handled by large operations. I urge you not to add to these challenges by limiting the options we have available to market our hogs. Punitive actions against packers do not necessarily benefit pork producers in the long run, unless the packers are clearly in the wrong and we have not seen any evidence of this, and Congress must proceed with caution, weighing the costs and benefits of such important public policy.

We thank you for the opportunity to be here today to represent the Nation's pork producers, and I will be glad to answer questions at the appropriate time.

Mr. BOSWELL. Thank you. Mr. Roenigk.

STATEMENT OF WILLIAM P. ROENIGK, SENIOR VICE PRESIDENT, NATIONAL CHICKEN COUNCIL

Mr. ROENIGK. Thank you and good afternoon, Chairman Boswell. We appreciate the opportunity to participate in this important hearing regarding the issue of market structure for the livestock and poultry industry. On behalf of the National Chicken Council, I appreciate your invitation to provide comments on the market structure of the US chicken industry. My name is Bill Roenigk and I am Senior Vice President of the National Chicken Council. Companies that produce and process more than 95 percent of the young meat chicken broilers in the United States are members of the National Chicken Council. I am pleased to have the opportunity to share with you information about the market structure of the US chicken industry.

More than a half a century ago, as farmers moved more and more away from dual-purpose chickens, those were chickens that produced both eggs and meat, and move more and more towards specialized breeds, those that laid eggs and those that were better at producing meat, a new industry and a new market structure began to emerge in poultry farming. These farmers sought greater stability and predictability in their incomes and return on their investments. With access to only limited capital, it was very important to lessen market risk by sharing those risks with others in the production process.

Although the vertical integration happened several different ways, the primary way it happened was with feed mills who provided the feed to the farmers growing the broilers, and they learned the best way to get paid for the feed they had in those chickens was to work with the grower and a processing plant to make sure that when the birds reached market weight, that they had a place to be processed. Because a chicken grows so quickly, the economics of feeding broilers requires prompt movement to market when they reach market weight, and a broiler grower is at a very distinct disadvantage if the processing plant is at capacity or the wholesale market for dressed chicken is depressed. By coordinating growing and processing and marketing, the surge in gaps in live production could be minimized. The chicken industry, as it began to use vertical integration to coordinate production, processing and marketing 50 years ago, was participating in a concept called just in time. At the time, we didn't know it was called just in time. The Japanese carmakers later labeled that and took credit for it. We invented it or at least we think we did, but we forgot to label it, so we don't get credit for it.

Contracts with growers offer many important benefits. These benefits and advantages include substantially reduced market risk, quicker and a more thorough understanding of production requirements, better access to capital, more reliable and predictable income flows to labor, management and investment, and better opportunity to leverage success to expand or diversify farm operations.

Family farms who contract with chicken companies have benefited in good measure over the past six decades. More than 25,000 family farms currently contract with companies to raise broilers and can do so more confidently because, to a very large degree, they are insulated from the risks of the chicken marketplace. Contract growers are basically guaranteed a fixed payment with a bonus for above-average performance. University studies have found that returns to growers and companies are very comparable.

As was mentioned earlier, companies, not every company, but most companies, have a list of farmers who would like to begin to grow chickens. They also have a list of growers who are currently growing chickens and would like to add additional housing capacity to their operations. And as was asked before, if this is not a good system, why has it existed for more than 50 years and why do we have these waiting lists? Vertical integration has stood the test of time very well.

As I noted in my statement, the consumption has gone up to where chicken is the most consumed meat in the United States, and the cost to consumers has come down dramatically. It takes only four minutes for the average worker to be able to earn enough wages to buy a pound of chicken. Consumption of chicken has doubled from more than 30 years ago. And until the ethanol issue came, I would predict that we were going to continue to increase that consumption, but that remains to be seen.

Chairman Boswell, the National Chicken Council appreciates the opportunity to share the broiler industry's story with you. As you begin to deliberate the various issues involving the upcoming farm bill, I respectfully suggest that trying to improve the market structure for the chicken industry should not be a high priority for the subcommittee nor for Congress. The National Chicken Council does not see the need for new or additional laws nor USDA regulations that would involve government further in the grower/company business relationship. Nonetheless, if you have concerns or questions about the chicken industry, with respect to this issue, the National Chicken Council would very much appreciate the opportunity to work with you to appropriately and adequately address those issues or concerns. Thank you.

Mr. BOSWELL. Fair enough. Mr. Queen, please.

STATEMENT OF JOHN QUEEN, PRESIDENT, NATIONAL CATTLEMEN'S BEEF ASSOCIATION

Mr. QUEEN. Mr. Chairman, my name is John Queen and I am a fourth-generation cattle producer and livestock market operator from Waynesville, North Carolina. I am President of the National Cattlemen's Beef Association and I am pleased to be with you to discuss our policy on market structure issues, policy which was brought forward by, debated by and voted on by our rancher members. This is grassroots policy where one member/one vote has always been the standard.

When it comes to market structure and competition issues, NCBA's position is simple: we ask that the government not tell us how we can or cannot market our cattle. The way we market our cattle has changed significantly over the years and it has come from the recognition within our industry that we are not just cattle producers, but beef producers and must be responsive to the consumers' demands. This consumer focus has led to many innovative marketing programs that have improved the quality of beef, given the consumer, what they are asking for, and allowed ranchers to get paid for the value that they add to their animal.

In addition to being responsive to our consumers, participation in these marketing arrangements provides a rancher with several tools that help improve their operations and herd management. The ability to manage price risk is one of the most valuable of these tools. Taking advantage of marketing arrangements, such as forward contracting, allows producers to make a price that allows them to be profitable. If the price doesn't fit their needs, they can walk away and find another buyer. Being a price maker rather than a price taker, puts ranchers in control of their business. Many ranchers who participate in these programs get information back from the feedlots, telling them how their cattle performed. Information also comes back from the packer, in the form of yield and quality grades. This information is critical in managing our herds and focusing on the trades which produce the highest quality animals.

The benefits of AMAs were recently supported by the results of the GIPSA Livestock and Meat Marketing Study conducted by RTI. This 3 1/2 year study was funded by 4 1/2 million taxpayer dollars and was billed as the definitive answer on these issues. The study supports what many ranchers across our country have known all along: a market-driven system works. The overwhelming conclusion of this study is that, overall, alternative marketing arrangements help all sectors of the industry, not just those that participate.

The report states that the leading reasons ranchers participate in AMAs are the ability to buy and sell higher quality cattle, improve supply chain management and obtain better prices. When talking about improved supply management, we have to once again go back to the consumer. The consumer does not come into their local Safeway looking for ranchers reserve beef only on Tuesdays. The consumer demands the convenience of picking up a package of ranchers reserve beef any day of the week. To meet that demand, the retailer and packer need a steady and constant supply of cattle that meet the qualifications of the store-branded program. If the packer is limited in its ability to source those cattle, the branded programs go away. The consumer chooses other products and cow/calf producers get less money.

So far, I have only talked about AMAs, but approximately 62 percent of cattle marketing is done through the cash or spot market. Spot markets such as auction barns are critically important to the US cattle industry. Ranchers who market this way cite several reasons for their choice. One reason is independence. Flexibility is also important to these producers. Selling on a spot market give ranchers the opportunity to participate in market rallies. We must remember, however, that this only gives them the opportunity to catch the rally. Timing the market is always a difficult task and adds to your price risk.

Even with traditional means of marketing, we have seen innovations that have been market driven. One of these innovations is video livestock auctions. With this method, ranchers can auction their animals by video and reach customers all across the country. The results of these innovations are telling. Demand for beef has grown over 20 percent since 1998. Consumers spent a record $71 billion on beef in 2006 and consumer confidence in our product is at 91 percent, greater than it was before the 2003 BSE case in Washington State.

The study concludes that restrictions on AMAs would cause a decrease in the supply of cattle, quality of beef and feeder cattle prices. These results would set our industry back and place the burden on the individual cow/calf producer. In a time where we continue to see an increase in feed costs due to competition with ethanol for corn, as well as an increase in fuel costs, the last thing we need to do is to add more burdens to our ranchers. Keep in mind that, for every agreement made by a packer, there is an individual rancher on the other side of that transaction who had decided that that agreement is in their best interest and they should be allowed to conduct that business privately, just like any other industry. Restrictions or bans on AMAs will eliminate or significantly reduce these programs and hamper the progress we made in keeping ranching a viable industry. In the end, we must have a government that works to help our industry, not one that limits or removes choices for cattlemen in the marketing of their cattle. Thank you.

Mr. BOSWELL. Thank you very much. Mr. Boyle.

STATEMENT OF J. PATRICK BOYLE, PRESIDENT & CEO, AMERICAN MEAT INSTITUTE

Mr. BOYLE. Good afternoon, Chairman Boswell, Ranking Member Hayes and Congressman Kagen. Thank you very much for the opportunity to represent the American Meat Institute here today. AMI represents 250 of the Nation's meat and poultry food manufacturers. Collectively, they produce 90 percent of the beef, pork, lamb, veal, and 75 percent of the turkey processed in the United States. These companies operate, compete, sometimes struggle but mostly thrive in one of the toughest, most competitive and certainly amongst the most scrutinized sectors of our economy.

Members AMI have concerns about legislative efforts to apply State-directed controls on an industry that competes intensely with each other and for a greater share of the consumers' food dollar from other segments of agriculture which would be free from such controls. Specifically, these concerns relate to proposals that would, first, prohibit the ownership of livestock by a packer and unduly regulate investment; second, prohibit or restrict contracting and livestock marketing arrangements upon which producers and packers freely agree and routinely utilize; and three, mandate an arbitrary cash or spot market purchase requirement. If enacted, these proposals would involuntarily expose producers and packers to the volatility of the cash markets, expose packers to the inconsistencies of raw materials, and subject consumers to fewer product choices at higher prices.

We believe the strength of the livestock marketing system in the United States is in the flexibility it provides to producers, packers, processors and retailers, in responding to market signals. Meat and poultry consumers continue to benefit from a wide array of value-added products at very reasonable prices. The amount of discretionary income that American consumers spend on food has fallen to a historic low of just four percent, of which meat and poultry products account for less than two percent of our disposal income each year. We believe that most appropriate government role in today's livestock marketing system is to enforce the numerous existing laws and regulations that ensure a fair and nondiscriminatory business practices amongst producers and packers, while allowing producers the freedom of choice on how best to market their livestock.

Two recently released studies agree with AMI's assessment of the competitive and rational nature of the livestock and meat markets, as well as the resulting benefits to American consumers. The first panel earlier today reported on the investigation and enforcement activities of GIPSA's and RTI's Livestock and Meat Marketing Study. I would like to emphasize two findings. First, the report found that contractual marketing arrangements between livestock producers and meat packers have numerous mutual benefits. They increase the economic efficiency of the cattle, hog and lamb markets, and these economic benefits are distributed forward to consumers, as well as shared between producers and packers. And secondly, the study concluded that restrictions on the use of these contractual arrangements, such as the legislative proposals that I have previously discussed and which AMI opposes, would have negative economic effects on livestock producers, meat packers and American consumers.

A second multi-year congressional-mandated report from the bipartisan Antitrust Modernization Commission was submitted to the Justice Department earlier this month. It concludes that "the government should not displace free-market competition, absent extensive, careful analysis and strong evidence that a market failure requires the regulation of prices, costs and the entry in place of competition." Clearly, the extensive, careful analysis of the 4-year, $4 1/2 million RTI study documents that we have nothing approaching market failure in the livestock sector of our agriculture economy. The RTI study is only the most recent in a long line of similar studies over nearly the past 20 years that have reached the same conclusions about the legality and vibrancy of our Nation's livestock marketing system. Many of these studies were either mandated by Congress or initiated by Federal regulatory agencies with oversight responsibility for the livestock and meat packing sectors. Others were funded by universities, and by private entities, to assess the health and competitiveness of this industry. And they have, every one them, all 34, without exception, reached the same conclusions as the most recent RTI study; that the livestock and meat packing market is competitive and that current oversight and enforcement are effective.

Congressman Hayes, you asked the last panel whether anything approaching an economic consensus exists on that conclusion. I would suggest that these 34 studies, representing nearly two decades of regulatory oversight and academic analysis, comes pretty darn close to representing that consensus about the health and vibrancy of this sector. I thank you for the time today. I ask that these be submitted for the record, and I look forward to your comments and observations and questions.

Mr. BOSWELL. The additional materials will be incorporated in the record, and thank you for that and we will start our question time now and I will just start off with Ms. Philippi. In the testimony today, you heard that somewhere between 60 and 80 percent of the hogs are either owned outright by packers or are tightly controlled by various contracts. At what point does packer control become an issue?

Ms. PHILIPPI. Well, to this point, we haven't seen that has been proven yet, what that level is going to be and we do believe that we need to continually look at that. And if you would like to have even more in-depth numbers, we could be able to probably look for those.

Mr. BOSWELL. I will appreciate that, but is there some point where you become alarmed?

Ms. PHILIPPI. We haven't been at this point.

Mr. BOSWELL. So where would it cause the yellow flag to go up in your mind?

Ms. PHILIPPI. Well, in my mind, I don't have any problems with the packers owning hogs.

Mr. BOSWELL. Okay. So if they have 90 percent of the hogs, there is no problem with you?

Ms. PHILIPPI. It is not with me personally, but we will get you information, if we can get that to you.

Mr. BOSWELL. All right. Thank you very much. Just to move along here, Mr. Roenigk, in Ms. Doby's testimony today, we heard of multi-year contracts being redrawn before the contract runs out and the terms are changed. We also heard about mandatory arbitration clauses being added to the contracts. You state in your written testimony that a measure of successful relationship between companies and contract growers is that the majority of the companies have a waiting list for growers who are requesting to add to existing grow-out housing, and I think you make the connection that, since this is the case, it must be a good relationship. Could it not also be the case that the industry is so integrated that this is the only option available for the poultry producers?

Mr. ROGERS. Permit me to——

Mr. BOSWELL. I will give you a minute.

Mr. ROGERS. To phrase the question, the question is, is there a better way to operate contracts with growers?

Mr. BOSWELL. Well, is there any other option for the producer?

Mr. ROENIGK. Given the current market forces, both in terms of inputs and in the consumer demand, I don't know of one, Mr. Chairman.

Mr. BOSWELL. That is my point there. Okay. Well, that is a concern that I hear people talking to me once in a while. Mr. Queen, if I could, what would be the result of prohibiting packer ownership for livestock for more than a couple weeks?

Mr. QUEEN. I am sorry, I didn't hear you.

Mr. BOSWELL. What would be the result of prohibiting packer ownership for livestock for more than 7 to 14 days before slaughter?

Mr. QUEEN. Because I think a lot of the value-added markets that we have, have to go through a chain of events and that packer is one of those links in that chain, going from the producer to the feeder to the packer to the retailer to the consumer, and if we don't let him fulfill that continuously, then we are going to lose that added value that we have in our commodities.

Mr. BOSWELL. Continuing that, could it be said that if a producer wanted to take advantage of high future prices, they could sell a CME contract? And could it also be said that if a processor wanted to take advantage of low prices and a short supply, could he not buy on the CME? Isn't that why live animal contract trading was started in the 1970s?

Mr. QUEEN. Yes, sir.

Mr. BOSWELL. So what are your comments? Why did you say yes?

Mr. QUEEN. Well, certainly the producer has that opportunity to sell that contract to protect himself in that risk, if he has monetary means of doing so. The producers in America today are so small, the average herd size is just 38, so very few producers in America have the ability to hedge those contracts the way the market was set up.

Mr. BOSWELL. In your testimony, you emphasize that the National Cattlemen's Association wishes the government to stay out of cattle marketing issues. A little later in your comments, you say how much you rely on Federal regulations to keep the playing field level for producers. Would everyone be better off if there were no AMAs or packer ownership and let contracts on the Chicago Mercantile Exchange manage the risk?

Mr. QUEEN. No, sir, I don't think so. I think we are trying to take away the American way, what our country was founded on, and that being the ability of every producer in this country to choose his own business model, that being the ability to sell his commodity to whom he wants to sell it to, when he wants to sell and for what price he wants to sell and to be delivered what day he wants to do that. That is the American way. That is what our country was founded on and I think we are trying to take that away from the livestock producers in America.

Mr. BOSWELL. Okay, I am going to stop now and come back to you in a little bit, Mr. Boyle. I would like to recognize Mr. Hayes.

Mr. HAYES. Thank you, Mr. Chairman. Mr. Roenigk, one of the legislative proposals we heard discussed today is the prohibition of mandatory arbitration clauses in poultry production contracts. Could you take a a minute to outline the use of these clauses and why your industry opposes the proposal to eliminate them?

Mr. ROENIGK. Well, mandatory arbitration is in many clauses. I don't think it is in all the clauses. But differences arise in any business relationship, contractual relationship. You need an efficient and timely way to resolve their differences. Mandatory arbitration does that. If someone can propose a better mechanism, I think we would be willing to consider it, but we are not aware of one. And the arbitration system, as I understand it, does not give someone a home field advantage or a home court advantage. You choose arbitrators who are fair and just to hear both sides and make a decision. To me, that sounds somewhat fair.

Mr. HAYES. Okay. Joy, the poultry contract grower on the previous panel made three specific legislative recommendations: prohibit mandatory arbitration, expand coverage under Packers and Stockyards Act over production contracts, and authorize collective bargaining power for contract growers. What is your thinking on each of these three?

Mr. ROENIGK. As my statement——

Mr. HAYES. Joy Philippi.

Mr. ROENIGK. I am sorry.

Mr. HAYES. I was asking Joy.

Ms. PHILIPPI. Those are three areas that we discussed. We also believe that the regulation of a contract like that doesn't need to be mandated. We believe that there are some agreements that can be made that producers can enter into. They can review them to know if they are good for their business model. I am a contract producer, so I was walking that right through my head as well, and we just don't believe that there is any need to have any further regulation on those things.

Mr. HAYES. Mr. Roenigk, do you want to comment on that?

Mr. ROENIGK. As my statement indicated, we believe, for further government intervention, whether it is congressional or USDA, it probably is not needed at this time. We think the system works well. Companies have grower relations committees where they meet periodically with growers. The State poultry associations include both growers and companies in there. There are a lot of opportunities to work out the differences and I think we should try and make that system work better before we have more government intervention.

Mr. HAYES. Okay, I am going to come back with another question. Mr. Boyle, talk about GIPSA's enforcement activities. Are they doing enough, not enough? Are we balanced here?

Mr. BOYLE. Well, my impression from the Administrator's update on steps that he has taken since he arrived to run that agency, suggests that it is a revamped, reorganized agency with a lot of investigations underway in the last few years. At AMI, we have been always supportive of a strong and effective GIPSA, as well as strong enforcement of our antitrust laws. I will point out for the record that, unlike all other segments of American business who have the pleasure of interacting on occasion with the antitrust division of the Department of Justice and the Federal Trade Commission, in the meat packing sector, we also have the opportunity to interact with the Packers and Stockyards, a unique agency with oversight of competitive practices and fair trading practices in the meat packing sector. So it is an additional layer of antitrust enforcement and review. We have always been supportive of it. We interact with them when necessary and I believe that the Administrator gave a fairly positive update of changes he has implemented since he arrived.

Mr. HAYES. Back to Mr. Roenigk for a minute. Interestingly, I was at the opening of a new poultry plant last week and this is based on rejuvenating older, smaller poultry houses, contracting with those folks for a different way of raising, air-chilled rather than—so there are a lot of organic, free range. A lot of different alternative markets are springing up. So I think, even though the integrators have a big impact on the market, there are a lot of alternatives that are being used out there. Mr. Chairman, time is running out here. With Mr. Queen, we will ask about animal ID on the next round.

Mr. BOSWELL. Thank you, Mr. Hayes. The chair recognizes my colleague from Iowa, Mr. King.

Mr. KING. Thank you, Mr. Chairman, and I want to thank the witnesses that are here. I am listening to this testimony and reading through it at the same time and I looked back on Joy Philippi. In your testimony, you mention a number of challenges facing the livestock industry, high feed prices, mandatory COOL, animal rights initiatives, and keep this list for me, because I am going to ask you a prioritized question. So high feed prices and mandatory COOL, environmental regulation. What else do I have? Let us see, packer ownership, lack of a livestock ID program. And out of those—no, I will go down through the list again. I have got them in order. High feed prices, mandatory COOL, animal rights initiatives, environmental regulation, packer ownership, and then I added the livestock ID, lacking a livestock ID program. Out of those, what would you say would be the greatest risk to the livestock industry? And if you would like to prioritize them, if you can do that on the spot, that would be wonderful.

Ms. PHILIPPI. That is pretty hard to do without reflecting my personal opinion as well. But we have treated the issues of the corn availability and corn price, the issue of mandatory country of origin labeling. All of those first that we identified, we were trying to address in an equal fashion, because we believe they are all going to have a cost effect, costs that our producers are going to have to somehow recover in the marketplace. But when we get to the issue of the way that—asking us to change our production practices, those costs are still very much unknown. So you know, we look at those things equally and that is why we hope that we don't have to have regulation on the way we do our business today.

Mr. KING. If I could then, you want us to fix them all at once.

Ms. PHILIPPI. That would be wonderful. And we will help you.

Mr. KING. And I appreciate that. Given the track record of Congress, though, we may want to be focusing on some priorities. I am going to ask Mr. Roenigk. Would you like to take a stab at that, please?

Mr. ROENIGK. Yes, thank you very much. And if I could just maybe add a couple, I think the Number one priority, and I don't know if they would change market structure, I think it would create greater concentration, and that is that we have to have a super-abundant corn crop, not just this year and not just next year, but until we get this breakthrough in yields, because the only way you get more corn right now is more acres. I am agreeing with the corn geneticists, some day we will get that breakthrough, but we have got to have more acres, we have got to have more corn and we have got to satisfy that. If we have a hiccup in our corn crop, I am sure there will be more than one hearing of this subcommittee about the impact of that. So that is Number one, not just this year, but I think for the next few years. I will try to stay in my one minute. But if you look at my graph on Page four, from 1970 to 1975, broiler production was flat. I hope I am wrong, but that is what I see for the next five years, flat, and I hope it is not down. We talk about contract growers and their opportunities. The way to get more opportunities is to keep that trend up and not flat. So I hope I am wrong, but that is my concern.

Number two, the likelihood of avian influenza, commercially a high pathogenic, avian influenza breaking out in the commercial flocks in this country is very, very small. USDA and the other agencies have done a beautiful job of putting up the biosecurity firewall, safeguards and so on and we have to keep that up. But if it was to happen, I suggest that, not just the companies, but the growers would not be thinking about whether mandatory arbitration was the most important thing in their life. They would be saying, how can I save my livelihood and my farm? If the system shuts down, we can't. The consumer confidence is a problem both in this country and other countries. We have already seen it. A truck drives through West Virginia with its doors shut. It can't ship to Japan because it went through West Virginia and because they had an outbreak. The turkeys were in the ground before the headlines were in the newspaper, but Japan cuts West Virginia off.

The third thing I would say is that there is an increasing likelihood of poultry inputs coming into this country from countries who can undercut our prices, and these are from countries who have— at least one country has been in the news recently, not about human food, but some other type of food.

Mr. KING. Thank you. If you don't mind, please, I would like to move over to Mr. Queen. I am running out of time. But your priorities on the greatest risks to the livestock industry? Yes, I read through most of them. High feed prices, mandatory COOL, animal rights activist initiatives, environmental regulation, packer ownership, lack of a livestock ID program. What puts the livestock industry at the greatest risk, Mr. Queen?

Mr. QUEEN. Well, I think that the greatest risk, as we have talked here, is doing away with their ability to market their cattle as they see fit, taking away that right from the citizen of America, the rancher.

Mr. KING. Thank you. And I am running out of time, so I will have to pass on Mr. Boyle and I will yield back the balance of my time then Mr. Chairman.

Mr. BOSWELL. We have been joined by Mr. Baca. The chair recognizes Mr. Baca from California.

Mr. BACA. Thank you very much, Mr. Chairman, and thank you very much for having this hearing. Let me ask this question to Mr. William R. Just like with the pork producers, you have seen some prosperous times recently. You say that the conditions currently placed are the ones that the market itself has indicated and decided work best. Is anyone being left out?

Mr. ROENIGK. I am not sure I understand that question. Are you asking, as vertical integration of the industry moves forward, have any parts of the farmers been left out?

Mr. BACA. Left out.

Mr. ROENIGK. I don't think so and in fact, as was mentioned by Congressman Hayes, we have a very dynamic industry and business and we are seeing the smaller producers produce the organic, free-range, exotic breeds, being able to go to live bird markets. So yes, there are large companies, but there is also this growing specialty market and in that sense, I don't think they are left out. In fact, I think, in today's market, they have much greater opportunity than ever before.

Mr. BACA. Okay. Then to John Queen. The marketing agreement and contracts you described in your testimony have clearly provided great benefit to many producers and consumers, but what about those that don't participate in contracts? Are producers who do not have the same advantages, are they being left behind or not?

Mr. QUEEN. No, sir, every producer has the same ability or the same chance to enter into these alternative marketing arrangements, and we have proven that in the southeast. We have very small producers there and the opportunity for those producers to come together whith their cattle—market them through an alternative marketing program to a feed lot or a packer, that certainly has been a great advantage to us there in the southeast.

Mr. BACA. And how are we reaching out to them to make sure that they are not left out?

Mr. QUEEN. Well——

Mr. BOSWELL. Mr. Baca, would you yield?

Mr. QUEEN. —it is just common knowledge that they have the——

Mr. BACA. I yield to the Chairman——

Mr. BOSWELL. So you are saying that a cooperative system or some kind of way that these small producers are banding together to provide a market that would interest an AMA-type operation?

Mr. QUEEN. Yes, sir. I run a video sale. We had 39 semi loads of cattle, and we could go today, that we sold there in western North Carolina. Those cattle, if you will look at the different opportunities from each individual load on there and how they were either age and source verified or——

Mr. BOSWELL. Okay, I understand what you are saying and I appreciate that. So give me some, if you can remember it, because I won't expect you have, but what size operators come together, bringing drafts of——

Mr. QUEEN. They can come from 10 head to 10,000 head. It makes no difference to commingle those calves to create those trailer-load lots, and each one of those trailer-load lots has a different——

Mr. BOSWELL. It almost sounds like an NFO operation. I am not being facetious. It does kind of sound like it.

Mr. QUEEN. No, sir. But in the past, in the south, we have had a terrible reputation for our cattle down there, so the producers are coming together to create better opportunities for the cattle in the south, and we are the largest cattle——

Mr. BOSWELL. I won't take up any more time and I might want to pursue this, to visit with you some on that. I appreciate you saying that. I yield back to you, Mr. Baca.

Mr. BACA. I think he has completed the answer and I think we still need to do a little bit more of the outreach to make sure that no one is left behind. So I think that was part of your additional question, too.

Mr. BOSWELL. It is but I am giving you back your time.

Mr. BACA. Yes, okay. No further questions. Thank you. I yield back the balance of my time.

Mr. BOSWELL. Well, thank you. Mr. Hayes.

Mr. HAYES. Mr. Queen, you have been extremely active and helpful, along with many others, on the voluntary animal ID situation. We have got the consent and agreement of USDA to do this, but had a little trouble winnowing down the requirements for them to certify. Just give us a quick update. That is still the way to go?

Mr. QUEEN. Yes, sir. We are strictly for a voluntary market-driven, cost-efficient animal ID system in America today. And it will work and it shows that through the alternative marketing agreements that we have, how that does add value. So it is ongoing and we have a lot of producers today.

Mr. HAYES. Thank you, Mr. Chairman. That is my question.

Mr. BOSWELL. Thank you, Mr. Hayes. Mr. Boyle, based on conversation with Mr. Queen, do you agree that the small operators out there across the country got that opportunity? It sounded like they are very organized in that part, but what about some of the other places?

Mr. BOYLE. That is true throughout the Nation, not only for small producers, but for the midsize and smaller packers that we represent. The arrangements that you have with one's livestock suppliers are not the size of the operation.

Mr. BOSWELL. Let us just say a small producer in the State of Nebraska, Missouri, Iowa or Minnesota got a 100 to 200 cow herd that they feed out. Can they take advantage? Will there be a market for them?

Mr. BOYLE. Absolutely. If they want to market their livestock in partnership with a feeder and a packer, absolutely. That is available to them.

Mr. BOSWELL. So you think there is an adequate market?

Mr. BOYLE. I do. And you have seen it grow dramatically on the hog side in the last five or six years. And there are fundamental marketplace reasons for the growth in those marketing arrangements on the hog side. The red meat retail case has become revolutionized in the last five or six years.

Mr. BOSWELL. Well, I hear a lot of different producers say that they just don't have access. Is it because they don't know how to get the access, these small operations that are scattered across parts of the country? Mr. Queen has talked about their solution. But do they have access, the person that is sitting out there in Missouri that wants to run a 100 to 200 head cow herd and find a market?

Mr. BOYLE. Sure. The economics and the marketplace rationale are different amongst various species. Ninety percent of the hogs, as RTI has indicated in its report, and it is not a surprising conclusion, are marketed through some sort of marketing arrangement or a vertically integrated company on the hog production import processing side. That leaves a very small percentage of producers outside of that option, but I suspect they remain outside of that option through their own business decisions.

Mr. BOSWELL. Would it surprise you that I have farmers come up to me pretty regularly and say there are days I cannot find a market?

Mr. BOYLE. Well, there may be days when they go to market and in their particular geographic region, there may not be a broad-based market to acquire their cattle. But aside from that observation from producers that you have in your district, Mr. Chairman, that perception has been studied in great detail, in terms of whether or not there is anything nefarious about it, anticompetitive about it, conspiratorial about it, and under each of those investigations, the regulators have come away saying it is the normal functioning of a vibrant and competitive marketplace.

Mr. BOSWELL. Okay. Well, Mr. Hayes, if you are finished, I think I might as well speak, too. We do want to close by thanking you for your coming today and giving us your time, your willingness to testify, your frankness, and I think we have gained some knowledge today on both sides of the issue and it was good for us to have this time together, so I appreciate it. With that, we will adjourn. Under the rules of the committee, the record of today's hearing will remain open for 10 days to receive additional material and supplementary written responses from witnesses to any questions posed by members of the panel. The hearing of the Subcommittee on Livestock, Dairy and Poultry is adjourned.

[Whereupon, at 1:30 p.m., the Subcommittee was adjourned.]

Chairman Leonard Boswell
Opening Statement
Draft
Subcommittee on Livestock, Dairy, & Poultry
Hearing to review the market structure of the livestock industry
April 17, 2006

I would like to thank everyone for joining me here today. I would like to give a special thanks to our witnesses for testifying before the Committee today and to offer insight into the market structure of the livestock industry. I appreciate this opportunity to hear what the current issues facing the market structure in the livestock industry are and how those issues are affecting producers across the country.

The over arching issue that I hope this hearing does not forget is that we, as the agriculture community, must ensure that we have a safe and plentiful food supply. We need assurances that producers can make a living while the processors and packers have enough product available so they can provide consumers in the United States with a reliable and safe food supply. With land prices at record numbers, the livestock industry is one of the last sectors in the agricultural industry that young, first-time farmers are able to get involved in. We must ensure that there is adequate market access for those producers to make a living.

The livestock industry has been extremely beneficial to rural develop—I see this all over the state of Iowa. We must ensure that the livestock industry stays strong and continues to contribute to rural communities.

Over the last 20 years the livestock industry has become more and more consolidated, a prime example is in the poultry industry. This concentration in the livestock industry raises many concerns on what the future may hold for independent producers. Unfortunately, this is not a cut and dry issue. There are many factors that contribute to the structure of the livestock market. And today I hope this hearing will address many of them.

We will hear testimony today that the packing industry not only influences the livestock market but dominates it with over 80 percent of beef, 60 percent of swine, and almost 60 percent of the poultry markets dominated by four packers. After reading through the testimony submitted today many argue that there is adequate competition in the livestock industry. But when between 60 to 80 percent of the respective livestock industries are dominated by four packers when is this concentration cause for concern? When they hit 90 percent dominance?

Independent livestock producers often contend the lack of buyers of their livestock and the use of captive supplies by packers have a negative impact on the price they ultimately receive for their animals. Because packers can utilize their own animals for daily slaughter needs, they purchase fewer animals on the spot market; and some contend, the reported price for livestock does not accurately reflect prices paid to producers.

A concern I hear over and over again from producers in my district is that large packers can control market prices using packer ownership. Say a packer owns tens of thousands of heads of cattle. That packer buys on the open market for four days but when prices get too high they go and slaughter the cattle they own, thus depressing market prices. How is this not manipulation of the open market? And how do we as an industry regulate this?

We will also look at the study done by USDA to review this issue. RTI International was contracted to study the market structure of the livestock industry and recently published their Livestock and Meat Marketing Study. I am interested to hear what RTI has to say and was very interested in the results of this study.

I also look forward to hearing what our producer panels have to say. I understand this is a difficult issue to discuss, especially when the industry is extremely concentrated but I appreciate your willingness to share your story and your candor.

After reading through the testimony for this hearing two issues grabbed my attention: animal identification and country-of-origin-labeling. There are various opinions out there about both of these topics. And some discussion has centered on merging the two together. This is a new approach to attempting to address these issues and welcome discussion on this issue.

One thing that many of the witnesses focused on in the written testimony was alternative marketing arrangements (AMA) such as forward contracts, marketing alliances, and packer ownership. I have concern if these AMA's actually help the market or suppress market prices. I welcome conversation about these issues and the problems and concerns-or lack there of-regarding these issues.

As we started the farm bill discussion there has been much talk if there will be a competition title in the farm bill. I welcome this opportunity to further that discussion with varying opinions. Thank you again for joining me here today.

At this time I would like to turn it over to my good friend and colleague, Robin Hayes from North Carolina for any opening remarks he would like to make

Opening Statement of Ranking Member Robin Hayes
Agriculture Subcommittee on Livestock, Dairy, and Poultry
Hearing to review the market structure of the livestock industry
April 17, 2007

Chairman Boswell has called today's hearing to discuss the structure of the livestock and poultry industries. We will hear from the U.S. Department of Agriculture's Grain Inspection, Packers and Stockyards Administration (GIPSA) whose role is to regulate and maintain fair competition among the livestock industry. Also joining USDA is RTI International based in Research Triangle Park, North Carolina, who conducted a study on Livestock and Meat Marketing. Our other two panels consist of producer groups and various associations interested in the economics of the livestock sector who will share their perspectives on these issues.

Let me start off by assuring all of those present and listening today that I support the full and rigorous enforcement of all laws intended to ensure a fair, orderly and transparent livestock market function. While we may differ about the future shape of policy in the area of market structure, I know of no disagreement about the fundamental need for strict enforcement of the authorities under the Packers & Stockyards Act.

After resisting the temptation in the last farm bill to further insert the federal government into the structure of livestock markets, Congress made a commitment in the Conference Report to look into this matter further. For this reason, in June of 2003 I took this Subcommittee to Grand Island, Nebraska to examine this topic. While most of the testimony that day centered on the specific idea of banning packer-owned livestock, discussions ranged across virtually all of the ideas regarding industry structure, so we had a very informative hearing.

For me, the most important impression from our hearing was a wide divergence of views held by the witnesses. We had testimony from both producers and packers from Nebraska, and my home state of North Carolina. And, while all witnesses shared a common desire for a profitable livestock production sector with orderly market operation, there was virtually no consensus along any lines about whether the proposed changes would improve conditions or harm those they were intended to help.

In 2003, Congress had recently appropriated $4.5 million in funding to produce GIPSA's Livestock and Meat Marketing Study which was just published on February 16th by RTI International. We did not have the benefit of this report at our hearing in Nebraska, and I look forward to today's testimony on the study's findings.

Mr. Chairman, as you and other Members of this Committee know, industry structure issues invoke passion and long-held beliefs from livestock producers across the country. What producers in the 8th District of North Carolina want and what producers in the 3rd District of Iowa want can be two completely different things. I personally believe the complexity and intricate details of marketing and competition issues deserve more than one hearing before any decisions are made. I do not believe these issues should be considered as part of any farm bill discussion as the laws governing industry structure are completely separate from that of the farm bill and it should be kept that way. These issues should be considered in their own forum and given the proper attention they deserve.

I appreciate all of the witnesses for being here today to discuss this important issue.

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Statement for the record for Congressman Walz

Mr. Chairman, Ranking Member Lucas, thank you for holding this hearing today.

Conservation is just an incredibly important part of our farm program. No one knows better than the agricultural producers who depend on the land to make their living just how important it is to be good stewards of our soil and water.

So I'm pleased that in recent years, our farm bills keep moving forward and making greater and greater investments in conservation programs.

I've conducted about 13 different farm bill forums around southern Minnesota to hear what people have to say about what they want included in the 2007 Farm Bill. And when I go out and do these meetings I have a big chart with me that shows how USDA's spending every year breaks down. And about 5% of all USDA spending goes to conservation programs. But I'll tell you what: the impact of those dollars far exceeds what you would think we'd be able to accomplish with that modest percentage.

I've been receiving the same message over and over again from the producers who have been coming to these farm bill meetings: we need to make the Conservation Security Program more user-friendly and easier to enroll in. This is a working-lands conservation program that is wildly popular with farmers, with environmentalists, with the wildlife and sportsmen's groups, and with urban folks who have no exposure to the farm program except the food that they eat. CSP is a winning program and we have been short-changing it and making it as tough as possible for people to participate in and that just needs to stop.

I have heard from dozens of my constituents who are enrolled in CSP and made improvements to the land in order to move from Tier One to Tier Two or from Tier Two to Tier Three. And when they did that, after they invested what, in some cases, amounted to several tens of thousands of dollars, they were told by USDA that there was not enough money in USDA's budget for the Agency to make good on its end of the contract. I think it is unbelievable that USDA would sign a contract with a farmer and then not pay them what they are entitled to. I sent an angry letter off to USDA about that a few weeks ago; I haven't heard back yet, but I'm going to keep pushing until I get a response.

I want to make a special note about one of the witnesses here today. Loni Kemp is a witness on the second panel, representing the Minnesota Project. Loni is a constituent of mine, and I'm proud that she's here today. The Minnesota Project does just outstanding work. For nearly 30 years they've been working to promote strong rural economies and helping farmers stay on the land. I know she's got a lot of insight into our conservation programs and what can be improved and I look forward to hearing from her and our other witnesses today.

House Agriculture Committee Chairman Collin C. Peterson
Opening Statement
Subcommittee on Livestock, Dairy, and Poultry
Hearing to review the market structure of the livestock industry
April 17, 2007

Thank you, Mr. Chairman, for calling this hearing today on issues related to the market structure of the livestock sector. I thank all the witnesses for their time today and I look forward to their testimony.

The livestock sector has been trending towards greater consolidation and vertical integration for two decades. Each year, a smaller number of processors are taking up a larger percentage of the market share in livestock production. According to USDA, four packers control more than fifty percent of the market share of beef, hog, and broiler output. In the poultry sector, where much of the industry is vertically integrated, processing companies are often involved in all stages of production, from the hatching of eggs to the wholesale marketing of finished goods.

One facet of this consolidation and reduction of competition is the growth of alternative marketing arrangements (AMA) like forward contracts, packer ownership, and marketing alliances. There is vigorous debate on these arrangements and their effect on market prices. Multiple studies have been called for and undertaken to examine these arrangements, since there are some producers that feel such alliances are anti-competitive and are causing the move towards greater consolidation in livestock production. I am sure we will hear those arguments today from some of our witnesses.

The most recent study was done by the Grain Inspectors, Packers, and Stockyards Administration, and I thank them for appearing today to discuss their findings. Their "Livestock and Meat Marketing Study" concluded that certain alternative marketing arrangements employed by meatpackers, including forward contracting and ownership of livestock, reduces the prices that livestock producers are paid. However, GIPSA's study also concludes that attempting to place restrictions on these arrangements would increase the prices consumers would pay at the supermarket but not add to the bottom lines of farmers and ranchers.

I tend to believe that producers and processors will enter into financial arrangements in their best interest and that we in Congress should not attempt to get ahead of them in predicting behavior. If the last year of prices has shown us anything, it's that locking in a price is not the worst thing in the world for a livestock producer to do. And if they think they can get a better price in the spot market, then they will take that route instead.

Nevertheless, we must ensure that producers are getting a fair market price and that they are playing on a level field when making these decisions. If the spot market price is being unduly affected by the animals that packers own and can slaughter as an alternative to the open market, then that may be an issue for Congress to address in the future.

I also noticed in the testimony the discussion of other issues facing the livestock sector, including mandatory country-of-origin labeling and animal identification. I look forward to hearing from the producer and packer groups about these issues, particularly the implementation of a mandatory COOL system, which was codified in the 2002 Farm Bill and should be implemented in a workable, cost-effective fashion without additional delays.

I thank the Chairman once again for calling this hearing today and I yield back my time.

Testimony of Mr. James E. Link, Administrator
Grain Inspection, Packers and Stockyard Administration
U.S. Department of Agriculture

Before the
Subcommittee on Livestock, Dairy, and Poultry,
House Agriculture Committee
April 17, 2007

Introduction

Mr. Chairman, and members of the Subcommittee, good morning. Thank you for the opportunity to discuss USDA's efforts to promote fair trade practices by prohibiting unfair trade practices and enforcing the law against anticompetitive practices in the marketing of livestock, meat and poultry. Accompanying me today is Mr. Alan Christian, Deputy Administrator for Packers and Stockyard (P&S) Programs, and Dr. Gary McBryde, Director of P&S Industry Analysis. My testimony will provide an overview of trends in the critical components of the U.S. livestock market, and changes USDA has made to more effectively deal with and regulate the industry.

My appointment to the Grain Inspection, Packers and Stockyard Administration (GIPSA) began October 17, 2005. Although I am new to the Department of Agriculture, I certainly am no stranger to the agricultural industry. Growing up on a farm and devoting my entire professional career to the livestock industry has given me a rich and diversified background from which I am able to speak to you today. My job is to enforce fair business practices and take action against anticompetitive practices in the market of livestock, meat, and poultry. Shortly after my arrival at GIPSA, I was given a briefing about an ongoing Office of the Inspector General audit. Now, over the past year we have worked extensively to enhance GIPSA's ability to regulate livestock marketing and procurement practices. Today, it is an honor to share with you the current trends we see in the industry and the steps we are taking in GIPSA to better enforce against unfair or anticompetitive acts or practices.

Trends in Structure and Financial Performance

The Packers and Stockyards Program of GIPSA administers and enforces the Packers and Stockyards Act (P&S Act) and monitors financial and business practices in the livestock, meatpacking, and poultry industries. All dealers, auction markets, and packers purchasing $500,000 or more of livestock annually are required to file an annual report with us. Data available from these reports provide a snapshot of trends in industry structure, financial performance, and business practices.

Aggregate Industry Trends

Through this data we have been able to see and analyze aggregate industry trends. The number of plants reporting slaughter of any species to GIPSA has declined by approximately 100 plants or 38 percent from 1995 through 2003 as plant size increased and smaller plants closed. This trend shows some signs of slowing since 2002. Let me share with you the species breakdown of the trend. The total volume of cattle (steers, heifers, cows, and bulls) slaughtered by firms reporting to GIPSA fluctuates with the cattle cycle and has trended downward over the last 10 years. Hog slaughter has trended upward in the last 10 years while the number of hog slaughter plants has declined over time. However, the rate of decline has slowed since 1999 and the number of hog slaughter plants actually increased in 2004. The volume of sheep and lambs slaughtered by packers reporting to GIPSA increased in 2004 for the first time since 1998 but declined in 2005. The number of plants slaughtering sheep and lambs declined by 43 from 1995 through 2002 but has been relatively stable since then.

In the poultry industry, federally inspected broiler slaughter (measured in pounds of ready-to-cook broilers) has trended upward since 1995, while turkey slaughter has been relatively constant. USDA's World Agricultural Outlook Board (WAOB) estimates that broiler and turkey slaughter will be 1 percent and 3.3 percent higher, respectively, in 2006 than in 2005.[1]

I will use two financial ratios, one for expenses and one for income, to provide a summary of financial conditions in the meat packing industry. First, operating expense expressed as a percentage of sales of meat packing firms has trended upward over the last several years, illustrating the combined effects of changes in input costs and in firms' production practices on the costs of doing business over time. This ratio for large firms tends to be lower than is the case for smaller firms. Second, operating income as a percentage of sales, a measure of profitability, has trended slightly upward in recent years, with considerable year-to-year variation.[2] These underlying financial conditions have implications at all levels of the market.

I would like to share some specific detail on the financial conditions for each livestock species. Large packers tend to have lower operating income on a per-herd basis than small ones, despite having lower operating expenses, due to the larger packers paying a higher average price for livestock. The four largest steer and heifer slaughter firms have accounted for between 78 and 82 percent of total annual volume of that type of slaughter since 1995. GIPSA expects a modest additional increase in the combined market share of the four largest firms in 2006. Among hog slaughter firms, slaughter concentration increased from 55 percent in 2002 to about 64 percent in 2003 and has remained at 64 percent since. We expect very little change in the four largest firms' market share in 2006. The combined market share of the four largest sheep and lamb slaughter firms has trended downward since 1998, but in 2005 the four largest firms increased their combined slaughter volume while total industry slaughter declined. We expect concentration to be close to 63 percent in 2006. In poultry slaughter, concentration has remained fairly constant since 2003, with slight declines in broiler and turkey slaughter in 2005. Recent firm acquisitions will likely increase concentration in broiler slaughter and turkey slaughter slightly in 2006.

Trends Related to Livestock & Poultry Procurement, Business Practices, and Vertical Coordination

I will share with you the vertical trends of the livestock and poultry industry, having reviewed the horizontal aspects of industry structure. Vertical structure relates to the relation between segments in the market channel.

1 Sources: World Agricultural Outlook Board, World Agricultural Supply and Demand Estimates, WASDE-445-31, WASDE-445, April 10, 2007, http://www.usda.gov/oce/commodity/wasde/latest.pdf

2 Operating income as summarized here is sales minus cost of sales (primarily cost of livestock) and minus operating expenses, and is essentially a measure of profit before taxes.

Packers use multiple procurement methods to obtain livestock for slaughter but the methods commonly fall into two categories: (1) cash sales for immediate delivery or normally within a 2-week period, and (2) "committed procurement" arrangements that commit livestock to a particular packer in excess of 14 days prior to delivery. These committed procurement methods include marketing agreements, forward contracts, and packer feeding.

We collect and audit data on the major committed procurement methods used by the four largest firms that slaughter fed cattle. Marketing agreements account for 24 percent of total procurement in 2006 by the four largest steer and heifer slaughter firms. Packers obtain six percent of their total slaughter from feeding arrangements and forward contracts. The remaining 70 percent is obtained on the spot market.

Approximately 10 percent of hogs are sold on the spot market, 70 percent through forward contracts and market agreements, and the remaining 20 percent are packer owned.[3]

Procurement methods used in the purchase of sheep and lambs for slaughter are similar to those used for other species and include purchase in spot markets, use of marketing agreements, use of various other forms of advance sales contracts, and packer feeding. On the other hand, we have seen the poultry industry become almost completely vertically integrated for several decades, and the use of spot markets for poultry is virtually nonexistent. Live poultry production is coordinated through production (grow-out) contracts, company-owned farms, and marketing agreements. With production contracts, the integrator (poultry slaughter and processing firm) owns the birds and the feed, and the grower's compensation is based on the services the grower provides. With marketing agreements, growers retain ownership of both the birds and the feed, and growers' compensation is determined by the difference between the stipulated price of the finished product and the cost of producing it. There are no marketing agreements in broiler production, but they are used in turkey production.

Administrative Implications of Industry Structural Trends

Now that I have reviewed the current market structure, I will share with you what this means for our organization. GIPSA has authority under the P&S Act to prohibit unfair or anticompetitive acts or practices in the marketing of livestock, meat and poultry. We do not have authority to review or prohibit mergers and acquisitions but often cooperate with and lend our industry expertise to the Department of Justice (DOJ) in DOJ's review of mergers in the livestock, meatpacking, and poultry industries.

Changes in concentration, vertical integration, producer complaints, or other changes in industry structure may lead us to focus more attention on particular firms or specific industry behavior. It is important to note that many of the changes in coordination associated with industry consolidation may also provide for improved performance of the industry. For example, structural change can facilitate penetration of retail markets with branded products. The capability to increase branded retail products depends on high levels of input supply management to achieve uniform and high levels of packing plant utilization, and production of carcasses that can be processed into uniform retail products.

[3] Grimes, G. Excerpt from U.S. Hog Marketing Contract Study. Based on MPR data. Jan., 2006. http://agebb.missouri.edu/mkt/vertstud06.htm

Recently we completed a broad study of marketing practices in the entire livestock and red meat industries from farmers to retailers, food service firms, and exporters. The study, completed under contract by RTI, Inc., included analysis of prices, costs, efficiency, livestock and meat quality, and of risk levels associated with alternative marketing arrangements (AMAs), and assessed the implications of potential future changes in the use of various types of marketing arrangements. The study found that the cash market continues to serve an important role in the industry for price discovery and in particular for smaller producers and packers. Cash market prices are also frequently used as the base for formula pricing under AMAs and are important for marketing arrangements using formula pricing. As long as prices are reported for different types of marketing arrangements—as with current USDA price reporting—base prices reflect expected supply-demand conditions.

While in the aggregate AMAs were given a good bill of health by the study, the measurements of the stability of the respective (cattle, versus hog, versus sheep) cash market prices indicate their sensitivity to volume changes and the need for monitoring to identify individual instances when AMA use maybe associated with a violation of the P&S Act and result in a need for enforcement action. Increased consolidation calls for increased vigilance by the P&S Program due to the increasingly complex nature of new marketing and procurement practices, and to the arguably increased potential for anticompetitive behavior.

We will continue to evaluate complaints alleging anticompetitive behavior, including those that arise from concerns about high levels of concentration, such as attempted restriction of competition, failure to compete, apportionment of territory, price discrimination, price manipulation, and predatory pricing. While we do not direct the form of continuing consolidation and increased coordination, we will play a role in helping the marketing system operate in a competitive manner to the maximum potential benefit of the industry members and also to the benefit of U.S. food consumers. As we evaluate the current status of the industry, we have also evaluated our own organization.

Current Initiatives

The following are some of the steps we have taken to strengthen the P&S Program in the last year:

Reorganization

We have reorganized our headquarters and regional office to deliver more efficient and effective services nationwide. Utilizing input from management consultants and organizational analysis, we initiated multiple changes in the structure of the organization and operations. At headquarters, we eliminated a complete layer of management in the P&S Program by dissolving the Regional Operations Division and having regional directors report directly to the deputy administrator. Further, we have combined all of our agency-wide support services into a single unit that provides "shared services" (e.g., personnel, purchasing, safety and health, labor relations, training, etc.) across all GIPSA programs. We also removed structural and policy boundaries that prevented direct communication across the organization. We now encourage through written policies, communication at all levels of the organization to effectively deal with policy development and program implementation issues. For example, our legal specialists now work directly with the Office of the General Counsel to improve the quality and timeliness of investigations. Our Financial and Business Practices Units hold monthly conference calls between the regions and headquarters to share investigative experiences and work on unit related issues collectively. Also the development of a comprehensive internal review program has improved monitoring and reporting on agency activities. All this in effect have reduced management layers and added additional cost savings to the Agency which allowed us to move 4 FTE's to field offices.

Policy and Direction

When I first began my role at GIPSA, I redirected the Agency to focus on our underlying mission to take action against business practices and anticompetitive practices in the marketing of livestock, meat, and poultry. It quickly became apparent to me that to really protect farmers and ranchers, and to adequately serve them in a consistent manner, we had to focus on updating our policies, procedures, and regulations in accordance with our mission.

In the past year, we have undertaken a top to bottom review of our regulations and policy. We established a regulation review task force to review existing regulations to ensure they were up to date and effectively addressed the current conditions in the industry. Several regulatory work plans were developed with the intent of proposing changes for public comment. A number of proposals to better define and enhance the regulations affecting poultry marketing will be published for public comment in the near future.

We have also issued 37 GIPSA Directives and 20 P&S Policy Memoranda providing instruction and guidance to the P&S employees. Much of the initial effort was in response to the OIG audit of January, 2006, but since that time we have established a permanent process to request and track policy issues that may be raised from anywhere in the organization. Also beginning in 2006 and continuing at 6 month intervals, we are updating our Employee Manual. The manual contains specific instruction to carry out the core functions of the organization and is an essential guide for both new and experienced personnel.

In response to an OIG recommendation and to strengthen accountability within P&S, we have developed a comprehensive internal review program. The accountability program monitors and assesses administrative and program activities for compliance with Agency policy, procedures, and performance measures.

Training

Both a Government Accountability Office report and OIG alluded to the importance of training the GISPA investigators to conduct complex investigations. Beginning in 2007, we are sending all of our investigators to the Department of Homeland Security's Federal Law Enforcement Training Center for basic investigative and interviewing training. We have completed 3 of the planned 5 courses and have received positive feedback from the employees on the value of the training. We have included the some of the Office of the General Counsel attorneys in the training courses to prepare them to better assist our investigations in more complex competition investigations and to foster a strong working relationship between P&S and OGC.

In addition, DOJ's Antitrust Division provided training for P&S and OGC on an issue that arose in competition investigations in 2006, and we are planning another training program with DOJ for later this year.

Internally, based on an employee assessment survey, we are developing a mandatory training program for investigators and a mentoring program for our remotely located resident agents

Strategic Business Plan

As we developed our new business plan we laid out 4 goals to 33 strategic activities with related measurable outcomes. Our intent is not only set forth goals but also to have tangible ways to measure our progress as we implement and evaluate our new business initiatives.

The four goals that we set forth are to (1) increase the level of compliance with the Packers and Stockyards Act through preventive regulatory actions; (2) attain compliance through investigation and enforcement; (3) implement directives, policies, regulations, and perform industry analysis that effectively and efficiently keep pace with the changing livestock, meat, and poultry industries; and (4) improve organizational efficiency and effectiveness. These four goals are the foundation for the steps we have taken over this past year.

To increase voluntary compliance with the P&S Act and increase enforcement against unfair trade practices and anticompetitive practices, we are focusing our first 2 programmatic goals on our regulatory reviews and investigation. We intend to determine the current compliance levels in the industry and target the areas with lower compliance rates for more inspection and regulatory activity. Some examples in the Business plan include:

1. Inspecting scales and carcass evaluation devices at all packing plants that kill over 1,000 head per year.
2. Inspecting scales at livestock markets to obtain a statistical sample of the compliance level at all markets to the 90% confidence level.
3. Checking prompt pay and custodial account compliance at packers, livestock markets and dealers to obtain a statistical sample of the compliance level to the 90% confidence level.
4. Initiate rapid response investigations within 2 business days of the complaint or event.
5. Decrease the average number of days to investigate and resolve potential violations by 5%.

Standard Operating Procedures

From October, 2006 through March, 2007 we undertook a complete review and reengineering of all of the P&S Program business processes. On April 2, 2007 we implemented the new standard operating procedures nationwide in headquarters and the 3 regional offices. Our new procedures will ensure we treat our customers and the regulated industry uniformly no matter where they are located. The new processes were developed from best practices we identified across the country and provide performance measures to compare and gauge our success at meeting our program goals. Our streamlined activities will allow more staff time to be devoted to program delivery – the regulatory reviews and investigations that are so important to enforcing the law against unfair and anticompetitive practices.

Investigations
In response to the 2006 Inspector General audit, GIPSA distinguished between investigations and regulatory compliance activities. The term Investigation means an activity that follows up on previously identified violations of the Act; is conducted in response to industry driven complaints, or is conducted in response to possible violations found in the course of compliance activities. In contrast Regulatory Compliance means activities of a routine nature that assess whether a subject entity is operating in compliance with the Act. These are activities conducted when P&SP has no reason to believe a violation has occurred.

Investigations are a top priority for us. Just this year by implementing our new business plan we have made significant progress. We look forward to continuing our progress and investigating for alleged violations in a timelier manner over the course of this fiscal year.

GIPSA is currently investigating a number of potential violations of Section 202 of the Packers and Stockyards Act by packers that include allegations of unfair or deceptive practices and attempts to apportion purchases or manipulate prices by packers. Some examples of current activity include:

Manipulation of the Cash Price -We have five open investigations that are focusing on allegations that packers attempted to manipulate the negotiated prices through buying, or selling. Three of the investigations involve the allegations of manipulating the cash price for hogs and one involves an allegation that packers conspired or agreed to act in concert to affect the cash market for cattle. GIPSA is working jointly with the Department of Justice on one of the investigations and OGC attorneys are working closely with us on the others.

Failure to Disclose Purchase Terms -We are investigating the alleged failure of at least two packers to fully disclose purchase terms and to properly apply premiums and discounts in their carcass merit or value-based purchases.

Failure to Properly Weigh- We have four open investigations involving allegations of improper weighing or instances where the entity did not pay based on the hot weight as required. These investigations include inaccurate scales, inaccurate tare weight for the scale trolleys, not using the hot weight in payment, not rounding the weight correctly and not weighing properly. Altogether in 2006 we had 57 investigations conducted against livestock dealers, markets and packers to protect farmers and ranchers from unfair practices. We had an additional 11 poultry inspections on weighing practices. In another case, GIPSA has filed a complaint against a packing company for improper recording of weights from 2001 to 2004.

Failure to Pay Promptly- GIPSA has two open investigations involving allegations that packers did not pay promptly as required by regulation. The investigations deal with cattle sold on a formula or non-cash basis. Also in 2006, 13 livestock dealers, 9 auction markets, and 5 packers experienced financial failures. These failures resulted in investigations that led to livestock sellers being compensated.

Unfair Competitive Practice- GIPSA has three open investigations focusing on allegations of unfair or discriminatory behavior including a packer's financial interest in a marketing agency, turn taking at livestock markets and refusals to purchase from certain sellers. These ongoing investigations are a significant piece of our efforts to regulate the industry, and again OGC attorneys are working closely with our investigations.

While the example mentioned above focuses on violations of Section 202 of the Act that regulates packers, live poultry dealers, and swine contractors, GIPSA is committed to enforcing the Act and regulations uniformly with regard to all regulated segments of the industry. We are aggressively pursuing violations involving prompt pay, custodial accounts, weighing, bonding and failure to register by dealers, market agencies and unregistered entities. The Act provides financial protections and enforcement authority over unfair trade practices throughout the marketing channels for livestock, meat and poultry. We are committed to improving our monitoring of all regulated activities for compliance. The increase in cases referred for formal administrative or civil action during 2006 and the first half of 2007 demonstrates our commitment to enforcement to ensure farmers and ranchers are not victimized by unfair practices or financial failures by buyers.

Immediate Concern - Bonding

As the current market structure changes, we will continue to adjust our regulatory efforts to monitor more efficiently and effectively the regulated industries. One issue of immediate concern is the level of financial protection provided by the current bonding requirements.

Over the past several years, we are finding that, in the event of a dealer market failure, sellers of livestock are only able to recover about 13 to 23 cents on the dollar from the current bonding required by regulation. For packer failures, the sellers are able to recover about 20 cents on the dollar partly due to the statutory trust fund that also provides protection. We are currently evaluating several options, both regulatory and legislative, to remedy the situation.

I am proud to serve as the administrator for GIPSA in a time where not only the industry, but also the organization is being evaluated, assessed and improved. It is exciting to be a part of such fundamental changes. With the continued work and efforts of the individuals within GIPSA, we will look forward to improving and becoming even better at regulating an industry where constant change is not only expected, but inevitable.

Conclusion

Mr. Chairman, Thank you again for the opportunity to appear before you today. We look forward to working with the Subcommittee to regulate these very important components of U.S. agriculture, particularly the livestock meat marketing sector. I will be happy to answer any questions that members might have for me.

Prepared remarks
of
Mary K. Muth, Ph.D.

Director, Food and Agricultural Policy Research Program
RTI International
before the
United States House of Representatives Committee on Agriculture's
Subcommittee on Livestock, Dairy, and Poultry

regarding

"Market Structure of the Livestock Industry"

April 17, 2007

RTI
INTERNATIONAL

Good morning Chairman Boswell and members of the subcommittee. My name is Mary Muth, and I am director of the Food and Agricultural Policy Research Program at RTI International, an independent not-for-profit research institute in Research Triangle Park, North Carolina. I was the project manager for the congressionally funded GIPSA Livestock and Meat Marketing Study that was completed earlier this year. I am an agricultural economist by training and have a PhD in economics from North Carolina State University. I have been conducting analyses of the livestock and meat industries for almost 15 years. In addition, my husband's family owns a cow-calf operation in western Kentucky. I am pleased to be here and thank you for the opportunity to provide an overview of the findings of the Livestock and Meat Marketing Study.

The study was conducted from July 2004 through January 2007 by a team of researchers at RTI International, Iowa State University, North Carolina State University, Montana State University, Colorado State University, and the Wharton School at the University of Pennsylvania. The team conducted a large number and range of analyses for the study to meet the requirements of the Performance Work Statement for the contract with GIPSA.

The study addresses the economic effects that alternative marketing arrangements have on the livestock and meat industries. As you know, the cash (or spot) market includes auctions, direct trade, and use of dealers and brokers. In contrast, alternative marketing arrangements include all other marketing methods such as marketing agreements, marketing and production contracts, packer ownership, and forward contracts. The final report comprises six volumes covering the various aspects of the analysis. It follows publication of an interim report in August 2005 that described marketing arrangements used in the livestock and meat industries and qualitatively the reasons why they are used.

In the final report for the study, we analyzed (1) the extent of use of alternative marketing arrangements, price differences across marketing arrangements, and the effects of using marketing arrangements on cash market prices; (2) the costs and benefits of various marketing arrangements, particularly as they relate to quality, costs of production, and risk; and (3) the implications of using marketing arrangements on livestock producers, meat packers, and consumers. We used state-of-the-art economic modeling and statistical analysis methods to address the requirements of the study with the following types of data:

- an industry survey of livestock producers, meat packers, meat processors, retailers, wholesaler, food service operators, and exporters;
- purchase and sales transactions data collected from meat packers and meat processors (2.5 years of data, from October 2002 through March 2005);
- profit and loss data from meat packers (also 2.5 years of data)
- results of industry interviews with producers, packers, and meat buyers;
- Mandatory Price Reporting (MPR) data; and
- other publicly available data.

Note that the industry survey was a statistically designed sample and included responses from 293 beef producers, 229 hog producers, and 302 lamb producers. The transactions data for beef represented 58 million head of fed cattle purchased by 29 beef plants, and the transactions data for pork represented 190 million head of finished hogs purchased by 29 pork plants.

In general, the study found that use of alternative marketing arrangements in the livestock and meat industries provides benefits not only to meat packers but also to livestock producers and meat consumers. Therefore, restricting their use would have negative economic consequences on most segments of the industry. Next, I would like to give a broad overview of the specific results of the study organized along the six central questions for the study.

The first question concerned what types of marketing arrangements are used and the extent of their use. Based on the data available for the study, we estimated that alternative marketing arrangements represent 38% of the volume for fed cattle, 89% of the volume for finished hogs, and 44% of the volume for fed lambs sold to packers. Furthermore, we estimated that packer ownership volumes represent less than 5% of fed cattle and fed lamb volumes and 20 to 30% for finished hogs. The higher estimate for finished hogs is based on assuming that transactions classified as "other purchase method" represent hogs raised under production contracts with a packer.

In the beef industry, fed cattle are sold primarily through the cash market (specifically, direct trade) and marketing agreements. Based on the industry survey and interviews we conducted, we expect alternative marketing arrangement use in the beef industry to remain at similar levels in the near term. In the pork industry, finished hogs are sold using a large number of methods, including direct trade, marketing contracts (highest), marketing agreements, and packer ownership (packer-owned farms and production contracts with packers). Based on the industry survey and interviews we conducted, we expect alternative marketing arrangement use in the pork industry to remain at similar levels in the near term. Finally, in the lamb industry, fed lambs are sold primarily through auctions and marketing agreements, but custom feeding and/or slaughter is also significant. Based on the industry survey and interviews we conducted, we expect a moderate increase in the use of alternative marketing arrangements in the lamb industry in the near term. Note that, across all species, most packers and many producers use portfolios, or combinations, of marketing arrangements rather than a single type.

In discussing the next five key study questions, I will focus primarily on beef and pork, but I will say a few words about the lamb industry at the end.

The second question concerned the price differences across marketing arrangements, and whether the use of alternative marketing arrangements affects cash market prices. In the beef industry, prices for fed cattle (for a given level of quality and controlling for seasonality) are similar for direct trade and marketing agreements, higher for the small percentage of auction barn cattle, and lower for the small percentage of forward contract cattle. We found that a 10% reduction in the volume of spot market transactions, assuming that volume is shifted into alternative marketing arrangements, results in an extremely small decrease in the spot market price of 0.1%. In the pork industry, prices for finished hogs (when controlling for differences in quality and seasonality) are higher for marketing contracts and lower for packer-owned hogs relative to the cash market. We found a relatively large effect of using alternative marketing arrangements on cash market prices for hogs. A 1% increase in hogs under contract is associated with almost a 0.9% decrease in cash market prices. We believe this estimate is this high because alternative marketing arrangements already comprise 89% of the volume of finished hogs sold; thus, a further increase from this high percentage causes a large effect on the cash market price. In addition, we found that a 1% increase in hogs under packer ownership is associated with a 0.3% decrease in cash market prices.

The third question concerned the effects of alternative marketing arrangements on costs of production at the packer level, that is, on costs other than the cost of purchasing livestock. In the beef industry, procurement of cattle through alternative marketing arrangements is associated with lower production costs per head than through cash markets, but this result does not hold for all packing plants. The estimated average cost savings are $6.50 per head, compared with an average processing cost of about $138 per head (or about 5%). In the pork industry, procurement of hogs through alternative marketing arrangements is associated with an extremely small decrease in production costs. Specifically, a 1% increase in alternative marketing arrangement use is associated with an extremely small decrease in marginal costs at the sample means because alternative marketing arrangement use is already extremely high.

The fourth question we analyzed was whether and how the quality of livestock and meat varies across marketing arrangements. In the beef industry, we found that cattle sold through marketing agreements, the primary alternative marketing arrangement, were higher quality and had less variation in quality than cattle sold through direct trade. Specifically, the increase in quality for marketing agreement cattle relative to direct trade cattle is equivalent to a 57 cent per cwt increase in value. It is also notable that the small percentage of sales through auctions was associated not only with the highest quality but also the highest variation in quality; this is likely due to specialty sales in particular regions of the country. In the pork industry, we found that hogs sold through marketing contracts, the primary alternative marketing arrangement, were higher quality than hogs sold through direct trade. Marketing contract hogs ranked higher across multiple quality measures, such as average lean percentage, loin-eye area, and average loin depth, compared with other types of marketing arrangements.

The fifth question we analyzed was how risk, particularly market access risk and price risk, varies across marketing arrangements Across all species, alternative marketing arrangements offer some guarantee of market access, for both livestock producers and meat packers. That is, alternative marketing arrangements ensure that producers can sell livestock and meat packers can purchase livestock when they need to for their business operations. In the beef industry, prices for cattle sold through marketing agreements, the primary alternative marketing arrangement, were less variable than for cattle sold through direct trade. Specifically, the variance of prices for marketing-agreement cattle was 18 to 20% less than for direct-trade cattle when controlling for differences in quality. Auction barn and forward contract cattle were associated with the highest levels of price risk for fed cattle. In the pork industry, prices for hogs sold through marketing contracts, the primary alternative marketing arrangement, had lower variance than hogs sold through direct trade. The variance of prices for hogs sold through marketing contracts was 5 to 45% less than for hogs sold through direct trade (but not controlled for differences in quality). Furthermore, in the pork industry, use of production contracts for hog producers eliminates about 94% of the producer income volatility compared with independent hog producers. Risk-averse producers, in particular, benefit from the availability of production contracts.

The final question we analyzed concerned the potential effects of restricting alternative marketing arrangements on livestock producers, meat packers, and consumers. We conducted simulations of various hypothetical scenarios in which alternative marketing arrangements were restricted. In general, these simulations indicate losses to livestock producers and consumers due to losses in efficiencies in the market. These losses in efficiencies translate into higher prices for consumers purchasing meat and lower prices for producers selling livestock. Specifically, in the beef industry, eliminating alternative marketing arrangements would cause livestock producers and feeders, beef packers, and consumers to lose economic surplus. Our beef industry model indicates that over 10 years, eliminating alternative marketing arrangements in the beef industry would reduce economic surplus by 5 to 16% for each sector of the industry. Even if you assume some level of market power exists in the industry, and that elimination of alternative marketing arrangements would eliminate the market power, all sectors of the industry still lose economic surplus, but the losses are slightly smaller. In the pork industry, one of the scenarios we considered was increasing the cash market share to 25%, from its current 11%. Our pork industry model indicates that this restriction would cause hog producers and pork consumers to lose economic surplus, but that pork packers would be affected very little. Our specific estimates are that, over 10 years, increasing the cash market share to 25% would reduce economic surplus by 3 to 5% for hog producers and pork consumers, but slightly increase economic surplus for pork packers. Reducing alternative marketing arrangement use benefits producers to some degree because of a reduction in market power by pork packers, but the loss in cost efficiencies offsets the effects of reduced market power.

To return to the results for the lamb industry, we found the results of analyses to be relatively similar to the results for the beef industry described above with a couple of notable differences. Specifically, we found that prices of fed lambs sold on the cash market are slightly higher than other methods, and use of alternative marketing arrangements does not appear to reduce price risk. However, procurement of lambs through alternative marketing arrangements is associated with lower production costs and higher quality.

In conclusion, use of alternative marketing arrangements in the livestock and meat industries provides benefits not only to meat packers but also to livestock producers and meat consumers. Restricting their use would have negative economic consequences on most segments of the industry. Across the scenarios analyzed, livestock producers would have greater economic losses due to restrictions than packers. However, it is also important to note that the cash market serves an important role in the industry, particularly for smaller producers and packers. Reported cash prices are frequently used as the base for formula pricing under, and thus are important for, any type of marketing arrangement that uses formula pricing.

Mr. Chairman, I would like to enter into the record Volume 1 of the report for the Livestock and Meat Marketing Study. This volume contains the executive summary and overview for the study. Thank you.

Testimony of Kay Doby
Poultry Grower
Cameron, North Carolina

Before the

House Committee on Agriculture
Subcommittee Livestock, Dairy and Poultry

Hearing on

A Review of the Market Structure of the Livestock Industry

April 17, 2007

Chairman Boswell, Ranking Member Hayes, Members of the Subcommittee-

My name is Kay Doby. I am poultry grower from Cameron, North Carolina. Thank you for this opportunity to submit this testimony on behalf of the Campaign for Contract Agriculture Reform.

The Campaign for Contract Agriculture Reform (CCAR) is a national alliance of organizations working to provide a voice for farmers and ranchers involved in contract agriculture, as well as the communities in which they live. The goal of the campaign is to assure that the processor-producer relationship serves as a fair partnership, rather than a dictatorship. I am the President of the North Carolina Contract Poultry Growers Association as well as a member of the National Contract Poultry Growers Association, both of which are long-standing members of CCAR.

In the past, farm bill debates have focused on issues such as research, credit, conservation, and the structure of commodity price support mechanisms and direct farmer assistance programs. Certainly, those issues will continue to be a central part of the debate for the 2007 farm bill. But the structure of U.S. agriculture is rapidly changing and therefore the focus of the farm bill process should also be broadened to keep pace with the modern realities facing farmers and their communities.

Unfortunately, farmers are rapidly losing their independence. The traditional relationship of independent producers selling their products to independent processors is quickly changing toward an environment in which contractual arrangements between farmers and vertical integrators and processors are commonplace. In addition, agribusiness firms are rapidly consolidating to gain market control. It is critical that the farm bill not only address the structural issues of agriculture to help independent farmers stay independent and viable, but it is also important to acknowledge the rapid shift toward contract production, and to address the unique needs and challenges of contract farmers.

No one knows about this changed structure and the pitfalls of those changes better than poultry growers. In fact, production contracts have been around for poultry since the 1950s, and nearly 100 percent of broilers are now produced under contract.

In previous Farm Bill debates, the voices of poultry growers have not been heard. Because of the contract relationship that growers have with their poultry integrator companies, it is very difficult for poultry growers to speak out about their problems.

In order to get started in the poultry business, a potential grower must take out a loan of over $300,000 per poultry house in order to build these sole-purpose structures on their farms to meet the terms of the poultry growing contact. The company provides the specifications for the house, but the grower has to pay for them. Often, growers don't even see the details of the contract before they take out the loan and build the houses, but instead are asked to move forward in making the financial commitment based on a "letter of intent" from the poultry integrator. So when a grower goes into debt to this extent, they must often put their farm and farmhouse up as collateral for the loan. At this point, the grower has very little choice but to sign the contract that is put before them. There are no negotiations. It is a take-it-or-leave-it contract. And it is subject to change at any time, based on the wishes of the poultry company. If you don't do as they say, they will stop delivering chickens to your farm, and you will not be able to make your loan payments. And as far too many growers have learned the hard way, if you attempt to speak out about your situation, or to work with other growers to raise concerns, you are vulnerable to contract termination or other more subtle methods of retaliation by the poultry integrator.

In 1993, my husband and I built two 500-ft poultry houses at a cost of $188,000 dollars. The specifications of how to build the houses were provided by the poultry company. The houses were financed through the poultry company with 20 acres of our land put up as collateral. The first contract I signed was for 5 flocks a year for 10 years, the length of the loan. In the beginning, things looked good. The first year we received six flocks, and I was hopeful, because it looked like I'd get my loan paid off before 10 years. Little did I know that after one year into my supposed 10-year contract, the company would bring us another contract to sign, this time for 3 years with no guarantee of the number of flocks.

The next contract was for 2 years with a mandatory arbitration clause added, saying that I could not take the company to court for any reason. Then a few years ago, I was presented with a yet one more version of the contract. That is only "flock to flock." The grow-out period for one flock is about 8 weeks. Talk about job security!! At that time, we still owed $60,000 on the houses and we were being told that we might get chickens to raise or we might not. Of course, without chickens in our houses, we would not be able to make the payments and we would lose the land we built the houses on. As a grower, you get the message very quickly. With your livelihood on the line, and the future of your business controlled completely by the company and its decision to give you birds or not, it's not a surprise the growers are reluctant to speak out about their circumstances. Plain and simple, they fear retaliation.

The Ranking System of Payment

Making matters worse, even when you do have chickens in your barns, growers are ranked against each other for their pay, based on the growers' success in adding weight to the bird over the grow-out period of 7 or 8 weeks. This is called your "feed conversion." The company will group you with between 4 to 15 other growers. They will take the average for that week of how much feed it took to grow the average weight bird. Then you will fall somewhere in the ranking system to determine what you will be paid. There will be half the growers making above the 50 percent mark and half of the growers will be in the minus. The companies will use the minuses to say you are a bad grower.

Now keep in mind that the company controls all of the inputs that determine your success in adding weight to the bird. For example, you have no control over the chicks that you receive. Maybe you received chicks that came from very young hens that just started laying, therefore you received little tiny chicks that have a hard time living and if they do live they never get to the weight of the others, but still eat as much. Now don't forget that your goal is to raise the heaviest bird on the least amount of feed. Maybe you received chicks that had an egg explode during the hatching process and it penetrated the other eggs with bacteria. If that happens, then you have sick little chicks. Yet you are being ranked for pay with growers that may have received healthy chicks.

The next problem is that you have no control over the feed. What if you get the wrong feed mixture for your age birds? If you get a low calorie feed, the birds are going to eat it and not put on as much weight.

Another factor that is beyond the growers' control is when the company will pick you your birds to take them to be processed. It is not uncommon for there to be a several-day variation in times that a grower's birds are picked up relative to other growers in their ranking. For example, if my birds are picked up at 58 days and the other grower's birds are picked up at 53, 54, 55 days, it makes a big difference. Your birds have just been sitting there for extra days eating thousands more pounds of feed and just adding to your litter. They have finished growing because the last days of feed are withdrawal, not packed with the calories for weight gain.

And even after your birds are picked up, there are still variations that could affect your pay greatly. Depending on the time they sit on the trucks before they go to processing, some of the birds may die. You aren't paid for a dead bird but you sure are charged for the feed that that bird ate.

The difference to my operation for being at the top of the ranking versus the bottom of the ranking for one flock is thousands of dollars. That's a lot of money, and it puts growers in the position to NOT want rock the boat, because the company can directly influence where you fall on that ranking. There is no way it can be fair to rank growers against one another when they never start out on the same level. There are too many things beyond the grower's control to base his pay on a ranking system, because a ranking system assumes fair competition and that growers are receiving the same inputs.

Forced Equipment Upgrades at Growers' Expense

One other commonly used practice that is economically abusive to growers is the practice of requiring equipment upgrades at the grower's expense, to make changes in the houses that were originally built to the company's own specifications.

With a traditional bank loan on a dwelling or land, one normally obtains equity as the loan is paid off. With loans for poultry houses and equipment, little equity is earned because the houses and equipment have limited salvage value. While loans are being paid off, cash flow is typically negative. After loans are paid off, cash flow may be positive, but inadequate to recover earlier losses.

Even with that dismal projection, the grower still works for the day that he will have the loan paid off. But guess what? The grower will never get to that day because the company won't let him. When a grower gets his houses paid for, the company wants the newer updated equipment in the houses or they will cut you off. So here you are with two choices, go back even deeper in debt or just sell your farm and salvage what you can.

The most recent example of this problem is tunnel ventilation. The poultry companies discovered by way of technology that if you put a chicken in a house and keep the temperature at 72 degrees after it feathers out and keep it virtually in the dark 24/7 for 8 weeks, you can raise a bigger bird on less feed. The feed is the company's only expense. Now this would be good if only the companies would share the profits with the growers, but they do not.

This new technology is achieved through what is known as tunnel ventilation. The curtains look white on the outside but they are black on the inside, no light can come through. Companies are now completely walling up one side of the houses. Some are even going so far as to wall up both sides. The only way the birds can get air is inlets in the ceiling that open when the fans come on to suck in air.

Our houses on our farm are what they call "conventional" houses. We have curtains that light can come through; the curtains come down automatically when it gets too hot. The company wanted us to convert our houses to tunnel ventilation, even though we paid hundreds of thousands of dollars to build our houses to their original specifications and still owed $60,000 on them. The new upgrades that they wanted us to make would cost an additional $80,000.

In other words it means that the company wants you to install tunnel ventilation so they can make more money off you. If you don't agree to do so, at your own expense, they threaten to stop giving you any more chickens and you will lose your farm. Poultry houses are a single-use structure and currently there is nothing else that can generate the revenue to pay for them that poultry can. You are completely vulnerable to the companies' demands.

I personally know growers that have been cut off. Others have given in and borrowed the money to do the upgrades, and are struggling under the additional debt.

While the companies do offer some additional pay to encourage you to shift to tunnel ventilation, I have looked at the figures and you can not make your additional loan payment with the improved pay they offer you. Not only can you not pay your loan, but you also have the additional expense of electricity because you must run fans to bring in fresh air in the summer. Before with conventional houses, you could just open the curtains, which is a much more energy-efficient strategy.

Farm business records show that contract producers who once had acceptable incomes from their poultry operations now put up a few hundred thousand dollars of equity, and borrow several hundreds of thousands more to hire themselves at minimum wage with no benefits and no real rate of return on their equity. Yet, integrators continue to earn 10 – 25 percent rates of return on equity.

Consumers have benefited from vertical integration in both quality and consistency of poultry products with lower prices. Reports show that many poultry integrators have benefited from vertical integration. Contract poultry producers have been left behind with a poverty level of existence.

Why Do Growers Sign the Contracts If They're So Bad?

A question often asked is: "If returns are really so low, why are people lined up to become contract producers?" Although no detailed studies are available, it appears that there are four major reasons why people continue to be interested in becoming contract producers. First, there are few other job opportunities in areas where poultry operations are often located. Second, many potential producers do not understand that cost and return budgets may use unrealistically long depreciation periods. In the past, some producers have been strongly discouraged by integrators from making public their contracts and financial information. And there may be deception in the information presented to potential producers by some integrators in that not all costs are shown, or costs are underestimated. Third, many potential producers may feel that they can be above average, even though the payment system prevents more than half of them from being above average. Fourth, the manner in which most integrators determine pay for individual flocks may result in declining pay as other producers adopt new, more efficient technology. Potential new producers may not recognize this and thus may not account for it in their profitability analyses.

Legislative Proposals To Address the Problems

Hopefully you are asking yourself, how can the companies do that? Because they have a contract that is written solely to benefit them. Because there are no laws that say they cannot do it, and because increasingly, their access to the courts of justice for growers are being barred by mandatory arbitration clauses in their contracts.

The companies are not going to change things unless they are made to do so, by commonsense laws governing fair standards of conducts in contracts, by adequate enforcement by USDA, and by a competitive market place that gives growers the ability and right to bargain for fair contract terms. The growers don't want anything that they are not entitled to, but they want things to be fair. And I have a few suggestions in that regard:

1) The Packers and Stockyards Act needs to be updated to give USDA's Grain Inspection, Packers and Stockyards Agency full authority, like the authority they already have in the red meat sector, to crack down on unfair and deceptive trade practices. Right now, their authority is very limited for poultry, and that means that there's no cop on the beat to make sure that poultry growers are not being abused. And even the limited authority that GIPSA has excludes any authority to provide protections for breeder hen and pullet growers. The Packers and Stockyards Act needs to be modernized to give GIPSA full authority to prevent unfair and deceptive trade practices in the poultry sector. And once they have that authority, we need to make sure that GIPSA is doing everything possible to fully enforce the law.

2) Pass legislation to specifically prohibit certain abusive contract clauses. For example, poultry growers, and some hog producers, are being forced to sign mandatory arbitration clauses. Often the company will force you to sign a new version of your old contract, but will add the arbitration clause, and threaten to stop sending you new chicks until you sign. This arbitration clause has the effect of saying that you can't seek justice in court, no matter what the company does to you. Even in the case of illegality, or breach of contact, or fraud, you can't go to court. Instead you have to go into a private arbitration system where you have no rights, and where they ask you to pay thousands of dollars up front just to start the arbitration process. Arbitration should be voluntary for both parties, not something forced on you by the company. Congress passed a law a few years ago to stop car manufacturers from using these abusive arbitration clauses on car dealers. Farmers would like the same protections that Congress has given to car dealers.

3) And what would be really best of all is if companies would be required to bargain in good faith with grower associations, instead of insisting on dealing with each grower individually. This is not a new idea. In fact in some states, like California and Michigan, the state laws have "good faith" bargaining requirements for some agricultural contracts. And it works well there. But the laws had to be there first to make this happen. We should do this at the national level too, by changing the Agricultural Fair Practices Act to require good faith bargaining in contract negotiations.

If large agribusinesses are allowed to control the terms of these take-it-leave-it contracts, and as long that Congress lets them abuse growers, companies will continue to shift the poultry model into other parts of agriculture, as we have already seen in many other commodities like hogs, tobacco, identity-preserved grains, and peanuts.

The problems of contracting and other manifestations of the lack of fair competition in agricultural markets are not confined to poultry. The problems are being seen in many other sectors of agriculture, particularly in the livestock sector. Therefore, over 200 organizations wrote to the House Agriculture Committee on January 18th of this year, in support of 8 legislative initiatives to help restore competition to agricultural markets, to the benefit of producers and consumers alike. A copy of that letter is attached to my written testimony. These legislative proposals include the ones that I have already mentioned, but also include others to address anti-competitive practices in the beef and hog sectors and elsewhere. It is my hope that this Committee will see fit to include a broad competition title in its version of the 2007 farm bill that will include provisions related to each of the 8 recommendations in the letter.

I would like to thank you for your time and willingness to listen to what's going on with today's poultry growers. The contract producer has been transferred into a mere servant of a corporation. Or, as some have said, contract producers are serfs – with a large mortgage.

January 18, 2007

The Honorable Tom Harkin
Chairman, Senate Committee on Agriculture, Forestry and Nutrition

The Honorable Saxby Chambliss
Ranking Member, Senate Committee on Agriculture, Forestry and Nutrition

The Honorable Collin Peterson
Chairman, House Committee on Agriculture

The Honorable Bob Goodlatte
Ranking Member, House Committee on Agriculture

The Honorable Patrick Leahy
Chairman, Senate Committee on the Judiciary

The Honorable Arlen Specter
Ranking Member, Senate Committee on the Judiciary

The Honorable John Conyers, Jr.
Chairman, House Committee on the Judiciary

The Honorable Lamar S. Smith
Ranking Member, House Committee on the Judiciary

Dear Chairmen and Ranking Members:

The over 200 undersigned organizations strongly urge you to make the issues of agricultural competition and market concentration a top priority as Congress considers the crafting of agricultural legislation and the next Farm Bill. During the 2002 Farm Bill debates, public testimony provided clear and compelling evidence of the need for free market competition and fairness for the nation's farmers and ranchers. Since that time these concerns have become even more urgent and prominent in the public eye.

Today, a small handful of corporations overwhelmingly dominate our food supply. The concentration of market control in the top four firms in U.S. food retailing, grain processing, red meat processing, poultry processing, milk processing, and nearly every category of food manufacturing is at an all time high. Corporate mergers and buyouts have concentrated the power of these firms and increased their ability to unfairly manipulate market conditions in their favor. This unprecedented level of horizontal market consolidation effectively eliminates free market competition to the detriment of independent family farmers and consumers.

Compounding the problem associated with horizontal consolidation is the rapid trend toward vertical integration. Manufacturers, processors, and packers increasingly control all stages of production and inventory through commodity ownership and one-sided contracts. This corporate control of production unnecessarily eliminates market transparency, creating an environment ripe for price manipulation and discrimination. It replaces farm-level decision making with centralized corporate planning and leaves farmers trapped in long-term debts tied to short-term, non-negotiable production contracts. In addition, top retailers and packers increasingly engage in relationships with dominant suppliers that exclude smaller competitors and minimize price competition. Because both supply and demand are controlled by the same few players in the market, the basic principles of supply and demand cannot function.

A critical role of government is to ensure fairness by facilitating properly operating markets and balance in the economic relationships among farmers/ranchers, consumers and food companies. Currently, inadequate federal legislation and the lack of enforcement of anti-trust policies allow a handful of corporations to continue to consolidate market power, manipulate prices, and create anti-competitive market structures. Federal government inaction has a dramatic, negative impact on not only farmers and ranchers, but also on rural communities, the environment, food quality, food safety, and consumer prices. It undermines sustainable production practices and state and local laws that support family-scale, sustainable farm and ranch operations.

Policy makers often voice the laudable policy goals of maintaining a diverse, farm-and-ranch-based production sector and providing consumers with a nutritious, affordable food supply. However, government failure to redress industry concentration--both vertical and horizontal--is thwarting these policy goals and driving the earnings of farmers and ranchers down and consumer prices up.

To address these problems, we urge you to champion a strong, comprehensive Competition Title in the 2007 Farm Bill. We also ask that you co-sponsor and support any of the following measures of this comprehensive package if they are introduced as separate or combined bills and to work for speedy congressional consideration of these proposals.

• LIMIT PACKER CONTROL/MANIPULATION OF LIVESTOCK MARKETS

1. ***Captive Supply Reform Act:*** This legislation will bring secret, long-term contracts between packers and producers into the open and create a market for these contracts. The Captive Supply Reform Act would restore competition by making packers (and livestock producers) bid against each other to win contracts. Currently, formula contracts and marketing agreements are negotiated in secret, where packers have all the information and power. These formula contracts and agreements depress prices and shut small and independent producers out of markets. The Captive Supply Reform Act would require such contracts to be traded in open, public markets to which all buyers and sellers have access.

2. ***Prohibition on Packer-Owned Livestock***: Meat packers such as Tyson, Cargill, and Smithfield Foods use packer-owned livestock as a major tool for exerting unfair market power over farmers and ranchers. This practice fosters industrial livestock production and freezes independent farmers out of the markets. Packer-owned livestock has been proven to artificially lower farm gate prices to farmers and ranchers while consumer food prices continue to rise. By prohibiting direct ownership of livestock by major meatpackers, a packer ban addresses a significant percentage of the problem of captive supply which packers use to manipulate markets, and would help increase market access for America's independent producers who currently experience great restrictions in market access due in part to packer ownership of livestock.

• INCREASE FAIRNESS IN AGRICULTURAL CONTRACTS AND MARKETS

3. Fairness Standards for Agricultural Contracts: In order to address the worst abuses contained in processor-drafted contracts, legislation that provides a set of minimum standards for contract fairness is urgently needed. Such standards should include at a minimum the following:

(a) prohibition of the use of forced, mandatory arbitration clauses, which have been used by some packers or integrators to force growers to give up their access to the courts, even in the case of fraud, breach of contract, misrepresentation or other blatant contract abuses by the integrator or packer firm;
(b) clear disclosure of producer risks;
(c) full prohibition on confidentiality clauses;
(d) recapture of capital investment so that contracts that require a significant capital investment by the producer cannot be capriciously canceled without compensation; and
(e) a ban on unfair or deceptive trade practices, including "tournament" or "ranking system" payment.

4. Clarification of "Undue Preferences" in the Packers & Stockyards Act (PSA): Packers commonly make unjustified, preferential deals that provide unfair economic advantages to large-scale agriculture production over smaller family owned and sustainable farms. Courts have found current undue preference legal standards virtually impossible to enforce. Additional legislative language is needed in the PSA to strengthen the law and clarify that preferential pricing structures (those that provide different prices to different producers) are justified only for real differences in product value or actual and quantifiable differences in acquisition and transaction costs. Specifically, we are asking to:

(a) Make clear that farmers damaged by packer/processor unfair and deceptive practices need not prove "harm to competition" to receive a remedy.
(b) Make clear that "pro-competitive effects" or "legitimate business justifications" are not recognized packer defendant defenses, and not necessary for farmer-plaintiffs to prove the absence of, in a court case under the PSA.
(c) Require courts to award attorneys fees to successful producer plaintiffs under the PSA.

5. Closing Poultry Loopholes in the Packers & Stockyards Act (PSA): USDA does not currently have the authority under the PSA to bring enforcement actions against poultry dealers. Poultry producers should have the same basic enforcement protection that is offered to livestock producers when packers and livestock dealers violate the PSA. We seek legislation to clarify that USDA has authority over PSA violations involving poultry dealers in their relations with all poultry growers, including those who raise pullets or breeder hens as well as broiler producers. The PSA enforcement loophole for poultry dealers should be closed.

6. Bargaining Rights for Farmers: Loopholes should be closed in the Agricultural Fair Practices Act of 1967 (AFPA) and processors should be required to bargain in good faith with producer organizations. The AFPA was enacted to ensure that livestock and poultry producers could join associations and market their products collectively without fear of retribution by processors. These goals have not been attained due to loopholes in that Act. Retaliation by processors is commonplace in some sectors. Legislation should be enacted that promotes bargaining rights and prevents processor retaliation.

• ASSURE ADEQUATE MARKET INFORMATION AND TRANSPARENCY FOR PRODUCERS AND CONSUMERS

7. Livestock Mandatory Price Reporting: The Livestock Mandatory Price Reporting Act of 1999 (LMPRA) requires packers, processors, and importers to provide price, contracting, supply and demand information to USDA, which then uses the information to create price reports for livestock producers. Since its implementation, bureaucratic inertia has blocked effective enforcement of the LMPRA and prevented the Act from operating to benefit independent livestock producers. The Government Accountability Office, at the request of Senators Harkin (D-IA) and Grassley (R-IA), has reviewed USDA implementation of the Act. In December 2005, the GAO issued a report documenting lengthy lag times for USDA corrections to missing or incorrect information from packers, and the failure of USDA to inform the public about violations of the Act revealed in USDA audits. The LMPRA was reauthorized in September 2006 without including GAO recommendations to improve the Act. If USDA does not implement these recommendations, Congress should amend the Livestock Mandatory Price Reporting Act in 2007 by incorporating the GAO report recommendations as legislative directives to USDA in implementing the Act.

8. Mandatory Country of Origin Labeling: Country of origin labeling (COOL) for beef, lamb, fresh fruits, fish and shellfish was passed as a provision of the 2002 Farm Bill. Mandatory COOL for the fish and shellfish commodities was implemented by USDA in April of 2005, but COOL implementation for all other commodities has been successfully stymied by the meatpackers and retailers. Country of origin labeling is a popular measure that allows consumers to determine where their food is produced and also enables U.S. producers to showcase their products for quality and safety. It also limits the ability of global food companies to source farm products from other countries and pass them off as U.S. in origin. Congress should reauthorize COOL to reiterate its benefits to producers and consumers and should provide funding to ensure that USDA undertakes immediate implementation of COOL.

In conclusion, farmers, ranchers, and consumers across the country are asking for these legislative reforms to ensure fair markets and a competitive share for family farmers and ranchers of the $900 billion dollars that consumers pay into the food and agriculture economy annually. Market reforms remain a key ingredient for rural revitalization and meaningful consumer choice. The legislative reforms summarized above are key to achieving the goals of promoting an economically healthy and diverse agricultural production sector and providing consumers with healthy, affordable food.

Thank you.

Sincerely,

A Little Taste of Everything
A Taste of the North Fork (NY)
Adams County Farmers Union (ND)
Agricultural Missions, Inc. (NY)
Agriculture and Land Based Training Association (CA)
Agriculture of the Middle
Alabama Contract Poultry Growers Association
Alabama Sustainable Agriculture Network
Alliance for a Sustainable Future (PA)
Alliance for Sustainable Communities (MD)
Alternative Energy Resources Organization (AERO) -MT
American Corn Growers Association
American Society of Agronomy
Appalachian Crafts (KY)
Art & Nature Project (NY)
Beartooth Stock Association (MT)
Berkshire Co-op Market
Bird Conservation Network
Blessed Kateri Tekakwitha Region, Secular Franciscan Order, NYS
Bronx Greens
California Dairy Campaign
California Farmers Union
California Institute for Rural Studies
Californians for GE-Free Agriculture
Campaign for Contract Agriculture Reform
Campaign for Family Farms and the Environment
Caney Fork Headwaters Association (TN)
Catholic Charities Diocese of Sioux City, IA
Catholic Charities of Chemung /Schuyler Counties (NY)
Catholic Charities of Kansas City - St. Joseph, Inc.
Catholic Charities of Louisville, Parish Social Ministry Dept. (KY)
Catholic Rural Life, Archdiocese of Dubuque, IA
Cattle Producers of Washington
Center for Food Safety
Center for Earth Spirituality and Rural Ministry (MN)
Center for Popular Research, Education and Policy (NY)
Center for Rural Affairs
Central Colorado Cattlemen's Association
Chemung County Church Women United (NY)
Chemung County Council of Churches (NY)
Church Women United of NYS
CitySeed (CT)
Community Action Resource Enterprises (OR)
Community Food Security Coalition
Concerned Citizens of Central Ohio
The Cornucopia Institute (WI)
Corson County Farmers Union (SD)
Court St Joseph #139, Catholic Daughters of the Americas, Corning (NY)
Court St Joseph #139, Corning/Elmira, Catholic Daughters of the Americas (NY)
Crop Science Society of America
Crowley-Kiowa-Lincoln Cattlemen's Association (CO)
Cumberland Counties for Peace & Justice (TN)
Dakota Resource Council
Dakota Rural Action of SD
Delmarva Poultry Justice Alliance
Delta Land and Community, Inc.
Eagle County Cattlemen's Association (CO)
Endangered Habitats League (CA)
Environmental Action Committee of West Marin (CA)
Environmental Coalition of Mississippi
Family Farm Defenders
Family Farms for the Future (MO)
Farm Aid
Farm Fresh Rhode Island
FH King Students of Sustainable Agriculture at UW Madison
First Nations Development Institute
Florida Organic Growers
Food Alliance (OR)
Food and Water Watch
Food Routes Network
Foodshed Alliance of the Ridge and Valley (NJ)
Friends of Rural Alabama
Georgia Organics
Georgia Poultry Justice Alliance
Global Exchange
Government Accountability Project
GRACE/Sustainable Table
Grassroots International
Hahn Natural Foods (PA)

Harding County Stockgrowers Association (SD)
Harvest Co-op Market (MA)
Heartland Center / Office of Peace and Justice for the Diocese of Gary, Indiana
Hispanic Farmers and Ranchers of America Inc.
Hispanic Organizations Leadership Alliance
Horseheads Grange #1118, Chemung City (NY)
Humane Society of the United States
Idaho Rural Council
Illinois Farmers Union
Illinois Stewardship Alliance
Independent Beef Association of North Dakota
Independent Cattlemen of Iowa
Independent Cattlemen of Nebraska
Independent Cattlemen's Association of Texas, Inc.
Indiana Campaign for Economic Justice
Indiana Farmers Union
Institute for Agriculture & Trade Policy
Institute for Responsible Technology
Iowa Citizens for Community Improvement
Iowa Farmers Union
Just Food (NY)
Just Harvest, Pittsburgh
Kansas Cattlemen's Association
Kansas City Food Circle
Kansas Farmers Union
Kansas Rural Center
Kerr Center for Sustainable Ag (OK)
Kit Carson County Cattlemen's Association (CO)
La C.A.S.A. de Llano (TX)
Ladies of Charity of Chemung County (NY)
Land Stewardship Project (MN)
Little Seed CSA (NY)
Madera County Cattlemen's Assoc (CA)
McKenzie City Energies & Taxation Association (ND)
Merced-Mariposa Cattlemen's Association, (CA)
Mesa County Cattlemen's Association (CO)
Michigan Farmers Union
Midwest Organic and Sustainable Education Service
Minnesota Farmers Union
The Minnesota Project
Mississippi Contract Poultry Growers Association
Mississippi Livestock Markets Association
Missouri Farmers Union
Missouri Rural Crisis Center
Montana Cattlemen's Association
Montana Farmers Union
National Campaign for Sustainable Agriculture
National Catholic Rural Life Conference
National Center for Appropriate Technology (NCAT)
National Family Farm Coalition
National Farmers Organization
National Farmers Union
National Hmong American Farmers, Inc.
National Latino Farmers & Ranchers Trade Association
National Organic Coalition
National Poultry Justice Alliance
Nebraska Farmers Union
Network for Environmental & Economic Responsibility
Nevada Live Stock Association
New England Small Farm Institute (NESFI)
New York Beef Producers Association Southern Tier Region
NY Sustainable Agriculture Working Group
Nojoqui Ranch Produce (CA)
North Carolina Contract Poultry Growers Association
North Dakota Farmers Union
Northeast Organic Dairy Producers Alliance
Northeast Organic Farming Assoc -MA
Northeast Organic Farming Assoc -NY
Northeast Organic Farming Assoc-CT
Northeast Organic Farming Assoc-VT
Northern Plains Sustainable Agriculture Society
Northern Plains Resource Coun (MT)
NYS Safe Food Coalition
Ohio Environmental Council
Ohio Farmers Union
Oregon Livestock Producer Association
Oregon Tilth
Organic Consumers Association
Organic Seed Alliance (WA)
Organization for Competitive Markets

The Partnership for Earth Spirituality (NM)
Past Regents Club, Diocese of Rochester (NY)
PCC Natural Markets (WA)
PCC Farmland Trust (WA)
Pennsylvania Association for Sustainable Agriculture
Pennsylvania Farmers Union
Perkins County Farmers Union (South Dakota)
Platte County Farm Bureau (NE)
Powder River Basin Resource Council (WY)
Producers Livestock
Provender Alliance (OR)
Putting Down Roots (PA)
Rainbow Natural Grocery (MS)
R-CALF United Stockgrowers of America
Red Tomato (MA)
Regional Farm and Food Project (NY)
Rochester Farm Connection (NY)
Rochester Roots (NY)
Rocky Mountain Farmers Union
Rural Advancement Foundation International-USA (RAFI-USA)
Rural Coalition/Coalición Rural
Rural Life Committee of the North Dakota Conference of Churches
Selene Whole Foods Co-op (PA)
Sevananda Natural Foods Market
Sierra Club Agriculture Committee
Social Concerns Office, Diocese of Jefferson City
Social Concerns/Rural Life Department, Catholic Charities, Diocese of Sioux City, IA
Soil Association
Soil Science Society of America
South Dakota District IV Farmers Union
South Dakota Farmers Union
South Dakota Stockgrowers Association
Southern Colorado Livestock Association
Southern Research & Development Corp. (LA)
Southern Sustainable Ag Working Group
Spokane County Cattlemen's Association (WA)
St John the Baptist Fraternity, Secular Franciscan Order, Elmira NY
Stevens County Cattlemen's Association (WA)
Sustainable Agriculture Coalition
Temple Beth El of Flint, Michigan
Texas Mexico Border Coalition Community Based Organization
Tilth Producers of Washington
United Hmong Association
The Urban Nutrition Initiative (PA)
Utah Farmers Union
Valley Stewardship Network (WI)
Virginia Association for Biological Farming
Washington Cattlemen's Association
Washington County Stockmen's Assoc (CO)
WA Sustainable Food & Farming Network
West Carroll Cattleman Assoc. (LA)
Western Organizations of Resource Councils
Wisconsin Farmers Union

FOR FURTHER INFORMATION, CONTACT:

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A COPY OF THIS SIGN-ON LETTER AND BACKGROUND INFORMATION ON THE 2007 FARM BILL'S COMPETITION AND CONCENTRATION ISSUES ARE POSTED ON THE NATIONAL CAMPAIGN FOR SUSTAINABLE AGRICULTURE'S WEBSITE AT:
http://sustainableagriculture.net/CompConc2007.php.

Statement of John Crabtree

Center for Rural Affairs
Lyons, Nebraska

House Agriculture Committee
Subcommittee on Livestock, Dairy and Poultry
April 17, 2007

Currently, a handful of corporations dominate the American food system. The concentration of market control in the top four firms in U.S. food retailing, grain progressing, red meat processing, poultry processing, milk processing and nearly every category of food processing has reached unprecedented levels.

Moreover, the rapid trend toward vertical integration, especially in hog production, further exacerbates the horizontal concentration in packing, processing and production. As the livestock sector has become increasingly concentrated and integrated, packers and processors increasingly control production at all stages.

In many rural places where livestock are raised there are only a few, or even just one, packer or processor for a given livestock species. This is especially true in the livestock and poultry sectors. At the same time there has been a dramatic increase in the use of production and marketing contracts that further diminish the bargaining power of farmers and ranchers. Currently, fully 89% of hogs are either owned outright by packers or tightly controlled through various contracting devices. Many farmers and ranchers face price discrimination and severely limited market access as a result.

USDA has demonstrated a nearly complete inability to enforce the Packers and Stockyards Act and other livestock market competition laws. The audit of the Packers and Stockyards Administration performed by USDA's Office of Inspector General that was released in February 2006 revealed that the Packers and Stockyards Administration has utterly failed to enforce the very law that gives the agency a reason to exist.

The Packers and Stockyards Administration has become anything but an enforcer of competition in livestock markets – robbing farmers and ranchers of the best assurance they have that livestock markets will be fair, open and competitive.

Senior officials in the Packers and Stockyards Administration blocked investigations from being referred to USDA lawyers or the Justice Department. Agency employees were instructed to create the appearance of enforcement activity by recording everything from routine correspondence and review of public data as "investigations."

Over 1,800 so-called investigations were documented between 1999 and 2005. According to the Inspector General's audit, 1,739 of those so-called investigations could not be traced to a specific complaint, producer, packer, or to other details that a true investigation would contain.

The Packers and Stockyards Administration perpetrated a lie and disillusioned farmers and ranchers in the process. It is wrong for government to turn a blind eye to citizens' concerns. It is worse when government tells citizens that their concerns are valid and, through pretense and deception, leads them to believe that their concerns are being addressed when they are not.

USDA has proven, again, that they lack the wherewithal, courage and political will to effectively enforce the Packers and Stockyards Act. And they certainly cannot be trusted to use the considerable authority vested in the Packers and Stockyards Act more expansively and, thereby, breathe life back into American livestock markets.

Repeated calls for competition reforms from farmers and ranchers as well as the National Commission on Small Farms, General Accounting Office, and Inspector General have fallen on deaf ears at USDA.

That is why Congress must act to define the rules of livestock market competition and provide clear direction for USDA's enforcement. Congress should not let another farm bill go by without making changes in the Packers and Stockyards Act and Agricultural Fair Practices Act that are necessary to breathe some life and competition back into livestock markets.

The Packers and Stockyards Act should be amended to:

- prohibit packer ownership of livestock more than seven days prior to slaughter;
- prohibit use of production contracts that do not fix base prices, with adjustments for quality, grade or other factors outside of packer control, at the point of sale;
- require the Secretary to write regulations defining the statutory term "unreasonable preference or advantage" to ensure that small and mid-sized farmers and ranchers are not forced to accept volume based price discrimination;
- establish that producers need not prove anti-competitive injury to an entire market in cases involving unfair or deceptive trade practices which have harmed them individually;
- provide USDA administrative authority to investigate and file complaints against violations of the Act regarding all types of poultry transactions.

The Agricultural Fair Practices Act should be amended to:

- make in unlawful for any firm to refuse to deal with a producer for belonging to or attempting to organize an association of producers or a cooperative;
- prohibit the use of binding mandatory arbitration clauses and restrictions on other legal rights available to farmers and ranchers involved in production and marketing contract disputes;
- expand the prohibition on confidentiality clauses to cover all agricultural marketing and production contracts, not just those for livestock and poultry, and to ensure that farmers and ranchers can share information about the details and terms of contracts with other farmers and producer associations;

- require that contracts include clear disclosure of producer risks. In addition, prohibit premature cancellation of contracts without a showing of good cause and providing for the recapture of producer capital investment, and ban unfair trade practices including "tournament" or "ranking" system payments that are calculated by the packer or processor and result in unpredictable and arbitrary payments.

Limiting Packer Control and Manipulation of Livestock Markets

1. *Captive Supply Reform Act:* This legislation would bring secret, long-term contracts between packers and producers into the open and create a market for these contracts. The Captive Supply Reform Act would restore competition by making packers (and livestock producers) bid against each other to win contracts. Currently, formula contracts and marketing agreements are negotiated in secret, where packers have all the information and power. These formula contracts and agreements depress prices and shut small and independent producers out of markets. The Captive Supply Reform Act would require such contracts to be traded in open, public markets to which all buyers and sellers have access. And it would require that forward contracts establish a fixed base price at the time the contract is executed.

2. *Prohibition on Packer-Owned Livestock:* Meat packers such as Smithfield, Cargill and Tyson use packer-owned livestock as a major tool for exerting unfair market power over farmers and ranchers. This practice fosters concentrated industrial livestock production, and the environmental nightmares that goes along with it. Packer-owned livestock artificially lowers farm gate prices to farmers and ranchers while consumer food prices continue to rise – as demonstrated repeatedly by USDA, land grant and non-profit research and analysis, most recently the GIPSA Livestock and Meat Marketing (RTI) Study released in January 2007. Despite a clear vertical integration and packer bias among the researchers that conducted that report, the conclusion that, "...the use of [captive supplies] is associated with lower cash market prices..."

Packers and processors claim that vertical integration increases efficiency. That is a lie. Small and mid-sized farms and ranches have demonstrated, time and again, that they can match or beat the cost of production in the packers' industrial facilities.

Packers use vertical integration and captive supplies to manipulate livestock markets, depressing cattle and hog prices across the board by killing their own when prices are high and turning to independent producers as residual suppliers when prices are low – to the detriment of farmers, ranchers and rural communities.

Prohibiting packer ownership of livestock dramatically reduces the ability of packers to manipulate livestock markets and helps secure increased market access for small and mid-sized family farms and ranches – access that is often severely limited today by the levels of vertical integration, particularly in hog production.

3. *Clarification of 'Undue Preferences' in the Packers & Stockyards Act:* Packers commonly make unjustified, preferential deals that provide unfair economic advantages to large volume livestock production over small and mid-sized family farms and ranches. Courts have been unwilling to enforce current undue preference standards. Additional legislative language is needed in the Packers and Stockyards to strengthen the law and clarify that preferential pricing structures (those that provide different prices to different producers) are justified only for real differences in product value or actual and quantifiable differences in acquisition and transaction costs. Specifically, we are asking to:
   (a) Make clear that farmers damaged by packers unfair and deceptive practices need not prove "harm to competition" throughout an entire economic sector to receive a remedy for harm done to them individually.
   (b) Make clear that "pro-competitive effects" or "legitimate business justifications" are not recognized packer defendant defenses, and not necessary for farmer-plaintiffs to prove the absence of, in a court case under the Act.

In the end, it comes down to this. In a nation where packers and processors own and control all of the livestock, what need is there of farmers and ranchers? And what hope have we for revitalizing family farming, ranching and rural communities, if we have no hope of revitalizing family farm and ranch livestock production? What hope, if we cannot breath life and competition back into our livestock markets?

My father always told me, "Say what you mean, and mean what you say." If we hope to create a farm bill that can be held up as a solution to some of the challenges that family farmers, ranchers and rural communities face, then we should all support a federal ban on packer ownership of livestock and a comprehensive competition title in the farm bill… in other words, we should mean what we say.

National Farmers Union

Testimony of Tom Buis

Before the
U.S. House of Representatives Agriculture Subcommittee
on Livestock, Dairy and Poultry

Concerning the
Market Structure of the Livestock Industry

Tuesday, April 17, 2007
Washington, D.C.

STATEMENT OF TOM BUIS

PRESIDENT, NATIONAL FARMERS UNION

BEFORE THE U.S. HOUSE AGRICULTURE SUBCOMMITTEE ON LIVESTOCK, DAIRY AND POULTRY

MARKET STRUCTURE OF LIVESTOCK INDUSTRY

APRIL 17, 2007

Chairman Boswell and members of the subcommittee, my name is Tom Buis, and I am president of the National Farmers Union-- a nationwide organization representing more than 250,000 farm, ranch and rural residents. I am pleased to be here today to discuss the market structure of the livestock industry. I will submit my full testimony for the record and would like to focus in my oral testimony on a summary of issues NFU believe should be included in a comprehensive competition title in the next farm bill.

NFU is releasing an updated commissioned study conducted by Drs. Mary Hendrickson and William Heffernan from the University of Missouri - Department of Rural Sociology, which reveals the top four firms in most agricultural sectors have continued to increase their stronghold since our last study in 2005.

The study shows the top four beef packers dominate 83.5 percent of the market, four pork packers control 66 percent of that market, and the top four poultry companies process 58.5 percent of the broilers in the United States. Tyson Foods is listed in the top two of the pork and broiler markets and number one in the beef packing market.

Ethanol production is the only agricultural sector in which concentration has steadily decreased. A decade ago, the top four companies owned 73 percent of the ethanol market. Today, the top four companies control 31.5 percent of the ethanol produced. The increase in ethanol production competition is in direct relationship to the high number of farmer-owned ethanol cooperatives built across the country. Farmer-owned ethanol plants account for 39 percent of total capacity. This is a clear example of the impact and potential for public policies that encourage diversification and discourage monopolization in our food system.

NFU has helped provide financial support to track agricultural concentration data since 1999, yet Dr. Heffernan has been tracking concentration data since 1987; we have witnessed the concentration levels rise in nearly every sector with each report. The concentrated power of these firms increases their ability to manipulate markets, effectively eliminating free market competition to the detriment of family farmers and consumers. I have included the updated tables in my testimony but wanted to bring to the subcommittee's attention the difficulty our researchers had in obtaining the data. Congress should direct the Departments of Agriculture and Justice to collect and publish concentration information. Corporations currently consider the data proprietary, and the public has limited, if any, access to the data.

The information contained in this new research is further reason for Congress to immediately pass legislation to restore true competition in the marketplace for U.S. farmers and ranchers. Independent producers cannot be successful in the absence of protection from unfair and anti-competitive practices. I have attached the updated tables to my testimony for the record.

In order to restore balance in the marketplace, NFU believes a comprehensive competition title is needed to untie the hands of family farmers and ranchers across the country. Congress must intervene and accept responsibility for our dysfunctional livestock markets by including a comprehensive, top-to-bottom remedy to end non-competitive practices in the 2007 farm bill. Further study and "tweaks" here or there are insufficient. A non-competitive marketplace is code for farmers and ranchers being robbed; without price discovery, producers are almost always paid less for their products than the true and fair value of those commodities. National Farmers Union has been steadfast in its belief of the traditional agricultural system which is grounded by independent family producers. Many cite the free market as a basis for not taking action, yet I ask: how can you have a free market when there is no competition? How can one rely upon a free market without recognizing when it needs fixing?

Competition Title

A comprehensive competition title should include the requirement that USDA and all federal agencies enforce current antitrust laws. In January 2006, a report revealed USDA's Grain Inspection, Packers and Stockyards Administration (GIPSA) failed to enforce laws created to combat increased consolidation and anti-competitive practices. The audit report revealed GIPSA has no policy to define investigations and therefore considers everyday tasks as "investigations." The agency does not maintain accurate records in a tracking system and never implemented previous recommendations from the Office of Inspector General (OIG) or the Government Accountability Office (GAO). The Packers and Stockyards Act of 1921 was passed to address the unfair and deceptive trade practices of meat packers, but if the Act is not enforced, it is pointless.

It is GIPSA's responsibility to maintain fair trade practices in the marketing of livestock; provide financial protection for participants in livestock transactions and ensure open competitive marketing conditions for livestock and meat. It appears farmers and ranchers have been fighting anti-competitive practices with one hand tied behind their backs. The report generates serious concern regarding the lack of action by GIPSA to enforce antitrust laws. Farmers and ranchers have seen and felt the negative impacts of increased consolidation and anti-competitive practices. The lack of action by GIPSA to combat anti-competitive practices is a disappointment for family farmers and ranchers across the country.

In 2002, the Senate approved a ban on packer ownership. Unfortunately, the provision was not approved as part of the final 2002 Farm Bill. Banning packer ownership of livestock is needed to ensure independent producers have a place in the future of livestock production. This is not setting precedence; instead, it is consistent with legislative action taken more than 85 years ago when Congress adopted the Packers and Stockyards Act to stop anti-competitive meat packer practices. Meat packers do not need to own livestock to improve meat quality or keep prices affordable, nor will banning packer ownership of livestock lead to market collapse.

With the recent decisions of the 8th U.S. Circuit Court of Appeals to declare state corporate farming bans unconstitutional, such as the Iowa ban on packer feeding and I-300 in Nebraska, it is increasingly important for this Congress to re-think its role in antitrust enforcement. A ban on packer feeding is that step in the right direction of increasing producer prices and restoring competition to a non-competitive market.

Captive supply reform is another step in the direction of restoring competition by requiring packers to bid against each other to win contracts. Instead of using its own captive supply of livestock to circumvent an open and transparent livestock market, contracts and agreements between packers and producers would be based upon fixed base prices. Today, packers directly own cattle and procure cattle through contracts. These two types of captive supply allow packers to fill daily slaughter needs without having to bid for cattle on the spot market. Captive supply reform does not eliminate the ability for cattle to be contracted for future delivery; instead, it would simply require all livestock marketing contracts to be traded in an open, transparent and public process, with all buyers and sellers having access to the same information.

Congress took action in 1999 to inject transparency in livestock markets by passing the Livestock Mandatory Price Reporting Act, which requires packers, processors and importers to provide price, contracting, supply/demand information to USDA. The department then uses the collected information to create price reports for producers. Since its implementation, the weight of bureaucracy has prohibited any true enforcement of the program from being realized, and the program has not been working as intended for the benefit of independent livestock producers.

Stronger oversight and review of the program is necessary to reach the original goal and congressional intent of the program. In a report released in December 2005, the GAO found that USDA regularly excluded transactions in its reports. From April through June 2005, USDA reports excluded nine percent of cattle transactions that packers had reported. GAO reviewed 844 USDA audits and found packers to have incorrectly reported or completely failed to report required information nearly 64 percent of the time. In order to achieve true market transparency for America's livestock producers, a competition title of the farm bill should address outstanding producer concerns and incorporate the recommended legislative fixes from GAO to the price reporting program.

In addition to injecting transparency and fairness into livestock markets, new marketing opportunities are required to ensure a strong and vibrant industry into the future. An end to the ban on interstate shipment of meat is needed to create such an opportunity. Many family farmers and ranchers have been forced out of business due to inadequate market competition. Ending the ban will increase competition and economic, marketing and trade opportunities for rural America.

Current law allows some meat products such as venison, pheasant and quail to be shipped between states without restriction. Foreign meat and poultry also do not face restrictions in interstate trading, while domestic meat is blocked. Removing the ban on interstate sales of meat and poultry will level the economic playing field for small business, promote competition in the marketplace and create a more uniform inspection system. Legislation has been introduced to achieve these goals and is supported by USDA advisory committees because of the multiple benefits.

In keeping with marketing opportunities, I must note that the current generation of commodity checkoff programs has lost the support and trust among a significant percentage of producers who pay for it. NFU believes mandatory checkoff programs should be legislatively reformed to become a truly voluntary program that earns the support and trust of the producers who financially support the program.

The May 2005 U.S. Supreme Court decision was surprising because the court ruled the mandatory beef checkoff program is a U.S. government program and the Constitution's First Amendment free-speech rights of producers funding the program do not apply. This contradicts mandatory checkoff proponents' arguments that the program is run and controlled by the producers. The disappointing aspect of the Supreme Court ruling was that it did nothing to address the problems or controversies surrounding mandatory producer funded checkoff programs. Issues such as accountability to producers who fund the programs and access to open and fair referendums remain unresolved. NFU supports a voluntary checkoff program, with producer participation determined at the point of sale. Any U.S. promotion program funded by producers of the commodities should be for the sole purpose of promoting U.S. products.

Earlier this year, Senator Tom Harkin introduced the Competitive and Fair Agricultural Markets Act of 2007, which NFU has endorsed. This legislation can and should serve as a basis for establishing a comprehensive competition title in the 2007 farm bill. Harkin's legislation establishes an Office of Special Counsel within USDA, which NFU has long advocated for in order to investigate and prosecute violations on competition issues. The position could streamline and increase the effectiveness of USDA to investigate and take action on antitrust law violations. Harkin's legislation puts power in the hands of producers by making it easier to prove unfair and anti-competitive actions by packers and processors via the judicial process. USDA would also be given authority to enforce the Packers and Stockyards Act relative to poultry sales; current law prohibits the department from prosecuting violations discovered in the poultry industry.

Senator Harkin's legislation goes on to enhance contract producer protections, including the right for a producer to review a contract for three days; prohibits confidentiality clauses. It prevents mandatory arbitration and protects producers from contracts arbitrarily terminated. Finally, Harkin's competition legislation prohibits unfair, anti-competitive or deceptive practices by anyone that would impact the marketing, receiving, purchasing, sale or contracting of commodities. Producers would also be protected from discrimination based upon their membership in a certain organization or cooperative.

NFU has been very frustrated and disappointed in USDA's mishandling of implementing a National Animal Identification System (NAIS). The department has spent nearly $100 million of federal dollars to register 25 percent of livestock premises across the country. In the meantime, the department has taken every position possible, from mandatory versus voluntary, public database versus private, protecting producer confidentiality versus not running cost estimates, and the list goes on. When discussions of establishing a national identification system started, many producers were open to the concept, in the interest of animal health, consumer health and beef/cattle trade issues. USDA's actions since 2004 have done nothing but erode producer confidence, by choosing to ignore the overwhelming number of questions and concerns of producers.

The development and control of a NAIS is a big concern to our members, who fear they will be held financially responsible and legally liable for a system that may or may not achieve the goals of a 48-hour trace-back capability. The current state of the NAIS could best be described as a mandatory-voluntary system, which results in nothing more than an unfunded mandate for livestock producers. U.S. producers have no assurance that their foreign competitors will have the additional burden and expense of complying with an animal identification system in their own country. We live in a competitive, global market where price determines market share. American producers are required to comply with strict labor, environmental and other production regulations, which drive up the cost of producing their commodities. Too often, our global competitors do not have to adhere to similar standards; a NAIS could simply be another example of increased production cost for U.S. livestock producers, with a potential loss of market share and no economic benefit.

National Farmers Union policy calls for a national animal identification system that:

- Is funded and controlled by the federal government;
- Mitigates producer liability;
- Limits producer information accessibility;
- Is coupled with the mandatory country-of-origin labeling law; and
- Is only accessed during times of animal disease or bioterrorism outbreaks.

Finally, Chairman Boswell, you well know that mandatory COOL was passed five years ago as part of the 2002 Farm Bill, but has been delayed by riders in must-pass appropriations bills. COOL was implemented on wild-caught and farm-raised seafood products in April of 2005 and is working.

Opponents of COOL say consumers do not care and do not want the information, yet every consumer survey demonstrates just the opposite. Last month, Food and Water Watch released its latest consumer poll which found 82 percent of consumers support mandatory COOL. Consumers not only want to know which country their food comes from but are willing to pay more for U.S. products. On February 28, one of the largest coalitions sent a letter to Congress urging an end to the prohibition on implementation funds for USDA. The letter, which is below, urged Congress to direct USDA to immediately prepare a common-sense rule for implementation of mandatory COOL on meat, produce and peanuts.

February 28, 2007

The Honorable Nancy Pelosi
Speaker
U.S. House of Representatives
235 Cannon House Office Building
Washington, D.C. 20515

The Honorable John Boehner
Minority Leader
U.S. House of Representatives
1011 Longworth House Office Building
Washington, D.C. 20515

The Honorable Collin Peterson
Chairman
U.S. House Agriculture Committee
2159 Rayburn House Office Building
Washington, D.C. 20515

The Honorable Robert Goodlatte
Ranking Member
U.S. House Agriculture Committee
2240 Rayburn House Office Building
Washington, D.C. 20515

Dear Speaker Pelosi, Minority Leader Boehner, Chairman Peterson and Ranking Member Goodlatte:

On behalf of millions of consumers and producers, we write to urge you to change the date of implementing mandatory country-of-origin labeling (COOL) for beef, pork, lamb, produce and peanuts to September 2007. The Farm Security and Rural Investment Act of 2002 included a provision requiring retailers to notify consumers of the country-of-origin of beef, pork, lamb, produce, peanuts and seafood. We represent millions of Americans that continue to stand united in support of this valuable program. Our coalition has grown impatient with the implementation delays in previous Congresses, which restricted USDA funds to implement this very popular provision. Your leadership is needed to ensure the intent of Congress and the will of the American people are met.

As the delayed implementation date of September 2008 nears, opponents of mandatory COOL are trying to convince Congress that a change in statute is needed in order to reduce the expense and burden of the program. We do not support changing a statute that has not been given a chance to prove itself. USDA implemented mandatory COOL on farm-raised and wild-caught seafood effective April 4, 2005 with the existing statute; the experience gained from seafood implementation should be utilized by USDA to write a final rule on the remaining covered commodities that is not burdensome or expensive and meets the goal and intent of Congress.

Consumer surveys repeatedly demonstrate overwhelming support for mandatory COOL. A poll conducted in June 2005 by Public Citizen found 85 percent of respondents wanted COOL; 74 percent supported Congress making labeling a mandatory program; and 55 percent had "little or not much trust" in the meat, seafood, produce and grocery industries to voluntarily provide country-of-origin information. In January 2004, National Farmers Union commissioned a national poll of likely voters on the issue of mandatory COOL. That survey found 82 percent of respondents believed food should be labeled with country-of-origin information; 85 percent stated they would be more inclined to buy food produced in the United States; and 81 percent said they would be willing to pay a few cents more for food products grown and/or raised in the U.S. and identified as such.

Many of the myths surrounding mandatory COOL have begun to resurface, despite being unsubstantiated for years. Consumers and producers have grown impatient with the backdoor delays and the rhetoric of packers, processors and retailers that flies in the face of common-sense. The time has come for Congress to end the prohibition on implementation funds for USDA and require the department to immediately prepare a common-sense rule for implementation of mandatory COOL; the regulation does not need to be burdensome or expensive.

Enclosed are three recent editorials that have been printed in support of repealing the implementation delay and moving forward with mandatory COOL as directed in the 2002 Farm Bill.

American consumers and producers have time and again expressed their strong support for this program. Given a choice, we believe consumers across the country will choose to purchase U.S. products; without mandatory COOL, consumers continue to be denied the ability to differentiate between U.S. and imported food products.

Thank you for your attention to this most important issue.

Sincerely,

Agriculture and Health Alive LLC (ME)
Alabama Contract Poultry Growers Association
Alaska Farmers Union
Alaska Marine Conservation Council
Alliance for a Sustainable Future (PA, NJ)
Ambler Environmental Advisory Council (PA)
American Agriculture Movement of South Dakota
American Agriculture Movement of Texas County (OK)
American Corn Growers Association
American Grassfed Association
Appalachian Crafts (KY)
Arkansas Farmers Union
Boulder County Community Gleaning Project (CO)
Buckeye Quality Beef Association (OH)
Calaveras County Cattlemen's Association (CA)
California Dairy Campaign
California Farmers Union
California Institute for Rural Studies
California National Farmers Organization
Campaign for Family Farms and the Environment (IA)
Caney Fork Headwaters Association (TN)
Cape Cod Commercial Hook Fishermen's Association (MA)
Carolina Farm Stewardship Association
Cattle Producers of Washington (WA)
Cattlemen's Texas Longhorn Registry (TX)
Center for Earth Spirituality and Rural Ministry (MN)
Center for Rural Affairs (NE)
Center for Science in the Public Interest
Center for Sustaining Agriculture & Natural Resources WSU (WA)
Church Women United of Chemung County (NY)
Church Women United of New York
Churches' Center for Land and People
Citizens Action Coalition (IN)
Citizens Awareness Network (MA)
Colorado Independent Cattle Growers Association
Colorado Women Involved in Farm Economics
Community Alliance with Family Farmers (CA)
Community Food Security Center, Community Food Bank, Inc. (AZ)
Community Food Security Coalition
Community Involved in Sustaining Agriculture, Inc. (MA)
Community Markets (NY)
Community to Community Development (WA)
Concerned Citizens of Central Ohio
Consumer Federation of America
Cornucopia Institute
Countryside Conservancy Farmland Center (OH)
Court St. Joseph #139, Catholic Daughters of the Americas (NY)
Cruetzfeldt-Jakob Disease Foundation
Cumberland Countians for Peace & Justice (TN)
Dakota Resource Council (ND)
Dakota Rural Action (SD)
Endangered Habitats League (CA)
Equal Exchange (MA)
Family Dairies USA
Farm Aid
Farm Fresh Rhode Island
Farms Without Harm (MI)
Ferris Farm (NY)
Florida Farmers, Inc.
Food and Water Watch
Foodshed Alliance (NJ)
Genesis Farm (NJ)
Georgia Organics
Georgia Poultry Justice Alliance
Go Wild Consumer Education Campaign (WA)
GrassWorks, Inc. (WI)
Hahn Natural Foods (PA)
Hispanic Farmers and Ranchers of America Inc.
HOLA/National Latino Farmers & Ranchers Trade Association
Horseheads Grange #1118 (NY)
Humane Society of the United States
Idaho Farmers Union
Idaho Rural Council
Illinois Farmers Union
Illinois National Farmers Organization
Illinois Stewardship Alliance
Independent Beef Association of North Dakota
Independent Cattlemen of Iowa
Independent Cattlemen of Nebraska
Independent Cattlemen's Association of Texas
Indiana Farmers Union
Indiana National Farmers Organization
Institute for Agriculture and Trade Policy
International Texas Longhorn Association (OH)
Intertribal Agriculture Council (MT)
Iowa Citizens for Community Improvement
Iowa Farmers Union
Kansas Cattlemen's Association
Kansas Farmers Union
Kit Carson County Cattlemen's Association (CO)
Ladies of Charity of Chemung County (NY)
Land Stewardship Project (MN)
League of Rural Voters (MN)
Lideres Campesinas (CA)
Lincoln County Stockmen's Association (CO)
Little Seed CSA (NY)
Louisiana Shrimp Association
Maine Organic Farmers and Gardeners Association
Mesa County Cattlemen's Association (CO)
Michigan Farmers Union
Michigan Land Trustees
Midwest Organic Dairy Producers Association (WI)
Minnesota Cattlemen's Association
Minnesota Farmers Union
Mississippi Contract Poultry Growers Association
Mississippi Livestock Markets Association, Inc.

Missouri Farmers Union
Missouri National Farmers Organization
Montana Cattlemen's Association
Montana Farmers Union
Moonglow Farms (WI)
Morrow County Livestock Growers Association (OR)
National Association of Counties
National Association of Farmer Elected Committees
National Campaign for Sustainable Agriculture
National Catholic Rural Life Conference
National Consumers League
National Family Farm Coalition
National Farmers Organization
National Farmers Union
National Grange
Nature's International Certification Services (WI)
Nebraska Farmers Union
Nebraska Grange
Nebraska State AFL-CIO
Nebraska Women Involved in Farm Economics
Neighborhood Farmers Market Alliance (WA)
Network for Environmental & Economic Responsibility (TN)
Nevada Live Stock Association
New England Farmers Union (ME, NH, VT, MA, CT, RI)
New England Small Farm Institute
New Entry Sustainable Farming Project (MA)
New Mexico Farmers Marketing Association
New York Beef Producers Association
New York National Farmers Organization
New York State Grange
New York Women Involved in Farm Economics
North Carolina Contract Poultry Growers Association
North Dakota Farmers Union
Northeast Organic Dairy Producers Alliance
Northeast Organic Farming Association of Massachusetts
Northeast Organic Farming Association of New York
Northeast Organic Farming Association of Rhode Island
Northeast Organic Farming Association of Vermont
Northeast Pasture Consortium
Northern Plains Resource Council (MT)
Northwest Atlantic Marine Alliance
NY Farms!
Ohio Environmental Council
Ohio Family Farm Coalition
Ohio Farmers Union
Ohio National Farmers Organization
Oregon Cranberry Farmers' Alliance
Oregon Farmers Union
Oregon Livestock Producers Association
Oregon Rural Action
Organic Choice Milk Procurement (WI)
Organic Consumers Association
Organic Farmers' Agency for Relationship Marketing, Inc. (WI)
Organization for Competitive Markets
Pacific Coast Federation of Fishermen's Association (CA)
Partnership for Earth Spirituality
Past Regents' Club of the Diocese of Rochester (NY)
PCC Natural Markets (WA)
Pennsylvania Farmers Union
Pennypack Farm Education Center for Sustainable Food Systems (PA)
Pesticide Action Network North America
Powder River Basin Resource Council (WY)
R-CALF United Stock Growers of America
Regional Farm And Food Network (NY)
Research, Education, Action and Policy on Food Group (WI)
Rochester Roots, Inc. (NY)
Rocky Mountain Farmers Union (CO, WY, NM)
Rural Advancement Foundation International-USA
Rural Opportunities Inc. (NY)
Rural Roots (ID)
Seattle Chapter of Chefs Collaborative
Sisters Hill Farm (NY)
Small Potatoes Gleaning Project (WA)
Sno-Valley Tilth (WA)
Social Concerns Office-Diocese of Jefferson City (MO)
Society for Animal Protective Legislation (Animal Welfare Institute)
South Dakota Farmers Union
South Dakota Livestock Auction Markets Association
South Dakota Stockgrowers Association
Southern Mutual Help (LA)
Southern Shrimp Alliance
Spokane County Cattlemen's Association (WA)
Sprout Creek Farm (NY)
St. John the Baptist Fraternity, Secular Franciscan Order (NY)
Stevens County Cattlemen's Association (WA)
Sustainable Agriculture Coalition
Sustainable Living Systems (MT)
Taste of the North Fork, Inc (NY)
Texas Farmers Union
Torborg Farms (MN)
True Roots (PA)
Utah Farmers Union
Veritable Vegetable (CA)
Virginia Association for Biological Farming
*Wal*Mart Watch*
Washington Biotechnology Action Council
Washington Cattlemen's Association
Washington County Stockmen's Association (CO)
Washington Farmers Union
Washington Sustainable Food and Farming Network
Western Organization of Resource Councils
Western Sustainable Agriculture Working Group (MT)
Wintergarden Sustainable Agriculture Coalition (TX)
Wisconsin Farmers Union
Wisconsin Independent Livestock Dealers Association
Wisconsin National Farmers Organization
Wisconsin Partners for SustainAbility
Women Involved in Farm Economics
World Hunger Year

As the delayed implementation date of September 2008 nears, opponents of mandatory COOL are trying to convince members of this subcommittee and your colleagues that a change in statute is needed in order to reduce the expense and burden of the program. NFU does not support changing a statute that has not been given the chance to prove itself. As I mentioned earlier, USDA implemented mandatory COOL on farm-raised and wild-caught seafood with the existing statute; the experience gained from seafood implementation should be utilized by USDA to write a final rule on the remaining covered commodities that is not burdensome or expensive.

One of the arguments against COOL is the statute is too restrictive and complicated. My quick response if that is if USDA can label a wild-caught piece of fish, surely it can label a piece of meat or tomato. Fish, after all, don't have ear tags and those that swim in the ocean are pretty slippery. I don't see why the department would have a problem labeling 1,000 pound beef cattle.

Opponents to COOL say hamburger and ground meat is too difficult to track and therefore should be exempt. Ground beef is one of the main reasons FOR mandatory COOL. U.S. companies are able to import cheap – often of lesser quality beef, mix it with U.S. fat trimmings – put a USDA inspection and grade stamp on it and pass it off as a U.S. product for a retail premium.

While this misleading marketing practice might be good for the importer's bottom line, it isn't good for U.S. producers or consumers. According to USDA's Economic Research Service, Americans eat an average of 67 pounds of beef per person per year, with ground beef holding the largest market share at 42 percent. More than three billion pounds of beef imported each year, yet our consumers have no way of knowing whether the meat they're feeding their families is a "Product of U.S.A." or imported. Again, I urge you to do all you can to direct USDA to issue a common-sense implementation rule for mandatory COOL as soon as possible under the existing statute.

I would like to include with my testimony a letter from a coalition of organizations that are supporting a comprehensive competition title in the next farm bill. The letter was sent January 18, 2007 to the chairmen and ranking members of the Senate and House Agriculture and Judiciary committees. With that Mr. Chairman, I thank you again for the opportunity to testify. I'd be pleased to take any questions and thank all of the Members for their support of and work on these important issues.

CONCENTRATION OF AGRICULTURAL MARKETS
April 2007

Mary Hendrickson and William Heffernan
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Columbia, MO 65211 (573)882-3776
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CR4 is the concentration ratio (relative to 100%) of the top four firms in a specific food industry.

BEEF PACKERS **CR4 = 83.5%***

	Daily Slaughter Capacity**
1. Tyson	36,000 head
2. Cargill	28,300 head
3. Swift & Co.	16,759 head
4. National Beef Packing Co.	13,000 head

Historical CR4

1990	1995	1998	2000	2005
72%	76%	79%	81%	83.5%

Source: *Cattle Buyer's Weekly: Steer and Heifer Slaughter reported in *Feedstuffs* 6/16/03.
**Feedstuffs Reference Issue 2006 (9/13/06) as reported in *Feedstuffs* 1/29/07.
Note: Smithfield Foods is the 5th largest beef packer after a series of acquisitions.

BEEF FEEDLOTS

Capacity	One-time
1. Five Rivers (Smithfield and ContiBeef)	811,000
2. Cactus Feeders Inc.	510,000
3. Cargill (Caprock Cattle Feeders)	330,000
4. Friona Industries	275,000

Top Cattle Feedlots 1998	
1. Continental Grain Cattle Feeding	405,000
2. Cactus Feeders Inc.	350,000
3. ConAgra Cattle Feeding	320,000
4. National Farms Inc.	274,000
5. Caprock Industries (Cargill)	263,000

Source: *Beef Today*, Nov-Dec. 1998

Source: *Feedstuffs* Reference Issue 9/13/06 as quoted in *Feedstuffs* 10/23/06

PORK PACKERS **CR4 = 66% (Estimated)***

	Daily Capacity**
1. Smithfield Foods	102,900
2. Tyson Foods	72,800
3. Swift & Co.	46,000
4. Cargill	36,000

Historical CR4

1987	1989	1990	2001**	2005***
37%	34%	40%	59%	64%

** *Feedstuffs Reference Issue* 2001.
*** 2007 *Feedstufs* Reference Issue

Source: *Smithfield is reported to process 27 million hogs per year and account for 26% of the total market. From this figure, we estimated the CR 4. *New York Times* 1/26/07 ** Daily Capacity from 2007 *Feedstuffs* Reference Issue.

PORK PRODUCTION

	Number of Sows*
1. Smithfield Foods	1,200,115
2. Triumph Foods	399,800
3. Seaboard Corporation	213,600
4. Iowa Select Farms	150,000

Number of Sows In 2001**	
Smithfield Foods	710,000
PSF	211,100
Seaboard	185,000
Triumph	140,000

** *Successful Farming Pork Powerhouses* (October 2001)

Source: * *Successful Farming Pork Powerhouses* (October 2006). Notes: Smithfield includes sow numbers from PSF that is pending acquisition. Triumph markets pork through Seaboard.

Prepared with financial assistance from National Farmers Union.

BROILERS **CR4 = 58.5%***

1. Pilgrim's Pride
2. Tyson
3. Perdue
4. Sanderson Farms

Historical CR4

1986	1990	1994	1998	2001
35%	44%	46%	49%	50%

Source: **Feedstuffs* 1/15/07
Note: The CR2 in this sector is 47%.

TURKEYS **CR4 = 55%***

	Slaughter Capacity
1. Butterball LLC**	1,420 Million #s
2. Hormel Foods (Jennie-O Turkey Store)	1,265 Million #s
3. Cargill	961 Million #s
4. Sara Lee	260 Million #s

Historical CR4

1988	1992	1996	2000	2005
31%	35%	40%	45%	51%

Source: **Feedstuffs* 10/9/06 (CR 4 is extrapolated from market share of new company.)
** Butterball LLC was created through a joint venture between Smithfield (49%) and Maxwell Foods (51%) that bought ConAgra's turkey operations.

ANIMAL FEED PLANTS	**ANNUAL CAPACITY***
1. Land O'Lakes LLC/Purina Mills	12.5 million tons
2. Cargill Animal Nutrition (Nutrena)	8.0 million tons
3. ADM Alliance Nutrition	3.2 million tons
4. J.D. Heiskell & Co.	2.8 million tons

Source: * 2007 *Feedstuffs Reference Issue* (9/13/06)

FLOUR MILLING **CR4 = unknown**

		Daily Milling Capacity*
1. Cargill/CHS (Horizon Milling)	CR3=55%**	291,500 cwts
2. ADM		277,800 cwts
3. ConAgra		248,600 cwts

Historical CR4

1982	1987	1990	2005
40%	44%	61%	63%

Source: * *Milling and Baking News* 10/10/06 and 2006 *Grain and Milling Annual*
** Total US 24-Hour Milling Capacity is 1,492,456 cwts (*Milling and Baking News* 6/20/06)

SOYBEAN CRUSHING **CR4 = 80%***

1. ADM
2. Bunge
3. Cargill

CR3=71%**

4. Ag Processing Inc.

Historical CR4

1977	1982	1987
54%	61%	71%

Census of Manufacturing

Source: *2002 Census of Manufacturing (released 6/06); ***Wall Street Journal* 7/22/02

ETHANOL PRODUCTION **CR4 = 31.5%**

	Million Gallons/Year (Capacity)
1. ADM	1070
2. US Biofuels	250
3. VeraSun Energy Corporation	230
4. Hawkeye Renewables	220

Historical CR4

1987	1995	1999	2002
73%	73%	67%	49%

Source: http://www.ethanolrfa.org/industry
Note: Farmer owned ethanol plants accounted for 39% of total capacity.

TOP DAIRY PROCESSORS IN U.S. AND CANADA

	Annual Sales*
1. Dean Foods	$10,106 Million
2. Kraft Foods (Majority owner is Philip Morris)	$ 4,400 Million
3. Land O'Lakes	$ 3,901 Million
4. Saputo Inc.**	$ 3,461 Million

Source: *Dairy Foods: Dairy 100 (2006)
Notes: ** Over 40% of Saputo Inc. plants are in Canada.

INPUT MARKET NOTES
Corn Seed: CR2=58%*

The CR2 in the U.S. corn seed market has remained relatively stable, changing little from a CR2 of 56%** that existed in 1997. However, while Pioneer dominated the market 10 years ago, now DuPont (Pioneer) and Monsanto have roughly equal shares.
Source: **Wall Street Journal*, 1/22/2007; ** Jorge Fernandez-Cornejo, 2004, USDA-ERS, The Seed Industry in the US.

Globally, Monsanto has its genetically modified seeds for corn, cotton, soybeans and canola on more than 90% of acreage that uses GMO seeds. By comparison, Syngenta is in 2nd place with about 4% of global biotech acreage using its seed.
Source: *Financial Times*, 11/16/2006.

Globally, four seed firms, DuPont (Pioneer), Monsanto, Syngenta and Limagrain have about 29% of the world market for commercial seeds.
Source: *Tracing the Trend Towards Market Concentration*. UN Conference on Trade and Development. 2006.

Global Phosphate, Nitrogen, Potash and Feed Phosphate Fertilizer Companies
1. Yara (6% of world's fertilizer market)*
2. Mosaic (Cargill owns 67% with ICM owning 33%)
3. Potash Corp

Source: * Dow Jones Commodities Service 2/14/07

U.S. FOOD RETAILING **CR5 = 48%***

Historical CR5		
1997	2001	2004
24%	38%	46%

Supermarket	Sales in Thousands 2006	2005	2004	Change '04-'06
1)Wal-Mart	$ 98,745,400	$ 79,704,300	$66,465,100	48.57%
2)Kroger	$ 58,544,668	$ 54,161,588	$46,314,840	26.41%
3)Albertson's**	$ 36,287,940	$ 36,733,840	$31,961,800	13.54%
4)Safeway	$ 32,732,960	$ 29,359,408	$29,572,140	10.69%
5)Ahold	$ 23,848,240	$ 21,052,200	$25,105,600	-5.01%

Source: * *Progressive Grocer's Super 50* (5/1/05) *Progressive Grocer* reports only grocery sales from supermarkets and does not report general merchandise, drug or convenience sales. **Note the CR5 is from 2005, and has most likely grown larger given the rates of change from 2004 to 2005.** In February 2005, the top 50 supermarkets accounted for 82% of total supermarket sales nationally.
** Supervalu completed their acquisition of 60% of Albertsons in June 2006. The remaining 40% was sold to Cerebus Capital Management. **Supervalu is now the 3rd largest supermarket.** *Progressive Grocer* 2/1/07.

WORLD'S TOP GROCERY RETAILERS 2006

1.	Wal-Mart Stores (United States)	$312.4 billion annual sales
2.	Carrefour (France)	$ 92.6
3.	Tesco (United Kingdom)	$ 69.6
4.	Metro Group (Germany)	$ 69.3
5.	Kroger (United States)	$ 60.6
6.	Ahold (The Netherlands)	$ 55.3
7.	Costco (United States)	$ 52.9
8.	Rewe (Germany)	$ 51.8
9.	Schwarz Group (Germany)	$ 45.8
10.	Aldi (Germany)	$ 45.0

Source: *Supermarket News* 5/29/06

TOP U.S. FOOD PROCESSING COMPANIES:

Company (Fiscal year in parentheses if different from calendar year)	2005 Food Sales ($ millions)	2002 Food Sales ($ millions)
1. Tyson Foods Inc. (10/1/05)	23,899	21,285
2. Kraft Foods Inc.	23,293	21,485
3 Pepsico Inc.	21,186	17,363
4. Nestle (US & Canada)	19,941	13,110
5. Anheuser-Busch Cos. Inc.	11,546	10,574
6. Dean Foods Co.	10,505	8,992
7. General Mills (5/28/06)	9,803	9,206
8. Smithfield Foods Inc. (4/30/06)	9,614	7,356
9. ConAgra Foods Inc. (5/28/05)	8,195	22,521
10. Swift & Company (5/29/05)	7,847	8,476

Source: Food Processing, Vol. 67(8):34-48, August 2006.

Prepared with financial assistance from National Farmers Union.

January 18, 2007

The Honorable Tom Harkin
Chairman, Senate Committee on Agriculture, Forestry and Nutrition

The Honorable Saxby Chambliss
Ranking Member, Senate Committee on Agriculture, Forestry and Nutrition

The Honorable Collin Peterson
Chairman, House Committee on Agriculture

The Honorable Bob Goodlatte
Ranking Member, House Committee on Agriculture

The Honorable Patrick Leahy
Chairman, Senate Committee on the Judiciary

The Honorable Arlen Specter
Ranking Member, Senate Committee on the Judiciary

The Honorable John Conyers, Jr.
Chairman, House Committee on the Judiciary

The Honorable Lamar S. Smith
Ranking Member, House Committee on the Judiciary

Dear Chairmen and Ranking Members:

The over 200 undersigned organizations strongly urge you to make the issues of agricultural competition and market concentration a top priority as Congress considers the crafting of agricultural legislation and the next Farm Bill. During the 2002 Farm Bill debates, public testimony provided clear and compelling evidence of the need for free market competition and fairness for the nation's farmers and ranchers. Since that time these concerns have become even more urgent and prominent in the public eye.

Today, a small handful of corporations overwhelmingly dominate our food supply. The concentration of market control in the top four firms in U.S. food retailing, grain processing, red meat processing, poultry processing, milk processing, and nearly every category of food manufacturing is at an all time high. Corporate mergers and buyouts have concentrated the power of these firms and increased their ability to unfairly manipulate market conditions in their favor. This unprecedented level of horizontal market consolidation effectively eliminates free market competition to the detriment of independent family farmers and consumers.

Compounding the problem associated with horizontal consolidation is the rapid trend toward vertical integration. Manufacturers, processors, and packers increasingly control all stages of production and inventory through commodity ownership and one-sided contracts. This corporate control of production unnecessarily eliminates market transparency, creating an environment ripe for price manipulation and discrimination. It replaces farm-level decision making with centralized corporate planning and leaves farmers trapped in long-term debts tied to short-term, non-negotiable production contracts. In addition, top retailers and packers increasingly engage in relationships with dominant suppliers that exclude smaller competitors and minimize price competition. Because both supply and demand are controlled by the same few players in the market, the basic principles of supply and demand cannot function.

A critical role of government is to ensure fairness by facilitating properly operating markets and balance in the economic relationships among farmers/ranchers, consumers and food companies. Currently, inadequate federal legislation and the lack of enforcement of anti-trust policies allow a handful of corporations to continue to consolidate market power, manipulate prices, and create anti-competitive market structures. Federal government inaction has a dramatic, negative impact on not only farmers and ranchers, but also on rural communities, the environment, food quality, food safety, and consumer prices. It undermines sustainable production practices and state and local laws that support family-scale, sustainable farm and ranch operations.

Policy makers often voice the laudable policy goals of maintaining a diverse, farm-and-ranch-based production sector and providing consumers with a nutritious, affordable food supply. However, government failure to redress industry concentration--both vertical and horizontal--is thwarting these policy goals and driving the earnings of farmers and ranchers down and consumer prices up.

To address these problems, we urge you to champion a strong, comprehensive Competition Title in the 2007 Farm Bill. We also ask that you co-sponsor and support any of the following measures of this comprehensive package if they are introduced as separate or combined bills and to work for speedy congressional consideration of these proposals.

• LIMIT PACKER CONTROL/MANIPULATION OF LIVESTOCK MARKETS

1. Captive Supply Reform Act: This legislation will bring secret, long-term contracts between packers and producers into the open and create a market for these contracts. The Captive Supply Reform Act would restore competition by making packers (and livestock producers) bid against each other to win contracts. Currently, formula contracts and marketing agreements are negotiated in secret, where packers have all the information and power. These formula contracts and agreements depress prices and shut small and independent producers out of markets. The Captive Supply Reform Act would require such contracts to be traded in open, public markets to which all buyers and sellers have access.

2. Prohibition on Packer-Owned Livestock: Meat packers such as Tyson, Cargill, and Smithfield Foods use packer-owned livestock as a major tool for exerting unfair market power over farmers and ranchers. This practice fosters industrial livestock production and freezes independent farmers out of the markets. Packer-owned livestock has been proven to artificially lower farm gate prices to farmers and ranchers while consumer food prices continue to rise. By prohibiting direct ownership of livestock by major meatpackers, a packer ban addresses a significant percentage of the problem of captive supply which packers use to manipulate markets, and would help increase market access for America's independent producers who currently experience great restrictions in market access due in part to packer ownership of livestock.

• INCREASE FAIRNESS IN AGRICULTURAL CONTRACTS AND MARKETS

3. Fairness Standards for Agricultural Contracts: In order to address the worst abuses contained in processor-drafted contracts, legislation that provides a set of minimum standards for contract fairness is urgently needed. Such standards should include at a minimum the following:

(a) prohibition of the use of forced, mandatory arbitration clauses, which have been used by some packers or integrators to force growers to give up their access to the courts, even in the case of fraud, breach of contract, misrepresentation or other blatant contract abuses by the integrator or packer firm;
(b) clear disclosure of producer risks;
(c) full prohibition on confidentiality clauses;
(d) recapture of capital investment so that contracts that require a significant capital investment by the producer cannot be capriciously canceled without compensation; and
(e) a ban on unfair or deceptive trade practices, including "tournament" or "ranking system" payment.

4. Clarification of "Undue Preferences" in the Packers & Stockyards Act (PSA): Packers commonly make unjustified, preferential deals that provide unfair economic advantages to large-scale agriculture production over smaller family owned and sustainable farms. Courts have found current undue preference legal standards virtually impossible to enforce. Additional legislative language is needed in the PSA to strengthen the law and clarify that preferential pricing structures (those that provide different prices to different producers) are justified only for real differences in product value or actual and quantifiable differences in acquisition and transaction costs. Specifically, we are asking to:

(a) Make clear that farmers damaged by packer/processor unfair and deceptive practices need not prove "harm to competition" to receive a remedy.
(b) Make clear that "pro-competitive effects" or "legitimate business justifications" are not recognized packer defendant defenses, and not necessary for farmer-plaintiffs to prove the absence of, in a court case under the PSA.
(c) Require courts to award attorneys fees to successful producer plaintiffs under the PSA.

5. Closing Poultry Loopholes in the Packers & Stockyards Act (PSA): USDA does not currently have the authority under the PSA to bring enforcement actions against poultry dealers. Poultry producers should have the same basic enforcement protection that is offered to livestock producers when packers and livestock dealers violate the PSA. We seek legislation to clarify that USDA has authority over PSA violations involving poultry dealers in their relations with all poultry growers, including those who raise pullets or breeder hens as well as broiler producers. The PSA enforcement loophole for poultry dealers should be closed.

6. Bargaining Rights for Contract Farmers: Loopholes should be closed in the Agricultural Fair Practices Act of 1967 (AFPA) and processors should be required to bargain in good faith with producer organizations. The AFPA was enacted to ensure that livestock and poultry producers could join associations and market their products collectively without fear of retribution by processors. These goals have not been attained due to loopholes in that Act. Retaliation by processors is commonplace in some sectors. Legislation should be enacted that promotes bargaining rights and prevents processor retaliation.

• ASSURE ADEQUATE MARKET INFORMATION AND TRANSPARENCY FOR PRODUCERS AND CONSUMERS

7. Livestock Mandatory Price Reporting: The Livestock Mandatory Price Reporting Act of 1999 (LMPRA) requires packers, processors, and importers to provide price, contracting, supply and demand information to USDA, which then uses the information to create price reports for livestock producers. Since its implementation, bureaucratic inertia has blocked effective enforcement of the LMPRA and prevented the Act from operating to benefit independent livestock producers. The Government Accountability Office, at the request of Senators Harkin (D-IA) and Grassley (R-IA), has reviewed USDA implementation of the Act. In December 2005, the GAO issued a report documenting lengthy lag times for USDA corrections to missing or incorrect information from packers, and the failure of USDA to inform the public about violations of the Act revealed in USDA audits. The LMPRA was reauthorized in September 2006 without including GAO recommendations to improve the Act. If USDA does not implement these recommendations, Congress should amend the Livestock Mandatory Price Reporting Act in 2007 by incorporating the GAO report recommendations as legislative directives to USDA in implementing the Act.

8. Mandatory Country of Origin Labeling: Country of origin labeling (COOL) for beef, lamb, fresh fruits, fish and shellfish was passed as a provision of the 2002 Farm Bill. Mandatory COOL for the fish and shellfish commodities was implemented by USDA in April of 2005, but COOL implementation for all other commodities has been successfully stymied by the meatpackers and retailers. Country of origin labeling is a popular measure that allows consumers to determine where their food is produced and also enables U.S. producers to showcase their products for quality and safety. It also limits the ability of global food companies to source farm products from other countries and pass them off as U.S. in origin. Congress should reauthorize COOL to reiterate its benefits to producers and consumers and should provide funding to ensure that USDA undertakes immediate implementation of COOL.

In conclusion, farmers, ranchers, and consumers across the country are asking for these legislative reforms to ensure fair markets and a competitive share for family farmers and ranchers of the $900 billion dollars that consumers pay into the food and agriculture economy annually. Market reforms remain a key ingredient for rural revitalization and meaningful consumer choice. The legislative reforms summarized above are key to achieving the goals of promoting an economically healthy and diverse agricultural production sector and providing consumers with healthy, affordable food.

Thank you.

Sincerely,

A Little Taste of Everything
A Taste of the North Fork (NY)
Adams County Farmers Union (ND)
Agricultural Missions, Inc. (NY)
Agriculture and Land Based Training Association (CA)
Agriculture of the Middle
Alabama Contract Poultry Growers Association
Alabama Sustainable Agriculture Network
Alliance for a Sustainable Future (PA)
Alliance for Sustainable Communities (MD)
Alternative Energy Resources Organization (AERO) -MT
American Corn Growers Association
American Society of Agronomy
Appalachian Crafts (KY)
Art & Nature Project (NY)
Beartooth Stock Association (MT)
Berkshire Co-op Market
Bird Conservation Network
Blessed Kateri Tekakwitha Region, Secular Franciscan Order, NYS
Bronx Greens
California Dairy Campaign
California Farmers Union
California Institute for Rural Studies
Californians for GE-Free Agriculture
Campaign for Contract Agriculture Reform
Campaign for Family Farms and the Environment
Caney Fork Headwaters Association (TN)
Catholic Charities Diocese of Sioux City, IA
Catholic Charities of Chemung /Schuyler Counties (NY)
Catholic Charities of Kansas City - St. Joseph, Inc.
Catholic Charities of Louisville, Parish Social Ministry Dept. (KY)
Catholic Rural Life, Archdiocese of Dubuque, IA
Cattle Producers of Washington
Center for Food Safety
Center for Earth Spirituality and Rural Ministry (MN)
Center for Popular Research, Education and Policy (NY)
Center for Rural Affairs
Central Colorado Cattlemen's Association
Chemung County Church Women United (NY)
Chemung County Council of Churches (NY)
Church Women United of NYS
CitySeed (CT)
Community Action Resource Enterprises (OR)
Community Food Security Coalition
Concerned Citizens of Central Ohio
The Cornucopia Institute (WI)
Corson County Farmers Union (SD)
Court St Joseph #139, Catholic Daughters of the Americas, Corning (NY)
Court St Joseph #139, Corning/Elmira, Catholic Daughters of the Americas (NY)
Crop Science Society of America
Crowley-Kiowa-Lincoln Cattlemen's Association (CO)
Cumberland Counties for Peace & Justice (TN)
Dakota Resource Council
Dakota Rural Action of SD
Delmarva Poultry Justice Alliance
Delta Land and Community, Inc.
Eagle County Cattlemen's Association (CO)
Endangered Habitats League (CA)
Environmental Action Committee of West Marin (CA)
Environmental Coalition of Mississippi
Family Farm Defenders
Family Farms for the Future (MO)
Farm Aid
Farm Fresh Rhode Island
FH King Students of Sustainable Agriculture at UW Madison
First Nations Development Institute
Florida Organic Growers
Food Alliance (OR)
Food and Water Watch
FoodRoutes Network
Foodshed Alliance of the Ridge and Valley (NJ)
Friends of Rural Alabama
Georgia Organics
Georgia Poultry Justice Alliance
Global Exchange
Government Accountability Project
GRACE/Sustainable Table
Grassroots International
Hahn Natural Foods (PA)

Harding County Stockgrowers Association (SD)
Harvest Co-op Market (MA)
Heartland Center / Office of Peace and Justice for the Diocese of Gary, Indiana
Hispanic Farmers and Ranchers of America Inc.
Hispanic Organizations Leadership Alliance
Horseheads Grange #1118, Chemung City (NY)
Humane Society of the United States
Idaho Rural Council
Illinois Farmers Union
Illinois Stewardship Alliance
Independent Beef Association of North Dakota
Independent Cattlemen of Iowa
Independent Cattlemen of Nebraska
Independent Cattlemen's Association of Texas, Inc.
Indiana Campaign for Economic Justice
Indiana Farmers Union
Institute for Agriculture & Trade Policy
Institute for Responsible Technology
Iowa Citizens for Community Improvement
Iowa Farmers Union
Just Food (NY)
Just Harvest, Pittsburgh
Kansas Cattlemen's Association
Kansas City Food Circle
Kansas Farmers Union
Kansas Rural Center
Kerr Center for Sustainable Ag (OK)
Kit Carson County Cattlemen's Association (CO)
La C.A.S.A. de Llano (TX)
Ladies of Charity of Chemung County (NY)
Land Stewardship Project (MN)
Little Seed CSA (NY)
Madera County Cattlemen's Assoc (CA)
McKenzie City Energies & Taxation Association (ND)
Merced-Mariposa Cattlemen's Association, (CA)
Mesa County Cattlemen's Association (CO)
Michigan Farmers Union
Midwest Organic and Sustainable Education Service
Minnesota Farmers Union
The Minnesota Project
Mississippi Contract Poultry Growers Association
Mississippi Livestock Markets Association
Missouri Farmers Union
Missouri Rural Crisis Center
Montana Cattlemen's Association
Montana Farmers Union
National Campaign for Sustainable Agriculture
National Catholic Rural Life Conference
National Center for Appropriate Technology (NCAT)
National Family Farm Coalition
National Farmers Organization
National Farmers Union
National Hmong American Farmers, Inc.
National Latino Farmers & Ranchers Trade Association
National Organic Coalition
National Poultry Justice Alliance
Nebraska Farmers Union
Network for Environmental & Economic Responsibility
Nevada Live Stock Association
New England Small Farm Institute (NESFI)
New York Beef Producers Association Southern Tier Region
NY Sustainable Agriculture Working Group
Nojoqui Ranch Produce (CA)
North Carolina Contract Poultry Growers Association
North Dakota Farmers Union
Northeast Organic Dairy Producers Alliance
Northeast Organic Farming Assoc -MA
Northeast Organic Farming Assoc -NY
Northeast Organic Farming Assoc-CT
Northeast Organic Farming Assoc-VT
Northern Plains Sustainable Agriculture Society
Northern Plains Resource Coun (MT)
NYS Safe Food Coalition
Ohio Environmental Council
Ohio Farmers Union
Oregon Livestock Producer Association
Oregon Tilth
Organic Consumers Association
Organic Seed Alliance (WA)
Organization for Competitive Markets

The Partnership for Earth Spirituality (NM)
Past Regents Club, Diocese of Rochester (NY)
PCC Natural Markets (WA)
PCC Farmland Trust (WA)
Pennsylvania Association for Sustainable Agriculture
Pennsylvania Farmers Union
Perkins County Farmers Union (South Dakota)
Platte County Farm Bureau (NE)
Powder River Basin Resource Council (WY)
Producers Livestock
Provender Alliance (OR)
Putting Down Roots (PA)
Rainbow Natural Grocery (MS)
R-CALF United Stockgrowers of America
Red Tomato (MA)
Regional Farm and Food Project (NY)
Rochester Farm Connection (NY)
Rochester Roots (NY)
Rocky Mountain Farmers Union
Rural Advancement Foundation International-USA (RAFI-USA)
Rural Coalition/Coalición Rural
Rural Life Committee of the North Dakota Conference of Churches
Selene Whole Foods Co-op (PA)
Sevananda Natural Foods Market
Sierra Club Agriculture Committee
Social Concerns Office, Diocese of Jefferson City
Social Concerns/Rural Life Department, Catholic Charities, Diocese of Sioux City, IA
Soil Association
Soil Science Society of America
South Dakota District IV Farmers Union
South Dakota Farmers Union
South Dakota Stockgrowers Association
Southern Colorado Livestock Association
Southern Research & Development Corp. (LA)
Southern Sustainable Ag Working Group
Spokane County Cattlemen's Association (WA)
St John the Baptist Fraternity, Secular Franciscan Order, Elmira NY
Stevens County Cattlemen's Association (WA)
Sustainable Agriculture Coalition
Temple Beth El of Flint, Michigan
Texas Mexico Border Coalition Community Based Organization
Tilth Producers of Washington
United Hmong Association
The Urban Nutrition Initiative (PA)
Utah Farmers Union
Valley Stewardship Network (WI)
Virginia Association for Biological Farming
Washington Cattlemen's Association
Washington County Stockmen's Assoc (CO)
WA Sustainable Food & Farming Network
West Carroll Cattleman Assoc. (LA)
Western Organizations of Resource Councils
Wisconsin Farmers Union

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STATEMENT OF THE
AMERICAN FARM BUREAU FEDERATION
TO THE
HOUSE COMMITTEE ON AGRICULTURE
SUBCOMMITTEE ON LIVESTOCK
REGARDING LIVESTOCK MARKET STRUCTURE

April 17, 2007

Presented by Bob Stallman
President, American Farm Bureau Federation

The American Farm Bureau Federation appreciates the opportunity to provide comments on the changing market structure of the livestock industry. Farm Bureau represents more than 6 million member families across the United States. Increasing producer competitiveness and access to a transparent marketplace is vital to sustaining domestic production agriculture for farmers and ranchers.

Farm Bureau is concerned that consolidation, and concentration within the agricultural sector, could have adverse economic impacts on U.S. farmers and ranchers. As contractual production and marketing arrangements between producers and processors become more prevalent, we see less connection with traditional cash markets which could result in reduced prices for all commodities paid to producers. It is important that markets be accessible to all producers and that these markets offer competitive prices for their products.

The landscape has changed for both crop and livestock producers in recent decades, both in purchasing inputs and in marketing finished livestock, grain and fiber. Consider these trends, as reported by various agencies of the Agriculture Department:

- From 1980 though 2004, the share of steer and heifer slaughter for the four largest beef packers increased from 36 percent to 80 percent.
- From 1985 through 2004, the share of hog slaughter for the four largest hog packers increased from 32 percent to 64 percent.
- From 1975 to 2004, the portion of fed cattle marketed by feedyards that had a 1,000-head or larger capacity increased from 74 percent to 95 percent.
- Currently, four-firm market shares in the broiler sector run higher than 50 percent.

The story is similar in much of the grain complex. For example:

- The three largest soybean processors controlled more than 70 percent of the U.S. market in 2003.

- The four largest agricultural chemical companies had 62 percent of the total world market share, based on 2004 data.

The Grain Inspection Packers and Stockyards Administration's (GIPSA) Livestock and Meat Marketing Study reveals significant information specific to the use of alternative marketing arrangements (AMAs) in the beef and pork processing sectors. From 2002 through early 2005, AMAs were estimated at 38 percent of fed cattle volume, 44 percent of the fed lamb volume and 89 percent of the finished hog market.

Packer ownership accounted for only 5 percent of fed cattle and lamb volume, but between 20 and 30 percent of fed pork volume. The report stated, "The use of AMAs is associated with lower cash market prices, with a much larger effect occurring for finished hogs than for fed cattle." While there is ample room to debate the merits of widespread use of AMAs increasing industry efficiency, increasing concentration and the conclusion about the impacts of AMAs on cash market prices call attention to why we discuss this issue today. It is also important to recognize that while AMAs are voluntary, we question whether they are truly voluntary in every region of the country, for every packer or for every species. Our producers often remind us that one cannot look at concentration in the aggregate for the entire country. A region by region review of AMAs would possibly provide different results.

AFBF supports the following issues to enhance competition in the current livestock marketplace:

- Farm Bureau supports enhancing USDA's oversight of the Packers and Stockyards Act (PSA). GIPSA investigations need to include more legal expertise within USDA to enhance anti-competitive analysis on mergers. Farm Bureau supports enforcement of antitrust laws and the PSA. USDA, in conjunction with the Department of Justice (DOJ), should closely investigate all mergers, ownership changes or other trends in the meat packing industry for actions that limit the availability of a competitive market for livestock producers. We support establishing an Office of Special Counsel for Competition at USDA.

- A few years ago, Farm Bureau helped secure a specific agriculture counsel at the DOJ. Farm Bureau works closely with the current counsel, Mr. Doug Ross, who understands agriculture and the regional, local and broad perspective that a potential agribusiness merger or acquisition would have on producers. Farm Bureau believes that this type of designated role at USDA would be beneficial to help enforce the PSA.
- Farm Bureau supports amending the PSA and strengthening producer protection and USDA's authority in enforcing the PSA to provide jurisdiction and enforcement over the marketing of poultry meat and eggs as already exists from livestock. This includes breeder hen and pullet operations ensuring they are treated the same as broiler operations.

- Farm Bureau supports efforts to provide contract protections to ensure that the production contract clearly spells out what is required of the producer. In addition, we support prohibiting confidentiality clauses in contracts so that producers are free to share the contract with family members or an outside advisor such as a lawyer or lender. Farm Bureau supports establishing GIPSA as the overall authority and provider of oversight to ensure livestock contracts are clearly written, confidentiality concerns are addressed, investments are protected, price transparency and discovery are enhanced, and contractors honor the terms of contracts.
- Farm Bureau supports legislation to prohibit mandatory arbitration. Producers should not be required to submit to arbitration and give up rights to seek remedy in court to resolve disputes with companies.

Farm Bureau appreciates the work by the House Agriculture Committees that reauthorized mandatory price reporting last fall. The program has worked well for our producers in providing increased price and market information. We look forward to working with USDA to ensure the program is properly implemented.

The following are additional issues that are indirectly related to competition and the changing market structure.

Interstate shipment of state inspected meat is another issue important to Farm Bureau members. Farm Bureau has long supported allowing meat and poultry inspected under state programs, which are equal to federal inspection and approved by USDA, be permitted to move in interstate commerce. There are 28 states with nearly 2000 state inspection facilities for meat products. All other products such as milk, dairy products, fruit, vegetables, fish, shellfish and canned products, which are inspected under state jurisdiction, are allowed to be marketed freely throughout the U.S. Movement of these products across state lines will increase marketing opportunities and provide more of a competitive marketplace for our farmers and ranchers.

Farm Bureau supports voluntary country of origin labeling. The costs associated with implementing a mandatory program, especially for meat products, would provide a competitive disadvantage for producers. USDA estimates the program could cost the industry between $500 million and $4 billion in the first year with per head costs at $10.00 per cow and $1.50 per hog. Until a cost-effective program can be implemented, Farm Bureau opposes a mandatory labeling program for meat, fruits and vegetables and peanuts.

Farm Bureau supports the establishment and implementation of a voluntary national animal identification system capable of providing support for animal disease control and eradication. Farm Bureau remains concerned about three major issues that will affect the success of this voluntary program and believes these issues must be resolved prior to the implementation of a program:

- Cost: How much will animal identification cost and who will pay the price? The price tag for a national ID system could run as high as $100 million annually.

The fiscal year 2007 agriculture budget provides $33 million to fund activities for system development, a level that is insufficient to obtain satisfactory producer participation in a voluntary program. Producers cannot and should not bear an unfair share of the costs of establishing or maintaining an animal ID system. Implementation of a successful ID program depends on adequate and equitable funding.

- Confidentiality: Who has access to the data used in the NAIS, and how can producers be assured protection from unintended use of the data they submit? Legislation is imperative to ensure the privacy of producers' information submitted to the NAIS, because producers must be protected from public disclosure under the Freedom of Information Act (FOIA). Otherwise, competitors or activist groups could exploit proprietary information. Furthermore, there must be clarity on which state and federal agencies will have access to the data.

- Liability: Are producers appropriately protected from the consequences of the actions of others, after their animals are no longer in their control? Many producers worry they might be forced to share liability for food safety problems that are now limited to meat merchandisers. In order to minimize the threat from occurring, Congress must pass legislation defining the duty of care of a livestock producer as "ordinary care."

Thank you for the opportunity to discuss issues related to the changing market structure for farmers and ranchers. We look forward to working with you to address issues that will enhance a competitive marketplace for our members in the upcoming Farm Bill.

Market Structure of the Livestock Industry

Testimony to the United States House of Representatives Committee on Agriculture, Subcommittee on Livestock, Dairy and Poultry

April 17, 2007

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Market Structure of the Livestock Industry

Testimony to the United States House of Representatives Committee on Agriculture, Subcommittee on Livestock, Dairy and Poultry

C. Robert Taylor

Thank you, Mr. Chairman and members of the Subcommittee for this opportunity to testify about important issues affecting the economic health of the American livestock and poultry industries.

I will restrict my comments today to market structure issues in the cattle and beef industry, beginning with a few facts.

Facts

Cattle feeders are justifiably concerned over declining profitability. Iowa State University[1] data shows that inflation-adjusted returns from feeding steers have generally trended downward over the past two cattle cycles of approximately 10-15 years duration. Inflation-adjusted returns averaged $40.26/head over 1981-1993, but only $21.32/head over 1994-2006, a 47% decline. Omitting the spike in returns that occurred during May 2003 through July 2005 when Canadian cattle imports were banned, returns to cattle feeding averaged only $2.29/head over the 1994-2006, which is a 94% long-term decline from the previous cycle. An average return of $2.29/head for feeding cattle four months will not economically sustain the American cattle industry, particularly given the financial risks associated with cattle. Cattle feeders therefore have justifiable concerns over declining profitability, a concern that applies to feeders with AMAs as well as to independent feeders.

Most of the USDA and academic studies of market concentration and captive supply refer to "small" effects on cattle markets. Big or small depends on perspective. A 2% impact on the price of fed steers translates into a 50% effect on returns to cattle feeding based on the Iowa returns.

Market Power

Disproportionate market power is the fundamental issue in livestock, dairy and poultry industries. Competitive athletic events require a balancing of power, a clear set of rules and impartial enforcement of those rules. Too few rules and athletic events turn into brawls or one-sided scores; too many rules and the refs take over without allowing athletes to really compete. Truly competitive markets have similar requirements: a balancing of power, clear rules and rigorous and impartial enforcement of those rules.

[1] Compiled by Dr. John D. Lawrence. Downloadable at: http://www.econ.iastate.edu/faculty/lawrence/Lawrence_website/livestockreturns.htm. Return data were converted to constant dollar returns using the consumer price index.

There are two very different sources of market power that occur in both cash markets and markets for contracts. The first is traditional market-share or size based market power (Type I). Market power also can come from deception, significantly imperfect or asymmetric information, or other types of market failures[2] (Type II). Often, Type II imperfections exacerbate the effects of Type I market power.

An imbalance of traditional market power is akin to one athletic team stockpiling all of the good players. Non-traditional sources of market power are akin to one side using unfair tactics. If such tactics are covered by existing rules and regulations, then they should be impartially enforced. If existing rules do not consider such tactics, then rules should be changed and enforced.

Both Type I and Type II sources of market power presently exist, or are emerging in livestock, dairy and poultry markets. Concentration of beef packers now exceeds the Department of Justice threshold for markets where a high degree of power may be exerted.

Three non-traditional (Type II) sources of market power merit emphasis in livestock markets. First, alternative marketing arrangements (AMAs) that tie a base price in any way to the cash market[3]--the predominant form of AMA--distort buyer incentives in concentrated markets[4]. (An illustration is given in Appendix A.) Even if such a distortion has not occurred in the past, the potential for market distortion clearly exists. Economists agree on this; many have publicly emphasized that USDA or Congress should prohibit such AMAs[5].

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[2] Robert H. Lande, Market Power Without A Large Market Share: The Role of Imperfect Information and other "Consumer Protection" Market Failures, The American Antitrust Institute Working Paper No 07-06, March 14, 2007.

[3] Tying a large number of AMAs to the futures market is also problematic. The cash and futures market are connected; distorted incentives in futures market therefore affects the cash market, and vice-versa.

[4] Theoretically, such AMAs would not be a problem in un-concentrated markets with many buyers.

[5] Statements by academic economists follow.

> *"Contracts with a formula arrangement where the base price is either a cash market in which the packer/processor is an active buyer or a plant average price paid for the week prior to delivery offer the wrong incentives. Whether buyers attempt to manipulate the cash market to which the contract price is tied is somewhat immaterial because the incentive to do so is present and is undeniable." Dr. Wayne Purcell, VPI,* Statement at the Public Forum on Captive Supplies held by the United States Department of Agriculture, Denver, CO, September 21, 2000

> *"... the practice of tying a formula base to an in-house average spot market price does distort packers' incentives and has the potential to result in harm to livestock producers. We suggest that the Secretary (of Agriculture) should consider regulations designed to prohibit this practice." Dr. John Schroeter, Iowa State University,* Statement at the Public Forum on Captive Supplies held by the United States Department of Agriculture, Denver, CO, September 21, 2000

> *"... base prices based on plant averages (which is a cash price) are not recommended and this has been a position I have held for a long time." Dr. Ted Schroeder, Kansas State University,* Statement made in response to questions at the Public Forum on Captive Supplies held by the United States Department of Agriculture, Denver, CO, September 21, 2000. Parenthetical statement added.

Second, economists also agree that asymmetric information favoring the buyer tends to depress price below competitive levels. Although mandatory price reporting (MPR) has provided much needed information to market participants, large transactions are not reported due to confidentiality requirements (the 70/30 rule), holding rights of the large market player—a few packers--above the rights of the small market player. This is problematic because large transactions—now unreported--move the market. Market transparency requires timely reporting of all transactions, large and small.

Captive supply as well as market transactions not reported due to confidentiality is akin to insider trading. For good reason, federal regulations require reporting of insider trading in the stock market. Similar transactions in both the cash and futures market for cattle need reporting to make those markets transparent and efficient.

Third, the packer-dictated narrow trading window can be a non-traditional source of market power. The trading window is often only an hour or less on any day of the week picked by the buyer. This day varies from week to week and buyer to buyer. Whether the bids are early in the week or late in the week affects the psychology of the market and contributes volatility to the market. Such a narrow trading window does not allow sellers sufficient time to solicit other bids and results in inefficient management and marketing decisions.

These three non-traditional sources of market power—(a) AMAs tied to the cash market, (b) imperfect information and (c) a narrow trading window—pinpoint significant real and potential future anti-competitive practices in the industry. Correcting these problems with regulatory or legislative solutions does not require major surgery or economic trauma for the cattle industry.

The Fallacy of Composition

Captive supply advocates argue that AMAs are good for both feeder and packer because they reduce the need to haggle over the price Based on such assertions, some immediately jump to the conclusion that if AMAs are good for the individual then they are good for the industry.

"(NCBA should) adopt a policy position opposed to contractual arrangements between cattle feeder/producer and packer when the base price is tied to a cash market in which the buying packer is active in buying fed cattle and/or when the base price is tied to plant or firm prices paid or cattle costs into the plant(s) for some time period prior to the date of delivery with the reasons for the policy position coming from the inappropriate incentives of this approach and from the need to restore integrity to the pricing system. The incentives facing buyers when price is tied to markets in which they are large buyers are not consistent with confidence and integrity of the pricing process." Drs. Wayne Purcell, Clement Ward, Ted Schroeder, Rodney Jones, James Mintert, James Trapp, Barry Goodwin, Matthew Holt, and DeeVon Bailey, White Paper on Status, Conflicts, Issues, Opportunities, and Needs in the U.S. Beef Industry, May 1999

Not so. There is a fundamental logical error in such reasoning, which is referred to in economics as the fallacy of composition. A fallacy of composition arises when one infers that something is true of the whole from the fact that it is true of some (or even every) part of the whole.

A common example of the logical fallacy is that any person can get a better view at a football game by standing. Of course, if one stands, then others stand because their view was blocked. If everyone stands, no one gets a better view. In fact, if standing people start moving around looking for an even better view, as they tend to do, then most people get a worse view than with all sitting. It is thus a fallacy to conclude that just because an individual can get a better view by standing, all would get a better view by standing.

A logical fallacy exists with AMAs if the base price in such arrangements is tied to the cash market, as is typical. This contract feature distorts packer's economic incentives. To the extent that feeders who sell on the cash market are harmed by marketing agreements, then feeders with AMAs, as a group, are equally harmed.

Econometric Exercises

Congress is well aware that well over $10 million in taxpayer funds have been expended for seemingly endless "studies" of these market concentration and captive supply, with the RTI study being the most recent. The numerous USDA/GIPSA studies conducted by academics have generally been severely restricted in evidentiary scope; GIPSA never specified what constitutes "evidence" or specified the evidentiary standard to be used by researchers. The studies have generally been turned into "academic exercises," narrowly restricted to quantitative data suitable for econometric analysis. Consequently, the studies have ignored a wealth of non-quantitative evidence pertinent to the issues[6].

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[6] For example, the GIPSA studies total ignore recorded statements by Bob Peterson, who began his career as a cattle buyer and who, as CEO of IBP (now Tyson), was responsible for acquisition of about one-third of fed cattle slaughtered nationally over 17 years. Peterson emphasized the leverage the packer obtained in the cash market with captive supplies in talks to cattlemen in 1988, just before IBP had significant captive arrangements, then again in two talks to cattlemen in 1994. Selected excerpts follow.

> *"...our competitors are promoting contracts ... and seeking more. These (forward) contracts coupled with packer feeding could represent a significant percentage of the fed cattle during certain times of the year... Do you think this has any impact on the price of the cash market? ... you bet! ... We believe that it's having a significant impact on the market—on the cash market place.[6]:"*

> *"...we believe that some of those who are feeding cattle and using forward contracting are creating aberrations within the market place by coming in and out of the market; that is not reflecting the true value of the cash market."*

> *"But with the packers in the feeding business and forward contracting, there's going to be a major, major shift against the leverage system."*

> *"In my opinion the feeder can't win against the packer in the real fair play if we go into the feeding and the hedging program."*

Evidentiary standards used to arrive at conclusions (or non-conclusions) in the GIPSA studies have never been articulated. They have not been articulated by GIPSA to researchers, or articulated in the final research reports. Apparently the researchers used an academic standard, call it academic certainty, or statistical significance. A more relevant standard for regulatory action under the Packers & Stockyards Act (PSA) appears to be the legal concept of "preponderance of evidence," particularly since this is the standard for civil litigation under the PSA. Academic certainty and statistical significance are much stricter standards, more akin to the legal concept of "beyond a reasonable doubt."

In my opinion, the contentious issues of market concentration and captive supplies will never be resolved with academic certainty, but this is an inappropriate standard for regulatory action under the PSA.

RTI Study

I will now turn to the RTI study because it is central to this Hearing.

A fundamental flaw of the RTI study is that ***all*** quality benefits were attributed to AMAs, ignoring the fact that about 20% of cash transactions occur with a negotiated grid (grade and quality premiums and discounts). Negotiated cash grid transactions can provide precisely the same quality benefits claimed for AMAs. In fact, all cash transactions could have a negotiated grid if the packers so chose. If packers are as interested in quality as they repeatedly claim, then why aren't all of their cash acquisitions on a grid?

Had the RTI study appropriately compared elimination of AMAs to a norm with all transactions occurring with a negotiated grid, the only benefit to AMAs would have essentially been a $0.40/head transaction cost saving reported by surveyed packers. This is only four one-hundredths of a percent (not 4% but 0.04%) of the value of a fed steer, hardly the 4-16% negative impacts touted by the RTI study.

> *"Do you think that if we had a million cattle on feed and we thought cattle were going to get higher we'd kill ours first and wait for yours until last? Or do you think we'd kill yours first and wait for ours until last? Do you think if it's going down we're going to buy yours and wait for ours until last? This is pretty basic. Boy Scouts and Girl Scouts are nice, but when you get back to money in the bank and the facts, I'm telling you the facts."*
>
> *"... not formula cattle but packer-fed cattle, which can be killed early or late to fill a particular time frame, be it a day or a week grant the packer far greater flexibility to move in and out of the market. On the way down (in price), he kills his cattle first and on the way up, last."*

Peterson's statements also apply to marketing agreement (also called "formula") cattle as well as packer-owned cattle because the packer generally decides the day of the week on which marketing agreement and other captive cattle were slaughtered. So with captive supplies committed to slaughter in a particular week, the packer can slaughter or acquire them early (late) in the week if they expect price to go down (up). With packer-owned cattle this would simply reduce the price the packer paid for slaughter cattle purchased on the market that week. But with marketing agreement and other captive supplies with a base price tied to the market or to the in-plant average cost, large buyers have a magnified incentive to play this within-week game because it affects not only the price paid on the cash market but also reduces the cost of the previously committed captive cattle.

There has been a lack of "innovative" effort by USDA to identify new ways of doing business that are economically efficient, fair to both sides of the transaction, do not distort buyer or seller incentives, and result in beef with the quality attributes that consumers desire. The bi-polar industry debate on current marketing practices, specifically cash or AMAs, has been carried over to the extensive GIPSA studies. In other words, marketing agreements or other captive arrangements are not the only way of rewarding quality, and not the only way of avoiding the time and expense of buyer and seller "haggling" over the price of every pen of cattle. Likewise, "on the hoof" is not the only way of having negotiated cash transactions.

The RTI study accepted, apparently without question, packers' common assertion that AMAs were more "reliable" than the cash market. The facts show just the opposite[7]:

- AMAs were 2.2 times more variable than supply from the cash market based on GIPSA monthly data for the 15 largest packers, 1988-98
- AMAs were 1.5 times more variable than supply from the cash market based on AMS "additional movement" weekly data, 1994-1998
- Tyson/IBP's captive supply was 1.5 times more variable than their acquisitions from the cash market based on weekly data made public in Pickett v. Tyson/IBP, 1994-2002
- AMAs were 3.5 times more variable than supply from the cash market based on GIPSA monthly data for the four largest packers, 1990-2002
- AMAs were 2.4 times more variable than supply from the cash market based on GIPSA "revised" monthly data for the four largest packers, 1999-2002
- AMAs were 1.4 times more variable than supply from the cash market based on MPR weekly data, April 2004 through January 2007
- Variability of total U.S. beef production has not changed appreciably in many decades, even though AMAs now account for about half of total slaughter of fed beef, strongly suggesting that AMAs are not more reliable.

Therefore, the facts establish that AMAs are generally ***less*** reliable than the cash market.

The RTI study subtly circumvented examination of whether AMAs depressed cash prices below competitive levels. In essence, the RTI study compared prices under various AMAs to the cash market. About 80% of AMAs are tied in some way to price in the residual cash market. If exertion of market power (Type I or II) depresses price, both AMAs and cash sellers will be negatively impacted. Average quality adjusted price with AMAs will move with average quality adjusted price in the cash market. To again use the metaphor of spectators at a football game, the RTI study looked around the stadium and compared height of spectators; significantly, they did not carefully look to see if everybody was standing (competitive prices) or sitting (depressed prices). Furthermore, they did not assess whether the rules of the game would lead to true competition, or if

[7] All variability comparisons are based on the coefficient of variation, a statistic that allows comparison of the variation of populations that have significantly different mean values.

existing rules were being rigorously and impartially enforced. The RTI study, perhaps by design, did not thoroughly and completely examine whether livestock markets have met the conditions for being truly competitive[8].

Regulatory or Legislative Solutions

Are effects of concentration and captive supplies on the cash market big or small? Are they significant? In my opinion these issues will never be resolved with academic certainty. These issues could have been (and have been in one instance[9]) resolved based on a preponderance of evidence, with evidence more broadly defined than in the numerous and expensive GIPSA studies.

Economists generally agree that AMAs tied in any way to the market distort buyer incentives and exacerbate economic efficiency problems in concentrated markets. Economists also generally agree that asymmetric information favoring the large buyer can lead to sub-competitive prices. Market transparency and efficiency of cattle markets would be improved if the big players were required to timely report large transactions, which are akin to unreported insider trading in the stock market. Rules and regulations governing trades in the New York Stock Exchange and the Chicago Mercantile Exchange provide a model for improving transparency and efficiency of livestock markets.

If reducing transactions costs—the costs of haggling over the price of a pen of cattle—is the issue, then why has attention not been directed toward "innovative" solutions that do not distort the market? For example, electronic bidding has promise, but because of potential antitrust issues, such an electronic market may need government oversight.

If offering quality attributes desired by consumers is really the purpose of AMAs, then why have we not developed a new grading system geared to taste, tenderness and other attributes consumers' desire, rather sticking to the largely meaningless USDA grading system (prime, choice, etc).

If market power is an issue affecting the industry, why has GIPSA focused on the market for fed cattle: what about market power exerted by packers or by meat retailers in the wholesale market for beef?

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[8] Unfortunately, much economics jargon is poorly defined and sloppily used in normal discourse. In particular, the word competition has many meanings. In concentrated markets two firms may be "competing" with each other in some sense, but this does not necessarily mean that the outcome measures up to widely accepted requirements for markets to be "competitive."

[9] Based on a preponderance of evidence standard, the Jury in Pickett v. Tyson Fresh Foods, Inc., a Jury found Tyson (previously Iowa Beef Packers, IBP) guilty that Tyson's use of captive supplies depressed the cash market. Peculiar reasoning by the Courts overturned this verdict. See, C. Robert Taylor (2006) "Proving Anti-Competitive Conduct in the U.S. Courtroom: Economic Issues with the Courts' Opinions in Pickett v. Tyson Fresh Meats, Inc.," Journal of Agricultural & Food Industrial Organization: Vol. 4 : Iss. 1, Article 9. Available at: http://www.bepress.com/jafio/vol4/iss1/art9

My recommendation is to correct the three non-traditional (Type II) sources of market power identified above, putting on hold any regulatory or legislative action aimed at size-based (Type I) market power. My view, based on extensive empirical analysis of marketing issues in the cattle industry, is that regulatory or legislative action should:

1. Prohibit AMAs tied to the cash market or to the futures market because they distort buyer incentives
2. Develop rules and regulations similar to those for the NYSE and CME so that large trades will be publicly recorded
3. Widen the trading window so that cash sellers can seek other bids

It is time to quit "studying" the same issues over and over again—they will never be resolved with academic certainty, but this is not the appropriate standard for regulatory action. Effort could more productively be redirected toward seeking innovative ways of trading that are more economically efficient than AMAs or traditional cash transactions, and seeking more meaningful beef quality standards.

At this time, regulatory or legislative solutions to the three cattle industry problems I have pinpointed do not, DO NOT, require breaking up the packers, banning all forms of packer ownership of cattle, or banning contractual arrangements, as long as the arrangements have a predetermined base price and grid, and as long as full market information is made available to all market participants in a timely way.

Returning to the metaphor of competitive athletic events, at this time players do not need to be put on probation or waivers, teams do not need to be broken up and new leagues formed. However, a few relatively small changes in rules governing the game are necessary, and rigorous and impartial refereeing of the rules is needed. Then true competition may be returned to the game.

Thank you.

Appendix A: The Simple Arithmetic of Captive Supply

Marketing agreements with a base price tied to a cash market price distort buyer incentives. This is a very basic Econ 101 causal explanation for a negative relationship between cash price and captive supply. Distorted incentives are apparent to buyers, as is evident from the following statement made by a fed cattle buyer to Randy Stevenson[10]:

> *"... an IBP cattle buyer ... looked at high quality cattle we had on our show list for sale. The market was about $66/cwt in the cash market, based on live weight. (He) was very complimentary of our cattle's quality. He said his hands were tied and he could not offer more for the cattle, despite their above average quality. (He) said* ***'In the old days I would have been able to offer $67.50 for these cattle, but now paying more would screw up 20,000 formula cattle.'*** *It was completely clear to me that (the buyer) was telling me paying a higher price for out cattle would influence prices for cattle bought on a formula contract basis, off the cash market, before the transaction involving our cattle occurred. We lost money in this deal because IBP would not allow its buyer to engage in competitive bidding."*

Here is the simple arithmetic. Suppose that the base price for the 20,00 head of formula cattle was the top-of-the-market price. We know such contracts exist. Also suppose that another packer—maybe a very small packer--had already established the weekly top-of-the-market price at $66.00. If the IBP buyer pays Randy an additional $1.50/cwt ($18/head) for his pen of 1,000 high quality cattle, then the "additional cost" is the extra $18,000 for Randy's cattle, *plus an extra* $360,000 on the 20,000 head of formula cattle. Paying Randy an extra buck fifty on 1,000 head would have cost IBP an extra $378,000. Obviously, IBP would not be willing to bid $67.50 in a $66.00 market. Looked at another way, offering $67.50 for Randy's pen of high quality cattle would have been the equivalent of offering $97.50/cwt in a cash market without the captive arrangement.

Such arrangements obviously soften bids, in this illustration costing Randy $18,000. In the lingo of economics, marginal cost of slaughter cattle is higher to the buyer because of the marketing agreements tied to cash price, causing cash price to be lower than it would be without such captive arrangements.

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[10] Affidavit by Randy Stevenson, dated October 11, 2002.

Testimony of
Joy Philippi
Pork Producer
Bruning, Nebraska

On behalf of

National Pork Producers Council

To

United States House Committee on Agriculture
Subcommittee on Livestock, Dairy and Poultry

April 17, 2007
Washington, D.C.

INTRODUCTION

The National Pork Producers Council is an association of 43 state pork producer organizations. NPPC is the voice in Washington for the nation's pork producers.

The U.S. pork industry represents a significant value-added activity in the agriculture economy and the overall U.S. economy. Nationwide, more than 67,000 pork producers marketed more than 103 million hogs in 2005, and those animals provided total gross receipts of $15 billion. Overall, an estimated $20.7 billion of personal income and $34.5 billion of gross national product are supported by the U.S. hog industry. Economists Dan Otto and John Lawrence at Iowa State University estimate that the U.S. pork industry is directly responsible for the creation of 34,720 full-time equivalent jobs and generates 127,492 jobs in the rest of agriculture. It is responsible for 110,665 jobs in the manufacturing sector, mostly in the packing industry, and 65,224 jobs in professional services such as veterinarians, real estate agents and bankers. All told, the U.S. pork industry is responsible for 550,221 mostly rural jobs in the U.S.

The hog industry in the United States has seen rapid structural changes in recent years, yet total hog numbers have trended up since 1990. In 1990, inventories were 54.5 million head; data from December 2006 showed inventories over 62 million head. And in 2006 2.74 billion pounds of pork and pork variety meats were exported; U.S. consumers purchased 18.8 billion pounds of U.S.-produced pork. Domestic consumption of pork in 2006 was 3 billion pounds higher than it was in 1990; exports were 2.2 billion pounds higher than they were in 1990.

The U.S. pork industry today provides nearly 21 billion pounds of safe, wholesome and nutritious meat protein to consumers worldwide. In fact, 2006 will be the fifth consecutive year of record pork production in the United States, and all indicators point to another record in 2007.

Exports of pork also continue to grow. New technologies have been adopted and productivity has been increased to maintain the U.S. pork industry's international competitiveness. As a result, pork exports have hit new records for the past 15 years. In 2006, exports represented nearly 15 percent of production.

The U.S. pork industry has enjoyed unparalleled prosperity over the past three years. According to estimates by Iowa State University, average farrow-to-finish producers completed their 35^{th} consecutive profitable month in December (See Figure 1) and made an average profit of $22.17 per head over that period. New Iowa State estimates based on modern technology and production coefficients indicate that these operations have remained profitable through March of this year in spite of near-record feed costs.

Pork cutout values reached record levels in 2004, and Iowa-Minnesota cash hog prices have been near-record high on several occasions since that time. As can be seen in Figure 2, Iowa-Minnesota hog prices have broken the downtrend of the 1990s and established a new, higher trend over the past four years. This new trend was started by a surge in domestic and export demand in 2004, with domestic demand bolstered by the popularity of low-carb, high-protein diets and export demand driven by better market access for U.S. products, a weaker U.S. dollar and U.S. products better tailored for export markets.

INDUSTRY VIEWS ON MARKET STRUCTURE

It is against this backdrop of financial success that we offer our views on market structure. But first we would ask: Is legislation that would limit producers' market-access options a solution in search of a problem?

There is no doubt that the structures of the U.S. pork industry and U.S. pork and hog markets have changed, but we urge Congress to focus not on structural issues but on the more important market efficiency measures of conduct and performance as you deliberate the wisdom of government intervention. While the 1990s were a difficult time for U.S. pork producers, we urge you to make policy based on the realities of today, not the past. This industry went through a major restructuring in the '90s, changes driven by new consumer demands, new technology and rationalizations of both old-line packing and old-line production capacity. Such sweeping changes are always painful and should not be forgotten, but they must also be kept in context and not used to forever drive a desire for the "way things used to be."

CAREFULLY AND THOROUGHLY CONSIDER RECENT RESEARCH AND INQUIRIES

Congress has invested significant resources in researching the current situation in livestock markets. Much of that research is relatively new, and we have had little time to consider what it tells us. We would urge Congress to move slowly as USDA and the industry digest and consider new knowledge and apply the findings.

Foremost among these is the recently released Grain Inspection, Packers, and Stockyards Administration (GIPSA) Livestock and Meat Marketing Study. This comprehensive and complex piece of research cost U.S. taxpayers $4.5 million. We believe that such a large investment of taxpayer dollars warrants careful and complete consideration of the study's findings and that any criticism should not be based on those findings but on the data and/or methods that were used. Let's learn from this study instead of making it a political football.

In addition, USDA's Office of the Inspector General (OIG)) study of GIPSA, completed in 2005, was a significant investment of federal funds. What is the status of GIPSA's response to the OIG audit? We know that the management team at GIPSA changed just before the audit was released, and we believe that GIPSA Administrator James Link has made substantial changes in the way GIPSA goes about its prescribed duties. However, we believe Congress should know specifically what has been done and how that is going to change GIPSA's future efforts to enforce the Packers and Stockyards Act.

Since 2000, the federal government has made major investments to improve price reporting by implementing the Livestock Mandatory Reporting Act. The express purpose of that Act and the mandatory price reporting system is to increase the transparency of livestock markets by requiring the reporting of prices by covered packers. We believe the system has accomplished that goal and that the refinements enacted in 2006 will further that cause. We await with anticipation USDA's new proposed rule on the price reporting act, which now includes several swine reporting enhancements that we advocated. Let us work to make this system better before we proceed with other actions.

All of these efforts have also involved significant investments on the part of the private sector. Producers and packers responded to lengthy, detailed GIPSA questionnaires as part of the livestock and meat marketing study. Data on millions of transactions was provided, all of which took valuable time and manpower. We should allow these investments to come to fruition.

Congress also should answer the question: What have past congressional efforts to make markets more competitive accomplished? From our perspective, the answer is not much. The obvious follow-up is to ask whether that lack of results is due to a lack of effort or is it that markets are, in fact, quite competitive. (We believe the answer may be both.)

An example of such past efforts is the 1999 appointment of a Special Counsel to the Assistant Attorney General in charge of the Anti-Trust Division of the Department of Justice. What has this person done? What has this new position contributed to the level of competition in agricultural markets? We have seen no evidence that this Special Counsel has actually done anything to make agricultural markets more competitive or transparent. Before proceeding to add more layers of bureaucracy, why not find out what this Special Counsel has done and what changes have been made at GIPSA – and to what effect?

FOCUS ON CONDUCT AND PERFORMANCE

The focus of most debates regarding competition has been the number and market shares of the various participants. That is, many try to use industry structure to draw direct conclusions that firms behave in certain ways and that prices and quantities are moved away from their competitive optimums. Structure should not be used to measure whether there is competition; Congress should look at performance of the market.

The pork production and packing sectors are more concentrated than they once were. Some regions have only one or two packers bidding for hogs. Some producers now control substantial shares of the live hog supply. But none of those mean that market power is being exerted on hog or pork prices.

The key is whether sufficient competitive pressure exists to make the fewer packers and fewer producers behave in a manner that approaches competitive norms and yields competitive prices and quantities. This can only be measured by looking at actual transactions to determine how firms act and what the results of those actions are.

The recent GIPSA Livestock and Meat Marketing Study did just that. Instead of looking at changes in ownership and market shares over time, the study examined transactions and looked at conduct and performance. We now need to step back and consider the methods and results of that research and, perhaps, ask and answer additional questions about those results.

This type of research is costly and time-consuming and thus hasn't been done often. It has been 10 years since GIPSA's previous such effort, and that time span is, we believe, too long. We ask that Congress consider an ongoing level of trend research. We believe doing so would provide much more timely information for policy decisions and possibly reduce the long-term cost of the research and data acquisition by making both more "standard operating procedure" instead of requiring specialized actions.

One particular need is for standardized data reporting if this type of study is going to be done in the future. Companies should be free to use any kind of internal accounting they wish, but if researchers are to make sense of these markets, it would help if the data generated by those systems were at least reasonably comparable. Other government agencies, most notably the SEC, require some level of standardized financial reporting. The livestock sector already has mandatory price reporting. If this type of research is to be conducted, GIPSA should require line-of-business financial reporting by meat companies to provide accurate, usable data from which to derive meaningful results.

DO NOT USE A POLICY BROAD BRUSH FOR ALL SPECIES

One of our consistent requests has been to avoid "one-size-fits-all" approaches and to address the separate species as the unique businesses they are. There is some thought found in pending legislation that takes aim at contractual issues in other industries. If those problems exist, by all means fix them. But we do not support applying those solutions to the pork industry when these contractual issues are not readily apparent in our industry.

FULLY CONSIDER UNINTENDED CONSEQUENCES

Virtually any well-intended public-policy action has unintended consequences, and part of the art of public-policy is balancing the costs and benefits of any public-policy proposal. In the area of competition and industry structure issues, there are a number of proposals that will have an adverse impact on pork producers.

As an example, consider the idea of requiring packers to buy at least 25 percent of their hog supplies on the spot market or through negotiated sales. First, the GIPSA Livestock and Meat Marketing Study came to the clear conclusion that such a requirement would make producers and consumers worse off and would leave packers not better off. The study shows that nobody wins from restrictions on the use of alternative marketing arrangements – non-negotiated trades.

The practical implications of such a requirement are daunting as well. Would the 25 percent be measured daily? Weekly? Would producers be required to sell 25 percent of their hogs through negotiated trades to provide the 25 percent that packers are required to buy through negotiated trades? If not, and since only 11 percent of all hogs are sold through negotiated trades now, which producers would have their contracts terminated to force their hogs into negotiated trades? And what happens when those contracts are terminated? Would the financing that was contingent on those contracts be withdrawn by risk-averse lenders?

While it is probably never possible to consider all unintended consequences, it would be foolish to ignore those that can be readily identified. We ask Congress take time to identify and consider them.

RECOGNIZE THAT OUR INDUSTRY STILL FACES GREAT CHALLENGES

The U.S. pork industry does not need more to worry about at the present time. Our producers and packers have been profitable in a very competitive meat sector. Domestic pork sales are good, and our export business is growing rapidly, and given trends in world populations and economic performance, we believe this growth will continue.

But we face many challenges. Corn prices driven by subsidized ethanol production are the most immediate threat to the economic viability of pork producers. Production costs have increased by roughly $10 per hundred pounds since just last fall. The impending mandatory country of origin labeling law promises more costs, especially for producers who import feeder pigs from Canada. The specter of animal rights-driven legislation dictating on-farm production practices hangs over us all. Not only does it threaten to add another layer of costs, but it will most assuredly drive some livestock production from U.S. soil. Finally, environmental regulations are increasingly stringent and impose costs that are almost universally better-handled by large operations thus putting our smaller members at a competitive disadvantage.

Anything that Congress does must be beneficial to this industry as a whole. Punitive actions against packers do not necessarily benefit pork producers in the long run unless the packer in question is very clearly in the wrong. We have seen no evidence of that kind of behavior at this point, and Congress must proceed with caution, weighing the costs and benefits of such important public-policy decisions.

The entire pork industry chain must work together for us to remain competitive in the global marketplace – and this means producers, packers and retailers.

CONCLUSION

We hear a few pork producers and several lawmakers frequently claim that "the system is broken and the market is not working!" When we ask what aspect of the market is not working or how the system is broken, though, we get vague answers. It is as though we respond "Why?" to a concern and receive an exasperated "Because!" in reply. Such an answer provides no help to us in solving the problem. It doesn't even clearly identify the problem.

In this regard, we are reminded of Alice in Wonderland and the Cheshire Cat. When Alice asks "Which road do I take?" the cat wisely replies, "That depends a good deal on where you want to get to." Alice's response of "I don't much care where" elicits an even wiser response form the smiling cat: "Then I guess it really doesn't matter ... which road you take."

It is imperative that Congress and the pork industry reach a common understanding of where we want to go before we begin choosing roads. When that choice is clearly made, we must then decide which road gets us to the chosen destination at the least cost and in a manner that provides the greatest value to our customers. We believe the time is right for contemplation and collaboration, and we stand ready to fully participate in that process.

Figure 1

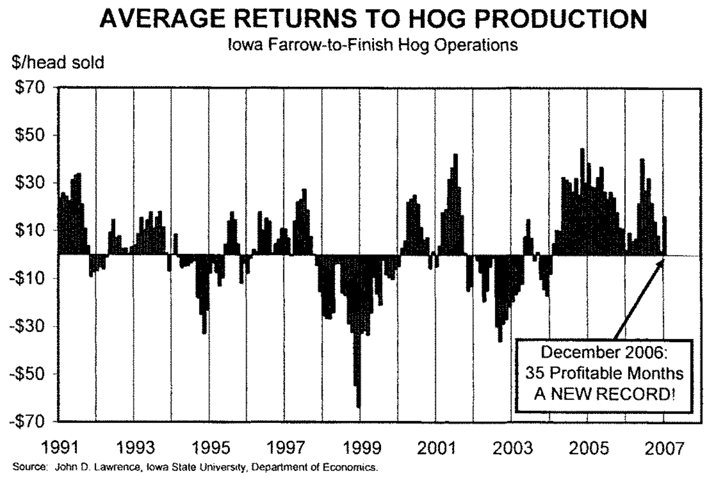
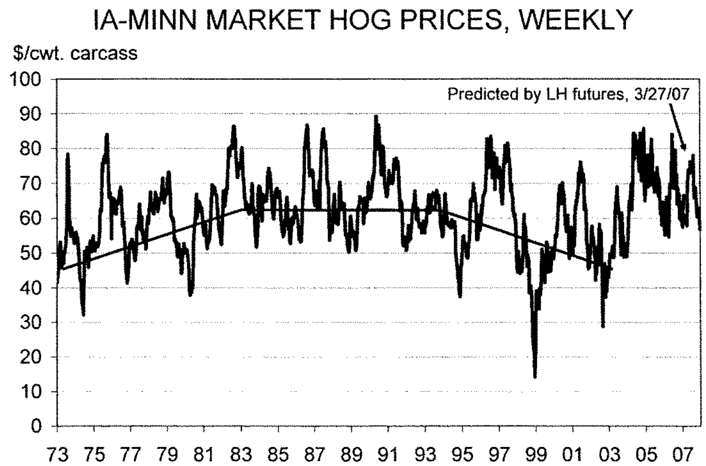

AVERAGE RETURNS TO HOG PRODUCTION
Iowa Farrow-to-Finish Hog Operations
$/head sold
$70
$50
$30
$10
-$10
-$30
-$50
-$70
December 2006:
35 Profitable Months
A NEW RECORD!
1991
1993
1995
1997
1999
2001
2003
2005
2007
Source: John D. Lawrence, Iowa State University, Department of Economics.

Figure 2


IA-MINN MARKET HOG PRICES, WEEKLY
$/cwt. carcass
100
90
80
70
60
50
40
30
20
10
0
73 75 77 79 81 83 85 87 89 91 93 95 97 99 01 03 05 07
Predicted by LH futures, 3/27/07

NATIONAL CHICKEN COUNCIL
1015 FIFTEENTH STREET NW, SUITE 930
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PHONE: 202-296-2622
FAX: 202-293-4005

STATEMENT REGARDING

LIVESTOCK INDUSTRY MARKET STRUCTURE

HEARING OF THE LIVESTOCK, DAIRY, AND POULTRY SUBCOMMITTEE HOUSE COMMITTEE ON AGRICULTURE

THE HONORABLE LEONARD L. BOSWELL
SUBCOMMITTEE CHAIRMAN

WILLIAM P. ROENIGK
NATIONAL CHICKEN COUNCIL
WASHINGTON, DC

APRIL 17, 2007
WASHINGTON, DC

Good morning, Chairman Boswell, Congressman Hayes, and members of the Subcommittee. Thank you, Chairman Boswell, for the opportunity to participate in this important hearing regarding the issue of the market structure of the livestock industry. On behalf of the National Chicken Council, I appreciate your invitation to provide comments on the market structure of the U.S. chicken industry.

My name is Bill Roenigk and I am Senior Vice President of the National Chicken Council. Companies that produce and process about 95 percent of the young meat chickens (broilers) in the United States are members of the National Chicken Council. I am pleased to have the opportunity to share with you information about the market structure of the U.S. chicken industry. For my statement for today's hearing, I will use the term "chicken" and "broiler" somewhat interchangeably.

More than half a century ago, as farmers moved more and more away from dual purpose chickens (table eggs and meat) and moved toward specialized breeds for table eggs and for producing meatier chickens, a new industry and market structure began to emerge in poultry farming. Chicken producers did not go to strategic planning sessions or consult with business organization experts to decide they needed to adopt the concept of vertical integration to improve their livelihoods and lessen the economic ups and downs in the chicken market cycle. They sought greater stability and predictability in their incomes and for their investments. With access to only limited capital it was very important to lessen market risk by sharing those risks with others in the production process. While it may make a better report to state that various parts of the chicken business came together in a proactive manner, the actual situation for most, but not all, companies was that coordinating the various parts of a business was, in large measure, a reactive process. More specifically, feed mills providing feed for farmers growing broilers learned that the best way to assure payment for the feed at the end of a broiler growout cycle was for the feed mill to help find a processing plant to slaughter the broilers when the birds reached market weight. Because the economics of feeding broilers requires prompt movement to market when they reach market weight, the broiler grower is at a distinct disadvantage if the processing plant is working at over-capacity or the wholesale market for dressed chicken is depressed. By coordinating growing, processing, and marketing the surge and gaps in live production could be minimized. The chicken industry, as it began to coordinate production, processing and marketing 50 years ago, was participating in just-in-time concept, but they just didn't know it until the Japanese car-makers labeled their concept decades later.

Contracts with growers offer many very important benefits. These benefits and advantages include substantially reduced market risks; quicker and more thorough understanding of production requirements; better access to capital; more reliable and predictable income flows to labor, management, and investment; and better opportunities to leverage success to expand and/or diversify farm operations.

Family farmers who contract with chicken companies have benefited in good measure over the past six decades. More than 25,000 family farms currently contract with companies to raise broilers and can do so more confidently because, to a very large degree, they are insulated from the risks of the chicken marketplace. Contract growers are basically guaranteed a fixed payment plus a bonus for above average performance. University studies have found that returns on investments for contract broiler farmers are very comparable to returns on investments for chicken companies. A young farmer starting out or a farmer with limited equity can obtain a loan to begin growing chickens because he/she can use the contract as collateral. Depending on the farmer's situation, more growout houses can be added to expand production and, in many cases, the farmer can mesh chicken growing with other aspects of the farming operation. Financial institutions tell the National Chicken Council that the default rate of contract growers is very low, perhaps, the lowest in all of agriculture.

Another measure of the successful relationship between companies and contract growers is that the majority of companies have a waiting list of growers who are requesting to add to existing growout housing capacity or farmers who wish to begin broiler growout operations. If the system was not a favorable one, would these waiting lists exist year-after-year and decade-after-decade?

Vertical integration for the chicken industry has stood the test of time quite well. The chicken industry has over the past six decades provided consumers at-home and abroad with an abundance of wholesome, affordable, and nutritious food. In 1955, broiler production was 2.4 billion pounds, ready-to-cook weight basis. This year (2007) broiler production will be 35.2 billion pounds or more than 14.5 times the quantity in 1955. Today, the price of chicken to consumers, adjusted for inflation, is less than one-fourth the cost of chicken 50 years ago. Another way to measure the cost of chicken to consumers is to note that in the mid-1950s, it took the average manufacturing worker 19 minutes of work time to earn enough in wages to buy a pound of chicken. Today, the same worker needs to work less than four minutes to purchase a pound of chicken.

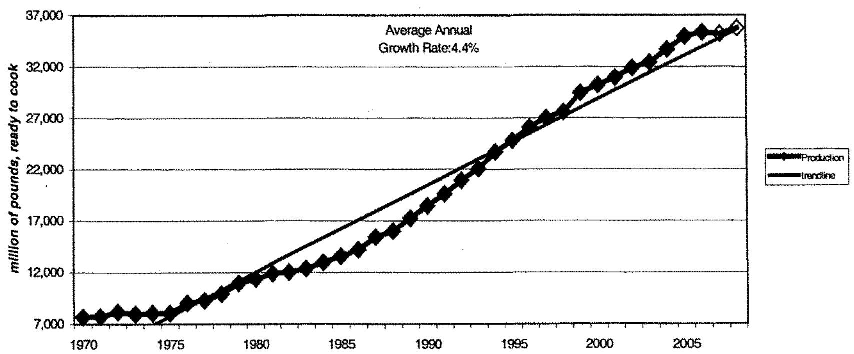
There have been many studies conducted about the broiler industry regarding market structure, competition, and related issues. One such study is considered a landmark report. It is the *Dynamic Factors in Vertical Commodity System: A Case Study of The Broiler System* by B.W. Marion and H. B. Arthur at the Ohio Agricultural Research and Development Center (1973). This study concludes "the primary function of almost any industry can be thought of as efficient bringing together—the integrating—of the resources, products, and services needed to provide an end product that will best satisfy the needs of customers. This is certainly true of the broiler system. And the dramatic reduction in the cost per pound of broilers and concomitant increase in consumption suggest that the system has performed well in accomplishing this task."

Although that study was done more than 30 years ago, I believe that conclusion is even more valid today. Consumption of chicken has more than doubled from 30 years and is the highest of any meat, measured on a retail-weight basis. Further, consumers today have an ever widening variety of chicken products that are more convenient, more nutritious, more affordable, and have a higher level of food safety. Vertical integration for the chicken industry very much facilitates end-market signals back through the system and is the basis for the more than 50 years of successfully serving the consumer.

Chairman Boswell, Congressman Hayes, and members of the subcommittee, I appreciate the opportunity to share the broiler industry's story with you. You have much to deliberate with respect to various issues involved in the upcoming farm bill. I respectfully suggest that trying to improve the market structure of the chicken industry should not be a high priority for the

Subcommittee nor Congress. The National Chicken Council does not see the need for new or additional laws nor USDA regulations that would involve government further in the grower-company business relationship. Nonetheless, if you do have concerns or questions about the chicken industry with respect to this issue, the National Chicken Council would very much appreciate the opportunity to work with you to appropriately and adequately address those issues or concerns.

U.S. Broiler Production
1970 to Estimated 2008



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Testimony

on behalf of the

National Cattlemen's Beef Association

with regard to

Market Structure of the Livestock Industry

submitted to the

United States House of Representatives - Committee on Agriculture
Subcommittee on Livestock, Dairy, and Poultry

The Honorable Leonard Boswell, Chairman

submitted by

Mr. John Queen

President
National Cattlemen's Beef Association

April 17th, 2007
Washington, D.C.

BEEF USA National Cattlemen's Beef Association

Mr. Chairman, members of the Committee, my name is John Queen and I am a cattle producer and livestock market operator from Waynesville, North Carolina. I am President of the National Cattlemen's Beef Association (NCBA) and am pleased to be with you today to discuss the market structure of the livestock industry.

When it comes to market structure and competition issues, NCBA's position is simple – we ask that the government not tell us how we can or cannot market our cattle. The way we market cattle has changed significantly over the years, and it has come from a recognition within our industry that we are not just cattle producers, but beef producers, and must be in tune with what our consumers prefer to purchase from their local retail meat case. This focus on consumer preferences has led to many innovative marketing programs that have improved the quality of beef, given the consumer what they are asking for, and made many of America's ranchers more profitable and efficient. Some of these innovations have come in the form of alternative marketing arrangements (AMAs) such as forward contracting, marketing alliances, and packer ownership. These marketing arrangements offer producers the opportunity to get paid for the value that they add to the animal.

Historically, cattle were marketed in lots or pens with every animal in the lot receiving the same average price. Since producers did not benefit from providing higher quality beef, they had no incentive to supply a higher quality product or meet consumer demands. As our industry struggled through the 1970s, 80s, and early 90s with decreasing demand, we did not see any market driven signals to produce the leaner, more consistent beef the consumer demanded. Many producers, however, took significant steps to produce high quality lean beef by making investments in genetics, management, and herd health to meet the demand we began to recognize. To pay for this investment, producers demanded a premium. This demand for premiums has manifested itself today into a system of value-based marketing that is reflected in the multitude of premiums, discounts, grids, contracts, formulas, and alliances that have become commonplace in the beef industry. Some of the marketing programs that producers participate in are:

- Certified Angus Beef
- U.S. Premium Beef, Ltd.
- Ranchers' Renaissance
- Harris Ranch

These are just a handful of the innovative marketing programs available. Many of the country's ranchers have made the choice to participate in a program that will offer them an opportunity for a larger share of the consumer's dollar. These arrangements are market and consumer driven, and in many cases, led by producers themselves. There are many more, particularly in areas where producers are teaming with other segments of the industry to take advantage of national, regional, and even niche market opportunities ranging from breed or genetics programs to natural and organic production. Process and source verified programs are utilizing today's technology, such as electronic identification of animals, allowing producers to become more efficient at raising high quality animals that yield the beef products that consumers will pay a premium for.

This growing number of innovators are ranchers who came together in a proactive way to address their desire for a growing, viable beef industry by developing bold new marketing strategies. Not only are ranchers, feeders, and packers working together in these programs to market cattle, but this innovation is also visible in the meat case. Consumers not only demand leaner, tender, more consistent products, but they demand convenience as well. The meat case is beginning to be filled more and more not by fresh beef, but by products that are pre-prepared and ready for the microwave.

In addition to being responsive to our consumers, participation in these marketing arrangements provide the producer with several tools that help improve their operations and herd management in an effort to capture the premiums I mentioned above. The ability to manage price risk is probably one of the most valuable of these tools. Taking advantage of marketing arrangements such as forward contracting allows producers to make a price that allows them to be profitable. If the price does not fit their needs, they can walk away and find another buyer. Being a "price maker" rather than a "price taker" puts ranchers in control of their business. Traditional routes of cattle marketing do not always offer that flexibility. Knowing that you have a guaranteed buyer and a price you can live with makes it easier to manage your day-to-day business and focus on operational improvements instead of always worrying where your money will come from.

Along those same lines, many producers rely on operating loans from their local bank to get the financing needed to run their operation from year to year. If a producer can go to their banker and show that they have secured a buyer for their cattle and can obtain a premium for those cattle, the banker is much more inclined to approve that loan than if he were dealing with a producer with no marketing plan.

Entering into these marketing agreements also has the added bonus of being able to pick up on operational efficiencies that make the most of your cattle, streamline your operation, and potentially save money. Many ranchers who participate in these programs get information back from the feedlots that tell them how their cattle performed while being fed. Information also comes back from the packer in the form of yield and quality grades. This information is critical in managing the herd to ensure that the traits which provide the higher quality animals and beef are the ones in which you focus on.

The benefits of alternative marketing arrangements are being seen everyday in the cattle business, and they were recently supported by the results of the Grain Inspection Packers and Stockyards Administration's (GIPSA) Livestock and Meat Marketing study conducted by RTI International and released in February. This three and a half year study was funded by four and a half million taxpayer dollars and was billed as the "definitive answer" on these issues. The study supports what many ranchers across the country have known all along – a market-driven system works. This study was based on over half a million transactions representing more than fifty-eight million head of cattle[1]. The overwhelming conclusion of this study is that overall, alternative marketing arrangements help all sectors of the industry, not just those that participate.

[1] RTI International, *GIPSA Livestock and Meat Marketing Study,* Vol. 1, Executive Summary, page 4

With all of the taxpayer money and time invested in this project, I think the livestock industry and Congress need to give serious consideration to its conclusions. The report states that the leading reasons producers participate in alternative marketing arrangements are the ability to buy or sell higher quality cattle, improve supply chain management, and obtain better prices[2]. All three of these tie into the topics we discussed above – higher quality cattle produce the beef products that the consumers desire. Providing this consumer preferred product allows us to capture more of that consumer dollar in the form of a premium. That bigger share of the consumer dollar is being passed down to the producer. The producer is getting a better price for their cattle and can use that money to continue to improve their operation.

When talking about improved supply management, we have to once again go back to the consumer. The consumer does not come into their local Safeway looking for "Rancher's Reserve" beef only on Tuesdays. The consumer demands the convenience of picking up a package of "Rancher's Reserve" beef any day of the week. To meet that demand, the retailer and packer need a steady and consistent supply of cattle that meet the qualifications of the store-branded program. This allows them to ensure this product is available daily. If the packer is limited in its ability to source these cattle, they cannot ensure that there will be a steady supply of animals coming through their processing plants. In turn, they can not supply "Rancher's Reserve" beef everyday, and the consumer chooses another source of protein for the center of the plate.

Thus far, I have only talked about alternative marketing arrangements and the benefits they have provided to our industry. One of the conclusions in the study, however, was that only a minority of the cattle marketed to the twenty nine largest packers was done so with AMAs. RTI International's results show that approximately twenty nine percent of cattle are marketed through marketing agreements, almost five percent through forward contracting, and only five percent were packer owned. Approximately sixty two percent of cattle marketed were done so through the cash or spot market[3].

Auction markets are a critically important part of the U.S. cattle industry. They have been the primary arena for marketing cattle for over a hundred years. In this method, a willing seller takes the highest bid for his cattle when he decides it is the right time to bring them to the auction barn. Ranchers who market this way cite several reasons for their choice. One reason is independence. By using the cash or spot market, you have no restrictions or cattle quality concerns that would keep you from selling your cattle – unlike marketing arrangements that require certain criteria be met before cattle qualify for filling the contract. Flexibility is also important to these producers. Selling on the spot market gives ranchers the opportunity to participate in market rallies whereas those who have already contracted their cattle lose that opportunity because they are already locked into a price agreement. We must remember, however, that this only gives

[2] RTI International, *GIPSA Livestock and Meat Marketing Study,* Vol. 1, Executive Summary, page 4
[3] RTI International, *GIPSA Livestock and Meat Marketing Study,* Vol. 1, Executive Summary, page 5

them the opportunity to catch the rally. Timing the market is always a difficult task and adds to your price risk.

Even with traditional means of marketing, we have seen innovations and improvements that have been market-driven. One of these innovations is video livestock auctions. With this method, ranchers can auction their animals by video and reach customers across the country and not just those that come to the sale barn that week. This style of spot market stemmed once again from ranchers who produce a higher quality product and want to make sure they are getting paid for the value they are adding to their cattle.

It is always a bonus when both the consumer and rancher can benefit from innovations in the cattle industry. Many of these new marketing methods and tools are great successes. The consumer is getting the beef products they prefer and ranchers are getting paid for that added value. The results are quantifiable as shown by the Livestock and Meat Marketing Study and by the numbers. Demand for beef has grown substantially over the past decade – twenty percent since 1998. Consumer expenditures on beef are at record levels of seventy-one billion dollars for 2006. More importantly, consumer confidence in beef is at ninety-one percent. This is greater than it was in September of 2003 (before the December 23rd BSE case in Washington state) when it was eighty-eight percent. All of this has translated into profitable market conditions for ranchers. In 1980, the average price for a 650 pound feeder steer was $73.11 per hundredweight. That price dropped to $65 per hundredweight in 1996. We saw tremendous improvement in the market over the next ten years resulting in an average price of $117.73 per hundredweight in 2005 and only a slight drop from that in 2006. This price increase was affected by many things, but one of those factors was meeting consumer demands with alternative marketing arrangements.

Demand is high, prices are at more profitable levels, and the market-driven innovations our industry has put in place are proving successful. Yet today, we continue to discuss legislation that would interfere with a market-driven structure. In today's marketplace, producers need the freedom and flexibility to market their cattle in ways that provide the best return on their investment. As I have already mentioned, ranchers can market their cattle in different ways and see additional economic benefits – all while maintaining a strong and viable cash market. The study shows that government-enacted restrictions on the market-driven system would be detrimental to all sectors of our industry[4].

The study concludes that reductions or restrictions on alternative marketing arrangements would cause a decrease in the supply of cattle, a decrease in the supply and quality of beef, and an increase in retail beef prices[5]. These are all results that would set our industry back rather than move it forward. The study continues by concluding that feeder cattle prices would decrease because of higher operating costs resulting from

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[4] RTI International, *GIPSA Livestock and Meat Marketing Study,* Vol. 1, Executive Summary, page 3

[5] RTI International, *GIPSA Livestock and Meat Marketing Study,* Vol. 1, Executive Summary, page 8

restrictions on alternative marketing arrangements[6]. That means that in the end, it is the individual cow/calf producers across this country that will bear the brunt of government restrictions. At the same time, we continue to see an increase in feed costs due to competition with ethanol for corn, and an increase in fuel costs. In a time of these additional costs and strains on the bottom line, the last thing we need to do is think about adding more burdens to our ranchers. On the surface, these restrictions and bans on alternative marketing arrangements, including a ban on packer ownership of cattle, look appealing, but in both the short and long-term, they will unintentionally hurt those it was intended to protect.

Rather than talk about restrictions on innovation, NCBA would prefer to talk about ways we can partner with Congress to keep the marketplace working fairly and efficiently. One program that has proven useful in making the marketplace more transparent and fair is mandatory livestock price reporting (MPR). Mandatory price reporting has been in place since 2001, and since then we have seen increased and more readily understandable information regarding pricing, contracting for purchase, and supply and demand conditions for livestock. This user-friendly information is essential to ranchers as they evaluate the marketplace and determine when and how to sell their cattle.

Fortunately we were able to work with Congress to get mandatory price reporting reauthorized last year after more than a year of the program being voluntary. As of today, however, we have still not seen the final rule from USDA that will once again require mandatory reporting. Although we appreciate the beef packers' continued voluntary reporting, we would like to see the rule to re-implement the program expedited and put back in place. We also thoroughly studied the Government Accountability Office's (GAO) report on mandatory price reporting. We thought the program was appropriately reviewed and that the GAO's recommendations were productive. We let the Agricultural Marketing Service (AMS) at USDA know of our support of the recommendations and have urged them to implement those changes as quick as possible. They already have several in place and we will continue to monitor their progress. Mandatory price reporting needs to remain an effective, viable, and reliable tool for producers to utilize when making their marketing decisions.

NCBA continues to look at additional legislation and programs that will help foster more competition in our industry. One of those priorities is the ability for small, state-inspected beef packers to ship their product across state lines. Smaller plants that currently operate under state-inspected programs are precluded from taking advantage of market expansion because they cannot ship across state lines. In order to take advantage of interstate shipment of their products, they must first make the necessary, and often expensive, steps to become federally inspected. NCBA recommends that meat inspected under state programs be accorded the same freedom of movement in interstate commerce that is accorded foreign-inspected imported meat.

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[6] RTI International, *GIPSA Livestock and Meat Marketing Study,* Vol. 1, Executive Summary, page 8

This change would provide smaller packers with the ability to expand their trade area and open new markets. Accessing new markets always provides economic benefit, and it will allow these packers to stay viable, grow, and provide more competition in the fed cattle market. These packers will also have the opportunity to develop local, state, or regionally branded beef products, which, in turn, will allow them to benefit from alternative marketing arrangements and help build a niche demand for their products.

Another avenue where Congress can be helpful in growing the cattle industry is in regards to trade. We just discussed how access to new markets can be economically beneficial, and in the world market, over ninety-six percent of the consumers live outside of the United States. Your support of the Market Access Program (MAP) and Foreign Market Development (FMD) program will help the beef industry regain demand in markets we lost after the 2003 BSE case, and to develop new markets. Congress can also be helpful in holding our trading partners accountable and making sure trade is fair and based on sound science.

Probably the most effective way for industry and Congress to ensure that the marketplace stays fair and competitive is to just ensure that the laws already on the books are readily enforced. The Packers and Stockyards Act (PSA) was passed to ensure that the marketplace stays competitive. USDA's enforcement of PSA and other anti-trust laws and regulations are critical in identifying, investigating, and prosecuting anti-competitive actions by packers, dealers, markets, and others who fall under its jurisdiction. To add additional support, it is also important that USDA work with the Department of Justice to bring to justice those who collude against the individual rancher.

There has been evidence over the past number of years that USDA has not been as effective as it could be in investigating allegations of anti-competitive activities, and even less effective at recommending cases for prosecution. We believe some beneficial changes have been made, but we encourage Congress to look at ways to help USDA overcome this issue and put the personnel and resources in place to make sure all cases are actively worked through the legal system. Increased activity in this effort would go a long way in discouraging people from engaging in anti-competitive acts.

NCBA supports a free market system and we trust in the ability, adaptability, and innovative skills of the U.S. rancher to be able to prosper in a relatively unregulated domestic and international marketplace. We rely on federal regulators to ensure that the marketplace is free from anti-trust, collusion, price fixing, and other illegal activities that damage the viability of the market and interfere with market signals, but also to keep the playing field level for cattle producers.

Our membership has consistently said that we want access to business opportunities that will help us improve our bottom line. Accordingly, keep in mind that for every agreement made by a packer, there is an individual rancher on the other side of that transaction who has decided that the agreement is in their own best interest, and they should be allowed to conduct that business privately, just like any other industry. Those cattlemen have exercised their personal right to willingly engage in that agreement because they perceive it to add value to their operation, to their business, to their livestock, and ultimately to their family. That opportunity in the end will help to continually improve their management, genetics, and long-term profitability. The opportunity to engage in and benefit from new advancements is good for the individual producer and good for the industry as we strive to supply the consumer with beef products they demand.

Our industry's reliance on a market-based, market-driven, consumer focused approach has and will provide opportunities for beef producers to be successful. By meeting customer needs, we can best create opportunity for ourselves. With all the choices today's consumers have, we must strive to meet their needs and demands. We have to compete in a global environment and meet global customer needs. To do that, we need to have the flexibility to adjust business plans and practices that help us meet global demand. We must continue to have a world class infrastructure that ensures safe, healthy, and wholesome beef to consumers. We must have a business and regulatory climate that ensures commerce is fair, open, transparent, and not overly burdensome. In the end, we must have a government that works to help our industry and not one that limits or removes choices for cattlemen in the marketing of their cattle.

AMERICAN MEAT INSTITUTE

Testimony of

J. Patrick Boyle
President and C.E.O.
American Meat Institute

Before the
House Committee on Agriculture, Subcommittee on Livestock, Dairy, and Poultry

Regarding
Review of Competition in the U.S. Livestock and Meat Markets

April 17, 2007

Good afternoon Mr. Chairman, Ranking Member, and Members of the Subcommittee. Thank you for allowing me the opportunity to appear before this Subcommittee. My name is Patrick Boyle and I am president of the American Meat Institute (AMI). AMI has provided service to the nation's meat and poultry industry -- an industry that employs more than 500,000 individuals and contributes more than $100 billion in sales to the nation's economy – for more than 100 years.

AMI's 250 members include the nation's most well-known meat and poultry food manufacturers. Collectively, they produce 90 percent of the beef, pork, veal and lamb food products and 75 percent of the turkey food products in the U.S. Among AMI's member companies, 60 percent are small, family-owned businesses employing fewer than 100 individuals and some are publicly trade and employ tens of thousands. These companies operate, compete, sometimes struggle and mostly thrive in one of the toughest, most competitive and certainly the most scrutinized sectors of our economy: meat and poultry packing and processing.

AMI appreciates the opportunity to provide perspective and hopefully insight into the competitive pressures and developments facing our member companies. Specifically, members of AMI have concerns about legislative and regulatory efforts to apply government directed controls on an industry whose members compete intensely with each other and for a greater share of the consumer's food dollar from other segments of agriculture. These concerns stem from proposals that would 1) prohibit the ownership of livestock by a packer and unduly regulate investment, 2) prohibit or restrict contracting, marketing agreements, or other livestock marketing arrangements that producers and packers rely on, and 3) establish an arbitrary cash purchase mandate and an involuntary exposure to the volatility of the cash market. This testimony also highlights some of the findings of one of the most comprehensive and exhaustive studies of the industry, which was recently completed for USDA.

Ban on Packer Ownership of Livestock and Marketing Agreements will be Detrimental to the Entire Livestock Sector

AMI is opposed to legislative and regulatory measures that would restrict livestock producers' marketing options and procurement methods of packer and processors. We believe the strength of the livestock marketing system in the U.S. is the flexibility it provides to producers, packers/processors and retailers in responding to market signals and offering increasing variety of alternatives for the producer through to the consumer. The wide range of options available to producers and packers provides a means for market signals and consumer demands to work rapidly and efficiently, while providing opportunities for all market segments. This flexibility has benefited consumers and for producers. Producer options include: spot market transactions, production contracts, cooperatives, bargaining associations, marketing agreements, and other options that allow them to align themselves with consumer demands through contractual arrangements to manage risk and produce a desired product.

These measures aid a livestock producer's ability to manage price and weather risks, access credit, and participate in valued-added, branded product lines. Within the last decade, we have witnessed significant sales growth in branded beef and pork products and the corresponding response to market signals by producers to increase production.

We believe that the most appropriate government role in today's livestock marketing system is to enforce the existing laws and regulations that ensure fair and nondiscriminatory business practices among producers and packers, while allowing producers the freedom of choice on how best to market their livestock. The government should exercise its current and vast authority under the Sherman Act, the Clayton Act, the Robinson-Patman Act, the Packers and Stockyards Act and other state statutes.

Producers and packers utilize contracts, cash negotiations, marketing agreements, and other arrangements for many reasons and often for very different reasons than their neighbors or other producers across the country. Each producer and packer's operation, skills, market position, and experiences are different and require a livestock marketing or procurement plan that is appropriate for their model. Opponents of these agreements would like Congress to believe that there exists a monolithic dogma among producers as to their means of marketing livestock. The truth is better reflected in John Kenneth Galbraith's words which define a market as "a series of opinions." The wide ranging opinions of producers and packers about the market and its direction are what make it work so effectively in allocating risk, reward, and resources.

The many marketing options provide producers the ability to diversify or concentrate their livestock marketing plan to best match their skills, experiences, capital base, or tolerance of weather and price risks. One of the more common reasons producers and packers enter arrangements is to manage price risks to aid in the access of credit and capital. As the graph in

Attachment A shows, agricultural commodity markets can be extremely volatile and experience very wide price swings – sometimes up and sometimes down. Producers and packers recognize that managing this volatility is critical to their long-term economic well-being and livelihood. This is true across agriculture, where more than 40 percent of all agricultural goods are produced via contracts or related agreements.

To illustrate how packer ownership provides mutual benefit to packers and producers, consider this: A producer may have a few empty stalls in his or her operation and the skills to manage additional animals, but he or she may lack the capital to afford the extra livestock. Thus, a producer may seek to enter an agreement with a packer to raise packer-owned livestock in the extra capacity in exchange for economic compensation. In this scenario, the producer benefits by maximizing the utilization and efficiency of his or her farm, improving his/her returns, and gaining additional experiences in raising the extra few head. Without the packer-owned livestock, this producer would be limited by his/her capital and would have an underutilized asset because of an arbitrary government restriction.

Producers, packers, and processors have not been the only beneficiaries of these agreements and arrangements. Consumers have benefited from more products that meet their needs and values as well as price competitiveness from improved efficiencies. According to the Bureau of Labor and Statistics an item such as ground beef has, on average, since 1984 consistently lagged the larger consumer price index increases, thereby, consistently improving the value returned to consumers for their food dollar relative to all other expenditures. Further, the amount of income that consumers spend on all meat and poultry products has shrunk to less than two percent of income!

AMI supports the continuance of free enterprise competitive policies that have served our economy and country so well by ensuring access to broad marketing opportunities for producers and procurement alternatives for packers. Domestic and international history is replete with examples of failures by government attempts to manage the market by limiting relationships that enterprises would mutually, normally, and voluntarily pursue. It is difficult to discern where, if any potential value would accrue to any party by a prohibition on ownership or other restrictions. The suggestion that such a restriction would add value to livestock or meat is without merit. Attempts to limit packers' and producers' abilities to engage in contracts, marketing agreements, and strategic mergers reduce capacity to respond to consumers and pursue economic, social, and environmental goals in rural America.

Requiring 25 Percent Spot Market Purchases

With respect to our views regarding legislation that would require a packer to purchase 25 percent of its daily slaughter from the cash market, AMI cannot see any positive impact from this type of policy recommendations. We are unaware of any evidence that any such proposals would add to the producer's bottom line. The most obvious and immediate impact would be that it would make certain companies' entire business models illegal and force packers to terminate risk management programs with producers. In effect, the proposal would cause packers to essentially fire a producer and force that producer's participation in a highly volatile spot market.

If the proposal were to become law, many producers and packers would experience an immediate devaluation of their assets, in effect a taking and devaluation by the federal government without compensation. AMI believes such proposals would hasten consolidation in the packing industry and lead to an immediate reduction in packing capacity, particularly in the pork sector. The added risk in this type of environment could further trigger a contraction in production and compound adverse impacts on remaining producers.

We are also concerned with the discriminatory nature of legislation that would require only certain packers to purchase 25 percent of their daily slaughter from the cash market. If a packer is a single plant operator, not required to report under the mandatory price reporting statute or the plant is owned by a cooperative – they would be exempt. In a free enterprise economy, everyone should be subject to the same rules - restrictions and freedoms - to compete fairly on a level playing field. To do otherwise results in the government picking winners and losers through non-uniform centrally regulated schemes, rather than through the free market economy. Providing benefits for one over another through state-like regulatory requirements also distorts credit and capital investment. The proposal imposes specific livestock procurement requirements in the beef and pork sectors, while direct competitors in the chicken and turkey sectors retain total flexibility. Further, it discourages smaller operations from growing their businesses and market share or they run the risk of having to comply with the legislation. Legislation that treats packers of various size and cooperatives differently is troubling, at best. Legislation that penalizes people and businesses for being successful is – frightening.

GIPSA/RTI Livestock and Meat Marketing Study Rejects the Proposals

As Congress contemplates possible policy changes to the current marketing system for livestock and meat, we would like to remind you of an important provision included in the Omnibus Appropriations Bill for FY 2003, which provided $4.5 million to USDA to conduct a comprehensive study on this subject. That study, now complete, is the most comprehensive and far reaching study that has ever been conducted on livestock and meat marketing. On the beef complex alone, transaction data was secured from the 29 largest beef packing plants and the report focused on 58 million cattle and 590,000 business transactions. The "GIPSA Livestock and Meat Marketing Study," released on February 16, 2007, focused upon, but was not limited to, an examination of various legislative proposals that were debated but not ultimately included in the 2002 Farm Bill. Those legislative proposals included a ban on packer ownership of livestock, a requirement that packers purchase 25 percent of their animals on the spot market, and bills that would either ban or restrict forward contracting and other marketing arrangements.

To conduct this study, the Secretary of Agriculture was required to issue a request for proposals from entities that had the means to conduct this study and the contract was awarded to RTI International though a competitive and open bid process (68 *Fed. Reg.* 32455). This study was conducted with the direct input and peer review of the nations leading business and agricultural universities.

Prior to issuing its notice and request for comments regarding the scope of the study in the *Federal Register*, USDA/GIPSA established a working group with representatives from a wide range of federal agencies with experience and regulatory oversight in the market place. The working group included representatives from the USDA's Office of the Chief Economist, Economic Research Service, Agricultural Marketing Service and National Agricultural Statistics Service in addition to the Department of Justice, Federal Trade Commission, and Commodity Futures Trading Commission (68 *Fed. Reg.* 32456).

The report found that alternative marketing arrangements (AMAs) increase the economic efficiency of the cattle, hog, and lamb markets, and that these economic benefits are distributed to consumers, as well as to independent producers and packers who use AMAs. Other significant conclusions in the study include the following:

- In aggregate, restrictions on the use of AMAs for sale of livestock to meat packers would have negative economic effects on livestock producers, meat packers, and consumers (RTI Study Vol.1 ES - pg. 3).

- Changing consumer expectations in terms of product quality have led retailers to modify their merchandising and purchasing practices in the meat, fruit, and vegetable sectors. These initiatives in response to consumer demand, have led to increased segmentation of product offerings on store shelves and in the meat case. Retailers now offer, in addition to standard products, differentiated products focusing on health, convenience, taste, and information about how the food was produced (RTI Study Vol. 6 pg. 1-12).

- Many livestock producers and meat packers benefit by using AMAs, and those benefits include (RTI Study Vol.1 ES - pg. 3):
  - Better quality assurance and consistency
  - Better risk management (market access and price risk)
  - Improved cost management.

- The producers surveyed that use AMAs identified the ability to obtain better prices, buy/sell higher quality cattle, and improve supply management as the leading reasons for using AMAs. In contrast, the producers surveyed that use only cash markets identified independence, flexibility, quick response to changing market conditions, and ability to buy at lower prices and sell at higher prices as primary reasons for using only cash or spot markets (RTI Study Vol.1 ES – pg. 4).

- The packers surveyed stated that their top three reasons for using AMAs were to secure higher quality cattle, allow for product branding in retail stores (adding value throughout the chain), and improve week-to-week supply management (RTI Study Vol.1ES – pg. 4).

- The producers and packers surveyed that use AMAs value them as a method of dealing with production, market access, and price risks. More specifically, feedlots believe that AMAs allow them to secure or sell better quality cattle and calves and improve operational management, efficiency, and capacity utilization. Packers identified AMAs as an important element of producing branded products and meeting consumer demand by producing a higher quality, more consistent product (RTI Study Vol.1 ES – pg. 8).

- Hogs purchased through AMAs are consistently associated with higher quality than hogs acquired through negotiated (spot market) purchases (RTI Study Vol.1 ES – pg.11).

- An analysis of risk associated with different marketing arrangements shows that different types of marketing arrangements exhibit different price volatilities as measured by variance of prices. From the hog producers' perspective, spot/cash market sales pose the greatest level of risk to the producer (RTI Study Vol.1 ES – pg. 12).

- In analyzing the economic effects of hypothetical restrictions on the use of AMAs in the hog and pork industries, the report concluded that hog producers would LOSE because of the offsetting effects of hogs diverted from AMAs to the spot market and consumers would LOSE because of higher wholesale and retail pork prices (RTI Study Vol.1 ES – pg.12).

- Restrictions on the use of AMAs may increase concentration of various segments of the lamb industry (RTI Study Vol.1 ES – pg. 15).

Maturing Industry Increases Specialization

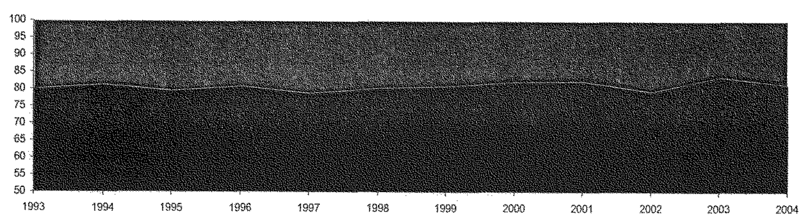
During the past two decades, the American meat and food manufacturing industry has been demonstrating signs of a maturing sector by its increasing specialization, its focus on brand development, value-added products, and its contracting size relative to its customer segment. The packing entities that are most successful in recent years have been those that have been the most agile, disciplined, and focused on providing their customers with the products they demand. To meet these changes, companies developed relationships to minimize the distance between producers and consumers while scaling to the size of business that would allow it to be competitive. Occasionally, criticism of profit or the scale of the top four, five, or twenty leading firms in a segment takes vogue and leads to unjustified incitement and calls for a more active state in participating in the market.

As a regulated industry, the barriers to entry are relatively high compared with the service, knowledge, or light manufacturing segments of our economy. Nevertheless, even with these higher costs it is amazing that there are more than 3,500 meat and poultry plants that are classified as small or very small by USDA and nearly 2,000 state-inspected plants that are mostly very small plants. The smaller operations in the business often focus on very narrowly defined niches and limited offerings. Many will often partner with a large packer or other entities to co-market to larger retailers and gain access to a broader consumer base.

As an industry with a long and diverse heritage, the meat industry has an appreciation for the special responsibilities that it has to its customers, employees, producers, investors, and suppliers. The use of contracting, marketing agreements, and related arrangements provide an economically beneficial way to assure customers of the claims made. Similarly for producers, the use of modern procurement methods is often viewed favorably by creditors and investors, thereby providing affordable capital resources to farmers. Additionally, the use of modern procurement methods and alignment provide a means for packers to work closely with its retail customers. Three of the largest grocers in the world have more **375 million people each week in their stores.** Meeting the weekly and daily demands of that many consumers requires a very sophisticated and sensitive approach, the tools, and the size to adequately negotiate and provide for these major outlets.

A specific critique that some individuals have pointed to is the level of market share of the leading four enterprises in the beef sector. In the beef industry, a simplistic segmentation of the industry could divide it into two main segments, fed beef and lean beef. Fed cattle are those that are often fed significant amounts of grain and marketed between 18-28 months of age. Lean cattle are often mature animals, some are fed grass or extensively grazed or originate within the 9 million head of dairy animals. The majority of the 33 million head marketed are from the fed side of the business. Since the 1990s as this chart illustrates, the level of market share by these four firms has remained relatively constant. A further study of this data would indicate that fed beef enterprises have historically maintained an economy of scale appropriate for their segment. At a few points during the past 120 years, cattle feeders and packers were even members of the Dow Jones Industrial Average Index's 30 firms. Relative to historical context recent and past, the market share and scale of the four leading enterprises has remained relatively constant with stiff competition among these members and new entrants. It is important to note that these four current firms have not been the same four enterprises that have always participated in this group. The competitive pressures and innovations of enterprises have propelled new firms in this category and others out. Indicating and conferring a robust and competitive marketplace.

Four Companies' Fed Slaughter as a Percentage of U.S. Commercial Slaughter



Source: US Department of Agriculture.

Finally, a recent report from the Congressionally authorized and funded multi-year bipartisan Antitrust Modernization Commission report released early this month recommended after their hearings, reviews, and work that "government should not displace free market competition absent extensive careful analysis and strong evidence that either 1) completion cannot achieve societal goals that outweigh consumer welfare or 2) a market failure requires the regulation of prices, costs, and entry in place of competition." This analysis combined with the findings and careful analysis of the USDA/GIPSA report provides a clear indication that the market is competitive and current oversight and enforcement are effective.

How Congress Can Assist the Livestock and Poultry Sectors in the 2007 Farm Bill

Support for Marketing Flexibility and the Free Enterprise System

Efforts to limit the day-to-day advancements of packers and producers cooperating to meet their customers' values can have adverse consequences on all parties. Past Congresses have attempted to prohibit the use of contracting, marketing agreements, and related arrangements as well as strategic mergers. All of these efforts would have impeded progress, investment, and the American agriculture atmosphere for growth. Should these succeed, the result of these efforts are likely less profit, less employment, less credit and investment, less (if any) progress toward social and environmental goals, and overall adverse impact on the competitiveness of American agriculture. We encourage Congress to reject any attempts to impede livestock marketing options and alternatives for producers, packers, and processors.

Trade

The members of AMI have supported and benefited greatly from the existing free trade agreements (FTA) and expanded market access from our World Trade Organization (WTO) membership. The economic well-being of meat and poultry packers and producers is closely tied to our competitiveness in accessing international markets. From the Uruguay Round Agreement to NAFTA, the U.S. meat and poultry community has consistently benefited from the market access to new, international consumers. In fact, Mexico and Canada are currently two of the largest export destinations for beef and beef variety meats, accounting for more than 2/3 of all beef trade and more than $1 billion in sales. For AMI pork exporters, nearly 17 percent of U.S. pork production is exported and the value of pork exports has increased by more than 350 percent since NAFTA's passage. AMI is fully prepared to be a strong and vocal supporter of the pending Korea FTA should Korea's ban on beef end and full market access for beef is restored. AMI encourages all countries that maintain restrictions on U.S. beef and other animal products to align their animal health policies with the guidelines of the World Organization for Animal Health (OIE).

Congress should advance policies that contribute to increased trade opportunities for animal agriculture and encourage trading partners to adhere to commerce based on internationally accepted scientific principles.

Energy-Based Opportunities

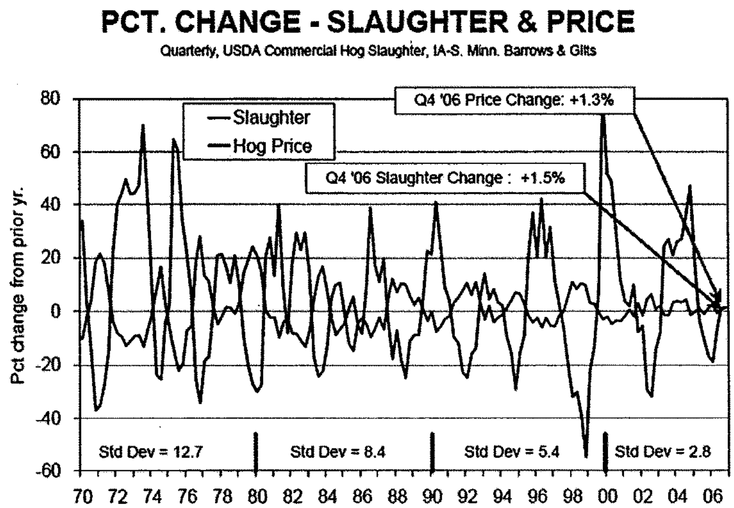
AMI member companies have been carefully observing recent developments in the feed industry, specifically the impacts from the increase in demand for corn from the ethanol industry. This rise in demand for corn has pressed market forces to demand higher corn prices. Consequently, and among other impacts, the change in price and availability has led animal agriculture producers to consider alternatives to their feeding, nutrition, and dietary regimen.

These changes can and do impact meat and poultry quality, consumer offerings, livestock and poultry farm efficiency, and the management of livestock and poultry operations.

It is for these reasons that AMI is asking Congress and the Administration to consider policies to support energy-based opportunities for animal agriculture, minimize adverse impacts on livestock and poultry producers and processors, and ultimately place the United States in a more competitive position in terms of energy availability. Specifically, AMI supports 1) research in ethanol byproduct safety, quality, and usability and renewable energy technologies, 2) equity of incentives for all renewable energy including renewable diesel and methane conversion, 3) a working lands conservation program to encourage environmentally friendly feed stuffs production, and 4) supports exposing consumers to more renewable fuels by allowing the ethanol tariff to expire.

Thank you for the opportunity to provide these perspectives today.

Testimony of J. Patrick Boyle
April 17, 2007
Page 10 of 13



Source: CME Daily Livestock Report, February, 14, 2007

Since 1970 through November 2006, the volatility of live hog prices has moved incrementally some years and dramatically other years to respond to market and seasonal supply and demand changes. Incidentally, in recent years, the live hog, live cattle, and feeder contracts are consistently the largest volume traded agricultural contracts at the Chicago Mercantile Exchange – a reflection of demand for risk management.

Portion of U.S. Farms with Livestock

	1950	1964	1974	1992	2002
Sheep	6.0%	7.4%	4.7%	4.2%	3.5%
Beef	75.5%	72.3%	44.3%	41.7%	37.4%
Hogs	56.0%	34.2%	20.3%	9.9%	3.7%
Dairy	67.8%	35.9%	17.4%	8.1%	4.3%
Chicken	78.3%	38.3%	13.7%	4.6%	3.5%

Source: U.S. Census of Agriculture

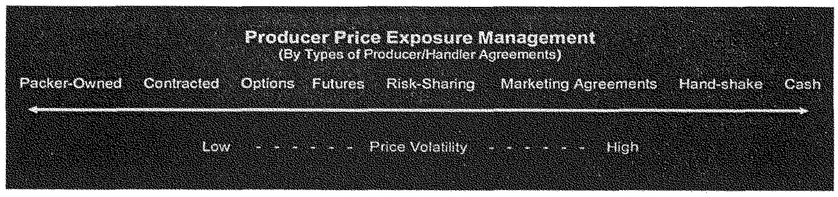
As the meat and poultry packing and processing sector matures and specializes, farmers have also increased their specialization. This data from the U.S. Census of Agriculture illustrates that more and more farms are becoming single specie producers and developing well defined expertise in the production of certain animals, breeds, and market segments.

Why production contracts? Start up costs & Risk mgt:

To be fully employed as an independent hog farmer requires a $700,000 investment and 50% equity		To be fully employed as a hog contract grower requires a $500,000 investment and 15% equity
$350,000	Versus	$75,000

Source: University of Missouri-Columbia, Dr. Ron Plain. "*Why U.S. Animal Agriculture Looks Like It Does.*"

Young producers and entities that seek to enter agriculture may have the skills, education, and some initial experience, but lack capital to enter farming. Contracting and other agreements provide a means for entry at a significant but much more achievable entry price. This chart shows the difference in start up capital often required by bankers and creditors of new producers. While there still are a number of operators that inherit farms from previous generations, these are fewer and sometimes have facilities that do not reflect the best in production science, animal well-being, or animal husbandry considerations.



Producers and packers often enter into agreements to limit exposure to market price volatility and guarantee themselves a price prior to delivery. The above illustrates the different types of agreements and an illustrative representation of the related risks. As it scales from left to right, the price risks for producers increases. USDA and private market research have provided indication that producers will often use a portfolio approach in marketing their livestock and employ a mix of methods to manage their price risk.

Comments of Allan Sents
Director of the United States Cattlemen's Association
Immediate Past President of the Kansas Cattlemen's Assoc.
April 17, 2007
Hearing on Market Structure of the Livestock Industry
Livestock, Dairy and Poultry Subcommittee of the
U.S. House of Representatives Agriculture Committee

Mr. Chairman and members of the sub-committee thank you for the opportunity to express my experiences and perspective on competition issues in the cattle industry. I have been a co-owner and manager of a 10,000 head commercial cattle feedyard located in Central Kansas for over 25 years. Prior to that I fed some cattle commercially in the 1970's. My comments stem from witnessing the changes in four different decades of cattle markets.

Background

You have heard testimony from industry representatives claiming current laws and regulations are working. Yet, we saw in the late 1990's the investigators within GIPSA bring an action against IBP for violations of the P&S Act. Further, twelve neutral jurors decided in the Pickett vs. IBP case that laws had in fact been violated. Each of these actions saw individual judges reaching different decisions than the numerous investigators and jurors involved. Dr. Robert Taylor from Auburn University has made the following assessment of those actions: "Livestock and poultry producers' legal rights under the PSA are seemingly more muddled than ever before. Inconsistent rulings by Circuit Courts may also frustrate any attempt by USDA/GIPSA to enforce the PSA since different policy may be required in different Federal Appellate Courts."[1]

In light of Dr. Taylor's comments it seems odd that J. Patrick Boyle (AMI President) can state "We believe that the most appropriate government role in today's livestock marketing system is to enforce the existing laws and regulations that ensure fair and nondiscriminatory business practices among producers and packers"[2] I can assure from my personal experiences outlined later in this article that current business practices in cattle procurement by packers are in no way available in a "fair and nondiscriminatory" manner. In addition, John Queen (President of NCBA) has stated "we ask that the government not tell us how we can or cannot market our cattle."[3] The whole problem is that you are hearing these messages from the "haves" of exclusive marketing arrangements that are benefiting over their peers without providing, in most cases, any different quality product. Instead they provide a supply that often is used to leverage down the price paid to other producers. This is confirmed in the recent GIPSA report: "The use of AMA's is associated with lower cash market prices"[4]

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[1] "Legal and Economic Issues with the Courts' Rulings in *Pickett v. Tyson Fresh Meats, Inc.*,a Buyer Power Case" by C. Robert Taylor, February 13, 2007, p. 25.

[2] Comments from J. Patrick Boyle testimony to the U.S. House Ag Subcommittee on Livestock, Dairy and Poultry April 17,2007, as reported by meatingplace.com.

[3] Comments from John Queen testimony to the U.S. House Ag Subcommittee on Livestock, Dairy and Poultry April 17,2007, as reported by meatingplace.com.

[4] GIPSA Livestock and Meat Marketing Study, Executive Summary and Overview, January 2007. Page ES-2.

A disturbing concept of the AMA (Alternative Marketing Arrangements) discussion is the impression that a negotiated sale cannot involve premiums and discounts to achieve the desired product. The current formulas used in AMA's could just as easily use a competitively determined base price to reward and discount quality differences. The best example of a consumer desired product rewarded competitively in the marketplace is the Certified Angus Beef program. I would think this is the largest volume, premium beef product currently available and the premiums to provide that product are available to all producers.

Personal Examples

Some current laws affecting the cattle trade seem to be appreciated by the industry. A couple of them that I have personal experience follow: 1) Prompt pay legislation was enacted back in the 1970's. This law requires payment for cattle within set parameters. In the 1990's a major packer began paying for cattle delivered in the afternoon on the following day, instead of on the day of delivery. This practice violated the law and a complaint to the regional P&S Office and a subsequent letter from them to the packer corrected the problem. Even now, some packers try to walk the edge of that prompt payment line by drawing checks on the most remote bank in a banking district which adds a day to the "collected" status of those funds. That "float" adds up to significant dollars in a year's time at the producer's expense and would undoubtedly be more abused if not regulated. 2) Within the last 10 years another major packer developed a market grid to determine value. An oversight in one part of that grid regarding standard grade cattle resulted in payment for less than the published schedule. Complaints to the packer resulted in being told "if you don't like it, don't use it." Given the limited number of options available to a producer and the principle of not abiding by a published record caused me to pursue the issue. Only after threatening to proceed with a formal complaint to P&S was the issue resolved.

Another example of packer intimidation occurred in 1994. Frustrated by an agreement of then IBP with several competing feedyards in my area I responded by telling IBP I would sell cattle in the same way they were buying cattle. That is, since IBP was (and still does) give these yards a "high of the week" guarantee in exchange for giving IBP a "right of first refusal" I was going to give the other packers a similar "right of first refusal" over IBP in buying my cattle. The head buyer for IBP promptly told my buyer to quit coming into my yard! (I thought there was a rule about that too) After a few months I was able to again sell them cattle, if I didn't make an issue of the first refusal practice, but the lesson of intimidation was received! About three years ago I was approached by a feedyard involved in this special deal with IBP about him buying my feedyard. His interest left when he discovered IBP would not add this yard to the "deal" he already had. These are the kind of stories we have heard occurring in the poultry business and I believe will become more common in the beef business if left unchecked. Is it possible that packers have enough "captive supplies" to allow them to depress the overall market while paying premiums to the select few? Perhaps that is why my buyer did not have access to the same deal for additional capacity. One would have to say that the value of my facility was lessened by that practice. Clearly, this practice is in violation of the intent of the P&S Act regarding "unfair, unjustly discriminatory" or "undue or unreasonable preference" rules.[5]

[5] Packers and Stockyards Act, 1921, As Amended. Section 202.

Remedies

Pass a Competitive and Fair Agricultural Markets Act. SB 622 introduced by Sen. Harkin strengthens the P&S Act and addresses needed reforms in what should be a non-controversial approach. This bill needs to be introduced on the House side.

Control of packer-owned livestock. The concentration and elimination of many producers is obvious in the pork and poultry industries. Smithfield has formed a partnership with Conti-Group cattle feeders and they have announced their intent to build a packing plant to process their own cattle in the Oklahoma panhandle. The exclusivity of the Caprock feedyards with Cargill Meat Solutions provides a large captive supply to their plants. A healthy debate of this issue is needed as the formula deals accomplish the same thing as packer owned cattle and must be evaluated as well.

Country of Origin labeling. The recently announced joint venture of Tyson and Cactus feeders in Argentina reinforces the concept that voluntary COOL will never happen. The largest U.S. packers have international holdings and want to source their beef from the cheapest location. Apparently, meat companies in other countries would also like access to the infrastructure within our country. This is evident in the recent news reports indicating a Brazilian firm was interested in buying Swift. We can be sure they are not interested in sourcing our U.S. beef! The American consumer deserves just as much a choice in buying their beef as they do in buying their clothes and tools. The U.S. cattle producer deserves the opportunity to market the high quality, safe product they strive to produce.

Summary

The very existence of significant and persistent voices of concern about competition issues in the cattle market should cause concern for lawmakers and regulators. Consolidation is occurring in the cattle industry to gather marketing power, not because of operating efficiencies. If this trend is left unchecked the cattle industry will more closely resemble the pork and poultry industries. These industries involve fewer participants and concentrate environmental and other concerns. If legislators have interest in rural development, effective legislation in this area of competition will keep more efficient producers supporting more rural communities and promote a healthy, competitive future for the beef industry.

Thank you for your consideration.

Economic Challenges and Opportunities Facing American Agricultural Producers Today

Testimony

of the

Ranchers-Cattlemen Action Legal Fund, United Stockgrowers of America (R-CALF USA)

To the

United States House of Representatives Committee on Agriculture, Subcommittee on Livestock, Dairy and Poultry

April 27, 2007

Presented By

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I appreciate the opportunity to testify about including livestock and competition issues in the 2007 Farm Bill. I am Randy Stevenson and along with my wife, Charlie, and our son, Oakley, we own and operate a beef feedlot and a cow/calf and farming operation near Wheatland, Wyoming, in Platte County. I am also a Board of Director of R-CALF USA.

R-CALF USA is a non-profit cattle-producer association that represents thousands of U.S. cattle producers in 47 states, along with over 60 state and local affiliates. R-CALF USA's mission is to ensure the continued profitability and viability of independent U.S. cattle producers. The demographics of R-CALF USA's membership are reflective of the demographics of the entire U.S. cattle industry, with membership ranging from the largest of U.S. cattle producers to the smallest. R-CALF USA's membership consists primarily of cow-calf operators, cattle backgrounders, and feedlot owners. Various main street businesses are associate members of R-CALF USA. The 2007 Farm Bill presents an important opportunity to strengthen the cattle sector and create a competitive playing field at home and abroad for United States cattle producers.

I. INTRODUCTION

Ensuring a market framework that provides participants in the U.S. live cattle industry with the opportunity to remain profitable should be a central focus of the 2007 Farm Bill. A profitable and vibrant U.S. cattle industry is vitally important to the health of our citizens and the overall welfare of Rural America. Today's production agriculture, which, in addition to its principal role of producing an abundance of safe, wholesome, and high-quality food, now includes the development of bio fuels and a heightened emphasis on international trade. This makes for a highly complex and dynamic industry that has created many overlapping and interconnected relationships.

To effectively address the new complexities that were brought about by changes in national policy, we must adhere to sound market principles. For example, R-CALF USA believes that each segment of U.S. agriculture should have the opportunity to prosper at the same time, without pitting one against another. This belief is based on our knowledge that competitive markets have long assimilated increased production costs without rendering entire industry segments unprofitable. When applying this principle to the nation's current policy of achieving more energy independence through alternative energy promotion, R-CALF USA does not join critics who claim the government's ethanol incentives are inappropriate. Instead, R-CALF USA believes the proper response by the U.S. cattle industry to this national energy policy is to work aggressively to remove the barriers that currently prevent the U.S. cattle market from assimilating necessary increases in productions costs. If appropriate reforms are made to enable U.S. cattle producers to begin receiving their competitive share of the consumers' beef dollar and their competitive share of the consumer beef market, then they will be able to recover increased production costs from the competitive marketplace.

The removal of current market-competition barriers from the U.S. cattle market would generate another benefit for the U.S. cattle industry, besides that of accommodating the nation's desire to achieve energy independence. Production agriculture is a capital intensive endeavor, making it very difficult for young people to gain entrance. For generations, livestock production has served as the means by which young entrepreneurs have gained entry into agriculture.

A young person with a little capital can take his money to Wall Street and compete with every other investor. If he uses his intelligence and works hard at it he can succeed because he is in a market where he is guaranteed treatment just like every other competitor. Market power and preferential treatment cannot be used against him. If he tries the same thing in agriculture the situation is different. The Packers and Stockyards Act once established a competitive livestock market, which provided hard working entrepreneurs with a genuine opportunity to prosper in the livestock industry. But it is now outdated and barely enforced so that young entrepreneurs have little opportunity to succeed. The 2007 Farm Bill could, again, reestablish competitive livestock markets that would afford that same opportunity to a whole new generation of livestock producers.

The core problem facing the cattle industry today that the 2007 Farm Bill can help to correct is that the overall framework that defines how our cattle industry operates is no longer adequate to ensure a balanced and properly functioning competitive marketplace. The present industry framework comprised of the statutes, regulations, and policies that govern contracts and market competition, consumer information and information disclosure, heath and safety, and trade have evolved under the considerable influence of the nation's largest meatpackers; and without sufficient counterbalance from producers. As a result, the balance of power within the present industry framework is tilted in favor of the meatpackers, resulting in a pricing advantage for them and an erosion of competition for livestock producers.

Independent livestock producers cannot match the economic or political power held by the nation's largest meatpackers – we cannot expect to level the playing field by correcting the deficiencies within our industry's framework through negotiations with the meatpacking sector. Ironically, we are in an intense competition to win back competition. Therefore, our success in winning back our competitiveness will depend on you, the Congress. .

R-CALF USA is deeply concerned that the recently completed GIPSA/RTI Livestock and Meat Marketing Study (RTI Study) is woefully inadequate for use by Congress as a meaningful decision-making tool for determining which types of alternative marketing arrangements must be reformed to restore robust and unimpeded competition in the U.S. cattle market.[1] Given that the study extracted data only from 293 beef cattle producers out of a population of approximately 800,000 domestic beef cattle operations,[2] its utility for evaluating the balance of market power between widely dispersed, independent producers and the concentrated meatpacking sector is negligible.

The RTI Study grossly oversimplified cattle procurement options presently employed by the meatpacking industry. It incorrectly divided cattle marketing methods into only two categories: the cash market and alternative marketing arrangements. Within the category of

[1] *See* GIPSA Livestock and Meat Marketing Study Final Reports, February 2007, available at http://www.gipsa.usda.gov/GIPSA/webapp?area=home&subject=lmp&topic=ir-mms.
[2] Livestock Operations 2003 summary, U.S. Department of Agriculture, National Agricultural Statistics Service, April 2004, available at http://usda.mannlib.cornell.edu/reports/nassr/livestock/operations/lvstan04.txt.

alternative marketing arrangements were marketing agreements, marketing and production contracts, packer ownership, and forward contracts. As a result, the RTI study completely ignored the fact that the cash market also includes cash transactions on a quality grid and it lumped all non-cash marketing methods into a single category. The RTI Study made no distinction between forward contracts that contained a firm base price and forward contracts that were tied to whatever the average cash price was that the packer paid during the week prior to the producers' delivery of cattle. The former contract would minimize the potential for market manipulation while the latter would facilitate market manipulation when in the hands of a concentrated industry. As a result of this major deficiency, the RTI Study did not determine, nor could it determine, that packers were using some of the alternative marketing arrangements, in particular those arrangements known as captive supplies, to manipulate the price of cattle. In fact, the term "captive supply" does not appear in the RTI Study's Final Report on Fed Cattle and Beef Industries.[3]

The RTI Study further failed to evaluate whether the growing trend of specific contractual relationships, in which contract prices are tied directly to either the cash or futures markets, was distorting the meatpackers incentives to participate aggressively in the cash market, particularly when an increased cash market price would necessarily lead to increased prices paid under all outstanding contracts.

The relevant question for Congress is not whether the aggregate use of alternative marketing arrangements bestows benefits on some or even most segments of the beef supply chain, which is what the RTI Study purports to have found. Rather, the relevant question is whether the marketplace is competitive, do certain contract arrangements diminish competition by affording buyers undue market power, and do any of the various alternative marketing arrangements provide concentrated buyers with the ability to disrupt an otherwise competitive market. The reason this question is relevant is because even in a market burdened by anti-competitive behavior and practices, benefits can be found among practices that partially mitigate the effects of the deteriorated market. Thus, benefits depend on the frame of reference: the best within a bad situation should not be viewed as the best situation.

Fortunately, Congress has an abundance of other sources from which to formulate its answer to the relevant question facing the U.S. cattle industry. I would like to take this opportunity to inform Congress of the significant competition-related challenges the U.S. cattle industry presently faces and identify the specific areas in which congressional reforms are needed to properly rebalance the framework that defines the operation of the U.S. cattle industry

II. CONTRACTS AND COMPETITION

The ongoing erosion of competition within the domestic livestock market is a threat to present and future generations of U.S. livestock producers. This Committee has heard convincing arguments over the past several years in support of the conclusion that competition

[3] *See Volume 3: Fed Cattle and Beef Industries Final Report*, GIPSA Livestock and Meat Marketing Study, RTI International, January 2007, available at http://archive.gipsa.usda.gov/psp/issues/livemarketstudy/LMMS_Vol_3.pdf.

has been significantly reduced in the domestic cattle market. These arguments have highlighted the radical changes that occurred to the structure of the U.S. cattle market over the past few decades. These unfavorable structural changes include:

A. UNFAVORABLE STRUCTURAL CHANGES

1. Unprecedented Consolidation of the U.S. Meatpacking Industry

Concentration in the meatpacking industry has tripled since the late 70s, and today just four meatpackers control over 83 percent of nation's steer and heifer slaughter.[4] By the mid-90s, a single packer – Tyson (then IBP) – purchased about 35 percent of slaughter cattle.[5] The General Accountability Office (GAO) reported in 2002 that "no other manufacturing industry showed as large an increase in concentration since the U.S. Bureau of the Census began regularly publishing concentration data in 1947. . ."[6] Such a high level of concentration is indicative of a severe lack of competitiveness in the industry, given that most economists believe competitive conditions begin to deteriorate once the four-firm concentration level exceeds 40 percent.[7]

2. Introduction and Increased Use of Non-traditional Contracting and Marketing Methods that Further Erode the Selling Power of Cattle Producers

While the meatpacking industry has become more integrated horizontally (through consolidation), it has also been increasing its vertical coordination through its contracting practices. Such methods include purchasing cattle more than 14 days before slaughter (packer-fed cattle), forward contracts, and exclusive marketing and purchasing agreements. Together, the four largest packing companies employed such forms of "captive supply" contracting methods for a full 44.4 percent of all cattle they slaughtered in 2002.[8] And use of these captive supply methods has been increasing rapidly, rising 37 percent from 1999 to 2002.[9] Captive supply practices push risks of price instability on to cattle producers and hold down cattle prices.[10] As prices for cattle are artificially depressed and become more volatile, it is cattle

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[4] J. McDonald et al., "Consolidation in U.S, Meatpacking," Food and Rural Economics Division, Economic Research Service, U.S. Department of Agriculture, Agricultural Economic Report No. 785, February 2000 at 7 and M. Hendrickson and W. Heffernan, "Concentration of Agricultural Markets," University of Missouri Department of Rural Sociology, February 2005, available on-line at http://www.foodcircles.missouri.edu/CRJanuary05.pdf.

[5] C. Robert Taylor, *Legal and Economic Issues with the Court's Ruling in Pickett v. Tyson Fresh Meats, Inc., a Buyer Power Case,* The American Antitrust Institute, Working Paper No. 07-08, at 6, available at http://www.antitrustinstitute.org/archives/files/AAI_Taylor_WP07-08_033020070955.pdf.

[6] U.S. General Accounting Office, *Economic Models of Cattle Prices: How USDA Can Act to Improve Models to Explain Cattle Prices*, GAO-02-246, March 2002.

[7] "Economic Concentration and Structural Change in the Food and Agriculture Sector: Trends, Consequences and Policy Options," Report Prepared by the Democratic Staff of the Committee on Agriculture, Nutrition, and Forestry, United States Senate, Oct. 29, 2004 at 4 – 5.

[8] RTI International, "Spot and Alternative Marketing Arrangements in the Livestock and Meat Industries: Interim Report," Report Prepared for the Grain Inspection, Packers, and Stockyard Administration, U.S. Department of Agriculture, July 2005 at 3-15.

[9] *Id.* at 3-17.

[10] *Id.* at 3-18 – 3-22 and John M. Connor, "The Changing Structure of Global Food markets: Dimensions, Effects, and Policy Implications," Paper Presented to The Conference on Changing Dimensions of the Food Economy: Exploring the Policy Issues, The Hague, Netherlands, Feb. 6 - 7, 2003 at 8.

producers who pay the price, even when broader demand and supply trends should be increasing returns to producers.

B. NEGATIVE EFFECTS OF PACKER CONCENTRATION AND ABUSIVE CONTRACTING PRACTICES ON PRODUCERS AND CONSUMERS

1. Producers' Share of the Consumers' Beef Dollar has Shrunk and the Spread Between Farm to Retail has Widened.

The impact of packer concentration and abusive contracting practices is evident in the declining share of each beef retail dollar that actually reaches cattle producers. The producers' share of each retail dollar earned on beef was 47 cents in 2006, down from 60 cents in 1990.[11] Looking the opposite direction along the food chain reveals that consumers have likewise not benefited from packer concentration and abusive contracting practices. The price spread between what the cattle producer receives per pound of beef sold and what consumers pay per pound of beef purchased has widened dramatically, with the spread nearly doubling from $1.13 per pound in 1990 to $2.10 per pound in 2006.[12] In fact, the retail carcass value paid by consumers in 2006 was $580 more than they paid in 1990, while cattle producers received only $89 more for their live cattle in 2006 than they did in 1990.[13]

As clearly revealed in Figure 1 below, the spread between the farm gate price of beef and the retail price of beef widened dramatically beginning in the early 90s. It is important to note that this chart depicts the value of carcasses based on fresh cuts of beef sold at the meat case, which are relatively low value-added cuts.[14] The U.S. Department of Agriculture, Economic Research Service warns, "Analysts who cite increasing value-added as a factor in pork and beef price spreads misunderstand how these are calculated."[15] The enlarged gap between the farm-gate price and retail price suggests that the meatpacking and retailing sectors have become less efficient at processing and/or selling beef, or they have acquired sufficient buying power to leverage down the price of live cattle, or both.

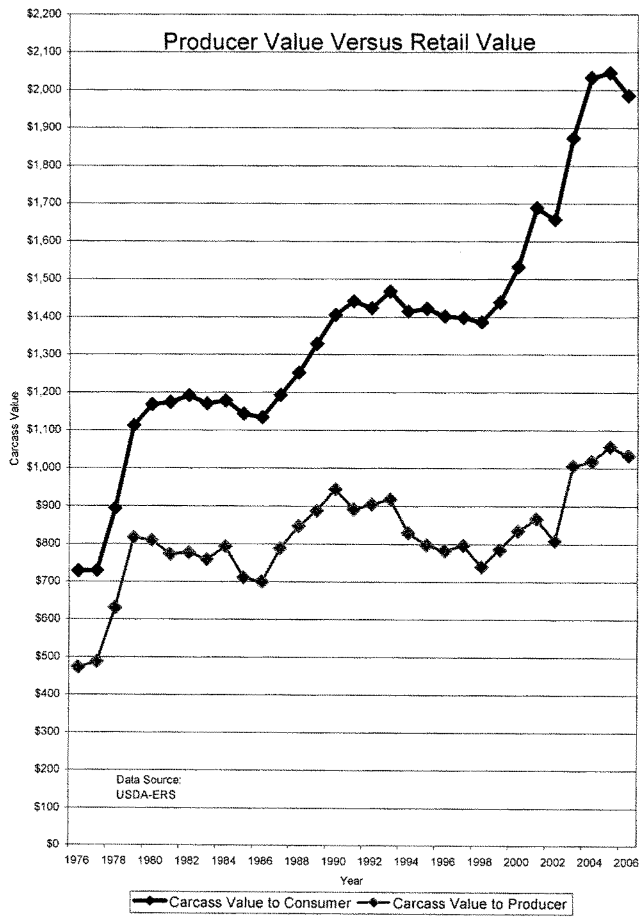
As a full-time cattle producer who feeds cattle, I find it hard to imagine how a competitive market would dictate that consumers would pay nearly twice the value for beef derived from the finished cattle. After spending 16 months being cared for and fed, a 1200 pound steer brought approximately $1,033 in 2006. After it was sold to a meatpacker, and within a matter of days or a few week, the fresh cuts of beef from it was sold to consumers for approximately $1,985, a mark-up of approximately $950.

But in 1990, a 1,200 pound steer sold for $944. The consumer at that time paid $1,405 for the beef from that steer after the meatpacker and retailer handled the beef for days or a few weeks, a mark-up of $461. If the meatpackers' claims are true – that consumers benefit from

[11] USDA Economic Research Service, "Beef Values and Price Spreads," available on-line at http://www.ers.usda.gov/briefing/foodpricespreads/meatpricespreads/.
[12] *Id.*
[13] *See id.*
[14] Beef and Pork Price Spreads Explained, U.S. Department of Agriculture, Economic Research Service, LDP-M-118-01, at 4, available at http://www.ers.usda.gov/publications/ldp/APR04/ldpm11801/ldpm11801r.pdf.
[15] *Id.* at 2.

increased efficiency attributed to horizontal consolidation and vertical integration – it is certainly not revealed by the more than two-fold mark-up on beef that occurred since 1990 after the live cattle producer sells his or her cattle. A competitive market would not have predicted this result and these facts reveal that the current market structure, from the early 90s on, is breeding inefficiency and windfalls for intermediaries at the expense of both producers and consumers.

Figure 1



2. Packers Have Gained a Significant Pricing Advantage in the Cattle Market

Since the early 90s, the largest meatpackers have perfected their exercise of buying power attained through consolidation and abusive contracting practices. The meatpackers' exposure to the cash market is now so limited that the current bidding practice involves an offer by the meatpacker once per week, and within only about a fifteen-minute timeframe. If the meatpackers are short bought, this fifteen-minute window may occur on a Thursday, or perhaps even on a Wednesday. However, if the meatpacker is long-bought, the fifteen-minute marketing opportunity may not occur until late Friday afternoon, after the close of the futures markets. This extremely narrow window of opportunity to market cattle places cattle feeders at a distinct disadvantage as there is insufficient time to make calls to other meatpackers after an offer is made – it is essentially a take-it or leave-it offer that, if refused, means you must continue feeding for another week, even if the cattle are finished, in hopes of a more realistic offer the next week. This limited and infrequent bid window affords the meatpackers with market power that gives them a distinct pricing advantage in the market.

The meatpacker's use of captive supply cattle is akin to insider trading. With captive supply cattle, the packers know how much of their slaughter capacity is filled each week and at what price before they enter the cash market; they also know how many captive supply cattle are available at a known price to fill their slaughter needs in the event the cash market is not low enough to achieve their pricing objectives. This information is not reported to the public, and certainly not to the cattle feeder. It is time for the cattle market to follow the long-established principle of transparency that facilitates competitive Wall Street-like trading.

The fact that meatpackers are using their buying power and abusive contracting practices to gain a distinct pricing advantage in the market is revealed by a combination of industry acknowledgments, academic studies, and empirical evidence.

i. Industry Acknowledgements

The concentrated meatpacking industry has acknowledged the profound impact their contracting practices have on the domestic live cattle market. Such acknowledgments began in 1988 when Bob Peterson, then Chairman of IBP (now Tyson) was quoted as saying:[16]

> Procurement practices are changing and this concerns me. There is a quiet trend towards packer feeding and it is much, much bigger than you think it is. We cannot stand by if the competitive playing field is unlevel. Our competitors are promoting contracts and seeking more. These forward contracts coupled with packer feeding could represent a significant percent of fed cattle at certain times of the year. Do you think this has any impact on the price of the cash market? You bet! We believe a significant impact.

[16] Affidavit of Lee Isaac, *Pickett v. Tyson,* July 26, 2002, containing the transcript of Bob Peterson's July 26, 2002, containing the transcript of Bob Peterson's July 1998 speech to the Kansas Livestock Association, pp. 7-8.

> ...we believe that some of those who are feeding cattle and using forward contracting are creating aberrations within the market place by coming in and out of the market; that is not reflecting the true value of the cash market.
>
> But with the packers in the feeding business and forward contracting, there's going to be a major, major shift against the leverage system.
>
> In my opinion the feeder can't win against the packer in the real fair play if we go into the feeding and the hedging program.

In written testimony before the July 16, 2002, United States Senate Agriculture Committee hearing on packer ownership of livestock, the meatpacking industry's trade association, the American Meat Institute (AMI), testified: "Demand for consistent quality product has led many firms to exert greater control over the supply chain." While AMI did not specifically state that firms were exerting control over livestock prices, a study commissioned by the National Cattlemen's Beef Association (NCBA) provides insightful documentation regarding the true nature of this industry control.

In its written testimony before the same July 16, 2002, Senate hearing, the NCBA attached the executive summery of the Sparks Study to its testimony. Specifically, the NCBA commissioned Sparks Study states the following:

> Packers use ownership of livestock to help control unit costs in a variety of ways. If this management tool is restricted, unit costs can be expected to increase (without increasing the value of the final product).[17]

Based on this Sparks Study finding, it is readily apparent that the "control" mentioned by AMI included control over the packers' unit costs. While the cost of live cattle is the single largest unit cost incurred by packers, this finding lacks specificity as to the exact nature of the "unit costs" that are being controlled by the packers. The Sparks Study, however, provides even greater clarity as to exactly what "unit costs" were being controlled by packers. The Sparks Study asserts that direct ownership of livestock limits the packers' market risk, arguing that the futures market is insufficient for this purpose. Therefore, according to the Sparks Study, one of the few tools available to packers to offset the smaller margins associated with higher livestock prices is through direct ownership of raw production materials, i.e., livestock, which enables them to reduce their margin risk. The Sparks Study states, "The pressure to reduce costs force the search for low-cost livestock supplies (often at the expense of producer returns)."[18]

Thus, it is readily apparent that the unit costs the Sparks Study finding referenced as among the unit costs controlled by packers through packer ownership of livestock is the cost of livestock itself. The Sparks Study adds additional insight into the packing industry's rational for supporting packer ownership of livestock as well as other means that contribute to vertical integration of their industry. The Sparks Study acknowledges:

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[17] *See* Sparks Companies Inc., "Potential Impacts of the Proposed Ban on Packer Ownership and Feeding of Livestock", A Special Study, (March 18, 2002) at 40.
[18] Id. at 22.

> For many meat packers, integration between the packing and feeding stages of livestock production is seen as an effective vehicle to reduce market risk exposure and loss of such a valuable tool increases their costs . . .[19] and,
>
> Vertical integration often attracts investors because of the negative correlation between profit margins at the packing stage and the feeding stage.[20]

It is clear that the current market structure affords meatpackers with a distinct pricing advantage over the U.S. cattle market, and this pricing advantage is disrupting the competitiveness of the U.S. cattle industry. Also obvious is the inherent disadvantage faced by domestic cattle feeders that must first compete against the same meatpackers when purchasing feeder cattle that they must later sell to when their cattle are finished.

ii. Academic Studies

In a report completed in 2002, the Grain Inspection Packers and Stockyards Administration (GIPSA) cited numerous studies indicating a correlation between captive supply volumes, including packer-owned cattle, and cash cattle prices. The report indicated that economists Schroeder, Mintert, Barkley, and Jones found a negative statistical relationship between fed cattle prices and captive supplies in 1992; that same year economist Elam found a negative statistical relationship between captive supplies and monthly average fed cattle prices; GIPSA's 1992 study found that packers use captive supplies, including packer owned cattle, strategically; economists Parcell, Schroeder, and Dhuyvetter found that a one percent increase in captive supply shipments was associated with a reduction in basis in Colorado and Texas in 1997; and GIPSA, in cooperation with economists Schroeter and Azzam, found a negative statistical relationship between weekly captive supply and the weekly average spot market price in 1999.[21]

These studies, beginning in 1992, are uncontested with respect to showing a negative statistical relationship between levels of captive supply and spot market prices, though GIPSA has not taken any enforcement action to reduce captive supply use. It is important to note that a March 2002 report completed by the General Accountability Office (GAO) had revealed that the USDA was without the analytical tools needed to accurately evaluate the effects of captive supplies during the time that GIPSA completed its 2002 captive supply report. The GAO report reminded us that over 10 years ago, in 1996, the Packers and Stockyards Administration could not conclude that the U.S. cattle industry was competitive. The 2002 GAO report further reveals that USDA has not properly maintained and updated the economic models used by it for evaluating the U.S. live cattle industry. The GAO stated that the USDA has not properly re-estimated, documented, or validated its models, and much of the data used in the original estimation was from the 1960s and 1970s.[22]

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[19] Id. at 24.
[20] Id. at 24.
[21] Captive Supply Report, GIPSA-USDA, January 18, 2002.
[22] U.S. General Accounting Office, *Economic Models of Cattle Prices: How USDA Can Act to Improve Models to Explain Cattle Prices*, GAO-02-246, March 2002.

Even in the preliminary stages of study, the authors of GIPSA's $4.5 million interim captive supply report found that meatpackers were accruing the benefits of vertical integration, though they found the impacts on the cash market to be "elusive." The report states: "While the empirical research, on balance, suggests an inverse relationship between captive supplies and cash market prices, establishing a causal link has been elusive." [23]

iii. Empirical Evidence

Unlike the meatpacking industry, the live cattle industry was in a serious state of decline and suffered through a dozen years of depressed prices from 1991 through 2002, beginning first with the decline in fed cattle prices and followed by the decline in feeder cattle prices. During the 12-year period from 1991 to 2002, the U.S. live cattle industry suffered staggering losses measured in the billions of dollars, with the value of cattle and calf production falling from $30.1 billion in 1990 to $26.9 billion in 2002.[24] U.S. cattle feeders lost approximately $3 billion just during the period from March 2001 through May 2002.[25] For the period from 1992 to 2001, the average return to U.S. cow/calf producers was a negative $30.40 per bred cow per year for each of those 10 years.[26] Consequently, the U.S. cattle industry has lost over 127,000 beef cattle operations since 1994.[27] This includes the estimated loss of over 8,500 U.S. feedlots just since 1995.[28] As revealed by Figure 2, the production capacity of the U.S. cattle industry has been shrinking since the late 70s.

[23] RTI International, "Spot and Alternative Marketing Arrangements in the Livestock and Meat Industries: Interim Report," Report Prepared for the Grain Inspection, Packers, and Stockyard Administration, U.S. Department of Agriculture, July 2005 at 3-17.

[24] *See Meat Animals Production, Disposition, and Income*, United States Department of Agriculture National Agricultural Statistics Service, 1990 and 2002 summaries, available at http://usda.mannlib.cornell.edu/reports/nassr/livestock/zma-bb/ .

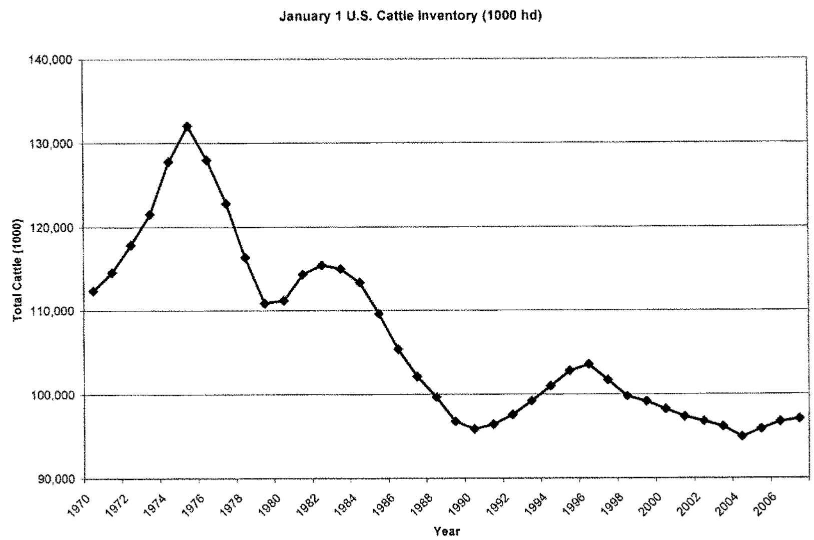
[25] Figures based on USDA's Great Plains cattle feedlot estimated returns data. *See Current State of the United States Live Cattle Industry (Revised), Presented at the 2002 Business Forum of the Free Trade Area of the Americas, Quito, Ecuador*, October 29-31, 2002, R-CALF USA, Figure 2, available at http://www.r-calfusa.com/FTAA-TPA/current_state_of_the_u_s__live_cattle_industry.htm .

[26] *U.S. Cow-Calf Production Cash Costs and Returns, 1990-95; 1996-99; 2000-2001*, Economic Research Service/USDA, available at http://www.ers.usda.gov/data/farmincome/CAR/DATA/Appendix/Cowcalf/US9095.xls; http://www.ers.usda.gov/data/farmincome/CAR/DATA/History/CowCalf/US9699.xls; and http://www.ers.usda.gov/data/CostsAndReturns/data/current/C-Cowc.xls , retrieved from the internet on October 18, 2002.

[27] *See* U.S. Department of Agriculture, National Agricultural Statistics Service Agricultural Statistics Database, *U.S. and All State Data, Cattle and Calves, Cattle Operations – Numbers*, 1994-2005, available at http://www.nass.usda.gov:8080/QuickStats/PullData_US.jsp .

[28] "Economist Sees Gradual Price Decline Next Two Years," *Livestock Weekly*, March 9, 2006.

Figure 2



Despite the fact that domestic beef consumption increased by nearly 3.8 billion pounds from 1993 to 2002,[29] no recovery to the protracted depression in live cattle prices occurred until 2003, the year the Canadian border was temporarily closed to imports of Canadian beef and cattle.

Beginning in 2003, U.S. cattle prices hit historic highs, and these higher prices were sustained through 2006, albeit not without considerable price volatility. The rise in prices afforded a four-year healing period, at least for cow/calf producers that experienced less price volatility than their cattle feeding counterparts.

But the gains in live cattle prices during this period were perhaps less than they might have otherwise been due to the continued decline in the producer's share of each consumer's beef retail dollar over the same period. The spread between producer prices and retail prices in each of the years of 2003, 2004, 2005, and 2006 was wider than at any time in the industry's recent history.[30] Furthermore, for the period June through August 2005, after USDA warned that

[29] *See* U.S. Department of Agriculture, Foreign Agricultural Statistics Database, *Production, Supply and Distribution Online*, available at http://www.fas.usda.gov/psd/complete_files/LP-0111000.csv.
[30] *See* U.S. Department of Agriculture, Economic Research Service, *Beef Values and Price Spreads*, available at http://www.ers.usda.gov/briefing/foodpricespreads/meatpricespreads/. *See also* U.S. Department of Agriculture, Economic Research Service, *Retail Price Spreads, Red Meat Yearbook*, available at http://usda.mannlib.cornell.edu/data-sets/livestock/94006/.

beef prices were too high,[31] the producer's share of the consumer's beef dollar fell below the historical low annual average of only 44 percent received in 2002,[32] when live cattle prices were seriously depressed and selling for $11.52 per cwt. less than producers received a dozen years earlier in 1990.[33] Live cattle prices fell to a 17-month low during the month immediately following USDA's public statement that beef prices were too.[34]

Thus, despite the relief associated with higher cattle prices that resulted from the closure of the Canadian border, it was the beef processing and retailing sectors that increasingly captured the lion's share of the record high beef prices experienced in 2003, 2004, 2005, and 2006, not U.S. cattle producers.

While USDA reports issued as recently as December of 2005 continued to predict bullish prices for domestic cattle prices,[35] something went terribly wrong beginning in January 2006 and live cattle prices fell precipitously. Fed cattle prices that were averaging $96.50 per cwt. in December of 2005 nosed downward in January 2006 and continued to decline for a full five months, hitting a low of $79.10 per cwt. in May of 2006.[36] This substantial decline more than ate up the entire increase in cattle prices experienced between the years 2002 and 2003.[37] U.S. cattle feeders again experienced staggering losses during the period of February through June of 2006. As revealed in Figure 3 below, U.S. cattle feeders lost over 3/4 of a billion dollars just from the sales of fed steers during the early months of 2006.

[31] Associated Press, *USDA Secretary Johanns: Beef Prices Too High,* Emily Johns, June 10, 2005.
[32] *Ibid.*
[33] U.S. Department of Agriculture, Economic Research Service, *Table 59, Slaughter Steer Price, Choice 2-4, Nebraska Direct, 1100-1300 lbs., Red Meat Yearbook*, available at http://usda.mannlib.cornell.edu/data-sets/livestock/94006/livestocklprices.xls.
[34] *Ibid.*
[35] *See* U.S. Department of Agriculture, Economic Research Service, *Livestock Dairy and Outlook Report LDP-M-138*, December 16, 2005, available at http://www.ers.usda.gov/Publications/LDP/Dec05/LDPM138T.pdf. "Interruptions in cattle moving to packing houses due to weather markets, such as the one observed last week in the Northern and Central Plains, will occur from now until April, briefly boosting prices with each occurrence."
[36] *See* U.S. Department of Agriculture, Economic Research Service, *Beef Values and Price Spreads*, available at http://www.ers.usda.gov/briefing/foodpricespreads/meatpricespreads/.
[37] *Ibid.*

Figure 3

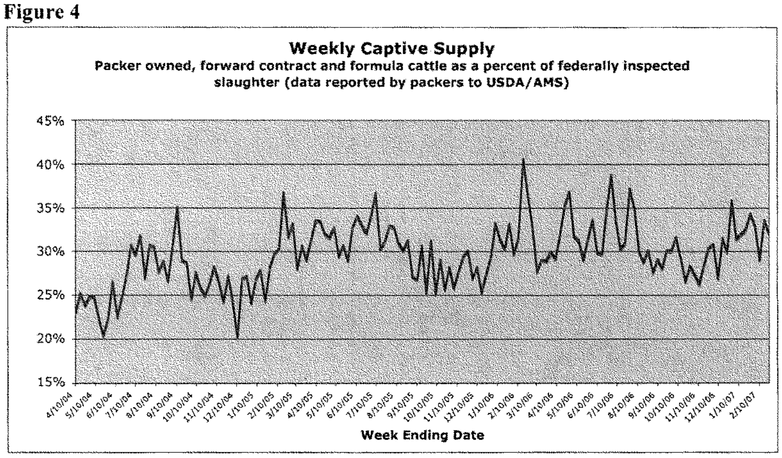
Month	**Great Plains Estimated Losses per Pound**[38]	**Estimated Live Weight**[39]	**Estimated per Head Loss**	**Number of Steers Slaughtered**[40]	**Total Loss to U.S. Cattle Feeders**
February 2006	(.0408)	1,200	($48.96)	1,189,000	($58,213,440)
March 2006	(.0983)	1,200	($117.96)	1,481,000	($175,052,640)
April 2006	(.1043)	1,200	($125.16)	1,400,000	($175,224,000)
May 2006	(.1293)	1,200	($155.16)	1,674,000	($259,737,840)
June 2006	(.0451)	1,200	($54.12)	1,752,000	($94,818,240)
Total 5-Month Loss on Steers				7,496,000	**($763,046,160)**

Based on these large financial losses associated with only fed steers, it can be conservatively estimated that U.S. cattle producers lost more than $1 billion during this 5-month period, given that comparable losses were experienced by feeders who fed the over 4.2 million fed heifers that were also marketed during this timeframe.[41] The circumstances surrounding the unexpected drop in cattle prices warrant careful review.

As revealed in Figure 4 below, weekly captive supply numbers increased significantly beginning in late 2005 and early 2006. In February 2006, all four major meatpackers – Tyson, Cargill, Swift & Co., and the National Beef Packing Co. – withdrew from the cash market in the southern plains for an unprecedented period of two weeks. The packers made minimal to no purchases on the cash market, relying on captive supplies of cattle to keep their plants running for two weeks and cutting production rather than participating in the cash market. As a result of the packers shunning the cash market, cash prices fell for fed cattle, replacement cattle, and in futures markets. Only with falling prices did packers reenter the cash market.

[38] *See* U.S. Department of Agriculture, Economic Research Service, *Production Indicators, Livestock Dairy and Outlook Reports,* January 2006 – June 2006, available at http://www.ers.usda.gov/Publications/LDP/.
[39] *See* U.S. Department of Agriculture, Economic Research Service, *High Plains Cattle Feeding Simulator, Livestock, Dairy and Poultry Outlook Tables*, at fn. 2, Updated May 22, 2006, available at http://www.ers.usda.gov/Publications/LDP/xlstables/High%20Plains%20Cattle%20Feeding%20Simulator%20May06%20F.xls. The USDA simulator is based on 1100 – 1300 pound steers, or an average of 1200 lbs.
[40] *See* U.S. Department of Agriculture, Economic Research Service, *Meat Statistics, Livestock Dairy and Outlook Reports*, January 2006 – June 2006, available at http://www.ers.usda.gov/Publications/LDP/.
[41] *Ibid.*

Figure 4



It is important to note that the abandonment of the cash market in February of 2006 occurred after the Livestock Mandatory Price Reporting (MPR) program expired. Thus, much less information regarding the incident is available than would be if the program had still been in effect. The episode may have lasted for much longer than the two weeks we can verify through public sources, possibly dragging on for as long as three or four weeks. Yet, without the benefit of the market transparency provided by the MPR program, we are only able to rely on other public sources of information documenting that the withdrawal from cash markets lasted for at least two weeks. The simultaneous abandonment of the cash market for cattle began in early February and continued through February 17. On February 13, 2006, market analysts reported that no cattle had sold in Kansas or Texas in the previous week.[42] No cash trade occurred on the southern plains through Thursday of the next week, marking, as one trade publication noted, "one of the few times in recent memory when the region sold no cattle in a non-holiday week."[43] Market analysts noted that "[n]o sales for the second week in a row would be unprecedented in the modern history of the market."[44] During the week of February 13 through 17, there were no significant trades in Kansas, western Oklahoma, and Texas for the second week in a row.[45] R-CALF USA members are convinced that the meatpackers' strategic timing and use of their captive supply cattle was the principal force that drove cattle prices down in the first half of 2006.

During the 2006 summer, fed cattle prices remained in the low $80s. By September cattle prices began to recover and were in the low $90s. Then, during the week that ended October 13, the meatpackers cast a negative psychology upon the market: three of the nation's

[42] "Packers Finally Seriously Cut Kills," *Cattle Buyers Weekly* (Feb. 13, 2006).
[43] "Classic Standoff Continues Through Thursday," *Cattle Buyers Weekly* (Feb. 20, 2006).
[44] *Id.*
[45] Curt Thacker, "Cash Cattle Quiet 2-20," *Dow Jones Newswires* (Feb. 20, 2006).

four largest beef packers announced they would all reduce cattle slaughter.[46] Even though they had bought very few cattle in the south and were short supplied, they cited high cattle prices, tight supplies, weak beef demand, and limited export access as the reasons they were cutting back.[47] During that week, the packers reportedly slaughtered an estimated 10,000 fewer cattle than the previous week, but 16,000 more cattle than they did the year before. Fed cattle prices still fell $2 to $3 and feeder prices fell $3 to $10.[48]

By Friday of the next week, October 20, the packers slaughtered 14,000 more cattle than they did the week before and 18,000 more cattle than the year before – obviously they didn't cut back slaughter like they said they would. In fact, the nation's federally inspected cattle slaughter increased steadily each week after the week ending October 14, 2006, with over 32,000 more cattle slaughtered the week ending November 4, 2006 than were slaughtered during the week ending October 14, 2006.[49] But live cattle prices kept falling, with fed cattle prices down another $1 to $2 and feeder cattle down another $4 to $12 by October 20, 2006.[50] Following this mid-October episode, fed cattle prices were pushed back to the mid to high $80s for the next five months.[51]

To those of us whose livelihoods depend on a properly functioning, competitive market, the events that took place in 2006 clearly show that the meatpackers are using their buying power to manage the price of domestic cattle. Using techniques such as negative market psychology, minimal market transparency, and increased captive supplies, the meatpackers gained significant control over the price of domestic cattle, to the financial detriment of us producers.

In the 2007 Farm Bill, steps must be taken to guard aggressively against anticompetitive practices and protect producers from the abuse of market power. There are two key components to this strategy: 1) strengthening tools to combat excessive concentration in the meatpacking industry; and 2) improving regulation to prohibit unfair contracting practices that deny market transparency and reduce producer bargaining power in open markets.

C. NEEDED REFORMS

The Farm Bill should ensure that antitrust and competition laws are effectively and vigorously enforced. The Farm Bill should provide additional funding for antitrust enforcement and ensure that the various government agencies entrusted with enforcement better coordinate their work to make the most of limited resources. Numerous studies have criticized the failure of the USDA's Grain Inspection, Packers, and Stockyards Administration, the Department of Justice, and Fair Trade Commission to work together more aggressively to scrutinize mergers

[46] Bob Buergdorfer, "Struggling U.S. Beef Industry Cuts Production," *Reuters* (October 10, 2006); *see also* "Swift to Stay with Reduced Production at U.S. Facilities," *Meatpoultry.com* (October 10, 2006).
[47] *See Ibid; see also* "National Beef Cuts Hours at Two Kansas Plants (Dodge City, Liberal), *Kansas City Business Journal* (October 10, 2006).
[48] *See* "Livestock Market Briefs," *Brownfield Ag Network* (October 13, 2006).
[49] *See* "Actual Slaughter Under Federal Inspection," *USDA Market News,* U.S. Department of Agriculture, Agricultural Marketing Service, for week ending 10/14/06, 10/21/06, 10/28/06, 11/04/06.
[50] *See* "Livestock Market Briefs," *Brownfield Ag Network* (October 20, 2006).
[51] *See* U.S. Department of Agriculture, Economic Research Service, *Beef Values and Price Spreads*, available at http://www.ers.usda.gov/briefing/foodpricespreads/meatpricespreads/.

and acquisitions in the industry and to pursue a proactive strategy for preempting and remedying anticompetitive practices.[52] Steps to consider include additional dedicated funding for the agencies to enforce antitrust rules in the meatpacking industry; regular reporting to Congress on cases referred, pursued, and prosecuted; and the establishment of market consolidation thresholds that trigger enforcement action. R-CALF USA supports the creation of an Office of Special Counsel at USDA to oversee both investigations under, and enforcement of the Packers and Stockyards Act (P&S Act).

Early last year, the Office of Inspector General (OIG) found that GIPSA's investigative tracking system for violations of the Packers and Stockyards Act was inaccurate and incomplete, that GIPSA's process for managing investigations was inadequate, that GIPSA left important policy decisions unmade for months and even years, and that previous recommendations from the OIG and the GAO to strengthen GIPSA had not been fully implemented. As a consequence of these failures, GIPSA has referred only one competition investigation to the USDA's Office of General Counsel (OGC) for follow-up since the end of 2002, and the OGC has not filed any administrative complaints against the meatpacking industry since 1999.[53]

R-CALF USA believes that (1) Congress should amend the P&S Act to prevent unfair or deceptive practices, to define "unreasonable preference or advantage," and to correct a recent misinterpretation by the U.S. appellant court system: a meatpacker should not be allowed to avoid the P&S Act's jurisdiction by claiming it engaged in unfair market practices (that are harmful to the economic wellbeing of producers) in order to maintain competitiveness with other meatpackers, that are likewise engaged in the same unfair practices. (3) Congress should take steps to reduce the volume of captive supplies. Limiting packer ownership of livestock and requiring a certain percentage of daily slaughter to be purchased from the cash market would minimize the negative effects of current captive supply use. (4) Congress should take steps to prohibit the use of certain anti-competitive, forward contracts that are not transparent and that do not contain a firm base price. In addition, the law should require processors to bargain in good faith and prohibit other unfair contract practices by (5) requiring a fixed base price in formula contracts; (6) ensuring cattle purchase contracts include a clear disclosure of producer risks; (7) requiring contracts to be traded in open, public markets and prohibit confidentiality clauses; and (8) Improving termination and arbitration provisions to protect producers' rights. Many of these important reforms are presently included in S. 622, S. 305, S. 786, and S. 1017.

Importantly, Congress should also remove the present deterrent against the expansion of state inspected meat processing plants. This deterrent is the result of restrictions that prohibit state inspected meat plants from engaging in interstate commerce. This deterrent can be lifted by allowing the interstate shipment of state inspected beef.

[52] *See, e.g.*, General Accounting Office, *Packers and Stockyards Programs: Actions Needed to Improve Investigations of Competitive Practices*, GAO/RCED-00-242, Sept. 2000 and General Accounting Office, *Justice's Antitrust Division: Better Management Information Is Needed on Agriculture-Related Matters*, GAO-01-188, April 2001.

[53] Audit Report, Grain Inspection, Packers and Stockyards Administration's Management and Oversight of the Packers and Stockyards Program, U.S. Department of Agriculture Office of Inspector General, Report No. 30601-01-Hy, January 2006.

III. CONSUMER INFORMATION AND INFORMATION DISCLOSURE

A. MANDATORY COUNTRY OF ORIGIN LABELING

Congress passed mandatory Country of Origin Labeling (COOL) for beef and other perishable agricultural products in 2002. The American people in poll after poll support knowing what country their food comes from, and domestic producers believe that labeling provides an excellent opportunity for promoting high-quality U.S agriculture products.[54] Due to historical anomalies in country-of-origin marking rules and the marking practices of the Bureau of Customs and Border Patrol, beef and other perishable products are some of the few items consumers purchase in the U.S. that lack country of origin information.[55] The vast majority of other developed countries have already implemented country-of-origin labeling programs for such products, including beef.[56] The positive track record with seafood country of origin labeling proves that such labeling can be implemented to the benefit of both consumers and industry in the U.S. Unfortunately, despite broad public support and the proven success of similar programs, COOL implementation was recently delayed until 2008 due to widespread misunderstandings about the costs and benefits of COOL.

Congress should restore COOL by moving its implementation date to September 30, 2007, as provided in S. 404. In addition, Congress should outline an implementation approach that ensures COOL is administrated in the most simple and cost-effective manner for producers while providing the full scope of information to consumers contemplated in the original COOL law. The GAO and independent analysts have expressed concern that initial plans for COOL implementation outlined by USDA are unnecessarily burdensome and expensive, and could be simplified significantly.[57] Packers should be capable of identifying those animals exclusively born and raised in the U.S., whose meat qualifies for a "U.S." label of origin under COOL, without passing along undue additional costs and legal liabilities to producers. Current marking and sealed conveyance requirements for cattle imported from Canada and Mexico due to health and safety concerns, together with any necessary modifications to marking law and regulations which exempt imported cattle from regular import marking requirements, should be sufficient to ensure that packers have all of the information they need to comply with COOL without imposing additional burdens on cattle producers. Finally, the Farm Bill should establish technology grants for COOL-related or other meat traceability programs to facilitate their implementation.

B. PRICE TRANSPARENCY

The 2007 Farm Bill should help promote transparency in the market by extending and strengthening Livestock Mandatory Price Reporting. Recently the GAO recommended a number of ways in which the current price reporting program could be improved to ensure that more

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[54] *See, e.g.*, John VanSickle et al., "Country of Origin Labeling: A Legal and Economic Analysis," University of Florida Institute of Food and Agricultural Science, May 2003. (Hereinafter VanSickle).
[55] *See, e.g.*, General Accounting Office, *Country-of-Origin Labeling: Opportunities for USDA and Industry to Implement Challenging Aspects of New Law*, GAO-03-780, Aug. 2000. (Hereinafter GAO-03-780).
[56] *Id.*
[57] *See, e.g.*, GAO-03-780 and VanSickle.

accurate and complete data are available, and the Farm Bill should adopt and build upon these recommendations.[58]

IV. HEALTH AND SAFETY

A. PREVENTING DISEASE INTRODUCTION

Congress should take steps to counteract the radical policy shift recently initiated by the USDA to abandon longstanding U.S. import restrictions established to prevent the introduction of foreign animal diseases in favor of attempting to mitigate disease spread after it is introduced. Unfortunately, the Animal Health Protection Act does not contain standards with which to measure the USDA's performance in preventing the introduction of foreign animal diseases; nor does it expressly state under what conditions the USDA is to impose import restrictions for this purpose. Congress should provide clearer direction to the USDA in this regard by amending the Animal Health Protection Act in the 2007 Farm Bill. Meanwhile, Congress should pass a Resolution of Disapproval to force the withdrawal of the USDA's proposed rule to allow the importation of cattle over 30 months of age and beef products from cattle over 30 months of age from Canada, a country that has detected multiple cases of BSE born years after the implementation of its feed ban.

In addition, Congress should take immediate steps to (1) prevent the USDA from continually relaxing BSE-related import standards for both Canada and Japan as this action subjects the U.S. cattle industry to increased exposure to BSE. (2) Prevent the USDA from relaxing our foot and mouth disease (FMD) disease protections via its proposal to allow a region of FMD-affected Argentina to begin importing fresh and chilled beef into the United States. (3) Require the USDA to impose more effective restrictions on the importation of cattle from Mexico in light of recent testimony by the USDA Office of Inspector General that indicates that approximately 75 percent of all bovine tuberculosis cases detected under U.S. slaughter surveillance originated in Mexico.[59]

Following the discovery of a Canadian cow with bovine spongiform encephalopathy (BSE) in Washington State in 2003, more than 50 countries banned U.S. cattle and beef imports, costing the U.S. industry billions of dollars. Though some key export markets, such as Japan, have begun to loosen their import bans on U.S. beef, it is unlikely that this partial market opening will allow for the full resumption of previous export volumes. While the U.S. has struggled to negotiate even limited access for U.S. cattle and beef exports to foreign markets, the domestic market has been thrown open to a much broader range of imports from abroad. As a result, cattle and beef imports into the U.S. face lower standards than U.S. exports must meet

[58] Government Accountability Office, *Livestock Market Reporting: USDA Has Taken Some Steps to Ensure Quality, but Additional Efforts Are Needed*, GAO-06-202, Dec. 2005.
[59] Statement of the Honorable Phyllis K. Fong, Inspector General, before the Subcommittee on Agriculture, Rural Development, Food and Drug Administration, and Related Agencies, Committee on Appropriations, U.S. House of Representatives, March 1, 2007, at 9.

overseas, giving foreign countries an excuse to keep their markets closed due to the potential risks posed by the lower health and safety standards the U.S. applies to its imports.

In the case of Japan, for example, USDA agreed to allow imports of Japanese beef with no age limits while securing access to Japan only for U.S. beef from animals aged 20 months or younger. The broad opening to Japanese beef makes the U.S. the only major beef-consuming country in the world to accept beef from a BSE-infected cattle herd – regardless of the scope of the disease problem in that country and without requiring the more stringent BSE risk mitigation measures recommended by the OIE (World Organization for Animal Health). This lack of a coherent BSE protection policy presents a major obstacle to United States cattle producers who seek to protect their herds from disease and market their high-quality product around the world.

The Farm Bill should lay out an aggressive, comprehensive global strategy for protecting the integrity of the United States cattle and beef supply. Ultimately, global markets for U.S. products will not re-open fully if U.S. health and safety standards, particularly import standards, are perceived as inadequate. The Farm Bill should direct USDA to engage with other countries to upwardly harmonize global import standards for beef. These standards must provide the highest level of protection for animal health and food safety and rely on sound science. The Farm Bill can ensure that USDA makes health and safety a top priority as it works to restore global export markets for U.S. beef by:

- Closing loopholes in the U.S. feed ban that were identified by an international scientific panel convened by USDA more than two years ago;
- Instructing USDA to adopt the most stringent BSE risk mitigation measures recommended for both imports and exports by the OIE pending an international agreement on BSE standards;
- Employing more FSIS meat inspectors to work the lines in the large processing plants rather than using HACCP inspection so that Specified Risk Materials (SRMs) and other prohibited cow parts are not entering the food system;
- Allowing voluntary BSE testing by U.S. packers; and
- Directing USDA to take the lead in bringing countries together to upwardly harmonize BSE standards that would allow trade of safe cattle and beef products to resume and prevent any further global spread of the disease.

A coherent, global approach to health and safety in the cattle and beef sector will protect livestock health, ensure that products coming into the U.S. face standards as high as U.S. exports face overseas, provide producers with certainty and predictability, and confirm for consumers at home and abroad that U.S. beef is among the safest, highest-quality product in the world.

B. IMPROVING ANIMAL DISEASE TRACE-BACK CAPABILITIES

The 2007 Farm Bill should be used to prohibit the USDA from imposing a costly and onerous mandatory animal identification system on the U.S. cattle industry. Congress, instead, should take steps to strengthen and expand the time-proven Brucellosis surveillance and vaccination program, which involves the placement of a permanent metal ear tag in breeding females. This current disease trace-back system, if strengthened and combined with the state brand laws in 17 states, would significantly improve the United States' current disease trace-back capabilities as desired by U.S. animal health officials.

V. TRADE

While the Farm Bill does not typically address U.S. trade policy, these policies have significant impacts on U.S. cattle producers, and it is therefore important that the Farm Bill examine whether U.S. trade policies are consistent with broader policy goals for the cattle and beef sector. The U.S. has not enjoyed a trade surplus in cattle and beef trade since 1997 in dollar terms, and the deficit in the sector has exploded over the past six years, hitting more than $3.3 billion in 2004. Given the supply-sensitive nature of the market for U.S. cattle, the growing trade deficit in both cattle and beef has a profound impact on the U.S. cattle industry. The lack of harmonization of health and safety standards plays a large role in the loss of U.S. export markets. United States' competitiveness is also undermined by large subsidies and high tariffs on cattle and beef in other countries, while the U.S. market is one of the most open in the world and U.S. cattle producers receive no trade-distorting subsidies. It will also be important that USDA become more engaged in researching how exchange rates play into agricultural trade flows and monitoring the manipulation of exchange rates.

Congress outlined a number of steps that should be taken to eliminate the gross distortions plaguing global cattle and beef trade in the Trade Act of 2002.[60] There have been varying degrees of progress in meeting these objectives in ongoing negotiations at the World Trade Organization (WTO). In the Trade Act of 2002, Congress called for reduction of foreign tariff levels to meet U.S. levels,[61] which would require substantial reductions in beef tariffs by trading partners such as Japan and Korea. It is too early to tell whether this goal will be met in the Doha Round because of on-going discussions around the scope of carve-outs for sensitive products and the extent of tariff reductions, though negotiators have agreed in principle to a formula that would cut higher tariffs more steeply than low tariffs. Congress also called for the elimination of "subsidies that decrease market opportunities for U.S. exports or unfairly distort agriculture markets" in the Trade Act of 2002.[62] Significant progress has been made on this objective, as WTO negotiators have agreed in principle to eliminate export subsidies in agriculture by 2013 and called for substantial reductions in trade-distorting domestic support.

Finally, because of the limited time periods in which perishable products can be marketed, Congress also called for the creation of special rules on perishable and cyclical agricultural products such as cattle and beef and timely access for growers of such products to import relief mechanisms.[63] R-CALF USA is troubled by the possibility that the special safeguard for agriculture that currently exists for beef could be given up by the U.S. at the WTO without the establishment of special rules for perishable and cyclical agriculture as directed by Congress. Preserving the right of developing countries to employ the special safeguard for agriculture while eliminating the right to do so for developed countries such as the U.S. could

[60] 19 U.S.C. § 3802.
[61] 19 U.S.C. § 3802(b)(10)(A)(ii).
[62] 19 U.S.C. § 3802(b)(10)(A)(iii).
[63] 19 U.S.C. § 3802(b)(10)(A)(ix) – (x) and (B)(i).

result in a mismatch of market opportunities that puts U.S. cattle producers at a competitive disadvantage. While the U.S. has tabled an initial paper flagging the need to discuss the creation of special rules for perishable and cyclical agriculture within the Doha Rules negotiations, it does not appear that this issue has been developed any further within the negotiating group.

There is no doubt that further trade liberalization without special safeguards will erode the market for the U.S. cattle industry. This could happen even in the absence of unfair trade practices. The U.S. Trade Deficit Review Commission noted, "Easy availability of imports can limit price increases either by expanding available supply or reducing the ability of businesses to raise prices in order to pass on increases in their costs."[64] This dynamic is particularly apparent in the cattle and beef industry, where, as former U.S. International Trade Commission Chairwoman Lynn Bragg observed, "The concentration of packers increases the packers' leverage relative to cattle producers, thus providing packers the ability to use imports to reduce domestic live cattle prices and/or prevent price increases."[65]

In addition, the Farm Bill should create a global marketing information program – building upon existing data sources such as the FAO – to provide regularly updated information by country on commodity prices, supply and consumption trends, exchange rate impacts, and the dominant market shares of trading companies in order to help U.S. producers better target potential export markets. This need for better trade information was highlighted in the report of the bipartisan U.S. Trade Deficit Review Commission, which noted, "The growing importance of trade in our economy and the needs of government and businesses for information to be able to make good decisions make it essential that data on international trade in goods and services be relevant, accurate, and timely."[66]

VI. <u>SUPPORT A STRONGER, MORE COMPETITIVE CATTLE AND BEEF SECTOR</u>

The 2007 Farm Bill is the ideal vehicle to make needed reforms to the current beef check-off program. Amendments are needed to this current program to (1) allow U.S. cattle producers to use their check-off contributions to promote beef that is exclusively born, raised, and slaughtered in the U.S., rather than to promote generic beef regardless of its origin; (2) provide for a periodic referendum every five years; (3) allow direct contracting of the program with vendors to avoid possible conflicts of interest; (4) limit representation by any one national policy organization on the Cattlemen's Beef Board to no more than 40 percent; (5) expand the definition of eligible program contractors to include organizations formed after the implementation of the program; and (6) limit contract awards to prevent any recipient from receiving more than 30 percent of annual award amounts.

VII. <u>CONCLUSION</u>

[64] "The U.S. Trade Deficit: Causes, Consequences and Recommendations for Action," Final Report of the U.S. Trade Deficit Review Commission, Nov. 14, 2000 at 26.
[65] *Live Cattle from Canada*, Inv. No. 731-TA-812 (Final), USITC Pub. 3255, Nov. 1999 at 50.
[66] "The U.S. Trade Deficit: Causes, Consequences and Recommendations for Action," Final Report of the U.S. Trade Deficit Review Commission, Nov. 14, 2000, at ch. 7.

The 2007 Farm Bill presents an important opportunity to reform U.S. agriculture policy to level the playing field for U.S. cattle producers. A dedicated competition title in the 2007 Farm Bill should guarantee a competitive domestic market for cattle and beef, improve consumer information and information disclosure, strengthen safeguards for health and safety, address global distortions in cattle and beef markets, and strengthen programs to support the continued vitality of the largest sector of United States agriculture.

Thank you, again, for allowing me the opportunity to provide input at this important hearing.

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Written Statement
of
National Association of State Departments of Agriculture (NASDA)
for the
House Agriculture Committee
Subcommittee on Livestock, Dairy and Poultry
Regarding
Competition in Agricultural Markets and Interstate Meat Sales
April 17, 2007

The National Association of State Departments of Agriculture (NASDA) represents the commissioners, secretaries and directors of agriculture in the fifty states and four territories. As Congress develops the 2007 Farm Bill, we urge the committee to address an important market competition issue and allow state-inspected meat and poultry to be sold in the national marketplace. Current law restricts fair, competitive, and open markets for small farms and meat processors.

Consumers in the United States enjoy the safest meat and poultry supply in the world. The foundation of this success is our system of food safety laws and inspection programs. Ironically, these same laws also unfairly penalize hard-working small business owners in the U.S. while giving preference to imports of meat products from foreign countries such as Croatia and Nicaragua. Meat and poultry products (beef, poultry, pork, lamb and goat) inspected under state inspection programs may only be sold within the borders of the state in which it is inspected. This makes no sense, whatsoever.

Three USDA Advisory Committees have recommended repealing the outdated law because it would create jobs and stimulate rural economic growth. More than 40 national, state and local agricultural organizations have urged Congress to level the economic playing field for small meat processors, and to allow them national market access. Congress needs to finally address this issue in the 2007 Farm Bill.

FAIR COMPETITION AND MARKET ACCESS

Twenty-eight states currently have their own meat and poultry inspection programs. We serve more than 2,000 state-inspected meat processors–mostly small, family-owned businesses–who are prevented from competing in the national marketplace. Consolidation in the meat processing industry continues to leave smaller farmers and ranchers with fewer and fewer buyers for their livestock and poultry. How can this arbitrary marketing restriction be justified, especially when imported foreign meat and poultry products can be freely shipped and sold anywhere in the United States?

The question before Congress is a simple fairness issue. Allowing interstate meat sales will resolve a basic inequity that has existed since 1967. The reasons to act promptly are clear and compelling:

- Meat and poultry products from 34 foreign countries can be freely shipped and sold anywhere in the United States, but domestic small businesses and processors cannot. This is unfair and wrong. *Why are small businesses in the U.S. denied the same market opportunities that are given to companies in foreign countries?*

- The restriction on interstate meat sales does not apply to "non-amenable" products—such as venison, pheasant, quail, rabbit, alligator and a host of others. These products are normally regulated by state inspection programs, yet can be shipped in interstate commerce without restriction. It does not make sense to allow these products across state borders while beef, pork, lamb and goat cannot be shipped interstate. *Where is the logic in this?*

- No other state-inspected food commodities are prohibited from being shipped across state lines. Other state-inspected food products (milk, dairy products, fruit, vegetables, fish and shellfish) are freely marketed across the country. *Why aren't the same market options available for meat and poultry?*

- Our locally-produced, state-inspected meat are some of the best specialty products in the country. Most of these small, state-inspected companies make and sell specialty products such as sausages, bratwurst, jerky and ethnic meat products which are generally not cost-effective product lines for large operations. *It doesn't make sense to say consumers in Iowa can enjoy these products while consumers across the state border in Missouri cannot eat and enjoy the same products.*

ECONOMIC GROWTH FOR RURAL SMALL BUSINESS

Livestock production and processing are the most important agricultural industries in many rural communities. Most state-inspected meat and poultry plants are owned and operated by small business owners who want to sell their products in the local region. Most of them produce specialty and seasonal meat products. They provide a market for local cattle, hog, goat, and sheep producers. However, the current ban on interstate meat sales prevents these small processors and businesses from serving rural areas which straddle state boundaries.

Market access is critical for small producers and processors who want to market and sell their products to consumers, grocery stores, and other retailers in multi-state regions. Maintaining the interstate sales ban denies these market sales to them. It also prevents them from capitalizing on other sales opportunities such as niche marketing through mail-order gift catalogs and internet sales. Internet sales now offer a huge potential for small rural businesses to sell their specialty products in the global marketplace. This innovation in the marketplace did not exist a few years ago, yet the interstate sales ban prevents these entrepreneurs from using this technology today.

Small processors and businesses are denied other economic opportunities as well, including sales to federally-inspected plants for further processing into finished products.

Concentration in the food processing sector continues to trend upward. This reduces market competition, and leaves farmers and ranchers with fewer and fewer buyers for their livestock. In some regions, farmers have to transport animals over long distances. The state-inspected plant is the most likely choice for farmers selling locally because they are generally smaller and more locally available. Allowing more competition in the national marketplace will give farmers and ranchers more local plant options for delivering their livestock.

Increased markets will not only benefit producers, processors and small businesses, but it also gives consumers more choices at the supermarket and convenient stores. It's just common sense and it's the right thing to do. *It is ridiculous that under current law, a restaurant in Minnesota or Virginia can purchase beef from a foreign competitor overseas, but not from a plant in Texas. How can anyone justify this?*

LOCAL ECONOMIC BENEFITS

Interstate markets for state-inspected products will help stimulate rural economies, create jobs and increase local tax bases. Increased markets will not only benefit producers and processors, but related industries such as paper products, printers, seasonings, distributors, and local shops carrying regional products. The Wisconsin Association of Meat Processors conducted a survey of their small business owners in April 2006. In the survey:

33% believed that interstate shipment would increase their total sales by more than 10%.
33% responded that interstate shipment would increase their total sales by 5 to 10%.
29% believed their sales would grow by 1 to 5%.

The Wisconsin survey also asked how this potential, additional sales increase would benefit their business and local economy. The survey showed:

79% would add employees or increase payroll hours.
83% would invest in additional equipment.
64% would expand their existing plant.
42% would open new retail locations.

SUPPORT FROM USDA & ADVISORY COMMITTEES

The debate about interstate meat sales has gone on long enough. Three USDA Advisory Committees have recommended that the ban on interstate shipment be removed because it would create jobs and stimulate rural economic growth:

- USDA's Advisory Committee on Agricultural Concentration (June 1996) issued a report recommending that USDA take "*aggressive action to end the inequities in meat inspection and that appropriate steps be taken to promote the ability of state-inspected packing plants that meet federal standards of inspection to compete by selling meat in interstate commerce.*"

- USDA's National Commission on Small Farms (January 1998) issued a report "*A Time to Act.*" The report outlines a general policy goal to "promote, develop and enforce fair, competitive and open markets for small farms." Specifically, the report "*urges USDA to take aggressive action in a timely manner to end the inequities in meat inspection. With regard to federal and state inspections, the commission recommends that appropriate steps be taken to promote the ability of state-inspected packing plants that meet federal standards of inspection to compete by selling meat in interstate commerce. Provided, however, that such steps do not undermine the integrity of the U.S. position regarding acceptable standards and safeguards for imported meat.*"

- The National Advisory Committee on Meat and Poultry Inspection (NACMPI) endorsed interstate meat sales in two reports (May 1998 and June 2002). NACMPI serves as an advisory committee to the USDA Secretary to consult before issuing product standards and labeling changes and on other matters affecting federal and state inspection programs.

LEGISLATIVE SUPPORT IN CONGRESS

Legislation to allow interstate meat sales has been introduced and debated in Congress for more than a decade. All of the hearings, reports, recommendations, and legislation have supported removing the ban on interstate meat sales.

The 1996 Farm Bill required USDA to submit recommendations to Congress on the steps necessary to achieve interstate meat sales. USDA sought public comment, held public hearings and developed a legislative proposal, which was subsequently introduced in Congress in 1999. At Senate Agriculture

Committee hearings in April 2000, USDA Deputy Secretary Richard Rominger testified for USDA and supported removing the ban on interstate meat sales.

The 2002 Farm Bill included language supporting the merits of interstate meat sales and required USDA to conduct a new, comprehensive review of state inspection programs. USDA began this review and further strengthened testing and training requirements in spring 2003, and in January 2007 issued a report which concluded that state inspection programs are "at least equal to" federal inspection. This review data continues to show that state inspection programs are highly effective and provide consumers with a wholesome, unadulterated food product that is properly labeled and safe.

There simply is no longer any valid reason to continue the ban on interstate meat sales. Congress needs to finally address this issue in the 2007 Farm Bill. The state departments of agriculture stand ready to work with the Committee on this effort which will greatly benefit producers, processors, and consumers.

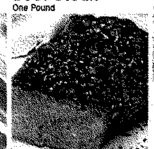
Farmer's Share Of Retail Food Dollar

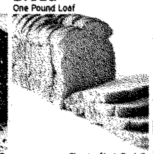
Did you know that farmers and ranchers receive only 20 cents of every food dollar that consumers spend on food at home and away from home?

According to USDA, off farm costs including marketing, processing, wholesaling, distribution and retailing account for 80 cents of every food dollar spent in the United States.

Bacon
One Pound

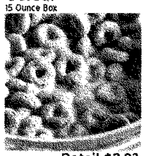
Retail $3.49
Farmer $0.44

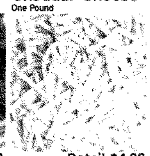
Beef Steak
One Pound

Retail $6.99
Farmer $0.84

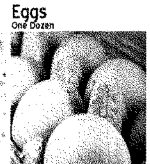
Bread
One Pound Loaf

Retail $2.69
Farmer $0.10

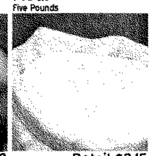
Fresh Carrots
Two Pounds

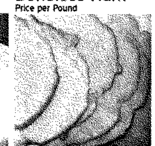
Retail $0.99
Farmer $0.38

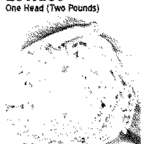
Cereal
15 Ounce Box

Retail $2.93
Farmer $0.08

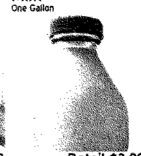
Cheddar Cheese
One Pound

Retail $4.99
Farmer $1.36

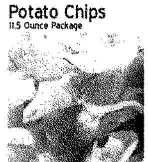
Eggs
One Dozen

Retail $2.19
Farmer $0.67

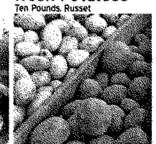
Flour
Five Pounds

Retail $2.15
Farmer $0.48

Boneless Ham
Price per Pound

Retail $3.79
Farmer $0.44

Lettuce
One Head (Two Pounds)

Retail $1.99
Farmer $0.54

Milk
One Gallon

Retail $3.99
Farmer $1.11

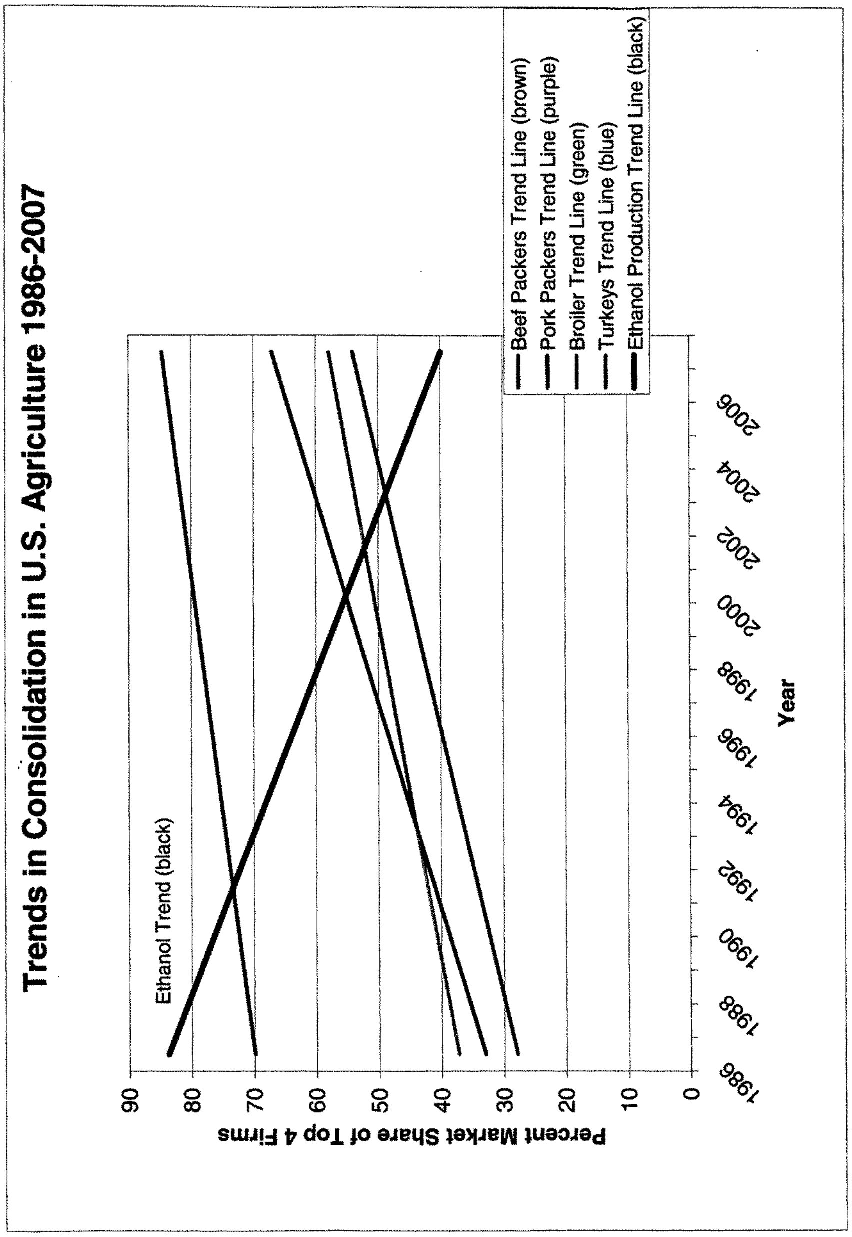
Potato Chips
11.5 Ounce Package

Retail $3.49
Farmer $0.07

Fresh Potatoes
Ten Pounds, Russet

Retail $3.99
Farmer $0.83

Farmer's share derived from USDA, NASS "Agricultural Prices," 2006.
Retail based on Safeway (SE) brand except where noted.

National Farmers Union
Greenwood Village, CO 303-337-5500
Washington, DC 202-554-1600
www.nfu.org

Updated 2-8-07


Trends in Consolidation in U.S. Agriculture 1986-2007
Ethanol Trend (black)
Percent Market Share of Top 4 Firms
0
10
20
30
40
50
60
70
80
90
1986
1988
1990
1992
1994
1996
1998
2000
2002
2004
2006
Year
Beef Packers Trend Line (brown)
Pork Packers Trend Line (purple)
Broiler Trend Line (green)
Turkeys Trend Line (blue)
Ethanol Production Trend Line (black)

January 2007

GIPSA Livestock and Meat Marketing Study

Contract No. 53-32KW-4-028

Volume 1: Executive Summary and Overview

Final Report

Prepared for

Grain Inspection, Packers and Stockyard Administration
U.S. Department of Agriculture
Washington, DC 20250

Prepared by

RTI International
Health, Social, and Economics Research
Research Triangle Park, NC 27709

RTI Project Number 0209230

RTI INTERNATIONAL

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RTI International is a trade name of Research Triangle Institute.

Abstract

Over time, the variety, complexity, and use of alternative marketing arrangements (AMAs) have increased in the livestock and meat industries. Marketing arrangements refer to the methods by which livestock and meat are transferred through successive stages of production and marketing. Increased use of AMAs raises a number of questions about their effects on economic efficiency and on the distribution of the benefits and costs of livestock and meat production and consumption between producers and consumers. This final report focuses on AMAs used in the beef, pork, and lamb industries from the sale of live animals to final meat sales to consumers and addresses the following parts of the Grain Inspection, Packers and Stockyard Administration (GIPSA) Livestock and Meat Marketing Study:

- Part C. Determine extent of use, analyze price differences, and analyze short-run market price effects of AMAs.
- Part D. Measure and compare costs and benefits associated with spot marketing arrangements and AMAs.
- Part E. Analyze the implications of AMAs for the livestock and meat marketing system.

This final report follows the publication of an interim report for the study that used qualitative sources of information to identify and classify AMAs and to describe their terms, availability, and reasons for use. The portion of the study contained in this final report is based on quantitative analyses using industry survey data from producers, feeders, packers, processors, wholesalers, retailers, and food service operators; transactions data and profit and loss (P&L) statements from packers and processors; Mandatory Price Reporting (MPR) data; and a variety of other published data sources.

The final report contains separate volumes that describe the data collection methods and results (Volume 2) and the analysis results for the beef industry (Volume 3), the pork industry (Volume 4), the lamb industry (Volume 5), and meat distribution and sales (Volume 6). Volumes 3 through 6 address the effects of AMAs on prices, costs, quality, risk, and consumers and producers, to the extent feasible given the availability of data.

The principal contributors to this study are the following:

RTI International Management, Data Collection, and Analysis (across all species):

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We would like to thank the anonymous peer reviewers and GIPSA staff who provided comments on earlier drafts, which helped us improve this report. We also thank Melissa Fisch and Sharon Barrell for editing assistance.

This report and the study on which it is based were completed under a contract with GIPSA, U.S. Department of Agriculture (USDA). Any opinions, findings, and conclusions or recommendations expressed in this report are those of the authors and do not necessarily reflect the views of GIPSA or USDA.

Contents

Executive Summary

As part of the congressionally mandated Livestock and Meat Marketing Study, this volume of the final report presents the results of analyses of the effects of alternative marketing arrangements (AMAs) in the fed cattle and beef, hog and pork, and lamb and lamb meat industries. This final report focuses on determining the extent of use of AMAs, analyzing price differences and price effects associated with AMAs, measuring the costs and benefits associated with using AMAs, and assessing the broad range of implications of AMAs. The analyses in this volume were conducted using results of industry interviews, industry survey data, transactions and profit and loss (P&L) statement data from meat packers, Mandatory Price Reporting (MPR) data, and data from other publicly available sources. Analyses are limited to the economic factors associated with AMA use, and the report does not analyze policy options or make policy recommendations.

In this report, AMAs refer to all possible alternatives to the cash or spot market. AMAs include arrangements such as forward contracts, marketing agreements, procurement or marketing contracts, production contracts, packer ownership, custom feeding, and custom slaughter. Cash or spot market transactions refer to transactions that occur immediately, or "on the spot." These include auction barn sales; video or electronic auction sales; sales through order buyers, dealers, and brokers; and direct trades.

It is important to note that the data collection period for the study, October 2002 through March 2005, was an unusual time for the U.S. meat industry. The beef industry experienced a turbulent market because of the discovery of bovine spongiform encephalopathy (BSE) in North America. The initial BSE case in Canada in May 2003 stopped imports of live cattle to the United States. The first U.S. case of BSE in December 2003 blocked U.S. beef exports until July 2005. Cattle prices set annual record highs in 2003, 2004, and 2005. Packers experienced significant losses because of tight cattle supplies and continued imports of Canadian boxed beef. While hog prices were not at record highs, hog producer returns, which were negative during 2002 and much of 2003, turned positive from February 2004 through the end of 2006. The higher hog prices in 2004 and 2005 came at a time of record production, while demand for pork improved. Lamb prices increased sharply—setting record highs in the first quarter and second quarters of 2005—while the supply of lambs declined.

ES.1 GENERAL STUDY CONCLUSIONS

Within the context of these market conditions, the general conclusions of the study are as follows:

- Use of AMAs during the October 2002 through March 2005 period, including packer ownership, is estimated at 38% of the fed beef cattle volume, 89% of the finish hog volume, and 44% of the fed lamb volume sold to packers.
- Packer-owned livestock accounted for a small percentage of transactions for beef and lamb (5% or less), even when the small percentage of partial ownership arrangements is included, but accounted for a large percentage of transactions for pork (20% to 30% depending on assumptions).
- Given the current environment and recent trends, we expect moderate increases in use of AMAs in the lamb industry, but little or no increase in the beef and pork industries.
- Cash market transactions serve an important purpose in the industry, particularly for small producers and small packers. In addition, reported cash prices are frequently used as the base for formula pricing for cash market and AMA purchases of livestock and meat.
- The use of AMAs is associated with lower cash market prices, with a much larger effect occurring for finished hogs than for fed cattle.

- Many meat packers and livestock producers obtain benefits through the use of AMAs, including management of costs, management of risk (market access and price risk), and assurance of quality and consistency of quality.
- In aggregate, restrictions on the use of AMAs for sale of livestock to meat packers would have negative economic effects on livestock producers, meat packers, and consumers.

Primary conclusions for this final report by species are described below.

ES.2 FED CATTLE AND BEEF INDUSTRIES

The primary conclusions for this final report, as they relate to the fed cattle and beef industries (Volume 3), are as follows:

- **The beef producers and packers interviewed believed that some types of AMAs helped them manage their operations more efficiently, reduced risk, and improved beef quality.** Feedlots identified cost savings of $1 to $17 per head from improved capacity utilization, more standardized feeding programs, and reduced financial commitments required to keep the feedlot at capacity. Packers identified cost savings of $0.40 per head in reduced procurement cost. Both agreed that if packers could not own cattle, higher returns would be needed to attract other investors and that beef quality would suffer in an all-commodity market place.
- **Eighty-five percent of small producers surveyed used only the cash market when selling to packers, compared with 24% for large producers, and pricing methods also differed by size of operation.** Large producers used multiple pricing methods, including individually negotiated pricing (74% of producers), public auction (35%), and formula pricing (57%). In comparison, small producers used individually negotiated pricing (32%), public auction (84%), and formula pricing (6%). Four times as many large producers sold cattle on a carcass weight basis with a grid compared with small producers.
- **Ten percent of large beef packers surveyed reported using only the cash or spot market to purchase cattle, compared with 78% of small beef packers.** Large packers relied heavily on direct trade and less on auction barns and dealers or brokers for their cattle procurement compared with small packers.

Conversely, small packers used AMAs for approximately half as much on a percentage basis as large packers. Both large and small packers used multiple pricing methods when buying cattle, including individually negotiated prices, formula pricing, public auction, and internal transfer pricing. While nearly all packers bought some cattle on a liveweight basis, 88% of large packers purchased cattle based on carcass weight with grids, while almost no small packers used this type of valuation.

- **Neither the producers nor packers surveyed expected the use of AMAs to change dramatically in the next 3 years.** In addition, they indicated that their use of AMAs had not changed significantly from 3 years earlier. Auction markets were the predominate marketing method across all producers selling cattle and calves. Based on the survey results, which tend to represent smaller packers, 19% of fed cattle are purchased through auctions. This is a substantially higher percentage than the estimate based on the transactions data obtained from larger packers.
- **The producers surveyed that used AMAs identified the ability to buy/sell higher quality cattle, improve supply management, and obtain better prices as the leading reasons for using AMAs.** In contrast, the producers surveyed that used only cash markets identified independence, flexibility, quick response to changing market conditions, and ability to buy at lower prices and sell at higher prices as primary reasons for using only cash or spot markets.
- **The packers surveyed that used AMAs said that their top three reasons for using AMAs were to improve week-to-week supply management, secure higher quality cattle, and allow for product branding in retail stores.** Much like producers, packers that used only cash markets identified independence, flexibility, quick response to changing market conditions, and securing higher quality cattle as reasons for using only the cash or spot market.
- **Transactions data summarized from the 29 largest beef packing plants during the time period of the study included more than 58 million cattle and 590,000 transactions and indicated that the cash or spot market was the predominate purchase method used.** Specific estimates of the percentage of cattle purchased through each type of marketing arrangement are as follows:

> Note: To ensure the confidentiality of the companies that provided data for this study, the packer ownership category is often combined with other categories in the summary statistics presented in this volume. Results of analysis for the packer ownership category are provided in cases for which the results do not reveal company-specific confidential information.

- 61.7% cash or spot market
- 28.8% marketing agreements
- 4.5% forward contracts
- 5.0% packer owned, other method, or missing information

Thus, marketing agreements are the primary AMA used in the fed cattle and beef industries, but other types of AMAs are used extensively by individual firms for specific reasons that benefit their operations.

- **Transactions data indicate that packing plants in the Cornbelt/Northeast used AMAs less frequently than plants in the High Plains or West regions.** High Plains plants procured 61% of cattle by direct trade, 30% through marketing agreements, and a very small percentage through auctions and forward contracts. Cornbelt/Northeast plants bought the majority of their cattle by direct trade, but some were purchased through auctions and marketing agreements. Plants in the West bought a lower percentage by direct trade compared with the other regions and a higher percentage through marketing agreements and auction barns.
- **Individually negotiated pricing was the most common method used to determine purchase prices for fed cattle.** Specifically, 60% of cattle purchased by plants in the High Plains used individually negotiated pricing, with a similar percentage in the Cornbelt/Northeast and a substantially lower percentage in the West. Formula pricing was used to purchase 34% of the cattle in the High Plains, with a higher percentage in the West and a substantially lower percentage in the Cornbelt/Northeast. The formula was based most often on either U.S. Department of Agriculture (USDA)-reported prices or subscription service prices. Cornbelt/Northeast packers purchased the largest percentage of cattle on a liveweight basis (47%) in comparison with the High Plains (40%) and the West (25%). Packers in the West purchased more than half of their cattle using carcass weight with grid valuation, while packers in the High Plains and Cornbelt/Northeast used this valuation method for 42% and 44% of their purchases, respectively. The remainder were predominately purchased on a carcass weight basis without a grid.

- **Regression analysis of the relationship between all fed cattle transactions prices and use of marketing arrangements indicates that, relative to direct trade transactions, prices for fed cattle sold through auction barns tended to be somewhat higher and prices for fed cattle sold through forward contracts tended to be somewhat lower.** These results are likely due, in part, to the differences in risk associated with the two methods: auction barn sales are subject to greater price risk, but forward contracts ensure market access and a guaranteed price for cattle producers. However, the results also are influenced by the period of the analysis, during which fed cattle prices were at record highs. The prices for fed cattle sold through marketing agreements and transferred through packer ownership were relatively similar to direct trade. Prices for cattle under packer ownership are internal transfer prices that are typically based on external market prices; thus, implications of the results for packer-owned cattle are less clear.
- **Regression analysis of the relationship between cash market (auction barns, dealers and brokers, and direct trade) transactions prices for fed cattle and use of marketing arrangements suggests that if capacity utilization within a plant increases through the use of AMAs, firms pay slightly less per pound for cattle purchased in the cash market.** Specifically, a 10 percentage point increase in capacity utilization through AMAs is associated with a 0.4 cent per pound carcass weight decrease in the cash market price. Furthermore, if more cattle are available through AMAs within the following 21 days, cash market prices decrease slightly. Specifically, a 10% reduction in the volume of cash market transactions, assuming that volume is shifted into AMAs, is associated with a 0.11% decrease in the cash market price.
- **Beef packer plant-level P&L data showed significant economies of scale in beef packing, and costs were decreasing across the entire data range analyzed.** When both are operated close to capacity, smaller plants are at an absolute cost disadvantage compared with larger plants. When larger plants operate with smaller volumes, they have higher costs than smaller plants operating close to capacity and, thus, have an incentive to increase throughput. For all plants, large and small, average total cost increases sharply as volumes are reduced. A representative plant operating at 95% of the maximum observed volume is 6% more

efficient than a plant operating in the middle of the observed range of volumes and is 14% more efficient than a plant operating at the low end of the observed range.

- **Based on an analysis of P&L statements, procurement of cattle through AMAs results in production cost savings to the plants that use them.** However, the results differ across firms and plants. Some plants benefited substantially from AMAs and other plants did not appear to capture any benefits. The weighted average industry total production cost savings associated with AMAs was approximately $6.50 per animal. For an industry with an average loss of $2.40 per head during the 30-month sample period, this is a substantial benefit.
- **Marketing agreements are the most widely used AMAs in the beef industry, and thus restrictions on the use of marketing agreements would have the greatest negative effects on costs of production in the beef packing industry.** Forward contracts and packer-owned cattle were used, but to a much lesser extent. Therefore, restrictions on the use of packer ownership and forward contracts for cattle would have lesser effects on costs of production.
- **While the results differ by plant and firm, simulation analysis indicates that reducing or eliminating AMAs would result in higher average total cost (ATC) for slaughtering and processing beef cattle and, likewise, reduced gross margins and packer profits.** The average increase to beef slaughter and processing ATC would be 4.7% with a hypothetical elimination of AMAs and 0.9% with a hypothetical 25% reduction is use of AMAs. Packer profits are estimated to decrease by 6.0% and 1.5% if AMAs were reduced by 100% or 25%, respectively.
- **Beef quality has a positive effect on beef demand, the producers and packers interviewed and surveyed believe that AMAs are important for beef quality, and quantitative analyses suggest that AMAs are often associated with higher quality.** Regression analysis of MPR data found a small but positive relationship between formula and packer ownership procurement and USDA Quality Grade and found no statistical relationship between cash purchases and USDA Quality Grade. Regression analysis on transactions data found that marketing agreement cattle had a higher percentage Choice and Prime carcasses without increasing the percentage of Yield Grade 4 and 5

carcasses and had only modest declines in Yield Grade 1 and 2 carcasses. Other procurement methods had a greater trade-off between preferred quality grade and preferred yield grade. Furthermore, marketing agreement cattle and packer-owned cattle were associated with relatively higher quality compared with direct trade cattle, as measured by a composite quality index, but the small percentage of cattle sold through auction barns was associated with the highest quality and the highest variability in quality. The small percentage of cattle sold through forward contracts was associated with the lowest quality but also the lowest variability in quality.

- **The producers and packers surveyed that use AMAs value them as a method of dealing with production, market access, and price risks.** More specifically, feedlots believed that AMAs allow them to secure or sell better quality cattle and calves and improve operational management, efficiency, and capacity utilization. Packers identified AMAs as an important element of branded products and meeting consumer demand by producing a higher quality, more consistent product.
- **Regression analysis accounting for cattle quality and sales month found that auction market and forward contract prices were more volatile than direct trade, marketing agreement, and packer-owned cattle prices.** Furthermore, the volatility of prices for direct trade and marketing agreement cattle were relatively similar. Results were generally consistent for fed beef cattle and fed dairy cattle.
- **Hypothetical reductions in AMAs, as represented by formula arrangements (marketing agreements and forward contracts) and packer ownership, are found to have a negative effect on producer and consumer surplus measures.** Beef and cattle supplies and quality decreased and retail and wholesale beef prices increased because of reductions in AMAs. However, feeder and fed cattle prices decreased because of higher slaughter and processing costs resulting from the AMA restrictions. The short-run, long-run, and cumulative present value surplus for producers and consumers associated with reduced AMA volumes are all negative. Over 10 years, a hypothetical 25% restriction in AMA volumes resulted in a *decrease* in cumulative present value of surplus of
  - 2.67% for feeder cattle producers,

- 1.35% for fed cattle producers,
- 0.86% for wholesale beef producers (packers), and
- 0.83% for beef consumers.

A hypothetical 100% restriction in AMA volumes resulted in a *decrease* in cumulative present value surplus of

- 15.96% for feeder cattle producers,
- 7.82% for fed cattle producers,
- 5.24% for wholesale beef producers (packers), and
- 4.56% for beef consumers.

Thus, feeder cattle producers lose more surplus relative to the other sectors under either scenario. In addition, the estimated changes would imply a reduction in the competitiveness of beef relative to other meats.

- **The cost savings and quality improvements associated with the use of AMAs outweigh the effect of potential oligopsony market power that AMAs may provide packers.** In the model simulations, even if the complete elimination of AMAs would eliminate market power that might currently exist, the net effect would be reductions in prices, quantities, and producer and consumer surplus in almost all sectors of the industry because of additional processing costs and reductions in beef quality. Collectively, this suggests that reducing the use of AMAs would result in economic losses for beef consumers and the beef industry.

ES.3 HOG AND PORK INDUSTRIES

Primary conclusions for this final report, as they relate to the hog and pork industries (Volume 4), are as follows:

- **AMAs are an integral part of hog producers' selling practices and pork packers' procurement practices.** There are significant regional differences in the observed patterns of use of AMAs: a stronger reliance on cash/spot markets and marketing contracts is apparent in the Midwest, and a stronger reliance on production contracts and packer ownership of hogs is apparent in the East. The pattern of future use of AMAs is not expected to change dramatically; hence, we do not expect that hog industry industrialization will emulate the industrialization of the poultry sector.
- **Based on individual transactions data, there are substantial differences in daily hog prices paid by packers on a carcass weight basis.** On average, the

price dispersion is about 40% of the average value of the transaction prices each day. One part of such strong price dispersion can be explained by factors such as region, quality, or plant size. However, even after controlling for these factors, the remaining differences must be due to organizational issues related to supply chain management in the pork processing sector.

- **Results indicate that, on average, plants that use a combination of marketing arrangements pay lower prices for their hogs relative to plants that use the cash/spot market only.** In addition, comparing the magnitudes of the portfolio effects to the magnitudes of the individual marketing arrangement effects shows that individual marketing arrangements have minimal additional impact on the average price after accounting for the portfolio effect. That is, the portfolio system categorical variables capture almost the entire effect on lowering the average price.
- **Of particular interest for this study is the effect of both contract and packer-owned hog supplies on spot market prices; as anticipated, these effects are negative and indicate that an increase in either contract or packer-owned hog sales decreases the spot price for hogs.** Specifically, the estimated elasticities of industry derived demand indicate
  - a 1% increase in contract hog quantities causes the spot market price to decrease by 0.88%, and
  - a 1% increase in packer-owned hog quantities causes the spot market price to decrease by 0.28%.

  A higher quantity of either contract or packer-owned hogs available for sale lowers the prices of contract or packer-owned hogs and induces packers to purchase more of the now relatively less expensive hogs and purchase fewer hogs sold on the spot market.
- **Based on tests of market power for the pork industry, we found a statistically significant presence of market power in live hog procurement.** However, the results regarding the significance of AMA use for procurement of live hogs in explaining the sources of that market power are inconclusive. Whereas the model based on farm–wholesale price spread data shows that a higher proportion of AMA use leads to increased market power, the model estimated with company-level individual transactions data indicates that AMA use may not be a source of market power in pork packing.

- **Estimated total and average cost functions indicate that economies of scale diminish as the pork packing firm size increases.** The estimates indicate that the scale economies are exhausted well within the sample output range such that the biggest plants already exhibit negative returns to scale. That is, they operate on the upward-sloping portions of their average cost curves. The observed patterns of procurement portfolio choices by packers also indicate that certain combinations of marketing arrangements may reduce costs and/or increase economies of scale. In particular, relative to using spot market procurements alone, all other combinations of marketing arrangements improve the efficient scale of production.
- **Based on the observation that packers use marketing arrangements in clusters (portfolios), we hypothesized that marketing arrangements may be complementary to each other in the sense that implementing one procurement practice may increase the marginal return of the other practice; however, the analyses of the complementarity of marketing arrangements produced inconclusive results.** Simpler tests based on the correlation/association approach indicate that marketing contracts are in fact complementary to production contracts and/or packer owned arrangements. Also, the portfolio coefficients in the performance equations based on either the earnings before insurance and taxes (EBIT) or the gross margin show that all marketing arrangement portfolios improve plant performance relative to simple spot market purchases. However, the coefficient associated with the portfolio of three marketing arrangements is smaller than the coefficient associated with portfolios of two marketing arrangements, thus violating the complementarity requirement. More conclusive formal tests were not feasible given data limitations.
- **To analyze quality differences in live market hogs across alternative procurement methods (AMAs), we tested whether various quality attributes used by the industry are significantly different across AMAs and found that different AMAs are associated with different levels of quality of hogs.** Even though the rankings are not unique, we found that marketing contracts (especially other purchase arrangements and other market formula purchases) are consistently associated with higher quality hogs than negotiated (spot market) purchases.

- **An examination of the relationship between the proportion of AMAs used to procure live hogs and the quality of resulting pork products indicates that a higher proportion of AMA use is associated with higher quality pork products.** We measured pork product quality using Hicks' composite commodity index and hypothesized that a higher percentage share of the AMAs (essentially marketing contracts and packer-owned hogs) should produce higher quality pork products. The correlation coefficient showed that these two series are positively correlated, thus confirming our hypothesis.
- **An analysis of risk associated with different marketing arrangements shows that different types of marketing arrangements exhibit different price volatilities as measured by the variance of prices.** Therefore, hog producers selling hogs using different types of marketing arrangements experience different levels of risk. From the hog producers' point of view, the ordering of marketing arrangements in decreasing order of risk is as follows: (1) spot/cash market sales; (2) marketing contracts in which the pricing formula is based on spot market prices; (3) marketing arrangements in which the pricing formula is based on some futures or options price; (4) other purchase arrangements containing ledgers, windows, and other pricing mechanisms, which may serve as a cushion against price volatility; and (5) production contracts.
- **In analyzing the importance of hog producers' risk aversion for contract choice, we found that hog producers who use production contracts are more risk averse than producers who use cash/marketing arrangements.** The difference in risk exposure between contract producers and independent farmers is substantial because production contracts eliminate all but 6% of total income volatility. Therefore, the utility losses associated with forcing producers to market their hogs through channels different from their risk-aversion-preferred marketing arrangement choice are substantial.
- **In analyzing the economic effects of hypothetical restrictions on the use of AMAs in the hog and pork industries, we found that hog producers would lose because of the offsetting effects of hogs diverted from AMAs to the spot market, consumers would lose as wholesale and retail pork prices rise, and packers would gain in the short**

run but neither gain nor lose in the long run. The results applied to three different simulations: (1) 25% reduction in both contract- and packer-owned hogs, (2) increase the spot/cash market share to 25%, and (3) complete ban of packer-owned hogs. The reason that producers and consumers lose in all three simulation scenarios is because of efficiency losses from reducing the proportion of hogs sold through contracts and/or packer owned channels. Although a reduction in AMAs leads to an improvement for hog producers through a reduction in the degree of market power, the loss in cost efficiencies offsets the gains from reduced market power. In all instances, the price spread between farm and wholesale prices would be expected to increase because of the net increase in the costs of processing. Moreover, wholesale, and hence retail, prices would increase, causing pork to become more expensive for consumers.

ES.4 LAMBS AND LAMB MEAT INDUSTRIES

Primary conclusions for this final report, as they relate to the lamb and lamb meat industries (Volume 5), are as follows:

- **Lamb packers procure fed lambs primarily through formula pricing arrangements and auctions.** According to MPR data, lamb packers procure 42.2% of fed lambs through formula pricing arrangements and 39.4% through auctions. Negotiated sales account for 12.0% of fed lamb procurement, and packer ownership represents 4.9%. Contracted procurement represents only 0.8% of lamb procurement, while imports represent only 0.7%. These data are similar to those obtained from the lamb packer survey.
- **The means and standard deviations of fed lamb prices from MPR data for formula pricing and cash arrangements were similar during the sample period.** The price series were highly correlated with an estimated correlation coefficient of 0.970. A reduced-form model of the difference between normalized formula pricing and cash fed lamb prices indicated that lamb inventories, lamb carcass price risk, and seasonality were the primary determinants of variations in the difference.
- **Changes in procurement methods for lamb would impose costs on the lamb marketing system by reducing efficiencies, but may also provide some benefits by altering potential market power effects.** If formula pricing procurement is restricted,

lamb acquisition costs would rise. However, some of this increase in costs may be offset by a reduction in potential oligopsony power. Ultimately, a combination of these effects yields net changes in lamb prices, quantities, and producer surplus.

- **Given that lamb markets are relatively thin, the primary effect of MPR may have been to reduce price risk rather than to influence price levels.** The implementation of MPR in 2001 increased slaughter lamb price by only 0.129%.
- **AMAs were found to have statistically significant although economically small effects on lamb prices.** A 10% increase in formula pricing lamb procurement would increase the slaughter lamb price by an estimated 2.54%; this effect is likely due to risk reductions. A 10% increase in cash lamb procurement increases slaughter prices by an estimated 2.68%. A 10% increase in packer ownership reduces slaughter lamb prices by an estimated 0.23%.
- **Increases in formula pricing and cash procurement methods reduce lamb procurement costs, while increases in packer ownership increase procurement costs.** The effects of formula pricing and cash procurement methods on procurement costs for lambs were similar and not statistically different from one another.
- **Technological change has likely increased lamb quality over time.** However, there does not appear to be any statistically significant difference in the quality of lambs procured through formula pricing and cash procurement methods.
- **Price risk shifting from lamb producers to lamb packers and breakers has not occurred as a result of AMAs.** No statistical difference was found between the variances of prices for each type of AMA.
- **Restrictions on the use of AMAs cause almost every sector in the lamb industry to lose producer surplus, even if potential market power (if it exists) is reduced or eliminated.** Reductions in the use of AMAs have both positive and negative effects on the lamb industry. Reductions in potential market power (a positive effect) do not offset the increases in processing costs and reductions in lamb quality (negative effects).
- **Restrictions on the use of AMAs would likely reduce the competitiveness of the lamb industry.**

Although lamb is not a strong substitute for beef and pork, restrictions on the use of AMAs would place it at a competitive disadvantage to these other meats. More importantly, however, it appears that imported lamb is a strong substitute for domestic lamb. Hence, the loss of competitiveness in response to restrictions on the use of AMAs is much more pronounced with respect to lamb imports.

- **AMAs may have multiple effects on accessing the lamb market.** Ease of entry may be affected by the availability of AMAs, because financing of production operations often depends on the assurance of market access and price risk management. However, for small producers, it may be more difficult to secure AMAs because it is more costly for packers to negotiate with many small producers relative to fewer large producers. Hence, if AMAs reduce the viability of public auctions, small producers may find that their market access is limited.
- **Restrictions on the use of AMAs may increase concentration of various segments of the lamb industry, but the effect of increased concentration on market power is unknown.** There are no clear effects of the changes in the use of AMAs on concentration in the lamb industry. Concentration in the lamb packing industry has remained relatively flat, even though the use of AMAs has increased. However, increased use of AMAs may reduce the viability of auctions and could lead to increased concentration in the lamb feeding sector. In addition, if restrictions on AMAs reduce the competitiveness of domestic lamb meat relative to lamb imports, then concentration in the lamb packing and processing industry is likely to increase in response to declining domestic demand.

ES.5 MEAT DISTRIBUTION AND SALES

Primary conclusions for this final report, as they relate to meat processing, distribution, and sales (Volume 6), are as follows:

- **Transactions data on meat processor purchases indicate a much larger use of AMAs than do the survey data.** Based on transactions data, only 21% of beef and pork products were purchased on the spot market. Internal transfers were a large factor for pork but were virtually nonexistent for beef. Forward contracts were 28% of beef purchases, but less than 1% of pork purchases. The type of purchase method used is either not important to meat processors or they did not understand the meaning of the categories, because 39% of beef and 32% of pork purchase methods were listed as "other or missing."

- **Approximately 99% of pork and 55% of beef product pounds that were priced using formula pricing used a USDA-reported price as the base.** The other base used for purchased beef was a subscription service. Although nearly all pork pricing formulas are based on USDA-reported prices, it is worth noting that wholesale pork, while reported by USDA, is not covered under Mandatory Price Reporting (MPR).
- **Meat processors play an important distribution role in the meat value chain by purchasing large lots from a few sources and selling small lots to many firms.** Transaction purchase data included 53,831 records from 32 firms, averaging 22,800 pounds per transaction. Sales transactions from 11 firms included 848,295 records, averaging 771 pounds per transaction, and these were all case ready or RTE. A high percentage of these transactions did not identify the sales method, indicating that processors either did not understand the meaning of the categories that were listed or do not track this information.
- **When examining data specific to the beef industry, aggregate cattle purchase and beef sales transactions data suggest no relationship between cattle purchase methods and branded beef sales, although this relationship may be important to individual firms.** Plants that sold 0% to 20% of their beef as branded product purchased approximately the same percentage of their cattle on the spot market as did plants that sold 21% to 40% of their beef as branded product. Although the differences were small, the 21% to 40% plants used more forward contracts and less packer ownership than did the 0% to 20% plants. Shares of marketing agreement cattle were nearly identical across the two groups. In addition, 60% of the meat purchased on the spot market by processors was branded product compared with none through marketing agreements and internal transfers.
- **Although potentially important to some beef industry firms, aggregate transaction data suggest that downstream marketing arrangements have no relationship to cattle purchase methods.** Beef plants were divided into two groups based on beef sales methods–0% to 50% and 51% to 100% cash or spot market beef sales. Transactions from both groups indicated that they each bought 60% of their cattle

through the spot market and 40% using AMAs. The 0% to 50% cash sales group used more marketing agreements, and the 51% to 100% cash sales group had more packer-owned cattle.

- **Aggregate transactions data for the beef industry suggest some relationship between meat buyer type and cattle purchase methods.** Packers that sold more beef to meat processors bought fewer cattle on the spot market but about the same number of cattle through AMAs (with the difference resulting from a larger percentage of other purchases or missing information). Packers that sold a larger amount of beef to retailers and food service operators bought a larger percentage of their cattle on the spot market and a slightly lower percentage of cattle through AMAs.
- **The pork industry is more vertically integrated than is the beef industry.** Pork packers produce a higher percentage of the animals that they slaughter than do beef packers, and pork processors acquire much more of their product through internal transfer than do beef processors.
- **Meat processor buyers mix and match purchase and pricing methods.** Formula pricing was used as the pricing method for spot market, forward contracts, and marketing agreements. Likewise, individually negotiated prices were more common in forward contracts than in spot markets.

ES.6 LIMITATIONS OF THE ANALYSES

Decisions regarding methodologies, assumptions, and data sources used for the study had to be made in a short period of time. The analyses presented in this final report are based on the best available data, using methodologies developed to address the study requirements under the time constraints of the study. Some analyses were limited because of availability and quality of the transactions and P&L statement data. However, secondary data were used, as available, to supplement primary data in order to conduct the analyses.

1 Introduction

AMAs include all possible alternatives to use of cash or spot markets for conducting transactions.

Over time, the variety, complexity, and use of AMAs have increased in the livestock and meat industries. Marketing arrangements refer to the methods by which livestock and meat are transferred through successive stages of production and marketing. A marketing arrangement also designates a method by which prices are determined for each individual transaction. The increased use of AMAs raises a number of questions about their effects on economic efficiency and on the distribution of the benefits and costs of livestock and meat production and consumption between producers and consumers.

USDA's GIPSA is charged with facilitating the marketing of livestock, meat, and other agricultural products. This agency also promotes fair and competitive trading practices for the overall benefit of consumers and American agriculture. In fulfilling its mission, GIPSA evaluates, among other things, the implications of the evolving landscape of AMAs and pricing methods.

In 2003, Congress allocated funds to GIPSA to conduct a broad study of the effects of AMAs on the livestock and meat industries.

In 2003, Congress allocated funds to GIPSA to conduct a broad study of the effects of AMAs on the livestock and meat industries. GIPSA developed the specific scope and objectives of the study, and following a competitive bidding process, RTI was awarded a contract to conduct the Livestock and Meat Marketing Study.

The questions posed by the Livestock and Meat Marketing Study included the following: What types of marketing arrangements are used? What is the extent of their use? Why do firms enter into the various arrangements? What are the terms and characteristics of these arrangements? What are the effects and implications of the arrangements on participants and on the livestock and meat marketing system?

The study examined the following species and meat types:

- fed cattle and beef,
- hogs and pork, and
- lambs and lamb meat.

The study comprised five main parts:

- Part A. Identify and classify types of spot marketing arrangements and AMAs.
- Part B. Describe terms, availability, and reasons for use of spot marketing arrangements and AMAs.
- Part C. Determine extent of use, analyze price differences, and analyze short-run market price effects of AMAs.
- Part D. Measure and compare costs and benefits associated with spot marketing arrangements and AMAs.
- Part E. Analyze the implications of AMAs for the livestock and meat marketing system.

The interim report released in August 2005 addressed Parts A and B of the study. This final report focuses on Parts C, D, and E.

An interim report released in August 2005 addressed Parts A and B of the study (Muth et al., 2005). The report described marketing arrangements used in the livestock and meat industries and defined key terminology.[1] Results presented in the interim report were preliminary because they were based on assessments of the livestock and meat industries using published data, review of the relevant literature, and industry interviews.

Concurrent with conducting Parts A and B of the study, the study team developed and pretested information collection plans for obtaining transactions data and P&L statements from packers, processors, and downstream market participants. In addition, the study team developed and pretested a set of 10 industry survey questionnaires to obtain additional information beyond what could be obtained in transactions data and P&L statements. We received approval for both information collection requests from the Office of Management and Budget (OMB) in October 2005.

[1] Terms used in the study are included in the glossary.

This final report describes the results of quantitative analyses addressing Parts C, D, and E of the study, using data from the industry surveys across all stages of livestock and meat production, transactions data and P&L statements from packers and processors, production contract settlement data from packers, and a variety of publicly available data. According to the Performance Work Statement (PWS) in the contract with GIPSA, the results of these analyses will provide information to

- livestock producers to help them make more informed production and marketing decisions,
- the general public to help them understand the roles and reasons for using these arrangements,
- GIPSA for its role in enforcing the Packers, and Stockyards Act, and
- USDA and Congress to help them determine whether policy changes affecting livestock marketing methods that were originally considered during the development of the 2002 Farm Bill are warranted.

The Livestock and Meat Marketing Study was limited to economic factors associated with spot marketing arrangements and AMAs and did not analyze policy options or make policy recommendations.

The study is national in scope, but it considered regional differences among marketing arrangements, if applicable, and international dimensions related to marketing arrangements, if significant. All stages of production and marketing were addressed, including farm level, slaughtering, processing, wholesaling and distribution, retailing, food service, and export. The Livestock and Meat Marketing Study was limited to economic factors associated with spot marketing arrangements and AMAs and did not analyze policy options or make policy recommendations.

2 Overview of Parts C, D, and E of the Study

Throughout the report, industry participants are grouped into the following categories:

- livestock producers and feeders
- meat packers and processors (or breakers)
- wholesalers and distributors
- exporters
- food service or restaurant establishments
- retail establishments

Parts C, D, and E include complementary analyses of the effects of AMAs in each industry. The aims of Part C were to determine the extent to which various types of spot marketing arrangements and AMAs are used, to analyze price differences among the marketing arrangements, and to analyze the effects of alternative arrangements on short-run spot market prices as follows:

- Determine the volume of livestock and meat transferred through the various types of spot and alternative arrangements by type, size, and location of market participants.
- Report average price levels and differences in prices by type, size, and location of market participants.
- Determine price differences associated with the various types of spot marketing arrangements and AMAs, adjusting for quality differences, lot size, and other relevant factors that may affect prices, and determine how price differences vary with market conditions.
- Determine if packers' use of alternative procurement and pricing arrangements for fed cattle, slaughter hogs, and lambs is causally related to spot market prices for these animals in the short run and determine the nature of the relationship.

The aims of Part D were to measure and compare possible costs and benefits associated with the various types of spot marketing arrangements and AMAs as follows:

- Determine cost and efficiency differences and measure size and other economies and diseconomies associated with the use of AMAs.
- Determine the extent to which any differences in animal and meat quality are associated with differences in spot marketing arrangements and AMAs.[2]
- Determine if the various types of marketing arrangements shift risks among market participants or alter risk levels.[3]

The aims of Part E were to analyze the implications of AMAs for the livestock and meat marketing system, using the models developed in Parts C and D, as follows:

- Assess system-wide economic implications of restrictions on AMAs used by packers to purchase livestock.
- Assess the relative overall strength of positive and negative economic incentives for increased or decreased use of the various types of marketing arrangements.
- Examine the implications of expected changes in the use of various marketing arrangements over time.

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[2] As noted in the PWS, quality measures might include meat grades, tenderness, taste, nutritional characteristics, consistency, and conformity to specifications.

[3] As noted in the PWS, risk might relate to price, quality, loss of product, loss of supplier, loss of buyer, reduced credit rating, or less reliable trading partners.

3 Information Sources Used for Parts C, D, and E of the Study

The analyses conducted for the final report build on information obtained for and summarized in the interim report. The interim report was based on information from the empirical agricultural economics and management literature, information from the development and pretesting of the data collection instruments for the transactions data collection and the industry surveys, available contract forms for beef cattle and hogs, discussions with trade associations, and discussions with industry participants.

The analyses presented in this final report use the following types of data:

- purchase and sales transactions data from meat packers and processors
- P&L statements from meat packers and processors
- production contract settlement data from hog packers
- industry survey responses from livestock producers, meat packers, meat processors, meat wholesalers, meat exporters, grocery retailers, and food service operations
- a broad range of publicly available data, including MPR data

4 Organization of the Report

This final study report provides information and quantitative results for Parts C, D, and E of the Livestock and Meat Marketing Study. The volumes of the final report are as follows:

- Volume 2: Data Collection Methods and Results
- Volume 3: Fed Cattle and Beef Industries
- Volume 4: Hog and Pork Industries
- Volume 5: Lamb and Lamb Meat Industries
- Volume 6: Meat Distribution and Sales
- Appendix A: Glossary

The results from Volume 2 are incorporated into all volumes, in the relevant sections. Volumes 3 through 5 have a similar structure, which follows the requirements of the study, as specified in the PWS. Volume 6 has a different structure to include additional analyses beyond the species-specific analyses included in the previous volumes.

5 References

Muth, M.K., G. Brester, J. Del Roccili, S. Koontz, B. Martin, N. Piggott, J. Taylor, T. Vukina, and M. Wohlgenant. July 2005. *Spot and Alternative Marketing Arrangements in the Livestock and Meat Industries: Interim Report*. Prepared for the U.S. Department of Agriculture, Grain Inspection, Packers and Stockyards Administration.