USDA's Proposed Rule on Livestock and Poultry Marketing Practices

Joel L. Greene
Analyst in Agricultural Policy

March 8, 2011

Congressional Research Service
7-5700
www.crs.gov
R41673

CRS Report for Congress
Prepared for Members and Committees of Congress

Summary

On June 22, 2010, the U.S. Department of Agriculture's (USDA's) Grain Inspection, Packers and Stockyards Administration (GIPSA) published a proposed rule on the implementation of regulations dealing with livestock marketing practices as mandated by the 2008 farm bill (P.L. 110-246). The proposed rule adds new details to the implementation of the Packers and Stockyards Act of 1921 (P&S Act) to clarify conduct that violates the P&S Act. The P&S Act regulations are used by USDA to ensure fair competition in livestock and poultry markets. USDA is now reviewing public comments in preparation for issuing a final rule.

In what some see as a major change from current practice, GIPSA proposes that a violation of the P&S Act does not require a finding of "harm or likely harm to competition." The proposed rule sets criteria for unfair, discriminatory, and deceptive practices, and covers undue or unreasonable preference or advantages that violate the P&S Act. Lastly, the proposed rule includes arbitration provisions to ensure that contract growers have the opportunity to participate in meaningful arbitration and the right to decline arbitration.

During congressional debate on the 2008 farm bill, some advocates proposed that a competition title be added to the farm bill to address perceived anticompetitive market behavior by large meat and poultry processing companies. Then and now, advocates for stronger anticompetitive measures contend that, because of substantial market consolidation over the past several decades, meat packers and poultry processors wield considerable market power over individual producers when negotiating contracts. Others argue that consolidation occurred in previous decades and has stabilized in recent years, bringing with it efficiencies that benefit producers and consumers alike.

A competition title was not passed, but the enacted farm bill included new provisions that amend the P&S Act to give poultry and swine growers the right to cancel contracts, require the clear disclosure by poultry processors to growers of additional required capital investments, set the choice of law and venue in contract disputes, and give poultry and swine growers the right to decline an arbitration clause that requires arbitration to resolve contract disputes.

Proponents of the proposed rule argue that the P&S Act has not lived up to its potential because rules have not been properly promulgated over the years and courts have incorrectly interpreted it. According to proponents, the proposed rule will bring fairness to contracts and reshape interactions between producers and large meat packers and processors. Opponents argue that the proposed rule goes far beyond the intent of Congress in the 2008 farm bill, particularly the proposed criteria for violating the P&S Act. Critics expect the rule to greatly alter how business is currently conducted to the detriment of producers, consumers, and the industry. Critics also say the proposed rule will result in increased litigation. In addition, one of the primary complaints by opponents of the proposed rule was that it lacked rigorous impact analysis that would uncover severe economic consequences.

USDA has not provided a specific timeframe for finalizing the proposed rule. Media reports have speculated that it will take several months to process the public comments, and a more thorough economic analysis as promised by USDA would also likely take a few months to complete. Last year, some Members of Congress commented on the proposed rule, and there may be considerable interest in the 112th Congress to further examine USDA's intent and implementation of the proposed rule.

Contents

Figures

Tables

Appendixes

Contacts

Introduction

On June 22, 2010, the U.S. Department of Agriculture's (USDA's) Grain Inspection, Packers and Stockyards Administration (GIPSA) published a proposed rule on the implementation of regulations dealing with livestock marketing practices as mandated by Title XI (Livestock) of the Food, Conservation and Energy Act of 2008 (2008 farm bill; P.L. 110-246).[1] The proposed rule adds new details to the implementation of the Packers and Stockyards Act of 1921 (P&S Act, 7 USC §181 *et seq.*) that describe and clarify conduct that violates the P&S Act (see box, "The Packers and Stockyards Act of 1921.")

GIPSA is the USDA agency that promulgates the regulations under the P&S Act to oversee livestock and poultry markets. GIPSA is responsible for monitoring, reviewing, and investigating livestock and poultry markets to promote fair competition, provide payment protection through bonding and packer trusts, and guard against deceptive and fraudulent trade practices.

Some farmers and ranchers and their advocate groups believe that as the meat and poultry industries have become increasingly concentrated over time, competition has eroded, and producers have little say in market transactions with large meat companies. In addition, some claim USDA has not used the P&S Act sufficiently to protect livestock and poultry producers, especially small producers, from perceived unfair trade practices of large meat companies.

During 2010, in order to address ongoing concerns about competition in the livestock and poultry industries, USDA and the Department of Justice (DOJ) jointly held five workshops to discuss competition and regulatory issues in agriculture.[2] The five workshops covered farming, poultry, dairy, livestock, and margins (the difference between the price producers receive and the price consumers pay). These workshops provided an opportunity for people from various sectors of the meat and poultry industries to air their concerns.

Since USDA issued its proposed rule on livestock and poultry marketing practices in mid-2010, proponents and opponents have espoused widely differing interpretations of it. According to USDA and supporters of the proposed rule, the regulations would allow for more effective and efficient enforcement of the P&S Act. According to USDA, the interaction between meat companies would be more transparent, as the proposed rule requires meat packers and poultry processors to justify pricing differences and provide sample contracts to GIPSA. The proposed rule defines and gives examples of practices that GIPSA considers unfair that would violate the P&S Act. The proposed rule will bring fairness to marketing transactions, according to supporters.

Opponents of the proposed rule claim that there will be unintended consequences that will adversely affect normal livestock and poultry marketing practices. They argue that the proposed rule amounts to the government stepping in to manage the day-to-day working of markets, which would lead to inefficiencies, increased litigation, and the loss of gains that the industry has experienced over the years.

[1] Grain Inspection, Packers and Stockyards Administration, USDA, "Implementation of Regulations Required Under Title XI of the Food, Conservation and Energy Act of 2008: Conduct in Violation of the Act," 75 *Federal Register* 35338, June 22, 2010. Hereafter referred to as the "proposed rule."

[2] Background and transcripts for the workshops are at http://www.justice.gov/atr/public/workshops/ag2010/index.html.

The Packers and Stockyards Act of 1921

Passage of the P&S Act in 1921 was "in response to concerns that, among other things, the marketing of livestock presented special problems that could not be adequately addressed by existing antitrust laws."[3] Parts of the act, as amended (7 USC §181 *et seq.*), prohibit unjustified discriminatory practices, as well as certain, specific activities that might adversely affect competition. As stated in 7 USC §192 of the act, it is unlawful for a packer or poultry dealer to "engage in or use any unfair, unjustly discriminatory, or deceptive practice or device; give undue/unreasonable preference/advantage to [persons or localities]"; apportion supply among packers in restraint of commerce or create a monopoly; trade in articles to manipulate or control prices, if such apportionment tends to restrain commerce or to create a monopoly; or conspire to apportion territory, or sales, or to manipulate or control prices.

The Secretary of Agriculture has assigned regulatory responsibility for the act to USDA's Grain Inspection, Packers and Stockyards Administration (GIPSA). GIPSA does not have a direct antitrust authority, and the P&S Act does not provide the agency with premerger review authority. The agency's role, however, is to maintain fair competition regulations. GIPSA is authorized to initiate and conduct investigations of alleged violations in the livestock industry, but generally not in the poultry industry. A violator of GIPSA regulations may, after a hearing before a USDA administrative law judge, be served a "cease and desist" order, and civil fines may be imposed.

If a packer disregards an order or refuses to pay fines, GIPSA may refer the case to the Department of Justice, which can enforce the order/fine through court action. According to GIPSA, most violations are corrected voluntarily by the individuals or firms when a violation is brought to their attention. Except for serious violations, disciplinary action tends to be the last resort, and is imposed only after substantial efforts to obtain compliance have failed.[4]

The proposed rule was issued with a 60-day comment period. After considerable comment and feedback, the comment period was extended for an additional 90 days ending November 22, 2010. The proposed rule generated more than 66,000 public comments.[5] GIPSA is now in the process of evaluating the public comments in preparation for publishing a final rule.

Some Members of Congress have expressed considerable interest in the proposed rule throughout the comment period, and the 112th Congress may have considerable interest in overseeing USDA's implementation of the final rule. This report provides background on the genesis of the proposed rule and a summary of its provisions. The last part of the report discusses some of the major concerns about the proposed rule.

Concern About Industry Structure and Competition

Advocates for stronger anticompetitive measures in the livestock industry contend that, because of the substantial market consolidation that has occurred over the past several decades, packers and poultry processors/integrators or live poultry dealers[6] have more market power than

[3] Government Accountability Office (GAO), *Packers and Stockyards Programs: Continuing Problems with GIPSA Investigations of Competitive Practices*, March 9, 2006, testimony before the Senate Agriculture Committee.

[4] See CRS Report RL33325, *Livestock Marketing and Competition Issues*, for discussion of other relevant authorities that govern livestock and poultry marketing and competition.

[5] Comments on GIPSA's proposed rule are posted on http://www.regulations.gov, where nearly 300 government agencies post copies of proposed regulations and the public can submit comments via the website.

[6] A packer slaughters and/or processes livestock into meat. Similarly, a poultry processor is an enterprise engaged in the business of converting live poultry into poultry meat products. An integrator is a poultry company that contracts with a poultry grower to raise live birds to contract specifications. The integrator provides inputs and processes the birds. Live poultry dealer is the term used in the P&S Act and in the proposed rule for a poultry processor or integrator. For more information on the structure of the U.S. broiler industry, see James M. MacDonald, *The Economic* (continued...)

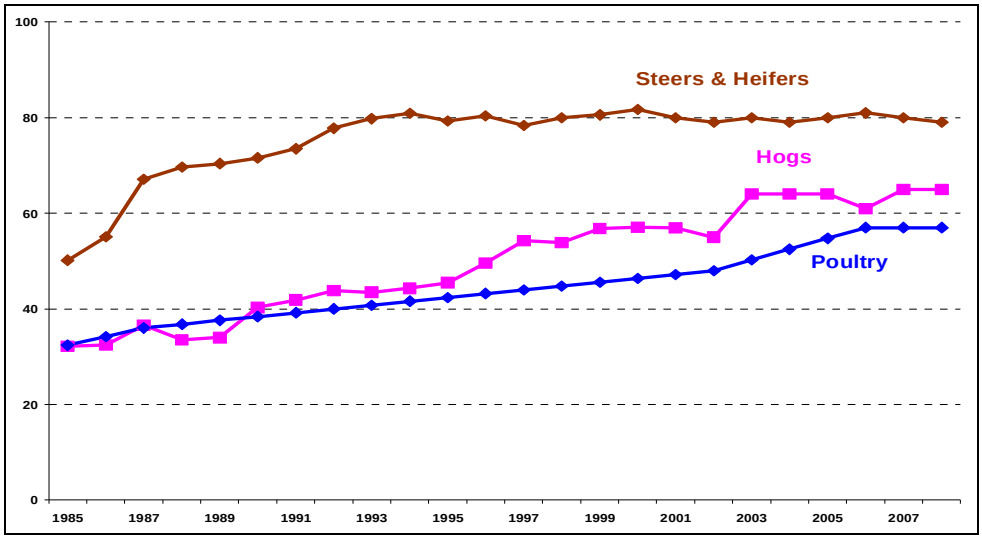
individual producers when negotiating contracts and in the livestock market in general. Others argue that this consolidation occurred in previous decades and has stabilized in recent years, bringing with it efficiencies that benefit producers and consumers alike. Furthermore, barring collusion, others argue that it only takes two interested buyers to have sufficient competition for a market to work properly.

Industry Consolidation

Market concentration in the meat and poultry industries has increased over the last two decades, with a few firms now dominating each sector. The "four-firm concentration ratio" measures the four largest firms' share of the market and is commonly cited as a summary indicator of concentration and overall structural change in the industry. The historical evolution of industry concentration ratios for the slaughter of fed cattle (steers and heifers), hogs, and poultry is shown in **Figure 1** below. From 1986 to 2008, the four-firm share of slaughter increased from 55% to 79% for cattle, 33% to 65% for hogs, and 34% to 57% for poultry. The concentration ratios appear to have stabilized in the mid-1990s for the cattle sector, around 2003 for the hog sector, and since about 2006 for the poultry sector.[7]

Figure 1. Concentration Ratios of the Top Four Processing Firms by Industry

Percent of Annual Slaughter or Production



Sources: Data for steers & heifers and hogs are from USDA, GIPSA, Annual Reports, various issues; poultry concentration data are from "Competition in the U.S. Chicken Sector," by Dr. Thomas Elam, FarmEcon LLC, May 19, 2010, prepared for the National Chicken Council.

Note: Poultry data are available only for five-year increments beginning in 1982. Inter-period years were extrapolated by a simple moving average. Therefore, caution should be exercised in making close comparisons of year-to-year trends in poultry with those of steers and heifers or hogs.

(...continued)

Organization of U.S. Broiler Production, Economic Research Service, USDA, Economic Information Bulletin, Number 38, Washington, DC, June 2008.

[7] For more information on industry structure, see CRS Report RL33325, *Livestock Marketing and Competition Issues*.

Recent estimates of the various marketing strategies employed by the three major livestock species are displayed in **Table 1**. Some in the industry are concerned that the share of cash transactions is not sufficient to adequately determine cash prices, which is critical because the cash market is often used as input for contracts or other marketing arrangements. The cash market still comprises a relatively large share (estimated at 41% in 2008) of fed cattle sales. The hog sector's cash market share of sales has been declining over the past several decades and now stands at less than 10% of all sales. However, the hog cash market is still fairly robust and provides the basis for much of the formula and forward contract pricing. In the poultry sector, cash sales of broilers are essentially nonexistent, with production contracts accounting for nearly all transactions.

Table 1. Livestock Marketing Strategies, by Share of Slaughter (Cattle and Hogs) or Production (Poultry)

Type	Steers & Heifers	Hogs	Broilers
	2008	2009	2006
Cash market	41%	8%	< 1%
Forward or formula contract	46%	49%	0%
Negotiated grid pricing	7%	0%	0%
Production contract	0%	12%	98%
Packer or processor-owned	6%	26%	1%
Packer sold	0%	6%	0%
Total Annual Marketing	**100%**	**100%**	**100%**

Sources: Data for Steers & Heifers are from "Extent of Alternative Marketing Arrangements for Fed Cattle and Hogs," AGEC-615, by Clement Ward, Oklahoma State University, January 2010; data for hogs are from "Wholesale Pork Price Reporting Analysis," A Value Ag, LLC Report, commissioned by the Agricultural Marketing Service, USDA, November 2009; and Broiler data are "The Economic Organization of U.S. Broiler Production," James M. MacDonald, EIB 38, Economic Research Service, USDA, June 2008.

Note: Formula contract pricing refers to establishing a transaction price using a formula that includes some other price as a reference. Grid pricing consists of a base price with specified premiums and discounts for carcasses above and below a base set of quality specifications. Under a production contract, a producer raises the livestock or poultry according to the instructions of a contractor. The contract specifies inputs supplied by the contractor and the producer's compensation. A substantial portion of the formula contracts for hogs are similar to production contracts in that they are enhanced formula pricing arrangements that may include some explicit production method or input requirements, but have not been explicitly categorized as production contracts by the data source.

Legal Challenges

Previously, producers initiated several closely watched lawsuits under the P&S Act challenging the contracting and marketing practices of large meat and poultry companies.[8] These generally unsuccessful efforts added impetus to calls for legislative action to strengthen existing antitrust authorities, to impose more mandates on the executive branch to enforce these authorities, and to provide new contract protections for farmers and ranchers.

[8] See http://www.nationalaglawcenter.org/assets/caseindexes/packersandstockyards.html for a comprehensive case law index for the P&S Act.

In what many analysts considered to be a landmark legal case under the P&S Act, (*Pickett v. Tyson Fresh Meats, Inc.*), a group of cattle feeders in 1996 sued Iowa Beef Packers (IBP), which was bought by Tyson in 2001, for violating the P&S Act. This was reportedly the first class action certified for producers against a packer in the P&S Act's long history. [9] Following eight years of litigation, a jury in early 2004 agreed with producer arguments that the packer had used "captive supplies"[10] to control the supply of cattle available on the market, thereby causing lower cattle prices. The jury set damages at more than $1.2 billion. However, the federal judge in the case set aside the verdict on the grounds that the jury had insufficient evidence to find that Tyson had no legitimate business reason for using captive supplies.

The plaintiffs appealed, but a U.S. Court of Appeals in August 2005 upheld the lower judge's decision. The appeals court rejected the plaintiffs' argument that there was a violation of the P&S Act. "If a packer's course of business promotes efficiency and aids competition in the cattle market, the challenged practice cannot, by definition, adversely affect competition," the court declared.[11] The plaintiffs and their supporters asked the U.S. Supreme Court to review the case, but the Court declined to do so in early 2006.[12]

In a more recent example, in January 2011, the U.S. Supreme Court declined to review the case, *Terry v. Tyson Farms, Inc.*, brought by a Tennessee poultry grower, Alton Terry, against Tyson Farms. Terry sued Tyson in federal court in 2008 claiming unfair practices under the P&S Act because Tyson would not allow him to view the weighing of his birds when they were delivered to the plant. Eventually Tyson canceled its contract with Terry. The federal court and the U.S. Court of Appeals, Sixth Circuit, had found that Tyson's action had not harmed competition, and Terry's P&S Act claims were dismissed.[13]

Earlier Debates in Congress on Competition

Over the past decade, some farmer-rancher coalitions have proposed to address perceived anticompetitive market behavior by large meat and poultry companies through legislation, specifically by adding a "livestock competition" title to the omnibus farm bill.

Early in the debate on the 2002 farm bill (P.L. 107-171) a coalition of farm groups proposed that Congress rework antitrust laws and change the P&S Act to reflect the consolidation in the meat industry.[14] An agriculture competition title was included in an early version of the farm bill (S.

[9] Pickett v. Tyson Fresh Meats Inc., 11th Cir., No. 04-12137.

[10] Captive supplies are cattle committed to a specific meatpacker two weeks or more ahead of slaughter. The three most common captive supply methods are marketing/purchasing agreements, forward contracts, and packer feeding.

[11] *Pickett v. Tyson Fresh Meats Inc.*, as reported in *Daily Report for Executives*, August 24, 2005. Some discussion of the case also is from David A. Domina, "Proving Anti-Competitive Conduct in the U.S. Courtroom: The Plaintiff's Argument in *Pickett v. Tyson Fresh Meats, Inc.*," *Journal of Agricultural and Food Industrial Organization*, vol. 2, 2004.

[12] "Supreme Court upholds contracts," *Feedstuffs*, April 3, 2006.

[13] Tom Johnston, " Supreme Court rejects farmer's plea to review case against Tyson," *Meatingplace.com*, January 25, 2011. Available at http://www.meatingplace.com/MembersOnly/webNews/details.aspx?item=21254.

[14] Steve Marbery, "Competition clause proposed in U.S. farm policy debate," *Feedstuffs*, June 4, 2001, http://www.feedstuffs.com/ME2/dirmod.asp?sid=49804C6972614A63A1A10DF54CD95D65&nm=Search+our+Archives&type=Publishing&mod=Publications%3A%3AArticle&mid=AA01E1C62E954234AA0052ECD5818EF4&tier=4&id=9B68F671C7F943A499F2D004477E1281.

1628) but was removed in the Senate Agriculture Committee markup.[15] During subsequent floor action on the bill, the Senate approved some individual competition amendments that were enacted in the final 2002 farm bill. One gave producers the right to discuss their contracts with family members and advisors, and the other extended new P&S Act protections to swine producers with production contracts (Sections 10502 and 10503 of P.L. 107-171).

In February 2007, ahead of deliberations on the 2008 farm bill in the 110th Congress, Senator Harkin introduced the Competitive and Fair Agricultural Markets Act of 2007 (S. 622) to clarify and strengthen the P&S Act and the Agricultural Fair Practices Act of 1967 (7 USC §2301 *et seq.*). S. 622 was intended to be the basis for a competition title in the new farm bill. A similar House bill (H.R. 2135) was introduced in May 2007.

Similar to proposals during the 2002 farm bill debate, S. 622 would have established an Office of Special Counsel for Competition within USDA to investigate and prosecute violations of the P&S Act and be a liaison with the Department of Justice and the Federal Trade Commission. The bill also would have set up production contract and enforcement provisions.[16] Parts of S. 622 were incorporated into the Senate-passed version (S. 2302) of the farm bill, which contained a new title on Livestock, Marketing, Regulatory, and Related Programs (Title X). The Senate version of the farm bill also contained a provision to ban packer ownership of cattle. Although the final version of the 2008 farm bill did not include a competition title or the ban on packer ownership of cattle, the enacted farm bill contained competition provisions that provided producers with contract and arbitration rights.

2008 Farm Bill Provisions

Although congressional interest in livestock market competition issues did not result in a competition title, the most recently enacted omnibus farm bill in 2008 (P.L. 110-246) included a livestock title (Title XI). Previous farm bills generally addressed livestock issues in miscellaneous titles.[17] The livestock title of the 2008 farm bill included 17 sections that cover issues such as mandatory price reporting for livestock, country-of-origin labeling for meat, and catfish grading and inspection.

Sections 11005 and 11006 of the farm bill dealt specifically with the P&S Act. The first of these sections deals with production contracts and the second section with promulgating regulations for the P&S Act. The proposed rule was issued by USDA to fulfill the requirements of the 2008 farm bill.

Production Contracts

Section 11005 of the 2008 farm bill amended the P&S Act to add Section 208, which provides poultry growers and swine producers the right to cancel contracts. The law now requires that growers and producers have at least three days from the date of contract execution to cancel. In

[15] Ted Monoson, "Agriculture Panel Far from Consensus on Farm Bill," *Congressional Quarterly*, November 13, 2001.

[16] Sen. Harkin, "Statements on Introduced Bills and Joint Resolutions," Senate speeches, *Congressional Record*, February 15, 2007, p. S2053.

[17] The main exception is dairy price support policies, which are covered under Title I, Subtitle E.

addition, contracts have to clearly disclose the cancellation rights of producers, including the method and deadline for cancellation.

The 2008 farm bill also requires that production contracts state whether poultry growers or swine producers would be required to make additional large capital investments during the life of the contract. Specifically, if the contract requires an additional investment, the farm bill requires that the first page of a contract include such a statement.

The farm bill also added Section 209 to the P&S Act to include provisions about the choice of law and venue in a contract dispute. The forum for resolving disputes over a poultry, swine, or marketing contract would be located in the federal judicial district where the contract is performed. Also, the contract must specify which state law is to apply if there is a dispute over production or marketing contracts.

Lastly, the farm bill added arbitration provisions in Section 210 of the P&S Act. The provisions state that if a livestock or poultry contract contains an arbitration clause for resolving disputes, then the grower or producer must have the option to decline arbitration. The enacted farm bill requires that contracts clearly disclose the right of a producer or grower to decline the arbitration provision. The law also provides that producers and growers could opt for arbitration even after declining the arbitration provision at the time of contract execution, if both sides agree in writing to take a dispute to an arbitrator. The Secretary of Agriculture was directed to promulgate regulations that would ensure producers and growers have a meaningful chance to participate in the arbitration process.

Promulgation of the Regulations

Following the addition of new laws on production contracts, Section 11006 of the farm bill required the Secretary of Agriculture to promulgate regulations concerning violations of the P&S Act. The regulations were to be issued within two years (June 2010) of the enactment of the farm bill. The farm bill specifically directed the Secretary of Agriculture to establish criteria in four areas. The first was criteria to determine if producers or growers are treated with undue or unreasonable preference or advantage. The second was criteria to determine whether or not poultry dealers give enough notice to poultry growers before suspending the delivery of birds. Third, the Secretary was to set criteria to determine if required additional capital investments during a poultry or swine contract were a violation of the P&S Act. Lastly, criteria are required to determine if poultry growers or swine producers are given enough time to remedy a breach of contract before contracts are terminated.

On June 22, 2010, GIPSA published the requisite proposed rule (9 CFR Part 201) in the Federal Register (75 Fed. Reg. 35338). The rule was initially opened for a 60-day comment period to expire on August 23, 2010; however, in response to substantial industry feedback and concerns expressed by some Members of Congress, GIPSA, on July 26, 2010, extended the comment period until November 22, 2010.

The proposed rule generated more than 66,000 public comments. Many of the public submissions were "form letter" comments, but USDA still received approximately 30,000 unique comments. GIPSA is now in the process of compiling the public submissions and is evaluating them in preparation for publishing a final rule.

Summary of GIPSA's Proposed Rule

Besides fulfilling the requirements of the farm bill, USDA also saw the proposed rule as an opportunity to address the increasing use of contracting in livestock and poultry production. USDA stated that, "The goal of this regulation is to level the playing field between packers, live poultry dealers, and swine contractors, and the nation's poultry growers and livestock producers."[18]

The proposed rule and GIPSA's discussion of the rule cover four broad areas: competitive injury, unfair practices, undue or unreasonable preference, and arbitration. The proposed rule addresses the poultry grower and swine producer contract provisions in the 2008 farm bill and also includes regulations that prohibit what USDA has deemed unfair market practices. The proposed rule introduces new requirements for contracts and market practices with the aim of creating a more fair, transparent market for livestock and poultry producers. The **Appendix** of this report includes a side-by-side synopsis of the proposed rules and a discussion of USDA's supporting arguments and opponents' concerns.

Competitive Injury

In the proposed rule, GIPSA established its definition of competitive injury or harm to competition. Section 202 of the P&S Act describes actions that are unlawful. Sections 201.2 and 201.3 of the proposed rule specifically address the first two unlawful acts of Section 202 of the P&S Act. They are (1) unfair, discriminatory, and deceptive practices; and (2) undue or unreasonable preferences. Other unlawful actions under Section 202 include conduct where packers, swine contractors, or poultry dealers apportion supply or control prices that restrain commerce (harm to competition) or create a monopoly.

When courts have heard P&S Act cases, the rulings usually have required that plaintiffs prove that the conduct of meat packers or poultry processors has harmed competition. Proponents of the proposed rule claim that it is nearly impossible for an individual grower or producer to prove a broad charge of harm to competition.

In Section 201.2 of the proposed rule, GIPSA defines competitive injury as any action that distorts competition in the marketplace. GIPSA defines likelihood of competitive injury as any reasonable basis that competitive injury will occur. This could be conduct by packers, contractors, or poultry dealers that raises costs for competitors or misuses market power to distort competition with rivals. In addition, the proposed rule extends the definition of likelihood of competitive injury to conduct by packers, contractors, and poultry dealers directed toward livestock producers and poultry growers. Conduct that depresses prices to producers and growers or prevents producers and growers from competing with other producers or growers can be a competitive injury or harm to competition. GIPSA also states in Section 201.3 of the proposed rule that depending on the circumstance, conduct could be a violation of the P&S Act without a finding of harm or likely harm to competition.

[18] Grain Inspection, Packers and Stockyards Administration, *Farm Bill Regulations—Proposed Rule Outline*, p. 1, undated, http://archive.gipsa.usda.gov/psp/Farm_bill_rule_outline.pdf.

Unfair Practices

The second category of issues in the proposed rule covers unfair, unjust discriminatory and deceptive practices. In this area USDA describes actions that it considers unfair and would be violations of the P&S Act. USDA specifically notes that these actions do not require a finding of harm or likely harm to competition to be a P&S Act violation.

In Section 201.210 of the proposed rule USDA provides eight examples of unfair practices by meat packers and poultry dealers. They are

1. actions that a reasonable person would consider unscrupulous or deceitful;
2. retaliatory actions, such as coercion or intimidation, in response to a lawful action by a producer or grower;
3. refusal to provide statistical data used to determine contract payments;
4. actions to limit producers' or growers' legal rights;
5. paying premiums or discounts without documenting a reason;
6. terminating a production contract based only on allegations of misconduct by a producer or grower;
7. practices that are fraudulent or likely to mislead a producer or grower;
8. and broadly, any act that causes or creates a likelihood of competitive injury.

In Section 201.215, USDA proposed that live poultry dealers provide at least 90 days' notice that they are going to suspend the delivery of birds to poultry growers. This period would provide growers an opportunity to find other options for using their growing houses.

Sections 201.216 and 201.217 of the proposed rule address capital investment requirements and the criteria that USDA would use to consider a required capital investment a violation of the P&S Act. Sample criteria include whether or not a poultry grower or swine producer has the discretion to decide against making the investment, whether or not they are coerced into making the investment, and whether or not other similar growers or producers are required to make additional capital investments. Also, if a poultry or swine contractor plans to substantially reduce or shut slaughter or processing facilities within 12 months of requiring additional capital investments, that could be a violation of the P&S Act. But contractors could get a waiver from that regulation for catastrophic or natural disasters, or other emergencies. If additional capital investments are required, the grower or producer must be given a contract of sufficient length to allow them to recoup 80% of the cost of the investment.

Section 201.218 of the proposed rule sets criteria to determine if a contract grower or producer has been given sufficient opportunity to remedy a breach of contract. The proposed rule requires that a written notice be given to the contract grower or producer and the notification should identify the breach, when it occurred, and how it can be remedied. Growers and producers must also have the chance to rebut a breach of contract claim. Contractors must also consider the welfare of the animals that growers or producers are responsible for when considering actions and timelines for remedying a breach of contract.

Lastly, USDA proposes in Section 201.212(c) that packer-to-packer sales of livestock be banned. This would include affiliated companies and wholly-owned subsidiaries. A packer could receive a waiver for catastrophic or natural disasters. In the rule discussion, GIPSA notes that it does not consider these transactions as part of its definition of unfair practices, but as a "separate and distinct regulation" that is intended to prevent packers from manipulating prices.

Undue or Unreasonable Preference

The third part of the proposed rule addresses undue or unreasonable preference or advantage, that is, when producers who produce the same or similar poultry or livestock product receive different treatment/payment from contractors. This includes proposed regulations for differential pricing, recordkeeping, and packer-dealer relationships. In general, the Secretary of Agriculture may use three criteria to determine if poultry growers or livestock producers have been treated with undue or unreasonable preference in violation of the P&S Act. They are (Section 201.211)

1. contract terms have to be available to any producer or grower who can meet the terms of the contract;
2. premiums for product standards must be offered to a producer or group of producers who can meet the standards; and
3. information about handling, processing, and the quality of livestock must be available to all producers if made available to one.

Two sections of the proposed rule, Sections 201.94 and 201.214, address prices in poultry and livestock markets. Section 201.94 requires that packers, swine contractors, and live poultry dealers keep written records to justify differential pricing. The justification would have to provide the cost-benefit basis for different prices. GIPSA notes in its rule discussion that participation in a branded product program could be justification for a packer paying premium prices to cattle producers. Section 201.214 prohibits discounting base pay by live poultry dealers who use the tournament system to pay poultry growers. In a tournament system a poultry grower's birds are ranked or compared with the performance of other growers. Then grower payments are adjusted up or down based on performance relative to the group.

In Section 201.212(a), GIPSA proposes to prohibit livestock dealers from buying livestock for more than one packer. Livestock dealers buy and sell livestock for their own account or for another vendor or purchaser. A dealer who buys for a packer is often called a packer-buyer. Also, Section 201.212(b), requires that a packer report to USDA if a packer-buyer relationship is established with a livestock dealer.

In order to provide more information for growers and producers, GIPSA proposes in Section 201.213 that contractors be required to provide sample copies of unique contracts to GIPSA. The sample contracts would be made publicly available except for trade secrets, confidential business, and personal identity information.

Arbitration

In Section 201.219 of the proposed rule, GIPSA sets the criteria to be used to ensure that contract growers have the opportunity to participate in meaningful arbitration. The first part of the proposed arbitration regulation requires that contracts clearly disclose the costs, the process, and

the limits to legal rights and remedies associated with arbitration. It states that the costs should be reasonable compared with typical arbitration processes and provide reasonable time limits and access to information discovery by growers and producers. The arbitration process should comply with the Federal Arbitration Act (9 USC § 1 *et seq.*). The second part of 201.219 also requires that contracts contain the following statement that gives a grower or producer the right to decline arbitration:

> Right to Decline Arbitration. A poultry grower, livestock producer or swine production contract grower has the right to decline to be bound by the arbitration provision set forth in this agreement. A poultry grower, livestock producer or swine production contract grower shall indicate whether or not it desires to be bound by the arbitration provision by signing one of the following statements:
>
> I decline to be bound by the arbitration provisions set forth in this Agreement _____
>
> I accept the arbitration provisions as set forth in this Agreement _____
>
> Failure to choose an option by signing one of the above renders the contract void.

A cross-reference of sections in the farm bill provisions and the relevant GIPSA proposed rule is provided in **Table 2** below. The **Appendix** of this report includes a side-by-side synopsis of the pro and con positions for each provision.

Table 2. Relationship Between GIPSA Proposed Rule and Farm Bill Requirements

Farm Bill Provision	GIPSA Proposed Rule §	Topic
	§ 201.2(l)-(u)	Terms defined
	§ 201.3	Applicability of regulations
Section 11005	§ 201.219	Arbitration
Section 11006(1)	§ 201.210	Unfair, unjustly discriminatory and deceptive practices or devices
"	§ 201.211	Undue or unreasonable preferences or advantages; undue or unreasonable prejudice or disadvantages
"	§ 201.212(a)-(b)	Restrictions on livestock purchasing practices between packers and livestock dealers
"	§ 201.212(c)	Prohibits packer-to-packer sales
"	§ 201.213(a)-(d)	Transparency restrictions on livestock and poultry contracts
"	§ 201.214	Restrictions on use of tournament system
"	§ 201.94	Records retention requirement for price differentials
Section 11006(2)	§ 201.215(a)-(b), (c)	Suspension of delivery of birds; waiver of (a)-(b)
Section 11006(3)	§ 201.216(a)-(g)	Capital investments criteria
"	§ 201.217(a)-(e)	Capital investment requirements and prohibitions
Section 11006(4)	§ 201.218(a)-(h)	Reasonable period of time to remedy a breach of contract

Source: GIPSA proposed rule (9 CFR Part 201) in the Federal Register (75 Fed. Reg. 35338). The proposed rule would revise and amend existing regulations under the P&S Act as amended and supplemented (7 U.S.C. 181 *et seq.*). It is available at http://archive.gipsa.usda.gov/rulemaking/fr10/06-22-10.pdf.

Selected Issues

Proponents of the proposed rule argue that the P&S Act has not lived up to its potential because rules have not been properly promulgated over the years and courts have incorrectly interpreted the act. The Organization for Competitive Markets (OCM), one of the leading proponents of the proposed rule, stated in its comments to GIPSA that, "perhaps its most important worth is in addressing what we believe to be errant court rulings that there is a requirement to establish 'harm to competition' prior to considering harm to an individual."[19] According to rule proponents, the proposed rule will bring fairness to contracts and reshape interactions between producers and large meat packers and processors, especially for poultry growers who rely almost entirely on contracts. The proposed rule, according to OCM, does not "reinvent" the P&S Act, but "reinvigorates" it. It also contends that opponents have overblown the potential impacts of the proposed rule.

Opponents of the proposed rule are concerned about how USDA proposes to establish criteria for violating the P&S Act, as well as a number of other provisions. Also, the proposed rule contains several provisions to address the perceived unequal balance of market power between packers or poultry dealers and individual producers or growers. Overall, opponents expect the rule to significantly alter how business is currently conducted, to the detriment—in their view—of producers, consumers, and industry participants. According to the critics, the proposed rule will result in increased litigation if GIPSA's view that harm to competition is not necessary to determine a violation of the P&S Act prevails. Opponents also are concerned that the proposed rule is an attempt to impose a "one-size-fits-all" rule on the marketing structure and processes of different livestock sectors. They point to a wide range of differences in structure and the nature of markets, with nearly all poultry produced under contract while a substantial portion of steer and heifer slaughter is traded on the cash market. The marketing of hogs falls in between poultry and cattle with respect to the four firm concentration and marketing methods (see **Figure 1** and **Table 1**). Hence they argue that several rules that might appear reasonable for one sector might be counter-productive for another.

The box below includes a partial list of organizations that have been actively involved in the debate over the proposed rule.[20] Several of the major concerns about the proposed rule are discussed in more detail below. A description of each section of the proposed rule and arguments for and against them as espoused by interested parties also is provided in the **Appendix** of this report.

[19] Letter from J. Randal Stevenson, President, Organization for Competitive Markets, to GIPSA, November 19, 2010, http://www.competitivemarkets.com/index.php?option=com_content&task=view&id=373&Itemid=50. Also see comments submitted to GIPSA, David A. Domina and C. Robert Taylor, *OCM Support for Rules Proposed to Implement Farm Bill Requirements for Rule-Making re Anticompetitive Market Activity*, Organization for Competitive Markets, http://www.competitivemarkets.com/index.php?option=com_content&task=view&id=373&Itemid=50.

[20] Comments on the proposed rule by several industry and livestock and poultry groups are available at http://www.regulations.gov/. National Cattlemen's Beef Association, ID# GIPSA-2010-PSP-0001-RULEMAKING-22431.1, National Pork Producers Council, ID# GIPSA-2010-PSP-0001-RULEMAKING-22460.1, National Chicken Council and U.S. Poultry & Egg Association, ID# GIPSA-2010-PSP-0001-RULEMAKING-22432.1, American Farm Bureau Federation, ID# GIPSA-2010-PSP-0001-RULEMAKING-13971.1

Industry Groups Choose Sides

Within the U.S. livestock sector, there appear to be few neutral parties regarding the proposed rule. Broadly, the industry appears to be sharply divided into two groups:

The proponent groups argue that the rule would achieve greater price transparency in livestock markets and greater fairness and protection for producers in production contract arrangements. A few examples of proponents of the proposed rule include:

- Organization for Competitive Markets (OCM): OCM is a non-profit research group whose work focuses on market competition in the food and agriculture sector.
- Ranchers-Cattlemen Action Legal Fund, United Stockgrowers of America (R-CALF USA): R-CALF USA represents U.S. cattle producers on domestic and international trade and marketing issues.
- U.S. Cattlemen's Association (USCA): USCA represents the U.S. cattle industry, focusing on efforts in Washington, DC, to further the interests of U.S. cattle producers on various marketing and competition issues.
- National Farmers Union (NFU): NFU represents family farmers, ranchers, and rural communities to protect and enhance their well-being through grassroots-driven policy positions.

The opponent groups argue that the rule would disturb carefully developed marketing arrangements that have evolved slowly over time to produce greater consumer choices in meat quality and variety, and would place an undue burden on packers and poultry dealers who are competing for consumer dollars with a wide array of other food products. A few examples of opponents of the proposed rule include:

- American Meat Institute (AMI): AMI represents red meat and turkey companies in the United States. AMI keeps track of legislation, regulations, and media activity that impacts the meat and poultry industry.
- National Cattlemen's Beef Association (NCBA): NCBA represents U.S. cattle producers to advance the economic, political, and social interests of the U.S. cattle business and to be an advocate for the cattle industry's policy positions and economic interests.
- National Chicken Council (NCC): NCC represents chicken producers/processors, poultry distributors, and allied industry firms to promote and protect the interests of the chicken industry and is the industry's voice before Congress and federal agencies.
- National Pork Producers Council (NPPC): NPPC represents U.S. pork producers and other industry stakeholders through public-policy outreach, working for reasonable legislation and regulations, and developing revenue and market opportunities that protect the livelihoods of pork producers.
- National Meat Association (NMA): NMA represents meat packers, processors, equipment manufacturers, and food suppliers to the meat industry through assistance on regulatory and technical issues.

Note: Descriptions of the groups above are taken from the groups' own websites.

Congressional Intent and GIPSA Authority

An initial concern expressed by many opponents is whether GIPSA has exceeded the intent of Congress as expressed in Sections 11005 and 11006 of the 2008 farm bill, and GIPSA's authority in revising and amending existing regulations of the P&S Act. According to opponents, the proposed rule includes provisions—such as banning packer-to-packer sales of livestock—that extend well beyond the requirements of the 2008 farm bill.

In the proposed rule GIPSA argues that its authority derives in large part from Section 407 of the P&S Act (7 U.S.C. 228), which provides that the Secretary "may make such rules, regulations, and orders as may be necessary to carry out the provision of the Act."[21]

[21] "Proposed Rule," p. 35338.

GIPSA is supported in this conclusion by a group of 21 Senators who, in an August 13, 2010, letter to USDA Secretary Vilsack,[22] argued that,

> GIPSA authority and responsibility to address the full scope of subject matter covered in the proposed rule is amply supported and justified by the letter and intent of the P&S Act, as amended, and by well-established principles of federal administrative law enunciated by the Supreme Court of the United States and other federal courts.

In contrast, concerned industry groups and some Members of Congress charge that the proposed rule goes beyond what was required in the farm bill.[23] Furthermore, opponents say it contradicts several congressional votes taken during the debate on the relevant farm bill Sections 11005 and 11006, and that the proposed rule appears to contradict the decisions of several federal courts.

Unfair Practice vs. Harm to Competition

One of the more contentious issues surrounding the proposed rule is GIPSA's view that harm to competition is not necessary to conclude that certain conduct violates the P&S Act. GIPSA argues in its discussion of the proposed rule that USDA has long believed that unfair or deceptive practices or unreasonable or discriminatory preferences (Sections 202 (a) and (b) of the P&S Act) can be a violation of the P&S Act without a finding of harm to competition. GIPSA contends that Congress intended the same. They say that unlike Section 202 (c)-(e), which specifically note conduct that harms competition or creates monopolies, Congress would have included the harm to competition and creates monopolies conditions to parts (a) and (b) if it believed harm to competition was necessary for determining a violation.

GIPSA further notes that courts of appeal have disagreed with USDA's view on harm to competition and the courts are inconsistent with the language of the P&S Act in rulings that required findings of harm to competition.[24] GIPSA says the courts have failed to defer to USDA's interpretation of the regulations. This line of reasoning is supported by the group of 21 Senators' letter (August 13) to Secretary Vilsack, which stated:

> A cardinal principle is that the courts are to give deference to the interpretation of laws by the federal agencies that are charged with implementing and administering them. Specifically, for instance, GIPSA is to be accorded deference in its interpretation, spelled out in the proposed rule, that the P&S Act protects individual producers against "unfair, unjustly discriminatory, or deceptive practice[s] or devices[s]" without a necessity of showing such conduct has an impact on the broader market.

In Sections 201.210 and 201.211 of the proposed rule, GIPSA proposes to establish criteria for determining conduct that violates the P&S Act. GIPSA contends that conduct that is unfair or deceptive, or discriminatory may not harm the larger market or harm competition within that market, but producers or growers may be hurt financially by the packer or poultry processor actions, and GIPSA says this is a violation of the P&S Act.

---

[22] Letter to Secretary Vilsack, August 13, 2010, signed by 20 Senators; available at http://johnson.senate.gov/public/index.cfm?p=PressReleases&ContentRecord_id=76a7ec03-7013-4759-8f54-be576ea17294.

[23] Copies of some letters from Members of Congress to Secretary Vilsack are available at the American Meat Institute, http://www.meatami.com/ht/d/sp/i/61286/pid/61286.

[24] Proposed rule, p. 35341. As noted earlier in this report, the *Terry vs. Tyson Farms* case was concluded with the Supreme Court declining to review the case.

Proponents of the rule contend that it is too difficult to prove harm to competition because sufficient or compelling evidence is difficult to acquire. GIPSA cites numerous examples where individual producers are harmed by packer or poultry processor behavior that do not necessarily involve harm to competition.[25] For example, some chicken growers have stated that even though there are two poultry processors in their areas, it is understood that growers can only grow for one company and cannot switch. Small hog producers claim that packers offer lower prices for small lots of hogs, even if hogs are comparable to larger lots from large producers.

In contrast, opponents of the regulations charge that federal courts have consistently ruled that a plaintiff must show such harm to win a case.[26] In particular, the American Meat Institute (AMI) contends that, "USDA is attempting to use the rulemaking process to outflank the courts. Our system of government, however, is designed such that if the law is going to be changed, it should be changed by Congress, not by bureaucratic fiat." AMI contends that if the requirement to prove harm to competition is waived, "In virtually every case brought, a trial lawyer representing a plaintiff in a P&S Act case will argue that there is no need for the plaintiff to show injury to competition."[27]

Many livestock groups and producers fear that this weaker standard of proof could undermine the use of alternative marketing arrangements (AMAs). [28] They are concerned it could lead to a profusion of litigation such that the use of AMAs will be reduced or that they will become so standardized that value-added improvements and other market innovations will be unrewarded and thus abandoned, leaving the industry less consumer driven. In the long run, some believe the meat industry would become more concentrated if AMAs are undermined, as packers and poultry processors would seek more control over their slaughter supplies.

Livestock and Poultry Purchasing Practices

According to opponents of the proposed rule, Sections 201.212 and 201.14, which cover the packer and dealer relationship and tournament systems for poultry pricing, overstep the farm bill, and would severely disrupt livestock and poultry markets. USDA and proponents of the proposed rule argue that these practices need to be limited because they allow packers and processors to manipulate prices.

Restricting Livestock Dealers to a Single Packer

Currently, livestock dealers often buy livestock for multiple packers. Dealers, or packer-buyers, often go to feedlots or sale barns and, based on packer specifications, purchase livestock for packers. Section 201.212(a) and (b) of the proposed rule would limit livestock dealers to working with a single packer. Likewise, packers may only enter an exclusive arrangement with a dealer

[25] For examples of producer comments during several GIPSA town hall meetings, USDA-DOJ Workshops, and congressional testimony see "Examples of Market Behavior," GIPSA, undated; available at http://archive.gipsa.usda.gov/psp/FB_examples.pdf.

[26] "AMI Fact Sheet: Ten Key Facts About the Proposed GIPSA Rule," July 2010, American Meat Institute.

[27] Letter to Secretary Vilsack from J. Patrick Boyle, AMI President and CEO, July 28, 2010, and accompanying document that responds to a GIPSA document entitled, "Farm Bill Regulations—Misconceptions and Explanations."

[28] AMAs refer to agreements to purchase livestock by means other than the cash market. They could be forward contracts, marketing agreements, or packer owned supplies. See "GIPSA Livestock and Meat Marketing Study," January 2007. Available at http://www.gipsa.usda.gov/GIPSA/webapp?area=home&subject=lmp&topic=ir.

who has been identified as the packer's buyer and has officially notified GIPSA. USDA argues that the regulation would open livestock markets to more buyers and prevent collusion between multiple packers using one dealer as an exclusive agent, which it says could lead to price manipulation. GIPSA notes that this would especially benefit the cow/bull slaughter market, where a single dealer often buys for multiple packers, by opening the market to more dealers.

Rule opponents argue that restricting livestock dealers to a single packer could impose a burden on packers, especially small packers who lack the resources to send multiple dealers across the countryside to various auction houses, sale barns, or feedlots. Currently, small packers may share the costs of a single dealer operating in different market zones. Similarly, a single dealer may need to interact with multiple packers in order to obtain sufficient earnings. Opponents also argue that restricting dealers could reduce competition, especially in small markets. Some packers could choose to exit small markets because transaction costs would rise if they are required to use their own packer-buyer instead of being able to share transactions costs with multiple packers.

Banning Packer-to-Packer Sales

Section 201.212(c) would ban packer-to-packer sales. USDA and proponents contend that price information is exchanged during packer-to-packer transactions, which creates a situation where packers may be able to manipulate prices to the detriment of producers. If the packer-to-packer sale price is not publicly reported, then the marketplace and producers are missing a crucial market signal.

Opponents argue that a ban on packer-to-packer sales as proposed in the rule could cause market harm and speed up industry consolidation rather than slow it down. Critics of such a ban say that packer-to-packer sales are a key tool for smoothly meeting occasional disequilibrium in supply and demand at the plant level. Without such sales, opponents say packers would further integrate into the livestock production sector to limit procurement risks stemming from a loss of this additional source of supply (i.e., purchases from other packers). Alternatively, they would have to sell feeding facilities (perhaps to other packers) that are not within a reasonable shipping distance to their own slaughter operations, raising animal welfare issues.[29]

Revising Tournament Systems

The tournament system is a ranking system used by poultry processors to pay their contract poultry growers. At the end of a seven-week growing period, the quality of each grower's flock of birds is ranked against a pool (settlement group) of other grower flocks. Depending on growing performance, a discount or a premium may be applied to the base contract pay for each grower. Section 201.214 of the proposed rule would require live poultry dealers that use a tournament system to pay the same base pay to growers who raise the same type and kind of poultry. They would be required to rank growers in settlement groups with other growers with like poultry growing facilities.

Proponents of the proposed rule, specifically some poultry producers, contend that the tournament system is "designed to appear like a method to allow growers to compete fairly for pay based on

[29] Temple Grandin, "Ag Department Proposal Threatens Animal Welfare," October 20, 2010, http://www.huffingtonpost.com/temple-grandin/ag-department-proposal-th_b_769717.html.

performance. However, because the inputs that determine a producer's performance are supplied by the poultry company itself, the ranking system has become a back-door, anticompetitive mechanism for poultry companies to shift risks to growers and to discourage dissension."[30] Proponents argue that because poultry processors provide inputs, such as chicks and feed, the contract growers have little control over the performance of their flocks.

Opponents of the proposed tournament provisions, primarily processors, argue the best contract growers will be penalized. Since the proposed rule prohibits discounts to base pay, poultry processors could reduce base pay below current levels to protect from paying poor performers more than if discounts were allowed. Premiums on base pay to the best growers might not match current levels. They argue that the current system already reflects the fundamentals of a free market that rewards efficiency. Also, opponents believe that under the proposed rule's fairness provisions, differential pricing will invite increased litigation, further depressing the incentive to provide premium pricing to the best growers.

Record Keeping to Explain Pricing

In Section 201.94, the proposed rule would require a packer, swine contractor, or live poultry dealer to maintain written records that provide legitimate reasons for differential pricing or any deviation from standard price or contract terms offered to poultry growers, swine production contract growers, or livestock producers.

According to USDA, producers who appear to be able to deliver the same product but currently receive lower prices than other producers have no means to capture higher returns that other producers receive. The department contends that better documentation would facilitate enforcement of the P&S Act, particularly regarding certain types of differential pricing or contract terms deemed to be unfair.

Opponents claim that this record-keeping rule is too vague about what documents and justifications will be suitable to maintain compliance. Combined with the belief that the proposed rule will lead to more litigation because a lower standard than harm to competition will be applied, buyers may no longer want to pursue alternative marketing arrangements (AMAs) that pay premiums for delivering livestock or poultry with particular traits. Opponents assert that buyers use these and other contracting arrangements to ensure a steady supply of animals (as well as other agricultural commodities) to keep high-capacity plants operating efficiently; such arrangements also allow for necessary price adjustments for quality, grade, or other market-prescribed factors. The proposals for change would hurt producers too, opponents have added, because many of them use contracts or other marketing agreements with packers to limit their own exposure to price volatility and to obtain capital. According to rule opponents, the result could be the loss of economic incentives to produce a higher quality of meat and would hurt "value-based marketing."

Opponents want to know if there are specific documents or records that would be deemed acceptable proof for price differentials in all cases. To gain industry-wide acceptance, this could be clarified so that companies could avoid uncertainty or error. Criteria could include feed/pasture

[30] Rural Advancement Foundation International-USA (RAFI-USA), *Comments from 26 organizations for the workshop on poultry*, Letter submitted to Dept. of Justice, December 31, 2009, available at http://www.justice.gov/atr/public/workshops/ag2010/comments/255196.pdf.

information, genetics, and medical history, for example. Also, livestock that command market price premiums typically have identifiable physical attributes that distinguish them from "average quality" livestock. Top livestock producers may already keep records that would be suitable for enforcement of the rule. However, rule critics, in their comments, have cited several examples of market situations where price differentials might emerge (for example, due to timing or geographic market conditions) for essentially the same livestock product.

To further illustrate, critics offer the example of a packer that needs an additional 1,000 head of cattle to run its plant at peak efficiency. In its first market price offer, it might be able to obtain only 500 head. As a result, it makes a second higher-priced offer to obtain the second 500 head, even though all of the cattle are of comparable quality. In responding to market conditions, the packer did not exert any undue market power in acquiring the 1,000 head. Yet it is not clear if this transaction would violate the law or what documentation would justify this type of price differential.

Poultry Provisions Shift Risk to Poultry Companies

Several provisions, Sections 201.215, 201.216, and 201.217 in particular, appear to address poultry growers. The proposed regulations appear to shift production risk from producers to poultry processors, in an attempt to alter the balance of power between processors and producers when negotiating and fulfilling contracts. For example, current business practices in the poultry industry sometimes require successive capital investment upgrades. USDA asserts that it needs authority to limit these practices because they can harm a producer's financial position. Also, the rule would require a production contract to be of sufficient length to allow poultry or swine growers to recoup 80% of the costs related to the capital investment. Some question whether the federal government should guarantee a certain rate of return for a producer. Critics contend that an underperforming producer would have an unfair advantage over a more efficient producer.

Also, the provisions guarantee that poultry growers receive a 90-day notice from a live poultry dealer before bird deliveries are suspended. Proponents argue that a 90-day period is excessive since unforeseen events, other than the excepted catastrophic or natural disasters and other emergencies, could warrant a shorter notification period. An example would be market economic conditions that change rapidly.

Making Contracts Publicly Available

Requiring public disclosure of contracts, Section 201.213, has received less criticism than some of the other parts of the proposed rule because increased market transparency is considered by most to be a desirable goal. The provision would correspond with the transparency requirements for contracts in other sectors (e.g., insurance markets). However, opponents are concerned that not all proprietary information would be concealed or removed from public view. The concern expressed by critics is how it would be determined when an alteration or adaptation to an existing contract is sufficient to render it a "unique" contract such that it must also be posted. If every adjustment to a standard contract is posted, then critics argue that they will reveal their proprietary marketing strategy and sacrifice market advantage to their competitors.

Economic Impact of the Proposed Rule

One of the primary concerns of opponents of the proposed rule is that it lacks a rigorous economic impact analysis. The rule was declared by the Office of Management and Budget (OMB) to be "significant," meaning it would have an annual effect on the economy of more than $100 million. A rule declared significant requires that an agency explain the need for the regulation, assess potential costs and benefits, and undergo OMB review. The proposed rule was not determined to be "economically significant," which requires an even more thorough cost and benefit analysis that includes a quantified assessment of the effects and possible alternatives to the rule.

Also, significant criticism has been generated over the cost-benefit analysis presented in the rule, which opponents say is incomplete and merits further discussion because it fails to account for potential market consequences under various scenarios.

On October 1, 2010, 115 Members of Congress sent a letter to Secretary Vilsack stating that the proposed rule went beyond the mandate of the 2008 farm bill and would cause major changes in livestock and poultry marketing. The letter stated that, "The analysis contained in the proposed rule fails to demonstrate the need for the rule, assess the impact of its implementation on the marketplace, or establish how the implementation of the rule would address the demonstrated need." [31] The Members asked that USDA's Office of Chief Economist provide a thorough economic analysis. In response to this request, Secretary Vilsack said in a letter to now House Agriculture Committee Chairman Lucas that, "Beyond the cost-benefit analysis we have conducted for the proposed rule, we look forward to reviewing the public comments to inform the Department if all factors have been properly considered, if or how changes should be incorporated, and to aid more rigorous cost-benefit and related analyses pursuant to the rulemaking process."[32]

Media reports indicate that in a December 13, 2010, conference call with stakeholders, Secretary Vilsack stated that USDA will review the public comments and conduct a more thorough cost-benefit analysis for the final rule.[33] R-CALF USA, one of the leading proponents of the proposed rule, endorsed USDA's move to conduct another cost-benefit analysis that R-CALF believes will show the proposed rule's tremendous benefit for rural America and allow USDA to properly implement and enforce the P&S Act.[34] Opponents note that the proposed rule would have to be deemed economically significant in order for a meaningful analysis to be conducted. Secretary Vilsack's comments that the rule would be redrafted after considering public comments have raised the hope of rule opponents that the final rule will be more limited in scope.[35]

[31] Letter to Secretary Vilsack, October 1, 2010, signed by 115 Members of Congress; available at http://www.meatami.com/ht/a/GetDocumentAction/i/63222. American Meat Institute.

[32] Letter to Congressman Lucas, October 15, 2010, signed by Secretary Vilsack; available at http://agri-pulse.com/uploaded/USDA_Lucas_re_GIPSA.pdf.

[33] Rita Jane Gabbett, "USDA to conduct further cost-benefit analysis of GIPSA rule," *Meatingplace*, December 14, 2010, Industry News-AM.

[34] R-Calf USA, "CEO Statement: We Support USDA Plan to Conduct New Cost-Benefit Analysis of GIPSA Rule," press release, December 14, 2010, http://www.r-calfusa.com/news_releases/2010/101215-ceo.htm.

[35] Steve Kay, "USDA Will Redraft the GIPSA Rule," *Cattle Buyers Weekly*, December 20, 2010.

GIPSA Cost Analysis

Since the proposed rule was deemed significant, it was reviewed by the OMB, and GIPSA was required to provide justification. In the proposed rule, GIPSA identifies three categories of costs: (1) administrative costs, (2) costs of analysis, and (3) adjustment costs. Most of the costs estimates are not quantified in the proposed rule but are of a qualitative nature. For example, the cost of the record retention requirement to support differential pricing would depend on the current level of recordkeeping. The stated benefit is that prices would be determined by supply and demand and that there would be increased transparency in the price decision-making process. For other provisions of the proposed rule, such as requirements for livestock dealers and the ban on packer-to-packer sales, the costs are "adjustment costs" associated with halting prohibited marketing practices. According to GIPSA, the costs to packers would increase because packers would have to pay higher prices to producers. The identified benefits would be the prevention of monopolistic practices and a more fair and competitive market.

Beyond qualitative costs and benefits noted for provisions of the proposed rule, GIPSA quantified several costs as required under the Paperwork Reduction Act of 1995 (44 USC 3501 *et seq.*) for Sections 201.94, 201.213, 201.215, and 201.218. GIPSA estimates the cost of keeping records and conducting analysis for differential pricing to be $372,300 per year for the industry. The cost of submitting sample contracts is estimated at $24,083 per year for the livestock and poultry industries, and changing notifications for the suspension of bird deliveries for live poultry dealers is $12,500 per year. The estimated cost is $6,000 for administering the remedy to breach of contract provision.

Industry Analysis

As a result of the perceived weaknesses of GIPSA analysis, the meat and poultry industries released three studies of the proposed rule during the comment period that analyzed its impact on the U.S. economy and the livestock and poultry sectors. The studies were prepared for the American Meat Institute, the National Meat Association, and the National Chicken Council. Each study was conducted using differing assumptions and methodologies and resulted in considerably larger impacts than indicated in GIPSA's analysis.

American Meat Institute

The first impact analysis of the proposed rule that the meat industry released on October 21, 2010, was the *Economic Impact of Grain Inspection, Packers and Stockyards Administration Proposed Rule*,[36] as prepared for the American Meat Institute (AMI). The analysis concluded that the proposed rule would result in increased litigation that would cause meat producers to move away from the use of marketing agreements and return to cash or spot market purchasing. The study contends that this would increase inefficiencies and raise retail meat prices and reduce meat

[36] John Dunham and Associates, Inc., *The Impact of Proposed Grain Inspection, Packers and Stockyards Administration Proposed Rule, Methodology and Documentation*, Prepared for the American Meat Institute, Washington, D.C., October 21, 2010, http://www.meatfuelsamerica.com/GIPSA/content/Meat%20GIPSA%20Impact%20Methodology.pdf. The AMI website includes an interactive map that provides state and district level impacts. John Dunham & Associates is a New York-based firm that conducts economic impact studies on a variety of issues.

demand. It projects that this would result in a $14 billion decline in U.S. gross domestic product (GDP) and a loss of more than 104,000 jobs.

National Meat Association

On November 8, 2010, Informa Economics, Inc. released *An Estimate of the Economic Impact of GIPSA's Proposed Rules*.[37] The study was prepared for the National Meat Association (NMA) in cooperation with the National Cattlemen's Beef Association (NCBA), the National Pork Producers Council (NPPC), and the National Turkey Federation (NTF). The study's researchers interviewed beef, pork, and poultry industry participants to determine expected responses to the proposed rule and expected costs and then used the information to determine impacts on the industries and the U.S. economy.

The Informa study makes one-time estimates of the direct costs to the industries—costs associated with compliance to the proposed rule—at $136 million ($39 million for beef, $69 million for pork, and $28 million for poultry). Ongoing direct annual costs are projected at $169 million ($62 million for beef, $74 million for pork, and $33 million for poultry). The estimated indirect costs—losses due to reductions in product quality and/or efficiencies—are substantially higher. The annual losses are estimated at more than $1.3 billion ($780 million for beef, $259 million for pork, and $302 million for poultry). The Informa study estimates the economy-wide impact to be a reduction of $1.56 billion in GDP and nearly 23,000 lost jobs. The Informa study notes that it will take two to three years for the decline in efficiency to result in the losses, and that the costs would lessen over the long term as the industries adjusted.

National Chicken Council

The National Chicken Council released *Proposed GIPSA Rules Relating to the Chicken Industry: Economic Impact* on November 11, 2010.[38] The report was prepared by FarmEcon LLC and focused only on the chicken industry. The study estimated that the proposed rule would cost the chicken industry more than $1 billion over five years, with costs increasing each year. Over the fiver-year period of 2011 to 2015, feed and housing costs increase $794 million; costs associated with bird death loss from less efficient management and increased feed sampling and analysis costs increase $225 million. In addition, the study projects a one-time administrative cost of $6 million for the industry during the first year. Furthermore, the FarmEcon study found that the proposed rule would lead to higher costs associated with increased litigation, which it says would cause the U.S. chicken industry to be less innovative.

[37] Informa Economics, Inc., *An Estimate of the Economic Impact of GIPSA's Proposed Rules*, Prepared for the National Meat Association, Oakland, CA, November 8, 2010, http://beefusa.org/uDocs/Gipsa-Report_2010-11-09.pdf. The Executive Summary can be found at http://beefusa.org/uDocs/GIPSA-Executive-Summary.pdf. Informa Economics, Inc. is a private agricultural commodity/products market research, analysis, evaluation, and consulting in Memphis, TN.

[38] Dr. Thomas E. Elam, FarmEcon LLC, *Proposed GIPSA Rules Relating to the Chicken Industry: Economic Impact*, Prepared for the National Chicken Council, Washington, D.C., November 11, 2010, http://www.nationalchickencouncil.com/files/FarmEcon%20study%20of%20GIPSA%20rule%20impact%20Nov%202010.pdf. FarmEcon LLC is an agricultural and food industry consulting firm located in Carmel, IN.

What Next?

USDA has not provided a specific timeframe for when the proposed rule will be finalized. Media reports have speculated that it will take several months to process the public comment, and a thorough economic analysis as promised by USDA would also likely take several months to complete.

During the interim as the final rule is being prepared, Congress has shown interest in GIPSA's intent and implementation of the proposed rule. Immediately after the November 2010 election, Representative Frank Lucas, now chairman of the House Committee on Agriculture, indicated that the proposed GIPSA rule could be of interest as part of the committee's oversight responsibilities during the first session of the 112th Congress.[39] Also, in a congratulatory letter to Senator Stabenow, chairwoman of the Senate Agriculture Committee, and Senator Roberts, ranking Member, Senator Johanns suggested that hearings on GIPSA's proposed rule should be one of several issues included in the Agriculture Committee's oversight responsibilities.[40]

On February 17, 2011, during general/oversight hearings conducted by both the House Committee on Agriculture[41] and the Senate Committee on Agriculture, Nutrition, and Forestry,[42] Secretary Vilsack was asked about when USDA's economic analysis would be completed and the proposed rule finalized. Without providing a timeframe, he indicated that USDA was working on the economic analysis, utilizing the numerous public comments, and would take the time necessary to complete a thorough analysis. The Secretary was also asked if USDA's economic analysis would be peer reviewed and made available for a public comment period, but no commitment was given.

[39] Andy Eubank, "Frank Lucas Anxious to Assume House Ag Leadership," *Hoosier Ag Today*, November 3, 2010, http://www.hoosieragtoday.com/wire/news/01167_lucashouseag_225014.php.

[40] Letter to Senators Stabenow and Roberts, January 12, 2011, signed by Senator Johanns. Available at http://johanns.senate.gov/public/?p=PressReleases&ContentRecord_id=e4e13759-37f3-4d6c-9e1c-05ab03483205.

[41] U.S. Congress, House Committee on Agriculture, *The State of the Farm Economy*, 112th Cong., February 17, 2011.

[42] U.S. Congress, Senate Committee on Agriculture, Nutrition, & Forestry, *Agriculture: Growing America's Economy*, 112th Cong., February 17, 2011.

Appendix. Pros and Cons of the proposed GIPSA Rule

Table A-1. Pros and Cons of the proposed GIPSA Rule

Section number and description of proposed changes[a]	Supporting arguments by USDA[a]	Counterarguments by critics[b]
201.2 Terms Defined. Defines terms for tournament system, principal part of performance, capital investment, additional capital investment, suspension of delivery of birds, forward contract, marketing agreement, production contract, competitive injury, and likelihood of competitive injury.	Two key definitions would allow USDA to address anticompetitive issues: A "competitive injury" occurs when conduct distorts competition in the market channel or marketplace. "Likelihood of competitive injury" means there is a reasonable basis to believe that a competitive injury is likely to occur in the market channel or marketplace.	These two definitions are vague and much broader than proving harm to competition. Because there are varying levels of competition, setting "perfect competition" is a very high standard.
201.3 Applicability of regulations. Conduct can be found to violate sections 202(a) and 202(b) of the P&S Act without a finding of harm or likely harm to competition.	Congress did not intend these sections to be limited only to harm to competition. Congress amended the P&S Act to specify instances of conduct prohibited as unfair that do not involve any inherent likelihood of competitive injury.	The proposed rule does not provide guidance on when proof of injury is required. This would invite significant litigation and discourage the use of marketing agreements that benefit the industry.
201.94 Record retention. Requires a packer, swine contractor, or live poultry dealer to maintain written records that provide legitimate reasons for differential pricing or any deviation from standard price or contract terms offered to poultry growers, swine production contract growers, or livestock producers.	No recourse is currently available for producers who appear to be able to deliver the same product but receive lower prices than other producers. Better documentation would facilitate enforcement of the P&S Act, particularly regarding certain types of differential pricing or contract terms deemed to be unfair.	The rule does not define "standard price or contract terms" and the vagueness of requirements for justifying payments will discourage use of marketing agreements (and practices) that have increased product demand and value to producers and the marketing chain. The meat industry (particularly beef and pork) might return to a "commodity" business with all animals "sold on the average" to the detriment of producers and consumers.
§ 201.210 Unfair, unjustly discriminatory and deceptive practices. Provides examples of conduct that would be considered unfair, unjustly discriminatory and deceptive practices to provide more clarity and allow improved enforcement under the act.	Court decisions that require proof of "competitive harm" have limited USDA's enforcement capabilities. USDA needs authority to address unfair practices that do not have anticompetitive implications, Examples include not allowing producers to watch their birds being weighed and providing growers with poor quality feed.	The "open-ended" nature of the rule will result in packers being reluctant to pursue practices that have benefited the entire livestock and meat marketing chain for fear they may be sued. For example, it does not appear that timing or marketing conditions or historical performance by the producer will be considered sufficient reasons for price differences. The proposed rule will increase vertical integration across the industry as packers increase animal ownership to avoid potential litigation. Inefficient or unreliable producers could be rewarded.

Section number and description of proposed changes[a]	Supporting arguments by USDA[a]	Counterarguments by critics[b]
201.211 Undue or unreasonable preferences/prejudice or advantages/disadvantages. Establishes criteria the Secretary may consider in determining if these actions have occurred under the P&S Act.	USDA needs authority to address practices that can reduce business opportunities for producers if a packer or processor cannot provide a legitimate justification for price disparities. For example, a packer or swine contractor might offer better price terms to producers who can provide a large volume of livestock than to a group of producers who collectively can provide the same volume of livestock of equal quality. Smaller producers will have restored ability to compete with larger-sized operators.	See arguments in above two boxes. Certain industry groups, including the National Pork Producers Council, fear the rule will prevent contracts from addressing a producer's unique situation and prevent packers from rewarding efficient producers. Also, these provisions fall outside the scope of the mandate of the 2008 farm bill. Finally, the rule does not prevent frivolous and unnecessary litigation that would disrupt normal business.
201.212 Livestock purchasing practices. Bans packer-to-packer sales and places restrictions on dealers (buyers), that is, they cannot represent more than one packer.	During packer-to-packer transactions, price information is exchanged, which creates a situation where packers may be able to manipulate prices to the detriment of producers. Also, the regulation opens livestock markets to more buyers in certain markets (e.g., cow/bull slaughter) by requiring each packer to have its own buyer and prevent collusion between multiple packers using one dealer as an exclusive agent to manipulate prices.	USDA has not provided any evidence (or pursued cases) that packer-to-packer sales have resulted in price manipulation. Banning sales and requiring buyers to represent only one packer would increase costs to the entire marketing chain, including producers, because livestock would need to be shipped further or a third-party dealer would need to be created as a "pass-through" agent. Overall, competition decreases and industry consolidation could increase.
201.213 Sample contracts. Requires packers, swine contractors and live poultry dealers to provide GIPSA with sample copies of contracts for public distribution.	Improved transparency of contracts puts producers on equal footing with packers/dealers and reduces misperceptions of unfair or preferential treatment. GIPSA has received complaints of preference or retaliation by packers and live poultry dealers in contracts and marketing agreements that, upon investigation, were found to be in compliance with the act.	In many cases producers have unique agreements with their packer, and the potential exists for requiring that each of those agreements be released publicly, creating a burden for the industry. The proposed rule seems to exclude producers from the decision on what information is confidential and would not be made public. A decrease in the variety of contracts that address various risk management strategies is possible.
201.214 Tournament systems. If a poultry company is paying growers on a tournament system (with some portion of the payment made to poultry growers based on a comparison of one poultry grower's performance with that of other grower's performance), dealers are required to pay the same base pay to those raising the same type/kind of poultry (with no one paid below the base). Live poultry dealers would also be required to rank growers with others with like house types.	Complaints from poultry producers indicate that current practices, including paying disparate rates to producers raising the same type and kind of poultry, injures individual producers. The new regulation would allow for better assessment of contract values at the time of contract negotiation, specifically by providing poultry growers with a more consistent benchmark to compare different contracts.	The tournament method of compensation may be unworkable if all producers receive the same base pay, raising questions about how to pay producers with different cost structures if they produce the same type and kind of poultry. Will the acceptable alternative result in compensating inefficient producers? Efficient producers may have difficulty obtaining additional credit to grow their business.

Section number and description of proposed changes[a]	Supporting arguments by USDA[a]	Counterarguments by critics[b]
201.215 Suspension of delivery of birds. Establishes criteria the Secretary may consider when determining whether or not reasonable notice (at least 90 days) has been given for suspension of delivery of birds.	Poultry producers are currently not given sufficient notice of suspension in order to consider options for utilizing their facilities and for keeping up with any loan payments. Without sufficient information, a poultry grower is unable to protect his or her financial interests and make informed decisions.	Ninety days is too long given the potential for rapid changes in market conditions.
201.216 Capital investment criteria. Establishes criteria the Secretary may consider when determining whether a requirement that a poultry grower or swine producer constitutes an unfair practice in violation of the act.	Current business practices in the poultry industry sometimes require successive capital investment upgrades. USDA needs authority to limit these practices because they can harm a producer's financial position or can require investments for some producers but not others as a way to "punish" certain producers.	The provisions are ambiguous and subject the processor to increased risk. Also, the type of investment is not specified, such as those required by the packer for efficiency (or other reasons) or by law (e.g., animal welfare) which are beyond the packer's control.
201.217 Capital investment requirements and prohibitions. Requires a production contract to be of sufficient length to allow poultry or swine growers to recoup 80% of investment costs related to the capital investment.	Currently, producers are often required to make capital investments as a condition to enter into or continue a production contract, which can send producers or growers into severe debt, potentially increasing loan defaults. Producers who make large capital investments will have basic protections from being forced further into debt.	Some question whether the federal government should guarantee a certain return for a producer. An underperforming producer would have an advantage over a more efficient producer. The word "opportunity" is missing from the language providing for the recovery of the investment.
201.218 Reasonable period of time to remedy a breach of contract. Establishes criteria for determining whether a processor has provided a producer a reasonable period of time.	Proposed regulation addresses directive on remedies for breach of contract provided in the 2008 farm bill. Producers often are not given sufficient information or time to remedy a breach of contract.	The criteria establish considerable leeway for favoring the producer over the packers, contractors, and dealers.
201.219 Arbitration. Establishes criteria the Secretary may consider when determining whether the arbitration process in a contract provides a meaningful and fair opportunity for the poultry grower, livestock producer, or swine production contract grower to participate fully in the arbitration process if he/she so chooses.	Proposed regulation addresses directive on ensuring producers have the opportunity to fully participate in the arbitration process if they so choose, as provided in the 2008 farm bill. Many contracts (unilaterally drafted by processors) contain provisions limiting the legal rights and remedies afforded by law to producers. Also, producers with contracts that require binding arbitration are often left with no means to resolve disputes if they lack resources to pay fees.	Procedures of the American Arbitration Association should be used instead of the criteria for "fair" arbitration contained in the rule.

Source: Congressional Research Service.

a. Summarized from USDA documents: (1) USDA, Grain Inspection, Packers and Stockyards Administration, "Implementation of Regulations Required Under Title XI of the Food, Conservation and Energy Act of 2008; Conduct in Violation of the Act," 75 *Federal Register* 35338-35354, June 22, 2010; (2) "Farm Bill Regulations – Proposed Rule Outline," http://archive.gipsa.usda.gov/psp/Farm_bill_rule_outline.pdf; and (3) "Questions and Answers for Proposed Rule," http://archive.gipsa.usda.gov/psp/farm_bill_QA.pdf.

b. Summarized from statements by the American Meat Institute, National Cattlemen's Beef Association, National Pork Producers Council, National Chicken Council, and others.

Author Contact Information

Joel L. Greene
Analyst in Agricultural Policy
jgreene@crs.loc.gov, 7-9877